# *立法會*
# *Legislative Council*

LC Paper No. CB(1)1336/10-11
(These minutes have been seen by the Administration)

Ref : CB1/PL/FA/1

**Panel on Financial Affairs**

**Minutes of meeting**
**held on Monday, 3 January 2011 at 10:45 am**
**in Conference Room A of the Legislative Council Building**

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| **Members present** | **:** | Hon CHAN Kam-lam, SBS, JP (Chairman)<br>Hon CHAN Kin-por, JP (Deputy Chairman)<br>Ir Dr Hon Raymond HO Chung-tai, SBS, S.B.St.J., JP<br>Dr Hon David LI Kwok-po, GBM, GBS, JP<br>Hon James TO Kun-sun<br>Hon Emily LAU Wai-hing, JP<br>Hon Abraham SHEK Lai-him, SBS, JP<br>Hon LEE Wing-tat<br>Hon Jeffrey LAM Kin-fung, SBS, JP<br>Hon WONG Ting-kwong, BBS, JP<br>Hon Ronny TONG Ka-wah, SC<br>Hon CHIM Pui-chung<br>Hon KAM Nai-wai, MH<br>Hon Starry LEE Wai-king, JP<br>Dr Hon LAM Tai-fai, BBS, JP<br>Hon Paul CHAN Mo-po, MH, JP |
| **Members absent** | **:** | Hon Albert HO Chun-yan<br>Dr Hon Philip WONG Yu-hong, GBS<br>Hon Vincent FANG kang, SBS, JP<br>Hon Andrew LEUNG Kwan-yuen, GBS, JP<br>Hon Mrs Regina IP LAU Suk-yee, GBS, JP |

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| **Public officers attending** | : | Agenda Item IV<br><br>Mr Patrick HO, JP<br>Deputy Secretary for Financial Services and the Treasury (Financial Services)<br><br>Agenda Item V and VI<br><br>Ms Julia LEUNG, JP<br>Acting Secretary for Financial Services and the Treasury<br><br>Agenda Item V<br><br>Mr Anthony LI<br>Principal Assistant Secretary for Financial Services and the Treasury (Financial Services)<br><br>Mr Edmond LAU<br>Executive Director<br>Monetary Management Department<br>Hong Kong Monetary Authority<br><br>Mr Colin POU<br>Head of Payment Systems Operation Division<br>Financial Infrastructure Department<br>Hong Kong Monetary Authority<br><br>Agenda Item VI<br><br>Miss Mandy WONG<br>Principal Assistant Secretary for Financial Services and the Treasury (Financial Services) |
| **Attendance by invitation** | : | Agenda Item V<br><br>Mr Keith LUI<br>Executive Director<br>Supervision of Markets Division<br>Securities and Futures Commission |

Mr Rico LEUNG
Senior Director
Supervision of Markets Division
Securities and Futures Commission

Mr Romnesh LAMBA
Executive Vice President
Head of Market Development Division
Hong Kong Exchanges and Clearing Limited

Mr Kelvin LEE
Vice President
Market Development Division
Hong Kong Exchanges and Clearing Limited

Agenda Item VI

Mrs Ivy LAI
Director, External Relations
Securities and Futures Commission

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

**Staff in attendance** : Mr Noel SUNG
Senior Council Secretary (1)4

Ms Haley CHEUNG
Legislative Assistant (1)8

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Action

**I Confirmation of minutes of meeting and matters arising**

(LC Paper No. CB(1)662/10-11 — Minutes of special meeting on 21 October 2010

LC Paper No. CB(1)935/10-11 — Paper on Deputy Chairman's proposed amendment of the minutes of special meeting on 21 October 2010

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| LC Paper No. CB(1)906/10-11 | — | Minutes of meeting on 1 November 2010) |

The Chairman informed members that subsequent to the issue of the minutes of the meeting held on 21 October 2010 (vide LC Paper No. 662/10-11), the Clerk had received one proposed amendment from the Deputy Chairman, and members had been informed of the proposed amendment (vide LC Paper No. CB(1)935/10-11). Members agreed to confirm the minutes of the meeting held on 21 October 2010 subject to the amendment proposed by the Deputy Chairman and to confirm the minutes of the meeting held on 1 November 2010 without amendment.

## II Information papers issued since the last meeting

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| (LC Paper No. CB(1)641/10-11(01) and (02) | — | Submissions from a member of the public dated 17 and 24 November 2010 regarding assessment of property tax (Restricted to members only) |
| LC Paper No. CB(1)717/10-11(01) | — | Administration's letter dated 7 December 2010 on "Depreciation allowances for profits tax in respect of machinery or plant under the Inland Revenue Ordinance (Cap. 112)" |
| LC Paper No. CB(1)843/10-11(01) and (02) | — | Hon Mrs Regina IP's letter dated 24 November 2010 on "Hong Kong Institute for Monetary Research" and the Administration's response |
| LC Paper No. CB(1)899/10-11(01) | — | Submission from a member of the public regarding charges on provision of account statements by banks |

2. Members noted the information papers issued since the last regular meeting on 29 November 2010.

## III Date of next meeting and items for discussion

(LC Paper No. CB(1)910/10-11(01) — List of outstanding items for discussion

LC Paper No. CB(1)910/10-11(02) — List of follow-up actions

LC Paper No. CB(1)902/10-11(01) — Hon Mrs Regina IP's letter dated 21 December 2010 requesting for discussion of the new initiatives introduced by Hong Kong Mortgage Corporation)

Meeting in February 2011

3. The Chairman said that the regular meeting of the Panel in February 2011 was scheduled for 7 February 2011. As the Chief Executive, Hong Kong Monetary Authority (CE/HKMA) had to attend the G20 Financial Stability Board meeting in early February 2011, the CE/HKMA's briefing on the work of HKMA had to be postponed to a special meeting to be held on 21 or 22 February 2011.

4. The Chairman said that Mrs Regina IP had requested in her letter dated 21 December 2010 that the Hong Kong Mortgage Corporation (HKMC) and other relevant parties should be invited to brief the Panel on its two new initiatives, namely the Small and Medium Enterprises Financing Guarantee Scheme and the Reverse Mortgage Pilot Scheme. He consulted members on the arrangement for discussion of the two items.

5. Ms Emily LAU was of the view that HKMC should be invited to brief the Panel on the Reverse Mortgage Pilot Scheme as soon as possible and the Panel should hear the views from the parties concerned on the issue.

6. Mr KAM Nai-wai and Dr David LI suggested that the regular meeting on 7 February 2011 and the special meeting on 21 or 22 February 2011 be merged into one meeting.

7. Members agreed to postpone the regular meeting on 7 February 2011 to 21 February 2011 for discussion of the items listed below:

(a) Reverse Mortgage Pilot Scheme;

(b) Small and Medium Enterprises Financing Guarantee Scheme;

(c) Briefing on the work of the HKMA; and

(d) Review of Minimum and Maximum Relevant Income for Mandatory Provident Fund Contribution.

**IV Creation of a supernumerary Administrative Officer Staff Grade C Post for the establishment of an independent Insurance Authority and a Policyholders' Protection Fund**

(LC Paper No. CB(1)910/10-11(03) — Administration's paper on "Creation of a supernumerary Administrative Officer Staff Grade C Post for the establishment of an independent Insurance Authority and a Policyholders' Protection Fund")

8. The Deputy Secretary for Financial Services and the Treasury (Financial Services) (DS(FS)) briefed members on the proposal to create a supernumerary post of Administrative Officer Staff Grade C to undertake the work related to the establishment of an independent Insurance Authority (IIA) and a Policyholders' Protection Fund (PPF).

Manpower arrangements for existing staff of Office of the Commissioner of Insurance

9. Noting that the proposed post would deal with inter alia staff issues arising from the abolition of the Office of the Commissioner of Insurance (OCI), Ms Emily LAU enquired about the arrangements for the staff concerned. DS(FS) responded that upon the establishment of the IIA, which would operate as an independent statutory body, the OCI would be abolished. Arrangement would be made for the transfer of the existing general grades staff of OCI, through internal re-deployment, to other Government Bureaux/Departments. There were about 50 Insurance Officers in the OCI, some of whom would have reached retirement age before 2013-2014. The detailed arrangements for affected Insurance Officers had yet to be finalised. The Commissioner of Insurance, the Civil Service Bureau (CSB) and the Financial Services and the Treasury Bureau (FSTB) would discuss with the staff concerned to sort out the arrangements.

10. Ms Emily LAU requested the Administration to provide, before the

relevant Establishment Subcommittee meeting, information on the existing staff situation of the OCI and the arrangements for the affected staff upon the establishment of the IIA.

(*Post-meeting note*: The information provided by the Administration was circulated to Members vide LC Paper No. CB(1)1021/10-11 on 10 January 2011)

Provisional office

11. Ms Emily LAU sought information on the provisional office to be set up to prepare for the establishment of IIA. DS(FS) responded that the approach for taking forward the preparatory work for the establishment of the IIA was being considered, and the idea of setting up a provisional office for the purpose of handling the staff recruitment for the new IIA, as involvement by the existing professional staff of the OCI would not be appropriate, as well as office accommodation and related matters which would facilitate smooth transition was being explored. The proposed post would be responsible for the detailed arrangements taking into account the provisions in the relevant legislation and the manpower requirements of the IIA. Ms Emily LAU requested the Administration to provide, before the relevant Establishment Subcommittee meeting, details about the idea of a provisional office, including the functions, staffing, duration and the estimated expenditure of the office.

(*Post-meeting note*: The information provided by the Administration was circulated to Members vide LC Paper No. CB(1)1021/10-11 on 10 January 2011)

Legislative time-table

12. In reply to Ms Emily LAU's enquiry about the timetable for the establishment of the proposed IIA, DS(FS) advised that the Government aimed to introduce the relevant Bill into the Legislative Council in 2011, with a view to completing the legislative procedures for the Bill within the current term of the Legislative Council. Assuming smooth progress of the necessary steps to be taken, the IIA was envisaged to start operation in 2013-2014 at the earliest.

Financial arrangement for the IIA

13. Mr WONG Ting-kwong enquired whether the Government had already formulated details of the organization of the IIA and the level of levy to be imposed on insurance policies for funding the proposed IIA. Mr WONG opined that the Government should carefully consider the imposition of a levy on insurance policies and the level of the levy as it would increase the burden on policyholders and affect the competitiveness of Hong Kong's insurance industry.

14. DS(FS) responded that after consulting the Panel on the framework of the proposed PPF in July 2009, an actuarial consultancy study had been commissioned in 2010 on the proposal and the consultant was still working on its report. The Government aimed to present the detailed proposals to the Panel and the public for consultation in the first quarter of 2011. DS(FS) said that members' views regarding the levy would be considered in drawing up the detailed proposals for setting up the IIA.

Scope of responsibilities

15. While supporting in principle the creation of the proposed supernumerary directorate post, Mr Jeffrey LAM enquired whether the proposed post would be involved in the work related to the voluntary health protection scheme.

16. DS(FS) responded that the proposed post would be engaged in the work relating to the establishment of the IIA and PPF, and given the complexity of the work and the heavy workload, the officer would not have spare capacity to take up other responsibilities. The work related to the voluntary health protection scheme was being handled by the relevant policy bureau, with the involvement of the OCI.

Priority of work

17. The Deputy Chairman opined that given the resource constraints, the setting up of PPF should have priority over the establishment of an IIA, as the former initiative was important for affording protection to insurance policyholders.

18. DS(FS) responded that the Administration appreciated that both initiatives were important and was working on them concurrently. As at present, the comments received during the consultation on the proposed establishment of the IIA were being studied in detail. The proposal for setting up a PPF involved very complicated technical issues, and the relevant actuarial

consultancy study was near completion. It was hoped that the IIA and PPF would come into operation in 2013-2014 at the earliest.

19. While supporting the approach of taking forward the two proposals concurrently, Ms Emily LAU enquired about the scale, complexity and sensitivity of the PPF proposal.

20. DS(FS) responded that after the global financial crisis, the response of the insurance industry to the proposed setting up of a PPF had been more positive than before. The complex issues involved in the PPF proposal included the levy to be imposed, the types of insurance policies to be covered, whether corporate policyholders should be covered, the investment and compensation arrangements of the fund, etc. and the proposal would have a significant impact on the insurance industry and policyholders.

Position on the staffing proposal

21. Mr James TO said that since Members belonging to the Democratic Party had yet to decide whether they would support the establishment of an IIA, Members of the Democratic Party reserved their position on the proposal of creating a supernumerary Administrative Officer Staff Grade C post to deal with the relevant work.

## V Latest developments in regulating the over-the-counter derivatives market

(LC Paper No. CB(1)763/10-11(02) — Paper on "Latest Developments in the Regulation of the Over-the-Counter Derivatives Market" provided by the Administration, Hong Kong Monetary Authority and Securities and Futures Commission)

Briefing by the Administration/Hong Kong Monetary Authority

22. The Secretary for Financial Services and the Treasury (Acting) (SFST (Atg)), the Executive Director, Monetary Management Department, Hong Kong Monetary Authority (ED(MM)/HKMA), and the Executive Director, Supervision of Markets Division, Securities and Futures Commission (ED(SM)/SFC) briefed members, through a Powerpoint presentation, on the

latest international developments in the regulation of the over-the-counter (OTC) derivatives market and the proposed way forward for Hong Kong.

(*Post-meeting note*: The presentation slides were issued to members through a Lotus Notes email on 3 January 2011.)

Types of OTC derivatives to be covered under the proposed regulatory regime

23. Mr Ronny TONG enquired about the rationale for not including equity derivatives under the proposed regulatory regime for OTC derivatives. SFST (Atg) responded that the Government had taken into account the degree of standardisation of the products concerned, the risks involved in selecting the products for regulation at the initial stage, and the relevant developments in the international arena. She pointed out that international consensus had yet to be reached on whether OTC equity derivatives should be subject to mandatory reporting and clearing requirements. ED(MM)/HKMA supplemented that, in terms of nominal amount, equity derivatives constituted about 5% of the overall OTC derivatives trades in Hong Kong. There was a wide variety of OTC equity derivatives which were far from meeting the standardisation requirement. Having regard to the large trading volumes of interest rate swaps (IRS) and non-deliverable forwards (NDF) and from the risk management angle, the Government proposed that the application of the proposed regulatory regime should start with IRS and NDF.

24. Mr Jeffrey LAM expressed concern about the feasibility and effectiveness of the proposed regulatory regime for OTC derivatives, in view of the wide variety of such derivatives the form of which would change over time, and the relevant international developments were still in a state of flux. Mr LAM enquired about the types and amounts of the OTC derivatives to be regulated under the proposal. He also enquired which regulatory body would be responsible for overseeing the operation of the Central Counterparties (CCP).

25. SFST (Atg) responded that IRS and NDF were already highly standardised, and were considered suitable for regulation based on international practices. The inclusion of non-standardised derivatives in the regulatory regime would entail higher regulatory and compliance costs. The CCP would be regulated by SFC. ED(SM)/SFC supplemented that currently there were CCPs for trading of securities and futures, and the Hong Kong Exchanges and Clearing Limited (HKEx) would set up a separate CCP for clearing of standardised OTC derivatives transactions. The International Organization of Securities Commissions (IOSCO) and the Committee on Payment and Settlement Systems (CPSS) had set up a committee to draw up international standards in 2011 for CCPs of OTC derivatives, and Hong Kong's

regulatory regime would model on such international standards. The future local CCP for OTC derivatives would be regulated under the SFO. ED(MM)/HKMA added that IRS and NDF constituted about 18% and 17% respectively of the local OTC derivatives market. The nominal amounts generated by IRS and NDF trades in 2009 were about $3,000 billion and $2,800 billion respectively. The OTC derivatives market in Hong Kong constituted about 0.89% of the global OTC derivatives market. Hong Kong would aim at developing its regulatory regime in tandem with relevant international developments.

26. Mr Paul CHAN expressed concern that the proposed regulatory regime would not cover equity derivatives and foreign exchange derivatives. He enquired about the practices in the United Kingdom (UK), United States (US) and Singapore in regulating the trading of equity and foreign exchange derivatives.

27. ED(SM)/SFC responded that it was difficult to achieve standardisation, a prerequisite for centralized clearing, for equity derivatives. The governments of UK, US and Singapore had put priority on regulating the interest rate related and credit related derivatives. Depending on the development in the international arena, Hong Kong might consider regulating OTC equity derivatives at a later stage. ED(MM)/HKMA supplemented that the OTC derivatives market in Hong Kong was similar to those in the UK, US and Singapore in that foreign exchange derivatives constituted the greatest share of the OTC derivatives market. However, the majority of the foreign exchange derivatives involved short term foreign exchange swaps whose risk was relatively low. Consideration would be given to including some of the long term foreign exchange derivatives in the regulatory system in future.

Funding arrangements

28. Mr Ronny TONG enquired about the financial arrangements for the establishment and operation of the CCP and trade repository (TR) in Hong Kong for the clearing and reporting of OTC derivatives transactions. Mr TONG was concerned that the development of the OTC derivatives market in Hong Kong might be adversely affected if the CCP charged a high fee for OTC derivative transactions. Mr Paul CHAN echoed Mr TONG's concern and remarked that the expenditure of the CCP should be borne by market participants, and no subsidy should be made from the public purse.

29. Mr James TO was concerned that the level of fees and the size of the guarantee funds would have an impact on the OTC derivative trades in Hong Kong, as the traders might choose to carry out the trades in other places if the fees in Hong Kong were relatively high. Mr TO was also concerned whether

the fee levels for certain OTC derivatives would be adjusted according to the changing risk situation and/or the volume of trade involved, which might again affect the competitiveness of the Hong Kong OTC derivatives market.

30. SFST (Atg) responded that the Government would not provide financial support for the establishment and operation of the CCP. The Executive Vice President, Head of Market Development Division, Hong Kong Exchanges and Clearing Limited (EVP(MD)/HKEx) remarked that the HKEx would make an investment of about $180 million for setting up the CCP, which was of strategic value for HKEx and Hong Kong's financial market. A guarantee fund would be set up jointly between HKEx and the subscribers to the CCP. The CCP would charge a fee on the OTC derivative transactions for the services provided, and the fees would not be set at such a level as to hinder the development of the market. The Government/HKMA/SFC/HKEx had yet to formulate a view on the fee levels or the size of the guarantee fund. The fees would be set based on a number of factors, including benchmarking with the fees charged in the global markets. The CCP was expected to operate at a loss in the initial years. ED(MM)/HKMA added that the fees of the CCP should be set at a level competitive with that of overseas financial markets so as to develop the local OTC derivatives market. At present, market participants would still need to post margin/collateral with each other in the bilateral trades in the OTC market and so central clearing might provide an opportunity for more efficient use of the collateral.

31. Mr Ronny TONG and Mr James TO remarked that more information about the funding arrangements, including the fees to be charged by the CCP, should be provided when a more concrete proposal was presented to the Panel.

General

32. Mr Abraham SHEK opined that the discussion paper for this item and the Powerpoint presentation did not provide adequate information for a thorough discussion of the very complicated subject. Mr SHEK doubted whether the Government had sufficient knowledge and understanding about the issues relating to the regulation of the OTC derivatives market. While supporting in principle the proposed regulatory regime, Mr SHEK questioned whether the Government and the relevant regulatory bodies had the expertise and competence for regulation of the OTC derivatives market, given that the Government and the regulatory bodies concerned had not performed their regulatory responsibilities satisfactorily during the Lehman Brothers Minibonds Incident. Mr SHEK was of the view that the Government should have acted before the Lehman Brothers Minibonds Incident in regulating the OTC derivatives market.

33. SFST (Atg) responded that at present, trading of OTC derivatives lacked transparency. The proposed establishment of a local CCP for the clearing of IRS and NDF, and a TR for the maintenance of transaction records of these OTC derivatives would improve the transparency of the OTC derivatives market, thereby enhancing investor protection. She remarked that the global financial markets would continue to make concerted efforts to establish and implement effective regulatory regimes for OTC derivative markets.

34. The Deputy Chairman expressed concern about the impact of the proposed arrangements for regulating OTC derivatives on the competiveness of the derivatives market in Hong Kong. He enquired about the impact of the proposed regulatory regime on the development of Renminbi OTC derivatives in Hong Kong.

35. SFST (Atg) responded that under the proposal, all standardised IRS and NDF were required to be traded through an authorized CCP, and HKEx would not enjoy monopoly in providing the CCP facility. Similar regulatory arrangements would be implemented in respect of standardized OTC derivatives in other major financial markets such as the US and the countries in the European Union. To ensure parity of Hong Kong's regulatory arrangements with those of global financial markets, Hong Kong would maintain close liaison and exchange information with other major financial markets on the regulation of OTC derivatives. Hong Kong enjoyed an edge over other financial markets in that it started the development of a Renminbi OTC derivatives market earlier than other places, e.g. a NDF market on Renminbi had already been established in Hong Kong. EVP(MD)/HKEx added that while the HKEx would not develop derivative products on its own, it would consider providing a platform for clearing of standardised OTC Renminbi derivative products.

36. Ir Dr Raymond HO enquired, based on the Financial Stability Board (FSB)'s recommendations, what robust risk management requirements would be introduced for the regulation of the remaining non-centrally cleared OTC derivative trades. In response, ED(MM)/HKMA said that given the higher risk involved in the trading of non-centrally cleared OTC derivatives, the contracts of such derivatives would be subject to higher capital requirements. The Basel Committee would review the capital requirement for financial institutions dealing with non-centrally cleared OTC derivatives.

37. Ir Dr Raymond HO enquired how the establishment of a local TR would help improve the assessment on the risk of OTC derivatives. ED(MM)/HKMA responded that the TR would enable the regulatory bodies to obtain information about the position held by individual financial institutions. Through the TR, market participants would also be able to obtain aggregate information on

certain asset classes of OTC derivatives in order to assess and map out their risk management and investment strategies.

38. In response to Ir Dr Raymond HO's enquiry as to Hong Kong's commitment to implement the international regulatory bodies' requirement on central clearing of standardised OTC derivatives and risk management measures for the remaining non-centrally cleared trades, ED((MM)/HKMA said that Hong Kong, being a member of FSB, the Basel Committee and IOSCO, and had the responsibility to comply with international standards for regulation of OTC derivatives. This was also important in living up to Hong Kong's role as an international financial centre.

Legislative timetable

39. In response to the Chairman's enquiry, SFST (Atg) advised that the current plan was to submit the relevant amendments to the Securities and Futures Ordinance (Cap. 571) to the Legislative Council in mid-2011.

## VI Proposed establishment of an Investor Education Council and a Financial Dispute Resolution Centre - Consultation conclusions

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| (LC Paper No. CB(1)910/10-11(04) | — | Administration's paper on "Proposed Establishment of an Investor Education Council and a Financial Dispute Resolution Centre — Consultation Conclusions" |
| LC Paper No. CB(1)771/10-11(01) | — | Administration's paper on "Proposed Establishment of an Investor Education Council and a Financial Dispute Resolution Centre — Consultation Conclusions" |
| LC Paper No. CB(1)909/10-11 | — | Background brief on proposed establishment of an Investor Education Council and a Financial Dispute Resolution Centre prepared by the Legislative Council Secretariat) |

Briefing by the Administration

40. SFST(Atg) briefed members, through a Powerpoint presentation, on the consultation conclusions on the proposed establishment of an Investor Education Council (IEC) and a Financial Dispute Resolution Centre (FDRC).

(*Post-meeting note*: The presentation slides were issued to Members through a Lotus Notes email on 3 January 2011.)

Financial Dispute Resolution Centre

*Maximum claimable amount*

41. Noting that the maximum claimable amount was proposed to be set at $500,000 as it covered about 83% of the monetary disputes handled by the HKMA, Mr Jeffrey LAM enquired about the average amount of payment made to a claimant in the monetary disputes. Mr LAM further asked about the views expressed by the respondents on the maximum claimable amount during the consultation exercise.

42. SFST (Atg) responded that the maximum claimable amount of $500,000 was proposed as about 80% of the 2 000 odd complaints handled by HKMA in 2009, and the majority of the complaints received in relation to the Lehman Brothers Minibonds Incident involved claimable amounts below $500,000. The proposed amount also covered about 80% of stock investors. Having considered the views received during the public consultation exercise, the Government considered the proposed maximum claimable amount appropriate. After the FDRC had operated for some time, a review of the scope of work and the maximum claimable amount would be conducted.

43. At the request of Mr Paul CHAN, the Administration agreed to provide information on the percentage of monetary disputes handled by HKMA and the percentage of stock investors that would be covered if the maximum claimable amount was set at $1 million. Mr Paul CHAN opined that a review of the maximum claimable amount should be conducted as soon as possible.

(*Post-meeting note*: The information provided by the Administration was issued to Members vide LC Paper No. CB(1)1071/10-11 on 14 January 2011.)

*Scope of coverage*

44. In response to Ms Starry LEE's enquiry, SFST (Atg) said that all financial institutions regulated or licensed by HKMA and SFC would be

obligated to join the financial dispute resolution scheme as members. Amendments would be made to the Code of Conduct for SFC licensees and the licensing conditions applied to authorized institutions regulated by HKMA to obligate them to join the scheme.

45. The Deputy Chairman was concerned that while the FDRC would not handle monetary disputes involving insurance companies, it would deal with cases involving insurance products sold in banks. The Deputy Chairman opined that to ensure consistency in the regulation of insurance services, all monetary disputes involving insurance products should be handled by one regulatory body, e.g. the future IIA, and not the FDRC.

46. SFST (Atg) responded that one of the reasons for carving out the insurance sector from the proposed dispute resolution mechanism was that the proposal on setting up an IIA was still under consideration. She however agreed to consider the Deputy Chairman's view regarding the arrangement for resolution of monetary disputes relating to insurance products sold in banks.

*Mediators*

47. Ms Starry LEE enquired about the number and qualifications of the mediators of the FDRC and whether they possessed investigative powers in mediating a case. SFST (Atg) responded that the mediators would be appointed by the FDRC based on a set of criteria. A mediator would not judge who was right or wrong. A mediator's role was primarily to mediate between the complainant and the financial institution concerned and assist them to identify and explore options for settlement, rather than investigate into a complaint. The intake officers of FDRC had the information gathering power. If mediation failed and if the claimant so wished, the case concerned would be resolved by arbitration.

*Legal representation in the mediation/arbitration process*

48. Mr Ronny TONG opined that the establishment of an FDRC would bridge a gap in the current system in resolving financial disputes, and remarked that in the absence of such a mechanism, only a small number of complaints in the Lehman Brothers Minibonds Incident had been settled through mediation. Mr TONG pointed out that in the existing adjudication mechanisms such as the Small Claims Tribunal and Labour Tribunal, an inequality of arms situation could arise, as an employer could be represented by an employee who was a lawyer, while a claimant was not allowed and might not have the resource to hire a lawyer to represent him at a hearing. Mr TONG enquired what measures would be taken to ensure that there would be an "equality of arms" in the resolution of financial disputes handled by the FDRC. Mr TONG opined that consideration should be given to forbidding companies from being represented by lawyers during mediation/arbitration.

49. SFST (Atg) responded that a working group on FDRC comprising representatives from the Law Society of Hong Kong, the Hong Kong Bar Association, the Hong Kong International Arbitration Centre, the regulators and professionals had been set up. One of the major issues being discussed in the working group was how to ensure "equality of arms". Consideration was being given to empowering the arbitrators under the Mediation and Arbitration Rules to obtain information for arbitration. Mr TONG's proposal of banning all forms of legal representation would be reflected to the working group for consideration.

*Mediation and arbitration vs ombudsman model*

50. Mr KAM Nai-wai had great reservation about the effectiveness of the FDRC and pointed out that out of the thousands of complaints arising from the Lehman Brothers Minibonds incident, only a score of the cases were settled through mediation. Mr KAM opined that in order to provide adequate protection for investors, a one-stop service system such as a financial services ombudsman should be established to deal with complaints from investors, investigation of the cases, imposition of sanctions and order of compensations from financial institutions.

51. Ms Emily LAU shared Mr KAM's concern and said that given the experience of the Lehman Brothers Minibonds Incident, the public might not want Members belonging to the Democratic Party to support the proposal of setting up an FDRC. Ms LAU enquired how the proposed FDRC would encourage the parties concerned to resolve the monetary disputes through mediation.

52. SFST (Atg) responded that 80% of the complaint cases, or about 70 complaint cases, seeking mediation in the Lehman Brothers Minibonds Incident had been settled. The main reason for having only a small number of cases in the incident settled through mediation was that many banks did not agree to resolve the dispute by mediation. Under the proposed financial dispute resolution scheme, banks would be obligated under the licensing conditions to join a mediation requested by a customer in order to resolve a monetary dispute. SFC was empowered under the SFO to investigate complaints and impose sanctions on a financial institution if appropriate. Although SFC could not order a financial institution to give compensation, in the Lehman Brothers Minibonds Incident, SFC had successfully arranged with the majority of the financial institutions and the complainants concerned, through mediation, to come to a resolution agreement, and the investors were able to claim back some of their money. SFST (Atg) said that at this stage, there was no plan to amend the SFO for empowering the SFC to order compensation.

*Schedule of fees*

53. In response to the Deputy Chairman's enquiry, SFST (Atg) remarked that the claimant and the financial institution concerned would be charged a fixed fee for the mediation, based on the assumption that the mediation would be settled within four hours. In the rare event that a mediation lasted for longer than four hours, an extra fee would be charged subject to the agreement of both parties.

*Funding for FDRC*

54. In response to Mr KAM Nai-wai's enquiry about the funding requirement of the proposed FDRC, SFST (Atg) remarked that the setting up cost for the FDRC was estimated to be around $15 million, and the annual recurrent expenditure of the FDRC would be about $55 million.

Investor Education Council

55. Ms Starry LEE enquired about the work of the IEC and the targeted group of investors. While emphasizing the importance of educating the younger generation on investment knowledge, Ms LEE enquired whether the Education Bureau had been requested to include subjects relating to the operation of the financial market in the school curriculum.

56. The Director, External Relations, SFC (D(ER)/SFC) responded that an elective subject in the curriculum for senior secondary schools, i.e. "Business, Accounting and Financial Studies", included study of basic financial knowledge such as the operation of the market, Mandatory Provident Funds. Different modes of education had to be adopted to educate different groups of

the community like housewives, pensioners, youngsters and working class. Programmes would be launched through the mass media to educate people who would not pro-actively learn about the financial market/services. Investor education for youngsters and adults with higher education level would mainly be provided through the school and the Internet.

57. Dr LAM Tai-fai remarked that the proposal showed that Government policies were lopsided towards the financial and property sectors. Dr LAM questioned why the Government did not propose setting up education councils for other sectors such as "a transformation of manufacturing industries education council", "a product branding education council", etc. Dr LAM opined that the IEC would face difficulty in educating groups of investors with different level of financial literacy. Dr LAM enquired about the meaning of enabling investors to make "better financial decisions" through the work of the IEC.

58. SFST (Atg) responded that the setting up of the IEC did not represent that Government policies were lopsided towards the financial sector. SFST (Atg) said that the IEC aimed to educate people such as pensioners and young investors to understand better an investor's rights and responsibilities and enhance their abilities in managing finance and making better financial decisions. D(ER)/SFC supplemented that investor education was one of the investor protection measures to enhance investors' ability in analysing the information provided by intermediaries and issuers on investment products so as to enable them to make better investment decisions.

Measures to enhance regulation of financial institutions

59. Mr Jeffrey LAM enquired, apart from the proposed IEC and FDRC, whether measures would be proposed to enhance the regulation of financial institutions in order to protect investors.

60. SFST (Atg) responded that in the past year, HKMA and SFC had made recommendations to enhance the regulation of the sale of financial products, many of which had already been implemented, e.g. separate areas had to be designated in a bank for usual banking services and for sale of investment products; provision of a "cooling-off period" for sale of structured products; enhanced disclosure of the risks of investment products, etc.

61. Pointing out that a committee of the Legislative Council was looking into issues relating to the Lehman Brothers Minibonds Incident, Ms Emily LAU was concerned whether the current proposals would pre-empt the actions to be recommended by the committee. She enquired whether the Administration would consider implementing the proposals only after the committee had released its conclusions and recommendations. Ms LAU

further enquired what actions would be taken if the proposed measures to enhance investor protection were in conflict with the recommendations of the committee.

62. SFST (Atg) responded that the Government pursued setting up an IEC and FDRC after public consultation. The Government would consider and take appropriate actions to follow up the recommendations of the Legislative Council committee when the recommendations were available. The Chairman said that the investor protection measures recommended by the Administration and the committee were not mutually exclusive, and could be taken forward concurrently.

## VII Any other business

Visit to Shanghai

63. The Chairman said that given that Shanghai would be developed into an international financial centre and Panel members were concerned about the relationship and co-operation between Shanghai and Hong Kong in financial matters, it would be opportune to conduct a duty visit to Shanghai to study the financial developments in the city. Indeed, there was such a suggestion made at a previous Panel meeting. The Chairman then sought members' views on the duty visit proposal.

64. Ms Starry LEE and Mr Paul CHAN expressed support for conducting a duty visit to Shanghai. Ms LEE opined that a visit to the Shenzhen financial authorities would also be useful, and the Panel could visit the Stock Exchange of Hong Kong before proceeding to the Mainland visit. Mr CHAN also opined that the visits to Shanghai and Shenzhen should be held separately.

65. After consulting members, the Chairman remarked that attempts would be made to contact the relevant Shanghai authorities to arrange a visit by Panel members to Shanghai around the Easter holidays in April 2011.

66. There being no other business, the meeting ended at 1:09 pm.

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