

LEGISLATIVE COUNCIL BRIEF

**SECURITIES AND FUTURES ORDINANCE
(Chapter 571)**

**SECURITIES AND FUTURES (LEVY) (AMENDMENT)
ORDER 2011**

AND

**SECURITIES AND FUTURES (LEVY) (AMENDMENT)
RULES 2011**

INTRODUCTION

At the meeting of the Executive Council on 28 June 2011, the Council ADVISED and the Chief Executive ORDERED that, pursuant to section 394(1)(c) of the Securities and Futures Ordinance (SFO), the Securities and Futures (Levy) (Amendment) Order, at Annex A, and the Securities and Futures (Levy) (Amendment) Rules, at Annex B, should be made to provide for the payment of Securities and Futures Commission (SFC) levies on the sale and purchase of futures contracts traded by means of automatic trading services (ATS), thus covering the ATS provided by Hong Kong Mercantile Exchange Limited (HKMEx).

A

B

JUSTIFICATIONS

2. Under section 394(1) of the SFO, the Chief Executive in Council may specify SFC levies in respect of the sale and purchase of –

- (a) securities which are recorded on a recognized stock market or notified to a recognized exchange company;
- (b) futures contracts traded on a recognized futures market; and
- (c) securities or futures contracts traded by means of authorized ATS.

The levies specified under section 394(1)(a) and (b) but not (c) are set out in the Securities and Futures (Levy) Order.

3. Separately, under section 394(5) of the SFO, the Chief Executive in Council may make rules on various matters relating to the collection, payment and refund of SFC levies and the keeping and inspection of related accounts. Such matters are prescribed under the Securities and Futures (Levy) Rules.

4. HKMEx obtained authorization from the SFC on 26 April 2011 to provide ATS and has commenced trading of gold futures contracts since 18 May 2011.

5. HKMEx is not the first ATS provider to be authorized by the SFC. Nevertheless, its authorization is unique in that it is the first authorized ATS to –

- (a) offer an exchange-like platform for the trading of futures contracts (i.e. a platform that matches buy and sell orders for futures contracts); and
- (b) be solely or primarily regulated by the SFC.¹

6. Because HKMEx offers an exchange-like platform for the trading of futures contracts and is solely regulated by the SFC, its position is similar to that of Hong Kong Futures Exchange Limited (HKFE), which also operates a futures market in Hong Kong, albeit as a recognized exchange company rather than as an authorized ATS provider.²

7. Against the background set out above, futures contracts traded by means of the authorized ATS provided by HKMEx are not subject to SFC levies. In contrast, futures contracts traded on HKFE are subject to SFC levies under Part 3 of the Securities and Futures (Levy) Order, generally at \$0.60 payable by both the seller and the purchaser. The existing arrangements regarding SFC levies have thus created an unlevel playing field between HKFE and HKMEx. Accordingly, we propose that SFC levies also be imposed in respect of futures contracts traded by means of ATS.

¹ Other ATS providers that are currently authorized by the SFC either do not offer exchange-like platforms (e.g. some only offer order routing services), or if they do, they are established overseas exchanges or trading platforms that are primarily regulated in their home jurisdiction with the SFC playing a relatively minor regulatory role in respect of activities in Hong Kong.

² Under section 19 of the SFO, both a recognized exchange company and an authorized ATS provider may operate a futures market.

8. However, given the different nature of ATS that may be authorized by the SFC, and the different extent of the SFC's regulatory role in respect of them, we propose that the legislation provide different levies to be payable in respect of different ATS. Specifically, we propose that –

- (a) in the case of any futures contracts traded by means of ATS provided by HKMEx, the SFC levy should be set at a general level of HK\$0.60 per contract per side; and
- (b) in the case of any futures contracts traded by means of any other ATS, the SFC levy should be set at nil.

9. The above proposal would allow futures contracts traded on HKMEx to be subject to an SFC levy at a rate that is comparable to the general one currently set in respect of HKFE contracts, thereby ensuring a level playing field between the two operations. At the same time, other ATS currently authorized by the SFC would remain unaffected. This would be appropriate given that these other ATS operations are either not exchange-like operations and futures contracts are not traded through such services, or they are not solely or primarily regulated by the SFC, and hence there is no justification to impose an SFC levy.

OTHER OPTIONS

10. As the rate of levies is specified in the Securities and Futures (Levy) Order and the rules governing the payment of levies are provided in the Securities and Futures (Levy) Rules, amendments have to be made to the two pieces of subsidiary legislation before levies can be specified on the sale and purchase of futures contracts traded by means of ATS. Non-legislative options are not available.

THE SECURITIES AND FUTURES (LEVY) (AMENDMENT) ORDER 2011 (THE ORDER)

11. The Order, at Annex A, seeks to amend the Securities and Futures (Levy) Order to impose a levy payable to the SFC in respect of the sale and purchase of a futures contract traded by means of authorized ATS.

12. **Section 3** of the Order adds a new Part 4 to the Securities and Futures (Levy) Order. It specifies that –

- (a) a levy of \$0.60 on the seller and the purchaser is payable in respect of the sale and purchase of a futures contract traded by means of authorized ATS provided by HKMEx; and
 - (b) a nil levy in respect of futures contracts traded by means of authorized ATS provided by a person other than HKMEx.
13. The new Part 4 also provides the following –
- (a) payment of any levy is in any event exempted for a period of six months commencing on the first day of trading in the futures contract in question. This exemption is consistent with the current arrangement under Part 3 of the Securities and Futures (Levy) Order for new futures contracts traded on HKFE;
 - (b) the levy will not in any event be payable in respect of futures contracts that are bought or sold before the Order comes into effect. This is to ensure the Order does not have retrospective effect; and
 - (c) in calculating the six month levy exemption period, any period of trading conducted before the Order comes into effect may be taken into account. This is to clarify that the exemption period need not start counting from the date the Order comes into effect. This is in line with previous practice.

THE SECURITIES AND FUTURES (LEVY) (AMENDMENT) RULES 2011 (THE RULES)

14. The Rules, at Annex B, seek to amend the Securities and Futures (Levy) Rules to extend their application to cover levies payable in respect of the sale and purchase of futures contracts traded by means of authorized ATS. The main provisions are as follows –

- (a) **Section 3** of the Rules replaces the definition of “Exchange Company” by the new definition of “Market Operator” which includes the Stock Exchange Company, recognized exchange companies that operate futures markets and authorized ATS providers; and
- (b) **Sections 4 to 12** of the Rules make consequential amendments to the Securities and Futures (Levy) Rules by replacing “Exchange Company” with “Market Operator”, and allowing for the possibility that a market operator may be a non-Hong Kong company.

C The existing provisions being amended are at Annex C.

15. The Order and the Rules, if made, will come into operation on 18 November 2011, which will tie in with the expiry of the six-month levy exemption after the first trading of gold futures contracts by HKMEX.

LEGISLATIVE TIMETABLE

16. The legislative timetable is as follows –

Publication in Gazette	8 July 2011
Tabling at the Legislative Council (LegCo) for negative vetting	13 July 2011

IMPLICATIONS OF THE PROPOSAL

Financial and Civil Service Implications

17. There are no financial and civil service implications to the Government arising from the proposal. Section 14 of the SFO provides that the Government shall provide funding to the SFC as appropriated by the LegCo. In practice, the SFC has not requested for appropriation from LegCo since 1993-94. Its funding basically comes from the market in the form of levies, fees and charges.

Economic Implications

18. Imposing SFC levies on futures contracts traded by means of authorized ATS will ensure a level playing field between market operators, and is thus conducive to the development of Hong Kong's securities and futures markets.

Other Implications

19. The proposal is in conformity with the Basic Law, including the provisions concerning human rights. It does not affect the current binding effect of the existing provisions of the SFO and its subsidiary legislation. It has no environmental or sustainability implications.

PUBLIC CONSULTATION

20. The proposal will ensure a level playing field between market operators and is not controversial. Public consultation and submission to the Panel on Financial Affairs of LegCo are considered not necessary.

PUBLICITY

21. A press release will be issued upon gazette of the Rules and the Order on 8 July 2011. A spokesman will be available to handle media enquiries.

BACKGROUND

22. Pursuant to section 394 of the SFO, the Chief Executive in Council may specify the rate of levy payable to the SFC by an order published in the Gazette and make rules on various matters relating to the collection, payment and refund of SFC levies and the keeping and inspection of related accounts.

ENQUIRIES

23. Any enquiries on this brief may be addressed to Ms Mandy Wong, Principal Assistant Secretary for Financial Services and the Treasury (Financial Services) (1), at telephone number 2528 9493.

**Financial Service Branch
Financial Services and the Treasury Bureau
6 July 2011**

Securities and Futures (Levy) (Amendment) Order 2011

(Made by the Chief Executive in Council under section 394 of the Securities and Futures Ordinance (Cap. 571))

1. Commencement

This Order comes into operation on 18 November 2011.

2. Securities and Futures (Levy) Order amended

The Securities and Futures (Levy) Order (Cap. 571 sub. leg. Z) is amended as set out in section 3.

3. Part 4 added

After Part 3—

Add

“Part 4

Levy Payable in respect of Sale and Purchase of Futures Contracts Described in Section 394(1)(c) of Ordinance

14. Application of Part 4

This Part applies in relation to a sale and purchase of a futures contract traded by means of authorized automated trading services.

15. Futures contracts traded by means of authorized automated trading services

(1) Subject to subsections (2) and (3), for the purposes of section 394(1)(c) of the Ordinance, the levy payable for a sale and purchase of a futures contract traded by means

of authorized automated trading services provided by Hong Kong Mercantile Exchange Limited—

(a) is payable by the seller and purchaser; and
(b) is—

- (i) in the case of the seller, \$0.60; or
- (ii) in the case of the purchaser, \$0.60.

- (2) For the purposes of section 394(1)(c) of the Ordinance, the levy payable for a sale and purchase of a futures contract traded by means of authorized automated trading services provided by a person other than Hong Kong Mercantile Exchange Limited is nil.
- (3) During the period of 6 months commencing on the first day of trading in a futures contract by means of authorized automated trading services, the levy payable under subsection (1) by the seller and purchaser for the sale and purchase of the futures contract is nil.
- (4) If a sale and purchase of a futures contract traded by means of authorized automated trading services occurs before the commencement date of the Securities and Futures (Levy) (Amendment) Order 2011 (L.N. of 2011)—
 - (a) subsection (3) does not have the effect of specifying a rate or an amount of levy on that sale and purchase; and
 - (b) in calculating a period of 6 months for the purposes of subsection (3), regard may be had to any period of trading conducted before that date.”.

Clerk to the Executive Council
COUNCIL CHAMBER

2011

Explanatory Note

The purpose of this Order is to amend the Securities and Futures (Levy) Order (Cap. 571 sub. leg. Z) by adding a new Part 4 to impose, for the purposes of section 394(1)(c) of the Securities and Futures Ordinance (Cap. 571), a levy payable to the Securities and Futures Commission (*Commission*) in respect of a sale and purchase of futures contracts traded by means of authorized automated trading services (*ATS*).

2. The effect of this Order is that a levy of \$0.60 on each of the seller and purchaser is payable in respect of a sale and purchase of a futures contract traded by means of authorized ATS provided by Hong Kong Mercantile Exchange Limited (*HKMEx*). However, the levy of \$0.60 is exempted for a period of 6 months commencing on the first day of trading in the futures contract by means of authorized ATS provided by HKMEx. The levy payable is nil if the futures contract is traded by means of authorized ATS provided by other operators.

Securities and Futures (Levy) (Amendment) Rules 2011

(Made by the Chief Executive in Council under section 394 of the Securities and Futures Ordinance (Cap. 571))

1. Commencement

These Rules come into operation on 18 November 2011.

2. Securities and Futures (Levy) Rules amended

The Securities and Futures (Levy) Rules (Cap. 571 sub. leg. AA) are amended as set out in sections 3 to 12.

3. Section 2 amended (Interpretation)

(1) Section 2—

Repeal the definition of *Exchange Company*.

(2) Section 2, definition of *levy*—

Repeal

“(a) or (b)”.

(3) Section 2, definition of *remittance*—

Repeal

“Exchange Company”

Substitute

“Market Operator”.

(4) Section 2—

Add in alphabetical order

“**Market Operator** (市場營辦者)—

(a) in relation to a levy payable under section 394(1)(a) of the Ordinance, means the Stock Exchange Company;

(b) in relation to a levy payable under section 394(1)(b) of the Ordinance, means the recognized exchange company that operates the futures market on which the futures contract is traded;

(c) in relation to a levy payable under section 394(1)(c) of the Ordinance, means the person who provides the authorized automated trading services by means of which the futures contract is traded;”.

4. Section 3 amended (Payment of levy)

(1) Section 3—

Renumber the section as section 3(1).

(2) Section 3(1)—

Repeal

“Exchange Company” (wherever appearing)

Substitute

“Market Operator”.

(3) After section 3(1)—

Add

“(2) In subsection (1)—

rules of the Market Operator (市場營辦者規章)—

(a) in the case of a person who provides authorized automated trading services, means the rules of the person as approved, if required, by the Commission under section 97(3)(a) of the Ordinance;

(b) in the case of any other Market Operator, has the same meaning as **rules** has, in relation to that Market Operator, under section 1 of Part 1 of Schedule 1 to the Ordinance.”.

- 5. Section 4 amended (Exchange Company to remit levies)**
- (1) Section 4, heading—
Repeal
 “Exchange Company”
Substitute
 “Market Operator”.
- (2) Section 4—
Repeal
 “Exchange Company”
Substitute
 “Market Operator”.
- 6. Section 5 amended (Returns relating to remittance)**
- (1) Section 5(1)—
Repeal
 “Exchange Company”
Substitute
 “Market Operator”.
- (2) Section 5(2)(b)—
Repeal
 “Exchange Company” (wherever appearing)
Substitute
 “Market Operator”.
- 7. Section 6 amended (Adjustment of remittance and returns)**
 Section 6—
Repeal
 “Exchange Company”

- Substitute**
 “Market Operator”.
- 8. Section 7 amended (Late remittance charge)**
 Section 7(1)—
Repeal
 “Exchange Company”
Substitute
 “Market Operator”.
- 9. Section 8 amended (Accounts)**
 Section 8—
Repeal
 “Exchange Company”
Substitute
 “Market Operator”.
- 10. Section 9 amended (Inspection of accounts)**
 Section 9—
Repeal
 “Exchange Company”
Substitute
 “Market Operator”.
- 11. Section 10 amended (Report)**
 (1) Section 10(1)—
Repeal
 “Exchange Company”
Substitute

“Market Operator”.

(2) Section 10(2)—

Repeal paragraph (b)

Substitute

“(b) prepared and certified, at the expense of the Market Operator, by—

- (i) an auditor appointed by the Market Operator under the Companies Ordinance (Cap. 32); or
- (ii) if the Market Operator is a non-Hong Kong company and is registered under Part XI of that Ordinance, an auditor appointed by the Market Operator.”.

12. Section 12 amended (Notification of failure to pay levy)

Section 12—

Repeal

“Exchange Company”

Substitute

“Market Operator”.

Clerk to the Executive Council

COUNCIL CHAMBER

2011

Explanatory Note

The Securities and Futures (Levy) Rules (Cap. 571 sub. leg. AA) (*principal Rules*) provide for various matters relating to the payment of levies payable to the Securities and Futures Commission in respect of the sale and purchase of futures contracts and securities, including the imposition of charges for late payment of such levies and the keeping and inspection of accounts relating to the collection and payment of such levies. The object of these Rules is to amend the principal Rules to extend the application of the principal Rules to cover levies payable in respect of the sale and purchase of futures contracts traded by means of authorized automated trading services.

2. The definition of *Exchange Company* is replaced by the new definition of *Market Operator* which includes the Stock Exchange Company, a recognized exchange company and an authorized automated trading services provider.
3. The Rules amend section 10(2)(b) of the principal Rules to include an auditor appointed by a Market Operator otherwise than under the Companies Ordinance (Cap. 32) if it is a non-Hong Kong company registered under Part XI of that Ordinance.
4. The Rules also make consequential amendments to sections 3, 4, 5, 6, 7, 8, 9, 10 and 12 of the principal Rules by replacing “Exchange Company” with “Market Operator”.

Chapter 571AA	SECURITIES AND FUTURES (LEVY) RULES	Gazette Number	Version Date
Section 2	Interpretation	L.N. 222 of 2002; L.N. 12 of 2003	01/04/2003

In these Rules, unless the context otherwise requires-
"Exchange Company" (交易所)-

- (a) in relation to a levy payable under section 394(1)(a) of the Ordinance, means the Stock Exchange Company;
- (b) in relation to a levy payable under section 394(1)(b) of the Ordinance, means the Futures Exchange Company;

"levy" (徵費) means a levy payable under section 394(1)(a) or (b) of the Ordinance;

"remittance" (轉付) means a payment, by way of remittance, by the Exchange Company to the Commission under section 4.

Chapter 571AA	SECURITIES AND FUTURES (LEVY) RULES	Gazette Number	Version Date
Section 3	Payment of levy	L.N. 222 of 2002; L.N. 12 of 2003	01/04/2003

A person who is liable to pay a levy shall pay the levy to the Exchange Company in such manner as may be specified from time to time in the rules of the Exchange Company.

Chapter 571AA	SECURITIES AND FUTURES (LEVY) RULES	Gazette Number	Version Date
Section 4	Exchange Company to remit levies	L.N. 222 of 2002; L.N. 12 of 2003	01/04/2003

Where the Exchange Company has collected the levy paid to it under section 3, it shall pay the levy, by way of remittance, to the Commission by paying it into such bank account as may be specified by the Commission, on the 15th day of the month following the month of the collection of the levy or, where the 15th day is not a business day, on the next business day.

Chapter 571AA	SECURITIES AND FUTURES (LEVY) RULES	Gazette Number	Version Date
Section 5	Returns relating to remittance	L.N. 222 of 2002; L.N. 12 of 2003	01/04/2003

(1) Within 7 days after the date of each remittance, the Exchange Company shall furnish to the Commission a return relating to the remittance.

(2) A return furnished under subsection (1) shall-

- (a) be in such form as may be specified by the Commission;
- (b) be signed by a director of the Exchange Company authorized by the Exchange Company either generally or specifically for that purpose; and
- (c) contain such information as may be specified by the Commission.

Chapter 571AA	SECURITIES AND FUTURES (LEVY) RULES	Gazette Number	Version Date
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Annex C

Section 6	Adjustment of remittance and returns	L.N. 222 of 2002; L.N. 12 of 2003	01/04/2003
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A return or the amount of remittance to which it relates may be adjusted by the Exchange Company to reflect any error in a previous return or remittance (as the case may be).

Chapter 571AA	SECURITIES AND FUTURES (LEVY) RULES	Gazette Number	Version Date
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Section 7	Late remittance charge	L.N. 222 of 2002; L.N. 12 of 2003	01/04/2003
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(1) If the Exchange Company fails to remit any levy when required under these Rules, it shall pay to the Commission a late remittance charge of 2% above the average of the best lending rates respectively quoted by each note-issuing bank within the meaning of section 2 of the Legal Tender Notes Issue Ordinance (Cap 65), on the amount of the levy, calculated on a daily basis commencing on the date of default until remittance of the levy is made.

(2) The late remittance charge payable under subsection (1) is recoverable as a civil debt due to the Commission.

Chapter 571AA	SECURITIES AND FUTURES (LEVY) RULES	Gazette Number	Version Date
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Section 8	Accounts	L.N. 222 of 2002; L.N. 12 of 2003	01/04/2003
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The Exchange Company shall keep proper accounts in respect of all transactions relating to the collection and remittance of levies.

Chapter 571AA	SECURITIES AND FUTURES (LEVY) RULES	Gazette Number	Version Date
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Section 9	Inspection of accounts	L.N. 222 of 2002; L.N. 12 of 2003	01/04/2003
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For the purpose of ascertaining whether the Exchange Company is complying or has complied with any provision of these Rules, a person authorized in writing by the Commission may at any reasonable time, upon production of a copy of the authorization, inspect and make copies of the accounts kept under section 8.

Chapter 571AA	SECURITIES AND FUTURES (LEVY) RULES	Gazette Number	Version Date
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Section 10	Report	L.N. 222 of 2002; L.N. 12 of 2003	01/04/2003
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(1) The Exchange Company shall, within one month after 31 March in each year or such longer period as may be specified by the Commission either generally or in a particular case, furnish to the Commission a report certifying that the returns furnished under section 5 and relating to all remittances made in the 12 months ending on 31 March in that year are correct and comply with these Rules, and that the levies to which the remittances relate have been paid in accordance with the Securities and Futures (Levy) Order (Cap 571 sub. leg. Z).

(2) The report furnished under subsection (1) shall be-

- (a) in such form as may be specified by the Commission; and
- (b) prepared and certified, at the expense of the Exchange Company, by an auditor

Annex C

appointed by the Exchange Company under the Companies Ordinance (Cap 32).

Chapter 571AA	SECURITIES AND FUTURES (LEVY) RULES	Gazette Number	Version Date
Section 12	Notification of failure to pay levy	L.N. 222 of 2002; L.N. 12 of 2003	01/04/2003

Where the Exchange Company is aware that any person has failed to pay a levy payable by him, it shall as soon as reasonably practicable notify the Commission in writing of the failure.