

**LEGISLATIVE COUNCIL BRIEF**

Securities and Futures Ordinance  
(Chapter 571)

**Securities and Futures (Investor Compensation—Levy)  
(Amendment) Rules 2019**

**Securities and Futures (Investor Compensation—Compensation  
Limits) (Amendment) Rules 2019**

**Securities and Futures (Investor Compensation—Claims)  
(Amendment) Rules 2019**

**Securities and Futures Ordinance (Appointed Day—Dealers Deposit  
Scheme) Notice**

**INTRODUCTION**

At the meeting of the Executive Council on 17 September 2019, the Council ADVISED and the Chief Executive ORDERED that, pursuant to section 244(1) of the Securities and Futures Ordinance (“Cap. 571”) (“Ordinance”), the following Rules should be made and tabled before the Legislative Council (“LegCo”)–

- (i) the Securities and Futures (Investor Compensation—Levy) (Amendment) Rules 2019 (“Levy Amendment Rules”) (at **Annex A**); and
- (ii) the Securities and Futures (Investor Compensation—Compensation Limits) (Amendment) Rules 2019 (“Limits Amendment Rules”) (at **Annex B**); and

2. Moreover, the Securities and Futures Commission (“SFC”) has, pursuant to section 244(2) of the Ordinance, made the Securities and Futures (Investor Compensation—Claims) (Amendment) Rules 2019 (“Claims Amendment Rules”) (at **Annex C**).

3. The above Amendment Rules will enhance the Investor Compensation Regime (“Regime”) for the trading of securities and futures contracts. Separately, to begin the process to wind up the Dealers Deposit Scheme (“DDS”), which is one of the compensation funds/schemes replaced by the Regime, the Secretary for Financial Services and the Treasury (“SFST”) has, pursuant to section 76(13) of Part 1 of Schedule 10 to the Ordinance, made the Securities and Futures Ordinance (Appointed Day—Dealers Deposit Scheme) Notice (“DDS Notice”) (at **Annex D**).

## **JUSTIFICATIONS**

### **(a) Enhancement of the Regime**

4. The objective of the Regime is to provide a degree of compensation to investors who have sustained loss in relation to exchange-traded securities or futures contracts as a result of a default by their intermediary in Hong Kong. It came into operation under the administration of the SFC in 2003 when the Ordinance took effect. An Investor Compensation Fund (“ICF”) was established under the Regime for the payment of compensation.

5. The current compensation limit under the Regime is \$150,000 per investor per default in respect of exchange-traded securities-related losses and a further \$150,000 per investor per default in respect of futures contracts-related losses. The ICF is mainly funded by a transaction levy (“ICF levy”) payable by persons who buy or sell securities or futures contracts on the Stock Exchange of Hong Kong (“SEHK”) or the Hong Kong Futures Exchange. A mechanism is in place under the Regime for suspending and reinstating the ICF levy when the net asset value of the ICF reaches certain trigger levels. This is to ensure that the size of the ICF is maintained at an appropriate level that allows for the payment of compensation when needed but does not result in the accumulation of excessive amounts at the market’s expense. Under this mechanism, the payment of ICF levy has been suspended since 2005. The key features of the Regime are at **Annex E**.

### *Need for further enhancements*

6. The SFC reviews the Regime from time to time, and if necessary, introduces enhancements to ensure that the arrangements are in keeping

with the times. In the last decade or so, our securities and futures markets have undergone substantial growth and development in terms of market capitalisation, average daily turnover, market reach and investor base<sup>1</sup>. Also, with the implementation of the Stock Connect programme<sup>2</sup>, the Hong Kong and Mainland stock markets are now accessible to investors in both markets. Against this backdrop, the SFC conducted a review of the Regime in 2017 and a public consultation exercise from April to June 2018 on the proposed enhancements to the Regime in certain areas. Taking into account the views received during the consultation exercise, the SFC proposes to enhance various aspects of the Regime as outlined in paragraphs 7 to 12 below.

### *The proposals*

#### *Raising the compensation limit*

7. According to surveys conducted by the SFC with selected intermediaries in 2014 and 2017, the value of client assets held with intermediaries has increased substantially<sup>3</sup> with the growth and development of our securities and futures markets. As a result, the present compensation limit of \$150,000 is no longer considered adequate<sup>4</sup>, and the SFC proposes that the **compensation limit be raised to \$500,000 per investor per default**. The proposal should keep the coverage ratio at a level of around 80%<sup>5</sup>. The proposed compensation limit of \$500,000 is on a par with the Hong Kong Monetary Authority's Deposit Protection

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<sup>1</sup> For example, between the end of 2008 and the end of 2018, the number of companies listed on the SEHK rose by 84% from 1 261 to 2 315. Market capitalisation almost tripled from about \$10 trillion to about \$30 trillion. Average daily turnover rose by about 49% from \$72 billion to \$107 billion. The number of exchange participants rose by 38% from 487 to 673.

<sup>2</sup> Stock Connect is a collaboration between the SEHK, Shanghai Stock Exchange and Shenzhen Stock Exchange to allow investors to trade securities in each other's markets through the trading and clearing facilities of their home exchange.

<sup>3</sup> The total value of client assets held with the securities intermediaries surveyed had increased by more than 50%, from \$598 billion in the 2014 survey to \$918 billion in the 2017 survey. For some intermediaries, the increase was close to or over 100%.

<sup>4</sup> For example, the survey results suggested that the \$150,000 compensation limit might have achieved an average coverage ratio (i.e. the estimated percentage of investors that would be compensated in full if their intermediary were to default) of about 75% in 2014. The ratio dropped to about 64% in 2017.

<sup>5</sup> The SFC generally aims for the compensation limit to achieve a coverage ratio of about 80%. This target may not always be met as it depends on the facts of a particular default case. If the compensation limit is raised to \$500,000, the average coverage ratio should rise to around 83%.

Scheme. While not directly comparable, the proposed limit is also within the range of that adopted by selected overseas jurisdictions<sup>6</sup>.

*Raising the trigger levels for levy suspension and reinstatement*

8. Consequential to the proposed increase in the compensation limit, it will be necessary to **raise the trigger levels for suspending and reinstating the ICF levy** to maintain a reasonable net asset level of the ICF without overburdening investors. **The SFC proposes to increase the suspension level from \$1.4 billion to \$3 billion, and the reinstatement level from \$1 billion to \$2 billion.** In proposing the new trigger levels, the SFC has taken into account the potential future growth in client assets and is cognizant of the need to ensure that the new levels should be sustainable for a reasonable period of time.

9. It should be noted that the proposed trigger levels above will not affect the levy suspension that is currently in place. This is because the net asset value of the ICF stands at \$2.39 billion at the moment, and is higher than the proposed reinstatement level.

*Adjusting coverage of the Regime to cater for the Stock Connect*

10. The SFC proposes to expand the coverage of the Regime so that it also **covers the northbound links of the Stock Connect** (i.e. trading on the Mainland stock markets through Hong Kong intermediaries and the facilities of the SEHK). The Regime is intended to protect investors against losses due to default by intermediaries in Hong Kong. As transactions under the northbound links of the Stock Connect must be routed through Hong Kong intermediaries, these transactions should be covered under the Regime as well. Consistent with this, transactions under the northbound links of the Stock Connect should also be subject to the ICF levy (if and when triggered) as mentioned in paragraphs 8 to 9 above.

11. On the other hand, there is no need for the Regime to also cover southbound trading under the Stock Connect. This is because such trading must be routed through Mainland regulated intermediaries, and

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<sup>6</sup> The SFC has looked into similar schemes adopted elsewhere including the European Union, Singapore, the United Kingdom, the United States and Canada. However, because these schemes differ in terms of the scope of persons and assets covered, and the circumstances in which compensation is paid, the limits adopted may not be directly comparable.

Hong Kong intermediaries play no role.

### *Amendments needed*

12. Three pieces of subsidiary legislation under the Ordinance have to be amended to implement the proposed enhancements. They include the Securities and Futures (Investor Compensation—Levy) Rules (Cap. 571 sub. leg. AB) (“Levy Rules”) and the Securities and Futures (Investor Compensation—Compensation Limits) Rules (Cap. 571 sub. leg. AC) (“Limits Rules”) (amended by the Chief Executive in Council (“CE-in-Council”) pursuant to section 244(1) of the Ordinance). The remaining one is the Securities and Futures (Investor Compensation—Claims) Rules (Cap. 571 sub. leg. T) (amended by the SFC in consultation with the Financial Secretary pursuant to section 244(2) of the Ordinance).

### **(b) Winding-up of the DDS**

13. When the ICF came into operation in 2003, it replaced the pre-Ordinance compensation funds/scheme which include the DDS<sup>7</sup>. Owing to certain technical legal issues, the winding-up procedures for the DDS have not commenced although it had ceased to operate since 2003<sup>8</sup>. The Ordinance was amended subsequently to deal with these technical issues<sup>9</sup>. We consider it timely to also take the opportunity to arrange for the winding-up of the DDS.

14. SFST has appointed 1 January 2020 as the appointed day to begin the process to wind up the DDS pursuant to section 76(13) of Part 1 of Schedule 10 to the Ordinance. After the appointed day, where there is any deposit or security forfeited by the SFC<sup>10</sup> under the DDS that has yet

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<sup>7</sup> The DDS was to compensate clients of a dealer (other than an exchange participant) or securities margin financier who sustained pecuniary loss because of a default by the dealer or financier. Its funding came from deposits paid by dealers and security lodged by securities margin financiers.

<sup>8</sup> As at 31 March 2019, the DDS had a balance of \$35.65 million from contributions made by dealers and securities margin financiers previously.

<sup>9</sup> Schedule 10 to the Ordinance was amended to rectify an anomaly with respect to transitional arrangements for the DDS for securities margin financiers, thereby enabling the winding-up of the DDS.

<sup>10</sup> The SFC may forfeit a deposit made by a dealer or apply security lodged by a securities margin financier for compensation purposes under certain circumstances. Such circumstances include the conviction of an offence involving fraud in respect of client’s assets.

to be disposed of, the SFC will specify a day on or before which claims for compensation against any such deposit or security may be made by the clients of the dealer(s) or securities margin financier(s) concerned and determine the claims (if any). Any remaining balance held in the DDS will then be returned to the dealer which made the deposit or the financier which lodged the security. Where the SFC is unable to locate the dealer or financier within the specified period, the relevant money shall be transferred to the ICF.

## **OTHER OPTIONS**

15. We must make the subsidiary legislation to effect the enhancements to the Regime and the winding-up of the DDS. There is no other option.

## **THE SUBSIDIARY LEGISLATION**

### **Made by CE-in-Council**

16. The Levy Amendment Rules and the Limits Amendment Rules are made by CE-in-Council. The main purpose of the former is to amend the Levy Rules to –

- (a) also apply the ICF levy to transactions of Stock Connect securities under the northbound links of the Stock Connect;
- (b) amend the trigger levels for suspending and reinstating the ICF levy; and
- (c) provide that the exemption notice on the suspension of ICF levy published on 11 November 2005 continues to be in effect despite the amendments to the Levy Rules.

The main purpose of the latter is to increase the compensation limits under the Limits Rules to \$500,000 per investor per default in respect of losses resulting from the default of an intermediary occurring on or after 1 January 2020.

## **Made by the SFC**

17. The main purpose of the Claims Amendment Rules is to expand the coverage of the Regime so that it also covers the northbound links of the Stock Connect.

## **Made by SFST**

18. The purpose of the DDS Notice is to appoint 1 January 2020 as the appointed day to begin the process to wind up the DDS.

## **LEGISLATIVE TIMETABLE**

19. The Levy Amendment Rules, the Limits Amendment Rules, the Claims Amendment Rules and the DDS Notice will be published in the Gazette on 11 October 2019 for tabling before LegCo at its sitting on 16 October 2019. Subject to negative vetting by LegCo, the three sets of Amendment Rules will come into operation on 1 January 2020, and the appointed day to begin the process to wind up the DDS is also 1 January 2020.

## **IMPLICATIONS OF THE PROPOSAL**

20. The Amendment Rules and DDS Notice are in conformity with the Basic Law, including the provisions concerning human rights. They do not affect the current binding effect of the existing provisions of the Ordinance. There are no productivity, environmental, family, gender implications, and no sustainability implications other than the economic implications as set out in paragraph 21 below.

21. There are no financial or civil service implications for the Government as the Regime will continue to be administered by the Investor Compensation Company Limited (a wholly-owned subsidiary of the SFC) and funded mainly by the ICF levy, and the winding-up of the DDS will be overseen by the SFC. On economic implications, the enhancements to the Regime would strengthen investor protection and investor confidence in the securities and futures markets in Hong Kong. The winding-up of the DDS is a technical house-keeping matter.

## **PUBLIC CONSULTATION**

22. The SFC conducted a public consultation on the proposed enhancements to the Regime from April to June 2018 and received strong support for the proposed enhancements. The SFC has taken into account the comments received in finalising the proposals under paragraphs 7 to 12 above.

23. We briefed the LegCo Panel on Financial Affairs on the enhancements to the Regime and the plan to wind up the DDS on 19 February 2019. Members generally supported the proposals.

## **ENQUIRIES**

24. Enquiries relating to this brief can be directed to Ms Estrella Cheung, Principal Assistant Secretary for Financial Services and the Treasury (Financial Services), at 2810 2054.

**Financial Services and the Treasury Bureau  
Securities and Futures Commission  
9 October 2019**



**Securities and Futures (Investor Compensation—Levy)  
(Amendment) Rules 2019**

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## Securities and Futures (Investor Compensation—Levy) (Amendment) Rules 2019

(Made by the Chief Executive in Council under section 244(1) of the Securities and Futures Ordinance (Cap. 571))

### 1. Commencement

These Rules come into operation on 1 January 2020.

### 2. Securities and Futures (Investor Compensation—Levy) Rules amended

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

### 3. Section 2 amended (interpretation)

Section 2—

#### Add in alphabetical order

“*Claims Rules* (《申索規則》) means the Securities and Futures (Investor Compensation—Claims) Rules (Cap. 571 sub. leg. T);

*Hong Kong securities* (香港證券) means any securities that are listed or traded, or to be listed or traded, on a recognized stock market;

*northbound link* (北向通) has the meaning given by section 2 of the Claims Rules;

*southbound link* (南向通), in relation to a Stock Connect arrangement, means the facilities provided or arranged by the operator of the relevant Stock Connect market under the arrangement—

(a) for routing orders for the sale or purchase of securities for execution on a recognized stock market operated by the Stock Exchange Company; and

(b) for handling matters relating to those securities;

*Stock Connect arrangement* (互聯互通安排) has the meaning given by section 2 of the Claims Rules;

*Stock Connect market* (互聯互通市場) has the meaning given by section 2 of the Claims Rules;

*Stock Connect securities* (互聯互通證券) has the meaning given by section 2 of the Claims Rules;”.

### 4. Part 2 heading amended (levy payable in respect of sale and purchase of securities)

Part 2, heading—

**Repeal**

“and”

**Substitute**

“or”.

### 5. Section 3 amended (application of Part 2)

Section 3—

**Repeal subsection (1)**

**Substitute**

“(1) This Part applies only to—

(a) a sale or purchase of Hong Kong securities—

(i) that is recorded on a recognized stock market or notified to a recognized exchange company under its rules; and

(ii) the order for which is not routed through the southbound link of a Stock Connect arrangement; and

(b) a sale or purchase of Stock Connect securities, the order for which is routed through the northbound link of a Stock Connect arrangement.”.

**6. Section 4 amended (securities)**

Section 4—

**Repeal**

everything after “levy”

**Substitute**

“is payable to the Commission—

(a) for a sale of securities—by the seller at the rate of 0.002% of the consideration for the sale; and

(b) for a purchase of securities—by the purchaser at the rate of 0.002% of the consideration for the purchase.”.

**7. Section 5 amended (no levy on stock options)**

Section 5—

**Repeal**

“and purchase of a stock option shall be”

**Substitute**

“or purchase of a stock option is”.

**8. Section 7A amended (no levy on sale and purchase of securities by securities market maker permit holders)**

(1) Section 7A, heading—

**Repeal**

“and”

**Substitute**

“or”.

(2) Section 7A, English text—

**Repeal**

“shall be”

**Substitute**

“is”.

**9. Section 24 amended (Commission to cause financial statement to be audited)**

(1) Section 24(1)—

**Repeal**

“\$1,400,000,000 as at that day, the Commission shall”

**Substitute**

“\$3 billion as at that day, the Commission must”.

(2) Section 24(2)—

**Repeal**

“\$1,000,000,000 as at that day, the Commission shall”

**Substitute**

“\$2 billion as at that day, the Commission must”.

**10. Section 25 amended (Commission to publish exemption notice)**

(1) Section 25(1)—

**Repeal**

“\$1,400,000,000, the Commission shall”

- Substitute**  
“\$3 billion, the Commission must”.
- (2) Section 25(1)—  
**Repeal**  
“sale and”  
**Substitute**  
“sale or”.
- (3) Section 25(1)(a), English text—  
**Repeal**  
“shall”  
**Substitute**  
“may”.
- (4) Section 25(2), English text—  
**Repeal**  
“shall”  
**Substitute**  
“may”.
- (5) Section 25(3), English text—  
**Repeal**  
“shall”  
**Substitute**  
“may”.
- (6) Section 25(4)—  
**Repeal**  
“\$1,000,000,000”  
**Substitute**

- “\$2 billion”.
- (7) Section 25(5)—  
**Repeal**  
“\$1,000,000,000”  
**Substitute**  
“\$2 billion”.
- (8) Section 25(5), English text—  
**Repeal**  
“shall”  
**Substitute**  
“must”.
11. **Section 26 amended (Commission to publish termination of exemption notice)**
- (1) Section 26(1)(a)—  
**Repeal**  
“\$1,000,000,000”  
**Substitute**  
“\$2 billion”.
- (2) Section 26(1), English text—  
**Repeal**  
“Commission shall”  
**Substitute**  
“Commission must”.
- (3) Section 26(1), English text—  
**Repeal**  
“date shall”

**Substitute**

“date may”.

- (4) Section 26(2), English text—

**Repeal**

“shall”

**Substitute**

“does”.

- (5) Section 26(3)—

**Repeal**

“\$1,400,000,000”

**Substitute**

“\$3 billion”.

- (6) Section 26(4)—

**Repeal**

“\$1,400,000,000”

**Substitute**

“\$3 billion”.

- (7) Section 26(4), English text—

**Repeal**

“shall”

**Substitute**

“must”.

**12. Section 27 added**

After section 26—

**Add**

**“27. Exemption notice published on 11 November 2005**

- (1) The Commission’s declaration that no person is required to pay any levy under Part 2 or 3, by the exemption notice published on 11 November 2005 under section 25(1), continues to have effect until the date to be specified for the exemption notice by a termination of exemption notice published under section 26(1).
- (2) To avoid doubt, subsection (1) applies—
  - (a) despite the amendments made to this Part by sections 9, 10 and 11 of the Securities and Futures (Investor Compensation—Levy) (Amendment) Rules 2019; and
  - (b) regardless of the net asset value of the compensation fund on 1 January 2020.”.

Clerk to the Executive Council

COUNCIL CHAMBER

2019

### Explanatory Note

Section 236 of the Securities and Futures Ordinance (Cap. 571) established the Investor Compensation Fund (*ICF*). The Securities and Futures (Investor Compensation—Levy) Rules (Cap. 571 sub. leg. AB) (*Levy Rules*) provide for levy payable for the purposes of the ICF.

2. Under the arrangements commonly known as Stock Connect—
  - (a) there is mutual market access between The Stock Exchange of Hong Kong Limited (*SEHK*) and the following exchanges—
    - (i) the Shanghai Stock Exchange (*SSE*);
    - (ii) the Shenzhen Stock Exchange (*SZE*); and
  - (b) investors may—
    - (i) sell or purchase certain securities traded on a market operated by the SSE or SZE through the northbound links of Stock Connect (*northbound sale or purchase*); or
    - (ii) sell or purchase certain securities traded on a market operated by the SEHK through the southbound links of Stock Connect (*southbound sale or purchase*).
3. These Rules amend the Levy Rules to provide that—
  - (a) a levy is payable for a northbound sale or purchase; and
  - (b) no levy is payable for a southbound sale or purchase.
4. Part 5 of the Levy Rules provides for a levy suspension and reinstatement mechanism. If the ICF's net asset value exceeds \$1.4 billion, the Securities and Futures Commission (*SFC*) may suspend any levy. After a suspension, the SFC may reinstate the levy if the

ICF's net asset value falls below \$1 billion. These Rules adjust those 2 trigger values to \$3 billion and \$2 billion respectively.

**Securities and Futures (Investor Compensation—  
Compensation Limits) (Amendment) Rules 2019**

(Made by the Chief Executive in Council under section 244(1) of the Securities and Futures Ordinance (Cap. 571))

**1. Commencement**

These Rules come into operation on 1 January 2020.

**2. Securities and Futures (Investor Compensation—  
Compensation Limits) Rules amended**

The Securities and Futures (Investor Compensation—Compensation Limits) Rules (Cap. 571 sub. leg. AC) are amended as set out in sections 3 and 4.

**3. Section 2 amended (interpretation)**

(1) Section 2—

**Repeal the definition of *associated person*, *claimant*, *default*, *related assets* and *specified person*.**

(2) Section 2, definition of *Claims Rules*—

**Repeal**

“sub. leg. T).”

**Substitute**

“sub. leg. T);”.

(3) Section 2—

**Add in alphabetical order**

“*associated person* (相聯者) has the meaning given by section 2 of the Claims Rules;

*claimant* (申索人) has the meaning given by section 2 of the Claims Rules;

*default* (違責) has the meaning given by section 2 of the Claims Rules;

*default date* (違責日期), in relation to a default, means—

(a) the date of the default determined by the Commission under section 7(1)(b) of the Claims Rules;

(b) if the Tribunal varies or confirms, under Part XI of the Ordinance, the date of the default determined by the Commission—the date as varied or confirmed by the Tribunal; or

(c) if the Court of Appeal varies, under Part XI of the Ordinance, the date of the default as varied or confirmed by the Tribunal (if any)—the date as varied by the Court of Appeal;

*related assets* (有連繫資產) has the meaning given by section 2 of the Claims Rules;

*specified person* (指明人士) has the meaning given by section 2 of the Claims Rules;

*Stock Connect securities* (互聯互通證券) has the meaning given by section 2 of the Claims Rules;

*Tribunal* (審裁處) means the Securities and Futures Appeals Tribunal established by section 216 of the Ordinance.”.

**4. Section 3 substituted**

Section 3—

**Repeal the section**

**Substitute**

**“3. Limits on compensation to be made to claimants**

- (1) If a claimant claims compensation in respect of the claimant’s loss sustained as a result of a default committed—
  - (a) by—
    - (i) a specified person; or
    - (ii) any associated person of a specified person; and
  - (b) in relation to—
    - (i) any of the following securities—
      - (A) securities listed or traded, or to be listed or traded, on a recognized stock market;
      - (B) Stock Connect securities; and
    - (ii) related assets of the securities,

the total amount of compensation payable under section 9 of the Claims Rules to the claimant must not exceed the sum specified in subsection (3).
- (2) If a claimant claims compensation in respect of the claimant’s loss sustained as a result of a default committed—
  - (a) by—
    - (i) a specified person; or
    - (ii) any associated person of a specified person; and
  - (b) in relation to—
    - (i) any futures contract traded on a recognized futures market; and
    - (ii) related assets of the futures contract,

the total amount of compensation payable under section 9 of the Claims Rules to the claimant must not exceed the sum specified in subsection (3).

- (3) The following sum is specified for subsections (1) and (2)—
  - (a) if the default date is before 1 January 2020—\$150,000;
  - (b) if the default date is after 31 December 2019—\$500,000.”.

Clerk to the Executive Council

COUNCIL CHAMBER

2019

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### Explanatory Note

The main objective of these Rules is to amend the Securities and Futures (Investor Compensation—Compensation Limits) Rules (Cap. 571 sub. leg. AC) (*Limits Rules*)—

- (a) to increase the maximum amount of compensation payable under section 9 of the Securities and Futures (Investor Compensation—Claims) Rules (Cap. 571 sub. leg. T) (*Claims Rules*) from \$150,000 to \$500,000; and
- (b) to amend section 3 of the Limits Rules (consequential to the amendments made by the Securities and Futures (Investor Compensation—Claims) (Amendment) Rules 2019, which extend the compensation scheme under the Claims Rules to cover securities traded under the northbound links of the arrangements commonly known as Stock Connect).

## Securities and Futures (Investor Compensation— Claims) (Amendment) Rules 2019

(Made by the Securities and Futures Commission under section 244(2) of the Securities and Futures Ordinance (Cap. 571) after consultation with the Financial Secretary)

### 1. Commencement

These Rules come into operation on 1 January 2020.

### 2. Securities and Futures (Investor Compensation—Claims) Rules amended

The Securities and Futures (Investor Compensation—Claims) Rules (Cap. 571 sub. leg. T) are amended as set out in sections 3 to 6.

### 3. Section 2 amended (interpretation)

#### (1) Section 2—

**Repeal the definition of *associated person***

**Substitute**

“*associated person* (相聯者) has the meaning given by section 236(2) of the Ordinance;”.

#### (2) Section 2—

**Repeal the definition of *related assets***

**Substitute**

“*related assets* (有連繫資產) means money and other property that relate to the—

- (a) purchase;
- (b) sale;

(c) holding;

(d) pledge;

(e) adjustment;

(f) exercise; or

(g) expiry,

of specified securities or futures contracts;”.

#### (3) Section 2—

**Repeal the definition of *specified person***

**Substitute**

“*specified person* (指明人士) has the meaning given by section 236(2) of the Ordinance;

**Note—**

See also section 2A.”.

#### (4) Section 2—

**Repeal the definition of *specified securities or futures contracts***

**Substitute**

“*specified securities or futures contracts* (指明證券或期貨合約) has the meaning given by section 236(2) of the Ordinance;

**Note—**

See also section 2B.”.

#### (5) Section 2—

**Add in alphabetical order**

“*northbound link* (北向通), in relation to a Stock Connect arrangement, means the facilities provided or arranged by the Stock Exchange Company under the arrangement—

- (a) for routing orders for the sale or purchase of securities for execution on the relevant Stock Connect market; and
- (b) for handling matters relating to those securities;

**Stock Connect arrangement** (互聯互通安排) means the arrangement between the Stock Exchange Company and the operator of a Stock Connect market that facilitates mutual market access through facilities for routing orders for the sale or purchase of securities and for handling matters relating to those securities;

**Stock Connect market** (互聯互通市場) means a stock market operated by the Shanghai Stock Exchange or the Shenzhen Stock Exchange;

**Stock Connect securities** (互聯互通證券) means any securities—

- (a) that are listed or traded or to be listed or traded on a Stock Connect market; and
- (b) in respect of which an order for sale or purchase is permitted to be routed through the northbound link of a Stock Connect arrangement under the rules of the Stock Exchange Company;”.

#### 4. Sections 2A and 2B added

Part 1, after section 2—

**Add**

##### “2A. Prescription of persons for definition of *specified person*

An authorized financial institution that provides securities margin financing is prescribed for the purposes of paragraph (c) of the definition of *specified person* in section 236(2) of the Ordinance.

#### 2B. Prescription of markets for definition of *specified securities or futures contracts*

A Stock Connect market is prescribed for the purposes of paragraph (b) of the definition of *specified securities or futures contracts* in section 236(2) of the Ordinance, but only to the extent that the market relates to Stock Connect securities.”.

#### 5. Section 4 amended (making a claim for compensation)

Section 4—

##### Repeal subsection (1)

##### Substitute

“(1) Subject to subsections (1AA) and (1A), if—

- (a) a qualifying client of a specified person sustains a loss, as a result of a default committed on or after the appointed day by—
  - (i) the specified person; or
  - (ii) an associated person of the specified person, in relation to any specified securities or futures contracts or related assets;
- (b) the specified securities or futures contracts or related assets are entrusted to or received by the specified person or the associated person; and
- (c) the qualifying client is entitled to, or has a beneficial interest in, the specified securities or futures contracts or related assets,

the qualifying client may claim compensation from the compensation fund in respect of the loss.

(1AA) In relation to Stock Connect securities or related assets that relate to Stock Connect securities, a qualifying

client must not claim compensation from the compensation fund unless the securities were or were to be—

(a) purchased; or

(b) otherwise acquired,

through the northbound link of a Stock Connect arrangement.”.

**6. Section 7 amended (determination by Commission)**

Section 7(3)(a)(ii)—

**Repeal**

“any specified securities, futures contracts”

**Substitute**

“any specified securities or futures contracts”.

Chief Executive Officer,  
Securities and Futures Commission

2019

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**Explanatory Note**

Section 236 of the Securities and Futures Ordinance (Cap. 571) established the Investor Compensation Fund (*ICF*). The Securities and Futures (Investor Compensation—Claims) Rules (Cap. 571 sub. leg. T) (*Claims Rules*), among other things, set out the circumstances in which a person is entitled to claim compensation, including the types of securities in relation to which a qualifying client of a specified person who has sustained a loss as a result of a default committed by the specified person (or an associated person of the specified person) may claim compensation from the ICF in respect of the loss.

2. Under the mutual market access arrangements between The Stock Exchange of Hong Kong Limited and the Shanghai Stock Exchange (*SSE*) or the Shenzhen Stock Exchange (*SZE*), certain securities may be traded on markets operated by the SSE or SZE through certain Hong Kong intermediaries. These Rules amend the Claims Rules to expand the types of securities in respect of which a loss may be compensated to cover securities traded under the northbound links of the arrangements commonly known as Stock Connect.
3. Section 6 amends section 7(3)(a)(ii) of the Claims Rules to correct a typographical error.

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**Securities and Futures Ordinance (Appointed Day—  
Dealers Deposit Scheme) Notice**

Under section 76(13) of Part 1 of Schedule 10 to the Securities and Futures Ordinance (Cap. 571), I appoint 1 January 2020 as the appointed day for the purposes of section 76 of that Part.

Secretary for Financial Services and  
the Treasury

2019

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**Explanatory Note**

This Notice appoints a cut-off date for the Dealers Deposit Scheme in order to begin the process to wind up the Scheme. The Scheme is an old arrangement established before the enactment of the Securities and Futures Ordinance (Cap. 571), consisting of funds under the repealed Commodities Trading Ordinance (Cap. 250) and Securities Ordinance (Cap. 333).

**Key features of the Investor Compensation Regime (“Regime”)**

- (a) **Compensation fund:** An Investor Compensation Fund (“ICF”) was established under the Regime from which compensation payments are made. Its key funding sources are: (i) monies from the pre-Ordinance compensation funds/scheme<sup>1</sup>; (ii) transaction levies payable by investors when buying or selling securities or futures contracts on the Stock Exchange of Hong Kong (“SEHK”) or on the Hong Kong Futures Exchange (“HKFE”)<sup>2</sup>; and (iii) investment income such as bank deposit interest. The ICF is administered by the Investor Compensation Company Limited, a wholly-owned subsidiary of the Securities and Futures Commission.
- (b) **Compensation coverage:** The Regime covers losses in respect of securities or futures contracts that are listed or traded on the SEHK or the HKFE, as well as any related assets (e.g. related purchase monies or sale proceeds). Losses covered under the Regime should be those sustained as a result of the default of a dealing or financing intermediary<sup>3</sup> in Hong Kong, or a person related to such an intermediary (e.g. its employee).
- (c) **Compensation limit:** The Regime sets a limit on the amount of compensation that can be paid to an investor in the event of a default. The current limit is \$150,000 per investor per default. This limit applies to securities-related losses and futures contracts-related losses separately.
- (d) **Levy suspension and reinstatement mechanism:** The Regime provides for a mechanism for suspending and reinstating the ICF levy when the net asset value of the ICF reaches certain trigger levels.

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<sup>1</sup> They are the Unified Exchange Compensation Fund, the Futures Exchange Compensation Fund and the Dealers Deposit Scheme.

<sup>2</sup> The current ICF levy on securities transactions is 0.002% payable per side by the buyers and the sellers. For futures contracts, it is \$0.5 per side per contract or \$0.1 per side per mini contract or stock futures contract.

<sup>3</sup> A dealing or financing intermediary refers to an intermediary (i.e. bank or broker) that engages in dealing in securities or dealing in futures contracts or that provides securities margin financing.

The current levy suspension and levy reinstatement levels are \$1.4 billion and \$1 billion respectively. Pursuant to this mechanism, the collection of ICF levy has been suspended since December 2005. As of end-March 2019, the size of the ICF was around \$2.39 billion.