

LEGISLATIVE COUNCIL BRIEF

**STAMP DUTY ORDINANCE
(Chapter 117)**

Stamp Duty (Amendment) Bill 2022

INTRODUCTION

A At the meeting of the Executive Council on 15 November 2022, the Council **ADVISED** and the Chief Executive **ORDERED** that the Stamp Duty (Amendment) Bill 2022 (“the Bill”), at **Annex A**, should be introduced into the Legislative Council (“LegCo”).

JUSTIFICATIONS

Strategic Importance

2. Our country’s economy has transformed from emphasis on high-speed growth to high-quality development, accelerating the establishment of a new development framework in which “domestic circulation” plays a key role amidst the complementary domestic and external “dual circulation”. The 14th Five-Year Plan outlines that our country would steadily promote the internationalisation of Renminbi (“RMB”). It also supports Hong Kong to strengthen its functions as a global offshore RMB business hub. Hong Kong has the world’s largest offshore RMB liquidity pool¹ and RMB foreign exchange and interest rate derivatives market². With our leading advantages in RMB trading and settlement, financing and asset management, as well as

¹ As of August 2022, the total RMB deposits (including certificates of deposit) in Hong Kong amounted to RMB 987.9 billion.

² As of April 2022, the average daily RMB foreign exchange turnover reached over RMB 1,234.7 billion, 77.7% increase as compared to the same month in 2019.

supply of a diversified range of RMB products and services, Hong Kong is well-placed to continue serve as a “testing ground” and “firewall” in the process of RMB internationalisation.

3. With concerted efforts over the past years, Hong Kong is already offering a diversified range of offshore RMB products such as bonds, funds and derivative products. The Hong Kong Exchanges and Clearing Limited (“HKEX”) established a mechanism in 2010 to allow issuance and trading of RMB securities either under a single RMB-counter (“single-tranche, single-counter”) model or a “dual-tranche, dual-counter” (“DTDC”) model, both of which cover issuance, pricing, trading and settlement of RMB securities products. Notably, the DTDC model supports simultaneous issuance of both Hong Kong dollar (“HKD”) and RMB securities by the same issuer, trading under two separate counters in the secondary market, and transfer of shares between the two counters. HKEX has also set up a “RMB equity trading support facility”, a standby facility to enable investors to buy RMB-traded shares in HKD if they do not have sufficient RMB or have difficulty in obtaining RMB from other channels. However, the potential of using RMB in the stock market has yet to be fully realised.

Latest development in promoting the issuance and trading of RMB securities

4. To facilitate issuers to set up RMB counters and issue more RMB stocks, there is a need to improve the trading mechanism of dual-counter stock. A working group formed by the Securities and Futures Commission, HKEX and the Hong Kong Monetary Authority identified that the relatively low liquidity in RMB counters has resulted in a price difference between HKD and RMB counters of the same stock, which adversely affects investors’ willingness to participate in RMB counter. It therefore proposed setting up a dual-counter market maker (“DCMM”) scheme to provide continuous quotes and respond to quotation requests in the counter with lower liquidity (i.e. the current RMB counter), so as to facilitate trading by investors at their preferred prices and hence promote price efficiency. At the same time, DCMMs can also conduct arbitrage transactions between the two currency counters of the same stock, so that the prices of the two counters will converge over a long-term horizon.

5. HKEX has been operating a market maker regime for exchange-traded funds (“ETFs”) since 2001 and market marking arrangements were extended to RMB ETFs in 2012³. Benefiting from the exemption of stamp duty for relevant transactions⁴, the regime has proven to be effective in promoting liquidity in the ETF market⁵. Extending similar arrangements to dual-counter stocks will enhance the overall efficiency and quality of the trading mechanism of RMB stocks, promote the liquidity of RMB stocks, and avoid widening of spread and excessive price fluctuations caused by insufficient product liquidity. We collaborate with HKEX to engage top-tier issuers of Hang Seng Index constituent stocks with promising turnover, and around 20 issuers have indicated that they would give favourable considerations to setting up RMB counters in addition to HKD counters following the introduction of the DCMM scheme.

6. The mutual market access programme between stock exchanges of Shanghai and Hong Kong launched in November 2014, and expanded to Shenzhen in December 2016, presents added opportunities for increasing investor demand for RMB stocks. While the average daily turnover nearly tripled from 2017 to 2022⁶, Mainland investors currently can only participate in the Southbound Trading⁷ of Stock Connect using HKD. We have proposed and the China Securities Regulatory Commission (“CSRC”) announced in September 2022 that it supports and plans to study setting up a RMB stocks trading counter for Southbound Trading under the Stock Connect. Such arrangement will lower the exchange rate risk and cost borne by Mainland investors, while at the same time bring additional demand for RMB stocks in Hong Kong.

³ There is at least one market maker for each counter of an ETF.

⁴ The stamp duty payable for transfers of shares or units of all listed ETFs was exempted in 2015. Stamp duty payable on stock transfers conducted by market makers in the course of allotting and redeeming ETF units listed in Hong Kong was further exempted in 2020.

⁵ Average daily turnover of ETFs increased by 35% from 2020 to 2021.

⁶ Total trading value from Southbound Trading of Stock Connect increased from HKD 9.82 billion in 2017 to HKD 29.12 billion between January and September 2022.

⁷ Mainland investors purchase and sell stocks listed in Hong Kong.

THE PROPOSAL

Proposed dual-counter market maker regime

7. It is *proposed* that the role of DCMMs⁸ be assumed by exchange participants (“EPs”) meeting specified eligibility requirements, conducting two types of activities under the regime:

- (a) Market making activities - to continuously provide bid and ask quotes within a specified range of the latest market price in the RMB counter (i.e. the counter with lower liquidity at present) for matching investors’ orders. Their trading objective is primarily to fulfil their market making obligations; and
- (b) Liquidity providing activities mainly for arbitrage purpose - if one finds that the market price of the same dual-counter stock on two trading counters still differs having discounted the currency exchange rate, for example, where the price of HKD stock in RMB is higher than that of RMB stock, they will conduct liquidity providing activities such as arbitrage transactions to sell HKD shares and buy RMB shares to reap a margin from the price differences. A large number of arbitrage transactions can facilitate the convergence in prices of different counters of the same stock, while promoting the liquidity in both counters and benefitting the development of dual-counter stock in tandem with market conditions.

Proposed stamp duty exemption for certain transactions relating to dual-counter stock made by DCMMs

8. Under current legislation, DCMMs will need to pay stamp duty for transactions relating to dual-counter stock when their market making quotes in the RMB counter have been matched. Stamp duty also applies when DCMMs conduct arbitrage transactions between the two counters. This would add to the cost burden of DCMMs in conducting market making activities and liquidity providing activities, discouraging EPs to become

⁸ Similar to the ETF market maker scheme, this could be expanded to Designated Specialists which are clients of EPs in future.

DCMMs. This is not conducive to the policy objective of minimising the price difference between the two counters and promoting the liquidity of RMB stocks.

9. To incentivise EPs to become DCMMs, it is *proposed* to exempt the stamp duty payable on certain transactions relating to dual-counter stock made by DCMMs, so as to create favourable conditions for them to engage in market making and liquidity providing activities with lower transaction costs. A diagram showing the activities conducted by DCMMs is at **Annex B**.

B

10. To ensure smooth operation of the scheme, HKEX will draw on the prevailing effective arrangements in the market making mechanisms for ETFs and derivatives to formulate detailed administrative rules, including the requirements of eligible stocks, qualifications for DCMMs, registration procedures, obligations and rights of DCMMs, as well as to devise administrative arrangements with the Inland Revenue Department for exempting stamp duty payable on certain transactions relating to dual-counter stock made by DCMMs. HKEX will also set up a monitoring mechanism, including reviewing relevant trading activities, requiring DCMMs to maintain and report transaction information, etc., to ensure that DCMMs will not abuse the proposed stamp duty exemption and engage in market transactions to meet their own investment needs outside the capacity of a DCMM.

OTHER OPTIONS

11. Amending the Stamp Duty Ordinance (“SDO”) is the only way to give effect to the proposed stamp duty exemption. There is no other option.

THE BILL

12. The main provisions of the Bill are as follows –

- (a) Clause 3 amends section 19(1DA) of the SDO so that the obligation under section 19(1) imposed on a person who effects any sale or purchase of Hong Kong stock to make and execute a contract note and cause the note to be stamped under

head 2(1) or (2) in the First Schedule to SDO does not apply to a transaction relating to dual-counter stock made by a DCMM specified in the new Schedule 11;

- (b) Clause 4 amends section 63 of the SDO to empower the Financial Secretary to amend the new Schedule 11 by regulations; and
- (c) Clause 5 adds a new Schedule 11 to the SDO so as to provide for the definitions for certain key terms such as “dual-counter stock” and “market maker”, and to specify a sale or purchase of a dual-counter stock that is made by a DCMM as a transaction to which section 19(1) of the SDO does not apply so that the transactions will not be subject to stamp duty.

LEGISLATIVE TIMETABLE

13. The legislative timetable will be –

Publication in the Gazette	18 November 2022
First Reading and commencement of Second Reading debate	30 November 2022
Resumption of Second Reading debate, committee stage and Third Reading	To be notified

IMPLICATIONS OF THE PROPOSAL

14. The proposal is in conformity with the Basic Law, including the provisions concerning human rights. The proposal will not affect the binding effect of the existing provisions of the SDO. There are no civil service, productivity, environmental, gender or family implications arising from taking forward the proposal. There are no sustainability implications other than those set out in the economic implications paragraph. The proposal has the implications set out in the ensuing paragraphs.

Economic Implications

15. The proposed stamp duty exemption will reduce the transaction costs of eligible stock trading by DCMMs. This should create favourable conditions for DCMMs to engage in market making and liquidity providing activities, which are conducive to promoting the liquidity and price efficiency of RMB-denominated stocks.

Financial Implications

16. The proposed stamp duty exemption would only cover certain transactions relating to dual-counter stock made by DCMMs. In other words, ordinary investors engaging in RMB or HKD-denominated stock transactions would still need to pay stamp duty. Without the proposed exemption, it is likely that very few or even no EP will register as DCMMs to fulfil market making obligations and hence only a limited number of such transactions would be performed considering the size of transaction cost incurred. Therefore, there would only be notional revenue forgone on the part of Government. On the other hand, with improved liquidity and growth of RMB counters once the DCMM scheme is put in place, we expect that new investors will be attracted to participating in relevant trading in dual-counter stock, which should have a positive effect on overall market turnover and in turn have the potential of bringing about additional stamp duty revenue.

PUBLIC CONSULTATION

17. We consulted the LegCo Panel on Financial Affairs on 3 October 2022 regarding the legislative proposal. Members welcomed the proposed stamp duty exemption and asked for its early implementation. On the same day, around 20 major listed issuers in Hong Kong also spoke positively and indicated their willingness to explore setting up RMB counters in Hong Kong after the launch of the DCMM scheme.

PUBLICITY

18. We will issue a press release upon the gazettal of the Bill, and arrange a spokesperson to answer media enquiries.

ENQUIRIES

19. Enquiries relating to this brief can be directed to Mr Larry Chu, Principal Assistant Secretary for Financial Services and the Treasury (Financial Services), at 2810 2056.

Financial Services and the Treasury Bureau
16 November 2022

A BILL

To

Amend the Stamp Duty Ordinance to give effect to the proposal in the Budget introduced by the Government for the 2022–2023 financial year to waive the stamp duty payable on certain transactions relating to dual-counter stock made by market makers.

Enacted by the Legislative Council.

1. Short title

This Ordinance may be cited as the Stamp Duty (Amendment) Ordinance 2022.

2. Stamp Duty Ordinance amended

The Stamp Duty Ordinance (Cap. 117) is amended as set out in sections 3, 4 and 5.

3. Section 19 amended (contract notes, etc. in respect of sale and purchase of Hong Kong stock)

Section 19(1DA)—

Repeal

“or Part 2 of Schedule 10”

Substitute

“, Part 2 of Schedule 10 or Part 2 of Schedule 11”.

4. Section 63 amended (regulations)

Section 63(c)—

Repeal

“and 10”

Substitute

“, 10 and 11”.

5. Schedule 11 added

After Schedule 10—

Add

“Schedule 11

[ss. 19 & 63]

Transactions relating to Dual-counter Stock

Part 1

Interpretation

1. In this Schedule—

dual-counter stock (雙櫃台證券) means a Hong Kong stock in 2 tranches denominated in different currencies both of which may be traded in 2 counters, which are designated by a recognized exchange company (in accordance with the rules of the company) as the primary counter and the secondary counter of the stock;

market maker (莊家), in relation to a dual-counter stock, means a person approved by or registered with a recognized exchange company for performing (in

accordance with the rules of the company) market making or liquidity providing activities in respect of the stock;

rules (規章), in relation to a recognized exchange company, has the same meaning as it has in relation to a recognized exchange company in section 1 of Part 1 of Schedule 1 to the Securities and Futures Ordinance (Cap. 571);

sale or purchase (售賣或購買) has the meaning given by section 19(16).

Part 2

Transactions to which Section 19(1) does not Apply

1. A sale or purchase of a dual-counter stock that is made by a market maker of the stock.”

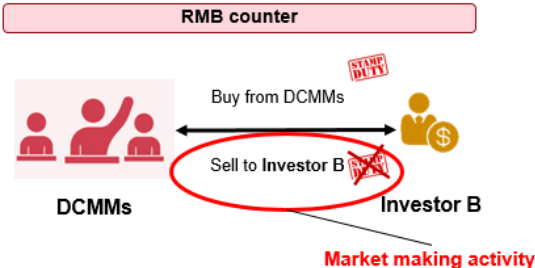
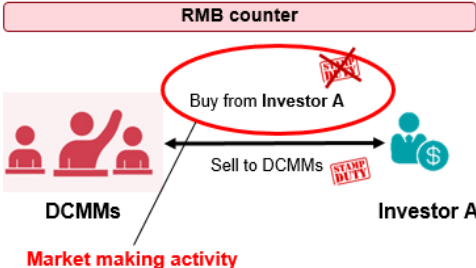
Explanatory Memorandum

The object of this Bill is to amend the Stamp Duty Ordinance (Cap. 117) (*Ordinance*) to waive the stamp duty payable on certain transactions relating to dual-counter stock made by market makers.

2. Clause 1 sets out the short title.
3. Section 19(1) of the Ordinance provides that a person who effects any sale or purchase of Hong Kong stock must execute a contract note and cause the note to be stamped under head 2(1) or (2) in the First Schedule to the Ordinance. Clause 3 amends section 19(1DA) of the Ordinance so that section 19(1) of the Ordinance does not apply to a transaction relating to dual-counter stock as specified in the new Schedule 11.
4. Clause 4 amends section 63 of the Ordinance to empower the Financial Secretary to amend the new Schedule 11 by regulations.
5. Clause 5 adds a new Schedule 11 to the Ordinance. Part 1 of the Schedule contains the definitions of certain terms, including *dual-counter stock* and *market maker*. Part 2 of the Schedule specifies a sale or purchase of a dual-counter stock that is made by a market maker of the stock as a transaction to which section 19(1) of the Ordinance does not apply.

Diagram showing activities conducted by DCMMs

(1) Market making activities



(2) Liquidity providing activities

