

Cross-Border Regulatory Co-operation

[This Chapter Is About]

- SFC's involvement in IOSCO
- Partnership with other regulators
- Combating money laundering
- Co-operation with Mainland China
- CEPA II
- Promoting international standards

What We Do

- Work with overseas regulators under co-operative arrangements;
- Participate actively in international securities regulators forum; and
- Develop and strengthen ties with Mainland authorities.

What We Did

The SFC does its best to contribute to the global efforts to enhance the quality and effectiveness of market regulation. We work closely with our counterparts worldwide and play an active role in the work of the International Organization of Securities Commissions (IOSCO). During the year, we further strengthened these ties.

We have 34 bilateral or multilateral co-operation arrangements with regulatory bodies around the world.



The SFC will host the 31st IOSCO Annual Conference in Hong Kong in 2006. This is the Conference logo.

IOSCO

IOSCO is the pre-eminent forum for international co-operation among securities regulators and is recognised as the international standard setter for the securities sector.

In May 2004, SFC Chairman Mr Andrew Sheng led a delegation to the Annual Conference of IOSCO in Amman, Jordan. During the conference, Mr Sheng was elected as the Chairman of the IOSCO Technical Committee for a two-year term. The SFC also set up an exhibition booth with poster display, videocast and souvenirs to promote the attractiveness and advantages of Hong Kong. Hong Kong will be hosting the IOSCO Annual Conference in June 2006. Preparation has started and a provisional conference website has been launched.

The Technical Committee successfully held its inaugural Technical Committee Conference in New York in October 2004 that has given IOSCO much greater visibility in the international financial

markets. The theme was Regulators and the Global Marketplace. The event was well attended by industry, academia, international financial institutions, and regulators from around the world.

In December 2004, IOSCO published the Code of Conduct Fundamentals for Credit Rating Agencies (CRAs). They represent a global, converged view of specific mechanisms CRAs can use to protect their analytical independence, eliminate or manage conflicts of interest, and appropriately handle confidential information shared with them by issuers.

The Code Fundamentals aim to promote investor protection by safeguarding the integrity of the rating process. CRAs are expected to incorporate the contents into their own code of conduct. The SFC actively participated in the Chairmen's Task Force of the Technical Committee which was responsible for developing the Code Fundamentals.

In March 2005, the Technical Committee released its Report on Strengthening Capital Markets Against Financial Fraud following an in-depth study of recent financial scandals involving large, global companies, including the discovery in December 2003 of financial improprieties at Parmalat S.p.A. in Italy.

The Technical Committee Task Force had looked into the regulatory issues exposed by these scandals. The Report outlines the issues and the action plan, including a description of priority work designed to rectify the most pressing concerns. The Report also sets out two overarching operational priorities for IOSCO's future: (1)

promoting implementation of existing international standards and principles; and (2) improving the abilities of securities regulators to co-operate with each other in enforcing existing securities laws and regulations. The Financial Stability Forum welcomed the report and the timely action taken by IOSCO to address the issues identified by the Task Force.

■ Multilateral Memorandum of Understanding

Adopted in May 2002, the IOSCO MMOU allows full investigatory co-operation among signatory jurisdictions. Hong Kong is one of the 26 signatories.

During the year, one more country signed the MMOU. Four more countries have committed themselves to changing their laws so they can become signatories. We sit on the committees that vet applications to the MMOU and monitor compliance with it.

■ Standing Committees under the IOSCO Technical Committee

The Corporate Finance Division participates in the Standing Committee on Multinational Disclosure and Accounting (SC1), which monitors and comments on international developments in accounting and auditing standards and drafts IOSCO standards relating to disclosure matters.

During the year, we continued to play an active role in SC1's Auditing Subcommittee and Accounting Subcommittee. We participated in the drafting of and responded to a survey on regulation and oversight of auditors. We reviewed and

Cross-Border Regulatory Co-operation

prepared comments on a consultation paper on proposed constitutional changes to the International Accounting Standards Committee Foundation and attended the Foundation's public hearing in Tokyo in July 2004. We also commented on International Standards on Auditing issued by the International Audit Assurance Standards Board and on International Financial Reporting Standards issued by the International Accounting Standards Board.

The Supervision of Markets Division participates in the Standing Committee on the Regulation of Secondary Markets (SC2). During the year, SC2 studied issues on transparency of corporate bond markets and error trade policies adopted by exchanges. We provided inputs to the reports on these issues and also responded to survey questionnaires on exchange demutualisation.

During the year, the Task Force on Securities Settlement Systems, which was jointly established by IOSCO and the Committee on Payment and Settlement Systems (CPSS), released a report to set out comprehensive standards for risk management of central counterparties for both securities and derivatives markets. We participated in the Task Force to formulate the standards.

The Intermediaries and Investment Products Division participates in the Standing Committee on the Regulation of Market Intermediaries (SC3). During the year, we assisted SC3 in soliciting and collating responses from local intermediaries on a survey of their outsourcing activities. We commented on the draft principles on outsourcing of financial services for market intermediaries.

In February 2005, SC3 issued the survey results and principles, which provide a flexible and practical approach that will assist firms in determining the steps to take when considering outsourcing activities.

The Enforcement Division participates in the Standing Committee on Enforcement and Exchange of Information (SC4). SC4 promotes mutual assistance among securities regulators to combat cross-border financial crimes and misconduct. SC4 is working on enforcement issues relating to gaps in international co-operation, international asset freezing, cross-border boiler rooms and cold calling, and the Internet.

To close the gaps in the global network of co-operating regulatory authorities, IOSCO has opened a confidential dialogue with jurisdictions whose ability or willingness to engage in enforcement co-operation with other regulatory authorities has been uncertain. The objective is to ascertain whether there are any obstacles in these jurisdictions to implementing the IOSCO principles on enforcement co-operation and information exchange, and to encourage and assist them to join the IOSCO MMOU. It is SC4's major task in the coming year.

The Intermediaries and Investment Products Division also participates in the Standing Committee on Investment Management (SC5). In particular, we responded to a survey by SC5 on market timing and explained our regulatory practice regarding the governance of collective investment schemes. We also shared with SC5 members the regulatory framework for retail

hedge funds, including practical matters encountered in the course of reviewing hedge fund applications and the types of hedge funds that we have authorised to date.

Partnership with Other Regulators

■ Co-operative Agreements

The SFC was very active in bilateral regulatory co-operation last year. We signed a Letter of Intent (LOI) with Indonesia's Ministry of Finance Capital Market Supervisory Agency (Bapepam) in May 2004 and a similar one with the Securities and Exchange Commission of Thailand in November 2004. In April 2005, we signed a third one with the Sri Lanka Securities and Exchange Commission.

Under the LOIs, the signatories agree to strengthen regulatory co-operation and work together with the objective of achieving the cross-border trading of mutually acceptable investment products in each other's markets.



SFC Chairman Mr Andrew Sheng (left) and Mr Tairachai Phuvanatanarubala, Secretary-General of the Securities and Exchange Commission of Thailand sign the Letter of Intent.



Mr Herwidayatmo (left), Chairman of the Bapepam, presents a souvenir to SFC Chairman Mr Andrew Sheng after the LOI signing in Jakarta, Indonesia.

In November 2004, we signed a MOU with the Philippine Securities and Exchange Commission. The MOU establishes a framework for mutual assistance and facilitates the exchange of information to enable better regulation and enforcement of the securities laws and regulations of Hong Kong and the Philippines.

■ Enforcement Related Assistance

In general, requests for enforcement related assistance made to the SFC involve getting public information such as company information, land title information, address checks and information about licensees. We also receive many requests for non-public information such as intelligence information about licensees or listed companies and for investigatory assistance. Investigatory assistance requests usually relate to bank records or information of subscribers to telephone lines.

Cross-Border Regulatory Co-operation

During the year, we arranged for overseas regulators interviews with suspects or witnesses in Hong Kong in three cases, all under legal compulsion. With our assistance, criminal charges were laid in one of the cases in a foreign country.

Last year, we received 47 requests for enforcement-related assistance: 13 were requests for investigatory assistance involving the SFC in the exercise of its statutory powers; and 34 were requests for information. On the other hand, we made seven requests to overseas regulators.

In respect of licensing-related matters, the SFC received 140 requests from overseas regulatory authorities and made 668 requests.

(FATF), an inter-governmental body which develops and promotes policies to combat money laundering. We seek to ensure that the SFC's Guidance Note on Prevention of Money Laundering and Terrorist Financing is in line with the FATF recommendations.

We also participated in the International Conference – Creating Global Partnership and Synergy in the Fight Against Money Laundering held in Hong Kong in February 2005. SFC delegates delivered a presentation to discuss the role of the securities sector in preventing money laundering, and exchanged experiences in tackling money laundering with renowned speakers and experts from overseas, the Mainland and the local business sector.

Requests for Regulatory Co-operation



	2004-2005		2003-2004		2002-2003	
	In	Out	In	Out	In	Out
Enforcement-related requests for investigatory assistance	13	4	11	4	13	14
Enforcement-related requests for information	34	3	35	2	28	6
Licensing-related requests for information	140	668*	103	383	200	451
Total	187	675	149	389	241	471

* More licensing-related requests were made to overseas regulators because there were more licence applicants from overseas and Mainland China.

Co-operation with Mainland China

Through the Memorandum of Regulatory Co-operation (MORC), the SFC, CSRC, HKEx, and the Shanghai and Shenzhen stock exchanges meet regularly to discuss regulatory issues and policies. The SFC hosted the 32nd MORC meeting in Hong Kong last June, and attended the 33rd meeting in Hainan in January 2005.

As part of the MORC meetings, divisional colleagues met their CSRC counterparts for in-depth discussions on regulatory developments in Hong Kong and the Mainland, surveillance, enforcement and other cross-border issues.

Combating Money Laundering

We continued to actively participate in the Financial Action Task Force on Money Laundering

CEPA II

The CEPA II arrangement was announced by the Central People's Government and the HKSAR Government in August 2004. Under this arrangement, SFC licensed firms which satisfy the requirements of the CSRC will be allowed to set up joint venture futures brokerage companies in the Mainland. Hong Kong firms may have up to 49% of the shareholding. CEPA II gives Hong Kong firms the advantage of early access to the developing Mainland futures market.

Promoting International Standards

On 1 March 2005, the SFC co-hosted with the HKMA a forum on Global Trends of XBRL and the Implications to Hong Kong's Regulatory Reporting Environment. XBRL stands for eXtensible Business Reporting Language and is an evolving global standard for the electronic communication of business and financial data. XBRL facilitates standardisation in the processing of accounting information, hence increasing efficiency, reducing error and permitting automatic verification in the handling of financial data.

The forum attracted 150 participants from government agencies, regulators, stock exchanges, banks, and market experts of the local financial sector. XBRL pioneers from the US, Mainland China and Japan provided instructive updates on the development of XBRL in overseas markets. The SFC will explore the use of XBRL in Hong Kong with the Government, regulatory authorities and users of financial information.



Market experts and regulators from the US, Japan, the Mainland and Hong Kong discuss development of XBRL.