

LEGISLATIVE COUNCIL BRIEF

Securities and Futures Ordinance (Cap. 571)

SECURITIES AND FUTURES (LEVERAGED FOREIGN EXCHANGE TRADING - ARBITRATION) RULES

INTRODUCTION

Pursuant to section 118(2) of the Securities and Futures Ordinance (Cap. 571) (SFO), the Securities and Futures Commission (SFC) has made the Securities and Futures (Leveraged Foreign Exchange Trading - Arbitration) Rules (the Rules) at the **Annex**.

BACKGROUND

The SFO

2. The SFO was enacted in March 2002. It consolidates and modernizes ten existing ordinances governing the securities and futures markets into a composite piece of legislation to keep the regulatory regime on a par with international standards and practices. For effective regulation, the SFO has already provided flexibility in addressing changing market practices and global conditions by empowering the Chief Executive in Council, the Financial Secretary, the Chief Justice and the SFC to prescribe detailed and technical requirements as necessary by way of subsidiary legislation, to supplement the regulatory framework laid down under the primary legislation.

3. On 22 February 2002, the House Committee of the Legislative Council has established the Subcommittee on Draft Subsidiary Legislation to be made under the SFO (the Subcommittee) to study the subsidiary legislation necessary for commencing the SFO. From March 2002 to October 2002, the Subcommittee held 12 meetings and considered a total of 37 sets of draft subsidiary legislation, including the *vires* to make them.

THE PROPOSALS

Major policy considerations

4. Part V of the SFO provides for the licensing and registration of individuals and corporations who carry on activities regulated by the SFC (regulated activities), including trading in leveraged foreign exchange contracts.

5. Section 118 of the SFO stipulates conditions to which a licence for certain regulated activities is subject. Section 118(1)(b) provides that it is a condition of a licence for carrying on trading in leveraged foreign exchange contracts that a client may have any dispute regarding or touching upon any matter concerning such trading settled by arbitration in accordance with rules made under section 118(2). The SFO basically preserves the existing arrangement in respect of settlement of dispute by arbitration for any dispute between a client and a licensed corporation in relation to leveraged foreign exchange trading as set out in the Leveraged Foreign Exchange Trading Ordinance (Cap. 451).

6. The Rules at the Annex provide for the establishment and functions of an arbitration panel, the selection and replacement of the arbitrator, the procedural rules for the commencement, conduct and termination of the proceedings, evidence and pleadings and other miscellaneous matters.

7. The Rules are largely based on the existing Leveraged Foreign Exchange Trading (Arbitration) Rules (Cap. 451 sub. leg. C). The Rules do not involve any changes in policy. The underlying policy for making provision for clients to have disputes relating to leveraged foreign exchange trading contracts settled by arbitration centres on the technical and specialist nature of leveraged foreign exchange trading and hence it would be beneficial to the parties concerned to have such matters settled by industry experts.

8. We have taken the opportunity to streamline the procedures of the arbitration proceedings and improve the drafting of existing law. The Rules are now technologically neutral, reflecting section 400 of the SFO, so that documents in relation to the arbitration proceedings are not precluded from being sent or served electronically.

THE RULES

9. Part 1 of the Rules provides for commencement, interpretation and purpose of the Rules and the establishment and constitution of an arbitration panel.

10. Part 2 of the Rules prescribes rules governing the commencement of arbitration proceedings, requirement for deposit and representation before the panel.

11. Part 3 of the Rules provides for the selection of the single arbitrator from the arbitration panel set up under Part 1, challenge to appointment and replacement of the arbitrator, and remuneration to be paid to the arbitrator.

12. Part 4 of the Rules prescribes matters relating to the conduct of the arbitration proceedings, pleadings and amendments and further statements, the arbitrator's jurisdiction and requirements in relation to the hearing of evidence.

13. Part 5 of the Rules prescribes matters relating to termination of proceedings, including settlement, termination, making of awards and costs.

14. Part 6 of the Rules prescribes miscellaneous matters in relation to the proceedings, such as notice periods, payment of interests on damages or costs, exclusion of liability, confidentiality and applicable law.

PUBLIC CONSULTATION

15. The SFC released a consultation document and an exposure draft of the Rules on 28 March 2002 for comment by the public. A total of two submissions were received. Both submissions were supportive of the draft Rules.

16. A draft of the Rules was considered by the Subcommittee at its meeting held on 6 June 2002. No major concerns were expressed by members of the Subcommittee at the meeting.

FINANCIAL AND STAFFING IMPLICATIONS

17. There are no financial or staffing implications for the Government.

COMMENCEMENT DATE

18. The Rules will come into operation on the day appointed for the commencement of the SFO, together with other subsidiary legislation necessary for the commencement. We expect this to take place shortly, after completion of the negative vetting procedure through the Legislative Council and allowing the industry a reasonable period of time for making necessary adjustments with reference to the subsidiary legislation. We aim to announce the commencement date by the end of 2002.

PUBLICITY

19. The Rules will be published in the Gazette on 29 November 2002. The SFC will issue a press release on the same day.

ENQUIRIES

20. For any enquiries on this brief, please contact Ms. Mary Ahern of the Legal Services Division of the SFC at 2283 6809 or Ms. Yvonne Mok of the Intermediaries Supervision Division of the SFC at 2842 7638.

The Securities and Futures Commission
25 November 2002