



SECURITIES AND
FUTURES COMMISSION
證券及期貨事務監察委員會

Consultation Conclusions on Electronic Submission of Financial Returns

HONG KONG
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INTRODUCTION

1. The Securities and Futures Commission issued a Consultation Paper on “Electronic Submission of Financial Returns” in November 2007 inviting comments on our proposal of amending the Securities and Futures (Financial Resources) Rules (“**FRR**”) to require all licensed corporations to submit their financial returns electronically. The consultation paper also sets out our proposals to facilitate e-submission such as by using private label digital certificates (“**private certificates**”) issued by a recognized certification authority for submission via Internet. The consultation period ended on 10 December 2007. In total, we have received eight written submissions. Six of the submissions were from licensed corporations/ groups of licensed corporations, one was from a law firm and another one was from the Hong Kong Law Society.
2. Four out of eight respondents stated that they were in support of the proposal or commented that the proposal was beneficial to the industry. Only one respondent objected to the proposal without providing any explanation even though it was already submitting financial returns electronically under the present system. Most respondents mainly raised technical questions regarding the e-submission procedures. The major comments of the respondents and the Commission’s responses are summarized below.

MAJOR COMMENTS AND THE COMMISSION’S RESPONSES

I. Renewal of private certificates and rejection of public certificates

Comments

3. One respondent questioned whether the renewal procedure is necessary for the private certificates if the signers of the returns are still the same. He also suggested the Commission to reject the public certificate issued by the Hong Kong Post as it is not widely accepted.

Commission’s responses

4. To follow the market best practices amongst certification authorities, licensed corporations should renew the private certificates at regular intervals, even if the signers have remained the same. The detailed private certificate application, renewal and cancellation procedures would be set out in a set of IT directions/ instructions to be published in due course.

Since some licensed corporations are currently using the public certificates issued by the Hong Kong Post when submitting their financial returns via FinNet, we intend to retain this option for the existing users.

Comments

5. A respondent was concerned whether the Commission’s hotline would be able to provide adequate support to the industry regarding forgotten password, loss of

token and private certificate application, cancellation and renewal etc. Another respondent also enquired about the detailed system and hardware requirements necessary for e-submission.

Commission's responses

6. For some years, the Commission's IT hotline has been assisting licensed corporations with their e-submission of financial returns via FinNet using the public certificate issued by the Hong Kong Post. The hotline would continue to provide necessary support and assistance to the licensed corporations after the introduction of the proposed requirement.
7. For e-submission of returns, licensed corporations only need to ensure that their computers meet some basic technical requirements. More details regarding the system and hardware requirements would be provided in the IT directions/instructions to be issued by the Commission.

Comments

8. A respondent requested that at least two private certificates should be issued per licensed corporation and a list showing the private certificate holders be made available via the Internet to the licensed corporation concerned.

Commission's responses

9. The Commission has always intended to issue two private certificates to each licensed corporation. In addition, licensed corporations may apply to the Commission for more certificates with reasons. Under the existing Electronic Financial Resources Rules Returns System ("e-FRRR system"), licensed corporations are already allowed to maintain their own list of e-certificate holders. This function would still be available after the implementation of the additional options for e-submission.

II. Failure to e-submit financial returns

Comments

10. Two respondents proposed that paper form submission should be allowed when e-submission is not possible under specific exceptional situations.

Commission's responses

11. Licensed corporations should report any such problems to the Commission's hotline immediately and based on the circumstances of each case, the Commission would adopt a pragmatic and flexible approach in determining the actions to be taken.

III. Other IT or security related issues

Comments

12. Three respondents requested an acknowledgement of receipt of the financial returns be issued to the licensed corporations and two of them also suggested the submission be time-stamped.
13. A respondent proposed that the e-FRRR system should be able to store historical submissions, print past and present submissions, maintain standing data and save half completed returns.

Commission's responses

14. Under the proposed e-FRRR system, an acknowledgement receipt showing the date and time of receiving the return will be automatically generated.
15. For security reasons, the proposed e-FRRR system has been designed not to allow online access facility for past submissions. However, in case of need, they could request the Commission on an ad-hoc basis to retrieve any of their returns. Also, as the financial return is in the form of an offline Microsoft Excel spreadsheet, licensed corporations could save the returns offline at any time.

Comments

16. Two respondents suggested that a hierarchy of access controls be structured into the e-FRRR system. One of them proposed that there should be one level of access for those inputting data and another level of access for the nominated persons to sign the returns.
17. A respondent asked what security measures would be put in place to ensure that submission via the Internet is performed by the nominated person.
18. Another respondent enquired about the legal or contractual obligations if the security measures are being compromised.

Commission's responses

19. The existing e-FRRR system already provides for two levels of access control, i.e. administration of system and submission of returns and this feature will remain in the proposed system. For internal control purposes, licensed corporations are expected to segregate duties over offline return preparation and online return submission.
20. The Commission will only grant the e-FRRR system login password and the PIN-protected private certificates to those persons nominated by the licensed corporation. Thus they would be the only persons who could sign and submit the returns on behalf of the licensed corporation.

21. Internet filing is considered safe by industry standard with all the security measures intended to be put in place by the Commission. However, if individual firms remain concerned, they still have the option of submitting their returns via the private network, i.e. the FinNet.

TIMING

22. The proposed amendments to the FRR are enclosed in Appendix 1. The amendments will be introduced into the Legislative Council for negative vetting as soon as practicable. Assuming that the legislative process runs smoothly, the Commission would start to provide training to licensed corporations and allow for testing of the new system in the third quarter of 2008 and roll out the new system in the fourth quarter of 2008.

FINAL NOTE

23. The Commission would like to thank all industry participants and other interested parties who have made constructive suggestions and comments in response to the Consultation Paper.

**Proposed amendments to ss. 56 and 58 of the
Securities and Futures (Financial Resources) Rules**

S.56 Licensed corporations to submit returns to Commission

(1) Subject to subsection (4), a licensed corporation licensed for one or more of the following-

- (a) Type 1 regulated activity;
- (b) Type 2 regulated activity;
- (c) Type 3 regulated activity;
- (d) Type 4 regulated activity, and it is not subject to the specified licensing condition;
- (e) Type 5 regulated activity, and it is not subject to the specified licensing condition;
- (f) Type 6 regulated activity, and it is not subject to the specified licensing condition;
- (g) Type 7 regulated activity;
- (h) Type 8 regulated activity;
- (i) Type 9 regulated activity, and it is not subject to the specified licensing condition,

shall, in respect of each month at the end of which it remains licensed, submit to the Commission, in the manner specified in subsections (5) and ~~(6)(d), (e) or (f) (as the case may be)~~, no later than 3 weeks after the end of the month concerned, a return, which is in the form specified by the Commission under section 402 of the Ordinance and signed in the manner specified in subsection (6), which and includes-

- (j) its liquid capital computation, as at the end of the month;
- (k) its required liquid capital computation, as at the end of the month;
- (l) a summary of bank loans, advances, credit facilities and other financial accommodation available to it, as at the end of the month;
- (m) an analysis of its margin clients, as at the end of the month;
- (n) an analysis of collateral received from its margin clients, as at the end of the month;
- (o) an analysis of its rolling balance cash clients, as at the end of the month;
- (p) an analysis of its profit and loss account;
- (q) an analysis of its client assets, as at the end of the month; and
- (r) where it is licensed for Type 3 regulated activity, an analysis of its foreign currency positions, as at the end of the month.

(2) Subject to subsection (4), a licensed corporation to which subsection (1) applies shall, in respect of each period of 3 months at the end of which it remains licensed, being such period in a year ending at the end of the month of March, June, September or December, respectively, submit to the Commission, in the manner specified in subsections (5) and ~~(6)(d), (e) or (f) (as the case may be)~~, no later than 3 weeks after the end of the period concerned, a return, which is in the form specified by the Commission under section 402 of the Ordinance and signed in the manner specified in subsection (6), which and includes-

- (a) an analysis of its clientele, as at the end of the 3 month period;
- (b) an analysis of its proprietary derivative positions, as at the end of the 3 month period;
- (c) where it is licensed for Type 3 regulated activity, an analysis of its recognized counterparties, as at the end of the 3 month period; and
- (d) where it is licensed for Type 9 regulated activity, an analysis of the assets under its management, as at the end of the 3 month period.

(3) Subject to subsection (4), a licensed corporation which is licensed solely for one or more of the following-

- (a) Type 4 regulated activity;
- (b) Type 5 regulated activity;
- (c) Type 6 regulated activity;
- (d) Type 9 regulated activity,

and subject to the specified licensing condition, shall, in respect of each period of 6 months at the end of which it remains licensed, being such period in a year ending at the end of the month of June or December, respectively, submit to the Commission, in the manner specified in subsections (5) and ~~(6)(d), (e) or (f) (as the case may be)~~, no later than 3 weeks after the end of the period concerned, a return, which is in the form specified by the Commission under section 402 of the Ordinance and signed in the manner specified in subsection (6), which and includes-

- (e) its liquid capital computation, as at the end of the 6 month period;
- (f) its required liquid capital computation, as at the end of the 6 month period;
- (g) an analysis of its profit and loss account;
- (h) an analysis of its clientele, as at the end of the 6 month period; and
- (i) where it is licensed for Type 9 regulated activity, an analysis of the assets under its management, as at the end of the 6 month period.

(4) A licensed corporation may elect to submit the return required under-

- (a) subsection (1), in respect of periods of not less than 28 days but not more than 35 days, each ending not more than 7 days before or after the end of a month;
- (b) subsection (2), in respect of periods of 3 months each ending not more than 7 days before or after the end of March, June, September or December in a year;
- (c) subsection (3), in respect of periods of 6 months each ending not more than 7 days before or after the end of June or December in a year,

determined by it on a basis according to which the ending date of each period so determined is predictable, and where it so elects and submits the return concerned, it shall be deemed to have submitted the return concerned in respect of the period required under subsection (1), (2) or (3) (as the case may be).

(5) For the purposes of this section, a licensed corporation shall submit a return referred to in this section to the Commission electronically by means of an online communication system approved by the Commission under section 58(7) for the purposes of this subsection.

~~(5) A return referred to in this section shall be signed in the manner prescribed in subsection (6) by a responsible officer or another officer of the licensed corporation approved by the Commission under section 58(5)(e) for the purposes of this section.~~

(6) For the purposes of this section -

- (a) a return referred to in this section shall be signed on behalf of the licensed corporation concerned by a responsible officer of the licensed corporation or another officer of the licensed corporation approved by the Commission under section 58(5)(e) for the purposes of this section, by way of attachment to the return of the digital signature or electronic signature of the responsible officer or other officer; and
- (b) the signature referred to in paragraph (a) shall –
 - (i) in the case of a digital signature, be supported by a recognized certificate, generated within the validity of that certificate and used in accordance with the terms of that certificate; or
 - (ii) in the case of an electronic signature, be authenticated in accordance with such directions and instructions for the use of the online communication system concerned as are published by the Commission under section 58(8).

~~(6) A licensed corporation may elect to submit a return referred to in subsection (3) to the Commission-~~

- ~~(a) electronically, by means of a secure online communication network approved by the Commission under section 58(7) for the purposes of this paragraph;~~
- ~~(b) in electronic form on a floppy disk, delivered by hand or by post to the Commission; or~~
- ~~(c) in paper form, delivered by hand or by post to the Commission,~~

and-

- ~~(d) where it submits the return in accordance with paragraph (a)-~~
 - ~~(i) the return shall be signed by way of attachment to the return of the digital signature of the licensed corporation, and the digital signature shall be-~~
 - ~~(A) supported by a recognized certificate;~~
 - ~~(B) generated within the validity of that certificate; and~~
 - ~~(C) used in accordance with the terms of that certificate~~
 - ~~(ii) if the return is not signed as provided for in subparagraph (i), it shall also submit a signed copy of the return in paper form, delivered by hand or by post to the Commission;~~
- ~~(e) where it submits the return in accordance with paragraph (b), the floppy disk shall be accompanied by a signed copy of the return in paper form; or~~
- ~~(f) where it submits the return in accordance with paragraph (c), the signed original of the return shall be submitted.~~

(6A) For the purposes of subsection ~~(6)(b)(i)(6)(d)(i)(A)~~, a digital signature is taken to be supported by a recognized certificate if it is taken to be supported by that certificate under section 2(2) of the Electronic Transactions Ordinance (Cap 553).

(7) In this section-

"digital signature" (數碼簽署) has the meaning assigned to it by section 2(1) of the Electronic Transactions Ordinance (Cap 553);

"electronic signature" (電子簽署) has the meaning assigned to it by section 2(1) of the Electronic Transactions Ordinance (Cap 553);

"recognized certificate" (認可證書) has the meaning assigned to it by section 2(1) of the Electronic Transactions Ordinance (Cap 553);

"rolling balance cash client" (滾存結餘現金客戶) means a client of a licensed corporation in respect of whom the amounts receivable from, and amounts payable to, him by the licensed corporation arising from the purchase and sale of securities on a cash-against-delivery basis by the licensed corporation for him may be set-off by the licensed corporation under section 21(3);

"within the validity of that certificate" (在該證書的有效期內) has the meaning assigned to it by section 6(2) of the Electronic Transactions Ordinance (Cap 553).

58 Approvals

(1) to (4) and (6) No change.

(5) The Commission may, on application in writing by a licensed corporation and payment of the fee prescribed in the Securities and Futures (Fees) Rules (Cap 571 sub. leg. AF), approve-

- (a) as approved redeemable shares, any redeemable shares issued by the licensed corporation;
- (b) as an approved subordinated loan, any subordinated loan obtained by the licensed corporation;

- (c) as an approved standby subordinated loan facility, any standby subordinated loan facility obtained by the licensed corporation;
- (d) for the purposes of section 3(3), the adoption by the licensed corporation of an accounting principle other than one of those referred to in section 3(1)(a);
- (e) for the purposes of section ~~56(5)~~56(6), an officer of the licensed corporation to sign a return;
- (f) for the purposes of section 41(1)(a)(v), a foreign currency; and
- (g) the withdrawal of an election made by the licensed corporation under any provision of these Rules.

(7) The Commission may, for the purposes of section 56(~~65~~)(a), approve an ~~secure~~ online communication ~~network~~system.

(8) Where the Commission approves an online communication ~~network~~system under subsection (7), it shall as soon as reasonably practicable publish ~~details of the network~~ directions and instructions for the use of that system in such manner as it considers appropriate.