

Comments on the Consultation Document on the Proposed Revisions to the Code of Conduct for Persons Registered with the Securities and Futures Commission

1 General

The financial institutions listed below (the “Group”) welcome the opportunity to provide comments on the Consultation Document on the Proposed Revisions to the Code of Conduct for Persons Registered with the Securities and Futures Commission (the “Revised Code”). We note that the purpose of the Revised Code is to extend its application to all intermediaries and their representatives and to rationalise the Revised Code with the Securities and Futures Ordinance (“SFO”) and the rules made under it. Consequently, most of the amendments are not material and the Group has limited comments on the Revised Code.

The Group’s main concern is in relation to the categorisation of professional investors under Paragraph 15.2B, which appears to lead to different tests applying under the Professional Investor Rules (the “PI Rules”) and the Code.

2 Paragraph 3.9 (Order Recording)

In the SFC Enforcement Reporter (December 2002), the SFC noted that it had disciplined a licensed firm for, among other things, not having a procedure to review regularly the tape recordings of client-broker phone conversations. The SFC then stated: *“Brokerages should review the recordings regularly on a sample basis to keep an eye on their staff.”*

We ask the SFC to confirm whether or not this is a requirement of the Code, and if it is, to set out clearly what the SFC’s expectations are, i.e. whether this should be done monthly, and as to how many samples should be reviewed.

3 Paragraph 5.4 (Client Identity)

We believe that the reference to “investment fund” in sub-paragraph (d) should refer to “collective investment scheme”, which is the definition used in the SFO.

Sub-paragraph (e) has been amended to refer to “a recognized stock market or a recognized futures market” rather than one of the Hong Kong exchanges. Please confirm that the intention remains that the client identity rule only applies to transactions relating to securities and futures contracts listed or traded in Hong Kong.

These comments are also relevant to the Client Identity Guidance Note in Schedule 2.

4 Paragraph 9.3 (Non-public, material information)

This paragraph has always had some language missing, which was not picked up when the existing code was revised in April 2001. We believe the words “or on the basis of” should be inserted before “other non-public information” in line 6 of this paragraph.

5 Paragraph 15 (Professional investors)

The Group would also ask the SFC to clarify what documentation is required to be kept to evidence a decision to treat someone as a “professional investor” within the categories set out in Schedule 1 to the SFO. The Keeping of Records Rules require firms to keep “records

showing particulars sufficient to establish that the client is a professional investor” (para. 4(a) of the Schedule). Where the client is a “professional investor” within the Professional Investor Rules (“PI Rules”), since only particular documentation can be relied upon, it is obvious that it is those documents that must be kept. For other professional investors, it should be sufficient for a firm to keep records showing that it has conducted checks to ascertain that a client falls within one of the categories (e.g. a record that it has checked that a client is, say, a bank regulated by the HKMA).

6 Paragraph 15.2B

In paragraph 15.2B a person falling within paragraph (j) of the definition of “professional investor” in the SFO is only to be treated as a professional investor by a licensed or registered person if the licensed or registered person is reasonably satisfied that the person is knowledgeable and has sufficient expertise in the relevant products and markets. In making that assessment the licensed or registered person should have regard to the tests in paragraph 15.3 of the Revised Code. In addition, paragraph 15.4 of the Code still requires that these clients consent in writing to being treated as professional investors.

This effectively means there are different tests for treating persons in this category as professional investors under the Code and the PI Rules, which will make it difficult for firms to administer the definitions in practice. Having different tests will also potentially lead to confusion for clients, as they may be treated as professional investors under the PI Rules but not as professional investors under the Code.

When discussing the PI Rules we understood that the SFC accepted the tests in paragraph 15.3 of the existing code were difficult in practice to comply with and that was one reason why such tests were not included in the PI Rules. In the SFC’s Consultation Conclusions on the PI Rules, the SFC stated that it had decided to align the Code definition with that under the SFO. If the SFC’s policy on this has changed, the reasons for this should be clearly explained.

7 Schedule 3 (Additional Requirements for Dealing in Securities Listed or Traded on the Stock Exchange)

Paragraph 13 of Schedule 3 sets out the contents requirements of a stock borrowing and lending agreement entered into by an Exchange Participant. Sub-paragraph 13(p) requires there to be included a warranty requiring the borrower to register the executed agreement with the Collector. In the case of a Hong Kong borrower this must be done no later than 2 weeks after the execution of the agreement and in the case of an overseas borrower this must be done no later than 1 month after the execution of the agreement. This is inconsistent with Section 19(12A) of the Stamp Duty Ordinance, which requires a copy of the executed agreement to be provided by the borrower to the Collector no later than 30 days after the first stock borrowing is effected under that agreement.

8 Schedule 4 (Additional Requirements for Dealing in Futures Contracts and/or Options Contracts on the Futures Exchange)

Paragraph 20 of Schedule 4 requires a Futures Exchange Participant to comply with certain specified circulars. It would be useful if copies of those circulars were made available on the HKEx website, as the Futures Exchange will not provide copies to persons who are not Futures Exchange Participants. This is not helpful to legal advisers or persons interested in

becoming Futures Exchange Participants. Having copies on the website would also provide an easily accessible reference source for participants.

If you would like to discuss any of the above issues with the Group collectively, please contact Stephen Fletcher at Linklaters, 10th Floor, Alexandra House, Chater Road, Central, Hong Kong (Direct Line: 2901 5350).

List of Submitting Group Members

Credit Suisse First Boston (Hong Kong) Limited

Goldman Sachs (Asia) L.L.C.

J.P. Morgan Securities (Asia Pacific) Limited

Merrill Lynch (Asia Pacific) Limited

Morgan Stanley Dean Witter Asia Limited

Salomon Smith Barney Hong Kong Limited

UBS Warburg Asia Limited

