

20th December 2002

SFC (Code of Conduct)
12/F, Edinburgh Tower
The Landmark
15 Queen's Road Central
Hong Kong

Dear Sir/Madam,

Re: Comments to Proposed Revisions to the Code of Conduct, November 2002

We are submitting our written comments on the Revised Code of Conduct.

Securities borrowing and lending (Schedule 3 to the Code of Conduct)

- 1) Pursuant to Para. 12(d), Schedule 3 on securities borrowing and lending, we like to seek clarification as to why the condition is only applicable to Exchange Participants. In so doing, it put Exchange Participants at a disadvantage. If an Exchange Participant borrows the securities from third parties, the collateral received will be passed on to the lenders. But in the case when securities are borrowed from the Participant's stock account, the collateral received must be placed in a separate bank account. The collateral under a SBL agreement, we understand, is not considered as clients' money and the collateral could be used at the discretion of the registered person.

If the collateral under a SBL agreement is considered as clients' money, it will be covered by Securities and Futures (Client Money) Rules. And therefore the requirement to place collateral in a separate bank account will become redundant. We suggest this requirement should be removed from the Code of Conduct

- 2) Pursuant to Para. 13(f), Schedule 3 on securities borrowing and lending, we again will like to seek clarification as to why the condition is only applicable to Exchange Participants. The amount of collateral required by the borrower is a credit decision best decided by the industry and is subjected to the terms and conditions of the SBL agreement negotiated by both the lender and borrower.

If it is mandated that the value of the collateral should at all times be not less than 100% of the current market value of the borrowed securities, in the case where the Exchange Participants borrow the securities from non-financial institutions including individual clients, and when the borrowed securities

drop in value, the value of the collateral provided will be greater than the current value of the securities borrowed. For prudent risk management, the Exchange Participants will need a margin to protect itself from fluctuation in value of the securities borrowed. The margin needed will depend on the credit standing of the lenders.

There are also several other requirements in the Code of Conduct that are only applicable to Exchange Participants. To include some of the “repealed rules” of the SEHK into the Codes put the Participants at a disadvantage and in some cases, direct business activities away from the Participants and distort workflow. We recommend that the SFC subject all registered and licensed persons to the same requirements, where possible and accord the Exchange Participants the flexibility that they so badly need in today very competitive business environment.

Prompt confirmation (Para. 8.2(a))

- 3) Paragraph 8.2(a) of the Code of Conduct states that “a licensed or registered person... should endeavour to confirm promptly with the client the essential features of the transactions”.

We will like seek clarification whether the “passive” order status service recommended in Para. 79(h) of the Consultation Paper on the Regulation of On-line Trading Of Securities and Futures published by the SFC in December 2000 complies with the above requirement.

Employee Dealings (Para. 12.2)

- 4) We will like to seek clarification whether a licensed or registered person is required to seek written consent and arrange for duplicate trade confirmation and statement of accounts to be provided to its senior management for monitoring in cases below:
 - (i) if the employer is a leveraged foreign exchange trader and it permits its employees to trade through another dealer for their own accounts in leveraged foreign exchange, securities or futures contracts (listed or traded on a recognized stock market or a recognized futures market);
 - (ii) if the employer provides trading services in securities or futures contracts, and it permits its employees to trade through another dealer for their own accounts in leveraged foreign exchange contracts.
 - (iii) If an employee of a licensed or registered person is permitted to trade, through another overseas dealer or licensed or registered person, for their own accounts in overseas stocks and futures contracts.

If the answers for the above cases are negative, by the same principle is it necessary for the licensed or registered persons dealing in securities to obtain

duplicate trade confirmation of their employees dealing in futures contracts with other houses?

Risk Disclosure Statement (Schedule 1 to the Code of Conduct)

- 5) Schedule 1 to the revised Code of Conduct requires a member of staff to sign and date a declaration confirming that the licensed or registered person has provided the risk disclosure statement in a language of the client's choice and invited the client to read the risk disclosure statement, ask questions and take independent advice if the client wishes.

The FAQ on Code of Conduct issued in July 2001 states that "where there is no face-to-face approach, the registered person should ensure that the covering correspondence should specifically draw the client's attention to the appropriate risk disclosure statements and client acknowledgement should be sought. It will not be necessary for the "declaration by staff" section to be signed." For the avoidance of doubt, we suggest that the SFC incorporates the exemption to Schedule 1 of the Code of Conduct.

We will like to thank the SFC for considering our comments.

Yours faithfully,

Phillip Securities HK Ltd