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Submission in response to the Securities and Futures Commission's (SFC) consultation Paper on Proposed Amendments to the Securities and Futures (Financial Resources) Rules issued in May 2011

May 2011

For enquiries on this submission, please contact _____ at _____ . **CompliancePlus Consulting Limited** understands and agrees that our name and/or submission may be published by the SFC.

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Introduction

We prepare this submission in response to the Securities and Futures Commission's (SFC) consultation Paper on Proposed Amendments to the Securities and Futures (Financial Resources) Rules issued in May 2011.

The Securities and Futures (Financial Resources) Rules (Cap. 571N, "FRR") was made pursuant to S.145 of the Securities and Futures Ordinance ("SFO"). The FRR prescribes the treatments for assets and liabilities related to transaction in futures or options contracts on a list of exchanges specified in Schedule 3 of the FRR ("specified exchanges"). For firms trading in contracts on exchanges not specified in Schedule 3, FRR modification is granted on an individual firm basis to alleviate the firm's compliance burden.

In summary the SFC proposes three amendments to the FRR. The first one is to update the names of a number of exchanges which are already on the lists, since the names of these exchanges have changed. The second amendment is to add four exchanges to the lists, namely the Hong Kong Mercantile Exchange Limited ("HKMEx"), the Taiwan Futures Exchange Corporation, the Thailand Futures Exchange Public Company Limited; and the Tokyo Commodity Exchange, Inc. The third amendment is to include participants of HKMEx in the definition of "exchange participant" in S.2(1) of the FRR, so that firms introducing clients to a HKMEx participant can apply for approval as an approved introducing agent under S.58(4) of the FRR.

We agree with these proposals.

Updating the names

We agree that the names of the exchanges have to be updated.

On the other hand, we wonder if it would be desirable for the SFC to update the names as soon as the names have been changed, instead of leaving Schedule 3 not updated for some years. We encounter the same problem in relation to the amendments to Parts 2 and 3 of Schedule 1 to the SFO. In that submission we pointed out that the SFO is given the power to amend the Schedule by notice published in the Gazette, and suggested that the SFC should consider invoking this power to update the Schedule once the names of the exchanges have changed. In relation to the FRR, the FRR is a subsidiary legislation defined in S.3 of the Interpretation and General Clauses Ordinance ("IGCO"). The SFC is given the power to make rules pursuant to S.145 and S.397 of the SFO (subject to approval of the Legislative Council: S.34 IGCO). It seems that the SFC should have the power to similarly amend the FRR, as clarified by S.37A of the IGCO:

"The amendment of subsidiary legislation by an Ordinance does not prevent, and has never prevented, a person on whom power is conferred by an Ordinance (as defined in section 3) to make that subsidiary legislation (and whether or not the person made the subsidiary legislation) from amending that subsidiary legislation."

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Again, we suggest that the SFC should consider invoking this power to update the lists once the name of an exchange has changed.

Adding four exchanges to the lists

The second amendment is to add four new exchanges to the lists. The argument is that many listed corporations are trading futures or options contracts on these exchanges, and instead of granting FRR modifications on an individual firm basis the SFC believes that adding them to the list would be more convenient. We agree with this amendment.

On the other hand, we wish to highlight that the treatments of the aforementioned four exchanges are different. With respect to the Hong Kong Mercantile Exchange Limited and the Tokyo Commodity Exchange, Inc., these two exchanges are added to Part 1 of Schedule 3, while with regard to the Taiwan Futures Exchange Corporation and the Thailand Futures Exchange Public Company Limited, these exchanges are added to Part 2 of Schedule 3.

It seems that the SFC has not brought out this issue in the consultation paper. The classification makes a difference in relation to the haircut percentages of shares listed on these exchanges. For shares listed on exchanges specified in Part 1, the haircut percentage is 20%, while for shares listed on exchanges specified in Part 2, the haircut percentage is 30%: see Table 3 of Schedule 2. While we recognize that licensed corporations mostly trade commodity in these exchanges, the SFC may still wish to justify the difference in treatments, and explain whether these treatments differ materially from the FRR modifications that it currently grants.

Including HKMEx participant as “exchange participants”

The purpose of this amendment is to enable listed corporations which introduce orders or clients to HKMEx participant to apply to be an Approved Introducing Agent under S.58(4).

We understand that promoting commodity exchanges in Hong Kong is regarded as a crucial step in maintaining our status as an international financial centre. The amendment can encourage the development of HKMEx and we agree with the SFC's proposal.

Conclusion

We agree with these proposals.

END