

The Hong Kong Chartered Governance Institute

Submission

The Securities and Futures Commission (SFC)

Consultation paper on Proposed Code and Guidelines for Implementing an Uncertificated Securities Market in Hong Kong

The Hong Kong Chartered Governance Institute 香港公司治理公會

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The Securities and Futures Commission
54th Floor, One Island East
18 Westlands Road
Quarry Bay
Hong Kong

Attn: Supervision of Markets Division

Dear Sirs/Madam,

Consultation paper on proposed code and guidelines for implementing an uncertificated securities market in Hong Kong

[Unless the context requires otherwise, the terms and expressions used in this submission shall have the meanings set out under the Consultation Paper.]

About HKCGI

The Hong Kong Chartered Governance Institute (HKCGI), formerly known as The Hong Kong Institute of Chartered Secretaries, is the only qualifying institution in Hong Kong and the Mainland of China for the internationally recognised Chartered Secretary and Chartered Governance Professional qualifications.

With over 70 years of history and as the Hong Kong/China Division of The Chartered Governance Institute (CGI), the Institute's reach and professional recognition extend to all of CGI's nine divisions, with about 40,000 members and students worldwide. The Institute is one of the fastest growing divisions of CGI, with a current membership of over 7,000, 300 graduates and 2,600 students with significant representations within listed companies and other cross-industry governance functions.

Believing that better governance leads to a better future, HKCGI's mission is to promote good governance in an increasingly complex world and to advance leadership in the effective governance and efficient Administration of commerce, industry and public affairs. As recognised thought leaders in our field, the Institute educates and advocates for the highest standards in governance and promotes an expansive approach which takes account of the interests of all stakeholders.

Overview

We must express our continued concern, which we have expressed in all of our submissions relating to the USM regime on the unsolved problem of costs related to implementing the USM regime. The user-pay principle ought to direct the allocation of these expenses, averting excessive financial strain on listed companies and their registrars. The latter will seek recovery from listed companies if shareholders fail to make appropriate contributions, barring government-instituted subsidies to advance Hong Kong's status as a global financial hub through the regime's implementation.

Also, on implementing the USM regime, stakeholders' opinions, including the industry's FSR, should be considered, particularly to minimise administrative hassles and associated expenses that don't pose a serious risk management risk. It is appropriate that approved securities registrars ("ASRs") be members of the FSR as set out under the consultation to uphold professional standards and discipline in addition to SFC's ultimate regulatory oversight. For example, there must be a genuine and commercial discussion with the FSR on the proposed fee levels under Schedule 1.

From a governance perspective, we have no issue with the underlying applied governance thoughts under the "General Principles (GPs)" on important aspects, including outsourcing, computer system standards, and information disclosure. Furthermore, in keeping with the electronic character of public offers and highlighting the critical function of ASRs, the proposed revisions to the Guidelines for Electronic Public Offerings reflect a timely response to changing market practices. The changes to the Stamp Duty Ordinance also reflect an appropriate adjustment to the updated function of ASRs in stamp duty arrangements while acknowledging the move towards electronic stamping. This strategy shows a dedication to maintaining the efficiency and integrity of Hong Kong's securities industry.

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| <p>Q1. Do you have any comments or concerns about the proposed new GP4 on outsourcing? If so, please elaborate.</p> |
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Incorporating the proposed new General Principle 4 (GP4) on outsourcing to the Code of Conduct for Approved Securities Registrars is part of applied governance. A sensible attitude to continuously recognising and managing potential risks is demonstrated by requiring ASRs to complete a risk assessment before outsourcing tasks, with regular evaluations. This practice contributes to the security and dependability of the securities market infrastructure. The requirements listed, including the necessity for written contracts and doing due diligence on service providers, align with established procedures and sufficient technical assistance to create a strong outsourcing structure that guarantees accountability and control. We defer to the industry views on the obligations imposed under the Code from this GP, which is related to our overall cost concern as part of applied governance.

Q2. Do you have any comments or concerns about the proposed new GP5 on ASRs' computer systems and facilities? If so, please elaborate.

The proposed new General Principle 5 (GP5) on ASRs' computer systems and facilities reflects the regulatory regime for ASRs' systems-focused approach. The fact that the criteria for these systems have been expanded is especially significant since it highlights the important role that ASRs' infrastructure and systems will play. The specific measures listed are necessary to preserve the integrity and security of financial systems. However, we defer to the industry views on the obligations imposed under the Code from this GP, which is related to our overall cost concern as part of applied governance.

Q3. Do you have any comments or concerns about the proposed new GP6 on information to be disclosed by ASRs to their issuer-clients and registered holders? If so, please elaborate.

The proposed new General Principle 6 (GP6) addresses information disclosure by ASRs to registered holders and issuer-clients. ASR-introduced service facilities, including the ePO channel and UNSRT system, represent a major change towards an electronic and more efficient securities market. The proposed GP6's transparency goals are praiseworthy. We defer to the industry views on the obligations imposed under the Code from this GP, which is related to our overall cost concern as part of applied governance.

Q4. Do you have any comments or concerns about the proposed amendments relating to GP1 on the honesty and fairness standards applicable to ASRs? If so, please elaborate.

The proposed changes to ASR Code section 2, which explicitly address GP1 on honesty and fairness, are acceptable and enhance the regulatory framework that ASRs are subject to. ASRs are explicitly required to charge fair and reasonable rates, especially to registered holders. There is a concern that this would pressure registrars to seek recovery from listed issuers to avoid arguments as to whether the items of cost recoupment are fair and reasonable. It will be important to consider the position of all USM regime participants to improve the standards and create a balanced regulatory framework that maintains integrity without placing undue financial constraints on market players. It is not correct that issuers should bear a substantial part of the costs from the applied governance perspective. There should be a cost analysis of what issuers are paying and what the USM regime would bring about.

Q5. Do you have any comments or concerns about the proposed amendments relating to GP2 on the diligence standards applicable to ASRs? If so, please elaborate.

The proposed changes to section 3 of the ASR Code, which notably addresses GP2 on diligence criteria, are well-founded and in line with the changing securities market environment. The importance of these facilities in maintaining and controlling holdings of prescribed securities

makes section 3.2's explanation of what ASRs can expect when offering service facilities for usage imperative. Engaging in active participation in talks will help guarantee that the recommendations achieve a fair balance between the operational realities encountered by market participants and regulatory obligations. We defer to the industry views on the obligations imposed under the Code from this GP, which is related to our overall cost concern as part of applied governance.

Q6. Do you have any comments or concerns about the proposed amendments relating to GP3 on ASRs' capabilities? If so, please elaborate.

A thorough attempt has been made to offer clarification and direction on the Securities and Futures Commission's (SFC) expectations, as seen by the proposed changes to section 4 of the ASR Code, which particularly addresses GP3 on ASRs' capabilities. ASRs must be prepared to fulfil the requirements of the USM environment; therefore, these revisions are essential. It is, however, important to ensure the requirements are reasonable and do not place a significant financial burden on listed issuers.

Q7. Do you have any comments or concerns about the proposed amendments relating to GP7 on conflicts of interest? If so, please elaborate.

The proposed revisions to ASR Code section 8, which pertain to GP7 on conflicts of interest, align with the expected demands of ASR obligations in the context of the USM. Engaging in constructive dialogue with the industry will aid in improving these principles, aiming to achieve a harmonious balance between resolving conflicts of interest and guaranteeing that the regulatory structure is workable and economical for market players. We defer to the industry views on the obligations imposed under the Code from this GP, which is related to our overall cost concern as part of applied governance.

Q8. Do you have any comments or concerns about the proposed amendments relating to GP9 on ASRs' compliance obligations? If so, please elaborate.

The proposed changes to Section 10, which deals with GP9 on ASRs' compliance requirements, represent a strategy to improve regulatory oversight and define expectations in the USM context. We defer to the industry views on the obligations imposed under the Code from this GP, which is related to our overall cost concern as part of applied governance.

Q9. Do you have any comments or concerns about the proposed amendments relating to GP10 on the responsibilities of ASRs' senior management? If so, please elaborate.

The suggested changes to section 11, which delineates the duties of senior management of ASRs, are a step in the right direction towards improving the regulatory framework's transparency and

accountability. It will be essential for participants to participate in discussions actively to improve these rules and make sure that senior management obligations are reasonable and balanced for market participants.

Q10. Do you have any comments or concerns about the Schedules proposed to be included? If so, please elaborate.

We are concerned about the costs that listed issuers and ASRs bear. We defer to the industry views on the obligations imposed under the Code, which is related to our overall cost concern as part of applied governance.

Q11. Do you have any comments or concerns about the proposed amendments to reflect changes in market practices? If so, please elaborate.

The proposed amendments to the ePO Guidelines to reflect changes in market practices appear reasonable and necessary given the evolution of electronic public offerings (ePOs) and the increasing reliance on electronic channels for IPO subscriptions. The amendments aim to align the guidelines with current market practices, including the shift towards electronic IPO processes and the use of mobile apps.

Q12. Do you have any comments or concerns about the proposed amendments to reflect ASRs' ability to offer ePO services without having to work with a Type 1 licensed intermediary? If so, please elaborate.

The proposed amendments to reflect ASRs' ability to offer ePO services without having to work with a Type 1 licensed intermediary seem reasonable and in line with the changes in the regulatory framework for ASRs. The amendments acknowledge the shift in responsibilities from Type 1 intermediaries to ASRs in providing ePO services. Furthermore, comments from the industry on these modifications can offer insightful information about possible problems or points that could require more explanation.

Q13. Do you have any comments or concerns about the proposal that the ePO Guidelines deal essentially with ePOs of prescribed securities, and have only limited application in respect of ePOs of nonprescribed securities? If so, please elaborate.

The proposal to amend the ePO Guidelines to cover ePOs of prescribed securities primarily is understandable, given the revised scope of regulation for ASRs. Focusing on prescribed securities aligns with the specific regulatory framework applicable to ASRs and their role in issuing and managing them. The expectations for issuers and intermediaries participating in ePOs of non-prescribed securities are made clear in the introduction of section 4.3.

Q14. Do you have any comments or concerns about the proposed further amendments regarding the arrangements for stamping and collecting stamp duty in the USM environment? If so, please elaborate.

The proposed changes to leverage existing e-stamping arrangements under Part IIA of the SDO, instead of introducing a separate process for ASRs, appear to be a pragmatic and efficient approach. Aligning ASRs with the existing electronic stamping framework simplifies the stamping and stamp duty collection process while maintaining consistency with established practices.

These modifications appear to be a reasonable adaptation for stamping and collecting stamp duty in the USM context since they seek to be consistent with current e-stamping methods and use known frameworks. This strategy should be deemed viable and consistent with modern electronic transaction practices by financial industry stakeholders.

If there are any questions, please feel free to reach out to Ellie Pang FCG HKFCG(PE), Chief Executive, HKCGI or Mohan Datwani FCG HKFCG(PE), Deputy Chief Executive, HKCGI at 2881 6177 or research@hkcgi.org.hk.

Yours sincerely,
For and on behalf of
The Hong Kong Chartered Governance Institute



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