

For information  
on 16 April 2003

**The Legislative Council  
Panel on Financial Affairs**

**Report of the Working Group on the  
Business Environment of the Stockbroking Industry**

On 15 January 2003, the Secretary for Financial Services and the Treasury (SFST) announced the establishment of a tripartite forum thereafter formally named as “the Working Group on the Business Environment of the Stockbroking Industry” (“the Working Group”) to examine with the stockbroking industry ways to enhance the competitiveness of the small and medium sized stock brokerage firms, and asked the Working Group to submit to him a report in three months’ time.

2. The Working Group submitted the Report to SFST on 15 April 2003. The Report was released to the public in the afternoon of the 16 April 2003.
3. A copy of the Report is at Annex for Members’ reference.
4. Members are invited to note the Report.

Financial Services Branch  
Financial Services and the Treasury Bureau  
16 April 2003

---

**Report of**

**The Working Group on the**

**Business Environment of**

**the Stockbroking Industry**

---

**April 2003**

---

# CONTENTS

---

	<i>Page</i>
<b>EXECUTIVE SUMMARY</b>	
SUMMARY .....	1
RECOMMENDATIONS .....	2
<b>CHAPTER 1 INTRODUCTION</b>	
ESTABLISHMENT OF THE WORKING GROUP .....	7
MODUS OPERANDI OF THE WORKING GROUP	
Listening to the stockbroking industry .....	7
Exchanging views with other relevant Organisations.....	8
<b>CHAPTER 2 BUSINESS ENVIRONMENT OF THE STOCKBROKING INDUSTRY</b>	
CHANGES IN INDUSTRY LANDSCAPE.....	9
LIBERALISATION OF THE COMMISSION RATE .....	12
<b>CHAPTER 3 ENGAGING THE INDUSTRY</b>	
INTRODUCTION .....	14
MAJOR ISSUES RAISED BY THE INDUSTRY .....	14

	<i>Page</i>
RESPONSES OF THE WORKING GROUP .....	16
Maintaining the 0.25% minimum commission rate?.....	16
Concern about predatory pricing .....	17
Would a system of two-tier commission rate help?.....	18
Leveling the playing field with banks –	
<i>Unsolicited calls in relation to securities         and futures contracts .....</i>	20
<i>Licensing fees for regulated activities.....</i>	21
Rationalising obsolete regulatory requirements and fees imposed by HKEx .....	22
Abolishing stamp duty on securities transactions .....	23
Supervision by the SFC .....	23
<i>Benefits of the new licensing regime under the SFO ..</i>	24
<i>New licensing fees under the SFO .....</i>	26
Review representativeness of HSI 33 .....	27
INITIATIVES PUT TO THE INDUSTRY .....	28
Transparency of fees and charges.....	29
Support for Investor Participant (IP) account.....	30
Promoting SME funding schemes .....	31
Promoting new products .....	32
Continuous training .....	33
<i>Facilitating re-entry of intermediaries into         the industry.....</i>	34
<i>Training and re-training of brokers .....</i>	34
<i>Promoting “portability” of qualifications attained         by members of the HKSI.....</i>	35

**CHAPTER 4 RECOMMENDATIONS**

INTRODUCTION .....	36
ENHANCING TRANSPARENCY OF FEES AND CHARGES .....	36
IMAGE BUILDING AND MARKET AWARENESS .....	37
LEVEL PLAYING FIELD –	
Enforcement of guidelines on “cold calls” .....	38
Regulatory fees for banks conducting securities business .....	38
RATIONALISING HKEX FEES FOR BROKERS .....	39
MINIMISING COMPLIANCE BURDEN.....	40
UPGRADING MARKET INFRASTRUCTURE – ENHANCED IP ACCOUNTS .....	41
NEW PRODUCTS .....	42
IMPROVING TRAINING OPPORTUNITIES.....	42

**CHAPTER 5 ACKNOWLEDGEMENT** 44**ANNEXES**

Annex A – Membership of the Working Group .....	A1
Annex B – Terms of reference.....	A2
Annex C – Chronology of events .....	A3
Annex D – Summary of written submissions to the Working Group .....	A5
Annex E – Licence fees charged by Hong Kong Monetary Authority and Securities and Futures Commission on Registered Institutions and Licensed Corporations for securities Business .....	A17
Annex F – SME funding schemes .....	A18

# **EXECUTIVE SUMMARY**

## **SUMMARY**

1. On 15 January 2003, the Secretary for Financial Services and the Treasury announced the establishment of the Working Group on the Business Environment of the Stockbroking Industry (“the Working Group”) to examine with the local stockbroking industry ways to enhance the competitiveness of the small and medium sized brokerage firms, and asked the Working Group to submit to him a report in three months’ time.

2. The Working Group comprises representatives from the Financial Services and the Treasury Bureau, the Securities and Futures Commission (SFC) and the Hong Kong Exchanges and Clearing Ltd (HKEx).

3. The Working Group attached great importance to engaging the stockbroking industry and listening to the industry’s views in examining proposals to improve the business environment and enhance competitiveness of the industry, in particular the small and medium sized brokerage firms. The Working Group met with members of the industry, including the five industry associations, namely, the Hong Kong Association of Online Brokers, the Hong Kong Securities Professionals Association, the Hong Kong Stockbrokers Association, the Hong Kong Securities and Futures Industry Staff Union and the Institute of Securities Dealers. To take forward the industry’s views and suggestions and explore ways to improve the business environment of the stockbroking industry, the Working Group has engaged relevant parties, including the regulators, government departments and industry organisations to address the issues of concern and consider possible solutions.

4. Major issues raised by the stockbroking industry include, amongst other things, maintaining the 0.25% minimum commission rate; concern about predatory pricing; proposing a system of two-tier commission rate; leveling the playing field with banks, particularly in the areas of unsolicited calls in relation to securities and futures contracts and licensing fees for securities activities; rationalising HKEx’s obsolete regulatory requirements and fees; and supervision by the SFC.

5. The Working Group also took the opportunity to put forward initiatives to the industry associations, which may help enhance the competitiveness of brokers, especially the small and medium sized players. These initiatives include enhancing the transparency of services provided by the intermediaries and their related charges; early implementation of the enhanced IP account model with straight-through processing capability; promoting SME funding schemes; diversifying brokers' product range to include retail bonds and investment funds; and promoting continuous training to facilitate re-entry of intermediaries into the industry, training and re-training of brokers, and "portability" of qualifications.

6. Having considered the views and suggestions from the industry, and input from relevant organisations, the Working Group puts forward recommendations which seek in the main to enhance transparency of fees and charges, promote image building and market awareness of brokerage firms, level the playing field between brokers and banks, rationalise HKEx fees for brokers, minimise compliance burden, upgrade market infrastructure, enable brokers to diversify their product range, and improve training opportunities for brokers. The recommendations are outlined in the ensuing paragraphs.

## **RECOMMENDATIONS**

7. To achieve fair competition, the Working Group supports enhancing transparency of fees and charges imposed by brokers and banks. This will also enable investors making more informed choices as well. The Working Group recommends that –

- (a) the SFC and the Hong Kong Monetary Authority (HKMA) should continue to monitor rigorously the disclosure by brokers and banks of the fees and charges imposed by them on their securities trading services;
- (b) both the SFC and HKMA should accord priority to the brokerage fee categorisation exercise and the stockbroking industry should contribute their views actively to the SFC for early completion of this exercise; and

- (c) the SFC should step up its publicity efforts to educate the investors to enable them to understand the services provided by intermediaries and compare the various fees and charges where necessary.

8. To promote image building for the brokers and market awareness of both the brokers and investors, the Working Group recommends that –

- (a) the stockbroking industry associations should consider setting up an electronic information directory for their members to promote their image and market awareness among clients; and
- (b) the HKEx should accord priority to hyperlink its web-site to those of its participants in order to provide a seamless information platform where investors and market participants alike will have free and unobstructed access to information on SEHK Participants.

9. To level the playing field between brokers and banks, the Working Group recommends that –

- (a) the HKMA should continue to ensure effective enforcement of its cold calling guidelines issued in January 2003 and to work closely with the SFC to ensure consistency in their regulatory approach towards banks and brokers; and
- (b) the HKMA should explore with the SFC the possibility of rationalising the relevant regulatory fees imposed on banks for conducting securities business, with a view to introducing a sliding scale of fees reflecting the size of the securities business of a bank.

10. On the rationalisation of HKEx regulatory requirements and the associated fees for brokers, the Working Group endorses the positive moves taken by the HKEx to abolish a number of regulatory requirements and the associated 10 fee items on brokers, ranging from \$100 to \$12,000 per fee



item, with effect from 1 April and 2 May 2003 respectively. In relation to this, the Working Group recommends that the HKEx and the SFC should accord priority to the review of fees inherited by the HKEx from the pre-merger entities, with a view to rationalising and simplifying them for Exchange users.

11. To minimise compliance burden on the small and medium sized brokers in light of the new regulatory regime introduced by the new Securities and Futures Ordinance (SFO), the Working Group recommends that –

- (a) the SFC should endeavour to adopt a pro-compliance approach in facilitating brokers' compliance with the new SFO and avoid any unnecessary regulatory burden for firms with good internal controls and good risk management and practice. The Working Group supports the flexible approach adopted by the SFC in calibrating regulatory action against brokers on minor, inadvertent or technical first-time breaches of new requirements under the SFO. In general, the SFC should continue to engage the industry in streamlining regulatory requirements;
- (b) the stockbroking industry, while continue to focus on compliance, should maintain dialogue with the SFC on any difficulties they experience in complying with the new requirements under the SFO and forward their suggestions for improvement to the SFC;
- (c) the SFC should consider, and work closely with the Hong Kong Securities Institute (HKSI) in developing, alternative means to satisfy the licensing competence requirements for re-entry seekers; and
- (d) the HKEx should consider possible areas for streamlining and rationalising the regulatory requirements in relation to SEHK Participants under the Rules of the Exchange.

12. To upgrade the market infrastructure so that the smaller brokers will be better positioned to compete with larger players, the Working Group

recommends that –

- (a) the SFC and the HKEx should accord priority to the development of a user-friendly and cost-effective Investor Participant (IP) account model with straight-through processing capability;
- (b) the industry associations should participate actively in the design and set up of the IP account model by offering their views to the IP Account Task Force of the SFC;
- (c) the industry associations should take their members through the proposed model to facilitate industry buy-in;
- (d) the SFC should examine the possibility of lowering capital requirement for brokers who do not hold client assets and tiering capital requirements according to risk and nature of business; and
- (e) the HKMA should make every effort to persuade banks to adopt a fair and transparent pricing structure for arranging money transfers to IP accounts and if necessary, to seek to provide the basis for such a structure through a code of conduct for the banking sector.

13. To enable brokers to diversify their product range to include retail bonds and funds, the Working Group –

- (a) supports the fostering of business partnership between the Hong Kong Investment Funds Association (HKIFA) and brokers, in particular small and medium sized brokers, and encourages collaboration between the HKIFA, the HKSI and other relevant groups in organising more training courses to enhance brokers' knowledge in new products; and
- (b) recommends the SFC and the HKEx to further facilitate

straight-through listing of the SFC authorised funds including, in particular, Exchange-Traded Funds, Real Estate Investment Trusts and bonds.

14. To improve training opportunities whereby the competitiveness of brokers will be enhanced, the Working Group recommends that -

- (a) the HKSI should continue to provide courses widening the skill set of brokers to enable them to provide new services, such as financial planning, and continue its efforts in taking forward its various initiatives, such as portability of qualifications;
- (b) the SFC should continue to play a supportive role in facilitating brokers meeting the continuous professional training (CPT) requirement such as providing speakers for CPT programmes organised by stockbroking industry associations;
- (c) the HKEx should extend education seminars to stockbroking industry associations to increase the infiltration of product knowledge and investment/trading strategies to their members, and to the investing public; and
- (d) the stockbroking industry associations should disseminate to their members information on the SME funding schemes and forward their views, if any, to the relevant government departments on ways to further improve the operation of these schemes.

# **CHAPTER 1 INTRODUCTION**

## **ESTABLISHMENT OF THE WORKING GROUP**

1.1 The Administration acknowledges the contribution of the stockbroking industry, including the small and medium sized brokers, to the financial markets of Hong Kong and fully recognises the difficulties faced by the stockbroking industry in prevailing market conditions. On 15 January 2003, the Secretary for Financial Services and the Treasury announced the establishment of a tripartite forum thereafter formally named as “the Working Group on the Business Environment of the Stockbroking Industry” (“the Working Group”) to examine with the local stockbroking industry ways to enhance the competitiveness of the small and medium sized brokerage firms, and asked the Working Group to submit to him a report in three months’ time.

1.2 The Working Group comprises representatives from the Financial Services and the Treasury Bureau (FSTB), the Securities and Futures Commission (SFC) and the Hong Kong Exchanges and Clearing Ltd (HKEx). Its membership is at Annex A.

1.3 The terms of reference of the Working Group, as approved by the Secretary for Financial Services and the Treasury, are at Annex B.

## **MODUS OPERANDI OF THE WORKING GROUP**

### **Listening to the stockbroking industry**

1.4 The Working Group attached great importance to engaging the stockbroking industry and listening to the industry’ views in examining proposals to enhance the business environment and competitiveness of the small and medium sized brokerage firms.

1.5 Following the establishment of the Working Group in mid January, the Working Group immediately arranged meetings with members of the industry, including the five industry associations, namely, the Hong Kong Association of Online Brokers, the Hong Kong Securities Professionals Association, the Hong Kong Stockbrokers Association, the Hong Kong Securities and Futures Industry Staff Union and the Institute of Securities Dealers. Suggestions on how to improve the business environment of the industry were discussed at the meetings. After the first

round of meetings, the industry associations were invited to send in written submissions and comments to the Working Group. Upon receiving the industry associations' suggestions and completion of preliminary analysis thereof, the Working Group arranged a second round of meetings with the associations in March 2003 to follow up on the various issues raised at the first round of meetings and discussed further the suggestions raised in their written submissions. Views made by the industry associations were thoroughly considered by the Working Group. Opportunities were also taken to consult the industry associations on other initiatives that were not raised by the associations, but which the Working Group considered worth exploring to enhance the competitiveness of the stockbroking industry. The Working Group is grateful to members of the industry for their constructive input without which this report could not take shape.

### **Exchanging views with other relevant organisations**

1.6 To take forward some of the suggestions made by the industry and the Working Group's own initiatives, the Working Group sought input from other relevant organisations, including the Hong Kong Monetary Authority (HKMA), the Hong Kong Investment Funds Association (HKIFA), the Hong Kong Securities Institute (HKSI) and the Hang Seng Index Services Limited (HSISL). The Working Group is grateful to these organisations for their valuable contributions in formulating relevant recommendations.

1.7 A brief chronology highlighting the above-mentioned events is at Annex C.

# CHAPTER 2 BUSINESS ENVIRONMENT OF THE STOCKBROKING INDUSTRY

## CHANGES IN INDUSTRY LANDSCAPE

2.1 The Working Group noted the changes in the stockbroking industry landscape since 1995, that we have experienced a bull market leading up to 1997, a market downturn during the Asian Financial Crisis in 1998, a subsequent rebound of the market in 2000 propelled by cyber fevers and a bear market after the burst of the cyber bubble in 2001.

2.2 At the end of 1995, there were 489 trading Participants of the Stock Exchange of Hong Kong (SEHK Participants). The number reached the record high of 500 at the end of 2000 and since then decreased gradually to 471 by the end of 2002, a net decrease of 29 from the peak. During the same period, 209 firms resigned from the Stock Exchange whereas 191 firms were admitted as new SEHK Participants. Among the new entrants, there were 38 SEHK Participants originating from overseas.

2.3 The annual market turnover was about HK\$827 billion in 1995, then reached a record high of HK\$3,789 billion in 1997 but dropped to HK\$1,599 billion in 2002 (a decrease of 58% from the peak). The benchmark Hang Seng Index declined from 10,073 to 9,321 during the same period, representing a drop of 7%. The market trend in recent years is largely in line with that in major international financial centres, as shown in Table 1 below. Although the stock market turnover rebounded to HK\$3,048 billion in 2000 due to the cyber phenomenon, it fell subsequently after the burst of the cyber bubble.

**Table 1: Performance of market indices in major overseas exchanges as at end of year**

Year	Hong Kong		Tokyo		New York		London	
	HSI	% change	Nikkei 225	% change	DJIA	% change	FTSE 100	% change
1995	10,073	-	19,868	-	5,117	-	3,689	-
1996	13,452	33.53%	19,361	-2.55%	6,448	26.01%	4,119	11.63%
1997	10,723	-20.29%	15,259	-21.19%	7,908	22.64%	5,136	24.69%
1998	10,049	-6.29%	13,842	-9.28%	9,181	16.10%	5,883	14.55%
1999	16,962	68.80%	18,934	36.79%	11,497	25.22%	6,930	17.81%

2000	15,096	-11.00%	13,786	-27.19%	10,788	-6.17%	6,223	-10.21%
2001	11,397	-24.50%	10,543	-23.52%	10,022	-7.10%	5,217	-16.15%
2002	9,321	-18.21%	8,579	-18.63%	8,342	-16.76%	3,940	-24.48%

Source: HKEx

2.4 The total number of SEHK Participants' Authorised Clerks, Dealing Directors, Registered Users and Sales Representatives engaging in dealing activities, increased from 5,683 in 1995 to 8,954 in 2002, representing a growth of 58%. Details of the changes are summarised at Table 2 below –

**Table 2 : Changes in number of SEHK Participants, HKEx Registered Persons (RPs) and market trend (1995 – 2002)**

Year As of Dec 31	No. of SEHK Participants (% Change)	No. of HKEx RPs (% Change)	Annual Turnover (HK 'M) (% Change)	HSI As of Dec 31 (%Change)
1995	489 (-)	5,683 (-)	826,800.60 (-)	10,073 (-)
1996	480 (-1.84%)	5,999 (5.56%)	1,412,242.38 (70.81%)	13,452 (33.543%)
1997	494 (2.92%)	7,183 (19.74%)	3,788,959.79 (168.29%)	10,723 (-20.29%)
1998	492 (-0.40%)	7,820 (8.87%)	1,701,112.01 (-55.10%)	10,049 (-6.29%)
1999	491 (-0.20%)	8,195 (4.80%)	1,915,940.58 (12.63%)	16,962 (68.80%)
2000	500 (1.83%)	9,497 (15.89%)	3,047,565.32 (59.06%)	15,096 (-11.00%)
2001	492 (-1.60%)	9,493 (-0.04%)	1,950,086.74 (-36.01%)	11,397 (-24.50%)
2002	471 (-4.27%)	8,954 (-5.68%)	1,599,062.36 (-18.00%)	9,321 (-18.21%)

Source: HKEx

2.5 A further review of SEHK Participants' market shares revealed that the market share for Category A<sup>1</sup> increased from 40.12% in 1995 to 49.35% in 2002, whilst that for Category C decreased from 27.62% to 19.18%. For the same period, the market share for Category B decreased only slightly from 32.26% to 31.47%. Over the years, local banks in general have been substantially expanding their retail stockbroking business to diversify and enlarge their revenue base. It would appear that the

---

<sup>1</sup> According to the HKEx, the first 14 SEHK Participants with the highest volume of turnover are categorised as Category A, the subsequent 15 to 65 as Category B, and the rest Category C.

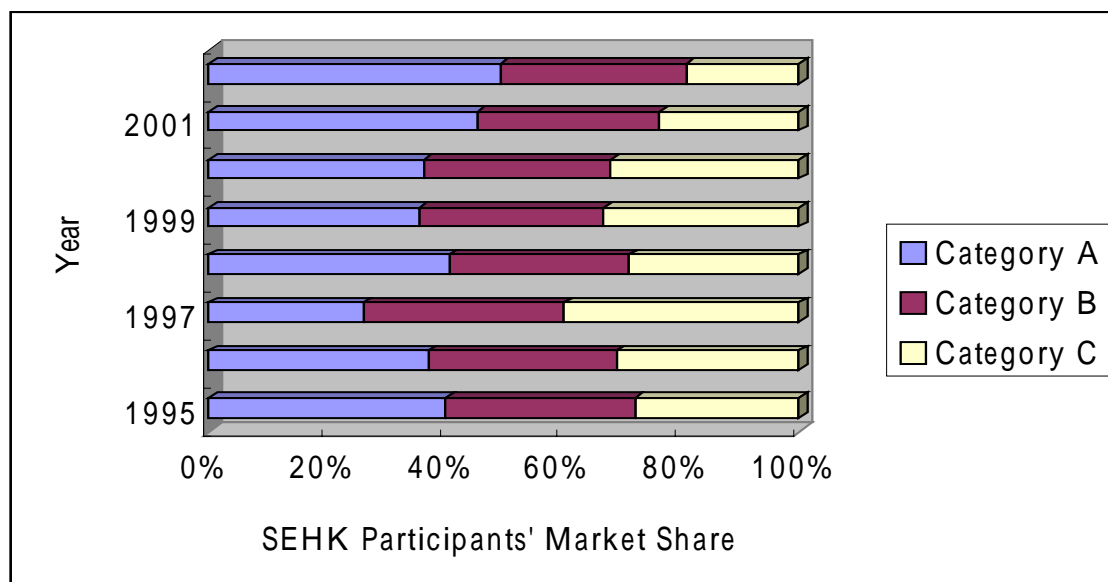
existence of minimum commission had no bearing to the changes in market share among SEHK Participants, as shown in Table 3 and Graph 1 below.

**Table 3 : SEHK Participants' market shares analysis (1995 – 2002)**

Year	Category A (Position 1 to 14)	Category B (Position 15 to 65)	Category C (Position > 65)
1995	40.12%	32.26%	27.62%
1996	37.10%	31.95%	30.95%
1997	26.22%	34.06%	39.72%
1998	40.71%	30.54%	28.75%
1999	35.50%	31.48%	33.02%
2000	36.55%	31.58%	31.86%
2001	45.54%	30.89%	23.57%
2002	49.35%	31.47%	19.18%

Source : HKEx

**Graph 1 : SEHK Participants' market shares analysis (1995 – 2002)**



Source : HKEx



## **LIBERALISATION OF THE COMMISSION RATE**

2.6 The Working Group noted that the minimum brokerage commission rule (the Rule) was set out in paragraph 534(1) and (2) in the Rules of the Exchange and, like any other Rules of the Exchange, was applied to the SEHK Participants and subject to the approval of the SFC before it might take effect.

2.7 The Working Group also noted that following consultations in March 2002, the Board of Directors of the HKEx endorsed on 17 May 2000 the proposal to remove the Rule with effect from 1 April 2002. In light of market conditions and Government's view, the Board of Directors of the HKEx decided on 20 February 2002 to defer abolition of the Rule for one year until 1 April 2003.

2.8 The Working Group further noted that the Board of Directors of the HKEx confirmed on 15 January 2003 its earlier decision that the Rule would cease to have effect from 1 April 2003. In relation to this, the HKEx Board had taken into account the views of the Government that the liberalisation of the brokerage commission was in the best interests of the public<sup>2</sup>.

2.9 The Working Group meanwhile noted the findings of a survey published by the Consumer Council in February 2003 on securities brokerage commissions and fees charged by brokers and banks<sup>3</sup>. The findings indicated that on average, the cost of securities transactions conducted through banks is higher than that of brokerage firms. Among the surveyed brokerage firms, the trading commissions varied over a wide range

---

<sup>2</sup> On 14 January 2003, the Secretary for Financial Services and the Treasury wrote to the Chairman of the HKEx, setting out the Administration's stance on the Rule. It is the Administration's long-held position that, with the merger of the pre-existing exchanges and clearing houses and subsequent listing of the merged entity, the level of commission charged by its participants should be a matter essentially between the participants and their clients. This is in line with the government overall competition policy, which aims to allow participants to compete freely in the market, and hence provide choices for both participants and investors. The deferral of the expiry date for the Rule in January 2002 has already allowed the industry a three-year transition period in preparing for the change that, in the Administration's view, is reasonable. The Administration believes that with the expiry of the Rule in April 2003, the ensuing liberalisation of the commission rate will be in the best interests of the public. The Administration also notes that in practice as non-Exchange participants were not subject to the Rule, they had always been able to offer different commission rates to their clients. Moreover, in more recent times, even some Exchange participants had ceased to observe the Rule. It is also noted that, whatever the legal position, this Rule is difficult to enforce.

<sup>3</sup> CHOICE Magazine, Issue No. 316, 17 February 2003.

from 0.1% to 0.5% of the transaction amount. Such factors as transaction channels (electronic channel vs traditional channel), the transaction amount and frequency, client relationship, etc all played a part in the determination of brokerage commissions to consumers. According to the Consumer Council, this clearly indicates that the minimum brokerage commission of 0.25% could be negotiable and subject to bargaining or circumvented through related non-SEHK Participants (including on-line brokers) who are not bound by the Rule.

## **CHAPTER 3     ENGAGING THE INDUSTRY**

### **INTRODUCTION**

3.1            In this chapter, we will address the major issues raised by the industry, set out the Working Group's response to these issues, and explain the initiatives that the Working Group has taken forward in response to some of the views of the industry.

### **MAJOR ISSUES RAISED BY THE INDUSTRY**

3.2            All the five industry associations have been positive in putting forward suggestions to the Working Group to improve the business environment of the stockbroking industry. Their key suggestions cover broadly the following areas –

(a)    Maintaining the minimum commission rate

Four of the five industry associations considered that the 0.25% minimum commission rate should be retained. They feared that liberalisation of the commission rate might allow for cut-throat price competition which would ultimately drive most of the small and medium sized brokerage firms out of business.

Three of the five industry associations suggested that the commission rate should be liberalised in phases. They advocated that a two-tier system should be introduced, with a minimum commission rate of 0.25% for transactions below a certain value. They suggested that the cut-off transaction value, below which investors were to be subject to a minimum commission rate, should be set at \$1 million<sup>4</sup>.

(b)    Leveling the playing field with banks

The respondents considered that brokerage firms were in a

---

<sup>4</sup> A survey was conducted by the industry in February 2003 (led by the Hon Henry K C Wu) and the survey results reflected the opinion of 183 respondent brokerage firms (out of a total of 478 firms surveyed). Among the 183 respondent firms, 161 agreed to a two-tier brokerage commission system with the specific invoice amount set at \$1 million, 10 agreed to a two-tier brokerage commission system with invoice amount set below \$1 million, 7 disagreed to a two-tier commission system with the specific invoice amount set at \$1 million and 5 offered no comment.

disadvantageous position when compared with banks since brokerage firms could only access one category of clients, i.e. securities clients, whereas banks have a large client base straddling banking, securities, insurance and other sectors. The respondents also complained banks “cold calling” their clients for promotion of securities trading.

The respondents were of the view that banks paid less regulatory fees than brokers because bank staff dealing with securities did not have to pay individual licence fees, whereas staff of brokerage firms had to pay individual annual fees as licensed representatives. They also perceived that banks paid a single fee to the HKMA which covered all branch offices whereas brokerage firms paid a licence fee for the head office and another fee for each branch office. The respondents urged the government to review the fees for banks conducting securities business with a view to bringing these fees on par with those imposed on brokers.

(c) Reviewing HKEx fees and stamp duty

The respondents considered that some of the HKEx fees were outdated and should be abolished to alleviate their cost of business. They were of the view that these fees should be rationalised in light of the migration of the stock exchange from a membership organisation to a for-profit listed company, and transfer of the role as a front line regulator of broker-participants from the Exchange to the SFC, after the merger and demutualisation exercise.

They also called for reduction or abolition of stamp duty on securities transactions.

(d) Reducing compliance burden

The respondents asked the SFC to avoid excessive and unwarranted inspections and inquiries involving interviews and examinations of brokers’ clients, as these would drive genuine investors away. They suggested that the supervision by the regulators should not be prosecution- or penalty-oriented. They were of the view that regulators should make every effort to assist brokers in complying with the regulatory requirements,

especially with the new requirements in place under the new Securities and Futures Ordinance (SFO).

3.3 A summary of the suggestions put forward by the industry associations in their submissions to the Working Group is at Annex D.

## **RESPONSES OF THE WORKING GROUP**

3.4 The Working Group noted the industry's views and suggestions. To take these forward and explore ways to improve the business environment of the stockbroking industry, the Working Group has engaged relevant parties, including the regulators, government departments and industry organisations to address the issues of concern and consider possible solutions. The Working Group's responses to the above-mentioned industry concerns, as exchanged over meetings with the five industry associations conducted in January and March, are summarised in the ensuing paragraphs.

### **Maintaining the 0.25% minimum commission rate?**

3.5 The Working Group noted that the SEHK Rule on minimum brokerage commission rate (the Rule) was only applicable to SEHK Participants. The Working Group also noted that in practice non-SEHK Participants dealers (including banks) are not bound by the Rule and were already offering different commission rates to their clients prior to 1 April 2003. It also noted that, whatever the legal position, the Rule was difficult to enforce.

3.6 The Working Group noted that a number of factors, including market turnover, types of investment products offered and quality of services provided as well as overall economic condition and investment sentiment, would affect the business environment of the stockbroking industry. The expiry of the Rule is not equivalent to the complete removal of commissions. This would actually lead to liberalisation of brokerage commissions so that brokers are allowed greater flexibility in structuring their pricing strategy according to the needs of their investors, and the nature and types of services rendered. They can be in a better position to adapt to changing market needs and conditions.

3.7 The Working Group noted that the removal of the minimum commission is in line with practices in most major international markets, including the USA, the UK and Japan. Not only would this benefit both

investors as well as further development of the securities market in Hong Kong, this would create a more level playing field for brokers in that they may compete freely on commissions with non-SEHK Participants who have not been subject to SEHK Rules governing commissions.

### **Concern about predatory pricing**

3.8 The Working Group took note of the industry's concern over possible cut-throat pricing competition with larger players adopting predatory pricing practices after 1 April 2003. The Working Group has referred the industry's concern to both the SFC and the HKMA. The regulatory authorities undertake to monitor the situation and take appropriate action as necessary.

3.9 As a matter of fact, the Working Group noted that the SFC, in its public circular of 19 March 2003, encourages investors to ascertain carefully the details of any promotional offers by a brokerage firm before trading through the firm. In particular, investors must exercise caution to ensure that all relevant features of the promotional offer are disclosed in full, including the method of calculation, the period for which such promotional offer will be available, any minimum threshold of charges, any eligibility conditions or restrictions, and whether there are other hidden charges. The SFC will immediately undertake a review of that broker's fitness and properness to remain registered and take appropriate disciplinary action if any broker is found to have issued an advertisement that is false, disparaging, misleading or deceptive.

3.10 In addition, as stated in another circular issued by the SFC on 27 March 2003, the SFC will step up its review of brokers' advertisements on promotional offers following the lapse of the Rule on 1 April 2003. It is stressed once again that the SFC will not tolerate dissemination of false or misleading information by brokers and banks to the investing public.

3.11 In respect of regulatory requirements on banks, the Code of Banking Practice (issued jointly by the Hong Kong Association of Banks (HKAB) and the Deposit-Taking Companies Association (DTCA), and endorsed by the HKMA) requires banks to ensure that all advertising and promotional materials are fair and reasonable, do not contain misleading information, and comply with all relevant legislation, codes and rules. This Code also requires that the terms and conditions should highlight any fees, charges, penalties and relevant interest rates as well as the customer's liabilities and obligations in the use of services provided by banks (including

securities services). The HKMA will take appropriate supervisory action if a bank's practice is found to have departed from the Code, e.g. issuing a false or misleading advertisement.

3.12 The Working Group believed that promoting price transparency and ensuring freedom of market entry will render any predatory pricing strategy unattractive. The Working Group also considered that an effective means to promote competition was to facilitate free flow of information on the nature of services provided and the fees and charges for such services in the market for the investors to compare and choose. In this regard, the Working Group noted and has informed the industry associations that the Consumer Council published a survey report on securities brokerage commissions and charges on 17 February 2003.

3.13 The Consumer Council's survey revealed that on average, the cost of securities transactions conducted through banks is higher than that of brokerage firms. The survey also found that there are over 70 types of charges applicable to the use of securities trading services. The varieties of charges are difficult for the investing public to understand the circumstances in which the charges are imposed or to compare them. Difference in nomenclature adopted by brokers and banks adds to the confusion of investors.

### **Would a system of two-tier commission rate help?**

3.14 The Working Group noted that three of the five industry associations suggested a two-tier brokerage commission system with a threshold set at a specific invoice amount below which a minimum commission rate of 0.25% should be imposed. The preliminary suggestion was to set the threshold at an invoice amount of \$1 million.

3.15 The Working Group has carefully considered this proposal but come to the view that such a system would not be conducive to improving the competitiveness of the stockbroking industry, especially the small and medium sized brokerage firms, for the following reasons –

- (a) Some market players, including the banks, could find ways to bypass Exchange rules on commission rates through a non-SEHK participant entity in their organisational set up. According to a survey<sup>5</sup> conducted by the SFC in 2001, clients of

---

<sup>5</sup> SFC's Business Activities Survey on Securities/ Futures Intermediaries and Exempt Persons, October 2001.

banks accounted for over 40% of the total number of active clients of brokers and banks in securities business. It would not be in the interest of the stockbrokers to impose any restriction on their pricing strategy if they are to compete with other players, notably the banks, which are free from such restriction. To do so would deter the brokers from targeting their clients with effective marketing strategy;

- (b) the Consumer Council's survey findings (see para. 3.13 above) revealed that even before 1 April 2003, the industry was offering different commission rates to different clients and individual brokerage firms set different minimum entrance fees for recovering the basic overheads. It would be against the going market trend to mandate a two-tier system for all brokers. This would deprive brokers of flexibility in devising market segmentation strategy and hence deter any efforts to enhance their competitiveness; and
- (c) imposing a threshold of \$1 million would deprive nearly all retail investors of the right to negotiate commission rates with the brokers. During February 2002 to March 2003, over 99% of matched deals on SEHK were below \$1 million. The same arguments against preserving a minimum commission rate, as set out in paragraphs 3.5 to 3.7 above, would equally apply. In short, a mandatory two-tier system would discourage the local brokerage industry to enhance its competitiveness through marketing and pricing strategies while their competitors around the globe are advancing themselves.

3.16 The Working Group considered that the proposal would be against the interest of the investing public as investors do not have collective bargaining power. It would be unfair to impose any arbitrary dividing line of transaction amount below which the investors are not allowed to negotiate the price with the brokers. It would deprive investors of choice. This runs against the free market philosophy on which our economy thrives. In this regard, the Working Group notes that there are no professional service providers in Hong Kong which adopt an industry wide price fixing practice.

3.17 The Working Group took note of the Consumer Council's position on this subject. The Consumer Council does not support a system that sets an industry wide rule fixing brokerage commissions, either on a tiered basis or otherwise. The Consumer Council considers that such an



arrangement is price fixing and goes against the very ideals of a free market that the Government and the Hong Kong business community so often proclaim as necessary for Hong Kong to maintain its competitive edge. It does not consider an industry wide rule that denies a section of the investing public the benefit of price competition, through fixing brokerage commissions, is conducive to enhancing the quality of Hong Kong's financial market or protecting investors. The small investors will be the ones losing out on the benefits of price competition. The Consumer Council is of the view that it is small investors who the Government should be specifically protecting, through ensuring that they are able to take advantage of the level of price competition that a free market brings about.

3.18 The Working Group noted that under the newly commenced SFO, the SFC's regulatory objectives are, inter alia, to maintain and promote the fairness, efficiency, competitiveness, transparency and orderliness of the securities and futures industry; and to provide protection for members of the public investing in or holding financial products<sup>6</sup>. It will therefore be *ultra vires* for the SFC to make any statutory rules mandating minimum commission rate and/or sanctioning two-tier commission rates, or approve any non-statutory rules made by the HKEx for the same purpose, as these will be construed as anti-competitive.

### **Leveling the playing field with banks**

#### ***(a) Unsolicited calls in relation to securities and futures contracts***

3.19 The Working Group has referred to the HKMA the industry's concern over banks' alleged "cold calls" on their depositors to solicit securities business. The HKMA informs the Working Group that it issued a Circular on Calls in Relation to Securities or Futures Products and Services to all authorised institutions ("banks") on 13 January 2003<sup>7</sup>. The Circular serves to provide specific guidance to banks on the restrictions on unsolicited calls ("cold calls") in relation to securities and futures contracts, and ensure that all banks have adequate procedures in place and provide proper training to relevant staff to promote compliance with the requirements. It should be emphasised that the same set of requirements are applicable to brokers and banks alike in this regard. The Working Group also noted that

---

<sup>6</sup> Section 4, Securities and Futures Ordinance (Cap. 571).

<sup>7</sup> For full version, please visit the website of the HKMA at <http://www.info.gov.hk/hkma/eng/guide/index.htm>.

the HKMA would continue to monitor and enforce restrictions on unsolicited calls among all banks.

3.20 After issuing the circular of 13 January 2003, the HKMA has conducted special meetings with various banks to provide further guidance on the practical application of the circular, to emphasise the importance of compliance, and to review banks' marketing policies and procedures in the day-to-day supervision process. During this period, the HKMA has not received any customer complaints against unsolicited calls made by banks. In light of the industry's concern, the Working Group put forward a recommendation in the next chapter.

***(b) Licensing fees for regulated activities***

3.21 The Working Group noted that there is a discrepancy in regulatory fees for banks and brokers which stems from the difference in the core business conducted by banks and brokers and the way in which the regulatory fees are structured. In response to the industry, the Working Group has referred to the SFC and the HKMA the industry's concern over the perceived difference in licensing fees paid by brokerage firms and banks for the same regulated activities. It has also conducted a comparison of these fees with the SFC and the HKMA, now set out at Annex E.

3.22 Under the new regulatory regime under the SFO, banks carrying on securities business must be registered with the SFC as "registered institutions" and pay an annual fee of \$35,000 per regulated activity. Annex E indicates that under the new regime, the average amount of fee payable by a bank (registered institution) is very close to that of a brokerage firm (licensed corporation) on a per establishment and per regulated activity basis. In response to the Working Group, the HKMA notes that banks are already subject to a range of fees in relation to their businesses (including annual fees for each of the branches which they maintain), which have not been charged on the basis of the number of activities or the number of staff employed. For brokers, corporations are only required to pay \$4,740, whilst representatives have to pay \$1,790 (or \$4,740 if they are responsible officers), in annual fees for each regulated activity<sup>8</sup>.

3.23 In terms of statutory capital requirements, banks are required to have a paid-up capital of \$300 million and maintain a capital adequacy ratio

---

<sup>8</sup> In general, stockbrokers are required to be licensed for Type 1 regulated activity (i.e. dealing in securities) only, in order to carry on stock brokerage business.

of 8% and a liquidity ratio of 25% as minimum requirements. These requirements are generally more stringent than those applied to the SFC-licensed brokers. A corporation engaging in securities dealing is required by the SFC to have a paid-up capital of \$5 million and a liquid capital of \$3 million or 5% total liabilities whichever the higher.

3.24 The above notwithstanding, the Working Group considered that the situation needs monitoring and put forward a recommendation in the next chapter.

### **Rationalising obsolete regulatory requirements and fees imposed by HKEx**

3.25 The Working Group has invited HKEx to consider the industry's concern over certain obsolete regulatory requirements and the associated fees imposed by HKEx. In response to the industry's concerns, HKEx has rationalised the situation and amended the Rules of the Exchange. The process is proceeding in two phases, first in April and second in May 2003.

#### **Phase I (with effect from 1 April 2003)**

In response to the industry's concerns, the HKEx has reviewed its Rules of the Exchange and to dovetail the commencement of the SFO on 1 April 2003, the HKEx brought forward the following changes to the Rules of the Exchanges –

- (a) Abolishing the existing mechanism for registration of Sales Representatives (at \$300 per application), approval of Branch Offices (at \$12,000 per application and monthly subscription of \$2,900 per branch), appointment of Branch Office Managers (at \$1,000 per application) and issue of Branch Certificates. The payment of fees and charges relating to such mechanism by SEHK Participants has accordingly been abolished;
- (b) Replacing the existing mechanism for prior written approval of the Stock Exchange for any change in the share capital structure not involving change in control of and payment of the related fee (of \$1,000 per application) by SEHK Participants by a notification requirement without the payment of any fee; and
- (c) Aligning the notification level for decrease in liquid capital by

SEHK Participants to 120% from 130% to level the requirement under the current Rules of the Exchange and the Financial Resources Rules (FRR) requirements of the SFC.

### **Phase II (with effect from 2 May 2003)**

HKEx will implement further rationalised fee items from 2 May 2003.

Details of these fees items will be set out in the next chapter.

### **Abolishing stamp duty on securities transactions**

3.26 The Working Group noted that the level of stamp duty on securities transactions has been reduced for over 60% from 0.6% in 1990 to the current level of 0.2%. In both Budget speeches of 2000-01 and 2001-02, the Financial Secretary proposed to lower the stamp duty on securities transactions having regard to the anticipated removal of the minimum brokerage commission rate then. The Working Group noted that the Government will keep the level of stamp duty on securities transactions under review.

### **Supervision by the SFC**

3.27 The Working Group has referred to the SFC the industry's concerns on the seemingly negative style of supervision by the SFC.

3.28 As a regulator, the SFC has the duty to make inquiries and enforce the law to protect not only the investors but also to ensure that the intermediaries remain fit and proper brokers. The SFC believes that, enforcing the law and protecting the investors are not mutually exclusive in helping the market and the industry. For example, the SFC has been granting modifications of FRR requirements to individual firms where it is satisfied that compliance is unduly burdensome and the granting of the modifications is not contrary to the interest of the investing public. On the same basis, the SFC may exercise discretion in allowing firms to continue operation despite a deficiency in liquid capital, subject to conditions.

3.29 The inspections conducted by SFC are risk-based. This entails high risk firms such as those known to have major internal controls or compliance deficiencies or thin regulatory capital that are inspected more frequently than low risk firms. This approach is commonly used by other

world-class regulators, such as the Financial Services Authority in the UK. The SFC's inspection targets selection approach, criteria and procedures are subject to vetting by the Process Review Panel, an independent panel appointed by the Chief Executive to review and monitor the process of the SFC to ensure that it observes due process for ensuring consistency and fairness in handling cases, taking actions or making decisions. Unwarranted inspections are prevented by internal procedural safeguards, which again are subject to vetting by the Process Review Panel.

3.30 The SFC has assured the Working Group that it believes in maintaining an open dialogue with the industry and providing assistance wherever possible. By regularly meeting with the various industry associations, the SFC is able to review all the rules and requirements on an ongoing basis to ensure that they strike an appropriate balance between market facilitation and investor protection.

3.31 To help the industry understand the new requirements under the SFO, the SFC has organised or taken part in some 60 training seminars over the past 12 months to familiarise more than 13,000 audiences with the new SFO requirements. The SFC's response to frequently asked questions is also posted on the SFC's web-site to explain its policy intention and to provide clarification on the application of the SFO where needed.

3.32 In response to the industry, the Working Group noted that a lot has already been done under the new SFO to streamline the regulatory requirements. These efforts are briefly set out in paragraphs 3.34 to 3.39 below. The Working Group has encouraged the industry to keep in view any compliance problems under the new SFO and to forward their suggestions for improvement to the SFC.

3.33 The Working Group also considered that further streamlining of regulatory requirements would be beneficial to the development of the industry and put forward a recommendation in the next chapter.

### ***Benefits of the new licensing regime under the SFO***

3.34 To give a clear picture to the industry, the Working Group took note of, and considered it useful to recapitulate here the benefits that the small and medium sized brokerage firms may capitalise on under the new licensing regime of the SFO in order to enhance their competitiveness.

- (a) The SFO seeks to provide a more level playing field for banks and brokerage firms conducting regulated activities (e.g. securities business defined in the SFO) –
  - banks will be required to be registered with the SFC for undertaking regulated activities;
  - banks will be subject to the same regulatory regime, including investigation powers and disciplinary sanctions;
  - relevant rules, the SFC codes and guidelines will apply to banks (and relevant individuals), including guidelines on competence, continuous professional training and the Code of Conduct.
- (b) The SFO seeks to facilitate business operations of brokerage firms by reducing their compliance burden –
  - allowing them to engage in multiple regulated activities under a single licence and with a single set of capital for all regulated activities of the firm; and
  - streamlining of annual return submission (a simple “no change declaration” in place of the previous full annual return submission).
- (c) The SFO seeks to streamline regulatory requirements on brokers by –
  - granting of provisional representative licences pending granting of normal representative licences that would enable the representative to start work much earlier;
  - extending licensing period for representatives to find new employment so that representatives will have a 180-day period to find a new employer before their licences lapse (as opposed to the previous 60-day period); and
  - relaxing the responsible officer requirement so that an experienced senior staff may be appointed as a responsible officer although not being a director.

- (d) The SFC has also issued various guidelines to complement the SFO to advance the implementation of the flexible requirements on brokers. These include –
- Waivers on competence requirement to facilitate experienced securities brokers diversifying into futures activities; and
  - Relaxation on Continuous Professional Training (CPT) requirements.
- (e) Meanwhile, a multiple range of rules under the SFO also provide for the conducive environment for brokers' compliance and conduct of business. Some examples are highlighted below –
- Relaxation of the client securities and client money rules, which are applicable only to client securities, securities collateral and client money received or held in Hong Kong. Under the Rules, automatic renewal of client standing authority subject to prescriptive client notification requirements is allowed;
  - Relaxation of rules regarding contract notes, statements of account and receipts, which (a) extends the time allowed for issuing contract notes to two days, (b) allows consolidation of contract notes, daily-statements and receipts into one document, and (c) permits the reporting of only average prices in contract notes; and
  - Relaxation of the FRR to (a) introduce an option for securities dealers to treat clients as rolling balance cash clients (subject to necessary safeguards), and (b) allow the inclusion of Certificate of Deposits and equity-linked instruments as liquid assets.

### ***New licensing fees under the SFO***

3.35 The SFC has assured the Working Group that brokers will not pay more licensing fees under the SFO than they are already paying. The SFC's new licensing regime will help reduce compliance costs to brokerage firms if they streamline their businesses and seek only to be licensed for those regulated activities necessary to run their businesses.

3.36 Under the SFO, a stockbroker (who is licensed for Type 1 regulated activity) does not need a licence for Type 4 (advising on securities), Type 6 (advising on corporate finance) and Type 9 (asset management) if the latter activities are carried out wholly incidental to the stockbroker's dealing in securities. With this "incidental" exemption, a stockbroker holding a licence for only Type 1 regulated activity may also, for instance, issue research reports concerning securities, provide corporate finance advisory services and manage discretionary accounts for its securities clients if such activities are carried out incidental to its securities dealing business. Moreover, where a person is applying for a licence, or is licensed for Type 1 or Type 2 regulated activity, the licensing fees (including application fee and annual fee) payable by that person in relation to Type 7 regulated activity (providing automated trading services) will be waived.

3.37 In addition to the above waivers, a 3% across-the-board reduction in fees has been introduced for all licensed corporations and representatives. For example, the annual and application fees for a securities dealer's representative have been reduced to \$1,790 (from \$1,850).

3.38 Furthermore, existing intermediaries seeking to convert their licences under the new licensing regime in the first year of the two-year transitional period will enjoy a further 5% early bird discount on their annual fees till the end of the transitional period, i.e. a possible saving of up to 8%.

3.39 The Working Group noted that the SFC's licensing fees have not been increased since 1993/94 despite a rise in the Composite Consumer Price Index of 23.1% since March 1993, and the revenue generated from licensing fees is insufficient to cover the SFC's costs on licensing and supervision works.

### **Review representativeness of Hang Seng Index 33**

3.40 An industry association raised with the Working Group that the constituency of the HSI 33 should be reviewed to include other stocks which are more representative of the local stock market, in order to enhance its popularity as a hedging instrument for the cash market. It considered that the design of the HSI 33 should take into account the integration of the Hong Kong-Mainland economic development and reflect duly Hong Kong's mission as the premier capital formation centre for the Mainland. In response to this suggestion, the Working Group met with the HSI Services Limited (HSISL) to reflect the industry's suggestion.



3.41 The Working Group relayed the industry views to the HSISL and urged the HSISL to consider whether the criterion of selecting constituent stock(s) for the HSI should be kept under regular review in light of the increasing economic integration between Hong Kong and the Mainland. This could be of particular relevance in view of the increasing trend of Mainland enterprises with substantial market capitalisation and material impact on market liquidity/turnover coming to list in Hong Kong. Notable recent examples are CNOOC and China Telecom.

3.42 The HSISL informed the Working Group that since its inception in 1969, the HSI has aimed at tracking the pulse of the local stock market with a statistic summarising the overall experience of all investors given the rise and fall in prices of individual stocks. Over the years, the identities of listed companies and their localities of operation have changed, but the purpose and fundamental of HSI have remained unchanged.

3.43 The HSISL considered that the arrangements for the listing of Mainland enterprises, both state and private, in Hong Kong are unique. The HSISL has been keeping track of these market developments closely with a view to maintaining HSI always as a faithful and consistent market benchmark. The inclusion of locally-incorporated Mainland enterprises such as China Mobile and CNOOC in HSI is a case in point. The HSISL was also aware of the growing diversity of investors and their diverse requirements in market trackers and has developed a diverse family of indices to satisfy their demands. The HSISL assured the Working Group that it would further add new member indices to the family as the market demands, and would ensure that the selection criteria are reflective of market reality and coherent with index fundamentals.

## **INITIATIVES PUT TO THE INDUSTRY**

3.44 During the meetings with the industry associations, the Working Group took the opportunity to put forward initiatives which may help enhance the competitiveness of brokers, especially the small and medium sized players; to listen to their views as to how the Working Group may facilitate the implementation of these initiatives; and to urge them to disseminate these messages to their members with a view to seeking their support for taking these initiatives forward. These initiatives are set out in the ensuing paragraphs.

## **Transparency of fees and charges**

3.45 The Working Group noted that the Government is committed to the promotion of competition. In respect of the securities market, Government's policy objective is to ensure a fair, transparent and orderly market where intermediaries are free to enter to offer various types of services and where investors are able to make informed choices. The Working Group shared its views with the industry associations that an effective means to promote competition is to facilitate free flow of information in the market on the nature of services provided by the intermediaries, and the fees and charges for such services, in order for the investors to compare and choose.

3.46 The Working Group informed the industry associations that, in regulating the intermediaries, enhancing the transparency of the securities industry has always been a priority of the SFC and the HKMA, especially on items and details of services provided by the intermediaries and their related charges. Under the Code of Conduct promulgated by the SFC, intermediaries (including banks that are registered institutions) are required to provide in the client agreement a description of any remuneration (and the basis for payment) that is to be paid by the client, such as brokerage commissions, and any other fees and charges. The Code of Banking Practice promulgated by the HKAB and DTCA, and endorsed by the HKMA, also requires banks to make available to customers details of the fees and charges in connection with the services they provide (including securities services), and to advise customers of the details of the basis of charges at the time the services are offered or on request.

3.47 The Working Group also informed the industry associations that the Consumer Council published a survey report on securities brokerage commissions and charges on 17 February 2003. The survey revealed that banks generally charge a custody fee for providing share custodial services and deposit fees for transferring shares into a securities account, while brokers do not. On the other hand, brokers usually recover from their clients the scrip fees charged by the Central Clearing and Settlement System (CCASS), while most of the banks do not impose such a charge. On average, the survey found that the cost of securities transactions conducted through banks is higher than that of brokerage firms.

3.48 The survey also found that there are over 70 types of charges applicable to the use of securities trading services which can be confusing. They cover trade-related fees (such as commissions), settlement fees, fees on

account maintenance, transfer and deposit or withdrawal of stocks, and registration and scrip fees. The variety of charges is difficult for the investing public to understand the circumstances in which the charges are imposed or to compare them. Difference in nomenclature adopted by brokers and banks adds to the confusion of investors. The Consumer Council therefore urges the intermediaries providing securities trading services to be more transparent in their fee structure and encourages standardisation of the categories of fees charged.

3.49 In this connection, the Working Group considered that further enhancement of transparency of the nature of services provided and the related fees and charges by both brokers and banks would help address the industry's concern about unfair pricing competition with banks. The Working Group also believed that this would be beneficial to the investing public. It has put forward a recommendation in the next chapter and has urged the industry associations to participate in the implementation process.

### **Support for Investor Participant (IP) account**

3.50 The Working Group recognised the importance of IP account for the development of the securities market in Hong Kong. The enhanced IP account infrastructure addresses the issue of broker risks by offering legal protection of an investor's assets in CCASS or a trusted third party. By providing security for clients' assets and money, IP account enables the small and medium sized brokerage firms to compete for business with large players in the market. The Working Group, therefore, has taken the initiative to brief the industry associations at the meetings on the general parameters of the enhanced IP account model with straight-through processing capability. The model has been discussed at the IP Account Task Force led by the SFC and with the participation of members of the stockbroking industry and HKEx. The Working Group also briefed the industry associations that the SFC is presently revisiting the existing capital requirements in its review of the financial regulatory framework for brokerage firms. It is envisaged that firms that do not hold client assets (as their clients operate the enhanced IP accounts) could be subject to a substantially lower capital requirement than firms that hold client assets. The Working Group believed that this would be an effective incentive in promoting the take-up rate of the enhanced IP account.

3.51 The Working Group was encouraged to note that members of the industry are largely supportive of the initiative. They believed that with a user-friendly, efficient and affordable IP account system, brokers would be

able to have their risks minimised and this would put them on a level playing field competing with larger players on the basis of quality of personalised service, something in which they believed brokers had a competitive advantage. This notwithstanding, the Working Group urged the industry associations to take its members through the proposed model to facilitate industry buy-in.

3.52 To facilitate early implementation of the proposed IP account model, apart from urging the SFC and HKEx to work on the design of the technical model and the funding and financing proposal, the Working Group has sounded out with the HKMA industry's concern over possible discriminatory/anti-competitive pricing practice of banks on money transfers of investors to their IP accounts. The HKMA informs the Working Group that there is already competition among banks in Hong Kong in many different areas and there is no reason to believe that they would take collective action to impose discriminatory pricing on the payment of the proposed IP accounts scheme. This notwithstanding, in order to discourage any anti-competitive practice by banks which would undermine the sustainability of IP accounts and hence impact adversely on systemic risk and reduce choices for retail investors, the HKMA has suggested benchmarking the relevant charges against similar electronic money transfers to third parties now being conducted by banks, taking into consideration possible IT upgrade investment required on the part of banks to effect money transfers to HKEx's IP accounts. The Working Group was pleased to note this suggestion by the HKMA and has put forward recommendations in the next chapter.

### **Promoting SME funding schemes**

3.53 The Working Group believed that brokers may enhance their competitiveness by providing more value-added services. This would require continuous professional training, upgrading of IT support, and enhanced marketing efforts. In this regard, it noted that the Government provides financial assistance to SMEs through a number of funding schemes administered by the Trade and Industry Department (TID). The Working Group has met with TID representatives to ascertain the suitability and availability of the schemes to the small and medium sized brokers. The Working Group provided detailed information on these schemes including brochures and application forms to the industry associations and briefed them at meetings on the various SME funding schemes provided by the Government which may be of assistance to their members in their IT and telecommunications upgrading, capital financing, employers' and

employees' training and export marketing (see Annex F on details of the available SME funding schemes). The Working Group encouraged the industry associations to disseminate to their members information on the schemes and forward their views, if any, to the relevant government departments on ways to improve further the operation of these funding schemes.

### **Promoting new products**

3.54 The Working Group shared the views of some industry leaders that future direction of growth of the small and medium sized brokerage firms is to diversify their service offerings from single product dealers to financial planners. They also pointed out to the Working Group that it would be difficult for brokers to sustain their business by relying on a single revenue source in the long run. The Working Group, therefore, has taken the initiative to invite views from the Hong Kong Investment Funds Association (HKIFA), the Hong Kong Securities Institute (HKSI), relevant government bureaux and public utility companies as to how they may assist in this service diversification process for the brokers.

3.55 The Working Group has exchanged views with the industry associations on the possibility for brokers to diversify their product range to include retail bonds and funds, in order to enrich their service portfolio and enlarge their client base. The Working Group has invited the HKIFA to consider organising workshops on investment funds for brokers.

3.56 The HKIFA is forthcoming in engaging small and medium sized brokers in their distribution network of retail funds. The HKIFA reckoned the unique competitive edge of these brokers, who have a wide and personalised clientele different from the banks, would help widen their reach to the investing public.

3.57 The Working Group noted that some members of the HKIFA are interested in pursuing the suggestion of engaging small and medium sized brokerage firms as distributors of their funds, with a view to broadening the distribution network. To this end, they are prepared to provide training and back-end support to the interested brokers.

3.58 However, the Working Group learned from the HKIFA that there might be some disincentives for brokers to diversify into the funds business. First, distribution of funds requires an incentive structure different from that for trading of securities by brokers; second, the retail

business set up requires relatively costly investment; and third, selling retail funds requires a relatively different skill set and knowledge and this necessitates re-training of brokers.

3.59 As an initiative to engaging brokers as distributors of funds, the Working Group was pleased to note that the HKIFA will co-host a seminar on funds shortly with the HKSI for the stockbrokers, especially the small and medium sized brokers. The theme of the seminar will focus on the skills in marketing funds, how to select fund providers and fund types, and the role of funds in a portfolio. The seminar will tie in with the HKSI's series of financial planning workshops for stockbrokers and other market practitioners. The SFC also indicates interest to co-sponsor similar seminars with the HKIFA for the brokers.

3.60 The Working Group is also pleased to note that some fund management company members of the HKIFA are prepared to offer to brokers IT support and training on their dealing platform. This will include training on client risk profiling, marketing and operating procedures, compliance and risk management. The Working Group has encouraged the industry associations to start and maintain a dialogue with the HKIFA.

3.61 The Working Group has also invited the Airport Authority, the Hong Kong Mortgage Corporation, the Kowloon-Canton Railway Corporation and the MTR Corporation to consider engaging the small and medium sized brokers in their retail bonds programme to enlarge and diversify the investor base of their bond issue; and listing their retail bonds on the Stock Exchange of Hong Kong to facilitate secondary trading.

### **Continuous training**

3.62 The Working Group believes that continuous professional training for members of the brokerage industry is important in upgrading their skill sets to meet present-day market needs. The Working Group has exchanged views with the HKSI on training opportunities for the brokers to facilitate their branching out into financial asset planning business. The HKSI has assured the Working Group that it is committed to provide education and training and promoting the development of knowledge and skills for stockbrokers, skilled practitioners and new entrants. The Working Group followed up the industry's views with the HKSI and the latter's response are set out in the ensuing paragraphs.

***(a) Facilitating re-entry of intermediaries into the industry***

3.63 Some industry members told the Working Group that the cyclical nature of the stockbroking industry requires down-sizing in lean years. During this period, practitioners may be forced to leave the industry. However, when market conditions improve, the industry may require ex-practitioners to join the work force at short notice. The three-year recency test as part of the competence requirements of the SFC creates hurdles for the re-entrants as they need to sit for the licensing examinations afresh. This requirement may delay the re-entry process as it may take a few months for an individual to prepare and pass the examination.

3.64 In response to the Working Group, the HKSI proposed an enhanced training programme for those intermediaries who may have to leave the industry for a short period but may re-enter the market as the general market conditions improve. The HKSI proposed to the Working Group that the SFC may consider setting less stringent licensing requirements for re-entry seekers than for new entrants, for example more flexible CPT hours to be achieved by re-entry seekers. As a contribution to the market as a whole, the HKSI undertakes to (a) structure special package courses to meet the needs of the non-practitioner category; (b) offer discounts on CPT courses to non-practitioners; (c) assist in the maintenance and issuance of CPT records; and (d) if the market requires, maintain a register of non-practitioner CPT records for all HKSI courses and events.

3.65 The Working Group welcomed these initiatives of the HKSI, and put forward recommendation in the next chapter.

***(b) Training and re-training of brokers***

3.66 The Working Group was informed by the industry associations that the courses provided by the HKSI were recurrent with limited input of new courses that were designed in response to changing market situation and investors' demand. The Working Group reflected these views to the HKSI. In particular the Working Group shared the views that HKSI should place particular focus on the training needs arising from the diversifying market development, emergence of new products and increasing demand from investors.

3.67 The Working Group was pleased to note that the HKSI recognises the new dimension of training needs and is launching a new

programme entitled “Professional Certificate in Financial Services” and a comprehensive course on financial planning leading to a Diploma Certificate for the brokers. The Working Group believed that these new training opportunities will help those small and medium sized brokerage firms in diversifying their services for retail clients.

*(c) Promoting “portability” of qualifications attained by members of the HKSI*

3.68 The Working Group noted the HKSI’s proposal of promoting “portability” of qualifications attained by its members, and understood that the HKSI has been in close liaison with overseas jurisdictions. The Working Group supported the proposal and encouraged the HKSI to keep up its effort in expanding to more jurisdictions.

3.69 In response, the HKSI informed the Working Group that the current HKSI examination has been included in the list of recognised overseas qualifications of the United Kingdom Securities Institute and has been approved by the Education and Training Committee of the Investment Dealers Association of Canada. The HKSI would seek continuous recognition from these two overseas institutions in respect of the New Licensing Examination. The HKSI conducted a comprehensive jurisdiction study in mid 2002 to ensure that the syllabus of the new examinations was comparable to similar examinations such as the United Kingdom, United States, Australia, China, Malaysia and Singapore. The HKSI would continue to seek international recognition for its examinations to strengthen the position and the marketability of its members internationally. The Working Group commended these efforts made by the HKSI.



## CHAPTER 4 RECOMMENDATIONS

### INTRODUCTION

4.1 In this chapter, we will set out the recommendations of the Working Group, having regard to the views and suggestions from the industry, and input from relevant organisations, as deliberated in the previous chapter. These recommendations seek in the main to enhance transparency of fees and charges, promote image building and market awareness of brokerage firms, level the playing field between brokers and banks, rationalise HKEx fees for brokers, minimise compliance burden, upgrade market infrastructure, enable brokers to diversify their product range, and improve training opportunities for brokers.

### ENHANCING TRANSPARENCY OF FEES AND CHARGES

4.2 As highlighted in paragraphs 3.45 to 3.49 in the previous chapter, the Working Group supports any measures to increase the transparency of client fees and charges for securities trading services, as well as standardisation of broad categories of the more than 70 items of fees and charges in the market. This will be an effective deterrent against any anti-competitive pricing practice by members of the industry and help the smaller brokers explain to their clients as to how they should compare the fees amongst brokers and banks. The Working Group also supports that investor education should be reinforced so that investors will be equipped to understand the services offered and compare the charges imposed by the intermediaries for different services.

4.3 The Working Group acknowledges that the survey on securities service fees conducted by the Consumer Council in February 2003 is a good starting point in reflecting the market practice and a useful tool to educate the investing public. *The Working Group recommends the SFC and the HKMA to continue to monitor rigorously the disclosure by brokers and banks of the fees and charges imposed by them on their securities trading services.*

4.4 The Working Group is pleased to note that the Consumer Council will, as a consumer advocate, continue to provide information to consumers on the market for brokerage services, as far as its resources permit, to assist them in making efficient transaction decisions. It will do this by periodically collecting marketplace information on the level of competition that is taking place, and continuing to encourage investors to

shop around for the bank or brokerage firm which is trustworthy, reliable in meeting their own individual needs and requirements, and willing to offer competitive commissions.

4.5 The Working Group is also pleased to note that the SFC will form a working group with representatives from the stockbroking industry associations to classify the fees and charges on securities trading services into broad and standardised categories, with a view to facilitating investors' understanding and comparison. Along the same vein, the HKMA will, in consultation with banks, analyse the fees and charges imposed by banks on their securities trading services with a view to fitting them into these broad categories. ***The Working Group recommends that both the SFC and HKMA should accord priority to the brokerage fee categorisation exercise and urges the stockbroking industry to contribute their views actively to the SFC for early completion of this exercise.***

4.6 In relation to this categorisation exercise, ***the Working Group recommends the SFC to step up its publicity efforts to educate the investors to enable them to understand the services provided by intermediaries and compare the various fees and charges where necessary.*** The SFC should remind investors of their right to information on the breakdown of sub-total fees and charges under each category, as well as the applicable fees and charges in respect of their own specific transaction pattern. The SFC should also encourage intermediaries to adopt the broad categories in classifying their fees and charges, preferably with illustrative examples; and disclose their fees and charges (as well as the sub-total) under each category in the monthly account statements to their clients. The Working Group was pleased to note that the HKMA will take appropriate steps to assist in the process, including issuing relevant guidance/instructions to banks.

4.7 Brokers and banks will be free to classify their fees into the broad categories, and investors will have a common information platform for better understanding and comparison. Brokers will then be in a better position to compete in the market with each other, as investors will no longer be confused by the level and types of fees that they are required to pay for the brokerage services and therefore be able to make more informed choices.

## **IMAGE BUILDING AND MARKET AWARENESS**

4.8 To complement the above efforts in enhancing the transparency of fees and charges, ***the Working Group recommends the stockbroking industry associations to consider setting up an electronic information***

*directory for their members to promote their image and market awareness among clients.* Industry associations are free to design the content of their own directory to make it informative and user-friendly to investors. The Working Group has provided examples of such web-sites<sup>9</sup> for the reference of the industry associations.

4.9 In relation to that, the Working Group was pleased to note that the HKEx has undertaken to hyperlink its web-site to those of its participants. *The Working Group recommends that the HKEx should accord priority to this hyperlink exercise in order to provide a seamless information platform where investors and market participants alike will have free and unobstructed access to information on SEHK Participants.*

#### **LEVEL PLAYING FIELD –**

##### **(a) Enforcement of restrictions on “cold calls”**

4.10 The Working Group is pleased to note that the HKMA has accorded priority in enforcing the restrictions on unsolicited calls by banks as described in paragraphs 3.19 to 3.20. *In light of the industry’s concern, the Working Group recommends the HKMA to continue to ensure effective enforcement of its cold calling guidelines issued in January 2003 and to work closely with the SFC to ensure consistency in their regulatory approach towards banks and brokers.*

##### **(b) Regulatory fees for banks conducting securities business**

4.11 The SFO has laid a level playing field for regulated activities conducted by brokers and banks, for example, by requiring banks to be registered with the SFC for undertaking regulated activities and subjecting them to the same regulatory code of conduct and disciplinary procedures and sanctions. In respect of the regulatory fees paid by brokers and banks, *the Working Group recommends the HKMA to explore with the SFC the possibility of rationalising the relevant regulatory fees imposed on banks for conducting securities business, with a view to introducing a sliding scale of fees reflecting the size of the securities business of a bank.* The Working Group recognises that the regulators will need to engage the

---

<sup>9</sup> Examples of websites established by stockbroking industry associations in other financial markets include –

(i) In the United States: Securities Industry Association of the United States (<http://www.sia.com>); and  
(ii) In Taiwan: Chinese Securities Association of Taiwan (<http://www.csa.org.tw>).

banking industry in conducting such a rationalisation exercise and any fee changes in this regard will require amendments to the rules on fees payable to the SFC made under the SFO.

## **RATIONALISING HKEX FEES FOR BROKERS**

4.12 The Working Group is pleased to note that the HKEx has removed the following fees with effect from 1 April 2003 as set out in details in paragraph 3.25 –

- (a) registration of sales representatives (at \$300 per application);
- (b) approval of branch offices (at \$12,000 per application and monthly subscription of \$2,900 per branch);
- (c) appointment of branch office managers (at \$1,000 per application); and
- (d) change in the share capital structure of by SEHK Participants (at \$1,000 per application).

4.13 In addition to the above, the Working Group notes that the HKEx will remove the following fees with effect from 2 May 2003 -

- (a) inspection of Registers of Exchange Participants, Stock Exchange Trading Rights, Authorised Clerks, Registered Users, Responsible Officers and others and provision of copies of extracts from such Registers (at \$100 per inspection);
- (b) registration of an Authorised Clerk (at \$300 each);
- (c) registration of Options Officers and Options Representatives (at \$300 each);
- (d) registration of a Responsible Officer (at \$1,000 each);
- (e) application for change of control except change in directors (at \$10,000 per application); and
- (f) application for appointment of directors (at \$1,000 each).

4.14 *On the rationalisation of HKEx regulatory requirements and the associated fees for brokers, the Working Group endorses the positive moves taken by the HKEx to abolish a number of regulatory requirements and the associated 10 fee items on brokers, ranging from \$100 to \$12,000 per fee item, with effect from 1 April and 2 May 2003 respectively.* These fee items are duplicative in nature as a result of, first, the transfer of relevant regulatory functions for SEHK Participants from the HKEx to the SFC; and second, the new licensing regime introduced under the SFO.

4.15 In relation to this, *the Working Group recommends that the HKEx and the SFC should accord priority to the review of fees inherited by the HKEx from the pre-merger entities, with a view to rationalising and simplifying them for Exchange users.* In this regard, the Working Group notes that the HKEx has put forward a request to the SFC that the fee review should be conducted on a “revenue-neutral” basis.

## **MINIMISING COMPLIANCE BURDEN**

4.16 The Working Group anticipates that during the initial period in implementing of the SFO, there might be some teething problems in both compliance and enforcement, and brokers may need time to adjust and adapt to the licensing regime.

4.17 The Working Group notes that in this regard the SFC has organised over 60 seminars and workshops and briefed over 13,000 market participants on the new requirements under the SFO in the run-up to the commencement on 1 April 2003 (see paragraph 3.31).

4.18 In response to the industry’s concern, *the Working Group recommends that the SFC should endeavour to adopt a pro-compliance approach in facilitating brokers’ compliance with the new SFO and avoid any unnecessary regulatory burden for firms with good internal controls and good risk management and practice.* *The Working Group supports the flexible approach adopted by the SFC in calibrating regulatory action against brokers on minor, inadvertent or technical first-time breaches of new requirements under the SFO.* In general, *the Working Group recommends the SFC to engage the industry in streamlining regulatory requirements.*

4.19 *The Working Group also urges the stockbroking industry, while continue to focus on compliance, to maintain a dialogue with the SFC on any difficulties they experience in complying with the new requirements under the SFO and forward their suggestions for*

*improvement to the SFC.*

4.20 As mentioned in paragraph 3.65, *to facilitate re-entry of intermediaries into the industry, the Working Group recommends the SFC to consider alternative means to satisfy the licensing competence requirements for re-entry seekers. The Working Group also recommends the SFC and HKSI to work closely together in developing such means.*

4.21 Further to the efforts mentioned in paragraph 4.14 above, *the Working Group recommends the HKEx to consider possible areas for streamlining and rationalising the regulatory requirements in relation to SEHK Participants under the Rules of the Exchange.* This, and the other recommendations put forward in this section, will be taken forward under existing and new channels of communication established by the SFC and the HKEx with the industry.

## **UPGRADING MARKET INFRASTRUCTURE – ENHANCED IP ACCOUNTS**

4.22 As mentioned in paragraphs 3.50 to 3.52 above, the Working Group notes the industry's broad support for the proposed enhanced IP account model which will assist the smaller brokers to compete with larger players as their clients will no longer need to worry about the security of their assets or money. In relation to this, *the Working Group -*

- (a) recommends the SFC and the HKEx to accord priority to the development of a user-friendly and cost-effective IP Account model as this will help enhance the competitiveness of the small and medium sized brokers.* In this regard, the Working Group notes that the HKEx will need to carefully examine whether there is a business case for it to invest in the initiative and HKEx will explore with the SFC possible means of funding both the initial investment and the subsequent operations of the project;
- (b) encourages the industry associations to participate actively in the design and set up of the IP Account by offering their views to the SFC IP Account Task Force; and*
- (c) urges the industry associations to take their members through the proposed model to facilitate industry associations buy-in.*

4.23 To facilitate brokers' adoption of the enhanced IP Account, *the Working Group recommends the SFC to examine the possibility of lowering capital requirement for brokers who do not hold client assets and tiering capital requirements according to risk and nature of business.*

4.24 As referred to in paragraph 3.52 above, in order to discourage any anti-competitive pricing practice by banks on money transfers of investors to their IP accounts, which would undermine the sustainability of IP accounts and hence impact adversely on systemic risk and reduce choices for retail investors, it is considered appropriate to benchmark the relevant charges against similar electronic money transfers to third parties now being conducted by banks, taking into consideration possible IT upgrade investment required on the part of banks to effect money transfers to the enhanced IP accounts. *The Working Group recommends the HKMA to make every effort to persuade banks to adopt a fair and transparent pricing structure for arranging money transfers to the enhanced IP accounts and if necessary, to seek to provide the basis for such a structure through a code of conduct for the banking sector.*

## **NEW PRODUCTS**

4.25 To enable brokers to diversify their product range to include retail bonds and funds, *the Working Group supports the fostering of business partnership between the HKIFA and brokers, in particular small and medium sized brokers, and encourages collaboration between the HKIFA, the HKSI and other relevant groups in organising more training courses to enhance brokers' knowledge in new products.*

4.26 *The Working Group recommends the SFC and the HKEx to further facilitate straight through listing of the SFC authorised funds including, in particular, Exchange-Traded Funds and Real Estate Investment Trusts and bonds.*

## **IMPROVING TRAINING OPPORTUNITIES**

4.27 The Working Group notes that it is important for brokers to upgrade their knowledge and skill set in order to meet new demands from investors in the fast-changing market. The Working Group has touched base with the HKSI on the enhanced training opportunities for the industry and is pleased to note that the HKSI is proactive and supportive in this aspect. *The Working Group recommends the HKSI to continue to provide courses*

*widening the skill set of brokers to enable them to provide new services, such as financial planning, and to continue its efforts in taking forward its various initiatives, such as portability of qualifications.*

4.28 *The Working Group recommends the SFC to continue to play a supportive role in facilitating brokers meeting the CPT requirement such as providing speakers for CPT programmes organised by stockbroking industry associations.*

4.29 *The Working Group also recommends the HKEx to extend education seminars to stockbroking industry associations to increase the infiltration of product knowledge and investment/trading strategies to their members, and to the investing public.*

4.30 In promoting the SME Funding Schemes referred to in paragraph 3.53 above, *the Working Group urges the industry associations to disseminate to their members information on these schemes and forward their views, if any, to the relevant government departments on ways to further improve the operation of these funding schemes.*



## **CHAPTER 5     ACKNOWLEDGEMENT**

5.1           The Working Group would like to express its appreciation to the following stockbroking industry organisations for their suggestions and comments on ways to improve the business environment of the stockbroking industry –

Hong Kong Association of Online Brokers  
Hong Kong Securities and Futures Industry Staff Union  
Hong Kong Securities Professionals Association  
Hong Kong Stockbrokers Association  
Institute of Securities Dealers

5.2           The Working Group would also like to express its appreciation to the following organisations for their support for and contributions to the Working Group –

Consumer Council  
Hang Seng Index Services Limited  
Hong Kong Investment Funds Association  
Hong Kong Monetary Authority  
Hong Kong Securities Institute  
Trade and Industry Department

5.3           The Working Group is grateful to Ms Kinnie Wong, Mr George Tam and Mr Dominic Lo of the Financial Services and the Treasury Bureau who help to put this Report together, in conjunction with the Executive of the Securities and Futures Commission and the Hong Kong Exchanges and Clearing Limited.

**Membership of the Working Group on the  
Business Environment of the Stockbroking Industry**

The Working Group on the Business Environment of the Stockbroking Industry comprises the following core members –

- Miss AU King-chi – Deputy Secretary for Financial Services and the Treasury, Financial Services and the Treasury Bureau (Convenor)
- Mrs. Alexa LAM – Executive Director, Intermediaries and Investment Products Division, Securities and Futures Commission
- Mr. Lawrence FOK – Deputy Chief Operating Officer, Hong Kong Exchanges and Clearing Limited

Other representatives from the Financial Services and the Treasury Bureau, the Securities and Futures Commission and the Hong Kong Exchanges and Clearing Limited are co-opted into the Working Group for examining specific recommendations.

**Terms of reference of the Working Group on the  
Business Environment of the Stockbroking Industry**

The Working Group on the Business Environment of the Stockbroking Industry is set up to examine with the local stockbroking industry ways to enhance the competitiveness of the small and medium sized stock brokerage firms.

The Group will aim to submit a report of recommendations to the Secretary for Financial Services and the Treasury in April 2003.

## Chronology of Events

<i>Event</i>	<i>Date</i>
The Secretary for Financial Services and the Treasury announced the establishment of a tripartite forum on stockbroking industry, which was subsequently named as the “Working Group on the Business Environment of the Stockbroking Industry” (“the Working Group”).	15 January 2003
The Working Group invited the five stockbroking industry associations, namely the Hong Kong Stockbrokers Association, the Institute of Securities Dealers, the Hong Kong Securities and Futures Industry Staff Union, the Hong Kong Association of Online Brokers and the Hong Kong Securities Professionals Association to the first round of meetings.	21 January 2003
First round of meetings between the Working Group and representatives of the industry associations.	Late January 2003
The Working Group exchanged views with representatives of the Hong Kong Investment Funds Association, the Hang Seng Index Services Limited and the Hong Kong Securities Institute.	Late January 2003
The Working Group invited the five stockbroking industry associations to provide written proposals on improving the business environment of the stockbroking industry.	11 February 2003
The Working Group received written proposals from the industry associations and the Hon Henry Wu.	From mid February to early April 2003
The Working Group wrote to the Hong Kong Securities Institute on proposals to enhance training for the stockbroking industry to meet market development need in terms of new services and products, promoting “portability” of qualification attained by members of the Institute, and facilitating re-entry by intermediaries into the industry.	24 February 2003
The Working Group wrote to the Hang Seng Index Services Limited (HSISL) inviting the HSISL to take into consideration, in reviewing the composition of the HSI, the need to facilitate development of derivative products that meet local market needs, and to consider whether the criterion of selecting constituent stock(s) for the HSI could be kept under regular review.	24 February 2003
The Working Group wrote to the Hong Kong Investment Funds Associations on the suggestion of engaging small and medium sized brokers in marketing retail funds.	24 February 2003

<i>Event</i>	<i>Date</i>
The Working Group invited the five stockbroking industry associations to the second round of meetings.	6 March 2003
The Working Group wrote to the five stockbroking industry associations to provide detailed information on three Small and Medium Enterprise Funding Schemes managed by the Trade and Industry Department.	11 March 2003
The Working Group conducted the second round of meetings with representatives of the industry associations.	12-25 March 2003
The Working Group wrote to the Airport Authority, the Hong Kong Mortgage Corporation Limited, the Kowloon-Canton Railway Corporation, and the Mass Transit Railway Corporation on the industry's proposals of engaging small and medium sized brokers in the distribution of their retail bond issues and listing of their retail bonds on the HKEx to facilitate secondary trading.	21 March 2003
The Working Group wrote to five stockbroking industry associations to recapitulate various initiatives on improving the business environment of the stockbroking industry discussed with them at meetings; and appealing to the associations for support and assistance in engaging their members on these initiatives.	27 March 2003

**Summary of written submissions to the Working Group<sup>1</sup>**

<i>Major comments</i>	<i>Gist of Working Group Response<sup>2</sup></i>
<b>(1) About commission rate</b>	
<p><b>(a) Retention of minimum commission rate</b></p> <ul style="list-style-type: none"> <li>The minimum commission rate of 0.25% should not be abolished until a proper study has been conducted and a plan has been formulated with both short and long term measures to help the industry.</li> </ul> <p><b>(b) Two-tier system</b></p> <ul style="list-style-type: none"> <li>The authority should consider adopting the tier system on commission rate with the specific invoice amount set at \$ 1 million.</li> </ul>	<ul style="list-style-type: none"> <li>Expiry of minimum commission rate rule leads to liberalisation of brokerage commission that allows brokers greater flexibility in structuring their pricing strategy, creates a more level playing fields for brokers competing freely on commissions with non-SEHK Participants and promotes a free market which is in the best interest of the public.</li> <li>In a survey on securities trading commission rate conducted by the Consumer Council with the result released in February 2003, it is revealed that the minimum commission rate could be negotiable or circumvented through non-SEHK Participants who are not bound by the minimum commission rule.</li> <li>The Working Group also notes the Consumer Council's position that it does not support a system that sets an industry wide rule fixing brokerage commission, either on a tiered basis or otherwise.</li> <li>During February 2002 to March 2003, over 99% of the value of matched deals was below \$1 million. The effect of a two-tier system at \$ 1 million would be the same as retention of the minimum commission rate.</li> </ul> <p>[See paras. 3.5 - 3.7, 3.12, and 3.14 - 3.18]</p>

**(c) Concern about cut-throat competition**

- Investors should be reminded that there is a risk in entrusting their assets to brokers who reduce their fees indiscriminately as a result of cut-throat competition.
- The Government should consider taking measures to prevent cut-throat competition on commission rates for securities trading.
- The SFC had issued a circular in March 2003 to remind investors to exercise caution in accepting any promotional offers.
- The regulatory authorities, the SFC and HKMA undertake to monitor the situation closely and take appropriate action as necessary.
- The SFC will identify whether there is any intermediary engaging in pricing or other forms of competition which exposes its clients to greater risk or diminishes its ability to comply with the FRRs.
- The Working Group believes that promoting price transparency and ensuring free market entry will be effective in rendering any predatory pricing strategy unattractive.
- In the Consumer Council February 2003 survey, it is reported that the cost of securities transactions conducted through banks is higher than that of brokerage firms.
- The Working Group recommends the SFC and HKMA to consider further enhancing fee transparency by grouping more than 70 fee items charged by banks and brokers into broad standard categories for easy comparison by investors.

[See paras. 3.8 - 3.13, and 4.2]

**(2) Promoting a level-playing field with banks**

***(a) Related to regulatory requirement***

- |  |   |
|--|---|
| <ul style="list-style-type: none"> <li>• Brokers are facing unfair competition from banks, and brokers and banks are subject to different regulatory requirements on securities trading. The Government should consider taking measures to prevent monopoly of securities trading by large broker firms and banks.</li> <li>• Other financial institutions, including banks, which conduct securities trading should be subject to the same regulatory requirements and supervision as the stockbrokers.</li> <li>• “Cold calls” restriction should be applied fairly to all intermediaries.</li> <li>• The Cold Call rules should be clearly interpreted such that recommendations on a variety of securities investment products, on where a person is at liberty to make his own choice should not be prohibited in order to allow brokers more freedom in promoting new products.</li> <li>• Stockbrokers are required under the Code of Conduct to include a description of any remuneration and other fees and charges in Client Agreements. All financial institutions carrying on stockbroking business should be subject to same requirement.</li> <li>• Stockbroking firms are in a disadvantageous position when compared with banks since stockbroking firms can only have one category of clients, i.e. securities clients, whereas banks have a large client base straddling banking, securities, insurance and other sectors.</li> <li>• Banks, securities and insurance used to be distinct sectors but now there are no more boundaries and financial conglomerates are straddling all sectors. This situation puts the regulator in a most disadvantageous position if it is to assess the overall market risk.</li> </ul> | <ul style="list-style-type: none"> <li>• The Working Group notes that the SFO has laid a level playing field for regulated activities conducted by banks and brokers, e.g. in requiring banks to be registered with the SFC for undertaking regulated activities and subjecting them to essentially the same regulatory code of conduct and disciplinary procedures and sanctions.</li> <li>• The Working Group recommends the industry associations to set up an electronic information directory for their members to promote their image and market awareness among clients.</li> <li>• HKMA has issued a circular in January 2003 to provide guidance to banks on the restrictions on “cold calls” and undertakes to enforce the guidance. The Working Group recommends the HKMA and the SFC to continue to work closely together to ensure effective enforcement of cold calling restrictions.</li> <li>• Regulators maintain close liaison and cooperation amongst them. The Administration coordinates their risk management efforts through the Financial Stability Committee.</li> </ul> <p>[See paras. 3.19, 4.8, and 4.10]</p> |
|--|---|



*(b) Related to regulatory fees*

- Banks pay a single registration fee to HKMA which cover all branch offices whereas brokers pay licence fees for the head office and another fee for each branch office.
- Bank staff dealing with securities do not have to pay fees whereas staff of brokers have to pay annual fees as licensed representatives.
- The Working Group notes that the discrepancy stems from the difference in the core business conducted by banks and brokers and the way regulatory fees are structured.
- The Working Group recommends the HKMA to explore with the SFC the possibility of rationalising the relevant regulatory fees imposed on banks for conducting securities business, with a view to introducing a sliding scale of fees reflecting the size of the securities business of a bank. The Working Group recognises that the regulators will need to engage the banking industry in conducting such a rationalisation exercise and any fees changes in this regard will require amendments to the rules on fees made under the SFO.

[ See paras. 3.21 and 4.11]

**(3) Streamlining regulatory requirements and facilitating compliance**

**(a) Regulatory requirements**

**General**

- There is concern on the outdated/excessive regulatory requirements set by the HKEx.
- Stockbrokers are subject to frequent operational / system modifications consequent to regulatory changes.
- Brokers are facing continuous and sudden changes in regulatory requirements and high compliance costs.
- Those less pressing regulatory requirements that result in an increase in the compliance cost of broker firms should be reviewed.

**Financial Resources Rule (FRR)**

- The requirement of 35% : 65% proprietary loan ratio under the FRR is an “overkill”.
- The recent change in the FRR effected on 1 Oct 2002 on illiquid collateral haircut and on firm borrowing margin loan ratio trigger would have adverse impact on margin loan financing and thereby affect the market turnover and the securities business as a whole.
- FRR computation on settlement day basis, instead of trade day basis, should be allowed to lower the demand on a broker’s liquid capital requirement.

- The Working Group recommends the SFC and HKEx to continue to engage with the industry in streamlining regulatory requirements and facilitating regulatory compliance.
- The Working Group notes that under the SFO, certain regulatory requirements have already been streamlined. It believes that further streamlining would be beneficial to the development of the industry. This should however not be at the expense of investors’ interest.
- The Working Group notes that SFC has formed a working group to review the financial regulation of intermediaries. One of its tasks is to consider possible areas for rule modification and exemptions in the FRR.

<p><b>Listing</b></p> <ul style="list-style-type: none"> <li>• The delisting mechanism should be reviewed with a view to promoting corporate governance by introducing rewards and penalties.</li> <li>• Impact of the proposed amendments to the Listing Rules on market turnover should be carefully assessed.</li> </ul> <p><b>E-placement</b></p> <ul style="list-style-type: none"> <li>• The restrictions on e-placement of securities should be continuously reviewed in order to meet the ever changing market as a result of advancement of information technology.</li> </ul> <p><b>Overlap</b></p> <ul style="list-style-type: none"> <li>• There is overlap in seeking both the SFC and HKEx’s approval for broker’s licence application as well as approval of substantial shareholders.</li> </ul> <p><b>Compliance burden</b></p> <ul style="list-style-type: none"> <li>• There is concern on the lack of control over the listed companies on their requests for information from brokers under section 18 of the Securities (Disclosure of Interests) Ordinance. The Financial Services and the Treasury Bureau and the SFC should issue guidelines to brokers in relation to requests from listed companies to investigate ownership of their shares.</li> </ul>	<ul style="list-style-type: none"> <li>• The Working Group has referred the comments to the SFC and HKEx for their consideration.</li> <li>• The Working Group notes that the regulation of offer of investments is under review by the SFC. The Government will relax relevant requirements by phases. Phase II being amendments to the Companies Ordinance to be introduced to LegCo in Q2/2003 that includes facilitation of e-placement of securities.</li> <li>• The Working Group urges the HKEx to consider possible areas for streamlining and rationalising the regulatory requirements in relation to Exchange Participants under the SEHK Rules.</li> <li>• The Working Group notes that the issues have been fully discussed at the LegCo Bills Committee scrutinising the Securities and Futures Bill in 2001. Members of the Bills Committee did not support a change to the powers of the listed companies. Instead, to better protect the brokers who would be subject to such requests from listed companies, section 334 of the SFO has been amended to provide for a defence if a person has a “reasonable excuse” for failure to comply with the request. The Working Group also notes that such self-enforcement arrangement has been in force in Hong Kong for over 10 years and operating without any problem.</li> </ul>
---	--

**(b) Regulators-related issues**

- Regulators should avoid excessive and unwarranted investigations involving interviews and examinations of brokers' clients that would drive genuine investors away.
- Regulators should not be prosecution or penalty oriented.
- Working level of the staff of the SFC and the HKEx should possess ample market experience.

**(c) HKEx's fees**

- The SFC and HKEx should together review all HKEx's fees.
- The fee for each "data monitor" at \$200 is excessive and inhibits brokers in installing more facilities.
- On a user-pay basis, the costs of the HKEx should be borne by investors who trade in shares. Therefore, the HKEx should fund its operating costs, research and development, and investments in technology, etc. from the income of the HKEx, i.e. the trading levy.
- There should be a mechanism for the brokers to pass on the HKEx levied costs to investors, e.g. the \$0.5 transaction fee per matched transaction.

As to the need for guidelines to brokers in relation to the requests from listed companies, the Working Group has referred suggestion to the SFC for consideration.

- The SFC should endeavour to adopt a pro-compliance approach to facilitate brokers' compliance with the new regulatory requirements of the SFO and avoid any unnecessary regulatory burden for firms with good internal controls and good risk management and practice.
- The SFC and HKEx notes the concern.
- The HKEx has reviewed relevant fees and has undertaken to abolish the mechanism of certain obsolete regulatory requirements and the associated fee items in two phases. The first phase has taken effect from 1 April 2003 and the second phase from 2 May 2003.
- The Working Group recommends that the SFC and HKEx should accord priority to the review of fees inherited by the HKEx from the pre-merger entities, with a view to rationalising and simplifying them for Exchange users. The Working Group notes that the HKEx has put forward a request to the SFC that the fee review should be conducted on a "revenue-neutral" basis.

<p><b>(d) Stamp Duty</b></p> <ul style="list-style-type: none"> <li>Stamp duty for securities transaction is outdated when compared with the US and UK markets and should be abolished.</li> </ul>	<ul style="list-style-type: none"> <li>The Working Group notes that the level of stamp duty on securities transactions has been reduced for over 60% from 0.6% in 1990 to the current level of 0.2%. The Working Group notes that the Government will keep the level of stamp duty on securities transactions under review.</li> </ul> <p>[See paras. 3.25-3.26, 3.32, 4.15, 4.18 and 4.21]</p>
<p><b>(4) Upgrading market infrastructure to enhance brokers' competitiveness</b></p>	
<p><b>(a) Investor Participant (IP) Account and Scripless Proposal</b></p> <ul style="list-style-type: none"> <li>The Scripless and the IP Accounts service should be implemented as soon as possible.</li> <li>Investment by the HKEx such as the IP Accounts should be funded from HKEx's internal resources or by other means available to listed companies, but not from the Participants.</li> <li>The IP Accounts service will ensure better investor protection and should be dealt with as a first priority.</li> <li>The capital requirements for brokers are excessive. The IP Account service would alleviate the problem.</li> <li>The IP Accounts service should be improved and made more user-friendly together with other market infrastructure upgrades such as dematerialisation, straight-through-processing, etc for costs and efficiency purposes.</li> </ul>	<ul style="list-style-type: none"> <li>The Working Group urges representatives of the stockbroking industry associations to secure support from its members for the proposed IP Account and Scripless project, and encourages the industry associations to continue to offer their views to the SFC IP Account Task Force and Scripless Implementation Working Group.</li> <li>The Working Group urges the SFC and the HKEx to accord priority to the development and implementation of a user-friendly and cost-effective IP Account model as this will help improve the competitiveness of the small and medium brokers.</li> <li>The Working Group recommends the SFC to examine the possibility of lowering capital requirement for brokers who do not handle client assets and tiering capital requirements in order to promote early adoption of the proposed IP Account.</li> </ul>

<ul style="list-style-type: none"> <li>• The regulators should aim at lowering the operating cost of broker firms when designing the market infrastructure.</li> <li>• The network development and operating costs are high and should be lowered.</li> <li>• In using electronic platform for securities trading, issues on systematic risks such as electronic failures and fraud, etc should be dealt with.</li> </ul>	<p>[See para. 3.50-3.51, 4.22 and 4.23]</p>
<p><b>(5) Market Development</b></p>	
<p><b>(a) Promotion of new products</b></p> <ul style="list-style-type: none"> <li>• Government assets offering to the investing public, in particular via the securities market, should allow all intermediaries to participate instead of a selected few by the Government. With a clear and reasonable set of criteria, intermediaries can then decide if they would participate in such offerings.</li> <li>• The funds and bonds are not listed in the Exchange and there is no secondary market. Industry participation in the funds and bonds market is important to improve the liquidity.</li> <li>• Variety of new products should be enriched and the HKEx should promote more new products as a means of diversification of business.</li> <li>• The constituent stocks of the Hang Seng Family of Index should be reviewed as there is no “H” shares among the 33 stocks.</li> <li>• Derivatives should not be introduced prematurely.</li> <li>• The entry barrier to new products for the brokers is the lack of idle funds for such products.</li> </ul>	<ul style="list-style-type: none"> <li>• The Working Group notes the wish of the industry and the investors for new investment products; and acknowledges that diversification of products will help boost market liquidity. In relation to this, the Working Group has invited the Airport Authority, the Hong Kong Mortgage Corporation, the Kowloon-Canton Railway Corporation and the MTR Corporation to consider engaging the small and medium sized brokers in their retail bonds programmes to enlarge and diversify the investor base of their bond issue and listing their retail bonds on the Stock Exchange of Hong Kong to facilitate secondary trading. The Working Group has also invited the Treasury Branch to consider the industry’s suggestions. They responded that they would take the suggestions into account at the time when considering the detailed structure of specific Government asset offerings in future. At present, there is no plan or intention to issue any retail bond to finance Government’s operations.</li> <li>• The Working Group recommends the SFC and HKEx to further facilitate straight through listing of the SFC authorized funds</li> </ul>

<ul style="list-style-type: none"> <li>• Brokers are required to undergo training and registration before they can sell the new products to clients to supplement their income and this should only be treated as a long term solution to improve the business environment of stockbrokers.</li> </ul> <p><b>(b) New Market</b></p> <ul style="list-style-type: none"> <li>• Government should assist brokers in tapping the China market in Hong Kong such as facilitating Mainland investors to invest in Hong Kong listed stocks.</li> <li>• Government should assess the economic trend of Hong Kong and assist in promoting the Hong Kong stock market, e.g. by inviting large international firms to increase their investment in Hong Kong stock market.</li> <li>• Regulators should join with market players and industry associations to promote online trading in order to increase market turnover.</li> </ul>	<p>including, in particular, Exchange-Traded Funds and Real Estate Investment Trusts and bonds.</p> <ul style="list-style-type: none"> <li>• The Working Group has invited the Hang Seng Index Services Limited (HSISL) to comment on the industry’s suggestion to review the constituent stocks of the Hang Seng Family of Index. HSISL advised that they have been keeping track of market developments closely with a view to maintaining Hang Seng Index always as a faithful and consistent market benchmark. HSISL is aware of the growing diversity of investors and their diverse requirements in market trackers and have developed a diverse family of indices to satisfy the demands; and shall further add new member indices to the family as the market demands.</li> <li>• The Working Group notes the SFC/HKEx/FSTB joint efforts in the Mainland in promoting Hong Kong as the premier capital formation centre for Mainland enterprises and monitoring the development with relevant authorities to assist brokers in tapping the Mainland market.</li> <li>• The Working Group notes that Government spares no efforts in promoting the Hong Kong stock market overseas.</li> <li>• The Working Group has referred the request to the SFC and HKEx for their consideration.</li> </ul> <p>[See paras. 3.40-3.43, 3.61, 4.26]</p>
--	---

<p><b>(6) Enhancing continuous training opportunities for the industry</b></p>	
<p><b>(a) Training standard</b></p> <ul style="list-style-type: none"> <li>• The Continuous Professional Training (CPT) programme helps raising the standard of market practitioners.</li> <li>• There is concern on the viability of training courses because of the costs involved in comparison with the economic return.</li> <li>• There may not be any more new training courses offered to account executives after a number of years.</li> </ul> <p><b>(b) Training cost</b></p> <ul style="list-style-type: none"> <li>• There should be a cap on the CPT training hours per licensed person per annum, at say 15 hours, as excessive training will result in increased cost but not a guarantee to improved quality.</li> <li>• There is a lack of cheap and convenient training courses.</li> <li>• Online training should be provided by the SFC or the HKSI at an attendance fee of no more than HK\$20 per course.</li> <li>• To extend the Small and Medium Enterprise Funding Schemes administered by the Trade and Industry Department from brokerage firms to non-profit making industry associations to organise training courses for their members.</li> </ul>	<ul style="list-style-type: none"> <li>• The Working Group recommends the HKEx to extend education seminars to stockbroking industry organisations to increase the infiltration of product knowledge and investment/ trading strategies to their members, and to the investing public.</li> <li>• The Working Group urges the industry associations to urge their members to make use of the Trade and Industry Department SME Funding Schemes to attend training courses.</li> <li>• The Working Group notes that training courses provided by the SFC are free of charge. Where possible, the SFC will provide speakers to assist the stockbroking industry associations in organising training courses for their members at cost. The Hong Kong Securities Institute (HKSI) has also introduced courses with reduced fees for members of the stockbroking industry.</li> <li>• The Working Group notes that it may not be appropriate for the SFC to develop online training as the SFC is not a training provider. The SFC has undertaken to invite HKSI to consider stockbroking industry's request for providing online training at a reasonable cost.</li> <li>• The Working Group was informed by the Trade and Industry</li> </ul>



	<p>Department that it is not feasible for the industry associations to apply for the funding schemes to organise their training courses. Members of these industry associations, however, can apply under the relevant scheme for funding to attend training courses organised by their respective industry associations.</p> <p>[See paras. 3.53, 4.29 and 4.30]</p>
<p><b>(7) Others</b></p>	
<ul style="list-style-type: none"> <li>• The SFC should hold regular press conferences to disseminate information regarding the current status and direction of the industry.</li> <li>• The Working Group on the Business Environment of the Stockbroking Industry should make recommendations which are suitable for the local economy.</li> <li>• The Government should educate investors and build up confidence in the market.</li> </ul>	<ul style="list-style-type: none"> <li>• The Working Group and the SFC notes the concern of the industry.</li> <li>• The Working Group notes that investors education is an on-going priority programme of the market regulators, in collaboration with the media, Consumer Council, etc.</li> </ul>

Footnotes :

<sup>1</sup> Based on written submissions/suggestions from the following parties to the Working Group –

- (a) Hong Kong Association of Online Brokers dated 28 February 2003 and 31 March 2003.
- (b) Hong Kong Securities and Futures Industry Staff Union dated 26 February 2003 and 18 March 2003.
- (c) Hong Kong Securities Professional Association in February 2003.
- (d) Hong Kong Stockbrokers Association in March 2003.
- (e) Institute of Securities Dealers dated 14 February 2003.
- (f) Hon. Henry K C Wu dated 26 February 2003, 26 March 2003 and 2 April 2003.

These submissions/suggestions have been uploaded to the web-site of the Financial Services Branch of the Financial Services and the Treasury Bureau [<http://www.info.gov.hk/fstb/fsb/>].

<sup>2</sup> Reference in bracket refers to those paragraphs of the Working Group report which are relevant to the comments.

**Licence Fees charged by Hong Kong Monetary Authority and Securities and Futures Commission on Registered Institutions and Licensed Corporations for Securities Business**

Fee Item	Registered Institutions i.e. Licensed Banks	Licensed Corporations i.e. Brokerage Firms
(A) Annual Fee	(1) \$480,000 per registered institution per annum (bank licence) (2) \$22,400 per local branch per annum (branch licence) (3) \$35,000 per regulated activity per annum	(1) For licensed corporation: \$4,740 per regulated activity per annum (2) For responsible officer: \$4,740 per regulated activity per annum (3) For licensed representative: \$1,790 per regulated activity per annum
(B) Statutory Capital Requirement	(1) \$300 million paid-up capital for a licensed bank in Hong Kong (2) maintain a capital adequacy ratio of 8% and a liquidity ratio of 25% as minimum requirement	(1) \$5 million paid-up capital and a liquid capital of \$3 million for a licensed corporation engaging in securities dealing

It is difficult to compare directly the licence fees charged on registered institutions and licensed corporations due to the fundamental difference in their core businesses and applicable regulatory requirements. The following comparison is for illustration only.

Licensed Bank	Brokerage Firm
<ul style="list-style-type: none"> <li>• each bank has on average 32 branches</li> <li>• registration fee of \$35,000 per annum</li> </ul> <p style="text-align: center;"><b>\$38,500 banking licence fee plus registration fee per branch per annum</b>  <math>(\\$480,000 + 32 \times \\$22,400 + \\$35,000) / 32</math></p>	<ul style="list-style-type: none"> <li>• average number of representatives (including responsible officers) of a brokerage firm = 17</li> <li>• 2 responsible officers and 15 representatives</li> </ul> <p style="text-align: center;"><b>\$41,000 per firm per annum</b>  <math>(15 \times \\$1,790 + 3 \times 4,740)</math></p>

Sources : SFC and HKMA

## Summary of SME Funding Schemes

<i>SME Funding Schemes</i> <sup>1</sup>	<b><u>SME Loan Guarantee Scheme</u></b>	<b><u>SME Training Fund</u></b>	<b><u>SME Export Marketing Fund</u></b>
<i>Objective</i>	To assist SMEs in obtaining banking facilities for acquiring business installations and equipment and for meeting working capital needs.	To encourage SMEs to provide training relevant to their business operations to their employers and employees, with a view to enhancing their human capital.	To help SMEs expand overseas markets through funding them to participate in export promotion activities.
<i>Type of support</i>	<b>Government-guaranteed loan</b> from Participating Lending Institutions (49 lending institutions have participated as at 11 March 2003)	<b>Government grant</b>	<b>Government grant</b>
<i>Government commitment (Total amount of guarantee/grant issued as of end Feb 2003)</i>	\$ 6.6 billion (\$1.2 billion)	\$ 400 million (\$ 26 million)	\$ 300 million (\$ 37 million)
<i>Eligibility</i>	<ul style="list-style-type: none"> <li>□ SMEs that are registered in Hong Kong under the Business Registration Ordinance (Chapter 310) (For non-manufacturing sector, SMEs mean businesses which employ fewer than 50 persons (both full time and part-time) in Hong Kong.)</li> </ul>	<ul style="list-style-type: none"> <li>□ SMEs that are registered in Hong Kong under the Business Registration Ordinance (Chapter 310) (For non-manufacturing sector, SMEs mean businesses which employ fewer than 50 persons (both full time and part-time) in Hong Kong.)</li> </ul>	<ul style="list-style-type: none"> <li>□ SMEs that are registered in Hong Kong under the Business Registration Ordinance (Chapter 310) (For non-manufacturing sector, SMEs mean businesses which employ fewer than 50 persons (both full time and part-time) in Hong Kong.)</li> </ul>

<sup>1</sup> The establishment of the SME funding schemes was approved on 9 November 2001 and subsequent changes to the schemes on 24 January 2003 by the LegCo Finance Committee. The schemes are administered by the Trade and Industry Department, with the Director-General of Trade and Industry as the Vote Controller.

## Summary of SME Funding Schemes

	<ul style="list-style-type: none"> <li>□ Lending institutions and/or their associates are not eligible to apply.</li> </ul>	<ul style="list-style-type: none"> <li>□ Employers/employees attending the training courses have to be holders of HKID card.</li> </ul>	
<p><i>Scope of Guarantee /Use of grant</i></p>	<p>A. Business Installations and Equipment Loan Guarantee</p> <p>For acquiring business installations and equipment, which may include:</p> <ul style="list-style-type: none"> <li>□ Machinery</li> <li>□ Tools</li> <li>□ Computer software and hardware</li> <li>□ Communication system</li> <li>□ Office equipment</li> <li>□ Transport facilities</li> <li>□ Furniture</li> <li>□ Fixture (e.g. air-conditioning system, built-in cabinets and lighting system)</li> </ul> <p>B. Associated Working Capital Loan Guarantee</p> <p>For meeting additional operational expenses arising from or in relation to the business installations and equipment acquired or to be acquired under the Scheme</p>	<p>For training directly relevant to the applicant's business operation, which include:</p> <ul style="list-style-type: none"> <li>□ Training courses provided by professional local or overseas training organisations (including distance learning and online learning); and</li> <li>□ Training courses commissioned by the applicant SME to suit its particular needs and conducted by experienced and professional local or overseas training organisations or instructors.</li> </ul>	<ul style="list-style-type: none"> <li>□ For participation in export promotion activities, include local and overseas trade fairs and exhibitions, and study missions, organised by experienced and reputable organisations. The activities have to be directly relevant to the business of the applicants.</li> <li>□ Expenditures such as participation fees charged by the organiser, travelling expenses, and hotel accommodation expenses can be funded.</li> </ul>

## Summary of SME Funding Schemes

	<p>C. Accounts Receivable Loan Guarantee</p> <p>For meeting short-term liquidity arising from extending credits to buyers</p>		
<p><i>Maximum amount (per business registration)</i></p>	<p><b>Total \$4 million</b>, or 50% of the approved loan, whichever is less, with the following breakdown:</p> <ul style="list-style-type: none"> <li>□ Business installations and equipment loan guarantee - \$2 million (maximum guarantee period: 5 years)</li> <li>□ Associated working capital loan guarantee - \$1 million (maximum guarantee period: 2 years)</li> </ul> <p>Note: The guarantee amount shall not exceed 50% of the guarantee amount for the co-related business installations and equipment loan.</p> <ul style="list-style-type: none"> <li>□ Accounts receivable loan guarantee - \$1 million (maximum guarantee period: 2 years)</li> </ul>	<p><b>Total \$30,000</b>, or 50% of training expenses, whichever is less, with the following breakdown:</p> <ul style="list-style-type: none"> <li>□ Employers - \$ 10,000</li> <li>□ Employees - \$ 20,000</li> </ul>	<p><b>Total \$40,000</b>, subject to a limit of \$20,000 per activity, or 50% of total approved expenditures for that activity, whichever is less.</p>
<p><i>How to apply</i></p>	<p>Applications must be lodged</p>	<p>Apply not earlier than 3 months</p>	<p>Apply 30 days before the activity</p>

## Summary of SME Funding Schemes

	through Participating Lending Institutions	from the commencement date of the training course and not later than 30 days after the completion date of the training course.	commenced.
<i>TID performance pledge</i>	3 working days for processing application for guarantee	12 working days for processing application for grant; and 30 working days for processing application for reimbursement of grant.	7 working days for processing application for grant; and 30 working days for processing application for reimbursement of grant.
<i>Approved applications made by SME financial services firms<sup>2</sup> (as of end Feb 2003)</i>	Statistics not available	About 560	About 80
<i>Enquiries</i>	Trade and Industry Department 6/F, Trade and Industry Department Tower, 700 Nathan Road, Kowloon. Tel: 2398 5125 / 2398 5129 Website: <a href="http://www.smefund.tid.gov.hk">www.smefund.tid.gov.hk</a>	Trade and Industry Department 6/F, Trade and Industry Department Tower, 700 Nathan Road, Kowloon. Tel: 2398 5125 / 2398 5126 Website: <a href="http://www.smefund.tid.gov.hk">www.smefund.tid.gov.hk</a>	Trade and Industry Department 6/F, Trade and Industry Department Tower, 700 Nathan Road, Kowloon. Tel: 2398 5125 / 2398 5127 Website: <a href="http://www.smefund.tid.gov.hk">www.smefund.tid.gov.hk</a>

<sup>2</sup> Including banks, stockbroking firms and insurance companies.