立法會
Legislative Council

LC Paper No. CB(1)1055/2023

Ref. : CB1/PL/FA

Report of the Panel on Financial Affairs
for submission to the Legislative Council

Purpose

This report gives an account of the work of the Panel on Financial Affairs ("the Panel") during the 2023 legislative session. It will be tabled at the meeting of the Legislative Council ("LegCo") of 6 December 2023 in accordance with Rule 77(14) of the Rules of Procedure of LegCo.

The Panel

2. The Panel was formed by a resolution passed by LegCo on 8 July 1998 and as amended on 20 December 2000, 9 October 2002, 11 July 2007, 2 July 2008 and 26 October 2022 for the purpose of monitoring and examining government policies and issues of public concern relating to financial and finance matters. The terms of reference of the Panel are set out in **Appendix 1**.

3. For the 2023 session, the Panel comprised 20 members, with Hon Jeffrey LAM Kin-fung and Hon Robert LEE Wai-wang elected as Chairman and Deputy Chairman respectively. The membership list of the Panel is in **Appendix 2**.

Major work

Macro economy

Hong Kong's economic performance

4. During the 2023 session, the Panel continued to provide a forum for LegCo Members to exchange views with the Financial Secretary ("FS") on matters relating to macro-economic issues. At the meeting on 5 June 2023, the Panel noted that while the external economic environment stayed weak in the first quarter of 2023, the Hong Kong economy improved visibly during the period, led by the strong recovery of inbound tourism and domestic demand. Real Gross

Domestic Product ("GDP") resumed growth, expanding by 2.7% year-on-year. The labour market continued to improve along with the recovery of economic activities, with both the unemployment and underemployment rates declining. On the asset markets, the stock market retreated due to external factors. In the property market, residential property prices rebounded in the first four months of the year. Looking forward, inbound tourism and domestic consumption would remain the major drivers of economic growth this year. If the external environment did not turn out to be too sluggish, Hong Kong's economic growth for the year as a whole would likely be near the higher end of the forecast range of 3.5% to 5.5% as estimated by the Government earlier. The forecast rates of underlying and headline consumer price inflation for 2023 were maintained at 2.5% and 2.9% respectively.

Overall Government Expenditure and Revenue

5. Members pointed out that although local economic activities were returning to normalcy, the market remained worried about the possible impact on the economy brought about by the sharp interest rate hikes since last year, and the Government was still expecting a budget deficit in 2023-2024 due to the reduction in major government revenue, including land sales, stamp duty on stock transfers and profits tax. Members enquired what measures the Administration would put in place to expedite the pace of economic recovery in Hong Kong, and whether it would consider modelling on the practice of the business sector of streamlining structure and manpower during the epidemic and suspend the creation of new civil service posts.

6. FS advised that the Government had maintained the policy of zero growth in the civil service establishment in recent years in order to ensure the sustainability of public finances. Where justified, individual bureaux/ departments might still increase their establishment to meet the actual operational needs of the Government. That said, the overall civil service establishment could still maintain zero growth by deleting vacancies in bureaux/departments to offset the creation of new posts. The total government expenditure for 2022-2023 had increased significantly, with its ratio to GDP rising to 28% mainly due to the huge expenditure involved in the implementation of massive counter-cyclical measures and anti-epidemic work. As most of the expenditure on anti-epidemic work would be cut following the subsiding of the epidemic, the overall government expenditure was expected to decrease gradually from 2023-2024 onwards, with its ratio to GDP at about 22% in 2027-2028.

7. On the revenue side, FS continued to say that revenue from profits tax and salaries tax for 2022-2023 had increased by about 4% and 5% respectively over the original estimates, while revenue from stamp duty had decreased by about 15% due to the decline in transaction volume as a result of the weak property and stock markets. The decrease in revenue from land sales in

2022-2023 was mainly due to a reduction in land premiums. FS envisaged that it would take some time for the Hong Kong economy to fully recover. The Government would continue to promote a steady recovery of the Hong Kong economy by adopting the strategy of supporting small and medium enterprises ("SMEs"), safeguarding jobs and stimulating consumption.

Initiatives to attract enterprises and investments

8. Members enquired about the details and progress of the work of the Office for Attracting Strategic Enterprises ("OASES") in attracting enterprises and investments, and whether the Administration would provide more facilitation and support measures for OASES so that the latter could more effectively attract enterprises to set up their presence in Hong Kong. In addition, Members were concerned whether OASES' initiatives to attract enterprises and investments and the Government's re-industrialization initiatives could create more job opportunities for the research and development ("R&D") industry and the middle and senior management levels in Hong Kong, as well as attract the business sector to bring in new industry chains, and enquired how the Administration envisaged the effectiveness of the above policy initiatives.

9. FS responded that OASES, which served as a one-stop window for attracting strategic enterprises, was committed to attracting high potential and representative strategic enterprises to set up their presence in Hong Kong. Its target industries included life and health technology, artificial intelligence and data science, financial technologies ("Fintech"), etc. OASES would proactively reach out to and carry out negotiations with strategic enterprises and, in consultation with the relevant bureaux, formulate attractive special facilitation measures and tailor-made plans based on the respective needs of individual enterprises, especially those of a large scale and making contributions to the local employment market and GDP, so as to facilitate the establishment of their presence in Hong Kong.

10. On job creation, FS advised that it was observed that overseas enterprises coming to Hong Kong would generally employ local staff for financial and management work. It was estimated that tens of thousands of quality and diversified employment opportunities would be created in Hong Kong when strategic enterprises set up their presence here. The Government was also making efforts to nurture and retain more innovation and technology ("I&T") talents in Hong Kong. This included providing funding support under the "Research Talent Hub" ("RTH") for eligible companies or organizations to engage researchers possessing a bachelor/master/doctoral degree in a science, technology, engineering and mathematics related discipline awarded by either a local university or a well-recognized non-local institution to conduct R&D. The Government expected that the researchers would stay in Hong Kong after the end of the RTH engagement period and would engage in scientific research, thus

providing a pool of I&T talents needed for the strategic enterprises to be set up in Hong Kong in future.

Labour market situation

11. While acknowledging FS's broad strategy to stabilize the local economy by supporting local consumption, Members were concerned that the shortage of manpower in the local labour market would exert pressure on Hong Kong's economic recovery. Members enquired about the Administration's measures to alleviate the shortage of local manpower, in particular the lower-skilled workers.

12. FS advised that in view of the manpower shortage faced by various trades and industries, the Government had enhanced the existing admission schemes and introduced the new Top Talent Pass Scheme at the end of last year. In addition, the Government had also imported labour under the Supplementary Labour Scheme for individual industries facing acute shortage of local manpower, including the importation of care workers for the elderly service industry. FS further explained that the current labour force in Hong Kong had shrunk by about 5% to 6% compared with that in 2019, mainly due to the ageing population as the labour force participation rate of the elderly population was generally lower. In the face of a declining labour force due to an ageing population, the Government would encourage the elderly and middle-aged to stay in employment and women to enter the labour market, as well as explore the introduction of labour importation measures.

Demand-side management and macro-prudential measures for the property market

13. Members pointed out that according to the paper provided by the Government, speculative activities in the property market and purchases of properties by non-local buyers had remained low, and the supply of first-hand residential flats in the private sector was expected to rise to a record high of 107 000 units in the coming three to four years. Members considered that the above market indicators had proved the effectiveness of the various demand-side management measures introduced by the Government, and urged the Administration to consider removing such measures.

14. FS advised that market speculation had cooled down after the introduction of various demand-side management measures. The number of residential property transactions last year was about 45 000 (about 74 000 in 2021; and about 50 000 to 60 000 per year on average from 2013 to 2020), which might be the result of the still slack economy, rising interest rates and buyers being cautious in entering the market. The Government would closely monitor the property market in the future, and would carefully consider whether there was room for relaxing the loan-to-value ratio to help local buyers to purchase their own homes.

Monetary affairs

15. The Panel continued to receive regular briefings from the Chief Executive of the Hong Kong Monetary Authority ("HKMA") and his colleagues on the work of HKMA. At the briefings held in February, May and November 2023, HKMA exchanged views with members on a number of subjects including the impact of the external investment environment on the stability of Hong Kong's financial system, investment performance of the Exchange Fund ("EF"), the Linked Exchange Rate System ("LERS"), support for SMEs and I&T enterprises in addressing the difficulties in opening bank accounts, and development of the financial infrastructure and Fintech.

Investment environment, investment performance of the Exchange Fund and the Linked Exchange Rate System

16. Members were concerned about the impact of the uncertainties in the external investment environment and the geopolitical situation on the stability of Hong Kong's financial system and the investment return of EF. Members also expressed concern that the interest rate payable by EF to the fiscal reserves in 2023 (i.e. 3.7%) was lower than that of the Hong Kong dollar and the United States ("US") dollar time deposits. Given that EF incurred investment losses in both equity and foreign exchange in the third quarter of 2023, members enquired whether HKMA would adjust the investment strategy of EF, including whether a more conservative strategy would be adopted to increase the proportion of cash deposits to total assets. In addition, members asked whether HKMA would, in selecting external fund managers, consider if the fund managers had imposed a cap on the investment in virtual assets ("VAs"), so as to enhance the risk control over EF's investment.

17. HKMA advised that while financial markets might remain volatile amid worries over the factors such as uncertainties in the economic outlook and geopolitical situation, Hong Kong's financial system, including financial institutions, had accumulated considerable experience in coping with such uncertainties and volatility. Regarding the investment of EF, HKMA remarked that over the past few years it had been adopting a relatively defensive approach, such as increasing its holdings of cash and bonds with shorter maturities (i.e. one to three months), and a diversified investment strategy, such as investing in private equity funds and the property market, so as to enhance the resilience of EF to counter adverse shocks, with a view to obtaining a better return in the medium to long term. In considering increasing the proportion of cash, HKMA would take into account the deposit-taking capacity of the banking system and strike a proper balance, given the sheer size of EF. HKMA also explained that the interest rate payable by EF to the fiscal reserves was calculated on the basis of a six-year

average rate of return with a view to providing the Government with a stable return in the medium to long term.

18. As regards investment in VAs, HKMA advised that while EF made no direct investment in crypto-assets, external investment managers engaged by HKMA did invest in a wide range of asset classes and markets around the world. It could not be ruled out that in the investment portfolios of these managers at different times, investment in crypto-assets might have been involved in individual cases, but the proportion of which would be insignificant. In selecting external fund managers, HKMA would take into account whether the fund managers adopted prudent investment strategies, as they would also set stringent requirements for their investment accordingly. Only an insignificant part of the investment made by external fund managers involved VAs, which covered not only cryptocurrencies but also investment in Fintech infrastructure, such as blockchain technology.

19. In view of the imminent threats of a structural deficit and a weakening Monetary Base in Hong Kong, members were concerned about the risks posed by these threats to LERS and the details of the early warning system established by the Administration in this regard.

20. HKMA stressed that the stability of LERS relied on the support of a large amount of US dollars. Given Hong Kong's foreign currency reserves currently standing at 1.7 times its Monetary Base, the market had full confidence in LERS having the foreign currency reserves as its bedrock. Although EF recorded an annual loss of $202.4 billion in 2022, it had performed well in the previous years with a total gain of $500-600 billion. In the long run, the ample foreign currency reserves and its stable income would be able to provide support for the Monetary Base. Broadly speaking, EF had two major portfolios, among which the Backing Portfolio ("BP") provided full backing to the Monetary Base. Compared with other investments of EF, the risk of BP was lower. Last year, the overall rate of return of EF was -4.4%, while that of BP was only -0.4%. As for the early warning system, HKMA had been closely monitoring the market conditions and, under the leadership of FS, maintained close liaison with the Securities and Futures Commission ("SFC") and the Administration to discuss issues related to the provision of early warning across markets.

Support for small and medium enterprises and innovation and technology enterprises

21. Members expressed concern about the difficulties encountered by I&T enterprises set up in Hong Kong in opening bank accounts in Hong Kong, where the time required for them to open accounts was much longer than that in neighbouring regions. Members were also concerned that with the commencement of the registration regime for dealers in precious metals and

stones ("PMS") under the Anti-Money Laundering and Counter-Terrorist Financing Ordinance (Cap. 615) ("AMLO") since April 2023, some PMS dealers had relayed that the registration procedures were cumbersome with high compliance costs. On the other hand, the licensing regime for virtual asset service providers ("VASPs") would come into force in June 2023, and potential applicants for a VASP licence had also reflected the difficulties in opening bank accounts.

22. HKMA advised that it noted the alleged difficulties in opening bank accounts and a dedicated team had been set up to handle the difficulties encountered by the public in this regard. HKMA recently undertook an extensive communication with the industry to explain the risk-based regulatory requirements for the banking sector in Hong Kong and issued circulars to banks reiterating the relevant policy objectives. In collaboration with SFC, HKMA had held roundtable meetings with the banking industry and major VASPs to facilitate direct communication on account opening arrangements with a view to rationalizing the account opening process. Earlier on, HKMA had also made a comparison between Hong Kong and other regions in terms of the requirements, principles, as well as the information and time required for account opening and found no significant differences.

23. HKMA continued that as the operation of some I&T enterprises might not require the opening of full-service bank accounts, they might consider the option of opening "Simple Bank Accounts" ("SBAs"). With narrower service scope and transaction volume, the risks involved in SBAs would be relatively lower and hence less extensive customer due diligence measures were required. Since the introduction of the SBA scheme in 2019, more than 10 000 accounts had been opened successfully. HKMA expected more retail banks to launch the SBA service in 2023.

Financial infrastructure and financial technology

24. Members were concerned about the plan and timetable for increasing the number of data providers in Commercial Data Interchange ("CDI"), such as the inclusion of government departments and online shopping platforms, so as to help more SMEs obtain financing through the data provided by CDI. Besides, members suggested that in future, HKMA should provide a more detailed breakdown of the loans facilitated by CDI, such as the number of difficult cases which were successfully approved loans through CDI, and the number of cases in other categories (e.g. renewal loans).

25. HKMA advised that instead of multiple one-to-one connections between banks and sources of commercial data, CDI was officially launched in October 2022 to provide independent connections for each bank and data provider. As of March 2023, it was estimated that CDI had facilitated the approval of more

than 2 300 loans, amounting to about $2.1 billion, since its production launch. HKMA would continue with its efforts to increase the number of data providers (including government departments) and enhance the data analytics functionality of CDI, so that financial institutions could embrace more innovative applications in processes such as credit assessment, loan approval and Know-Your-Customer.

26. Members noted that HKMA and the Bank of Thailand had confirmed the launch of a new service called "FPS x PromptPay QR Payment" with effect from 4 December 2023, which enabled the use of Hong Kong's Faster Payment System ("FPS") and Thailand's PromptPay by visitors from the two places for local payment. While welcoming this new cross-boundary payment initiative, members expressed concern about the application and development of e-payment as well as e-HKD at the local retail level, and enquired about the measures to promote the popularization of e-payment and e-HKD.

27. HKMA advised that the lack of popularity of e-payment at the local retail level (including taxis) was related to the acceptance of e-payment by individual merchants and members of the public in terms of its technological aspects and daily application. In this connection, HKMA had stepped up promotion and maintained liaison with payment operators to promote wider application of e-payment. In addition, the several rounds of Consumption Voucher Scheme launched by the HKSAR Government had also helped further consolidate the habit of merchants and the public of using e-payment, thereby facilitating the development of the digital economy. In response to members' suggestion of introducing clauses under the relevant licensing regimes and the government loan measures requiring applicants to provide e-payment options, HKMA pointed out that such clauses might have certain impacts on the operating costs and operations of the industry, and had to be carefully considered.

<u>Proposal on establishing a policy holders' protection scheme</u>

28. At the meeting on 3 April 2023, the Administration briefed the Panel on the objectives and guiding principles of the proposed policy holders' protection scheme ("PPS") and its key features, including the proposed coverage, options of compensation limit, funding arrangement and administrative arrangements. Panel members generally expressed support for the establishment of PPS, which in their view, could provide a safety net for policy holders in the event of an insurer becoming insolvent.

29. Members sought explanation on the detailed calculation of levies under PPS, and enquired how the Administration assessed whether the insurers would pass on the proposed 0.07% initial levy to policy holders, resulting in upward pressure on premiums.

30. Members noted that if the proposed Long Term Fund and General Fund were insufficient to meet all the liabilities of an insolvent insurer, the proposed PPS could facilitate borrowing from a third party subject to LegCo's approval. Members enquired about the details of the borrowing, including the maximum amount and duration of borrowing that could be made, whether the Government would guarantee the borrowing, and whether the levy rate would need to be adjusted upwards in the light of the interest expense incurred from the borrowing.

31. The Administration advised that two separate funds, namely the Long Term Fund and General Fund, would be set up under PPS to collect levies from insurers based on the applicable premium income from the protected policies. The levies would be collected from insurers in a progressive manner, starting at 0.07% and stepped up to include an additional levy capped at 1% upon occurrence of an insolvency. Given that the proposed initial levy rate of 0.07% was relatively low, and in view of the keen competition in the insurance market, the Administration expected the impact of the levy on premiums to be minimal. Regarding the borrowing arrangements, the Administration remarked that policy holders' protection schemes in different places had arrangements for borrowing from third parties, and the amount of borrowing would generally be determined by the amount of claims that policy holders could make from insurers in the event of insolvency.

32. Regarding members' enquiry on the coverage of PPS, the Administration advised that all in-force policies would be covered under PPS except reinsurance business, long term business of managing contributions under a retirement scheme, general business subject to alternative protection (e.g. motor vehicle policies and employees compensation policies), general business focused on specialty risks, business which were unusual for individuals, and offshore risks of policies other than travel, accident, sickness and goods in transit. Foreign-incorporated insurers protected by a similar scheme in other jurisdictions with the coverage and compensation not less than those of PPS would be exempted on a case-by-case basis to avoid double levy. The Administration would consider requiring insurers to set out clearly at the time of issuance of policies whether such policies were covered by PPS. The Administration would also work with the Insurance Authority ("IA") to strengthen publicity and education for the insurance industry and consumers when PPS was put to implementation.

<u>Latest progress of the eMPF Platform Project</u>

33. At the meeting on 17 March 2023, the Administration and the Mandatory Provident Fund Schemes Authority ("MPFA") updated the Panel on the latest progress of the eMPF Platform Project ("the Project"). MPFA advised that based on the assessment of PCCW Solutions Limited, the Project Contractor ("the Contractor"), there would be delay in software development and hence it was

highly likely that the delivery of a fully functional system by the Contractor would be delayed by eight months as compared to the requirement stipulated in the contract. Nonetheless, the ultimate target of making the Platform fully functional in 2025 remained unchanged.

34. Expressing grave concern that it was highly likely for the completion of system development work of the eMPF Platform to be deferred to mid-2023 and the delivery of a fully functional eMPF Platform by the Contractor to be delayed by eight months, members enquired MPFA about: (a) measures in place to ensure that there would be no further slippage in system delivery, including how the Contractor's work was monitored round the clock; (b) how to ensure the Contractor could catch up on the progress while ensuring the quality of the system was up to standard; and (c) the penalties for the Contractor's delay in system delivery.

35. MPFA advised that the delay was mainly because the progress of software development had been lagging behind; and according to the Contractor, the major cause of the delay in software development was manpower shortage and high staff turnover rate. MPFA and the eMPF Platform Company Limited ("eMPF Company") had taken appropriate actions, including requiring the Contractor to recruit more staff as well as enhance work efficiency, and to work out a recovery plan to catch up on the progress and minimize the expected delay. Moreover, MPFA and the eMPF Company had requested the Contractor to engage a third-party professional consultant to conduct an independent assessment on the recovery plan to ascertain its feasibility and credibility. In addition, the eMPF Company had issued both verbal and written warnings to the Contractor and had reserved all its rights under the contract, including legal actions against the Contractor such as claiming liquidated damages from the Contractor for its delay in system delivery. MPFA pointed out that the contract signed with the Contractor had clearly set out the calculation of liquidated damages the eMPF Company could claim from the Contractor. There were also provisions in the contract providing for the right of the eMPF Company to terminate the contract or replace the Contractor. MPFA stressed that to prevent further slippage of the Project and safeguard system integrity, MPFA and the eMPF Company had put in place various project management enhancement measures to step up the involvement of the Contractor's top management, project monitoring and resources management. These measures included shortening the cycle of submitting progress indicator reports by the Contractor, conducting on-site inspection at the Contractor's offices, and requiring more frequent working meetings with the Contractor. Based on MPFA's observation, the Contractor had recently made improvement in both manpower shortage and work progress and MPFA's target of making the Platform fully functional in 2025 remained unchanged.

36. On the quality of the eMPF Platform system, MPFA advised that it would make its best endeavours to ensure the timely delivery of the Project and to make sure that the quality of the system could meet public expectation. MPFA added that before the launch of the system, the eMPF Company would conduct a series of internal testing to ensure that the system was safe and secure. Besides, the eMPF Company would engage independent professional consultants to conduct third-party testing and evaluation of the system's cybersecurity, personal data protection and overall system functionality.

37. Regarding members' enquiries on how a smooth transition of all Mandatory Provident Fund ("MPF") schemes to the eMPF Platform could be ensured, and on the system security as well as the information security level of the eMPF Platform, MPFA advised that repeated testing would be conducted before the system became fully functional to make sure the onboarding of all MPF schemes to the eMPF Platform would be completed smoothly. MPFA pointed out that the design of the system was made with reference to internationally recognized standards on information security and was in line with the Government's guidelines on storage and processing of classified information. In building the data centres, the Office of the Government Chief Information Officer had also provided technical input to the eMPF Company. Upon the implementation of the eMPF Platform, the eMPF Company would monitor its cyber system round the clock and set up back-up data centres to make sure that the day-to-day administration of the MPF schemes would not be affected by the data migration.

<u>Development of financial technologies and other innovations for financial services in Hong Kong</u>

38. At the meeting on 5 June 2023, the Administration briefed the Panel on the latest development and measures of Fintech and other innovations for financial services in Hong Kong, as well as the progress on the regulation of VAs.

39. Pointing out the unsatisfactory earning power of the existing eight virtual banks in Hong Kong and some I&T enterprises coming to Hong Kong for fundraising, Panel members enquired how the Administration would support the long-term development of virtual banks.

40. The Administration advised that it would explore with Fintech enterprises coming to Hong Kong for fundraising on how to create more value-adding opportunities for their value chains, including assisting the responsible persons of such enterprises to set up family offices in Hong Kong. On the development of virtual banking, the Administration advised that since the introduction of virtual banking in 2020, licensed virtual banks had been actively introducing new products and new technologies to enhance customer services and

promote financial inclusion. With the epidemic coming to an end, the financial position of the virtual banks was gradually improving. As at March 2023, over 1.9 million accounts were opened in the eight virtual banks, with total deposits exceeding HK$30 billion. HKMA was also facilitating the sharing of business data between enterprises and banks (including virtual banks) through CDI launched in 2022, to facilitate the digital approval of loans by banks.

41. Members urged the Administration to step up publicity and promotion on the licensing regime for VASPs, the Hong Kong Dollar-Renminbi Dual Counter Model ("Dual Counter Model") and measures to attract family offices to set up in Hong Kong through organizations such as the Investor and Financial Education Council ("IFEC"). Members also enquired about the progress of the licensing of VASPs.

42. The Administration advised that it would work with IFEC, the Financial Services Development Council ("FSDC"), regulators and other organizations concerned to actively promote the initiatives. For the Dual Counter Model, in particular, the Administration had drawn up an overall publicity plan in collaboration with the Hong Kong Exchanges and Clearing Limited and SFC. The Administration would also work with FSDC for the production of Announcements in the Public Interest to introduce the work on promoting the development of Renminbi. Besides, OASES and Invest Hong Kong had dedicated teams responsible for the tasks of attracting family offices to Hong Kong. Regarding the licensing of VASPs, the Administration responded that at present two VA exchanges had already been licensed by SFC as VA trading platforms under the Securities and Futures Ordinance (Cap. 571) ("SFO"). SFC was actively recruiting additional staff to process the applications and had advised applicants to appoint an independent body to assess in advance whether their applications met SFC's licensing requirements so as to expedite the vetting and approval process.

43. Given that Fintech involved access to and transmission of large amount of data, members enquired about the Administration's measures to promote the development and enhance the competitive edge of Hong Kong in the Fintech landscape on the premise of safeguarding the financial and data security of the country and Hong Kong.

44. The Administration responded that financial security was an important part of national security. The Administration was looking into the detailed arrangements of the regulatory regime for crowdfunding activities and would report the outcome of the public consultation as well as the further proposals to the Panel in due course. The Administration also continued to implement the work related to financial security through enhanced cooperation with various regulators. Besides, HKMA had introduced the Cybersecurity Fortification Initiative since 2016 to raise the cyber resilience of the banking system and help

the industry identify cyber security gaps. The Initiative was upgraded to Cybersecurity Fortification Initiative 2.0 and came into effect in 2021 to raise the cyber resilience of the banking system to a higher level.

Regulation of virtual asset trading platforms

45. At the meeting on 30 Oct 2023, the Administration, SFC and IFEC briefed members on the policy initiatives of and latest development on the regulation of virtual asset trading platforms ("VATPs"), including implementation of the licensing regime as well as related publicity and investor education efforts.

46. Members expressed grave concern about how SFC handled a suspected fraud case involving a VATP which attracted much attention in the community. Opining that law enforcement agencies should step up efforts in collecting intelligence and combating fraudulent conducts, members suggested that SFC should notify law enforcement agencies as soon as possible when dealing with similar cases in future. SFC should also consider drawing reference from overseas practices and announced, within 24 hours after detection of individual suspicious websites, the investigation results thereon. The Government should also consider enacting legislation to empower law enforcement agencies to duly handle or even shut down suspicious websites immediately with a view to enhancing investor protection.

47. SFC advised that in respect of the case which was of concern to members, shortly after SFC's attention was drawn to the making of suspected misleading online representations by the VATP concerned in 2022, SFC had placed it on the Alert List. Since then, SFC issued investor alerts on multiple occasions, on an anonymous basis, against dealing with unlicensed platforms and related malpractices. SFC received the first investor complaint against the VATP concerned in April 2023 and had since June 2023, by virtue of the enhanced investigative power conferred by the licensing regime under AMLO, collected more evidence of suspected fraud relating to the subject VATP, culminating in the decision to publish the relevant information on 13 September 2023. SFC stressed that while it had all along shared information with the Police on suspicious activities of and breaches by VATPs (including the VATP concerned), a joint working group had been set up with the Hong Kong Police Force to enhance the exchange of intelligence in future.

48. Members expressed concern whether there might be loopholes in the promotion, marketing and sales practices of VAs at present. They pointed out that non-SFC licensees, including some online key opinion leaders, might promote VAs to retail investors without conducting due diligence on customers and products, thus rendering it difficult to protect investors' interests. In this regard, members suggested that the Administration step up regulation on persons who were engaged in introducing and selling VA services or products to the

public, including the requirements for them to undergo training and continuing education, assume self-responsibility, disclose remuneration, obtain licences, declare whether they were licensees, and/or even enacting legislation to directly prohibit them from marketing and selling such services and products to retail investors.

49. In response, the Administration and SFC pointed out that under AMLO and the current licensing regime, it would be an offence for any person to operate a VA exchange in Hong Kong without a licence or to engage in the marketing of VA exchange services to the public of Hong Kong. SFC was vested with a range of statutory powers and tools to combat fraudulent or deceptive behaviour in any transaction involving VAs, as well as behaviour involving the use of fraudulent or reckless means (e.g. issuing untrue and misleading information or advertisements) to induce others to invest in VAs, including issuing a "cease and desist" order to the person involved and applying to the court for an injunction order. Nevertheless, SFC remarked that at present, any person advising the public on a specific security on platforms such as newspapers, radio programmes and the Internet was generally not required to obtain a licence if he did not receive income in this regard from companies relating to that security. Hence, the suggestion of requiring key opinion leaders to hold a licence before they could recommend VA services or products to the public (regardless of whether they received an income in this connection from the companies concerned) might not be in line with the current regulations and measures, and the Administration would need to study the suggestion in detail.

50. Members considered that the large number of victims falling prey to the typical investment scam of "low risk, high return" claims was a sign that the effectiveness of investor education was still far from satisfactory. Members suggested that investor education should be stepped up, including enhancing public awareness of the risks associated with VAs and potential fraudulent behaviour, conducting publicity in a more lively and engaging manner from the public's perspective such as by replacing text with video clips in publicity materials, as well as promoting investment education among secondary students.

51. IFEC remarked that it was committed to promoting investor and financial education in an engaging and lively manner, and had been keeping tabs on market developments, such that investor education would be launched once new investment products or jargon emerged in the market. IFEC pointed out that wide publicity on the basic principles of financial management could help the community guard against the ever-changing fraudulent practices. Meanwhile, elements of financial education had already been incorporated into the secondary school curriculum. As far as VAs were concerned, IFEC had since 2017 engaged investors through various channels such as mass media, social media and education talks in order to explain to them the characteristics, operation and risks of VAs.

52. Regarding members' enquiry on whether the Administration would consider imposing an interim prohibition against the sale of VA products to retail investors by any person until there was a way to safeguard against such products becoming worthless all of a sudden, the Administration responded that it had already taken into account how best to enhance protection for retail investors when formulating the regulatory requirements of the licensing regime. VATPs which intended to provide services to retail investors must meet stringent licensing conditions and regulatory requirements, such as those on client onboarding, safe and segregated custody of client assets, as well as submission of listing plans to SFC for approval before product launch. Looking forward, IFEC would need to step up efforts in educating investors on the main points to be aware of under the current regulatory landscape so as to help retail investors better understand the risks of investing in VA market nowadays.

Company re-domiciliation regime

53. At the meeting on 3 July 2023, the Administration briefed the Panel on its proposal to introduce a company re-domiciliation regime to facilitate non-Hong Kong companies' re-domiciliation to Hong Kong. Panel members noted that if a company was not required under the laws of its original domicile to obtain its members' consent for re-domiciliation, it must fulfil the following two requirements: (a) its members had consented to the re-domiciliation by a resolution that had been passed by at least 75% of the members entitled to vote on the resolution; and (b) its members had been given at least 21 days' notice of the meeting concerned and the proposed resolution. In this connection, Panel members suggested that consideration be given to raising the required passage by at least 75% of members' votes to 100%, so to avoid any disputes arising from the re-domiciliation. Enquiries were also raised about the threshold of 75% of votes in comparison with other jurisdictions. Given that the notice period for removing auditors under the Companies Ordinance (Cap. 622) ("CO") was 28 days, members enquired why the notice period for re-domiciliation, which was of greater significance, was set at 21 days only.

54. The Administration advised that under the proposed company re-domiciliation regime, if a company was not required under the laws of its original domiciles to obtain its members' consent for re-domiciliation, the requirements under CO for calling general meetings and passing special resolutions would apply, i.e. at least 21 days' notice given and passage by at least 75% of votes obtained. In the light of the comments received during the consultation period, the Administration was considering relaxing the requirements.

55. Members enquired about the regions and industries whose enterprises would benefit from Hong Kong's re-domiciliation regime, and the overall

competitiveness of the proposed company re-domiciliation regime compared with other jurisdictions.

56. The Administration advised that during the consultation period it was aware of the strong demand from the insurance industry for re-domiciliation to Hong Kong. For instance, many of the 12 insurers registered in Bermuda had expressed interest in re-domiciling to Hong Kong by utilizing the proposed regime. In addition, among some 14 000 registered non-Hong Kong companies that had a place of business in Hong Kong, over half of them were registered in the British Virgin Islands and about 20% in the Cayman Islands. It would be more likely for these companies with business connection with Hong Kong to re-domicile to Hong Kong through the proposed regime. Regarding the competitiveness of the proposed regime, the Administration advised that unlike the practices of other jurisdictions such as Singapore, no economic substance test would be imposed on companies intending to re-domicile to Hong Kong, which was meant to ensure that the applicability of the re-domiciliation mechanism would be as extensive as possible to cover companies of different sizes. The Administration added that there were increasingly stringent regulatory requirements on the registration of various types of enterprises in overseas jurisdictions. With the implementation of a global minimum corporate tax rate, it might not be effective for enterprises to reduce their taxation costs by domiciling overseas. It was opportune for Hong Kong to introduce a re-domiciliation regime to allow companies originally domiciled outside Hong Kong for tax considerations to re-domicile to Hong Kong.

57. Members noted that under the Administration's proposal, companies must notify the Registrar of Companies ("R of C") of their de-registration in their original domiciles within 60 days after a certificate of re-domiciliation was issued to them, and such requirement was similar to the relevant requirement of Singapore, a major competitor of Hong Kong. Members suggested relaxing the 60-day requirement to allow sufficient time for re-domiciling companies to deal with the related tax and legal arrangements. Members also enquired on how the Administration would deal with re-domiciliation applications of companies which failed to de-register in their original domiciles within 60 days.

58. The Administration advised that the requirement for re-domiciling companies to notify R of C within 60 days was modelled on the requirements in other jurisdictions, and it was proposed to provide in the legislation that R of C might approve applications for extension of the 60-day period, subject to any condition considered appropriate. Such requirement was meant to minimize the cases of re-domiciling companies, which would have completed their registration in Hong Kong, holding concurrent registration status in both their original domiciles and Hong Kong. However, as some companies would be required to submit to their original domiciles the certificate of re-domiciliation issued by Hong Kong before they could be de-registered by the government of their original

domiciles, it would be impossible to hold off the issuance of the certificate of re-domiciliation to re-domiciling companies until they had completed de-registration in their original domiciles. As such, a balance had to be struck in respect of the notice period.

Other work

59. During the 2023 legislative session, the Panel also discussed with the Administration and related bodies a number of other subjects. The major ones are:

(a) legislative proposals, including;

(i) amendments to Schedule 5 to SFO to introduce "providing depositary services for relevant collective investment schemes ("CISs") as a new regulated activity, to bring depositaries of SFC-authorized CISs under the licensing, supervision and enforcement regime of SFO;[1]

(ii) amendments to the Inland Revenue Ordinance (Cap. 112) ("IRO") to enhance the certainty of non-taxation in relation to onshore gains from disposal of equity interests of capital nature;[2]

(iii) amendments to IRO to refine Hong Kong's foreign-sourced income exemption regime with regard to foreign-sourced disposal gains;[3]

(iv) legislative proposals relating to the implementation of the Basel III final reform package;

(v) amendments to the Deposit Protection Scheme Ordinance (Cap. 581) and the Deposit Protection Scheme (Representation on Scheme Membership and Protection of

---

[1] The nine pieces of subsidiary legislation relating to regulation of depositaries of public CISs were tabled for LegCo's negative vetting on 29 March 2023, and the new regulatory regime would commence on 2 October 2024.

[2] The Inland Revenue (Amendment) (Disposal Gain by Holder of Qualifying Equity Interests) Bill 2023 would resume its Second Reading debate at the LegCo meeting of 6 December 2023.

[3] The Inland Revenue (Amendment) (Taxation on Foreign-sourced Disposal Gains) Bill 2023 was passed at the LegCo meeting of 29 November 2023.

Financial Products under Scheme) Rules (Cap. 581A) to implement the final proposals on enhancements to the Deposit Protection Scheme; and

(vi) amendments to IRO to increase tax deduction under profits tax for MPF voluntary contributions made by employers for their employees aged 65 or above;

(b) staffing proposal on the creation of a permanent Assistant Commissioner post in the Inland Revenue Department;[4]

(c) the work of FSDC in 2022-2023 and its work plan for 2023-2024; and

(d) the proposed budgets of SFC, IA, MPFA and the Accounting and Financial Reporting Council for the financial year 2023-2024.

60. From January to November 2023, the Panel has held a total of 11 meetings, including a joint meeting with the Panel on Manpower to discuss the Government's further review on the arrangement relating to the employment of non-skilled workers under government service contracts including remuneration of the workers and the relevant monitoring mechanism. The Panel has scheduled another meeting for 4 December 2023 for FS to brief Members on Hong Kong's latest overall economic situation and consult Members on the 2024-2025 Budget, and for the Administration to consult the Panel on the proposed refinements to the regime of Automatic Exchange of Financial Account Information in Tax Matters, as well as the proposed plan for the 2026 Population Census.

Council Business Division 1 and Public Complaints Office
<u>Legislative Council Secretariat</u>
28 November 2023

---

4 The proposal was endorsed by the Establishment Subcommittee at its meeting on 5 May 2023 and approved by the Finance Committee at its meeting on 19 May 2023.

Appendix 1

Legislative Council

Panel on Financial Affairs

Terms of Reference

1. To monitor and examine Government policies and issues of public concern relating to financial and finance matters.

2. To provide a forum for the exchange and dissemination of views on the above policy matters.

3. To receive briefings and to formulate views on any major legislative or financial proposals in respect of the above policy areas prior to their formal introduction to the Council or Finance Committee.

4. To monitor and examine, to the extent it considers necessary, the above policy matters referred to it by a member of the Panel or by the House Committee.

5. To make reports to the Council or to the House Committee as required by the Rules of Procedure.

Appendix 2

Panel on Financial Affairs

Membership list for 2023 session

Chairman	Hon Jeffrey LAM Kin-fung, GBM, GBS, JP
Deputy Chairman	Hon Robert LEE Wai-wang
Members	Hon Tommy CHEUNG Yu-yan, GBM, GBS, JP Hon Starry LEE Wai-king, GBS, JP Hon CHAN Kin-por, GBS, JP Hon CHAN Chun-ying, JP Dr Hon Johnny NG Kit-chong, MH, JP Hon Duncan CHIU Dr Hon Wendy HONG Wen Hon Rock CHEN Chung-nin, SBS, JP Hon CHAN Pui-leung Hon Sunny TAN Dr Hon Kennedy WONG Ying-ho, BBS, JP Hon Edmund WONG Chun-sek Hon TANG Fei, MH Hon TANG Ka-piu, BBS, JP Hon Louis LOONG Hon-biu Dr Hon SO Cheung-wing, SBS, JP Hon Adrian Pedro HO King-hong Hon SHANG Hailong
	(Total：20 members)
Clerk	Miss Sharon LO
Legal Adviser	Mr Mark LAM