



THE

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OF HONG KONG

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23 March 2010

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8/F, Chater House  
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Dear Sir/Madam,

**Re: Joint Consultation Paper on a Proposed Operational Model for  
Implementing a Scripless Securities Market in Hong Kong**

I refer to the Joint Consultation Paper and attach the Law Society's submissions for consideration. The submissions will be posted onto the Law Society's website.

Yours sincerely,

cc Company and Financial Law Committee  
Securities Law Committee



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## **Consultation on Scripless Securities Law Society's Response**

### **Questions**

1. Do you agree that investors should be given the option to hold securities in paper form and to rematerialise securities that have been dematerialised? If not, why not?

### **Answers**

We agree that investors should be given the option initially to hold securities in paper and scripless form. Reform having a direct impact on investors should be allowed to evolve gradually. There are still many retail investors who are uncomfortable with relinquishing their paper certificates for various reasons. However, in view that the dual system will eventually phase out, those investors who opt for scripless form at the beginning of the dematerialisation process should not be permitted to rematerialise their scripless securities, at least after a certain period of time after they have dematerialised. Allowing rematerialisation after dematerialisation at any time prior to a compulsory scripless environment will be regressive. The advantage of disallowing rematerialisation after the lapse of a certain time period when an investor opts for dematerialisation is that the number of securities in paper form will gradually diminish during the dual

phase period and the market will be more prepared for a completely scripless environment with time.

2. Do you agree that the scripless system should eventually be made compulsory and the paper-based option removed altogether? If not, why not?

We agree that in principle, this should be the long-term aim. In the interest of promoting efficiency, there should be an end to the dual system but that should only be done when it is clear that the market and the various stakeholders (in particular the retail investors) are all ready for the compulsory scripless system. The public should be further consulted on the final abolition of the dual system when the market shows signs that it will be ready for a full dematerialization.
3. Do you agree that implementation of a scripless securities market should proceed in phases? If not, why not?

Agree.
4. Do you agree with the proposed phasing, i.e. dematerialising securities in batches, and dematerialising Hong Kong securities first? If not, why not?

Agree.
5. Do you have any views on the proposed dematerialisation process and HKSCC Nominees Limited's diminishing role?

Views on the dematerialization process

  1. The dematerialization and account opening procedures will have to be simple, easy to understand and follow, and related costs will have to be low to provide certificated investors the incentive to change.
  2. Details of any upgrading that will be required of the existing IT and operational systems of the participants and the costs therefore should be provided as early as possible and kept as minimal as possible. There will be issues on how the participants may recoup their costs. Market participants should be consulted on the timing, scope and charges of the implementation of each stage.

3. Each implementation stage should be preceded by a wide reaching investor education campaign to enable the retail investors to understand the costs and benefits and the steps involved.

**Views on HKSCC's roles**

The diminished role of CCASS would mean that brokers/banks/custodians will be handling instructions for investors in their capacity as the registered holders of uncertificated securities. Under the existing system, it is known that CCASS participants do not proactively seek voting instructions from their retail investors. When the CCASS participants become registered holders in place of HKSCC Limited, they would need to set up an effective system to handle corporate communication, including sending corporate representatives to attend meetings and exercise voting rights. There is uncertainty whether all brokers are properly equipped to deal with corporate communication when HKSCC Limited's role gradually fades out. Further consultation should be made among CCASS participants to ascertain whether the majority could build up the infrastructure to deal with corporate communication.

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| 6. | Do you agree with the proposal that the formal register comprise two parts as discussed in paragraphs 49 to 53 of the paper? If not, why not? | Agree.  |
| 7. | Do you agree with the proposal to facilitate name-on-register within CCASS? If not, why not?  | Agree.  |
| 8. | Do you consider that the proposed arrangements for addressing any concerns arising from the removal of the immediate credit                   | There should be system development for those qualified to provide registrar services to ensure that dematerialisation |

arrangement are adequate? If not, why not?

of certificated securities and deposit into CPA, PSA, IPA or ISA should be confined to one working day in order not to affect the T+2 settlement.

Under the proposed model, the complete register of holders will make up of the uncertificated sub-register and the certificated sub-register. Transfers between the two sub-registers may occur routinely. There should be operational safeguards in place to ensure that credit entry to one sub-register will occur simultaneously with a corresponding debit entry to the other sub-register.

9. Do you think the proposed model provides enough options (in terms of account types) for investors? If not, what other options do you think should be provided and why? The options are adequate. Any more available options could be confusing to unsophisticated investors.
10. Should broker/bank/custodian nominees in CCASS be allowed to appoint multiple representatives so that their investor-clients can attend and vote at meetings? If not, why not? Multiple representatives should be permitted.
11. Should broker/bank/custodian nominees in CCASS be allowed to appoint both proxies and multiple representatives in respect of the same meeting? If not, why not? No, we consider the common law position that a proxy is revoked when a shareholder (attending in person or acting through corporate representatives) attending and voting in meeting should be preserved.
12. Do you agree that investors should be required to provide a unique identification number irrespective of whether they obtain their securities by way of a transfer or through an IPO? Agree.
13. Do you agree with the proposal to introduce a new Registrar Participant category in CCASS? If not, why not? Agree.

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| 14. | Do you agree that share registrars who provide scripless related services should be more directly and robustly regulated than they are today? If not, why not?  | Agree. Regulations should be in place to ensure that entities providing registrar services have the financial capabilities and appropriate system infrastructure in place to ensure an expedited dematerialisation process and a simultaneous transfer between the two sub-registers can take place. However, more robust regulations may increase costs which may directly or indirectly be passed onto the relevant stakeholders and a balance should be struck to ensure that, in particular, the investors will not be disadvantaged. |
| 15. | Do you consider that a graduated approach should be taken towards regulating share registrars (i.e. that the level of regulation should vary according to the type and range of scripless related services provided), or that a uniform approach should be taken such that a common standard is applied in all cases? | Uniform approach is preferred if a common standard can be developed and agreed upon. Uniform approach is conducive to efficient and effective supervision.  |
| 16. | Do you have any views on the proposed changes to the IPO process?   | No.   |
| 17. | Do you agree that the scope of the scripless operational model should extend to all publicly traded securities in Hong Kong (including therefore securities such as derivative warrants and CBBCs)?   | Agree. In the interest of promoting efficiency, a scripless environment for all should be the ultimate aim, but for the avoidance of doubt, as mentioned in footnote 31, the implementation of scripless securities should not require issuers of those securities which are currently available in scripless form (such as derivative warrants, CBBCs) to offer a paper option.  |
| 18. | If not, to what extent should the scope be limited, and why?  | Not applicable.   |
| 19. | What are your views on the costs and benefits of introducing a scripless securities market in Hong Kong?  | As a matter of principle, there should be a balance between enhancing market efficiency and competitiveness and   |

ensuring an appropriate level of investors' choice and protection.

There will be costs involved in introducing a dual system and a scripless environment. As noted in paragraphs 79 to 81 of the Consultation Paper, the related costs such as: costs for initial development, implementation and on-going maintenance as well as associated fees and expenses, which will be borne by the participants and investors, have not, as yet, been provided. Without such information, the costs benefits analysis remains conceptual and is incomplete.

Further, given physical holding constitutes around 51% of all issued securities by value (see paragraph 22 (1) of the Consultation Paper), it will be vital to the success and smooth transition of this initiative that a significant number of investors shift to scripless holdings. Currently, set up and on-going expenses are minimal for investors holding physical share certificates and so cost will be an important consideration especially for those medium to long term investors and retirees, in deciding whether or not to dematerialise. The SEHK, SFC and the Federation will have to demonstrate that such costs will be low and will remain affordable after dematerialisation.

Thoughts should also be given to standardise certain fees that may be payable in order to encourage investors' dematerialisation process. For example, under the existing system, the costs of transfer of securities by an investor from one CCASS participant's account to another could vary substantially. This has the effect of discouraging an investor from changing brokers. When the dual system is in place, there could be standardised fees, for example, for

(i) the transfer from a certificated sub-register to an ISA;  
(ii) transfer of a CPA to PSA within the same CCASS participant; (iii) transfer of CPA/PSA between CCASS participants.

20. Regarding the dematerialisation of shares and debentures of overseas companies, do you agree with the proposed approach to focus first on Bermuda, Cayman Islands, Mainland China and UK companies? If not, why not?

Agree. However, as Mainland China company listing is increasingly important both in terms of value and market value, priority should perhaps be given to dematerialization of securities of these companies.

**The Law Society of Hong Kong**  
**Company and Financial Law Committee**  
**Securities Law Committee**  
**23 March 2010**  
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