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30 March 2010

Dear Sir

**JOINT CONSULTATION PAPER ON A PROPOSED OPERATIONAL MODEL FOR
IMPLEMENTING A SCRIPLESS SECURITIES MARKET IN HONG KONG**

We welcome the opportunity to comment on the joint Consultation Paper on a Proposed Operational Model for Implementing a Scripless Securities Market in Hong Kong ("Consultation Paper"), issued by the Securities and Futures Commission (SFC) together with the Federation of Share Registrars Limited (Federation) and Hong Kong Exchanges and Clearing Limited (HKEx) on 30 December 2009.

We support the implementation of a scripless securities market in Hong Kong and consider it a positive step towards enhancing Hong Kong's overall securities market infrastructure. Particularly, by enabling investors to hold and transfer securities within CCASS and in their own names will enhance transparency, and offer a more efficient and convenient trading platform for investors. One issue to bear in mind in the future is that there may come a point where dematerialisation is compulsory. Consideration needs to be given to security documents that are no longer appropriate, as they may require substantial amendments.

We have provided responses to those questions posed in the Consultation Paper on which we have particular views.

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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?

We agree that investors should be given the option to hold securities in paper form when a paper-based regime is run in parallel with the new scripless regime. However, it is not clear why the rematerialisation option is necessary when we note in paragraph 12 that a dual system is only an interim step before moving on to a compulsory scripless environment. This option appears to contradict the ultimate objective of the scripless exercise and may introduce complexities operationally.

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

The compulsory scripless system is only appropriate for certain securities listed on the HKEx. Please refer to our comment in Question 20 on the dematerialisation of shares and debentures of overseas companies.

If the scripless system should eventually be made compulsory it is necessary to give stamp duty considerations to products whose registers are currently held outside Hong Kong, e.g. as in the case of some ETFs.

3. Do you agree that implementation of a scripless securities market should proceed in phases? If not, why not?

Yes.

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

Yes.

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

No.

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?

In principle, we agree with the proposal that the share register comprises two parts. However, thought needs to be given on what happens if there is a conflict between the records of a share registrar and the records of CCASS and the liability imposed on the issuers and the share registrars for failing to keep an updated record of the register. In CREST, if there is any conflict between the CREST register and the register of certificated shares maintained by the registrar, the CREST register prevails. Under the CREST rules and English company law, investors can inspect the register of certificated shares of a company, but not the CREST register, therefore this could cause problems if there are inconsistencies. The company is not

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liable if it takes action based on the duplicate record of the CREST register, provided it has "regularly reconciled" the record with the CREST register, but this protection does not apply to other persons.

7. Do you agree with the proposal to facilitate name-on-register within CCASS? If not, why not?

Yes, provided that the name-on-register feature is not compulsory, as stated in paragraph 59.

8. Do you consider that the proposed arrangements for addressing any concerns arising from the removal of the immediate credit arrangement are adequate? If not, why not?

The proposed workflow to address the absence of the immediate credit arrangement should be closely monitored at the start-up phase to ensure the transfer process is not delayed in practice.

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 four proposed account holding structures for holding securities will provide investors with choices in terms of form (before a compulsory scripless environment is imposed), ownership type and the extent of control over their holdings. Whilst we understand that there is a trend to move away from omnibus account, three out of the four proposed holding structures are through segregated accounts. HKSCC needs to consider whether from an operational standpoint it has the capability to operate the numbers of segregated accounts as envisaged.

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?

Under Section 115 of the Companies Ordinance, CCASS / HKSCC Nominees Limited may appoint more than one authorized representative to attend any meeting of the company, provided that each authorization specifies the number and class of shares in respect of which each person is authorized.

Under the proposed scripless model, securities held in a CCASS Participant Sponsored Account / Investor Participant Account / Issuer Sponsored Account will be registered in the name of the investor. Where securities are held in a CCASS Participant Account registered in the name of the broker/bank/custodian nominees, the arrangement is in fact analogous to the existing nominee arrangement by HKSCC Nominees Limited.

It has been held in **Re CA Pacific Finance Ltd [1999] 2 HKLRD 1** that investors in CCASS are treated by the company as members enjoying rights of ordinary membership. In relation to their rights to attend and vote at general meetings, investors who wish to exercise those rights may request their CCASS participants (if they are not investor participants), which in

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turn request the CCASS nominee, to arrange for their exercise; whereas for investors who are investor participants and hence also CCASS participants, they may relay their request to the CCASS nominee direct. Similar to investors outside CCASS, CCASS investors do not have to attend the meetings in person but can send a representative or a proxy for the purpose of attending and voting at such meetings on their behalf. Since the investors are not the registered holders of the securities, they cannot appoint the relevant person themselves but through the CCASS nominee, and such arrangement is enabled by Section 115 of the Companies Ordinance.

We fail to see the reason why, under the new scripless model, investors holding securities in a CCASS Participant Account via broker/bank/custodian should be treated differently. The underlying investors, as the ultimate beneficial owners of the relevant securities, should not be disenfranchised with their shareholder rights. Accordingly we believe broker/bank/custodian nominees in CCASS should be allowed to appoint multiple representatives so that their investor-clients can attend and vote at meetings. This also means that an enabling provision similar to Section 115 of the Companies Ordinance will need to be introduced in respect of broker/bank/custodian nominees in CCASS.

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?

From a legal perspective, there are fundamental differences between a corporate representative and a proxy. For example, a corporate representative can vote on both a show of hands or a poll, whereas a proxy can only vote on a poll but not on a show of hands (unless the articles of association of the company otherwise provide). A corporate representative will be counted towards the quorum, however, in the case of a proxy, he will not be counted towards the quorum (again, unless the articles otherwise provide). As the concepts of "corporate representative" and "proxy" are built upon different sets of legal principles and case law, we believe allowing broker/bank/custodian nominees in CCASS to appoint both proxies and multiple representatives in respect of the same meeting may lead to chaos and confusion.

Under the current arrangement, HKSCC Nominees Limited cannot appoint both proxies and corporate representatives in respect of the same meeting. We believe the same restriction should apply to broker/bank/custodian nominees in CCASS under the new model.

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?

We don't have any particular views on the unique identification number.

13. Do you agree with the proposal to introduce a new Registrar Participant category in CCASS? If not, why not?

Currently, the share registrar acts as the issuer's agent in providing corporate communications with investors or their nominees. If the share registrar is a CCASS Participant, would its role

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as the issuer's agent be maintained? There may be issues if the issuer is insolvent and the share registrar is unable to carry out instructions of the investors who had opened accounts with them. This may not be the case had the investor opened an account with another CCASS Participant instead. Perhaps the proposed improvements in information-sharing and processing in paragraph 74 could be achieved via a separate framework, rather than having the share registrar being a CCASS Participant.

In the case that the share registrar is to be included as a new category of participant, it may be more appropriate if it is admitted as a "limited participant" with limited rights (e.g. to extract information and update the register, but not the right to give buy/sell instructions in CCASS or hold shares through segregated accounts). In any event the rights and obligations, as well as the laws and regulations which share registrars will be subject to, need to be more clearly defined.

By way of analogy, in CREST, a registrar is a system participant for technical reasons. A registrar needs to have access to the system so that it can, for examples, procure credit of shares to CREST accounts upon issue of shares, and check the shares recorded in the register of title constituted by the CREST accounts, but a registrar is not a CREST member in the sense of holding any shares. The registrar (and the issuer) has access to CREST to enable it to check the shares recorded in CREST, and is responsible for maintaining a duplicate record of that CREST register.

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?

If the proposals that investors can open an account with the relevant share registrar and hold shares as shareholders eventuate, the share registrar must be regulated like other intermediaries so that they will be subject to, inter alia, the Client Securities Rules. Moreover, care will need to be taken in defining the registrar's different capacities to avoid conflicts of interest – the registrar is normally regarded as agent of, and owing duties to, the issuer, not to shareholders.

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?

A uniform approach should be adopted for consistency purpose.

16. Do you have any views on the proposed changes to the IPO process?

We acknowledge that turning scripless is an inevitable trend so we agree in principle the phased approach for IPOs as suggested in the Consultation Paper. We look forward to

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reviewing the proposed amendments to the Listing Rules which set out the actual logistics as to how it works.

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)?

Yes.

18. If not, to what extent should the scope be limited, and why?

N/A.

19. What are your views on the costs and benefits of introducing a scripless securities market in Hong Kong?

One of the benefits set out in the consultation paper for introducing a scripless securities market is that it should provide a better platform for listed corporations to communicate directly with investors. This may not necessary be the case as very often investors will appoint intermediaries/custodians to hold shares in CCASS. In other words, investors will need to continue to rely on intermediaries/custodians to forward corporate actions to them.

Having said that, the move towards a scripless platform enhances Hong Kong status as a major international financial centre. The scripless model should help improve overall efficiency and promote transparency in the securities market of Hong Kong and given time, the benefits gained will outweigh costs.

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?

It may be very unwieldy to dematerialise the shares of foreign companies listed on the HKEx while complying with the conflicts of laws principles applicable to these shares. It is also worth noting that the UK and Australia have not implemented dematerialisation of foreign companies listed in their jurisdictions, even when their domestic issuers had gone through dematerialisation for more than ten years.

Should you wish to discuss any of our comments, please do not hesitate to contact
and

Yours faithfully



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