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Supervision of Markets Division
Securities and Futures Commission
8/F Chater House
8 Connaught Road Central
Hong Kong

Dear Sirs

Joint Consultation Paper on A Proposed Operational Model For Implementing a Scripless Securities Market in Hong Kong ("Consultation Paper")

We refer to the above Consultation Paper jointly issued by the Securities and Futures Commission (SFC), the Federation of Share Registrars (Federation) and the Hong Kong Exchanges and Clearing Limited (HKEx) on 30 December 2009.

Based on the review by the Custodian Working Group of the Hong Kong Association of Banks (HKAB), comprising 10 representatives from member banks of different sizes providing custody services to retail, commercial, institution, global custodian, investment and/or private banking clients, has carefully reviewed the Consultation Paper. We would like to set out our response in this submission.

We support the implementation of a scripless securities market in Hong Kong to help enhance the overall efficiency and competitiveness in the securities market. We believe that this is an important step in maintaining Hong Kong's status as a leading financial centre. As a matter of principle, we consider that there should be a balance between enhancing the overall efficiency and competitiveness in the securities market and securing an appropriate and improved level of investor choice.

Our detailed comments on the specific issues raised in the Consultation Paper are set out in the enclosed Annex. We would like to highlight the following issues, which we believe should be carefully reviewed in implementing a scripless securities market in Hong Kong:

Chairman Standard Chartered Bank (Hong Kong) Ltd
Vice Chairmen Bank of China (Hong Kong) Ltd
The Hongkong and Shanghai Banking Corporation Ltd
Secretary Rita Liu

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主席 渣打銀行（香港）有限公司
副主席 中國銀行（香港）有限公司
香港上海滙豐銀行有限公司
秘書 廖碧瑩



1. The Consultation Paper proposes a dual system for moving towards a scripless securities market in Hong Kong rather than a model for a fully scripless market. This should be clearly communicated to investors and market participants in the consultation conclusion to be issued by the SFC, Federation and HKEx to avoid any misconception that the entire market will become scripless from the very beginning of implementing the model.
2. The Government should commit to a target timetable as to when Hong Kong will move completely from the current largely paper-based system to a mandatory scripless one. While we understand that a phased implementation approach is being contemplated by the Government, we urge that the transition period should be as short as practicable, with clear milestones as to when it will expire to allow full dematerialization.
3. The dematerialisation process should be simple and the cost to the community should be kept as low as practicable in order to achieve greater market efficiency within a short transition period. In particular, we consider that the proposal of introducing the new Registrar Participant category (Registrar Participant Accounts (RPA) and Issuer Sponsored Accounts (ISA)) and the CCASS Participant Sponsored Accounts (PSA) (collectively referred to as "the Proposal") might confuse investors and bring inefficiency to the market given the additional layer and account types. In addition, significant development and maintenance cost in this regard will be required and may somehow be transferred to investors and/or market participants directly or indirectly. The Proposal may therefore require reconsideration and further deliberation. Alternatively, we believe that the benefits stated in the Consultation Paper can be largely achieved by adding on the new proposed features (e.g. registered legal ownership and direct control over account activities) to the existing three account types within CCASS (i.e. CCASS Participant Accounts (CPA), CCASS Participant Stock Segregated Accounts (SSA) and Investor Participant Accounts (IPA)). In particular, we encourage CCASS and listed companies to use the cost saving from developing and maintaining the new account structures and types to enhance the current IPA to benefit a larger group of investors by including the features of ISA.
4. As a minimum, all IPO applications through e-channels should be in scripless form from phase 1 onwards. This will enable more retail investors to be familiarised with dealing in shares issued in scripless form.



5. During the transition period, an option to rematerialize securities that have been dematerialized will work against the objective of implementing a scripless securities market in the long run and is confusing to the market. We therefore strongly suggest that this option should be discouraged through appropriate monitoring and other measures. We will be pleased to further discuss with you details of such measures where appropriate.
6. The current services provided by HKSCC Nominees Limited should continuously be made available to the market directly or through the registrars or an equally adept administrator without compromising the quality of services and requiring additional or significant cost.

We hope that you will find the comments useful. HKAB, through the Custodian Working Group, will welcome the opportunity to work with the SFC, the Federation and the HKEx to develop details of the operational model for implementing a scripless securities market in Hong Kong.

Yours faithfully

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Appendix

**Response to the Joint Consultation Paper on a Proposed Operational Model for Implementing a Scripless Securities Market in Hong Kong
published by the Securities and Futures Commission, the Federation of Share Registrars Limited and Hong Kong Exchanges and Clearing Limited
(Consultation Paper)**

No.	Consultation Question	Proposed HKAB's response
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?	<p>We agree that the implementation of a scripless securities market in Hong Kong will help enhance the overall efficiency and competitiveness in the securities market. This is an important step in maintaining Hong Kong's status as a leading financial centre.</p> <p>As a matter of principle, we consider that there should be a balance between enhancing the overall efficiency and competitiveness in the securities market and securing an appropriate and improved level of investor choice. The Consultation Paper has set out various issues that we need to consider in moving Hong Kong towards a scripless securities market. We believe that it will be appropriate to adopt the following principles in debating these issues and how they should be addressed:</p> <ul style="list-style-type: none">• The Government should commit to a target timetable as to when Hong Kong will move completely from the current largely paper-based system to a mandatory scripless one.• The Australian model – whereby it achieved full dematerialization for securities of all of its domestic issuers at the beginning of 1999 without giving an option to investors to hold domestic securities in certificated form - has clear advantages. We recognize this may not be a practicable approach for Hong Kong given its specific circumstances. While we understand that a phased implementation approach is being contemplated by the Government, we urge that the transition period between the launch of the dual

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		<p>system and the fully scripless market should be as short as practicable, with clear milestones as to when it will expire to allow full dematerialization.</p> <ul style="list-style-type: none"> Should the phased approach ultimately be adopted in Hong Kong, we urge that as a minimum, all IPO applications through e-channels should be in scripless form from phase 1 onwards. This will enable more retail investors to be familiarised with dealing in shares issued in scripless form. <p>Furthermore, we consider that during the transition period, an option to rematerialize securities that have been dematerialized will work against the objective of implementing a scripless securities market in the long run and may deliver an inconsistent message to the public. We therefore strongly suggest that this option should be discouraged through appropriate monitoring and other measures. We will be pleased to further discuss with you details of such measures where appropriate.</p>
2.	Do you agree that the scripless system should eventually be made compulsory and the paper-based option removed altogether? If not, why not?	<p>We agree that the scripless system should eventually be made compulsory and the paper-based option removed altogether. We suggest that the dematerialization process should be simple and the cost to the community should be as low as practicable in order to achieve a shorter transition period and gain efficiency in the market.</p> <p>Please also refer to our comments in question 1.</p>
3.	Do you agree that implementation of a scripless securities market should proceed in phases? If not, why not?	<p>We agree that implementation of a scripless securities market should proceed in phases and the implementation should be kicked off as soon as practicable.</p>

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		Please also refer to our comments in questions 1 and 2.
4.	Do you agree with the proposed phasing, i.e. dematerialising securities in batches, and dematerialising Hong Kong securities first? If not, why not?	We agree with the proposed phasing.
5.	Do you have any views on the proposed dematerialisation process and HKSCC Nominees Limited's diminishing role?	<p><u>Views on the proposed dematerialisation process</u></p> <p>As we understand that about half of the total market cap shares in certificated form will be impacted by the dematerialization process¹, we submit that the dematerialization process should be carefully considered, particularly in respect of the following areas:</p> <ul style="list-style-type: none"> • The dematerialization process, including the opening of securities accounts within CCASS, must be simple and accessible in order to encourage dematerialization among the wider public and enhance market efficiency. For example, the share registrar may attach a form when sending annual reports to investors and provide a website for investors to download the form to instruct the share registrar for dematerialization by opening a securities account within CCASS. Alternatively, the locations of physical outlets to open the above accounts should be convenient to investors. In addition, the timeframe for the implementation of dematerialization should be short and there should be a standardized procedure for all registrars to process dematerialization. Please also refer to our comments regarding account types and structures in question 13. • The cost to the community for dematerialization should be as low as practicable. • Considerable benefits should be given by listed companies and CCASS to investors if dematerialization is not compulsory; otherwise investors will see no reason to go

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		<p>through the hassle of opening and maintaining a new account and canceling their paper certificates.</p> <ul style="list-style-type: none"> The Government should conduct wide-spread investor education programmes on the importance and benefits of dematerialization to the Hong Kong market and how retail investors can achieve dematerialization. <p>¹According to the website of the Hong Kong Exchange and Clearing Limited (HKEx), shares equivalent to 49.19% of the total market cap were held at CCASS as of the end of December 2009.</p> <p><u>Views on the roles of HKSCC Nominees Limited</u></p> <p>Please clearly state any changes to the roles and responsibilities of HKSCC Nominees Limited and the share registrars after the implementation of the proposed scripless model. Please also clarify how the new role of HKSCC Nominees Limited will impact the market with regards to corporate actions services and auto-compensation arrangement in case of failure in Continuous Net Settlement trade.</p> <p>We submit that the current services provided by HKSCC Nominees Limited should continuously be made available to the market directly or through the registrars or an equally adept administrator without compromising the quality of services and requiring additional or significant cost.</p> <p>Furthermore, in case Hong Kong Securities Clearing Company Limited ("Hongkong Clearing") is to act as an agent appointed by CCASS Participants for providing corporate actions service to its participants continuously, there may be concerns from the participants' perspective as they will have to undertake agency risk (since the agent i.e. Hongkong</p>

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		Clearing will be appointed directly by CCASS Participants); whereas corporate actions service is currently provided by Hongkong Clearing as part of its central depository functions and CCASS Participants normally do not undertake depository risk within the existing model.
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?	We agree with the proposal that the formal register should comprise two parts but the certificated sub-register should only exist in the transition period.
7.	Do you agree with the proposal to facilitate name-on-register within CCASS? If not, why not?	We are supportive of this proposal.
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?	<p>In line with the spirit of the proposed scripless model of enhancing overall market efficiency, the Hongkong Clearing and the share registrars should derive a measure for immediate credit arrangement to prevent degradation of the current service standard. We submit that the following issues should be carefully considered in this regard:</p> <ul style="list-style-type: none"> • Turnaround time of dematerialization should not be longer than the current service level i.e. investors should be able to utilize the shares in CCASS on the date of deposit once immediate credit is granted to the CCASS participant. The standard dematerialization turnaround time to be adopted by Hongkong Clearing or the Registrar should not be longer than 24 hours in order to cater for the T+2 settlement cycle in Hong Kong. • Changes, if any, to the procedures for depositing certificated securities into CCASS. • Securities blocking mechanism, if any, during the dematerialization process. • Any charges involved in the process.

No.	Consultation Question	Proposed HKAB's response
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?	We believe that the proposed model can be simplified to avoid confusing investors. Please refer to our comments in question 13.
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?	We agree that 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 aligns with the current arrangement for shareholders who hold their shares in physical form.
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?	<p>We consider that broker/bank/custodian nominees in CCASS should be allowed to appoint both proxies and multiple representatives for the same meeting. This is in line with a key objective of the scripless operating model for enhancing corporate governance by having more investors to participate in proxy voting events.</p> <p>In addition, we would like to understand the procedures in this regard, including the contingency plans in adverse weather situations. We suggest that the appointment should be allowed to be submitted via electronic form. As this is not possible under the existing model, an assessment is required on its feasibility.</p>
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?	While we do not support the proposal of introducing the new account types, i.e. Registrar Participant Accounts (RPA), Issuer Sponsored Accounts (ISA) and CCASS Participant Sponsored Accounts (PSA) (please refer to our comments in question 13 below), if it is decided to proceed with the proposal, we consider that Investor Participant Account (IPA)

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		<p>and ISA would require a unique identification number during the account opening process. However, we believe CCASS Participant Accounts (CPA) and PSA holders would not need a new set of unique identification number given that CPA are already CCASS Participants each with a distinct participant ID, while PSA are directly linked to CPA. The holdings are recorded in the broker/bank/custodian nominee's books at a level one layer down from the holders recorded on the books of the registrar. This has worked well in the existing environment and should continue under the new model.</p>
13.	<p>Do you agree with the proposal to introduce a new Registrar Participant category in CCASS? If not, why not?</p>	<p>We do not see significant benefits deduced from the introduction of the new Registrar Participant category. On the contrary, confusion may be brought about by the additional account layer and types.</p> <p>In addition, we are of the view that the proposal of introducing the new account structures and types (RPA, ISA and PSA) may impact the prevailing operation model adopted by CCASS Participants, particularly those involved in the retail market, in terms of the system capacity in respect of the volume of settlement instructions, as well as the sub-custodian structure of the clients' holdings. The expected increase in the volume of settlement and corporate actions instructions may also impact the system capacity of CCASS. We therefore submit that the proposal should be discouraged, in line with the spirit of the proposed scripless model of enhancing overall market efficiency in the market and avoiding unnecessary cost to be borne by the industry in the form of information technology and operational development by the registrars and Hongkong Clearing.</p> <p>In particular, we would like to point out that we have significant concerns on the potentially</p>

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		<p>huge operational problems that the proposed PSA may cause. For example, it will be difficult to use the approach of PSA for each individual/legal entity for the benefit of tax deduction at sources, e.g. 10% PRC tax, simply because the number of PSA to be opened for individuals is expected to be huge. We also have concerns on the increase of corporate actions instructions due to the introduction of PSA. We therefore consider it impractical to offer PSA due to operational risks and the significant system development and maintenance cost.</p> <p>While we would appreciate elaboration and clarification of the benefits of the new account structure and types to investors, registrars, CCASS and CCASS Participants, according to the explanations given in the Consultation Paper, we note that the handling of an ISA is quite similar to IPA as in the existing model. Essentially, the nature of both account types is to give registered investors legal ownership over assets and direct control over the account's activities. The two notable differences between ISA and IPA are that (i) an ISA will have a holistic view of both certificated and uncertificated shareholdings, which is achieved through accessing either individual share registrar's online system or the Federation of Share Registrars' (Federation) single web-based platform, whereas, IPAs will get access to the same information through the CCASS platform; and (ii) an ISA is not required to pay CCASS custody fees because it is an issuer sponsored account.</p> <p>Technically, the same benefits can be achieved without adding RPA and ISA. The existing infrastructure with the three account types (CPA, CCASS Participant Stock Segregated Accounts (SSA) and IPA) can simply be expanded to cover the new proposed features such as registered legal ownership and direct control over account activities. Below is an example:</p>

No.	Consultation Question	Proposed HKAB's response				
			CPA	SSA (PSA under the proposed scripless model)	IPA (IPA & ISA under the proposed scripless model)	Certificated holdings
		Registered owner	The CCASS Participant ¹	The investor	The investor	The investor
		Account Administrator	CCASS Participant	CCASS Participant	Investor and Investor Participant ²	Investor
		Whether and how can investor view holdings?	No, unless the CCASS Participant provides such facility	Yes, via CCASS Internet System and CCASS Phone System	Yes, via CCASS Internet System, CCASS Phone System, and on-line service provided by the share registrar ³	Yes, through an online service provided by the share registrar
		Must the investor initiate a transfer of the securities to another one of the account types to settle HKEx trades?	No	No	Yes, investor must initiate a transfer of the securities to his executing broker's CPA	Yes, investor must first deposit his securities with his executing broker for dematerialization and credit into the broker's CPA
		¹ Only if the investor is the CCASS Participant. In all other cases, the investor will have a beneficial interest in the securities.				

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		<p>²CCASS can create a new distinction between Investor and Investor Participant, but technically they are the same type of investors.</p> <p>³CCASS and the Federation or the share registrars will have to establish linkage to allow for inter-changing of shareholder information in a timely manner.</p> <p>As indicated in the above table, we believe that the benefits stated in the Consultation Paper can be largely achieved by maintaining the existing three account types within CCASS (i.e. CPA, SSA and IPA), which will keep the cost to the community low and the proposal simple. We also encouraged CCASS and listed companies to use the cost saving from developing and maintaining the new account structures and types to enhance the current IPA to benefit a larger group of investors by including the features of ISA.</p> <p>Separately, since Hongkong Clearing will forward stock holdings position held in CCASS for all types of accounts to share registrars at the end of the day, it may be worth to explore whether it would be appropriate for Hongkong Clearing to also act as the share registrar for all listed companies in Hong Kong, similar to the operating model in the Mainland China i.e. The China Securities Depository and Clearing Corporation Limited performs both clearing and registration roles for the investors. With this model, the Registrar Participant role may not be required.</p>
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,	As share registrars are administrative agents carrying no or limited fiduciary responsibility, it will not be justified if registrars providing scripless related services are more directly and robustly regulated than they are today because this will entail heavy costs to the community such as establishing a separate supervisory body under specific legislation. Unless share

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	why not?	registrars are to become an active component of the model which poses substantial liability on the part of the share registrars, we suggest that share registrars providing scripless related services should render their services according to the best industry practices and standard guidelines uniformly applicable to all share registrars in Hong Kong. This may be achieved, for example, by expanding the existing Code of Conduct for Share Registrars to cover new responsibilities under the proposed model and, if deemed necessary, additional disciplinary penalties determinable by the Share Registrars' Disciplinary Committee.
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?	Please refer to our comments in question 14.
16.	Do you have any views on the proposed changes to the IPO process?	<p>For white form application, we suggest that paper certificates can be maintained in the early stage but they should be dematerialised upon trading. To encourage uncertificated securities, a fee may be imposed on IPO applications opting for paper certificates. In the medium term, all white form application and white form eIPO should only allow for uncertificated securities to be credited to applicants' securities accounts within CCASS to promote scripless usage. There should be a defined timeline in this regard.</p> <p>In addition, investors should be given the option in their IPO application forms to authorize</p>

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		<p>share registrars to open securities accounts within CCASS for crediting any shares allotted. The IPO application form may be modified to request additional information for account opening, such as a photocopy of applicant's Hong Kong Identity Card / passport.</p>
17.	<p>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)?</p>	<p>We agree that the scope of the scripless operational model should extend to all publicly traded securities in Hong Kong but securities which are currently only available in scripless form, such as derivative warrants and CBBCs, should continue to be offered in scripless form only.</p> <p>In addition, as mentioned in our comments in question 13, we submit that the proposal to introduce RPA, ISA and PSA should be discouraged. If, however, it is decided to proceed with the proposal, we suggest that the registrar for derivative warrants and CBBCs can opt out of being a RPA and providing ISA and, accordingly, the uncertificated sub-register will only be available for CPA, PSA and IPA.</p>
18.	<p>If not, to what extent should the scope be limited, and why?</p>	<p>Not applicable.</p>
19.	<p>What are your views on the costs and benefits of introducing a scripless securities market in Hong Kong?</p>	<p>The costs and benefits of introducing a scripless securities market in Hong Kong will depend on the final flow of the process which may impact on all stakeholders. In general, we believe that introducing a scripless securities market will enable Hong Kong to comply with the Group of Thirty (G30) recommendation, in line with the international directive recommended by the Committee on Payment and Settlement Systems (CPSS) and the International Organization of Securities Commissions (IOSCO) 20 years ago. A key point</p>

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		<p>for success is to minimize inconvenience and complication in the process of conversion and implementation. Our specific concerns are set out below:</p> <ul style="list-style-type: none"> • The new model should not generate excessive settlement instructions due to, for example, transfer of securities between different account types. • The new model should not generate excessive corporate actions related instructions due to the introduction of the PSA which may not be fundamental to a scripless environment. • The industry should be provided with a cost analysis in relation to the existence of ISA, including the cost and benefits to CCASS Participants and investors. • With a scripless market the existing scrip fee should be eliminated and consideration should be given by the HKEx to introducing fees at a sufficiently high level for producing and receiving paper scrips. • Charges to CCASS Participants and investors on dematerialization should be as low as practicable. A preferential fee rate can be offered to investors who dematerialize their holdings at an early stage. • Charges to CCASS Participants and investors on various types of instructions/ transactions/ services as a result of the implementation of the new model should be as low as practicable. This includes the Registration Fee currently charged to CCASS participants by Hongkong Clearing. • Resources required for the operational and system changes to cope with the new model should be minimized.
20.	Regarding the dematerialisation of shares and debentures of overseas companies, do you agree	We agree with the proposed approach.

No.	Consultation Question	Proposed HKAB's response
	with the proposed approach to focus first on Bermuda, Cayman Islands, Mainland China and UK companies? If not, why not?	