

## LCQ2: Strengthening the regulation of the capital markets

Following is a question by the Hon Lau Kwok-fan and a written reply by the Acting Secretary for Financial Services and the Treasury, Mr Joseph Chan, in the Legislative Council today (April 21):

Question:

In February this year, the Securities and Futures Commission (SFC) and the Financial Reporting Council (FRC) concluded a new Memorandum of Understanding (MoU) to promote the collaboration between the two parties, thereby strengthening the regulation of the capital markets. According to the MoU, both parties will enhance the areas of collaboration, including case referrals, joint investigations, mutual assistance and capacity building. In this connection, will the Government inform this Council:

- (1) of the circumstances under which FRC will, upon initiating a formal investigation into a listed company, refer the relevant case to SFC;
- (2) of the details of SFC's procedure for handling cases referred to it and the law enforcement actions that it may commence;
- (3) of the scope of actions that SFC and FRC may commence, and whether it includes investigating the conduct of the boards of directors of listed companies and their members, and imposing punishments on those persons involved in non-compliance incidents; if not, of the reasons for that;
- (4) given that SFC and FRC have agreed to notify each other before preparing and issuing policies or guidelines which may bring a significant impact to the regulatory functions of the other party, of the specific examples of such policies or guidelines; and
- (5) whether, apart from concluding the MoU, SFC and FRC have other specific plans to enhance the quality of financial reporting by listed companies and the quality of audit work conducted by auditors of listed companies, and to regularly conduct performance reviews on the relevant work; if so, of the details?

Reply:

President,

My response to the various parts of the question, in consultation with the Securities and Futures Commission (SFC) and the Financial Reporting Council (FRC), is as follows:

- (1) Upon the FRC's initiation of a formal investigation into a listed

company, during the performance of its duties, if the FRC notices any matter which may fall within the regulatory remit of the SFC, the FRC will refer the matter to the SFC for consideration of appropriate follow-up actions.

(2) Upon the FRC's referral of cases, the SFC may initiate an investigation if it has reasonable cause to believe that an offence or misconduct under any of the relevant provisions of the Securities and Futures Ordinance (SFO) may have been committed. The SFC will assess the information provided by the FRC and any other relevant information. If an investigation is initiated and there is sufficient evidence to substantiate the suspected offence or misconduct, the SFC may, after taking into account legal advice and any other relevant factors, decide to take appropriate enforcement actions. The SFC will consider all factors relevant to the pursuit of its regulatory objectives set out in section 4 of the SFO and the performance of its functions set out in section 5 of the Ordinance.

(3) The scope of an investigation and the resulting enforcement actions of the SFC and the FRC, if any, will depend on the circumstances of each case. If it appears to the SFC that market misconduct, such as disclosure of false or misleading information, may have taken place, it may institute proceedings in the Market Misconduct Tribunal (Tribunal) concerning the matter. The Tribunal may make an order to disqualify a person who has been identified as having engaged in market misconduct from being a director of any company in Hong Kong. The Court of First Instance may also, upon an application made by the SFC, disqualify a person from being a director of any company in Hong Kong, if the Court is of the opinion that the business of the affairs of a listed company have been conducted in certain manners, such as involving fraud or other misconduct. If a current director of a listed company is disqualified by the Tribunal or the Court, that person will cease to be a member of the Board of Directors of the company. Whether the Tribunal or the Court will impose such an order will depend on the circumstances of the case, such as the strength of the evidence and the gravity of the misconduct concerned.

The subjects of the FRC's investigation include Public Interest Entities auditors and their registered responsible persons. In addition, the FRC may refer the relevant matter to relevant regulatory bodies for consideration of investigation or disciplinary actions against directors of listed companies as appropriate.

(4) The Memorandum of Understanding (MOU) between the SFC and the FRC provides that each party, as and when it considers appropriate and to the extent practicable and subject to applicable laws, will notify the other party of any issue that the notifying party believes may have a significant implication for the other party. This may include the development and publication of policies and guidelines. Since the MOU came into force in February this year, the two parties have not come across any situation warranting relevant notifications.

(5) The SFC and the FRC hold regular meetings to discuss issues of common interests and explore co-operation initiatives. Both regulators are keen on

collaborating more closely with a view to enhancing the audit quality and financial reporting quality of listed companies and improving corporate governance of these companies.

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## LCQ3: Self-regulation of the legal profession

Following is a question by the Hon Cheung Kwok-kwan and a written reply by the Secretary for Justice, Ms Teresa Cheng, SC, in the Legislative Council today (April 21):

Question:

At the end of last year, the Council of the Law Society of Hong Kong (Law Society) intervened in the operation of a law firm (the firm) pursuant to the relevant legislation. The firm's practice forthwith ceased, and all the money of the firm has been held by the Law Society on trust. Given that the firm, prior to its cessation of practice, was one of the major law firms in Hong Kong engaging in cases of sale and purchase of second-hand property units, more than 150 clients of the firm were affected by the incident (affected clients), and at least \$375 million of clients' money was frozen. Some affected clients have pointed out that they have suffered huge losses as the money they deposited in the firm has been frozen, and that the incident has also illustrated that the self-regulatory regime of the legal profession cannot adequately protect the interests of clients of law firms. In this connection, will the Government inform this Council:

- (1) whether it knows the number of law firms the operation of which was intervened by the Law Society in the past 10 years, and set out in a table for each case (i) the date of intervention, (ii) the name of the law firm, (iii) the number of clients affected, (iv) the total amount of clients' money frozen, and (v) the duration of the intervention;
- (2) of the number of enquiries or requests for assistance, received by the Department of Justice (DoJ) in the past 10 years, from the clients of the law firms which had been intervened, and the follow-up actions taken by DoJ;
- (3) whether DoJ regularly reviewed in the past 10 years if the legislation relating to the self-regulation of the legal profession could dovetail with the current situation, thereby being able to effectively protect the interests of members of the public and clients of law firms; if DoJ did, of the dates and outcome of such reviews; if not, the reasons for that, and whether DoJ will conduct a review immediately; and
- (4) given that in a judgment handed down on February 19 this year on an application for leave to apply for judicial review in relation to the

aforesaid incident, the Court of First Instance of the High Court pointed out that the parties concerned could consider and implement tailor-made, perhaps innovative, solutions seeking to alleviate the harshness of the impact felt by clients of the firm (such as making an early and significant interim payout), and that the Court would remain ready to provide such assistance and directions as might be sought, whether DoJ will follow up on this advice, and discuss with the Law Society solutions for helping the large number of affected clients; if so, of the details; if not, the reasons for that?

Reply:

President,

The Legal Practitioners Ordinance (Cap. 159) (the Ordinance) and its subsidiary legislation provide for the powers and functions of the Law Society of Hong Kong (the Law Society) as the regulatory body for solicitors in Hong Kong. Under the self-regulatory regime for Hong Kong's legal profession, the Law Society must, in compliance with the relevant laws, exercise its powers and perform its functions independently.

The mechanism which provides for the Law Society to intervene into the practice of a law firm is an important regulatory tool under the legislative scheme of the Ordinance. Part IIA of the Ordinance confers the relevant powers on the Law Society with due regard to protection of clients and the public interests. The circumstances under which the Council of the Law Society (the Council) may intervene into a law firm's practice include cases of suspected dishonesty (Note 1), bankruptcy (Note 2), or breaches of other rules made under the Ordinance (Note 3). The progress of an intervention would depend on a number of factors, including the number of clients of the intervened firm, the amount of records of the intervened firm, and whether the files and accounting records are complete.

In the course of intervention, the Council shall, as required by the law, hold all sums of money of an intervened firm on trust for the persons beneficially entitled to them. This is to avoid any misappropriation of such funds in order to protect the interests of the clients and the public. As the trustee of the funds, the Council may apply to the court for directions or determination of any question arising in the execution of a trust (Note 4). The intervention agent, appointed by the Council to assist the intervention, would first verify any claims for return of money paid to an intervened firm and the manner of release of such client money will be subject to authorisation by a court order obtained upon the Council's application to the court.

With regard to various parts of the question, having made enquiries with the Law Society, the Department of Justice (DoJ) replies as follows:

(1) DoJ does not have the information requested in the question. The Law Society, on our enquiries, agreed to disclose the following information.

Between 2011 and 2020, there are in total 23 interventions by the Law Society. The names of such intervened firms and the respective dates of

intervention are listed in Annex.

In respect of the 21 interventions from 2011 to 2019, the Law Society received a total of 979 claims (excluding subsequently withdrawn applications). Regarding the two interventions in 2020 which are still in receipt of claims, the Law Society is unable to provide the respective number of claims at this stage.

In relation to the total amount of frozen client funds, the total relevant amount in respect of the interventions over the past 10 years is approximately HK\$538 million.

The Law Society indicated that according to its record, with regard to the interventions in the past 10 years, it took on average 2 years and 7 months from the date of the intervention to the grant of court orders in relation to disposal and distribution of the relevant funds.

(2) DoJ does not maintain statistics on public enquiries and requests for assistance to DoJ on interventions. Whenever on receipt of enquiries about and comments on the intervention of law firms, DoJ would follow up as appropriate. If necessary, DoJ, having acquired the consent of the relevant persons, would refer the relevant enquiries or comments to the Law Society for follow-up as appropriate.

(3) & (4) In relation to the intervention since December 24, 2020 undertaken by the Law Society mentioned in the question, the Law Society indicated that in deciding whether to exercise its statutory power to intervene into the practice of that intervened firm, the Council had already taken into account all relevant circumstances and the risks to clients' money being misappropriated, and accordingly decided to exercise its statutory power to so intervene.

DoJ understands the impact of such intervention on the clients of the intervened firm, and has since then been in touch with the Law Society. Further, DoJ understands that the Hong Kong Monetary Authority (HKMA) has, since it became aware of the incident, also been closely monitoring the impact of the incident on bank customers and has requested banks to proactively approach affected customers and provide appropriate assistance in a reasonable and accommodating manner. The HKMA is currently studying with the banking industry an alternative payment arrangement for property transactions and the related operational flows and details. The arrangement aims at enabling settlement of the payments of the property mortgage loan proceeds (and other sizable funds) in property transactions without involving funds going through law firms, while preserving the primary roles and legal responsibilities of the various parties in a property transaction (including the buyer, the seller, their respective lawyers, and their respective mortgage banks (if applicable)). This would help minimise any impact on banks and customers in case the operation of a law firm is materially at issue, as well as enhance protection to the parties concerned. The HKMA and the banking industry are actively discussing and following up with the relevant stakeholders (including the Law Society) on the alternative payment arrangement proposal. DoJ is willing to assist when needed.

Besides, in a set of litigation in relation to the aforementioned intervened firm, the court indicated that it would be ready to provide such assistance and directions as may be sought (Note 5).

As the regulatory body of solicitors in Hong Kong, the Law Society has already set up a working group to review the intervention process, and also indicated that it would keep their operation under constant review and is always open to suggestions with a view to improving it. DoJ will continue to maintain communication with the legal industry and other stakeholders in this regard.

Note 1: Section 26A(1)(a) of the Ordinance.

Note 2: Section 26A(1)(d) of the Ordinance.

Note 3: Section 26A(1)(c) of the Ordinance.

Note 4: Order 85, Rule 2(2)(a) of the Rules of the High Court (Cap. 4A).

Note 5: Ng Wing Hung v The Council of the Law Society of Hong Kong (HCAL 70/2021) [2021] HKCFI 379.

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## [LCQ19: Alternative payment mechanism for property transactions](#)

Following is a question by the Hon Chan Chun-ying and a written reply by the Acting Secretary for Financial Services and the Treasury, Mr Joseph Chan, in the Legislative Council today (April 21):

Question:

At the end of last year, the Council of the Law Society of Hong Kong (Law Society) suspected after investigation that a former employee of a law firm (the firm), which took up a significant number of property sale and purchase cases, had dishonestly misappropriated the money of the clients of the firm, and the Law Society intervened in the operation of the firm pursuant to the relevant legislation. The firm's practice forthwith ceased, and all the money of the firm has been held by the Law Society on trust. It has been reported that the firm's clients suffered huge losses because huge sums of money they deposited with the firm for property transactions (including deposit money and mortgage money from banks) were frozen. In order to prevent the occurrence of similar incidents, the Hong Kong Monetary Authority (HKMA), in collaboration with the banking industry, is exploring a payment mechanism for property transactions that does not involve law firms (alternative payment mechanism), with an option under consideration being that the purchaser's bank transfers the major sums of payments involved in a property transaction directly into the vendor's bank account. In this connection, will the Government inform this Council:

(1) if it knows the total amount of money frozen in the past 10 years due to the Law Society's intervention which had been deposited with law firms by their clients for property transactions, as well as the amount and percentage of such money which has now been unfrozen and returned to the clients concerned;

(2) whether HKMA has explored ways to enable the alternative payment mechanism to better ensure, as compared with the existing mechanism, the security of property transactions (e.g. ensuring that the purchaser's solicitor has verified the title prior to the transfer of money by banks); and

(3) whether HKMA has commenced a consultation exercise with the stakeholders on the alternative payment mechanism; if so, the initial views received; if not, when the consultation exercise will commence?

Reply:

President,

Having consulted the Department of Justice and the Hong Kong Monetary Authority (HKMA), my reply to the various parts of the question is as follows:

(1) According to the information provided by the Law Society of Hong Kong (Law Society), there were a total of 23 interventions involving law firms between 2011 and 2020.

In respect of the 21 interventions from 2011 to 2019, the Law Society received a total of 979 claims (excluding those that were subsequently withdrawn). The total amount of admitted claims was about HK\$130 million. For the two interventions in 2020 which are still in receipt of claims, the Law Society is unable to provide the total number of claims at this stage. The Law Society has also indicated that as the intervention agents did not categorise the amount of claims by their nature, it is not able to provide other figures sought in the question.

(2) As noted from the above figures, apart from Messrs. Wong, Fung & Co. whose practice was intervened by the Law Society in December 2020, the past decade also saw other incidents in Hong Kong where clients involved in property and other transactions were affected by law firms with problematic practices. The HKMA is studying with the banking industry an alternative payment arrangement for property transactions and the related operational flows and details. Without prejudice to the roles and responsibilities of the various parties involved in a property transaction (including the buyer, the seller, their respective law firms, and their respective mortgage banks), the new arrangement will allow banks to settle payments of property mortgage loan proceeds and other sizable funds in relation without routing through the accounts of law firms. The proposed arrangement aims at minimising any impact on banks and clients in the event of serious disruption in the operation of a law firm and enhancing protection for the parties involved in a property

transaction. In fact, under special circumstances there are at present certain property transactions in which the mortgage loan proceeds and other related payments are settled using bank cashier's orders without going through accounts of law firms.

(3) The HKMA and the banking industry are closely discussing and following up on the alternative payment arrangement proposal with the relevant stakeholders (including the Law Society and the Consumer Council). From the comments received so far, there was support for the objective of the proposed arrangement to protect various parties in a property transaction; some stakeholders considered that the proposed arrangement should be implemented as soon as practicable; others also suggested the need for the proposed arrangement to cater for property transactions in different scenarios and circumstances with a view to ensuring adequate protection for all the parties involved. The HKMA and the banking industry will take into account the comments received to refine the proposal and firm up the operational flows and details.

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## **Application for local fishing vessel registration under the Fisheries Protection (Amendment) Ordinance 2020 to close soon**

The Agriculture, Fisheries and Conservation Department (AFCD) today (April 21) announced that the application for concerned local fishing vessel registration, Provisional Approval of Registration (PAR) and Certificate of Eligibility for Registration (CER) under the Fisheries Protection (Amendment) Ordinance 2020 (the Ordinance) will be closing on May 5.

The Ordinance empowers the Director of Agriculture, Fisheries and Conservation (DAFC) to exercise discretion, in order to consider registration applications of local fishing vessels that did not possess a valid operating licence on June 15, 2012, but were used or intended to be used for fishing up to June 14 that year.

An AFCD spokesman said, "Some vessel owners who thought that their fishing vessels did not fulfil the above registration requirement might have already sold or disposed of their fishing vessels. Under such circumstances, the DAFC is provided with the discretion in considering issuing a PAR which certifies a right to register a fishing vessel within two years from the issue of the PAR, to eligible vessel owners."

Furthermore, the spokesman noted that those trawler owners whose CER

applications were rejected because of failing the above requirement can also re-apply for a CER if their trawler was used for fishing up to June 14, 2012.

The deadline for applications for concerned local fishing vessel registration, PAR and CER is May 5 this year. Application forms are available on the AFCD website ([www.afcd.gov.hk](http://www.afcd.gov.hk)) and at AFCD headquarters, 8/F Cheung Sha Wan Government Offices, 303 Cheung Sha Wan Road, Kowloon.

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## **LCQ14: Development of data centres**

Following is a question by the Hon Frankie Yick and a reply by the Acting Secretary for Innovation and Technology, Dr David Chung, in the Legislative Council today (April 21):

Question:

In 2012, the Hong Kong Science and Technology Parks Corporation (HKSTPC), which is wholly owned by the Government, introduced concessionary measures to facilitate the development of data centres. Such measures include the granting of dedicated sites in the Industrial Estates (IEs) under the HKSTPC at premiums below the market value for setting up data centres. Some members of the industry have pointed out that as the development of data centre services has become increasingly matured in recent years, this concessionary measure should be cancelled. In this connection, will the Government inform this Council:

(1) whether it knows the number of data centres in Hong Kong and the annual growth rate of such number, in each of the past five years; of (i) the number of sites granted by the Lands Department (LandsD) for constructing data centres and the average land premiums per square foot, as well as (ii) the number of temporary waivers granted by the LandsD for converting industrial buildings into data centres and the total amount of waiver fees exempted, in the past five years;

(2) whether it has assessed if the concessionary measure of granting dedicated sites in IEs has resulted in an unfair competition in the data centre industry; if it has assessed, of the details and whether it can provide this Council with the assessment report; how the Government ensures the healthy and sustainable development of the industry;

(3) of the considerations and criteria based on which the HKSTPC vets and approves applications for dedicated sites for data centres, and whether details of each approved application will be made public in order to enhance transparency; if so, of the details; if not, the reasons for that;

(4) as the current IE policy has stipulated that most enterprises set up in IEs are only allowed to lease the specialised multi-storey industrial

buildings built by the HKSTPC and only under exceptional circumstances will sites be granted to single users to build their own factories, what the relevant exceptional circumstances are;

(5) as it has been reported that some grantees, instead of using the dedicated sites for operating their own data centres, have leased the premises concerned to various data centre operators to earn rents at the market value, whether the HKSTPC has devised new measures to eradicate such an act of profiteering by misusing public resources; and

(6) given that early last year, the Government commenced a review on data centre development in Hong Kong and the relevant concessionary measures, of the progress and preliminary conclusion of the review; when the review outcome will be published?

Reply:

President,

In consultation with the Lands Department (LandsD), our reply to the various parts of the question is as follows:

(1) The setting up or operation of data centre in Hong Kong does not require application to or registration with the Government. We do not have the actual number of data centres in Hong Kong. According to relevant market research, the gross floor area of data centres in Hong Kong has increased from about 465 000 square metres in 2015 to about 743 000 square metres in 2019, representing an average annual growth rate of around 10 per cent.

Over the past five years, the Government has approved a site in Tseung Kwan O designated for high-tier data centre use for \$5.456 billion through open tender. The tender result has been published on the LandsD's website.

With regard to the conversion of existing industrial buildings for data centre use, according to prevailing concessionary measures, the Government will waive the standard waiver fees currently chargeable to applications for conversion of existing industrial buildings to information technology and telecommunications industries use (which include data centres). Over the past five years, the LandsD has issued a total of 22 waivers under this category.

Under general circumstances, the amount of waiver fee payable for the approved applications will depend on the floor area, location, and the proposed use of the premises in question. As the waiver fees for the above uses were already exempted by the Government in accordance with the said initiatives, the Government has not assessed the waiver fees for the above applications.

(2) to (5) The Hong Kong Science and Technology Parks Corporation (HKSTPC) manages and operates the three Industrial Estates (IEs) in Tai Po, Yuen Long and Tseung Kwan O. The pre-2015 arrangement was to grant IE sites to those interested and eligible enterprises to build their industrial production facilities. The relevant arrangement was applicable to all industries, including the site granted by the HKSTPC in 2012 for the development of a

data centre. The HKSTPC does not have preferential measures specifically for data centres.

In 2015, the HKSTPC revised its IE policy under which the HKSTPC would, in general, provide specialised multi-storey and highly-efficient industrial buildings for leasing to multiple users, with a view to encouraging manufacturers to set up their production bases in Hong Kong and attracting high value-added technology industries and manufacturing processes suitable for Hong Kong. However, the HKSTPC will still consider granting sites to single users under exceptional circumstances such as the industry's need for purpose-built factory, the industry's significant contribution to Hong Kong's economic development, etc. However, open tendering would be adopted for invitation of tenders in general.

All along, grantees for admission to the IEs have been selected by the HKSTPC under a rigorous and objective assessment mechanism. Enterprises (including data centres) admitted to the IEs are required to go through HKSTPC's assessment. The prevailing assessment criteria cover the societal and economic benefits brought to Hong Kong by the proposed projects, investment in factory, whether it can create quality jobs, level of product technology, whether or not advanced processes have been introduced, research and development element, sustainability, etc. All applicants are required to submit the relevant investment details, business models and estimated schedule of development to facilitate the assessment of their applications. The above assessment criteria are applicable to different industries including data centres. As the assessment involves commercially sensitive information, the HKSTPC would not announce details of each of the approved applications.

Upon the grant of sites, all grantees in the IEs are required to sign with the HKSTPC a lease agreement that stipulates the rights and responsibilities of both parties including, for instance, only operations approved by the HKSTPC can be carried out at the premises, the required investment in the facilities or machinery of the factories, alienation restriction, prohibition against subletting, terms of surrender and the HKSTPC's rights of factory inspection.

In view of the unique operation model of data centres, the HKSTPC has requested those grantees to provide a proforma service agreement specifying the service level and scope that they provide for their clients, access arrangements to the data centres for security and clients, etc. The proforma service agreement is subject to the approval of the HKSTPC to ensure that no subletting of the premises to data centre clients is involved. The HKSTPC has all along undertaken vigorous lease enforcement actions and conducts regular site inspections of the premises. If a grantee is found to be in breach of the terms and conditions of the lease agreement, the HKSTPC will take appropriate actions.

In sum, the HKSTPC will review its IE development strategy from time to time in the light of technological advancement and market conditions.

(6) Data centre is an essential information and communications technology

(ICT) infrastructure that supports the continuous growth of Hong Kong's digital economy. The Government has been committed to promoting data centre development in Hong Kong by implementing various facilitation measures, including the provision of land, encouraging conversion of industrial buildings and use of industry lots, as well as providing one-stop support services. In early 2020, the Government engaged a consultant to conduct a review on data centre development in Hong Kong, including the concessionary measures implemented by the Government and feedback from the industry. The initial findings of the review were submitted to the Legislative Council Panel on Information Technology and Broadcasting in May 2020, and the review was completed in early 2021. The findings of the review show that the demand for data centre facilities and services in Hong Kong will continue to be driven by global and local technology advancement. The market demand for data centres in Hong Kong is very positive. A considerable number of local and non-local ICT enterprises, including international technology giants, Internet, cloud service and data centre providers will continue to expand their presence in Hong Kong. Industry players generally consider that the concessionary measures are effective in facilitating data centre development, particularly high-tier data centres. They also support the continuous implementation of the concessionary measures by the Government to facilitate data centre development.

The summary of the review report will be uploaded onto the thematic portal ([www.datacentre.gov.hk](http://www.datacentre.gov.hk)) after consolidation for reference by the industry and the public.