

Financial Regulatory Structure in Hong Kong: Looking Forward

Professor Douglas W. Arner
Head, Department of Law
University of Hong Kong
Douglas.Arner@hku.hk

Financial Development

- 1840s-1865: StanChart (1859, 1862)
- 1865-1948: HSBC (1865), HKSE (1891)
- 1948-1987: Banking Ord. (1948, 1964, 1986), crisis (1965, 1973), Securities Ord. (1974), HKFE (1976), HKAB (1980), DTC Ord. (1981), crisis (1982), stock market crash (1987)
- 1987-present: Davison Report (1988), SFC Ord. (1989), HKMA (1993), AFC (1997), HKEx (2000), SFO (2003), IMF FSAP (2003), GFC (2008)

Themes: British Period

- Banking and securities law developed largely in response to (1) crisis experiences and (2) British developments, with a more limited impact from (3) international standards.
- Crisis experiences: especially 1987 and 1991
 - Davison Report (1988): securities law reform – establishment of Securities and Futures Commission (1989)
 - HKMA (1993)
- British developments: less influence following Single European Act (1986)
- International: Basel Committee on Banking Supervision, International Organisation of Securities Commissions
- Overall: frequent reforms

Themes: Post-1997

- Basic Law
- Regulatory independence: HKMA, SFC
- Regulation v. legislation: Banking Ordinance, Securities and Futures Ordinance

Post-1997 Experience

- Crisis response: 1997, 2008 (SFC and HKMA Lehman reports)
- International standards: membership of Financial Stability Forum (1999), Financial Stability Board (2009), Basel Committee (2009)
- International Monetary Fund review (2003)
- Independent reports (Carse, penny stocks)

Hong Kong Financial Law

- Financial Regulatory System
- Key Financial Laws
- Banking
- Securities Regulation
- Insurance

Basic Structure and Principles

- Basic Law: One Country, Two Systems
- Ordinances / Sub-legislation: Statutes / Regulations
- Common Law (plus regulatory guidance)
- Principles
 - Permissive: Permitted unless prohibited
 - Flexible: Contract and courts
 - Open to all unless closed

Basic Law Art. 109

- The [HKSAR Government] shall provide an appropriate economic and legal environment for the maintenance of Hong Kong as an international financial centre.

Financial Regulatory Structure

- Regulatory structure in Hong Kong
 - Sectoral: securities / futures, insurance, pensions
 - Institutional: banking
- Regulatory structure: Options
 - Sectoral (Mainland China, US)
 - Institutional
 - Functional (Australia)
 - Consolidated (UK, Japan, Singapore)
 - Twin Peaks (Netherlands, France)

Regulatory Structure (2)

- Three tier structure
 - Government: Financial Services and the Treasury Bureau (Chief Executive, Financial Secretary, Financial Services Secretary)
 - Regulator
 - Self-regulatory organization (SRO)
- Cooperation / coordination
 - Committees
 - MoUs (Memoranda of Understanding: interagency, agency / SRO, domestic / foreign / Mainland)
- Financial Sector Assessment 2003 (IMF)

Regulatory Structure (3)

- Central Bank: Hong Kong Monetary Authority (HKMA)
- Banking
 - HKMA
 - HK Deposit Protection Board (HKDPB)
 - Hong Kong Association of Banks (HKAB)
- Securities / futures
 - Securities and Futures Commission (SFC)
 - Hong Kong Exchanges and Clearing (HKEx)
- Insurance
 - Office of the Commissioner of Insurance (OCI)
 - Hong Kong Federation of Insurers (HKFI)
- Pensions: Mandatory Provident Fund Schemes Authority (MPFA)
- Others: Financial Reporting Council (FRC), Companies Registry, Independent Commission Against Corruption (ICAC), Consumer Council

Council of Financial Regulators

- FS (chair), FSTB, HKMA, SFC, OCI, MPFA
- Objectives:
 - Contributing to the efficiency and supervision of financial institutions
 - Promotion and development of Hong Kong's financial markets
 - Maintenance of financial stability

Financial Stability Committee

- FSTB (chair), HKMA, SFC, OCI
- Objectives:
 - Monitoring the functioning of the financial system in Hong Kong
 - Deliberating on issues with possible cross-market and systemic implications and formulating and coordinating responses,
 - Reporting to the Financial Secretary as necessary

Main Financial Laws in Hong Kong

- Basic Law
- Exchange Fund Ordinance
- Banking Ordinance
- Clearing and Settlement Systems Ordinance
- Deposit Protection Schemes Ordinance
- Companies Ordinance
- Securities and Futures Ordinance
- Insurance Companies Ordinance
- Mandatory Provident Funds Schemes Ordinance
- Occupational Retirement Schemes Ordinance
- Plus: FRC Ordinance, Money Lenders Ordinance etc

The Global Financial Crisis: Consequences in Hong Kong

- Bank of East Asia
- AIG
- CITIC Pacific
- Lehman Brothers / Minibonds

Current Issues

- Post-crisis financial regulatory reform
- Competitiveness
- Yuan finance
- Institutional structure

G20/FSB Financial Regulatory Reform Agenda

- Capital, leverage, liquidity and procyclicality
- OTC derivatives
- SIFIs and resolution regimes
- Compensation arrangements
- Expanding the regulatory perimeter: Shadow banking
 - Credit ratings and credit rating agencies
 - Hedge funds
 - Securitisation
- Accounting standards
- Macroprudential frameworks
- Adherence to international standards: FSB, peer review (G20, FSB), IMF Art. IV, IMF/World Bank FSAP
- Plus: international institution reform (esp. IMF)

Regulatory structure: Options

- Sectoral (Mainland China, US)
- Institutional
- Functional (Australia)
- Consolidated (UK, Singapore)
- Twin Peaks (UK, Netherlands, France)

Useful References

- D. Arner, B. Hsu, A. Da Roza, F. Da Roza, S. Johnstone & P. Lejot, “The Global Financial Crisis and the Future of Financial Regulation in Hong Kong”, AIIFL Working Paper No. 4 (Feb. 2009) (available at www.aiifl.com and ssrn)
- R. Buckley & D. Arner, *From Crisis to Crisis: The Global Financial System and Regulatory Failure* (London: Kluwer 2011)