

**LEGISLATIVE COUNCIL BRIEF**

**BANKING ORDINANCE**

**(AMENDMENT OF SEVENTH SCHEDULE) NOTICE 2001**

**INTRODUCTION**

At the meeting of the Executive Council on 5 June 2001, the Council **ADVISED** and the Chief Executive **ORDERED** that the Banking Ordinance (Amendment of Seventh Schedule) Notice 2001 (“the Notice”), at the **Annex**, should be made under section 135(1) of the Banking Ordinance, so that share premium could be taken into account in assessing whether a company applying for authorization satisfies the capital requirements stipulated in that Schedule.

**BACKGROUND AND ARGUMENT**

**The Seventh Schedule to the Ordinance**

2. Under section 16(2) of the Ordinance, the Monetary Authority shall refuse an application for authorization if any one or more of the criteria set out in the Schedule to the Ordinance applicable to or in relation to the applicant are not fulfilled.

3. Paragraph 6 of the Seventh Schedule to the Ordinance (“the Schedule”) imposes the following requirements in respect of the capital of an applicant for authorization -

- (a) in the case of a company incorporated in Hong Kong seeking authorization to carry on banking business in Hong Kong, its paid-up share capital must be not less than \$150,000,000 or an equivalent amount in any other approved currency;
- (b) in the case of a company seeking authorization to carry on a deposit-taking business as a deposit-taking company, its paid-up share capital must be not less than

\$25,000,000 or an equivalent amount in any other approved currency; and

- (c) in the case of a company seeking authorization to carry on a deposit-taking business as a restricted licence bank, its paid-up share capital must be not less than \$100,000,000 or an equivalent amount in any other approved currency.

4. Accordingly, only paid-up share capital will be taken into account in assessing whether an applicant satisfies the stated capital requirements. Other items under shareholders' fund in the balance sheet, including share premium, cannot be counted.

5. In processing applications for authorization, the Monetary Authority has experienced difficulties with the above capital requirement in that an applicant's paid-up share capital is below the level specified in the Schedule, although it has a huge balance in its share premium account. At the same time, the applicant concerned fully satisfies the financial requirements in its home jurisdiction where the licensing requirements include both issued share capital and unimpaired reserves (i.e. including share premium). In light of this, it is necessary to review whether the existing capital requirements in the Schedule remain appropriate.

### **Share premium**

6. Share premium arises from the accounting treatment of proceeds resulting from the issue of shares. It is a generally accepted accounting practice that proceeds of share issue that are attributable to the nominal value of the shares concerned are booked as paid-up share capital. On the other hand, proceeds attributable to the difference between the actual issue price and the nominal value of the shares concerned are booked as share premium.

7. Like paid-up share capital, reduction of share premium is subject to stringent requirements specified in the Companies Ordinance (Cap. 32). Share premium thus has a high degree of permanence comparable to paid-up share capital<sup>1</sup>. Therefore, both paid-up share capital and share premium are useful indicators of the financial strength

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<sup>1</sup> Section 48B(1) of the Companies Ordinance states that the provisions in that Ordinance relating to the reduction of the share capital of a company shall, save for some minor exceptions, apply to a share premium account as if the share premium account were paid-up share capital of the company.

of a company. Other items under shareholders fund such as reserves are relatively less stable in the sense that they can be distributed to shareholders readily.

### **Comparison with practices in other financial centres**

8. Compared with other financial centres, the authorization criteria in the Ordinance in respect of minimum paid-up capital requirements appear to be more restrictive. In Europe, the authorization conditions are harmonised on the basis of a banking directive which explicitly states that capital includes share premium. In the U.S., there is no law requiring banks to maintain a minimum amount of paid-up capital. In assessing banks' capital adequacy, the U.S. regulators will take into account all capital components including paid-up share capital and share premium.

### **Proposed amendment**

9. Given that share premium has a comparable degree of permanence to paid-up share capital, it is recommended that paragraph 6 of the Schedule be amended so that the Monetary Authority will take into account share premium in assessing whether an applicant meets the statutory capital requirements. This would enable institutions which have strong capital base, albeit in the form of share premium, to conduct banking or deposit-taking business in Hong Kong.

10. We note that other jurisdictions may have more relaxed treatment for share premium. The proposed amendments will therefore specify that where an applicant for authorization is incorporated outside Hong Kong, its share premium account irrespective of the name by which it is identified or described must have the same characteristics as in the case in Hong Kong (i.e. the reduction of balance in such share premium account is subject to equally stringent requirements).

### **THE NOTICE**

11. Under section 135(1) of the Ordinance, the Chief Executive in Council may, by notice in the Gazette, amend the Schedule.

12. The Notice at Annex will amend the Schedule so that share premium account will be counted in assessing whether an applicant for authorization meets the capital requirements specified in paragraph 6 of the Schedule.

### **LEGISLATIVE TIMETABLE**

13. The Banking Ordinance (Amendment of Seventh Schedule) Notice 2001, being subsidiary legislation, will come into operation when it is published in the Gazette on 8 June 2001. The Notice will be tabled at the Legislative Council on 13 June 2001 for negative vetting.

### **BASIC LAW IMPLICATIONS**

14. The Department of Justice advises that the Notice is consistent with the Basic Law.

### **HUMAN RIGHTS IMPLICATIONS**

15. The Department of Justice advises that the Notice has no human rights implications.

### **BINDING EFFECT OF THE LEGISLATION**

16. The Notice does not affect the current binding effect of the existing provisions of the Ordinance.

### **FINANCIAL AND STAFFING IMPLICATIONS**

17. There are no financial or staffing implications for Government.

### **ECONOMIC IMPLICATIONS**

18. The amendment is conducive to maintaining Hong Kong's status as an international financial centre. It will enable financial institutions with strong capital base, albeit in the form of share premium, to conduct banking or deposit-taking business in Hong Kong, and bring

the authorization requirements in Hong Kong more in line with the practices in other financial centres.

## **PUBLIC CONSULTATION**

19. We have consulted the Hong Kong Association of Banks and the DTC Association. They do not have any objection to the proposed amendment.

## **PUBLICITY**

20. The Monetary Authority will issue a circular letter to authorized institutions informing them of the change.

## **ENQUIRIES**

21. Enquiries may be directed to Miss Clara Tang, Principal Assistant Secretary for Financial Services at 2529 0121.

**Financial Services Bureau**  
**8 June 2001**

**BANKING ORDINANCE (AMENDMENT OF SEVENTH SCHEDULE) NOTICE  
2001**

(Made by the Chief Executive in Council under section 135(1)  
of the Banking Ordinance (Cap. 155))

**1. Minimum criteria for authorization**

The Seventh Schedule to the Banking Ordinance (Cap. 155) is amended -

(a) in paragraph 1(1), by adding -

""share premium account" (股份溢價帳) —

- (a) in relation to a company incorporated in Hong Kong, means a share premium account referred to in section 48B(1) of the Companies Ordinance (Cap. 32) maintained in respect of the company;
- (b) in relation to a company incorporated outside Hong Kong, means an account having the same characteristics of a share premium account referred to in section 48B(1) of the Companies Ordinance (Cap. 32) irrespective of its name;"

- (b) in paragraph 6(a), (b) and (c), by repealing "its paid-up share capital" and substituting "the aggregate amount of its paid-up share capital and the balance of its share premium account".

Clerk to the Executive Council

COUNCIL CHAMBER

2001

**Explanatory Note**

This Notice amends the Seventh Schedule to the Banking Ordinance (Cap. 155) so that share premium can be taken into account in assessing whether a company applying for authorization satisfies the capital requirements stipulated in paragraph 6 of that Schedule.