

LEGISLATIVE COUNCIL BRIEF
CITIC Ka Wah Bank Limited (Merger) Bill

INTRODUCTION

The Chief Executive granted his consent for the Bill to be introduced before the Legislative Council on 17 May 2002. This Bill is introduced under Article 74 of the Basic Law by Legislative Council member, Dr. Hon. David Li Kwok-po. The Bill was considered by the Financial Affairs Panel of the Legislative Council on 9 April 2002 and no objections to the Bill were raised.

BACKGROUND AND ARGUMENT

2. The Bill provides for the downward merger of CITIC Ka Wah Bank's banking business with that of the Hongkong Chinese Bank. The Hongkong Chinese Bank is a wholly-owned subsidiary of CITIC Ka Wah Bank. As CITIC Ka Wah Bank is listed on the Hong Kong Stock Exchange, the intention of the merger is to allow CITIC Ka Wah Bank to consolidate its banking business in the Hongkong Chinese Bank whilst becoming a financial holding company. After the merger, CITIC Ka Wah Bank will have its banking licence revoked and will change its name. CITIC Ka Wah Bank will, however, continue to be listed on the Hong Kong Stock Exchange.

3. In a number of jurisdictions, such as the United States, Japan and Switzerland, two banks can merge with one another by way of "universal succession". However Hong Kong company law does not have such a concept as universal succession. Accordingly, bank mergers in Hong Kong may only be effected either by transfer of property and liabilities by way of novation or assignment or by introducing a Bill to the Legislative Council which transfers the property and liabilities of the merging bank. Given the large number of

outstanding banking related agreements between CITIC Ka Wah Bank and its customers, it is not practical to transfer such assets and liabilities by way of novation and assignment to the Hongkong Chinese Bank.

4. It is the Government's stated policy to support the consolidation of the banking sector in Hong Kong, which should improve its competitiveness and contribute to systematic stability in the longer term. As part of this policy, the Government has previously supported bank mergers where reasonable proposals are submitted for consideration. This is, however, always subject to the overriding aim to promote the stability of the banking system and to provide an appropriate degree of protection to depositors. The Hong Kong Monetary Authority has no objection to the proposed merger of CITIC Ka Wah Bank's banking business being effected by way of a private bill such as the Bill.

5. The Bill has advantages for CITIC Ka Wah Bank's customers. Customers will have the reassurance that all Hong Kong law governed property and liabilities of CITIC Ka Wah Bank have been properly transferred to the Hongkong Chinese Bank. Customers of CITIC Ka Wah Bank will also not be inconvenienced by having to sign new customer documentation. Further, the basis of the transfer of the Hong Kong law governed property and liabilities between CITIC Ka Wah Bank and Hongkong Chinese Bank will be publicly known and uniform. In addition, following the merger, the consolidated surviving bank should be financially stronger, contributing to the stability of the banking sector in Hong Kong.

6. The Bill also has advantages for CITIC Ka Wah Bank's shareholders. The banking business of two banks within the CITIC Ka Wah Bank group will be combined within a single bank, the Hongkong Chinese Bank, facilitating economies of scale. CITIC Ka Wah Bank will be better able to conduct its affairs, as a listed company in the interests of its shareholders, as a financial holding company rather than as a bank. The Hongkong Chinese Bank will remain a wholly owned subsidiary of CITIC Ka Wah Bank following the merger. In the interests of both CITIC Ka Wah Bank's depositors and shareholders, CITIC Ka Wah Bank will be required, as a precondition to the revocation of its banking licence under the Banking Ordinance, to

satisfy the Hong Kong Monetary Authority that all non Hong Kong law governed, banking related properties and liabilities (not otherwise transferred by the Bill) are adequately and satisfactorily transferred on a case by case basis to the Hongkong Chinese Bank. Assuming the Hong Kong Monetary Authority is satisfied of the foregoing, the merger will proceed. It is proposed that the appointed day of the merger occurs later this year and prior to the year end. CITIC Ka Wah Bank will agree the appointed day with the Hong Kong Monetary Authority and this will, subject to the Hong Kong Monetary Authority's discretion, be concurrent with the revocation of CITIC Ka Wah Bank's bank licence.

7. Since the early 1980s the Legislative Council has passed fifteen ordinances implementing mergers of banks and other authorised institutions. The Bill is based on the form of the four most recent bank merger ordinances enacted by the Legislative Council over the course of the last year.

THE BILL

8. The purpose of the Bill is to transfer the undertaking of CITIC Ka Wah Bank to the Hongkong Chinese Bank. Both banks are licensed under the Banking Ordinance and are incorporated in Hong Kong.

9. The Bill provides for the vesting of the undertaking of CITIC Ka Wah Bank in the Hongkong Chinese Bank on the appointed day. The key provisions of the Bill are summarised in the following paragraphs.

10. **Clause 2** sets out the definitions of certain terms used in the Bill. In particular, there is a definition of "excluded property and liabilities" which follows the same formulation used in The Bank of China (Hong Kong) Limited (Merger) Ordinance. Sub-paragraph (d) of this definition permits the board of directors of CITIC Ka Wah Bank to resolve that certain property and liabilities (subject to the agreement of the Hongkong Chinese Bank) are excluded from being included in the undertaking of CITIC Ka Wah Bank for the purposes of the Bill. The

effect of this provision is that CITIC Ka Wah Bank may exclude non-banking assets from being transferred to the Hongkong Chinese Bank.

11. **Clause 3** provides that the board of directors of CITIC Ka Wah Bank may determine an appointed day upon which the merger will take effect and that such appointed day must be notified by both CITIC Ka Wah Bank and the Hongkong Chinese Bank in the Gazette.

12. **Clause 4** provides that both CITIC Ka Wah Bank's and Hongkong Chinese Bank's name be changed on the appointed day and CITIC Ka Wah Bank's banking licence be revoked on a day determined by the Hong Kong Monetary Authority and notified in the Gazette. CITIC Ka Wah Bank's name will be changed to "CITIC International Financial Holdings Limited 中信國際金融控股有限公司" and Hongkong Chinese Bank's name will be changed to "CITIC Ka Wah Bank Limited 中信嘉華銀行有限公司". **Clause 4** is similar to the same provision in the Dao Heng Bank Limited Ordinance.

13. **Clause 5** is the main transfer and vesting provision in the Bill. It provides that the undertaking of CITIC Ka Wah Bank (not including the "excluded assets and liabilities") shall transfer to and vest in the Hongkong Chinese Bank as if the Bank were the same person in law as CITIC Ka Wah Bank upon the appointed day.

14. **Clause 6** deals with property which, before the merger, is held by CITIC Ka Wah Bank in a capacity as a trustee. It provides that in such case, the relevant document should be read as if references to CITIC Ka Wah Bank were references to the Hongkong Chinese Bank.

15. **Clause 7(a) to (k)** provides that all contracts and agreements made with, given to or by or addressed to CITIC Ka Wah Bank (being transferred by the Bill) shall, after the merger takes effect, be construed as if the Hongkong Chinese Bank had been the original party instead of CITIC Ka Wah Bank and, accordingly, all references CITIC Ka Wah Bank must be construed as if they were to the Hongkong Chinese Bank. **Clause 7(a) to (k)** also provides for accounts, negotiable instruments, powers of attorney, security, court orders, arbitration awards and judgements to be transferred to the Hongkong Chinese Bank upon the appointed day. **Clause 7(g)(v) and**

(vi) are provisions which seek to reflect previous concerns in respect of other bank mergers (first raised by the Hon. Albert Ho Chun-yan) regarding the possible increase of security or charges over customers' assets as a result of the merger. These provisions seek to ensure that Hongkong Chinese Bank's existing charges and security interests will not be expanded over assets previously held by CITIC Ka Wah Bank of a common customer of both the Hongkong Chinese Bank and CITIC Ka Wah Bank.

16. **Clause 7(l)** deals with data privacy issues under the Personal Data (Privacy) Ordinance. It provides that the Privacy Commissioner may exercise in respect of the Hongkong Chinese Bank any power which he may, before the merger, have exercised in respect of CITIC Ka Wah Bank. It also provides that the transfer of personal data from CITIC Ka Wah Bank to Hongkong Chinese Bank under the Bill shall not result in a breach of any duty of confidentiality or a contravention of the Personal Data (Privacy) Ordinance.

17. **Clause 8** provides for the accounting treatment of the Hongkong Chinese Bank following the transfer of CITIC Ka Wah Bank's undertaking to it. It provides that the balance sheets and profit and loss accounts of CITIC Ka Wah Bank and Hongkong Chinese Bank for the accounting period of each company in which the appointed day falls shall be prepared in all respects as if the undertaking had vested in Hongkong Chinese Bank on the first day of such accounting period of Hongkong Chinese Bank.

18. **Clause 9** provides for the taxation arrangements following the transfer of the undertaking of CITIC Ka Wah Bank to Hongkong Chinese Bank. **Clause 9** also provides that only a single profits tax computation shall be prepared by Hongkong Chinese Bank in respect of the profits and losses of CITIC Ka Wah Bank and Hongkong Chinese Bank in respect of the year of assessment the basis period for which the transfer of the undertaking takes place. **Clause 9** is intended to have similar effect as the provisions dealing with taxation matters in previous bank merger ordinances. The effect of this provision is consistent with Government policy on taxation, as stated in the context of recently enacted bank merger ordinances and in its Information Note to the

Financial Affairs Panel dated 9 April 2002 [CB(1)1408/01-02(03)] in respect of the Bill.

19. **Clause 10** provides that, in respect of all CITIC Ka Wah Bank's contracts of employment with those employees who are transferred to the Hongkong Chinese Bank at the merger, such contracts shall be deemed for all purposes to be a single continuing employment. **Clause 10** also provides that no directors, secretary or auditor of CITIC Ka Wah Bank shall, by virtue of the merger only, automatically become a director, secretary or auditor of Hongkong Chinese Bank. Not all employment contracts (and therefore employees) of CITIC Ka Wah Bank are intended to be transferred to Hongkong Chinese Bank, although most will be. The number of employees who will be excluded and so who will remain with CITIC Ka Wah Bank will be approximately 40, whilst all of the other staff (approximately 950 in total) will be transferred to the Hongkong Chinese Bank.

20. **Clause 11** ensures that CITIC Ka Wah Bank employees who are members of pension fund schemes of CITIC Ka Wah Bank shall continue to be members of those schemes notwithstanding the transfer of their respective employment to the Hongkong Chinese Bank at the merger. It ensures that former employees of CITIC Ka Wah Bank and existing employees of the Hongkong Chinese Bank shall continue to enjoy the same rights following the merger as before the merger under their respective pension fund schemes and that the merger shall not automatically bestow any additional entitlements to such employees.

21. **Clause 12** prevents the merger of CITIC Ka Wah Bank with the Hongkong Chinese Bank constituting an event of default or a termination event in a contract or agreement to which any of CITIC Ka Wah Bank or the Hongkong Chinese Bank or their respective subsidiaries is a party.

22. **Clauses 13 to 15** set out provisions dealing with evidence and the admissibility of evidence in respect of any matter for or against CITIC Ka Wah Bank which, after the merger, becomes admissible in evidence in respect of the same matter for or against the Hongkong Chinese Bank. **Clause 14** provides that, for the purposes of the

Evidence Ordinance, banker's records of CITIC Ka Wah Bank vested in Hongkong Chinese Bank by the Bill shall be treated as if these were always banker's records of Hongkong Chinese Bank.

23. **Clause 16** deals with the effect of the merger on interests in land in Hong Kong held by CITIC Ka Wah Bank and provides that the vesting of CITIC Ka Wah Bank's interests in land in the Hongkong Chinese Bank pursuant to the merger does not constitute an acquisition, assignment, transfer or parting with possession under the Landlord and Tenant (Consolidation) Ordinance. **Clause 16** also provides that the vesting in the Hongkong Chinese Bank of CITIC Ka Wah Bank's interests in land under the merger will not affect or extinguish any priority under the Land Registration Ordinance. **Clause 16(3)** of the Bill automatically amends the registrations of property interests in the name of CITIC Ka Wah Bank, which are not transferred to Hongkong Chinese Bank by the Bill, to refer to its new name in order to distinguish legal title to such interests from Hongkong Chinese Bank (when its name is changed by the Bill to "CITIC Ka Wah Bank Limited") at the appointed day. For the avoidance of doubt, the Bill also states that nothing in **Clause 16** exempts either Hongkong Chinese Bank or CITIC Ka Wah Bank from the provisions of the Stamp Duty Ordinance.

24. **Clause 17** states that nothing in the Bill shall exempt either CITIC Ka Wah Bank or the Hongkong Chinese Bank from any of the provisions of the Banking Ordinance and other ordinances regulating the carrying on of their businesses.

25. **Clause 18** provides that the Bill does not prevent the Hongkong Chinese Bank amending its memorandum and articles of association or dealing with its property or business generally. **Clause 18** also provides that nothing in the Bill prevents CITIC Ka Wah Bank doing the same before the merger.

26. **Clause 19** provides that nothing in the Bill once enacted shall affect the rights of the Central Authorities or the Government under the Basic Law and other laws.

LEGISLATIVE TIMETABLE

27. The proposed legislative timetable is as follows -

Financial Affairs Panel	9 April 2002
Publication in the Gazette for the first time	3 May 2002
Publication in the Gazette for the second time	10 May 2002
Member in charge of the Bill gives notice of intention to present the Bill to the Clerk of the Legislative Council	17 May 2002
First Reading and commencement of Second Reading debate	29 May 2002
House Committee	31 May 2002
Resumption of Second Reading, Committee Stage and Third Reading	To be notified

ECONOMIC IMPLICATIONS

28. The Bill facilitates the merger of the banking business of CITIC Ka Wah Bank with that of the Hongkong Chinese Bank. The consolidation of the banking sector in Hong Kong, such as that facilitated by the Bill, should improve its competitiveness and contribute to systematic stability in the longer term to the advantage of Hong Kong's economy.

PUBLIC CONSULTATION

29. The Bill effects the merger of CITIC Ka Wah Bank with the Hongkong Chinese Bank, which is a wholly owned subsidiary of

CITIC Ka Wah Bank. No public consultation has been conducted. However, the Financial Affairs Panel have considered the Bill and each of the Hong Kong Monetary Authority, Financial Services Bureau, Department of Justice, Inland Revenue Department, Companies Registry, Lands Registry, Securities and Futures Commission and Office of the Privacy Commissioner for Personal Data have reviewed and commented upon the Bill.

PUBLICITY

30. The Bill was published in the Gazette on 3 and 10 May 2002 and notice of the Bill has been given by way of advertisements in the South China Morning Post and the Hong Kong Economic Times on 7 and 10 May 2002. CITIC Ka Wah Bank will also make an announcement pursuant to Hong Kong Stock Exchange Listing Rules. In addition a further press release will be issued by CITIC Ka Wah Bank upon completion of the legislative process.

ENQUIRY

31. Enquiries on this Brief may be directed to Dr. Hon. David Li Kwok-po at 2842 3449.

17 May 2002