

立法會
Legislative Council

LC Paper No. CB(1)996/05-06
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by the Administration)

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Panel on Financial Affairs

Minutes of special meeting
held on Wednesday, 14 December 2005 at 8:30 am
in Conference Room A of the Legislative Council Building

- Members present** : Hon Bernard CHAN, JP (Chairman)
Hon Ronny TONG Ka-wah, SC (Deputy Chairman)
Hon James TIEN Pei-chun, GBS, JP
Dr Hon David LI Kwok-po, GBS, JP
Hon James TO Kun-sun
Hon CHAN Kam-lam, SBS, JP
Hon SIN Chung-kai, JP
Hon Emily LAU Wai-hing, JP
Hon Abraham SHEK Lai-him, JP
Hon Jeffrey LAM Kin-fung, SBS, JP
Hon WONG Ting-kwong, BBS
Hon CHIM Pui-chung
Hon Albert Jinghan CHENG
- Members attending** : Hon WONG Kwok-hing, MH
Hon Alan LEONG Kah-kit, SC
Hon LEUNG Kwok-hung
- Members absent** : Ir Dr Hon Raymond HO Chung-tai, S.B.St.J., JP
Hon LEE Cheuk-yan
Hon Andrew LEUNG Kwan-yuen, SBS, JP
Hon TAM Heung-man

- Public officers attending** : Mr Michael M Y SUEN, GBS, JP
Secretary for Housing, Planning and Lands
- Mr TAM Wing-pong, JP
Acting Permanent Secretary for Housing, Planning and Lands
(Housing)
- Mr Kenneth MAK, JP
Deputy Director (Corporate Services)
Housing Department
- Ms L K LAM
Assistant Director (Divestment)
Housing Department
- Mr Kevin HO, JP
Permanent Secretary for Financial Services and the Treasury
(Financial Services)
- Attendance by invitation** : Mrs Alexa LAM
Executive Director, Intermediaries and Investment Products
Securities and Futures Commission
- Ms Alice LAW
Director, Intermediaries and Investment Products
Securities and Futures Commission
- Mr Richard WILLIAMS
Head, Listing Division
Hong Kong Exchanges and Clearing Limited
- Clerk in attendance** : Miss Salumi CHAN
Chief Council Secretary (1)5
- Staff in attendance** : Ms Connie SZETO
Senior Council Secretary (1)4
- Ms May LEUNG
Legislative Assistant (1)8
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I. Financial issues related to the listing of the Link Real Estate Investment Trust

(Papers for this special meeting)

- LC Paper No. CB(1)514/05-06(01) — Paper provided by the Housing, Planning and Lands Bureau

- LC Paper No. CB(1)514/05-06(02) — Paper provided by the Securities and Futures Commission

- LC Paper No. CB(1)514/05-06(03) — Letter dated 12 December 2005 from the Chairman of the Board of Directors, The Link Management Limited, including:
 - Annex 1: Appendix 4 of the Company's Corporate Governance Policy
 - Annex 2: Press statement issued by The Link Management Limited on 9 December 2005
 - Annex 3: Press statement issued by Deutsche Bank on 9 December 2005

- LC Paper No. CB(1)514/05-06(04) — Extracts from the Securities and Futures Commission's Code on Real Estate Investment Trusts (June 2005), including:
 - Explanatory notes
 - General principles
 - Effect of breach of the Code
 - Chapters 8, 9 and 10
 - Appendices B and D

- LC Paper No. CB(1)514/05-06(05) — Press release issued by the Housing Authority on 8 December 2005

LC Paper No. CB(1)514/05-06(06) — Statement issued by The Link Management Limited on 8 December 2005

LC Paper No. CB(1)524/05-06(01) — Relevant press cuttings from 26 November to 13 December 2005

Paper for the House Committee meeting on 9 December 2005

LC Paper No. CB(1)514/05-06(07) — Letter dated 9 December 2005 from Hon Albert CHENG to the Chairman of the House Committee

Papers for the special meeting of the Panel on Housing on 20 October 2005

LC Paper No. CB(1)62/05-06(01) — Background brief on “Divestment of Housing Authority's Retail and Car-parking Facilities” prepared by the Legislative Council Secretariat

LC Paper No. CB(1)514/05-06(08) — Opening statement by the Secretary for Housing, Planning and Lands

LC Paper No. CB(1)62/05-06(03) — Paper provided by the Administration

LC Paper No. CB(1)62/05-06(02) — Letters dated 4 and 7 October 2005 from Hon Albert CHAN to the Administration

LC Paper No. CB(1)108/05-06(01) — Administration's written reply to Hon Albert CHAN's two letters)

Purpose of the meeting

The Chairman advised that pursuant to the decision of the House Committee on 9 December 2005, the special meeting of the Panel on Financial Affairs (FA Panel) was arranged for Members to discuss the financial issues related to the listing of The Link Real Estate Investment Trust (The Link REIT). He drew Members' attention that in response to the Panel's invitation, Mr Paul CHENG, Chairman of the Board of Directors of The Link Management Limited (The Link), had indicated in his reply dated 12 December 2005 that due to short notice and his prior commitment in China, he was unable to attend the meeting.

Declaration of interest

2. The Chairman reminded Members that in accordance with Rule 83A of the Rules of Procedure of the Legislative Council (LegCo), a Member should not move any motion relating to or speak on a matter in which he had a pecuniary interest, whether direct or indirect, except where he had disclosed the nature of that interest. The Chairman declared interest that his company was a unit-holder of The Link REIT.

3. Mr SIN Chung-kai declared interest that he was a member of the Supervisory Group on Divestment established by the Housing Authority (HA) to steer and monitor the divestment project of HA's retail and car-parking (RC) facilities.

Papers for the meeting

4. The Chairman drew Members' attention to the relevant papers listed on the agenda, in particular the following papers:

- (a) Paper provided by the Housing, Planning and Lands Bureau (HPLB) (LC Paper No. CB(1)514/05-06(01));
- (b) Paper provided by the Securities and Futures Commission (SFC) (LC Paper No. CB(1)514/05-06(02)); and
- (c) Reply dated 12 December 2005 from Mr Paul CHENG, Chairman of the Board of Directors of The Link to the Clerk to FA Panel (LC Paper No. CB(1)514/05-06(03)).

5. The Secretary for Housing, Planning and Lands (SHPL) pointed out that the Administration had received a copy of the letter dated 13 December 2005 from Mr Paul CHENG to the Clerk to FA Panel. The letter, which was subsequently sent to the LegCo Secretariat, was tabled at the meeting.

(Post-meeting note: The letter dated 13 December 2005 from Mr Paul CHENG, Chairman of the Board of Directors of The Link, was issued to members of the Panel and non-Panel Members vide LC Paper No. CB(1)532/05-06(01) on 14 December 2005.)

Discussion on regulation of REITs

6. Mr SIN Chung-kai enquired about the differences between the regulatory requirements for REITs and listed companies in respect of share interest disclosure and the regulatory requirements for directors and senior officers. He also enquired whether the SFC would consider reviewing the disclosure regime for REITs in the light of recent market developments.

7. Mrs Alexa LAM, Executive Director, Intermediaries and Investment Products, the SFC advised that REITs were not subject to the existing share interest disclosure regime under the Securities and Futures Ordinance (SFO) (Cap. 571), which required shareholders to disclose interest of 5% or more shareholdings in a listed company. In drawing up the Code on REIT (REIT Code), consideration had been given to the question of whether REITs should be subject to the same disclosure regime applicable to listed companies. In this connection, the SFC was mindful of the need to strike a proper balance between enhancing the transparency of shareholding interests and minimizing compliance cost. According to the REIT Code, a REIT was structured as a unit trust governed by the provisions of a Trust Deed. As a unit trust, REIT had to appoint an independent Trustee and be managed by a REIT Manager licensed and monitored by the SFC. Under the Trust Deed of The Link REIT, a person having an interest in 10% or more of all the units in issue was a “significant holder”. A significant holder was required to notify the Trustee and the Manager of The Link REIT within three business days next following the acquisition of such interest and of every subsequent change in unit-holding by a whole percentage point above such threshold. However, in response to recent market developments concerning substantial acquisitions of REITs and the call for enhancing the transparency of shareholding interests of REIT units, the SFC had reviewed the situation and decided to adopt the 5% disclosure threshold under the SFO for REITs. The new disclosure threshold would apply to existing listed REITs and new REITs to be listed on the Stock Exchange of Hong Kong (SEHK). The SFC was discussing with The Link and its Trustee on applying the new threshold to The Link REIT.

8. As regards the regulation of REIT Manager, Mrs Alexa LAM advised that a Manager, i.e. a management company, was appointed in accordance with the REIT Code to manage the REIT. The REIT Manager was a corporation licensed by the SFC to carry out Type 9 Regulated Activity of Asset Management under the SFO. As a licensed corporation, the REIT Manager was subject to the application of the relevant codes of conduct and guidelines, including the Code of Conduct and the Fit and Proper Guideline for Licensees, issued by the SFC from time to time. At least one responsible officer of the REIT Manager was required to be a Director of the Board of the management company. The REIT Manager had to satisfy the SFC that it had put in place sufficient internal systems of controls and measures to ensure the compliance with all regulatory requirements, including the adoption of good corporate governance principles, avoiding and managing possible conflict of interests in order to safeguard investors’ interests. The SFC would monitor the REIT Manager on an on-going basis to ensure its compliance with the REIT Code, such as by conducting inspections on its internal systems of control. A breach of the relevant code of conduct and SFC’s guidelines by the REIT Manager would reflect badly on the licensed corporation’s fitness to remain as a SFC’s licensee.

Discussion on conflict of interest issue

9. Mr WONG Kwok-hing, Ms Emily LAU, Mr James TO, Mr Ronny TONG, Mr Albert CHENG and Mr LEUNG Kwok-hung expressed concern about the issue of possible conflict of interest between Mr Paul CHENG's advisory role with Deutsche Bank and his role as Chairman of the Board of Directors of The Link. Given the public concern about the issue, they considered that Mr CHENG should attend the Panel meeting to explain the matter. Mr Albert CHENG considered that even if Mr Paul CHENG was out of town, The Link should send other representatives to attend the meeting.

10. Members noted that Mr Paul CHENG was appointed as an independent non-executive director and Chairman of The Link on 1 April 2005, and appointed by Deutsche Bank as a Senior Advisor to its Asia Pacific Regional Advisory Board on the same day. Mr CHENG's advisory role with Deutsche Bank was not included in the Offering Circular in the Initial Public Offering (IPO) for The Link REIT (The Link REIT IPO) which was published on 14 November 2005.

Possible conflict of interest between Mr Paul CHENG's two roles

11. Mr WONG Kwok-hing was of the view that in considering whether there was any conflict of interest between the two roles of Mr Paul CHENG, it was necessary for Members to know the duties and responsibilities of Mr CHENG as the Senior Advisor to Deutsche Bank and whether he was remunerated for the position. Mr James TO raised the same points of concern. The Deputy Director (Corporate Services) of the Housing Department (DD(CS)HD) said that it was inappropriate for the Administration to respond on behalf of Mr CHENG. He however pointed out that Mr CHENG had, in his reply dated 12 December 2005 to the Clerk to FA Panel (LC Paper No. CB(1)514/05-06(03)), provided information on the responsibilities of his role as the Senior Advisor to Deutsche Bank.

12. Mr James TO pointed out that according to the press statement issued by Deutsche Bank on 9 December 2005 (Annex 3 of LC Paper No. CB(1)514/05-06(03)), Mr Paul CHENG's role as the Senior Advisor "extends to providing guidance and counsel to Deutsche Bank management on the general business and commercial environment in Hong Kong and Asia; its overall business development in Asia ...", etc. Mr TO was concerned whether Mr CHENG's provision of guidance and counsel on the overall business development of the Bank in Asia might cover the advice on the Bank's investment strategies, including the acquisition of additional units of The Link REIT and related issues.

13. Mr WONG Kwok-hing was concerned that if Deutsche Bank joined with some significant holders to propose replacing the Board of The Link or selling The Link REIT's assets, what position Mr CHENG would take in serving as the Senior Advisor to Deutsche Bank as well as the Chairman of the Board of Directors of The

Link, and whether there would be any real, potential or perceived conflict of interest involved. Ms Emily LAU shared Mr WONG's concern. DD(CS)HD advised that according to the Trust Deed of The Link REIT, unit-holders might raise a request at a general meeting of unit-holders for replacing the Board of Directors of The Link. The Board should then deal with the request in accordance with relevant provisions in the Trust Deed.

14. Mr WONG Kwok-hing and Ms Emily LAU enquired what actions the Administration would take to address the public concern about the conflict of interest issue relating to Mr Paul CHENG. Mr WONG also enquired whether the Administration would consider appointing another director to replace Mr CHENG as the Chairman of the Board of Directors of The Link. SHPL clarified that the appointment of Mr Paul CHENG as the Chairman of the Board of Directors of The Link had been made by the Board of Directors, not by the Administration or HA. Given that The Link was a private company and that both the Administration and HA did not retain any unit-holdings of The Link REIT, changes in the directors or Chairman of The Link was a matter for the Board of Directors of The Link to decide. The Administration or HA did not have any role to play in such matters. In this connection, Acting Permanent Secretary for Housing, Planning and Lands (Housing) advised that Mr CHENG had indicated in his reply dated 12 December 2005 that he would continue to review his position and consult The Link Board going forward.

Non-disclosure of Mr Paul CHENG's advisory role with Deutsche Bank

(a) in the Offering Circular for The Link REIT IPO published on 14 November 2005;
(b) during the meeting on 19 November 2005 to decide the pricing and allocations to investors for The Link REIT IPO

15. Ms Emily LAU was concerned why Mr Paul CHENG's advisory role with Deutsche Bank had not been included in the Offering Circular for The Link REIT IPO published on 14 November 2005. In this connection, she noted that the Administration was of the view that Mr CHENG's advisory role with Deutsche Bank was not material information that required disclosure in the Offering Circular (paragraph 21 of LC Paper No. CB(1)514/05-06(01)). Ms LAU enquired whether the SFC shared the Administration's view.

16. Mrs Alexa LAM advised that the SFC would not comment on individual cases. In general, REITs were required to comply with the REIT Code on disclosure requirements and ongoing reporting and compliance requirements, and to disclose information pertinent to them on a timely basis. Prior to listing, a REIT had to make adequate disclosure of relevant and material information about its operations in the offering circular. As regards whether a piece of information was material, it would be decided on the facts and circumstances of the case. Subsequent to listing, the REIT and its Manager had to ensure that the market was kept informed of any price sensitive information to avoid the creation of a false market. Mrs LAM added that disclosure of false information was a criminal offence under the SFO and the SFC would take follow-up action on relevant offence and breaches of the REIT Code.

17. Ms Emily LAU was concerned whether there would be any real, potential or perceived conflict of interest involved in Mr Paul CHENG's two roles if Deutsche Bank continued to purchase units of The Link REIT in the market. She considered that there might be loopholes in the disclosure requirements of the REIT Code and suggested that the SFC should review the REIT Code in respect of the information subject to the disclosure requirements.

18. Pointing out that directorships and positions taken up by Mr Paul CHENG with other companies/organizations had been included in the Offering Circular of The Link REIT IPO, Mr James TO queried why Mr CHENG's advisory position with Deutsche Bank had not been included. In this connection, he noted from Mr CHENG's reply dated 12 December 2005 that "[g]iven the general and advisory nature of my role with Deutsche Bank and the focus in the Offering Circular on the requirement to disclose other directorships, we did not consider the details of my advisory position with Deutsche Bank to be material information for the purposes of disclosure in the Offering Circular at the time of its publication" (paragraph 7 of LC paper No. CB(1)514/05-06(03)). Mr TO queried whether the word "we" referred to the Board of Directors of The Link, and whether the Board came to such a view before or after the publication of the Offering Circular on 14 November 2005. SHPL advised that the Administration was not in a position to respond on behalf of Mr CHENG. Mr TO then enquired whether the word "we" mentioned in the reply included HA. DD(CS)HD advised that Mr CHENG had not consulted the Administration before issuing his reply to the Clerk to FA Panel, and the Administration was not sure what the word "we" referred to. However, the Administration was of the view that Mr CHENG's advisory role with Deutsche Bank was not material information that required disclosure in the Offering Circular. Whether Mr CHENG wished to include that particular information in his bio-data in the Offering Circular was a matter for Mr CHENG to decide.

19. Referring again to Mr Paul CHENG's reply dated 12 December 2005, Mr James TO noted that Mr CHENG's advisory position with Deutsche Bank had been disclosed in his profile on The Link's website form 1 April 2005 and his business card. Mr TO queried why the same information had not been disclosed in the Offering Circular for The Link REIT IPO. He considered that Mr Paul CHENG, the Administration and the SFC should respond to his questions. Moreover, the Administration and the SFC should take follow-up actions to address the issues and problems revealed in the listing of The Link REIT.

20. Mr James TIEN noted from Mr Paul CHENG's letter dated 13 December 2005 that Mr CHENG did not disclose his advisory role "because all along, that advisory role is regarded to be different to a directorship which was why it was not disclosed in the offering circular in the first place" (LC paper No. CB(1)532/05-06(01)). Mr TIEN enquired whether the Administration and the SFC accepted Mr CHENG's explanation. Mrs Alexa LAM reiterated that the SFC would not comment on individual cases.

21. Mr Ronny TONG pointed out that Mr Paul CHENG, as the Chairman of The Link and a Senior Advisor to Deutsche Bank, was under fiduciary duties to act in the best interest of The Link and Deutsche Bank respectively. As such, he considered that there was potential conflict of interest between the two roles taken up by Mr CHENG. In this connection, Mr TONG noted that paragraph 8.2 of the REIT Code required the disclosure of, inter alia, any potential conflict of interests involving a connected person (including the management company of the scheme, its directors and senior executives/officers) in the scheme's offering document, and paragraph 10.1 of the REIT Code stated that "[t]he management [of the company] shall keep holders informed of any material information pertaining to the scheme in a timely and transparent manner". Mr TONG enquired whether the non-disclosure of Mr CHENG's advisory role with Deutsche Bank in the Offering Circular for The Link REIT IPO had contravened the relevant provisions of the REIT Code; and if had, what follow-up actions had been or would be taken by the Administration or the SFC.

22. Mr Ronny TONG also noted from the paper provided by HPLB that "[d]uring the meeting to decide the pricing and the allocations to investors under the IO [International Offering], Mr Paul Cheng did not remind the meeting of his advisory role with Deutsche Bank. We have carefully examined the matter and are satisfied that in the circumstances of the case, allocations to all investors under the IO have been made objectively and impartially, and the 'non-declaration' by Mr Paul Cheng did not have any impact on the outcome of the allocations" (paragraph 23 of LC Paper No. CB(1)514/05-06(01)). Mr TONG was concerned whether there was any real, potential or perceived conflict of interest involved in the non-declaration by Mr CHENG and what follow-up actions had been or would be taken by the Administration, HA and the SFC on the non-disclosure. He considered that the Administration, the SFC, The Link and Mr Paul CHENG should take action to address the concern about the conflict of interest issue. He was of the view that a possible option was for Mr CHENG to resign from one of his positions with Deutsche Bank or The Link. He further enquired whether there was a mechanism to require Mr CHENG to resign from one of the two positions.

23. Given that the conflict of interest issue relating to the listing of The Link REIT had aroused considerable public concern, Mr Albert CHENG considered that Mr Paul CHENG should consider resigning from one of the two positions concerned.

24. Mrs Alexa LAM said that the structure and operation of The Board of Directors of The Link were comparable to those of the board of directors of a listed company. Both the boards of The Link and listed companies were required to observe good corporate governance principles in conducting their activities, including setting up systems for disclosure of interests by directors, and putting in place avoidance of conflict of interest measures, such as requiring directors who had declared interests in a matter not to participate in the discussion and decision-making process on the matter. While refraining from giving comments on the conflict of

interest issue relating to Mr Paul CHENG, Mrs LAM re-iterated that The Link, as a licensed REIT Manager, was subject to the regulation of the REIT Code. As a SFC licensee, The Link was also subject to the relevant codes of conduct and guidelines issued by the SFC. Breaches of the codes or guidelines would result in disciplinary action taken by the SFC. Moreover, the conduct of The Link would have impact on its fitness and propriety to continue to be a SFC licensed corporation.

Discussion on other relevant issues

Government policy on asset divestment

25. Mr Jeffrey LAM noted that the Government had remained the largest shareholder of the Mass Transit Railways Corporation Limited (MTRCL) since the listing of the Corporation and had imposed shareholding limit on single shareholders of the Hong Kong Exchanges and Clearing Company Limited (HKEx) upon the listing of the Company. He enquired about the reasons for not making similar arrangements for the divestment of HA's RC facilities. He further noted that while the Chairmen of the Boards of Directors of the MTRCL and the HKEx were appointed by the Chief Executive, the same arrangement was not made for The Link. In this connection, Mr LAM expressed concern that the Government had adopted different policies in respect of shareholdings and appointment of directors of the companies concerned in the divestment of public assets. He enquired about the criteria adopted in determining the arrangements to be made for different divestment projects.

26. SHPL advised that he was not in a position to respond to Mr Jeffrey LAM's questions, as they were within the purview of the Financial Services and the Treasury Bureau (FSTB). He also pointed out that HA's RC facilities were HA's assets, not Government's assets. DD(CS)HD added that it was the objective of HA to divest completely its ownership and control of the 180 RC facilities. This objective had been clearly stated during previous discussions on the divestment project with the Panel on Housing in 2003 and 2004, as well as the debate on the adjournment motion on the subject at the Council meeting on 1 December 2004. The objective had been achieved through the injection of those facilities into The Link REIT, and the public listing of The Link REIT on 25 November 2005. After the divestment, HA did not have any unit-holding interest in The Link REIT. In other words, The Link was fully independent of HA.

27. Mr Albert CHENG pointed out that the listing of The Link REIT was part of the privatization plan of the Government, and he did not agree with SHPL that the assets involved were not Government's assets. While the HA was responsible for taking the divestment project forward, HPLB and FSTB should also have an important role to play.

28. The Permanent Secretary for Financial Services and the Treasury (Financial Services) advised that the Government had conducted a number of projects on the sale of public assets in the past, and the method and strategy of divestment varied with the

nature of the assets in question and different circumstances of each project. The same approach was also adopted by overseas jurisdictions in selling public assets.

29. Responding to Mr Jeffrey LAM's question of why an upper limit had not been imposed on the shareholdings of The Link REIT to be acquired by individual parties, DD(CS)HD said that consideration had been given to the proposal. However, it was considered that the proposal, even implemented, would not prevent joint actions of unit-holders to control The Link REIT. He added that there were features under the REIT Code and/or the Trust Deed of The Link REIT that might limit the ability of a significant unit-holder from controlling The Link REIT to its own advantage rather than to the advantage of all unit-holders as a whole. The details of the features were set out in paragraph 9 of the paper provided by HPLB (LC Paper No. CB(1)514/05-06(01)).

Protection of interests of tenants concerned

30. Mr LEUNG Kwok-hung expressed grave concern about the divestment of HA's RC facilities. He pointed out that the conflict of interest issue concerning Mr Paul CHENG and the acquisition of substantial units of The Link REIT by hedge funds had demonstrated that the divestment project was fundamentally wrong.

31. Mr Albert CHENG said that all along, he did not support the divestment project and the listing of The Link REIT. Mr CHENG and Mr LEUNG Kwok-hing expressed concern about how the Administration or HA would protect the interests of the tenants concerned after completion of the divestment project, in particular, in preventing possible joint actions taken by significant holders of The Link REIT to replace the Board of Directors of The Link or to sell The Link REIT's assets. Mr CHENG queried why the Administration had not put in place the following measures in the listing of The Link REIT:

- (a) To allow HA to retain the controlling unit-holdings of The Link REIT after its listing;
- (b) To impose an upper limit on unit-holdings of The Link REIT to be acquired by individual parties and restrictions on the voting rights of significant holders so as to prevent manipulation by significant holders; and
- (c) To appoint "cornerstone investors" who/which were prohibited from selling the units of The Link REIT within a certain period of time after its listing.

32. On paragraph 31(a) above, Mr Albert CHENG pointed out that if The Link REIT wished to sell a property within two years of its acquisition, the sale must be approved at a general meeting of unit-holders by a special resolution, and the passing of the special resolution required a quorum of two or more unit-holders holding at

least 25% of all units in issue. As such, if HA retained the controlling unit-holdings of The Link REIT, it would prevent manipulation by significant holders, such as the hedge funds.

33. On paragraph 31(c) above, DD(CS)HD explained that cornerstone investors were involved in the original IPO exercise in 2004 with a view to securing validation for the investment case and early demand for units. However, given the actual experience of the IPO in 2004 that demand for units of The Link REIT was high and broadly based, HA had decided not to have any cornerstone investors for the re-launch of the IPO in 2005. This had allowed HA a greater flexibility to allocate more units to other investors, including the retail investors and mandatory provident funds. DD(CS)HD added that The Link had engaged the same strategic partner in the re-launch of the IPO in 2005. The partner was pre-allocated about 4% of the units in issue and in return was prohibited from selling the units for a certain period of time after the listing of The Link REIT.

34. Given that there were abnormal price movements on The Link REIT arising from continuous purchase by hedge funds in the market in late November 2005, Mr Albert CHENG queried why HA still exercised its over-allotment option to dispose of its units in The Link REIT in early December 2005. DD(CS)HD advised that the option was exercised at the discretion of the underwriters for the listing without the need for approval from HA. The over-allotment option was part of a technical arrangement commonly deployed for the sole purpose of post-listing stabilization of the price of units/shares sold in the IPO. As the price of The Link REIT had risen after its listing, it was not necessary for the underwriters to keep the over-allotment shares.

35. Mr WONG Kwok-hing expressed concern that joint actions might be taken by significant holders to replace the Board of Directors of The Link or to demand for higher returns by imposing huge rent increases on the commercial tenants concerned. He enquired whether the Administration or HA would consider acquiring units of The Link REIT from the market to retain the controlling unit-holdings of The Link REIT in order to protect the interest of the tenants concerned.

36. DD(CS)HD re-iterated that it was the Administration's stance as stated in the closing of the Adjournment Debate on 1 December 2004, that in a free economy like Hong Kong, trading would follow market forces and the Government would not preclude any investor from acquiring units of The Link REIT from the market to become a significant holder. Nonetheless, the Administration had noted the concern about the impact of emergence of significant holders. In designing the structure of The Link REIT, the Administration and HA considered that the multiple layers of protection available to a REIT were sufficient in addressing the concerns about one investor or a group of investors acquiring a controlling interest in The Link REIT. The details of the protection were set out in paragraphs 9 to 12 of the paper provided by HPLB (LC Paper No. CB(1)514/05-06(01)). For instance, there were features in the REIT Code and/or the Trust Deed of The Link REIT for limiting the ability of a

significant holder from controlling The Link REIT to its advantage. These included restricting The Link REIT's key business to investment in real estate which would generally produce sustainable income, such as rental income, thus preventing the engagement in property development or speculative investments. Moreover, no unit-holder had a right to require that any assets of The Link REIT be transferred to him. A significant holder and its related parties were prohibited from voting their units or being part of a quorum for any meeting of unit-holders convened to approve any matter in which the significant holder had a material interest in the business to be conducted.

37. As regards the impact on public rental housing tenants, DD(CS)HD said that in July 2005, the Court of Final Appeal (CFA) had affirmed that the divestment by HA of RC facilities was consistent with HA's object to secure the provision of housing and such amenities ancillary thereto as HA considered fit. CFA had ruled that to secure the provision of RC facilities did not mean that HA needed to be the direct provider itself. CFA had also noted that The Link would adopt a market-oriented commercial approach in operating the RC facilities. Given that the RC facilities were located in public housing estates, market forces and commercial principles would compel The Link to take full account of the needs and purchasing power of the major users of those RC facilities, i.e. public rental housing tenants. DD(CS)HD added that it was stated in the Offering Circular of The Link REIT that The Link's business strategy was to raise return for units through measures, including improvement of RC facilities to enhance the business of commercial tenants and achieving savings in operating the RC facilities, instead of through substantial increases in rental.

38. On the question of acquiring The Link REIT units from the market, SHPL stressed that the Administration's objective was to divest the ownership and control of HA's RC facilities completely in one go. The Administration or HA did not have any plan to acquire The Link REIT units from the market after divestment.

39. Mr Albert CHENG and Mr LEUNG Kwok-hung considered that the Administration's response had not addressed their concern that both the REIT Code and the Trust Deed of The Link REIT would not be able to prevent the sale of RC facilities after the initial two-year period. They maintained the view that HA should retain the controlling unit-holdings of The Link REIT in order to protect the interests of tenants concerned.

40. DD(CS)DH re-iterated that it was not the intention of the Administration or HA to prohibit the sale by The Link REIT of its assets. Nevertheless, the sale of the assets would not affect the facilities under The Link REIT being continuously used for retail and car-parking purposes, and would not affect the terms of use prescribed by the applicable government lease.

Valuation of RC facilities

41. Mr Albert CHENG noted the comments made by some financial analysts that the unit price of The Link REIT should be much higher than that fixed in the IPO in 2005. In this connection, Mr CHENG expressed concern about the underestimation of the value of the RC facilities and the resultant loss in the proceeds for HA from the sale of its assets.

42. DD(CS)HD said that there were a lot of factors affecting the prices of REITs and in general, prices were determined by market forces. At around the time of the IPO, the great majority of market players were of the view that the offered unit price of The Link REIT was set at an appropriate level. The Assistant Director (Divestment) of the Housing Department (AD(D)HD) added that HA had used the same methodology adopted for The Link REIT IPO in 2004 for the valuation of the properties in the re-launch of the IPO in 2005. The re-valuation had followed the stringent standard set out in Chapter 6 of the REIT Code and the international practice for valuation of REITs. With improved prospect of rental income growth for The Link REIT and enhanced cost control measures adopted by The Link, the asset value of The Link REIT had increased by 9.6% in the 2005 IPO vis-à-vis the valuation in the 2004 IPO. AD(D)HD added that it was inappropriate to make direct comparison on prices of REITs due to differences in their valuation methods and structures.

Discussion on the way forward

43. Given the various concerns expressed by members at the meeting, the Chairman invited members' view on the need for the FA Panel to follow up the financial issues relating to the listing of The Link REIT, such as the conflict of interest and disclosure issues involved.

44. Mr James TIEN said that the FA Panel might consider following up the issue relating to conflict of interest. Mr Abraham SHEK considered that issues relating to the divestment of HA's RC facilities were under the purview of the Panel on Housing and not the FA Panel. Mr Ronny TONG opined that conflict of interest of company directors was an issue relating to corporate governance of companies and was under the purview of the FA Panel. Mr CHAN Kam-lam did not consider it necessary for the issues to be followed up by the FA Panel or the Panel on Housing.

45. In response to the Chairman's further enquiry, Mr CHAN Kam-lam and Mr Abraham SHEK considered it not necessary for the FA Panel to discuss the subject further and to invite Mr Paul CHENG to attend a meeting of the Panel for discussion of the issue of conflict of interest between his advisory role with the Deutsche Bank and his role as the Chairman of the Board of Directors of The Link. Other members present did not express other views. The Chairman concluded that it was not necessary for the FA Panel to follow up the issue.

(Post-meeting note: At the suggestion of Mr James TO, the FA Panel subsequently decided at its meeting on 5 January 2006 that the conflict of interest issue and other financial issues involved in and after the listing of The

Link REIT be further discussed at the Panel meeting on 3 April 2006. Mr Paul CHENG and other representatives of The Link, and the Administration (including representatives from the HPLB and the Financial Services and the Treasury Bureau), the SFC, and the Hong Kong Exchanges and Clearing Limited had been invited to attend the meeting.)

II. Any other business

46. There being no other business, the meeting ended at 10:35 am.

Council Business Division 1
Legislative Council Secretariat
3 March 2006