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**Report of the Panel on Financial Affairs**
**for submission to the Legislative Council**

## Purpose

This report gives an account of the work of the Panel on Financial Affairs ("the Panel") during the 2019-2020 legislative session. It will be tabled at the meeting of the Legislative Council ("LegCo") of 15 July 2020 in accordance with Rule 77(14) of the Rules of Procedure of LegCo.

## The Panel

2. The Panel was formed by a resolution passed by LegCo on 8 July 1998 and as amended on 20 December 2000, 9 October 2002, 11 July 2007 and 2 July 2008 for the purpose of monitoring and examining government policies and issues of public concern relating to financial and finance matters. The terms of reference of the Panel are set out in **Appendix I**.

3. The Panel comprises 20 members, with Hon Christopher CHEUNG Wah-fung and Hon Kenneth LEUNG elected as Chairman and Deputy Chairman respectively. The membership list of the Panel is in **Appendix II**.

## Major work

Macro economy

*Hong Kong's economic performance*

4. During the 2019-2020 session, the Panel continued to provide a forum for LegCo Members to exchange views with the Financial Secretary ("FS") on

matters relating to macro-economic issues. At the meeting on 1 June 2020, the Panel noted that since the beginning of 2020, the threat of the coronavirus disease-2019 ("COVID-19") had seriously disrupted a wide range of local economic activities and supply chains in the Asian region, and led to sharp moderation or even shuttering of economic activities worldwide. The Hong Kong economy contracted sharply by 8.9% for the first quarter of 2020 over the same period of 2019, and the gross domestic product ("GDP") also plunged by 5.3% on a seasonally adjusted quarter-to-quarter comparison. Both rates of decline were the steepest for a single quarter on record. On the economic outlook for 2020, Members noted that for 2020 as a whole, the GDP growth forecast (made at the end of April 2020) was revised downwards to -4% to -7% while the forecast rates of underlying and headline consumer price inflation were 2.2% and 1.4% respectively. The near-term economic outlook would be subject to a high level of uncertainties. If the COVID-19 pandemic was getting contained and Hong Kong's trading partners could proceed with their plans to reopen their economies, Hong Kong's economic performance would hopefully come out of the trough in the second half of 2020. If violent acts re-emerged, the pace of economy recovery would certainly be hindered. The proposed national security legislation to be enacted by the Standing Committee of the National People's Congress for Hong Kong ("the proposed NSL") might also bring about uncertainties to the local economy in the near term.

*Impact of the proposed national security legislation on the Hong Kong economy*

5. Members expressed concern on the possible sanctions the United States ("US") Government might impose on Hong Kong in light of the proposed NSL, including cancelling Hong Kong's preferential treatment as a separate customs and travel territory from the rest of China and charging additional tariff on goods manufactured in Hong Kong and exported to US. Members enquired about the Administration's assessment of the impacts of US's possible sanctions on the Hong Kong economy and measures to counteract the possible adverse impacts, especially the continuous implementation of the Linked Exchange Rate System ("LERS") and free flow of capital in and out of Hong Kong.

6. FS said that while US's possible sanctions on Hong Kong might cause certain disturbance to the market, the actual impact on Hong Kong would be limited. It was because manufacturing only accounted for 1% of Hong Kong's GDP, and goods manufactured in Hong Kong and exported to US only accounted for 0.1% of Hong Kong's total value of exports in a year. On the other hand, US had very substantial business interests in Hong Kong. On the trade front, over the past decade US all together had a positive balance with Hong Kong of about US$300 billion. Besides, US had very strong

professional and financial services representation in Hong Kong that generated substantial economic benefits. Any restriction measure would only at the same time harm the interests of US's enterprises in Hong Kong. While remarking that it would be inappropriate to speculate on the possible actions to be taken by the US Government, FS assured Members that the Administration would keep in view the latest developments and take precautionary actions where necessary.

7. As regards capital and foreign exchange controls, FS stressed that Article 112 of the Basic Law stipulated that no foreign exchange control policies shall be applied in Hong Kong, the Hong Kong dollar ("HKD") shall be freely convertible, and markets for foreign exchange, gold, securities and futures shall continue, and the free flow of capital within, into and out of Hong Kong shall be safeguarded. As for LERS, it was introduced in Hong Kong in 1983 and the US-Hong Kong Policy Act was legislated in 1992. LERS had no correlation with the US-Hong Kong Policy Act, and the continuous implementation of LERS in Hong Kong was not subject to US's consent. The Administration was determined and had confidence and capability to defend LERS. LERS was underpinned by Hong Kong's strong foreign reserves position of over US$440 billion at present. There had been no noticeable capital outflow from Hong Kong recently. Also, the Hong Kong banking system remained healthy and strong with the capital adequacy ratio and liquidity ratio stood at very high levels as compared to international standards. The Administration and financial regulators were closely monitoring the operation in the financial markets and had not observed any irregularities. In addition, a swap arrangement with the People's Bank of China ("PBoC") had been in place so that in the event that Hong Kong required additional US dollars ("USD"), Hong Kong would provide PBoC with HKD in exchange for US dollars.

*Measures to revive the local economy and support enterprises*

8. Members expressed concern that local social incidents involving violent acts in 2019 and the COVID-19 epidemic since the beginning of 2020 had led to a significant fall in visitor numbers and deterioration in economic conditions which dealt a heavy blow to various sectors particularly retail and catering, and in turn adversely affect the employment situations. Members urged the Administration to formulate measures to support enterprises and safeguard jobs, especially to provide relief for small and medium sized enterprises ("SMEs") to tide over the difficult period and assist them to grasp new information technologies, as well as to help local enterprises to explore business opportunities in new and emerging markets.

9. FS advised that the Administration had rolled out a series of relief measures since August 2019 to safeguard jobs, support enterprises, stabilize the economy and protect livelihood which included the relief package in the 2020-2021 Budget and the two rounds of measures under the Anti-epidemic Fund ("AEF") involving some HK$290 billion in total. AEF in particular was to enhance Hong Kong's overall capability in combating COVID-19, and to provide assistance or relief to enterprises and members of the public hard-hit by the epidemic or affected by anti-epidemic measures. The first-round of AEF covered a one-off subsidy for workers in some sectors. The second-round of AEF included the $81 billion Employment Support Scheme with the aims to preserve employment and assist the self-employed irrespective of the sectors to which they belonged in order to provide extra relief to sectors hard hit by the epidemic and paving the way for post-pandemic economic recovery. As regards support for SMEs, with a view to enhancing their competitiveness, the Administration had introduced the Technology Voucher Programme to subsidize local SMEs in using technological services and solutions to improve productivity and upgrade or transform their business processes. On new markets development, the Administration had established the Dedicated Fund on Branding, Upgrading and Domestic Sales to assist enterprises in exploring and developing new markets, including developing brands, upgrading and restructuring enterprises' operations, and promoting domestic sales in the Mainland market, as well as markets of member states of the Association of Southeast Asian Nations and economies which had signed Free Trade Agreements with Hong Kong. In order to facilitate local enterprises to explore new investment opportunities in the new and emerging markets, the Commerce and Economic Development Bureau and the Hong Kong Trade Development Council had also made arrangements for enterprises to visit these markets with a view to helping them to better understand the economic policies and development opportunities in the markets.

Monetary affairs

10. The Panel continued to receive regular briefings from the Chief Executive of the Hong Kong Monetary Authority ("HKMA") and his colleagues on the work of HKMA. At the three briefings during the 2019-2020 session, HKMA provided information on the global, regional, and local financial and economic situations, assessment of risks to Hong Kong's financial stability, banking supervision, development of financial infrastructure and the financial market, investment performance of the Exchange Fund ("EF"), and measures implemented by the Hong Kong Mortgage Corporation ("HKMC").

*Financial and monetary stability of Hong Kong*

11. Members expressed concern that the lingering social unrest in Hong Kong might undermine its financial stability and cause large-scale capital outflow. As some media reported an increasing number of Hong Kong people and companies converting HKD into USD and opening offshore bank accounts, Members sought information on HKMA's precautionary measures to counteract capital outflow and defend LERS. Some Members further stressed the importance for HKMA to dispel vicious rumours about the monetary and financial stability of Hong Kong.

12. HKMA advised that maintaining monetary and financial stability was the top priority of HKMA. HKMA had been closely monitoring HKD exchange rate against USD and deposit levels in the local banking system, and had not observed noticeable capital outflow from HKD or the Hong Kong banking system. On the operation of LERS, when the HKD exchange rate weakened to the weak-side Convertibility Undertaking of HK$7.85 to US$1, HKMA would buy HKD from banks, leading to a decline in the aggregate balance in the banking system and a rise in HKD interest rates. This would induce investors to sell USD for HKD, which would in turn support HKD exchange rate and attract capital inflow. This automatic adjustment mechanism would help stabilize the HKD exchange rate under LERS. While HKMA noted that some investors were concerned about the social situations in Hong Kong, they in general appreciated that Hong Kong's fundamentals and core competitiveness as an international financial centre remained strong. Notwithstanding that there was capital outflow, there was also capital inflow looking for investment opportunities in Hong Kong. As regards HKMA's efforts in upholding market confidence, HKMA stressed that it was committed to refuting unfounded rumours firmly and in a timely manner. HKMA had been on high alert for rumours on social media platforms and strived to respond swiftly to false rumours through the use of traditional and social media platforms. To maximize the reach of its messages, HKMA had set up a network of key contacts such that important statements or clarifications could be sent to relevant stakeholders in a more systematic and effective manner.

*The property market and the Mortgage Insurance Programme*

13. HKMC announced in October 2019 amendments to the Mortgage Insurance Programme ("MIP") for completed residential properties ("the MIP amendments") which, inter alia, sought to increase: (a) the maximum property value eligible for mortgage loans up to 80% loan-to-value ("LTV") ratio from HK$6 million to HK$10 million; and (b) for first-time homebuyers, the maximum property value eligible for mortgage loans up to 90% LTV ratio from

HK$4 million to HK$8 million. Some Members expressed concern that the MIP amendments might drive up property prices further and induce the public to make imprudent decisions in purchasing properties. Moreover, while the MIP amendments could help reduce down payment by homebuyers, they would need to pay more interests and instalments for longer periods for their mortgages. On the other hand, some Members were concerned that the outbreak of COVID-19 might lead to a surge in the number of negative equities. The Panel urged HKMA to step up its efforts in explaining to the public the objectives of the MIP amendments and the need to make prudent decisions in purchasing residential properties, as well as assessing the impact of COVID-19 on Hong Kong's property market.

14. HKMA stressed that the property market was affected by a host of factors including interest rates, economic environment, land supply, and the demand for and supply of residential flats. Thus members of the public should carefully assess the outlook of the property market and their affordability when making purchase decisions. Regarding the MIP amendments, the main objective was to provide assistance to homebuyers with immediate housing needs and long-term repayment ability but without a sufficient down payment. Mortgage loans under the revised criteria would only apply to completed residential properties and those households who were not holding any other residential properties. The measure was intended to provide an additional option for this specific group of households. HKMC would step up publicity to promote public understanding of the objective of and points to note for the MIP amendments. On the possible impacts of COVID-19 on the local property market, HKMA pointed out that there was not yet a clear trend for the market at this juncture. HKMA would continue to closely monitor developments in the market and would consider any need for an adjustment in its countercyclical macroprudential measures as appropriate should a clear change in the property market cycle be ascertained. As regards negative equities in Hong Kong, HKMA pointed out that the majority of cases were bank staff housing loans and residential mortgage loans under MIP. These loans generally had a higher LTV ratio. Homebuyers applying to use MIP would have to meet a set of established eligibility criteria, and there had not been a significant increase in the default risk.

*Relief measures to help local enterprises and mortgage borrowers*

15. Members noted that the banking industry had introduced various relief measures to help local enterprises ride through the challenges arising from the COVID-19 outbreak, such as the Special 100% Loan Guarantee ("the 100% LG") and the offer of principal payment holiday for various types of borrowers (e.g. principal moratoriums for residential mortgages). The Panel urged

HKMA to step up publicity to enhance the understanding of local enterprises and borrowers on such measures, as well as to call on banks to expedite processing relevant applications and adopt a less stringent approach in handling loans of SMEs and mortgage borrowers. Some Members further suggested that HKMA should consider relaxing the application criteria for the 80% and 90% Guarantee Products so that more enterprises could benefit.

16. HKMA advised that the 100% LG aimed to provide loans to applicants as quickly as possible and the majority of applications referred to HKMC were approved within three days[1]. HKMA had been closely working with HKMC and the banking industry on expediting the approval process as far as possible. HKMA was also liaising with the banking industry on further streamlining the approval process of the 80% and 90% Guarantee Products. As regards the measure on principal payment holiday, the banking industry had notified over 60 000 eligible corporate customers about the new Pre-approved Principal Payment Holiday Scheme since mid-April 2020. On banks' handling of loan applications from SMEs, HKMA had encouraged banks to adopt an accommodating stance in dealing with customers facing financial stress due to the COVID-19 epidemic, and would continue discussing relevant issues with banks under the Banking Sector SME Lending Coordination Mechanism as well as examining how the measures agreed under the Mechanism could be conveyed effectively to all retail banks in Hong Kong. Besides, HKMA had lowered the countercyclical capital buffer from 2.5% to 2% in October 2019 to free up additional capital such that banks could have additional headroom to support SME financing.

*Investment of the Exchange Fund*

17. Noting that EF's investment in alternative assets held under the Long-Term Growth Portfolio ("LTGP") had been gaining relatively high annualized internal rate of return in recent years, some Members enquired whether HKMA would consider increasing EF's investment under LTGP. Members also raised enquiries on EF's Mainland-related investment.

18. HKMA advised that LTGP had achieved a relatively high investment return in the past 10 years, and there was still room to increase EF's allocation to LTGP. That said, HKMA would need to strike a proper balance in asset

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[1] According to the Hong Kong Monetary Authority at the meeting on 4 May 2020, the banking industry had received over 2 000 applications since the launch of the Special 100% Loan Guarantee on 20 April 2020. Among these, 503 applications had been submitted to the Hong Kong Mortgage Corporation involving loan amount of $1.2 billion and an average $2.5 million per application. 432 applications had been approved so far.

allocation, including LTGP, to ensure EF maintained sufficient liquidity as LTGP primarily invested in alternative assets in private markets, which in general had longer investment period and lower liquidity. Moreover, EF followed the principle of "Capital Preservation First, Long-Term Growth Next" in making investment, and adopted robust credit risk management and monitoring procedures. EF strictly followed the same set of criteria when considering investments in debt instruments (bonds, notes, and bills), irrespective of whether they were issued by Mainland or overseas institutions. As such, the debt instruments currently held by EF were of good credit quality and with very low default risk. The vast majority of Mainland debt instruments held by EF was sovereign debt, with the rest issued by commercial institutions of high credit quality.

Development of the Hong Kong securities market

*Strategic development of Hong Kong as a premier listing platform*

19. At the meeting on 2 March 2020, the Panel discussed with the Administration, the Securities and Futures Commission ("SFC") and the Hong Kong Exchanges and Clearing Limited ("HKEX") on the strategy to develop Hong Kong as a premier listing platform, and future development of HKEX as set out in its Strategic Plan 2019-2021.

20. Noting that in recent years share prices of some newly listed stocks had declined drastically soon after listing, some members expressed concern about the protection for investors' interests and the adverse impact on Hong Kong's reputation as an international financial centre. They enquired about measures taken by SFC and HKEX to enhance the quality and governance of listed companies (majority of which were Mainland companies in recent years), as well as to improve market quality.

21. SFC advised that it had adopted a front-loaded regulatory approach since early 2017 to enhance market quality by taking early preventive actions against suspected serious market misconduct behaviours. Besides making amendments to the Listing Rules in August 2018 to delist, in a timely manner, companies that no longer meet the continuing listing criteria, HKEX had been applying a heightened review on listing applications that could marginally meet the eligibility requirements under the Listing Rules, as well as tightened the Listing Rules and practices relating to backdoor listings. In addition, SFC and HKEX had been working closely to introduce a series of reforms to the listing regime to combat "shell" listing and related activities, and were studying measures to enhance the structure of the initial public offering process including the price discovery process. Indeed, subsequent to the reforms made to the

Main Board and the Growth Enterprise Market ("GEM") Listing Rules in 2018, the price-volatility of newly listed GEM stocks had significantly reduced and more restrictions had been imposed on share subscription activities.

22. Regarding HKEX's Strategic Plan 2019-2021, while some members expressed support for the initiative of "China Anchored", some other members cautioned that HKEX should not merely focus on the Mainland market and capital. They pointed out that with growing number of Mainland companies seeking listing in Hong Kong in recent years, there was concern that the Hong Kong stock market had become a listing platform for mainly Mainland companies instead of an international listing venue.

23. HKEX explained that strengthening mutual market access with the Mainland was indeed conductive to supporting the development of Hong Kong as a more international listing platform. For example, the Stock Connect schemes would help attract international investors to access the Mainland capital market through Hong Kong on one hand, and drive the flows of Mainland capital into Hong Kong on the other. Increasing and continuous international and Mainland capital flow to Hong Kong could help sustain the development of local businesses and boost local employment, thus contributing to the long-term prosperity of Hong Kong.

24. Regarding the joint statement issued by HKEX and SFC in February 2020 on the publication of financial information by listed issuers in response to the outbreak of COVID-19 in Hong Kong ("Joint Statement"), members noted that the Joint Statement stated that if issuers had difficulties in fulfilling the reporting obligations, they were required to consult HKEX on the financial information that they should report on, and HKEX and SFC would consider the most suitable arrangement on a case by case basis. In view of the uncertainty in the development of the COVID-19 epidemic, some members asked if HKEX would consider giving a blanket approval to all listed issuers allowing them to defer the publication of their financial information.

25. HKEX advised that according to the Joint Statement, where an issuer with financial year ended 31 December 2019 was unable to obtain agreement from its auditors but was able to publish its preliminary results in full compliance with the other reporting requirements set out in the Listing Rules by 31 March 2020, HKEX would normally allow trading of the securities of the issuer concerned to continue with a view to minimizing disruptions to trading while ensuring that the investing public could continue to make informed investment decisions. It would not be advisable to give a blanket approval to all listed issuers in this regard as HKEX had to ensure that the publication of

financial information by issuers had to be sufficient and up-to-date in order to maintain an orderly, informed and fair market.

26. On HKEX's proposal to acquire the London Stock Exchange Group plc ("LSEG") in September 2019 ("the Offer") which was subsequently declined by LSEG, some members were concerned about the negative impact on HKEX's development, and enquired how HKEX would further enhance cooperation and collaboration with LSEG, particularly in view of the opportunities arising from Brexit.

27. HKEX advised that HKEX was one of the world's major market infrastructure groups, operating a range of equity, commodity, and fixed income and currency markets. It was believed that the combination of LSEG and HKEX was strategically compelling and could create a world-leading market infrastructure group. The Offer would also enable the connection of the established financial markets in the West with the emerging markets in the East, particularly in the Mainland, reinforce Hong Kong's position as the portal connecting the Mainland and Asian markets with the world, and enhance the long-term resilience and relevance of Hong Kong and London as global financial centres. Though HKEX was unable to proceed with the Offer, it would continue to look for opportunities to increase its global connectivity and reinforce Hong Kong's role as a global financial centre. As regards HKEX's cooperation and collaboration with LSEG, since the acquisition of The London Metal Exchange ("LME"), HKEX had been playing a key role in underpinning LME's position as the pre-eminent global centre for metals trading. Moreover, HKEX had a strong partnership with LSEG through active collaboration with its subsidiaries, such as FTSE Russell.

*Budget of the Securities and Futures Commission*

28. When the Panel was consulted on SFC's proposed budget for 2020-2021 at the meeting on 17 March 2020, some members welcomed SFC's decision to waive the annual licensing fees in 2020-2021 in order to alleviate the cost burden of brokerage firms under the difficult operating environment. These members further called on SFC to seriously consider continuing the fee waiver when preparing its budget for 2021-2022 in view of the significant downturn in the Hong Kong economy caused by the COVID-19 epidemic.

29. SFC advised that after the annual licensing fee waiver which ended in March 2019, collection of the annual licensing fees had resumed in a phrased approach with a 50% discount in the fees for 2019-2020 and 2020-2021, and to fully reinstate the fees from 2021-2022 onwards. However, after reviewing its fees and charges level and the market conditions, SFC decided in

December 2019 to fully waive the annual licensing fees for one year in 2020-2021 as a relief measure for brokerage firms. SFC would carefully review the market conditions when considering whether and when to reinstate collection of the annual licensing fees.

30. On the "Guidelines for Securities Margin Financing Activities" issued by SFC in 2019 ("the New Guidelines"), some members pointed out that brokerage firms had urged SFC to allow flexibility in enforcing the Guidelines, particularly those relating to the new margin call policies. As the spread of COVID-19 might have adverse impact on the securities market and investors, brokerage firms were concerned that under the New Guidelines they would need to request Mainland clients to settle margin calls during a short period of time.

31. SFC stressed that proper management of margin lending risk was crucial in protecting market integrity especially during periods of great market volatilities, hence the New Guidelines had required brokers to set prudent triggers for margin calls. That said, if a broker could not meet all the benchmarks set out in the New Guidelines, the broker was allowed to deviate from a benchmark provided that compensating measures were taken by the broker to mitigate the additional risk that might result from the deviation. It was observed that implementation of the New Guidelines had been smooth, and SFC would continue to constructively engage individual brokers in discussions on practical compliance issues.

32. Noting that the relocation of SFC's office from Central to Quarry Bay in the second quarter of 2020 could achieve rental savings, together with the reserves SFC had ring-fenced in previous few years for the potential purchase of office premises, some members enquired if SFC would consider purchasing its office premises in the coming few years, in particular having regard to the possible adjustment in property prices amidst an economic downturn.

33. SFC advised that purchasing its own office premises was all along its long term goal. However, it would take time for SFC to identify suitable office premises in an appropriate location and of a considerable size for accommodating its some 900 staff. The relocation of SFC's office from Central to Quarry Bay could achieve savings of about $1,000 million in rentals over the eight-year lease. Together with the $3,000 million which had been ring-fenced for the purchase of its office, SFC would have about $4,000 million at its disposal for the purchase. SFC would keep in view the availability of suitable office premises in the market as well as development in the property market, and when appropriate, might consider purchasing its office premises before the expiry of the eight-year lease.

<u>Establishment of a limited partnership regime for funds</u>

34. At the meeting on 2 December 2019, the Administration consulted the Panel on the legislative proposal to establish a limited partnership regime for funds ("LPF regime") in Hong Kong. Under the proposal, a limited partnership fund ("LPF") would be an arrangement meeting the definition of fund that was structured in a limited partnership form, and would be constituted by at least two partners (one general and one limited) under a written agreement. The general partner of an LPF would have unlimited liability in respect of the debts and liabilities of the fund and ultimate responsibility for the management and control of the fund, while the limited partner(s) of an LPF would not have day-to-day management rights or control over the underlying assets held by the fund and hence their liability would generally be limited up to the commitment they made to the fund.[2]

35. Members welcomed the proposed LPF regime in general and sought details on the benefit of introducing the regime for Hong Kong. Members also sought the Administration's view on the competitiveness of the proposed LPF regime vis-à-vis similar regimes in other jurisdictions in particular with regard to the confidentiality protection for limited partners (i.e. investors of the fund) and preferential tax treatment for funds offered by other jurisdictions.

36. On the benefits of the LPF regime, the Administration pointed out that as a result of the global implementation of the Base Erosion and Profit Shifting package of the Organisation for Economic Co-operation and Development ("OECD"), which required taxation to happen where asset management activities took place, funds would be incentivized to align their structures with business activities and move from offshore to onshore. The LPF regime would attract more investment funds to establish and operate in Hong Kong, and would in turn increase the demand for local professionals such as lawyers, accountants, auditors and investment managers, and would benefit Hong Kong's financial services industry in the long run. Regarding competitiveness, the Administration believed that the proposed LPF regime would be as competitive as those of other jurisdictions including Singapore. Moreover, under the proposed LPF regime, the confidentiality protection extended to limited partners was on a par with that adopted by other offshore fund centres, like the Cayman Island.

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[2] The Limited Partnership Fund Bill received its First Reading at the Legislative Council ("LegCo") meeting of 10 June 2020. The Administration has given notice to resume the Second Reading debate on the Bill at the LegCo meeting of 8 July 2020.

37. As there would be no qualification requirement on the investment managers of an LPF, members expressed concern as how investors' interests would be protected. Given that the general partners of an LPF had to bear unlimited liability in respect of the debts and liabilities of the fund and ultimate responsibility for the management and control of the fund, some members also enquired whether there would be qualification requirements on the general partners.

38. The Administration explained that the proposed LPF regime allowed the general partners of an LPF to appoint a person who was not a licensee of the SFC to be the investment manager if the fund did not engage in SFC's regulated activities. This proposal was made having considered that investors of an LPF were generally large institutional investors (such as sovereign wealth funds and pension funds) who would carry out risk assessments and were well-placed in protecting their own interests. As regards qualification requirements of the general partners, the Administration advised that other comparable jurisdictions did not impose any qualification requirements on such partners. It was anticipated that in practice the general partners of LPFs would possess relevant professional qualifications or experience, or otherwise it would be difficult for them to persuade investors (who were usually large institutional investors) to invest in the funds.

Promoting development of the insurance industry in Hong Kong

39. The Panel received a briefing by the Administration and the Insurance Authority ("IA") at the meeting on 2 December 2019 on the progress in taking forward initiatives in promoting development of the insurance industry in Hong Kong, including modernizing the insurance regulatory framework, enhancing competitiveness and promoting market development, and developing Insurtech. As it was envisaged that IA would face a funding shortfall in 2020-2021 and the subsequent few years, the Administration also consulted the Panel on the proposal to provide a capital injection of $300 million to IA to assist it to tide over the projected cash shortfall in the short to medium term and to maintain an appropriate level of reserve.[3]

40. In response to members' enquiries on the progress of enhancing market access of the local insurance industry to the Guangdong-Hong Kong-Macao Greater Bay Area ("the Greater Bay Area"), the Administration advised that the Central Government had announced three policy measures related to the insurance sector, namely (a) supporting Mainland insurers to issue catastrophe

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3 The capital injection was incorporated in the Appropriation Bill 2020 which was passed at the LegCo meeting of 13 May 2020.

bonds in Hong Kong; (b) extending the preferential treatment to Hong Kong qualified reinsurers under the "China Risk Oriented Solvency System"; and (c) removing the requirement on years of operating experience for Hong Kong service suppliers to provide insurance loss adjusting services in the Mainland. The Administration assured members that it would continue to liaise with the relevant Mainland authorities on other initiatives such as cross-boundary motor vehicle insurance products and setting up of after-sale service centres. On the development of cross-boundary motor vehicle insurance policies that involved different legal regimes in the Mainland, Hong Kong and Macao, mutual recognition might be able to engineer a breakthrough.

41. While members in general had no objection to provide IA with a capital injection, they expressed concern whether IA would suffer from a persistent operating deficit in the foreseeable future, and whether it could achieve the ultimate goal of becoming financially independent from the Administration. Some members further enquired if IA would consider adjusting its current levy rate on insurance premiums in order to achieve financial independence as soon as possible. Members also sought clarification on whether the provision of capital injection was the Administration's usual practice in providing additional funding to statutory bodies.

42. Some members, however, were opposed to the proposal of providing IA with a capital injection, and considered that the funding should be made in the form of an interest-bearing loan. These members also enquired how IA would bridge its funding gap and achieve a break even position in its budget as soon as possible.

43. The Administration and IA explained that IA's funding shortfall in 2020-2021 was mainly attributed to a longer lead time required to complete the takeover of regulatory responsibilities from the former Office of the Commissioner of Insurance which resulted in delay in the collection of premium levies and authorization/annual fees (amounting to some $260 million) from insurers, as well as lower actual income as compared with the estimates adopted in preparing IA's indicative budget which was used to work out the initial capital injection of $650 million. The proposed additional funding would help IA tide over its projected cash shortfall in the short to medium term and allow it to maintain a modest reserve. If the proposed additional funding was made in the form of a loan, it might be more difficult for IA to achieve full financial independence and maintain an appropriate level of reserve. This was because IA's existing funding model effectively prevented it from building up excessive reserves. Under the Insurance Ordinance (Cap. 41), when the reserves of IA were more than twice its estimated operating expenses for the financial year (after deducting depreciations and all provisions) and subject to

no outstanding borrowing, IA had to consult FS with a view to recommending to the Chief Executive in Council that the rate or amount of a levy be reduced. As regards the provision of funding to statutory bodies in the financial services sector, the Administration usually provided additional funding to them in the form of direct capital injection in their initial years of operation, such as the two direct capital injections provided to SFC during its initial years of operation, and an injection of $5 billion to the Mandatory Provident Fund Schemes Authority ("MPFA") for its establishment.

Progress update on the eMPF Platform

44. At the meeting on 2 December 2019, the Administration and MPFA updated members the latest development on establishing a common electronic platform ("eMPF Platform") to facilitate the standardization, streamlining and automation of Mandatory Provident Fund ("MPF") scheme administration processes. The Administration also proposed to incorporate additional functionalities in the eMPF Platform and provide funding for the initial operation of the subsidiary company wholly-owned by MPFA for running the Platform (i.e. "eMPF Platform Company"). The Panel noted that an additional funding of $536.48 million would be required for enhancing the infrastructure of the eMPF Platform and funding the set-up and first two years' operation of the eMPF Platform Company.[4]

45. While members in general had no objection to the proposed additional funding for developing the eMPF Platform, some members considered that the funding should be provided in the form of a loan instead of direct grant by the Administration in order to facilitate LegCo's monitoring on the use of public money.

46. The Administration advised that the decentralized MPF scheme administration, cumbersome administration processes, and different commercial models of trustees had contributed to the high administration cost of the MPF System. Therefore MPFA had proposed developing the eMPF Platform to maximize operational efficiency of MPF schemes with a view to creating more room for fee reduction so as to benefit scheme members. The eMPF Platform was financed by public money and would be a public infrastructure operated by

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[4] The additional funding of $536.48 million was incorporated in the Appropriation Bill 2020 which was passed at the LegCo meeting of 13 May 2020. The Mandatory Provident Fund Schemes (Amendment) Bill 2019 (which seeks to empower the Mandatory Provident Fund Schemes Authority to establish the eMPF Platform Company) received its First Reading at the LegCo meeting of 23 October 2019. The Administration has given notice to resume Second Reading Debate on the Bill at the LegCo meeting of 8 July 2020.

the eMPF Platform Company. Providing direct grant to the eMPF Platform Company would provide necessary incentive to trustees to centralize, streamline and standardize their currently inefficient scheme administration procedures. On the contrary, an interest-bearing loan could push up the administrative cost of using the eMPF Platform and thus the fee to be paid by scheme members, which would defeat the ultimate purpose of bringing fee reduction to scheme members.

47. Members urged that the Administration and MPFA should develop measures to ensure scheme members could benefit from fee reduction as early as possible after the launch of the eMPF Platform.

48. The Administration reiterated that the major objective of developing the eMPF Platform was to create room for reducing the administration fee of MPF schemes. It was expected that the fee level would be driven down as the centralization of scheme administration would bring higher efficiency to the MPF System. Also, the digitalization of scheme administration would help tackle the high administration fee of MPF schemes caused by the huge manpower cost in undertaking scheme management and the reliance on paper-based MPF transactions by a large number of scheme members and some trustees. The eMPF Platform Company would be a non-profit making entity, and would not seek to make profit from managing MPF schemes. Moreover, the lower threshold to enter the MPF market would attract smaller firms to enter the market as trustees, and the competition among trustees would further create room for lowering the administration fee of MPF schemes. Given that the success of the eMPF Platform would depend on its take-up rate, the Administration and MPFA would endeavor to boost the digital take-up of the Platform to ensure it would effectively lower the administration fee of MPF schemes.

**Other work**

49. During the 2019-2020 legislative session, the Panel also discussed with the Administration and related bodies a number of subjects. The major ones are:

(a) funding/legislative/establishment proposals, including:

(i) providing electricity charges subsidies to eligible residential electricity accounts;[5]

(ii) enhancing and relocating the Information Technology systems and facilities of the Inland Revenue Department;[6]

(iii) implementation of an Electronic Submission System for the Official Receiver's Office;[7]

(iv) implementing OECD's recommendations regarding the legislative framework for automatic exchange of financial account information in tax matters in Hong Kong;[8] and

(v) creation of a permanent Principal Valuation Surveyor post in the Government Property Agency to oversee the property and facilities management of the boundary control points;

(b) briefings on the work of the Financial Services Development Council and the work of the Financial Reporting Council in 2019, and on the proposed budget of IA for the financial year 2020-2021; and

(c) update on the development of financial technologies in Hong Kong.

50. From October 2019 to June 2020, the Panel has held a total of 10 meetings, including a joint meeting with the Panel on Commerce and Industry, the Panel on Economic Development and the Panel on Information Technology and Broadcasting to discuss the economic impact on Hong Kong arising from the social incidents and changes to external environment in 2019, as well as another joint meeting with the Panel on Economic Development on the Government's investment in Cathay Pacific Airways Limited under the Land

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5 The funding proposal (i.e. FCR(2019-20)39) was approved by the Finance Committee ("FC") at its meeting on 6 December 2019.

6 The funding proposal (i.e. FCR(2020-21)8) has been submitted to FC for approval.

7 The funding proposal (i.e. FCR(2020-21)32) has been submitted to FC for approval.

8 The relevant subsidiary legislation (i.e. Inland Revenue Ordinance (Amendment of Section 50A) Notice 2020 and Inland Revenue Ordinance (Amendment of Schedule 17D) Notice 2020) were tabled at LegCo for negative vetting at the meeting of 22 April 2020.

Fund to uphold Hong Kong's status as an international aviation hub amidst the threat arising from COVID-19.

Council Business Division 1
Legislative Council Secretariat
8 July 2020

**Appendix I**

# Legislative Council

## Panel on Financial Affairs

## Terms of Reference

1. To monitor and examine Government policies and issues of public concern relating to financial and finance matters.

2. To provide a forum for the exchange and dissemination of views on the above policy matters.

3. To receive briefings and to formulate views on any major legislative or financial proposals in respect of the above policy areas prior to their formal introduction to the Council or Finance Committee.

4. To monitor and examine, to the extent it considers necessary, the above policy matters referred to it by a member of the Panel or by the House Committee.

5. To make reports to the Council or to the House Committee as required by the Rules of Procedure.

**Appendix II**

## Panel on Financial Affairs

## Membership list for 2019 - 2020 session*

| | |
|---|---|
| **Chairman** | Hon Christopher CHEUNG Wah-fung, SBS, JP |
| **Deputy Chairman** | Hon Kenneth LEUNG |
| **Members** | Hon James TO Kun-sun<br>Hon Abraham SHEK Lai-him, GBS, JP<br>Hon Jeffrey LAM Kin-fung, GBS, JP<br>Hon WONG Ting-kwong, GBS, JP<br>Hon Starry LEE Wai-king, SBS, JP<br>Hon CHAN Kin-por, GBS, JP<br>Hon Mrs Regina IP LAU Suk-yee, GBS, JP<br>Hon WU Chi-wai, MH<br>Hon Charles Peter MOK, JP<br>Hon Alice MAK Mei-kuen, BBS, JP<br>Hon Dennis KWOK Wing-hang<br>Hon Martin LIAO Cheung-kong, GBS, JP<br>Ir Dr Hon LO Wai-kwok, SBS, MH, JP<br>Hon CHU Hoi-dick<br>Hon Holden CHOW Ho-ding<br>Hon SHIU Ka-fai, JP<br>Hon CHAN Chun-ying, JP<br>Hon CHEUNG Kwok-kwan, JP |
| | (Total：20 members) |
| **Clerk** | Ms Connie SZETO |
| **Legal Adviser** | Ms Clara TAM |

* Changes in membership are shown in Annex.

# Panel on Financial Affairs
## Changes in membership

| **Member** | **Relevant date** |
|---|---|
| Hon Jimmy NG Wing-ka, BBS, JP | Up to 17 October 2019 |
| Hon Paul TSE Wai-chun, JP | Up to 24 October 2019 |
| Hon Steven HO Chun-yin, BBS | Up to 25 October 2019 |
| Hon POON Siu-ping, BBS, MH | Up to 25 October 2019 |
| Dr Hon CHIANG Lai-wan, SBS, JP | Up to 27 October 2019 |
| Hon WONG Kwok-kin, SBS, JP | Up to 27 October 2019 |
| Hon LUK Chung-hung, JP | Up to 27 October 2019 |
| Hon Frankie YICK Chi-ming, SBS, JP | Up to 27 October 2019 |
| Hon YIU Si-wing, BBS | Up to 28 October 2019 |
| Hon Elizabeth QUAT, BBS, JP | Up to 28 October 2019 |
| Hon CHAN Han-pan, BBS, JP | Up to 28 October 2019 |
| Hon MA Fung-kwok, SBS, JP | Up to 29 October 2019 |
| Hon Tony TSE Wai-chuen, BBS | Up to 30 October 2019 |
| Hon CHAN Hak-kan, BBS, JP | Up to 1 November 2019 |
| Hon AU Nok-hin | Up to 16 December 2019 |