

立法會
Legislative Council

LC Paper No. CB(1)634/01-02
(These minutes have been
seen by the Administration)

Ref : CB1/PL/FA/1

Legislative Council
Panel on Financial Affairs

Minutes of Meeting held on
Monday, 5 November 2001 at 9:30 am
in the Chamber of the Legislative Council Building

Members present : Hon Ambrose LAU Hon-chuen, GBS, JP (Chairman)
Hon Henry WU King-cheong, BBS (Deputy Chairman)
Hon James TIEN Pei-chun, GBS, JP
Hon Albert HO Chun-yan
Hon LEE Cheuk-yan
Hon Eric LI Ka-cheung, JP
Dr Hon David LI Kwok-po, GBS, JP
Hon NG Leung-sing, JP
Hon James TO Kun-sun
Hon Bernard CHAN
Hon CHAN Kam-lam
Hon SIN Chung-kai
Dr Hon Philip WONG Yu-hong
Hon Jasper TSANG Yok-sing, JP
Hon Emily LAU Wai-hing, JP
Hon MA Fung-kwok

Non-Panel members : Hon CHAN Yuen-han, JP
attending Hon LAU Kong-wah
Hon Albert CHAN Wai-yip
Hon LEUNG Fu-wah, MH, JP
Hon Audrey EU Yuet-mee, SC, JP

**Public officers
attending**

: For item IV

Mr Joseph YAM, JP
Chief Executive
Hong Kong Monetary Authority

Mr David CARSE, JP
Deputy Chief Executive
Hong Kong Monetary Authority

Mr Norman CHAN, SBS, JP
Deputy Chief Executive
Hong Kong Monetary Authority

Mr Anthony LATTEER, JP
Deputy Chief Executive
Hong Kong Monetary Authority

For item V

Mr Stanley WONG
Deputy Secretary for Financial Services

Mr Joseph YAM, JP
Chief Executive
Hong Kong Monetary Authority

Mr David CARSE, JP
Deputy Chief Executive,
Hong Kong Monetary Authority

Mr Y K CHOI
Executive Director (Banking Supervision)
Hong Kong Monetary Authority

Mr Peter WONG
Chairman, Hong Kong Association of Banks
Chief Executive and General Manager,
Hong Kong Standard Chartered Bank

Mr C H LO
Representative, Hong Kong Association of Banks
Deputy General Manager,
Bank of China (Hong Kong) Limited

Mr Dicky YIP
Representative, Hong Kong Association of Banks
Senior Executive Deputy Head of
Personal Financial Services
HSBC

For item VI

Mr Stanley WONG
Deputy Secretary for Financial Services

Mr Eddie YUE
Executive Director (Corporate Services)
Hong Kong Monetary Authority

For item VII

Representatives from the Administration

Mr Stanley WONG
Deputy Secretary for Financial Services

Miss Clara TANG
Principal Assistant Secretary for Financial Services

Mr NG Hon-wah
Principal Assistant Secretary for Home Affairs

Mr Y K CHOI
Executive Director (Banking Supervision)
Hong Kong Monetary Authority

Mr Arthur YUEN
Head (Banking Supervision)
Hong Kong Monetary Authority

Representatives from concerned banks for the
"Bank of East Asia, Limited (Merger) Bill"

Mr CHAN Kay-cheung
Executive Director, The Bank of East Asia, Ltd.

Mr Daniel WAN
Chief Executive Officer, First Pacific Bank

Mr Alan COLLINS
General Counsel, The Bank of East Asia, Ltd.

Ms Mimi KAM
Head of Merger Management Office
The Bank of East Asia, Ltd.

Ms Amy LO
Partner, Clifford Chance

Mr Rolfe HAYDEN
Solicitor, Clifford Chance

Representatives from concerned banks for the
"Mizuho Corporate Bank, Limited (Hong Kong
Consolidation) Bill"

Mr Tomonori KOBAYASHI
Chairman of the Hong Kong Consolidation
Committee, and General Manager, The Fuji Bank,
Limited, Hong Kong Branch

Mr Yoshiyuki TOYODA
General Manager, The Dai-Ichi Kangyo Bank,
Limited,
Hong Kong Branch

Mr Makoto MASUDA
General Manager, The Industrial Bank of Japan,
Limited,
Hong Kong Branch

Mr Hiroshi FUJIMOTO
Joint General Manager, The Fuji Bank, Limited,
Hong Kong Branch

Ms Maggie CHEUNG
Manager - Compliance, The Fuji Bank, Limited,
Hong Kong Branch

Ms Junri KONII
Partner, Baker & McKenzie

Mr Charles KINSLEY
Senior Tax Manager, KPMG

For item VIII

Miss Susie HO
Deputy Secretary for Financial Services

Action

Mr G W E JONES
Registrar of Companies

Mr T C HO
Business Manager, Companies Registry

Miss Peggy LAU
Development Manager, Companies Registry

Clerk in attendance : Ms Anita SIT
Chief Assistant Secretary (1)6

Staff in attendance : Ms Pauline NG
Assistant Secretary General 1

Mr Jimmy MA
Legal Adviser
(for item VI only)

Ms Bernice WONG
Assistant Legal Adviser 1
(for item VII only)

Mr WONG Tin-yau, Anthony
Senior Assistant Secretary (1)8

I Confirmation of minutes of meeting and matters arising
LC Paper No. CB(1) 125/01-02 - Minutes of meeting held on
11 October 2001

The minutes of the Panel meeting held on 11 October 2001 were confirmed.

II Information papers issued since last meeting
LC Paper No. CB(1) 91/01-02 - "Mandatory Provident Fund Schemes
Statistical Digest"

LC Paper No. CB(1) 174/01-02 - "Impact of the 11 September 2001
Terrorist Attacks on the Insurance
Industry"

2. Members noted that the above papers had been issued since last meeting.

Action

III Date and items for discussion for the next meeting

LC Paper No. CB(1) 169/01-02(01) - List of outstanding items for discussion

LC Paper No. CB(1) 169/01-02(02) - List of Follow-up Actions

3. In line with the agreed arrangement that the Financial Secretary (FS) would brief the Panel on Hong Kong's latest economic situation on a regular basis, members agreed that FS should be invited to give the next briefing at the regular Panel meeting on 3 December 2001. Members also agreed that pursuant to the relevant advice of the House Committee on 2 November 2001, the Panel should invite FS to brief Members on his recent visit to Beijing at the same meeting. Miss Emily LAU suggested and members agreed that FS's briefing on the two topics should be conducted separately, and to allow sufficient time for discussion, the discussion on each topic should be allocated about one hour.

4. Pursuant to the advice of the House Committee on 2 November 2001 that the Panel should invite the Commissioner for Census and Statistics to brief Members on the Summary Results of the 2001 Population Census, members agreed that a special meeting for the briefing would be held on 8 November 2001 at 4.30 pm.

IV Briefing by the Chief Executive of the Hong Kong Monetary Authority

LC Paper No. CB(1) 169/01-02(03) - Presentation material prepared by the Hong Kong Monetary Authority

Briefing by the Chief Executive of the Hong Kong Monetary Authority

5. The Chief Executive of the Hong Kong Monetary Authority (CE/HKMA) gave a power-point presentation to update the Panel on the work of the Hong Kong Monetary Authority in its four main areas of responsibilities, namely, maintaining currency stability, promoting the safety and stability of the banking system, enhancing the efficiency, integrity and development of the financial infrastructure, and the management of the Exchange Fund.

6. In his preamble, CE/HKMA highlighted that while the economy had deteriorated as a result of the recent terrorist attacks in the United States (US), thus increasing financial risks for Hong Kong, HKMA had been coping with these challenges and continuing its work in the four main areas successfully.

Action

Currency stability - risks

7. CE/HKMA said Hong Kong's economy had suffered under the current global economic slowdown. Notwithstanding the stability of the US dollar, there could be pressure on the Asian currencies, including the Hong Kong dollar, should significant fluctuations in the financial and equity markets occur. He then explained the specific risk factors relevant to Hong Kong. CE/HKMA said that continued support for and confidence in the linked exchange rate system (the Link) was crucial to maintaining stability for Hong Kong. He said that the Link had served Hong Kong well in the past. Each monetary regime had its pros and cons, but in Hong Kong's case the advantages of the Link far outweighed its disadvantages.

Banking - reform measures

8. Turning to the banking sector, CE/HKMA said that despite difficult times, the banking sector had been stable, and reforms were continuing. Interest rate deregulation had been implemented in full since 3 July 2001. A working group under HKMA was considering the proposal of setting up a Commercial Credit Reference Agency. Consultation was being carried out on the technical aspects of the Deposit Insurance Scheme. It was hopeful that the draft legislation for the scheme would be ready by the end of 2002. The Three-building Condition applicable to foreign banks licensed since 1978 was due to be removed before the end of 2001. On consumer protection, HKMA was gathering public response to its comparative study published in late April 2001 and awaiting the results of the research on similar issues being conducted by the Legislative Council Secretariat. While the revised Code of Banking Practice was being finalized and would be published shortly, HKMA was also consulting banks on a guideline to be issued on complaint handling procedures to improve standards of banking services.

Banking - current issues

9. CE/HKMA said that HKMA had reminded banks of their obligation to supply information to relevant authorities on terrorist financing and money laundering. Turning to the rising trend of personal bankruptcy, CE/HKMA advised that a high level round-table discussion among the Hong Kong Association of Banks, the Financial Services Bureau, the Official Receiver, the Privacy Commissioner, and the HKMA was recently held. One of the measures identified was to expand the scope of consumer credit data sharing to include more positive data with a view to enhancing credit risk assessment by banks.

Financial Infrastructure

10. CE/HKMA advised that the Hong Kong dollar and US dollar payment systems in Hong Kong had functioned smoothly despite the "911" incident and

Action

HKMA had been encouraging greater usage of the US dollar payment system by banks to reduce and diversify risk. In the light of current low deposit interest rates, HKMA was seeking to develop Hong Kong's retail bond market through debt issues by the Hong Kong Mortgage Corporation Limited as a low-risk investment alternative for investors. HKMA had conducted a review of retail payment systems in Hong Kong. The review concluded that the systems generally functioned well, with no major shortcomings that would pose a risk to the systematic stability of Hong Kong's financial system or to public confidence. Work on upgrading the Central Moneymarkets Unit (CMU) into an International Central Securities Depository was in good progress and the two-way linkage with Euroclear and the modernization of the CMU was scheduled for completion by end-2002. The Working Group on Money Settlement for the Central Clearing and Settlement System (CCASS) items had identified deficiencies in the money settlement arrangement and had proposed a number of recommendations.

Exchange Fund

11. Referring to the Exchange Fund Balance Sheet tabled, CE/HKMA pointed out that the item "Placements by other Hong Kong Special Administrative Region government funds" under "Liabilities and Accumulated Surplus" had reduced from \$439,228 million in March 2001 to \$375,572 million in October 2001 due to drawdown to finance the fiscal deficit for the period. From January to September 2001, there was a loss of HK\$ 40 billion on Hong Kong equities and an exchange loss of HK\$6.4 billion. These losses were partly offset by a return of HK\$40.2 from bonds, giving a net loss of HK\$ 6.2 billion in investment income. Figures for January to October 2001, however, showed that return on bonds increased to HK\$52.8 billion, giving a net investment income of HK\$ 6.1 billion. The equity portfolio held by the Exchange Fund was valued at HK\$75.2 billion as at the end of October 2001. Part of the portfolio would be disposed of at an appropriate time while the remaining part would be held as long-term investment.

Discussion with Members

The linked exchange rate system

12. Mr James TIEN expressed concern that the Link in tying Hong Kong to the US interest rates prevented Hong Kong from having an independent monetary policy to flexibly resolve its own economic problems. With the Mainland's impending entry into the World Trade Organization and the possibility of the Renminbi becoming freely convertible, Mr TIEN sought clarification on Government's long-term monetary policy for the Hong Kong dollar. CE/HKMA replied that while the Link had imposed limitations on Hong Kong's monetary policy, the benefits of maintaining the Link far outweighed the disadvantages. HKMA had conducted a number of studies which concluded that there was no better or less risky alternative system to the Link given the characteristics of the Hong Kong economy. The decrease in demand for exports

Action

was due to the adverse US economic conditions, which could hardly be improved by devaluating the Hong Kong dollar. Alternatively, giving up the Link might seriously undermine the confidence in Hong Kong's currency and cause inflation, which in turn might increase interest rates.

13. As regards the possible impact on the Hong Kong dollar of possible changes in the Renminbi exchange rate system, CE/HKMA advised that as Hong Kong maintained an independent currency system, the changes in the Mainland's policy for the Renminbi would not affect the determination of Hong Kong SAR Government in maintaining the Link. While there might be more flexibility given for the Renminbi, he did not envisage that it would become freely convertible in the foreseeable future. He however welcomed more discussion on the relationship between Renminbi and the Hong Kong dollar in the light of growing interdependence of the economies of the Mainland and Hong Kong.

14. Mr Albert HO recalled that in the recent World Economic Forum, there was suggestion of establishing an Asian currency system. He enquired about the Administration's view in this regard and asked whether pursuing this system would provide an opportunity for Hong Kong to de-link the Hong Kong dollar from the US dollar. In response, CE/HKMA replied that this was a subject arising from the Asian financial crises in 1997 and 1998, which revealed that many Asian economies, being small and open economies, were subject to significant impact of volatile capital flow to and from these economies. Theoretically, developing a common currency among these Asian economies would in effect create an enlarged economy with greater strength to withstand challenges posed by external financial and economic factors. CE/HKMA said that he did not envisage that this development would materialize in the foreseeable future, as there was no indication that the Asian economies as a whole concerned had the determination to pursue this development.

Purchase of new office for HKMA

15. Miss Emily LAU questioned if the purchase of the new office for HKMA was still considered as a sound investment, or if the value of the office had fallen substantially to become a negative equity since April 2001 when the Memorandum of Understanding for the purchase was signed. CE/HKMA replied that the decision to purchase the new office was arrived at after careful consideration of various factors including its cost-effectiveness. As the purchase was a long-term investment, it should not be assessed against short-term price fluctuations. He also clarified that as the office purchase was not financed by borrowings, negative equity was not an issue.

Performance of the Exchange Fund

16. Miss Emily LAU enquired how the performance of the Exchange Fund compared with other investment funds. Noting that the total asset value of the Exchange Fund had reduced to below HK\$1000 billion as at end October 2001,

Action

she asked if CE/HKMA would consider reducing his salary voluntarily in the light of the performance of the Exchange Fund.

17. Regarding the performance of the Exchange Fund, CE/HKMA pointed out that although the investment environment had been difficult throughout the year, the investment return on the Exchange Fund for the period January to October 2001 compared favourably to many other investment funds. He remarked that the reduction of the asset value of the Exchange Fund to below HK\$1000 billion was mainly due to the drawing on the fiscal reserves placed with the Exchange Fund by the Government to meet the fiscal deficit during the period.

18. As regards salary adjustment for HKMA staff, CE/HKMA advised that the salary of HKMA staff was approved by the Financial Secretary in consultation with the Exchange Fund Advisory Committee having regard to the results of the annual surveys on salary levels and trends in the financial services sector conducted by independent consultants engaged by HKMA, and with reference to the achievements of HKMA in the preceding year. The next annual survey would be conducted in early 2002. He said that he personally would accept a reduction in salary if this was in line with the trend in the financial services sector. He remarked that the basic salary of HKMA's management staff had not been increased since 1998. In reply to Miss Emily LAU's further enquiry, CE/HKMA advised that the variable component of the remuneration for HKMA staff, on average, accounted for about 15% of the entire remuneration package, and the amount disbursed depended on the performance of individual staff members.

19. Mr NG Leung-sing noted that domestic lending of the banking sector continued to shrink. The quarterly decline rate accelerated from 0.4% in the second quarter to 1.7% in the third quarter of 2001. He asked whether HKMA would work with banks to consider measures to improve the situation, such as raising the 70% loan-to-value lending ratio for mortgage loans, lengthening the repayment period and relaxing the deadline for repayment etc. CE/HKMA clarified that the terms of mortgages and other loans were essentially the commercial decisions of banks, though HKMA provided guidelines pertinent to prudent regulation of the banking sector, such as the 70% loan-to-value guideline. He considered that decisions regarding the schedule of loan repayment should be left to banks as they were in a better position to evaluate their respective risk acceptance levels. He also remarked that HKMA must be very cautious in considering any changes to the prevailing policy or guidelines for banks as such changes might adversely affect the credit rating of Hong Kong.

20. Mr Henry WU observed that some banks and on-line brokers had recently reduced their brokerage commission to below the minimum rate of 0.25% and/or offered rebate to vie for customers. He questioned that these activities might be unfair to other brokers who had to observe the minimum brokerage rule, even though this was scheduled for abolishment on 1 April 2002.

Action

CE/HKMA responded that generally, HKMA supported fair competition provided that market order and stability was not adversely affected. The Deputy Chief Executive, HKMA (DCE/HKMA) supplemented that currently when a bank executed a customer's order for a security transaction, it had to pay the minimum commission of 0.25% to its broker regardless of whether the broker concerned was within the same group or a third-party entity, as in both cases, the broker was a member of the Hong Kong Stock Exchange subject to the minimum brokerage commission rule. It was however up to the bank to make a commercial decision as to how much the commission would be passed onto its customers. HKMA would not interfere with banks' commercial decisions in this regard.

21. On behalf of the Panel, the Chairman thanked CE/HKMA and his colleagues for attending the meeting.

V Residential mortgage loans in negative equity

LC Paper No. CB(1) 169/01-02(04) - Information paper provided by the Administration

LC Paper No. CB(1) 231/01-02(02) - Supplementary information on Residential Mortgage Loans in Negative Equity - Results of Survey on Loans Associated with Co-financing Schemes provided by HKMA

22. On behalf of the Panel, the Chairman welcomed representatives of the Hong Kong Association of Banks (HKAB) and the Administration for attending the meeting to discuss this agenda item.

23. At the invitation of the Chairman, Mr Peter WONG, the Chairman of the Hong Kong Association of Banks (HKAB), briefly outlined the position of HKAB on the issue of negative equity, the measures banks were taking to assist property owners in negative equity, and the considerations which banks had to take into account in taking these measures. He highlighted the following points -

- (a) Banks and customers were on the same side, as customers defaulting on their mortgage loans would only increase the bad debts borne by banks;
- (b) Banks were only able to assist owner-occupants but not property speculators as the risks involved were different;

Action

- (c) Negative equity was not simply an interest rate issue, but a matter of repayment ability, and banks in assisting homeowners with negative equity would focus on enabling these homeowners to continue with their loan repayment; and
- (d) Interest rate should be determined by the market. Compelling banks to reduce interest rates to assist homeowners with negative equity would affect Hong Kong's status as a free market and an international financial centre.

24. On the measures taken by banks to assist homeowners with negative equity, Mr Peter WONG advised that banks had offered various relief arrangements including the provision of loan refinancing packages at a lower mortgage interest rate, extending the repayment period up to forty years, suspending the requirement to repay the loan principal, and other loan restructuring arrangements. Mr WONG remarked that in pursuing these arrangements, banks must be very prudent so as not to adversely affect depositors' interest and banks' own credit ratings by international credit rating agencies. Should banks' credit ratings fall as a result of these measures, the cost of funds for banks would rise and such additional cost would partly be passed onto customers.

25. At the invitation of the Chairman, CE/HKMA advised that HKMA in principle would support measures by banks to improve the quality of their loans, whether by loan restructuring or other means. He said that while HKMA would not object to authorized institutions refinancing residential mortgage loans (RMLs) in negative equity up to 100% of the current market value of the mortgaged property, HKMA maintained that the 70% loan-to-value guideline for RMLs remained generally appropriate as a long-term prudent lending criteria. On the interest rates for RMLs, CE/HKMA said that competition between banks had already driven down the interest rates significantly and this had in turn benefited some property owners with negative equity.

26. In presenting the supplementary information on "Residential Mortgage Loans in Negative Equity - Results of Survey on Loans Associated with Co-financing schemes provided by the HKMA" tabled, DCE/HKMA advised that the ad hoc survey was conducted among banks and covered only owner-occupied properties. The survey did not cover investment properties or properties financed under the Home Ownership Scheme, Private Sector Participation Scheme and Tenants Purchase Scheme. DCE/HKMA explained that according to the survey, there were some 21 400 cases of RMLs associated with co-financing schemes. Of these, about 5 400 cases had already been included in the 65 000 cases of RMLs in negative equity (where only the first mortgages in the banking sector were taken into account). Assuming that all the remaining 16 000 cases of RMLs associated with co-financing loans were in negative equity, the number of RMLs in negative equity when second mortgages were also taken into account would add up to 81 000 cases in total.

Action

Discussion with members

27. Mr LEE Cheuk-yan commented that the most effective means to assist negative equity homeowners was interest rate reduction and he therefore urged banks to consider giving higher priority to this relief arrangement. In response, Mr Peter WONG said that banks would be willing to assist negative equity homeowners but whether this would be in the form of refinancing at a lower interest rate or other arrangements would depend on the circumstances of individual cases. He reiterated that banks needed to balance different considerations including their overall portfolio of RMLs, the nature and extent of risks associated with individual cases in making such arrangements.

Admin. 28. At Mr LEE's request, the Administration agreed to provide a further breakdown of the number of cases of RMLs in negative equity under the category of ">BLR to BLR + 2%" (where BLR represents Best Lending Rate).

29. Mr LAU Kwong-wah highlighted that banks were unwilling to consider any relief arrangements for negative equity owners of the Sandwich Class Housing Scheme (SCHS) flats if these owners had taken out second mortgages with the Hong Kong Housing Society (HKHS). He was given to understand that the HKHS had subsequently sold the second mortgages to the Hong Kong Mortgage Corporation Limited (HKMC). He urged HKMA to discuss with banks and HKMC to see if the concerned parties could take any measure to assist these negative equity homeowners.

Admin. 30. CE/HKMA responded that as far as he understood, the owners of the SCHS flats were not required to repay the second mortgage loans for a period of three to five years and the interest rate charged by banks on their first mortgages was relatively low, tantamount to a rate of around Best Lending Rate minus 1.75%. Stating that HKMA's objective was to strengthen the asset quality of banks pursuant to maintaining the stability of the banking sector, CE/HKMA agreed to initiate discussion with HKAB and HKMC to see if any arrangement could be made to assist the negative equity owners of SCHS flats.

31. Miss Emily LAU expressed appreciation to HKAB for attending the meeting to exchange views with members on the issue of negative equity. She said that members did not intend to put pressure on the banking sector but would like to work in collaboration with the sector to identify feasible measures to address the problem of negative equity. She then asked if the banking sector had come to any general agreement on the measures to be taken to assist negative equity property homeowners.

32. In response, Mr Peter WONG clarified he had no authority to interfere with individual banks' commercial decisions. He explained that the problem of negative equity had existed for some time and banks had taken various measures to assist negative equity property owners to enable them to continue with their

Action

mortgage repayment without resorting to bankruptcy. He promised that HKAB would initiate further discussion of the issue among its member banks and members' views would be duly reflected to the member banks.

33. Mr Albert CHAN said that while banks had announced that they were willing to assist negative equity homeowners, he understood that many negative equity homeowners, especially those who were most desperate for a respite, had encountered much difficulty when they approached banks at the branch level for loan restructuring arrangements. Some of the reasons given by the branch managers were the negative equity homeowners' poor repayment history or HKMA's relevant guidelines. He therefore requested HKAB and HKMA to clarify banks' policies and HKMA's relevant guidelines respectively.

34. Mr Albert HO Chun-yan expressed concern that instead of working out feasible loan restructuring arrangements, some banks adopted a very harsh approach towards negative equity homeowners. Even though the homeowners were willing to continue with loan repayment, these banks still threatened foreclosure or bringing the owner to court, which was contrary to the HKAB's announced policy of assisting negative equity homeowners.

35. Mr Henry WU referred to the paper CB(1) 169/01-02(04) and sought clarification on HKMA's guideline regarding banks' refinancing of RMLs for homeowners in negative equity. He was concerned that those negative equity homeowners who were in a transient period of financial hardship might not be able to benefit from the relaxed refinancing guideline.

36. CE/HKMA clarified that HKMA did not discourage banks from arranging loan re-structuring with homeowners in negative equity, and in fact such loan re-structuring was encouraged if it helped reduce the risk of loan delinquency. Regarding HKMA's advice to banks that it would not object if authorized institutions were to depart from the 70% guideline in refinancing RMLs for homeowners in negative equity while still observing normal prudent lending criteria, DCE/HKMA explained that the 70% loan-to-value guideline for RMLs provided a cushion to protect banks' asset quality at times of falling property prices. HKMA had to ensure that relaxing this guideline would not bring about undue additional risks to the banking system. HKMA therefore reminded banks that they should still observe the normal prudent lending criteria, such as the debt service ratio, when making refinancing loans. Mr Peter WONG said that to ensure the robustness of their own financial position vis-à-vis their risk exposure level, banks were required to act prudently according to HKMA's guidelines. He however agreed to convey members' concerns to the member banks of HKAB about the difficulties encountered by negative equity homeowners in seeking loan restructuring arrangements.

Action

37. Mr Albert CHAN suggested that HKMA should review the current 70% loan-to-value guideline for RMLs in view of the availability of 100% financing for buyers of newly completed properties. CE/HKMA explained that the 70% loan-to-value guideline was applicable to both second-hand and newly completed properties. It was through a second mortgage that buyers of newly completed properties could finance their purchase beyond the 70% level. The Executive Director (Banking Supervision), Hong Kong Monetary Authority added that there were means to finance the purchase of a second-hand property beyond the 70% level. An example was to take out insurance with the HKMC for financing up to 85% under the Mortgage Insurance Scheme.

38. Mr MA Fung-kwok sought clarification on the definition of negative equity in arriving at the figure of 65 000 cases of RMLs in negative equity. DCE/HKMA clarified that HKMA defined negative equity from the perspective of banks. The 65 000 cases of RMLs in negative equity covered those RMLs provided by the banking sector where the outstanding loan exceeded the current market value of the mortgaged property. However, the co-financing loans provided by lenders not regulated by HKMA had not been taken into account in arriving at the estimate of 65 000 cases of RMLs in negative equity.

39. To ascertain the extent and gravity of the negative equity problem, Mr Albert CHAN, Mr MA Fung-kwok and Mr James TO requested the Administration to provide more information on the actual number of cases of negative equity when co-financing loans were taken into account and the amount of outstanding loans vis-à-vis the current market value of the properties concerned. Mr MA said that figures showing the numbers of RMLs in positive equity by 10%, 5%, 0%, and RMLs in negative equity by -5%, -10%, -15% etc. would be useful for assessing the overall extent of the negative equity problem.

40. In response, CE/HKMA and DCE/HKMA acknowledged that the information collected by HKMA was restricted to RMLs in the banking sector but noted Members were concerned with the overall situation of negative equity which also involved loans taken out with financiers not subject to HKMA's regulatory purview. While pointing out that there would be difficulty in collecting the requested information, they agreed that HKMA would discuss further with HKAB and other concerned parties to see if further relevant information was available.

Admin.

41. Noting that the issue of negative equity also involved property developers and certain financiers not under the regulatory purview of HKMA, Miss Emily LAU suggested that the Panel should consider whether another meeting should be convened with the presence of all relevant parties to further discuss the issue. The Chairman said that Miss LAU's suggestion would be considered under the last agenda item "Any other business" of the meeting.

Action

VI Permanent accommodation for the Hong Kong Monetary Authority
LC Paper No. CB(1) 169/01-02(05) - Background brief on permanent accommodation for the Hong Kong Monetary Authority prepared by the LegCo Secretariat

42. The Deputy Secretary for Financial Services (DS/FS) updated members on the purchase of permanent accommodation for HKMA. He said that with the approval of FS, the Sale and Purchase Agreement for the purchase of 12 office floors and two auditorium floors at Two International Finance Centre had been signed on 5 October 2001. The total area of the premises purchased was 341 711 square feet and the purchase price was HK\$3,699 million. The expenditure had been charged to the Exchange Fund.

43. Regarding the legality of the office purchase, DS/FS recapitulated that pursuant to members' request, FS had sought the legal advice of the Department of Justice (DoJ) on the matter. In gist, DoJ was of the view that according to the Exchange Fund Ordinance (EFO) (Cap. 66), it was appropriate to charge the expenditure for the office purchase to the Exchange Fund. Specifically, section 6(b) of EFO provided that the Chief Executive might approve any incidental expenditure to be charged to the Exchange Fund as necessary for the due performance of the duties laid upon the Financial Secretary and the Exchange Fund Advisory Committee in connection with the operation of the Fund.

44. DS/FS further said DoJ had also examined the comments of the Legal Adviser of the Legislative Council Secretariat (LA) regarding the application of certain provisions in the Basic Law to the office purchase and the interaction between these provisions and the provisions in the EFO. Having regard to the constitutional background, DoJ was of the view that the Hong Kong SAR Government had the power to invoke the relevant provision in the EFO to allocate funds from the Exchange Fund to finance the purchase of office accommodation for the HKMA. There was no need to obtain the approval of the Legislative Council (LegCo) for the relevant expenditure. The details of DoJ's advice had already been set out in the letters issued by FS's Office to this Panel on 19 July 2001 and on 3 September 2001. Hopefully, the advice of DoJ would be able to remove any doubt of Members and the public on the legality of the office purchase.

Legality of using the Exchange Fund for the purchase

45. Miss Emily LAU and Ms Audrey EU expressed appreciation to the legal advice provided by LA for the Panel in the course of its deliberation on the matter. Miss Emily LAU expressed regret for the confusing manner in which the Administration had handled the matter, highlighting that initially, the former FS relied on the advice of the General Counsel to HKMA in approving the office purchase, asserting that the cost of providing accommodation for HKMA could

Action

properly be regarded as a "staff cost" which might be charged to the Exchange Fund under section 6(a) of the EFO. It was only upon the request of the Panel that the former FS sought the advice of DoJ on the matter. In July 2001, FS's Office informed the Panel of DoJ's advice that FS, who was vested with the delegated authority to approve expenditure under section 6(b) of the EFO, had been satisfied that the expenditure on the accommodation was necessary and approved it. When the purported delegation of the power from the Chief Executive (CE) to FS to approve the purchase under section 6(b) was again challenged by LA, FS sought further advice from DoJ and thereafter informed the Panel in September 2001 that FS had sought and received the approval for the purchase from CE under Section 6(b) of EFO. Miss LAU further said that she maintained her strong reservation on the propriety of using \$3.7 billion for the office purchase under the current economic climate and her doubt on the legality of the purchase.

46. Mr Albert HO commented that given the huge sum of public monies involved and the important legal issues to be fully addressed, the Administration should not have made hasty decisions on the purchase by entering into the Memorandum of Understanding (MOU) for the purchase in April 2001 and signing the Sale and Purchase Agreement in October 2001. Mr HO expressed regret for the handling of the matter by the former FS and HKMA, in particular their reckless approach in handling the legality issue of the purchase.

47. Pointing out that the MOU for the purchase had been signed in April 2001, when the Administration was still relying on section 6(a) of the EFO as the legal basis for the purchase, Miss Emily LAU questioned whether the Administration's subsequent switch to rely on section 6(b) of the EFO was acceptable from the legal viewpoint.

48. In response, DS/FS reaffirmed the Administration's position that the purchase of the office accommodation in question for HKMA was entirely lawful.

49. LA recapitulated the principles underlying his legal analyses on the matter as follows-

- (a) the expenditure for the purchase of office accommodation for HKMA as a government department was definitely a public expenditure;
- (b) given that this was a public expenditure, the approval of the Legislative Council (LegCo) for the purchase was required in accordance with the Basic Law, unless LegCo had, in accordance with the law, delegated the authority to a specified person; and
- (c) even if CE considered that the proposed expenditure was within his power to approve under section 6(b) of EFO, he might still cause that to be proposed to LegCo for approval in accordance with the Public Finance Ordinance (Cap. 2).

Action

50. LA further said that as he did not have the knowledge of the legal details surrounding the transaction in respect of the office purchase, he could not comment on the propriety and strength of the legal basis on which the parties to the transaction relied in the process. As regards the Administration's switch from relying on section 6(a) to relying on section 6(b) of the EFO to substantiate the legality of the purchase, LA said that this change of stance appeared to raise the issue of how the Administration should properly discharge its duty of accountability to LegCo on the issues relating to the office purchase.

51. Miss Emily LAU sought clarification on whether the approval by CE for the expenditure of the purchase to be charged to EFO under section 6(b) was consistent with the principle that the expenditure was a public expenditure.

52. LA said that as analysed in his paper for the Panel, when a person outside the LegCo had been delegated the authority to approve a public expenditure, he should exercise the authority in accordance with the conditions stipulated under such delegation. In this case, as stipulated in section 6(b) of EFO, CE had to be satisfied that the nature of the expenditure was incidental and that it was necessary for the due performance of duties laid upon FS and the Exchange Fund Advisory Committee in connection with the operation of the Fund. In exercising the power, CE should follow the general principles that such statutory power should be exercised in good faith and in accordance with the usual standards of reasonableness consistent with the scope and policy of the ordinance in question.

53. Mr Albert HO sought clarification on whether CE had been delegated the authority to approve the expenditure of the purchase, and whether the office purchase in question satisfied the necessity criterion stipulated in section 6(b) of the EFO.

54. Miss Audrey EU commented that the crux of the whole issue lay in whether the strength of the legal and operational justifications provided by the Administration were proportionate to the vast sum of money spent on the purchase. She sought the advice of LA on whether, from the legal viewpoint, the expenditure for the purchase could be regarded as an incidental expenditure in the context of section 6(b) of the EFO, and if the answer to the question was in the affirmative, given that LA had confirmed his view that the expenditure was a public expenditure, whether the Administration was still required to obtain the approval of the LegCo for the expenditure in accordance with the Basic Law.

55. LA advised that section 6(b) of the EFO was a clear delegation of authority to CE. He reiterated his view that even if CE considered that the proposed expenditure was within his power to approve under section 6(b), he might still cause that to be proposed to LegCo for approval in accordance with the EFO. It was CE's own judgement on which course of action was appropriate. Referring to Article 64 of the Basic Law which provided that the

Action

Administration should be accountable to LegCo, LA said that CE would be accountable to the LegCo for his decision to approve the purchase under section 6(b) of the EFO and this decision was amenable to judicial review.

56. LA further advised that whether the purchase was necessary was a matter of judgement. According to the letter from FS's Office dated 19 July 2001 to the Panel, DoJ had not expressly given a view on the necessity of the purchase, but had mentioned that "the Monetary Authority clearly requires accommodation to enable him and his staff to undertake their functions and duties under the Ordinance". A general observation was that this factor alone was insufficient to satisfy the conditions stipulated under section 6(b). Other factors including the location, size, tenure and price etc. of the office to be acquired vis-à-vis the operational requirements of HKMA might also be relevant. However, the Administration had not revealed how CE had arrived at his decision to approve the purchase. As such, Members might consider inviting the Administration to explain this decision.

57. As to whether the expenditure for the purchase was an incidental expenditure, LA advised that there was no precise definition of "incidental expenditure" in the law, but two relevant principles were observed in precedent cases. Firstly, the expenditure should be incurred for purposes subsidiary but necessary for attaining a pre-determined primary objective. Secondly, the question of whether an expenditure was "incidental expenditure" should be considered 'in the context' of the reasons and factors surrounding the expenditure and this to a certain extent involved matters of judgement.

Consideration of public sentiments in deciding the office purchase

Admin. 58. Mr SIN Chung-kai expressed dissatisfaction that despite the poor performance of the Exchange Fund and the difficult economic climate, the Administration still insisted on using a huge sum of public money to purchase a new office of the premium standard for HKMA. He questioned whether the Administration had taken into account the views and sentiments of the community towards the then proposed purchase before making its decision to complete the purchase agreement. DS/FS said that as he was not directly involved in the decision-making process, he would relate Mr SIN's question to the responsible officer(s) for a reply after the meeting. He then affirmed the Administration's position that there was a need to purchase permanent accommodation for HKMA and the premises acquired met the operational requirements of HKMA. The Administration also considered that from the long-term perspective, the purchase was a sound investment.

Review of HKMA's powers and management structure

59. Members noted that at the Panel meeting on 20 April 2001, CE/HKMA had informed members that the Administration had plans to further clarify the policy objectives, the mandates, the authority, and the governance and

Action

accountability arrangements of HKMA to ensure that it was able to discharge its functions effectively and professionally. In response to Miss Emily LAU's enquiry about the progress of the review, DS/FS said that according to his understanding, the former FS had mentioned about the plan to review the powers and management structure of HKMA to reinforce its accountability and transparency in the 2001-02 Budget Speech. At this stage, the Administration did not have a timetable on the matter.

60. Miss Emily LAU expressed disappointment that the Administration was not able to report any progress of the review to members although the plan to conduct the review had already been announced in March 2001 by the former FS. DS/FS said that he would convey members' views on the matter to FS. At Miss LAU's request, the Chairman agreed to write to FS to convey members' concern and draw FS's attention to the need to take up the matter.

(Post-meeting note: The Chairman's letter to FS and FS's reply were issued to members vide LC Paper No. CB(1)373/01-02 dated 21 November 2001 and CB(1)610/01-02(01) dated 14 December 2001.)

Security of the new office

61. Mr Albert HO expressed concern about the security of the new office. Noting that it would be located at the top floors (at levels 77 to 88) of Two International Finance Centre, he asked whether the security aspect had been reviewed in the light of the terrorist attacks in the United States on 11 September 2001. In response, DS/FS advised that according to the Administration's assessment, the risk associated with terrorist attacks in Hong Kong was very low. Hence, there was no reason to believe that Two International Finance Centre would be a probable target of terrorist attacks. In terms of internal security control, there would be improvement upon removal of HKMA from the current accommodation to the new accommodation, as the security requirements of HKMA would be taken into account in the design and fitting-out of the new office. The Executive Director (Corporate Services), HKMA (ED/HKMA) supplemented that there would be separate lifts designated for exclusive use by HKMA and this would facilitate better security control by HKMA.

Expenditure for fitting out the new office and other concerns

62. Miss Emily LAU asked whether the Administration concurred that the expenditure for the purchase was a public expenditure and sought confirmation on whether the Administration would seek the approval of LegCo for the expenditure for fitting out the new office accommodation. In response, ED/HKMA advised that this expenditure would also be charged to the Exchange Fund and would be subject to FS's approval. However, HKMA would be pleased to provide relevant information to members when the details were confirmed.

Action

63. To clarify the Administration's position, DS/FS referred members to the advice of DoJ set out in paragraph (d) of the letter from the FS's Office dated 19 July 2001 to the Panel that "...Following from this, it is unlikely that the duty to obtain approval for public expenditure is applicable in the context of the Exchange Fund under Article 113 of the Basic Law (BL 113), as long as the relevant expenditure falls within the terms of BL 113 and the EFO". He said that as the expenditure for the office purchase fell within the terms of BL 113 and the EFO, there should be no need to obtain LegCo's approval for the expenditure. DS/FS added that it was not uncommon for legal experts to have different view points on a legal issue.

64. LA said that while he agreed to DoJ's analysis set out in paragraph (d) of the letter from the FS's Office dated 19 July 2001, his understanding of the advice was different from that of DS/FS. He pointed out that the duty to obtain approval for public expenditure was not applicable only if the relevant expenditure fell within the terms of BL 113 as well as those of the EFO. He was of the view that while the expenditure referred to in sections 3(1) and 3(1A) of the EFO was covered by BL 113, the expenditure referred to in sections 6(a) and 6(b) of the EFO was not covered by BL 113.

65. The Chairman suggested that in view of the complicated legal issues involved, LA be invited to provide written views on the issues for further consideration by members. Miss Emily LAU suggested that the Panel Clerk should seek further information from the Administration, including the justification for CE's decision to approve the purchase, and work together with LA to prepare a paper for the Panel.

66. Mr NG Leung-sing requested the Administration to confirm whether the control and management of the office accommodation in question fell under the purview of the Government Property Administrator.

67. Mr Albert HO said that he was given to understand that the Director of Lands had made an assessment of the value of the premises in question before the MOU was signed. He requested the Administration to confirm this and to inform the Panel of the results of the assessment.

68. The Chairman concluded that the Panel would decide how it would proceed with the deliberation on the matter upon receipt of further information from the Administration and perusal of the paper to be prepared by LA and the Panel Clerk.

69. DS/FS remarked that as the Administration was accountable to LegCo, the Administration would try its best to facilitate the Panel's deliberation on the matter.

Action

- VII Bank of East Asia, Limited (Merger) Bill and Mizuho Corporate Bank, Ltd. (Hong Kong Consolidation) Bill**
LC Paper No. CB(1) 103/01-02(01) - "Bank of East Asia, Limited (Merger) Bill"
- LC Paper No. CB(1) 169/01-02(06) - "Mizuho Corporate Bank, Ltd. (Hong Kong Consolidation) Bill"

Briefing on the two Bills

70. The Chairman welcomed representatives from the banks and the Administration who attended the meeting for this agenda item and requested the Administration's views on the consolidation.

71. DF/SF said that the Administration welcomed the two Bills which were in line with the Government's policy to support consolidation of the banking sector in Hong Kong. The proposed mergers would promote stability of the banking system, enhance cost-effectiveness and internal controls of the banks concerned, and facilitate supervision of the merged entities by the HKMA.

72. On the draft Bank of East Asia, Limited (Merger) Bill, Mr NG Leung-sing, who would present the Bill to LegCo, advised that in drawing up the draft Bill, consideration had been given to address the concerns raised by Members in scrutinizing the two bank merger bills (Bank of China (Hong Kong) Limited (Merger) Bill and The Bank of East Asia, Limited Bill) passed by LegCo in July 2001. Subject to Panel members' views, consent of the Chief Executive for introducing the Bill would be sought in accordance with Article 74 of the Basic Law.

73. At the Chairman's invitation, Mr CHAN Kay-cheung, Executive Director, Bank of East Asia, made the following points in respect of the draft Bank of East Asia, Limited (Merger) Bill-

- (a) The proposed consolidation between The Bank of East Asia Limited (BEA) and First Pacific Bank Limited (FP) aimed to enhance the banks' operational efficiency and competitiveness. In effecting the transfer of FP's undertaking to BEA, care had been and would be taken not to generate any disruption to the continued operation of either bank's business.
- (b) Early passage of the Bill would provide a clear direction for the existing staff members to tackle the imminent restructuring of the banks' operations.

Action

- (c) BEA has established a consolidation planning division to ensure a smooth consolidation process and a consolidation liaison group to answer enquiries from customers and staff; and
- (d) As neither BEA nor FP had suffered loss for the year of assessment in question, the consolidation would not decrease either bank's tax responsibilities.

74. On the draft Mizuho Corporate Bank, Ltd. (Hong Kong Consolidation) Bill, Mr David LI Kwok-po, who would present the Bill to LegCo, appealed to members for support of the Bill. He said that the proposed consolidation of The Dai-Ichi Kangyo Bank, Limited (DKB), The Industrial Bank of Japan, Limited (IBJ) and The Fuji Bank, Limited (Fuji) was scheduled to take effect from 1 April 2002.

75. At the Chairman's invitation, Mr Tomonori Kobayashi, Chairman of the Hong Kong Consolidation Committee and General Manager of the Fuji Bank of Hong Kong, made the following points in respect of the draft Mizuho Corporate Bank, Ltd. (Hong Kong Consolidation) Bill-

- (a) The objective of the Bill was to facilitate the consolidation of the businesses of three banks i.e. DKB, Fuji and IBJ in Hong Kong. The consolidation was made in the context of a global reorganization and consolidation of the Mizuho Financial Group, which was scheduled to take effect on 1 April 2002;
- (b) With the proposed consolidation, the entire business, assets and liabilities of the Hong Kong branches of the DKB and IBJ would be transferred to and succeeded by the Fuji Bank branch in Hong Kong. Fuji Bank would be renamed as Mizuho Corporate Bank Limited upon completion of the global consolidation;
- (c) The proposed consolidation would enhance the services of the three banks in Hong Kong, which in turn would contribute to the prosperity of Hong Kong's financial markets;
- (d) The Bill would enable a smooth and efficient transfer of business with minimum disruption to operations, staff and customers;
- (e) Upon consolidation, employees of the Hong Kong branches of the DKB and IBJ would become employees of the Mizuho Corporate Bank and their accrued employment entitlement would be preserved;
- (f) Customers, suppliers and other parties having business relationships with the consolidating banks would not be adversely affected by the proposed consolidation; and

Action

- (g) The Bill was consistent with Government's stated taxation policy.

Discussion with Members

76. Members noted that there was a provision in both draft Bills to provide that the transfer of personal data in the course of the merger/consolidation would not result in a breach of any common law duty of confidentiality or a contravention of the Personal Data (Privacy) Ordinance (PDPO)(Cap. 486).

77. Mr SIN Chung-kai recalled that during the Panel discussion on two other bank mergers in June 2001, it was suggested that the Administration should consider introducing general exemption provisions in PDPO regarding the transfer of personal data in acquisition and merger activities. He enquired about the progress in this regard. Miss Emily LAU also asked if the relevant amendments to PDPO could take effect before the two proposed Bills were formally introduced into LegCo.

78. The Principal Assistant Secretary for Home Affairs (PAS/HA) replied that having discussed the issue with the Office of the Privacy Commissioner for Personal Data (PCO), the Administration agreed in principle that legislative amendments should be made to introduce exemption provisions in PDPO regarding the transfer of personal data in acquisition/merger activities. HAB would consider the content and wording of the exemption provision with PCO. Representative bodies would be consulted on the draft thus prepared. It was unlikely that PDPO would be amended before 1 April 2002. As such, it would be necessary to include an exemption provision in respect of personal data privacy in the two Bills in question.

79. In reply to Miss Emily LAU's enquiries, Mr Tomonori Kobayashi advised that a total of 550 staff were being employed by the Hong Kong branches of Fuji, DKB and IBJ. Of these, about 60 to 70 were staff deployed from Japan, and the rest were recruited in Hong Kong. Both Mr Tomonori Kobayashi and Mr CHAN Kay-cheung advised that the banks concerned did not have plans to lay off staff immediately after the proposed mergers took effect.

VIII Progress of the Strategic Change Plan in the Companies Registry

LC Paper No. CB(1) 169/01-02(07) - Information paper provided by the Administration

80. Noting that phase one of the Integrated Companies Registry Information System (ICRIS) was scheduled for completion in September 2003, Mr CHAN Kam-lam enquired about the feasibility to shorten the implementation timetable. In reply, the Registrar of Companies (RC) and the Development Manager, Companies Registry (DM/CR) explained that given the magnitude and complexity of the ICRIS, which covered the core business activities and

Action

electronic service delivery of the whole Companies Registry, the current timetable was appropriate and realistic. However, the Company Registry would work closely with the project consultant to expedite the implementation as far as practicable.

81. Mr SIN Chung-kai urged the Administration to proceed with the tendering exercise for the ICRIS promptly to take advantage of the prevailing market conditions to attain lower contract prices. The Administration took note of Mr SIN's view.

82. Dr Philip WONG Yu-hong expressed concern that some company names proposed for registration might give a wrong impression that these companies were connected in some way with another well-established company with the mere addition of words such as 'group', 'Hong Kong' etc. He suggested that to avoid possible confusion, the Companies Registry should take the initiative to consult the registered company concerned on a company name proposed for registration which was similar to the name of the registered company.

83. In response, RC explained that the Companies Ordinance had been amended in March 1991 so that a proposed company name which was the same as, instead of 'similar to', a registered company's name would not be registered. The amendment had been made in response to the business community's demand to streamline and shorten the incorporation and registration process. On the suggestion of consulting registered companies on similar company names proposed for registration, RC responded that this would lengthen the registration process to a completely unacceptable extent as well as having considerable staff resource implications.

84. Dr Philip WONG asked if the Companies Registry had maintained liaison with the relevant Mainland authority to protect companies registered in Hong Kong from being misrepresented in the Mainland. In reply, RC said that this matter was outside the purview of CR. The Chairman suggested that the issues raised by Dr WONG might be further discussed at a future Panel meeting.

IX Any other business

85. Referring to her earlier suggestion of convening another meeting to further discuss the issue of negative equity, Miss Emily LAU suggested that the Panel should first write to the Real Estate Developers Association of Hong Kong (REDA) to enlist its assistance in gathering information on co-financing loans provided by property developers for the purchase of residential properties. Upon receipt of the information/response from REDA, the Panel might consider how to proceed with the deliberation on the issue. Members agreed.

Action

(*Post-meeting note:* The letter to REDA was issued on 8 November 2001.)

86. In reply to Miss Emily LAU's enquiry about the progress of the research being conducted by for the LegCo Secretariat on protection for banking consumers, the Chairman advised that the draft research report had been completed and an informal meeting to discuss the report would be arranged.

(*post-meeting note:* An informal meeting was held to discuss the draft research report on 15 November 2001.)

Legislative Council Secretariat
28 December 2001