

For information on
4 February 2004

**Bills Committee on
Deposit Protection Scheme Bill**

**Summary of Law Society of Hong Kong's comments on the
Committee Stage Amendments**

At the meeting of the Committee held on 5 January 2004, Members requested the Administration to provide its response to the latest comments of the Law Society of Hong Kong. The response is enclosed at the Annex.

Hong Kong Monetary Authority
Financial Services and the Treasury Bureau
January 2004

Deposit Protection Scheme Bill

**Summary of Law Society of Hong Kong's Comments on the
Committee Stage Amendments (CSAs)**

<u>Subject/Clause</u>	<u>Comments</u>	<u>HKMA's response</u>
1. Subrogation	<p>The Society considers that Clause 36 on subrogation must be clarified to state exactly what rights are being subrogated. Are they rights held by the depositor in respect of his own deposits (i.e. the depositor's own rights), or are they rights of the relevant beneficiaries (under bare trusts), or clients (in respect of funds in the client's account)?</p> <p>Corresponding amendments will also be necessary, in respect of payments made to a depositor, in order to clarify the capacity in which the payment is received by the depositor.</p>	<p>It is unlikely that the DPS Board would have paid compensation to a law firm only in respect of its client account but not in respect of its office account. Therefore, the possibility that the interests of a law firm would be affected is remote.</p> <p>Moreover, the amendments proposed by the Society, if introduced, would substantially complicate the operation of the DPS as well as the payout procedures of the liquidator. In this regard, we have sought the advice of a few insolvency practitioners, and they share the same concerns with us.</p> <p>In the light of the above, we do not suggest amending clause 36 as proposed by the Society.</p>
2. Client's account	<p>The definition of client's account should refer to "one or more clients".</p>	<p>We have consulted the Department of Justice. Since Cap.1 has already specified that a word in the singular includes the plural, the amendment suggested by the Society is not necessary.</p>

<u>Subject/Clause</u>	<u>Comments</u>	<u>HKMA's response</u>
3. Depositor	In relation to the definition of "depositor", while it probably covers the situation of a garnishee (because payment to the garnishee discharges the repayment obligations in respect of the underlying deposit and should therefore count as a "repayment" of a deposit), the drafting should be clarified to cover the situation where the garnishee order relates only to part of the deposit. Note that only a "protected deposit" is defined to mean part thereof.	We agree with the Society that a garnishee would be covered in the definition of "depositor". Since clause 24 already specifies that a reference to a protected deposit includes a portion of the deposit for the purpose of determining compensation, we believe that the existing provisions are already clear on this issue.
4. Stakeholders' funds	With respect to section 2(1A) ¹ , it is not clear what is meant by "under a trust for the client" when perhaps the whole point is that a stakeholder does not hold the funds on trust for any specific client. The sub-section has to be redrafted to clarify that stakeholders' funds, as well as "uncleared trusts" (money paid into a client's account which in fact belongs to the solicitor, but the solicitor has not yet transferred the funds over to the office account) should be excluded as a deposit in a client's account for the purpose of the Ordinance.	<p>We will amend clause 2(1A) to address the Society's comment.</p> <p><i>[In the light of the Society's comments, the Administration has reconsidered this issue. It is believed that clause 27(5), as amended, should be able to address the Society's concerns. Clause 27(5) provides that "if a depositor of a protected deposit with a failed Scheme member holds the deposit in a client account <u>for a client</u>, the client, but not the depositor, is entitled to compensation from the Fund". If a law firm holds a deposit as a stakeholder in a client account, it is not holding the deposit <u>for a client</u>. Therefore, clause 27(5) shall not apply in this situation. Instead, since the deposit is held by the law firm as a trustee, the law firm will be entitled to compensation under</i></p>

¹ We believe that the Society is referring to clause 2(1A) rather than clause 2(1)(a).

<u>Subject/Clause</u>	<u>Comments</u>	<u>HKMA's response</u>
		<p><i>clause 28. The same analysis applies to funds paid into a client account which in fact belongs to the law firm. In such cases, the deposit is held by the law firm in its own right rather than for a client. Therefore, the law firm will be entitled to compensation under clause 26 instead of clause 27(5).</i></p> <p><i>Nonetheless, it is noted that funds held by a depositor in a client account for a client may also be considered as funds held by the depositor as a trustee or bare trustee. There is therefore a need to clarify the interaction between clause 27(5), clause 27(1) and clause 28. It is proposed that clause 27(5), instead of clause 27(1) or clause 28 should apply in such situations. This can help to simplify the payout operation of the Board. To give effect to this proposal, clause 2(1A) will be amended as follows:-</i></p> <p><i>“(1A) If a deposit, or portion thereof, held by a depositor in a client account for a client is also held by the depositor as a trustee or bare trustee under a trust or bare trust, the deposit or portion is, for the purposes of this Ordinance, taken as being held by the depositor for the client and not as such trustee or bare trustee.”]</i></p>