

Bills Committee on Deposit Protection Scheme Bill

Summary of concerns (as at 10 September 2003)

<u>Subject/Clause</u>	<u>Organization</u>	<u>Concern/View</u>	<u>Administration's response and follow-up action</u>
Membership of the Deposit Protection Scheme (DPS)	The DTC Association	The business of deposit taking companies (DTCs) and restricted licence banks (RLBs) will be adversely affected if they are excluded from DPS. DTCs and RLBs should be given the option to participate in the Scheme as otherwise they may need to set up a private scheme providing similar or improved levels of protection.	<p>Under the current three-tier system of authorization, RLBs and DTCs are not permitted to take small deposits¹, which the DPS is designed to protect. In practice, therefore, most of these institutions provide services mainly to corporate customers or more affluent individuals. Since the coverage limit of the proposed DPS in Hong Kong would be set at a relatively low level (i.e. HK\$100,000), the Administration does not expect that the business of RLBs and DTCs will be significantly affected if they are excluded from the DPS. In any case, the authorization criteria for a banking licence have been relaxed since May 2002. A RLB or DTC which wishes to become protected under the DPS may seek to be upgraded to the status of a licensed bank.</p> <p>It is important to note that participation in a DPS must be mandatory in order to avoid the problem of adverse selection whereby only riskier institutions choose to join the scheme. Therefore, even if RLBs and DTCs were to be allowed to join the DPS, their participation would have to be mandatory. It would clearly be undesirable and unfair to have a scheme in which participation is mandatory for banks but voluntary for RLBs and DTCs. The proposed arrangements under the Bill are consistent with the practices of other established schemes in overseas countries.</p>

¹ RLBs may take call, notice or time deposits from the public in amounts of HK\$500,000 or above. DTCs are restricted to taking deposits of HK\$100,000 or above with an original term to maturity, or call or notice period, of at least 3 months.

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	Consumer Council	Measures should be put in place to ensure that depositors can distinguish between member and non-member institutions and provisions should be introduced to prohibit false or deceptive representations concerning membership status.	<p>The HKMA has already taken on the board the Consumer Council's suggestion. Clause 47 of the DPS Bill provides that no person shall, with intent to deceive, make any false, misleading or deceptive statement or representation as to whether or not a person is a Scheme member, or whether or not a deposit or any other financial product is a protected deposit. Clause 49(1)(e) further empowers the DPS Board to make rules requiring a Scheme member to make known to the public under specified circumstances whether or not it is a member of the Scheme or whether or not a deposit, or any other financial product offered by the Scheme member, is a protected deposit. With these arrangements in place, the Administration believes that depositors will be able to distinguish between member and non-member institutions.</p> <p>In addition, the DPS Board may also publish a full list of the Scheme members on its website and in its Annual Report. The Administration is prepared to make this proposal to the DPS Board when it is established.</p>

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Composition of the DPS Board	Consumer Council	<p>To ensure that depositors' interest are adequately represented and protected in the event that the Hong Kong Monetary Authority (HKMA) is appointed as the agent for the day-to-day administration of the Scheme, consideration should be given to appointing to the DPS Board persons who have the appropriate qualifications to represent consumers' interests. In this connection, clause 4(1)(c)(ii) should be amended as follows –</p> <p><i>“not fewer than four and not more than seven other members, who have knowledge of, experience in consumer protection or are competent to otherwise represent consumer, as distinct from industry, interests.”</i></p>	<p>The Government's policy is that the DPS Board should be broadly based and representative of public interest, in particular the depositors' interest. In this light, it may not be desirable to specify in the legislation that all the non-executive members of the Board should have consumer protection background. To do so would undermine the Government's ability to ensure that the Board is served by the best available candidates and has a good mix of expertise and experience (e.g. members with accounting and insolvency law background) required to enable the Board to discharge its functions effectively.</p>

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DPS Board's duties and powers Clauses 30(1)(b) and 49	The Hong Kong Society of Accountants (HKSA)	Need for a cross-reference between clause 30(1)(b) on the requirement for depositors to produce documents in support of entitlement for compensation and clause 49 on the rule-making power specifying the documents which should be produced.	The Administration will consider the suggestion of the Society in consultation with the Law Draftsman.
Subrogation Clause 36(1)(b)	HKSA	The subrogation provision under clause 36(1)(b) may create uncertainty over the rights of depositors to receive compensation.	The Society is concerned whether clause 36(1)(b) would affect a depositor's right to prove his claim in the liquidation of the failed bank. The Administration has explained that the purpose of this clause is to make it clear that the rights and remedies of the DPS Board acquired from the depositor will rank in priority to any residual rights and remedies of the depositor in respect of his deposits. This arrangement aims to reduce the cost of the scheme. To give effect to this proposal, clause 36(1)(b) imposes a restriction on the right of the depositor to receive payment from the liquidator until the Board has been reimbursed in full. According to the Department of Justice, the clause will not affect the depositor's right to prove in a winding up. The Administration notes that the Society is content with the explanation.

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Reimbursement from provisional liquidator Clause 37	HKSA	The circumstances under which a provisional liquidator may make payments to the DPS Board out of the assets of a failed member bank are unclear.	The Administration has explained to the Society that clause 37 only enables, but does not oblige, the provisional liquidator (PL) of a failed Scheme member to make payment to the DPS Board. The intention is to allow the possibility of shortening the time required for the Board to receive payment from the liquidation, thereby helping to reduce the financing cost of the scheme. To protect the interests of the PL, it is expected that the DPS Board would provide an indemnity to the PL in respect of the payment. In addition, any such payment will be subject to the sanction of the court, which will take into account the interests of all relevant parties in determining whether the payment should be approved. It is relevant to note that in 1992 the PL of the Bank of Credit and Commerce Hong Kong Ltd made an interim payment to all depositors against an indemnity provided by the Government after obtaining the court's approval of such an arrangement. The Administration notes that the Society is content with the clarification.
Definition of "depositor"	HKSA	References to "depositor" seem to be somewhat loose and ambiguous in places.	As defined in clause 2, the term "depositor" means a person entitled to repayment of a deposit, whether made by him or not. This definition is the same as the one used in the Banking Ordinance and the Companies Ordinance. The Administration has explained to the HKSA how this would work in practice. The Administration notes again that the Society is content with the clarification.