HONG KONG BAR ASSOCIATION

Comments on Deposit Protection Scheme Bill 2003

1. The Bar has no comment on the general policy as enshrined in the proposed legislation but make the following comments on certain specific aspects of the Bill.

2. Section 12(4)(c)

The Bar is of the view that the language of the existing section can be improved. The Bar suggests the following as an alternative:

> "the scope and the level of protection available to those deposits under that scheme are not more limited or lower than that which would be available to those deposits under the Scheme if the bank were not exempted."

3. Section 12(5)

(1) Section 12(5)(a)(ii) provides, inter alia, that a bank "shall forthwith notify the Board of any change of circumstances which may affect the exemption".

(2) However, the Bar notes that there does not appear to be any sanction for breach of this reporting obligation (contrast section 12(11) which imposes criminal sanction for certain other infringement), and that therefore the continuation of exemption depends more or less entirely on the exempted banks' observance of their duty to report any change of circumstances to the Board.

(3) In order to ensure that exempted banks properly honour this reporting obligation, it may be desirable for the legislation to impose sanction for breach of this subsection, short of imposing an annual or otherwise periodic system for renewal of the exemption.

4. Section 21(2)

(1) Section 21(2) as it stands is ungrammatical; in particular, subsection (a) appears to be incomplete.

(2) The Bar suggests the following as an alternative:

"If –

(a) (i) a Manager within the meaning of section 2(1) of the Banking Ordinance (Cap. 155) has been appointed under section 52 of that Ordinance in respect of a Scheme member; or

(ii) a provisional liquidator has been appointed in respect of a Scheme member; and

(b) the Monetary Authority ..."

5. Section 21(3)

This subsection is a deeming provision in relation to the service of written notice by the Monetary Authority on the Board. Given that the Board is a public body which consists of the Monetary Authority as an ex officio member (s.4(1)(b)) and acts through the Monetary Authority (s.6(1)), the Bar queries whether this subsection is necessary which seems more apt for a person who may otherwise evade service.

6. Sections 27(3) and 27(4)

(1) These two subsections deal with an agent's entitlement to compensation. It is unclear to the Bar why it is necessary to have these two provisions.

(2) First, the expressions "agent" and "agency" are not defined in the proposed legislation. It is unclear whether and, if so, to what extent an "agency" within the meaning of sections 27(3) and 27(4) overlaps with a trust.

(3) In a case where a depositor holds the deposit as an agent, it seems to the Bar that such a depositor would also hold the deposit as a trustee, since he does not have beneficial ownership in the chose in action in question (being the debt owed by the bank). In such a case, either section 27(1) and (2) or section 28 would apply. Accordingly, the Bar does not see why a separate provision has to be included with respect to agents.

7. Section 27(5)

The Bar notes that there is no statutory definition of the expression "client account". A definition of the nature of such an account will in the Bar's view be useful.

8. Section 34

(1) It is unclear whether all the conditions set out in subsections (a), (b) and (c) need to be satisfied before the Board can make an interim payment. The word "and" or "or" between subsection (b) and subsection (c) is missing.

(2) In any event, it seems to the Bar that it is impossible to satisfy subsection (c), in view of section 33, which provides that the amount of compensation payable to a depositor of a failed Scheme member shall not exceed the amount in respect of which the depositor would, on the winding up of the failed Scheme member, be entitled to priority under section 265(1)(db) of the Companies Ordinance.

9. Section 36(1)(a)

(1) This subsection will have the effect that the Board has priority over the depositor, for example, in proving in any winding up. The point is best illustrated by an example. Assume that a depositor has a deposit of $200,000 with the bank. The bank fails. The Board pays the depositor $100,000 under the Scheme; the depositor has a claim for $100,000 which is not satisfied. By virtue of this section, the Board can prove, to the full extent of the $100,000 which it has paid the depositor, for $100,000 in the winding up of the bank. The depositor can also prove for his remaining $100,000, but his proof is subordinated to that of the bank by section 36(1). Assume that the total dividend payable in the liquidation is 50 cents in a dollar; this means the Board will get back its $100,000, and the depositor will get nothing in the liquidation.

(2) This is a different scheme from that in respect of the United Exchange Compensation Fund as formerly governed by Part X of the Securities

Ordinance (i.e. sections 98-121A). In Re Forluxe Securities (20.12.00, Yuen J), p.14, the Court held that the SFC was entitled under s.118 to be subrogated to a client's right *in the proportion which the compensation payment bears to the client's claim*. In the example given above, under this approach the Board and the depositor would both have an equal right to prove in the liquidation. It follows that they would each get a dividend of $50,000 in the liquidation.

(3) The Bar assumes that a deliberate policy decision has been made to give priority to the Board over a depositor's remaining claim, but it does mean that in cases like the above example, the depositor would not ultimately be any better off under the Protection Scheme.

10. Section 36(1)(b)

(1) The Bar queries whether the phrase "or any person who is subrogated, whether or not before the Board's subrogation, to the rights and remedies or the depositor in relation to those rights" is necessary.

(2) As a matter of common law, any person who is subrogated to the rights and remedies of the depositor in relation the deposits will be subject to prior equities. Accordingly, the express reference to such persons in section 36(1)(b) appears to be superfluous.

(3) Moreover, by expressly referring to these "any person who is subrogated", is it intended that other successors-in-title of the depositor like assignees or personal representatives are to be excluded from the operation of this subsection by virtue of the maxim *expressio unius est exclusio alterius*?

11. Section 39(10)

The Bar thinks that the legislation should expressly provide for the right to legal representation at hearings before the Tribunal for review of a decision or assessment of the Board or a decision of the Monetary Authority. It is desirable for the legislation expressly to allow an applicant to be represented by counsel, a solicitor or

such other representative authorised by the applicant as may be approved by the Tribunal.

12. Schedule 1, para 1(a)(i)

The expression "agreed to by the depositor at the most recent time it was negotiated" appears to the Bar to be too vague and infelicitous. An alternative is "a deposit which had an original term to maturity of more than 5 years", which is a phrase based on section 60(6)(b) of Banking Act 1987 (UK).

13. Schedule 5, para 1(d)(iii)

(1) Under the definition of "excluded person", the Bar suggests para (b)(ii) be revised as follows:

"the date on which the petition for the winding up of the company being wound up was presented"

(2) Under the definition of "related company", the Bar suggests para (c) to be revised as follow:

"a subsidiary of the holding company of the company"

Dated 19th September 2003.