

LEGISLATIVE COUNCIL BRIEF

DAO HENG BANK LIMITED (MERGER) BILL

Introduction

1. The Chief Executive granted his consent for the Bill to be introduced before the Legislative Council on 24 January 2003. This Bill is introduced under Article 74 of the Basic Law by Legislative Council member, Dr. Hon. David Li Kwok-po, GBS, JP. The Financial Affairs Panel of the Legislative Council was consulted regarding the Bill on 4 November 2002, and Members supported the general objectives of the Bill.

Background and Purpose

2. The Bill provides for the merger of Overseas Trust Bank, Limited (*OTB*) and DBS Kwong On Bank Limited (*DKOB*) and together with OTB, the *Transferring Banks*) with Dao Heng Bank Limited (*Dao Heng Bank*). The intention of the merger is to allow Dao Heng Bank to consolidate its banking business with the Transferring Banks to increase efficiency through economies of scale. All of the banks are members of the DBS Group which is headed by The Development Bank of Singapore Limited.

3. In a number of jurisdictions, such as the United States, Japan and Switzerland, two banks can merge with one another by way of "universal succession". However Hong Kong company law does not have such a concept as universal succession. Accordingly bank mergers in Hong Kong may only be effected either by transfer of all property and liabilities by way of novation or assignment or by introducing a Bill to the Legislative Council which transfers all property and liabilities of the merging bank which are governed by Hong Kong law. Given the large number of outstanding agreements between the Transferring Banks and their customers, it is not practical to transfer such assets and liabilities by way of novation and assignment to Dao Heng Bank.

4. It is the Government's stated policy to support consolidation of the banking sector in Hong Kong, which should improve its competitiveness and contribute to systemic stability in the longer term. As part of this policy, the Administration has previously supported bank mergers where reasonable proposals are submitted for consolidation. This is, however, always subject to the overriding aim of promoting the stability of the banking system and providing an appropriate degree of protection to depositors in the merged institutions and to depositors generally. The Hong Kong Monetary Authority (*HKMA*) has no objection to the proposed merger of the Transferring Banks' banking businesses being effected by way of a private bill such as the Bill.

5. The Bill has advantages for the Transferring Banks' customers, who will have the reassurance that all Hong Kong law governed property and liabilities have been properly transferred to Dao Heng Bank. Such customers will also not be inconvenienced by having to sign new customer documentation. Further, the basis of the transfer of such property and liabilities between Dao Heng Bank and the

Transferring Banks will be publicly known and uniform. In addition, following the merger, the consolidated surviving bank should be financially stronger, contributing to the stability of the banking sector in Hong Kong.

6. The Bill also has advantages for the Transferring Banks' and Dao Heng Bank's shareholders. The three Hong Kong banking subsidiaries of the DBS Group will be combined into a single bank, Dao Heng Bank, facilitating economies of scale.

7. Since the early 1980s the Legislative Council has passed sixteen ordinances implementing mergers of banks and other authorised institutions. The Bill is based on the form of the five most recent bank merger ordinances enacted by the Legislative Council over the course of 2001 and 2002.

The Bill

8. The purpose of the Bill is to transfer the undertakings of the Transferring Banks to Dao Heng Bank. All of the banks involved in the merger are licensed under the Banking Ordinance and are incorporated in Hong Kong. In conjunction with the merger under the Bill, the Transferring Banks will seek the revocation of their banking licences by the HKMA pursuant to the Banking Ordinance. None of the banks involved in the merger are currently listed on The Stock Exchange of Hong Kong Limited.

9. The Bill provides for the vesting of the undertakings of the Transferring Banks in Dao Heng Bank on the appointed day. Except for a very limited range of excluded property, as explained in Section 10(a) of this brief, all of the business of the Transferring Banks will form part of the undertakings vested in Dao Heng Bank by the Bill.

10. The key provisions of the proposed Bill are similar to those of the recently enacted merger bills and are summarised in the following paragraphs.

- (a) **Clause 2** sets out the definitions of certain terms used in the Bill. In particular, there is a definition of "excluded property" which follows the same formulation used in The Bank of China (Hong Kong) Limited (Merger) Ordinance. A very limited range of property is excluded (for example, the common seal, documents required by the Companies Ordinance and the issued share capital of the Transferring Banks) only for the purpose of complying with the Companies Ordinance and no discretion is given to Dao Heng Bank or the Transferring Banks to exclude any property or liabilities from the vesting of undertakings.
- (b) **Clause 3** provides that the board of directors of Dao Heng Bank may determine an appointed day upon which the merger will take effect and that such appointed day must be notified by both the Transferring Banks and Dao Heng Bank in the Gazette.
- (c) **Clause 4** provides that DKOB's and OTB's names will be changed to "DBS Kwong On Limited" and "Overseas Trust Limited" respectively on the

appointed day. In addition, the Transferring Banks authorized and issued share capital will be reduced on the appointed day, and their banking licences will be revoked on a day determined by the HKMA and notified in the Gazette. The current intention is that this day will coincide with the appointed day upon which the merger will take effect.

- (d) **Clause 5** is the main transfer and vesting provision in the Bill. It provides that the undertakings of the Transferring Banks (not including the “excluded property”) shall transfer to and vest in Dao Heng Bank as if Dao Heng Bank were the same person in law as the Transferring Banks upon the appointed day.
- (e) **Clause 6** deals with property which, before the merger, is held by a Transferring Bank in a capacity as a trustee. It provides that in such case, the relevant document should be read as if references to the Transferring Bank were references to Dao Heng Bank.
- (f) **Clauses 7(a) to (k)** provide that all contracts and agreements made with, given to or by or addressed to the Transferring Banks (other than excluded property) shall, after the merger takes effect, be construed as if Dao Heng Bank had been the original party instead of the Transferring Banks and, accordingly, all references to the Transferring Banks must be construed as if they were to Dao Heng Bank. **Clauses 7(a) to (k)** also provide for accounts, negotiable instruments, powers of attorney, security, court orders, arbitration awards and judgements to be transferred to Dao Heng Bank upon the appointed day. **Clauses 7(g)(v) and (vi)** are provisions which seek to reflect previous concerns in respect of other bank mergers expressed by Members of the Legislative Council regarding the possible increase of security or charges over customers' assets as a result of the merger. These provisions seek to ensure that Dao Heng Bank's existing charges and security interests will not be expanded over assets previously held by the Transferring Banks of a common Dao Heng Bank/DKOB/OTB customer.
- (g) **Clause 7(1)** provides that the transfer of personal data from the Transferring Banks to Dao Heng Bank under the Bill shall not result in a breach of any duty of confidentiality or a contravention of the Personal Data (Privacy) Ordinance. The Privacy Commissioner may exercise in respect of Dao Heng Bank any power which he could, before the merger, have exercised in respect of the Transferring Banks.
- (h) **Clause 8** provides for the accounting treatment of Dao Heng Bank following the merger. It provides that the balance sheets and profit and loss accounts of the Transferring Banks and Dao Heng Bank for the accounting period of each company in which the appointed day falls shall be prepared in all respects as if the undertakings had vested in Dao Heng Bank on the first day of such accounting period of Dao Heng Bank.
- (i) **Clause 9** provides for the taxation arrangements following the merger. It also provides that for the purposes of the Inland Revenue Ordinance, Dao Heng Bank shall be treated as if it were the same person in law with regard to the undertakings as the Transferring Banks on and from the appointed day and

any profits or losses of the Transferring Banks shall be treated as profits and losses of Dao Heng Bank. **Clause 9** is intended to have a similar effect to the provisions dealing with taxation matters in previous bank merger ordinances. The effect of this provision is consistent with Government policy on taxation, as stated in the context of recently enacted bank merger ordinances.

- (j) **Clause 10** provides that, in respect of all the Transferring Banks' contracts of employment with those employees who are transferred by the Bill to Dao Heng Bank at the merger, such contracts shall be deemed for all purposes to be a single continuing employment. **Clause 10** also provides that no directors, secretary or auditor of the Transferring Banks shall, by virtue of the merger only, automatically become a director, secretary or auditor of Dao Heng Bank.
- (k) **Clause 11** ensures that the Transferring Banks' employees who are members of pension fund schemes of the Transferring Banks shall continue to be members of these schemes after the transfer of the Transferring Banks' undertakings to Dao Heng Bank. It also ensures that former employees of the Transferring Banks and existing employees of Dao Heng Bank shall continue to enjoy the same rights following the transfer as before under their respective pension schemes and that the transfer by virtue of the Bill shall not automatically bestow any additional entitlements to such employees.
- (l) **Clause 12** prevents the merger of the Transferring Banks with Dao Heng Bank constituting an event of default or a termination event in a contract or agreement to which a Transferring Bank or Dao Heng Bank or their respective subsidiaries is a party.
- (m) **Clauses 13 to 15** set out provisions dealing with evidence and the admissibility of evidence in respect of any matter for or against the Transferring Banks which, transferred by the Bill, becomes admissible in evidence after the merger in respect of the same matter for or against Dao Heng Bank. **Clause 14** provides that, for the purposes of the Evidence Ordinance, banker's records of the Transferring Banks vested in Dao Heng Bank by the Bill shall be treated as if these were always banker's records of Dao Heng Bank.
- (n) **Clause 16** deals with the effect of the merger on interests in land in Hong Kong held by the Transferring Banks and provides that the vesting of the Transferring Banks' interests in land in Dao Heng Bank pursuant to the merger does not constitute an acquisition, assignment, transfer or parting with possession under the Landlord and Tenant (Consolidation) Ordinance. **Clause 16** also provides that the vesting in Dao Heng Bank of the Transferring Banks' interests in land under the merger will not affect or extinguish any priority under the Land Registration Ordinance. For the avoidance of doubt, the Bill stipulates that nothing in **Clause 16** exempts either Dao Heng Bank or the Transferring Banks from the provisions of the Stamp Duty Ordinance.

- (o) **Clause 17** states that nothing in the Bill shall exempt either the Transferring Banks or Dao Heng Bank from any of the provisions of the Banking Ordinance and other ordinances regulating the carrying on of their businesses.
- (p) **Clause 18** provides that the Bill does not prevent Dao Heng Bank from amending its memorandum and articles of association or dealing with its property or business generally. **Clause 18** also provides that nothing in the Bill prevents any member of the DBS Group from altering its memorandum and articles of association or dealing with its property generally before the appointed day.
- (q) **Clause 19** provides that nothing in the Bill once enacted shall affect the rights of the Central Authorities or the Government under the Basic Law and other laws.

Legislative Timetable

11. The proposed legislative timetable is as follows –

Financial Affairs Panel	4 November 2002
Publication in the Gazette for the first time	30 January 2003
Publication in the Gazette for the second time	7 February 2003
Member in charge of the Bill gives notice of intention to present the Bill to the Clerk of the Legislative Council	7 February 2003
First Reading and commencement of Second Reading debate	19 February 2003
House Committee	21 February 2003
Resumption of Second Reading, Committee Stage and Third Reading	To be notified

Economic Implications

12. The Bill facilitates the merger of the Transferring Banks with Dao Heng Bank. The consolidation of the banking sector in Hong Kong, such as that facilitated by the Bill, should improve its competitiveness and contribute to systemic stability in the longer term to the advantage of Hong Kong's economy.

Taxation

13. As mentioned above, **Clauses 8 and 9** have the effect of deeming Dao Heng Bank as one and the same as the Transferring Banks in law, and allowing any profits

and losses of the Transferring Banks to be treated as the profits and losses of Dao Heng Bank from the beginning of the financial year of the merger.

14. In the recently enacted merger bills, the Government has allowed the merged entity, for tax assessment purposes, to carry forward any losses accumulated by any of the merging entities. As neither of the Transferring Banks carries any accumulated losses for tax assessment purposes, the Bill should not result in any loss of Government's revenue.

Public Consultation

15. The Financial Affairs Panel have considered the Bill and each of the Hong Kong Monetary Authority, the Financial Services and the Treasury Bureau, the Department of Justice, the Commissioner of Inland Revenue, the Companies Registrar, the Land Registrar, the Privacy Commissioner for Personal Data, the Securities and Futures Commission and the Mandatory Provident Fund Schemes Authority have been consulted on the Bill and have provided their comments (if any). Additional consultation with the public has not been deemed necessary. Arrangements to answer questions from customers and the public will be made as part of the merger notification exercise.

Publicity

16. The Bill was published in the Gazette on 30 January and 7 February 2003 and notice of the Bill has been given by way of advertisements in the South China Morning Post and the Ming Pao Daily News on 27 and 28 January 2003. In addition, a further press release will be issued by Dao Heng Bank upon completion of the legislative process.

Enquiries

17. Any enquiries about this brief can be directed to Mr. Andrew Burns at the Office of Legislative Councillor, Dr. Hon. David Li Kwok-po, GBS, JP at telephone number 2842 3499 or fax number 2526 1909.

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