立法會
Legislative Council

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Paper for the House Committee Meeting on 2 May 2003

Legal Service Division Report on Deposit Protection Scheme Bill

I. SUMMARY

1. **Objects of the Bill**	To provide for the establishment of a Deposit Protection Scheme (DPS); the related management and administrative organ; the financial arrangements; the entitlement and payment of compensation and incidental and consequential matters.
2. **Comments**	(a) The Monetary Authority (MA) would be the executive organ of the DPS Board. The costs and expenses incurred by MA would be paid out of the Exchange Fund (ExF) and ExF would in turn be reimbursed by the DPS Fund. MA would also be the authority to decide when compensation is to be paid from the DPS Fund. (b) The DPS would be mandatory. The DPS Fund would be accumulated from contributions from the banks.
3. **Public Consultation**	Public consultation has been conducted in late 2000 and in March 2002.
4. **Consultation with LegCo Panel**	The Financial Affairs Panel was consulted on the legislative proposal at its meeting held on 6 January 2003.
5. **Conclusion**	The Bill signifies an important step in the protection of depositors. It may also alter the legal and business environment in which the banking industry operates. Members may wish to form a Bills Committee to study the provisions of the Bill in detail.

II. REPORT

Objects of the Bill

To provide for the establishment of a mandatory Deposit Protection Scheme (DPS) for the purpose of providing compensation to depositors under specified circumstances, a DPS Board and a DPS Fund; to provide for contributions to the Fund and for the entitlement to and payment of compensation from the Fund; and to provide for incidental and consequential matters.

LegCo Brief Reference

2. B9/2/2C dated 16 April 2003 and issued by the Financial Services Branch of the Financial Services and the Treasury Bureau.

Date of First Reading

3. 30 April 2003.

Comments

4. The Legislative Council has on 13 December 2000 passed a motion urging the Administration to expeditiously implement a deposit insurance system, which is cost effective and easy for depositors to understand, for effectively protecting small depositors and to formulate appropriate complementary measures aiming at reducing the risk of moral hazard. The proposed DPS appears to be a response to that call.

5. The DPS would be a mandatory scheme for all banks in Hong Kong. A bank, which is incorporated outside Hong Kong and has a comparable scheme in the jurisdiction that it is incorporated, may apply for exemption. The scheme would cover all deposits excluding term deposits for a period exceeding 5 years, secured deposits, deposits taken outside Hong Kong, deposits held for account of the Exchange Fund, any bearer instrument and deposits by banks or their related companies. A deposit made by an officer of a member of DPS or its related company immediately before a manager is appointed or a winding-up petition is presented in respect of that member would also be excluded. Deposits covered by the scheme are referred to as "protected deposits".

6. The DPS would be maintained by the DPS Board (the Board). It would be a body corporate of perpetual succession. It would be comprised of the Secretary for Financial Services and the Treasury (or his representative) and the Monetary

Authority (or his representative) as ex officio members; the chief executive officer of the Board as an executive member; and 4 to 7 non-executive members. All members other than the ex officio members would be appointed by the Chief Executive (CE). He would also appoint the chairman of the Board from the non-executive members. Public officers are not eligible to be appointed as non-executive members.

7. The Board would be required to perform its functions through the Monetary Authority (MA), who would do all acts and things necessary for implementing the decisions of the Board. All costs and expenses incurred by MA in this connection would first be paid out of the Exchange Fund. The Financial Secretary (FS) would determine the amount to be paid to the Exchange Fund from the DPS Fund. The CE may on grounds of public interest give the Board written directions regarding the performance of the Board's functions.

8. There would be established a DPS Fund (the Fund). It would be managed and administered by the Board. Each member of DPS (Scheme member) would be required to make contributions to the Fund. The contributions would be comprised of a build-up levy, an expected loss levy and a surcharge.

9. The build-up levy will be payable annually until the target fund size (TFS) has been reached and thereafter to maintain the TFS. The TFS would be set at 0.3% of the total protected deposits maintained with all Scheme members as at 20 October of the immediately preceding year. The build-up levy payable by a Scheme member would be calculated by multiplying the amount of protected deposits maintained with the Scheme member as at 20 October of the preceding year (the base amount) by the applicable specified percentage which is determined according to its MA supervisory rating. The MA supervisory rating is assigned to a Scheme member by MA and reflects MA's assessment of its overall financial condition and of its quality of management.

10. The expected loss levy would be payable annually after the TFS has first been reached except where the TFS is increased as a result of a change in the specified percentage for the calculation of the TFS. The levy payable by a Scheme member is calculated by multiplying the base amount by the applicable specified percentage determined according to its MA supervisory rating.

11. A surcharge is payable after the TFS has first been reached and the balance of the Fund as at 20 October of the immediately preceding year is less than 70% of the TFS. The aggregate amount of surcharge payable for any year would be the difference between the aggregate amount of build-up levies payable by all Scheme member for that year and the aggregate amount of expected loss levies payable by all Scheme member for that year subject always to a cap of 30% of the amount by which the TFS for that year exceeds the balance of the Fund as at 20 October of the immediate preceding year.

12. Under the DPS, compensation would be payable upon the occurrence of

a specified event in respect of a Scheme member. A specified event would occur if a winding-up order has been made by the Court of the First Instance in respect of a Scheme member or MA has served on the Board a notice of his decision to pay compensation to depositors of a Scheme member, whichever first occurs. MA may serve the aforesaid notice on the Board after consultation with the FS if a manager has been appointed under section 52 of the Banking Ordinance (Cap. 155) or a provisional liquidator has been appointed in respect of a Scheme member and MA is of the view that the Scheme member is insolvent or likely to become unable to meet its obligations or about to suspend payment to its depositors.

13. The maximum amount of compensation payable to a depositor in respect of each Scheme member would be $100,000 regardless of the number or amount of deposits. Deposits held by a bare trustee or agent or in a client account for a person will be counted as deposits made by that person. Where deposit is held by 2 or more persons jointly, each is deemed to have an equal share in the protected deposit unless the contrary is proved to the satisfaction of the Board. A partnership would, however, for the purpose of entitlement to compensation from the Fund be taken to be a single and continuing body of persons as distinct from the persons who may from time to time be the members of the partnership.

14. If the Board makes a payment of compensation to a depositor from the Fund, it would be subrogated to the full extent of the payment and accrued interest to all the rights and remedies of the depositor in relation to all the depositor's deposits (whether or not protected deposits) with the failed Scheme member in priority over the rights and remedies of the depositor and his subrogator.

15. Where a bank outside Hong Kong seeking exemption, or a depositor claiming compensation is aggrieved by a decision of the Board under the relevant provisions or a Scheme member disagrees with the Broad's assessment of the amount of its contribution, each may appeal to the Deposit Protection Appeals Tribunal (the Tribunal) for review.

16. The Tribunal would be comprised of a chairman and 2 members from a panel. The chairman would be a judge appointed by the CE upon the recommendation of the Chief Justice. The members of the panel would be appointed by the CE. Their term of office would not exceed 3 years. A person is not excused from complying with an order, notice, prohibition or requirement of the Tribunal on the ground of doing so might incriminate himself. Such evidence, answer or information that might incriminate the person giving it would not be admissible in evidence against that person in criminal proceedings in a court of law except for perjury or an offence under clause 40(3) of the Bill. Appeal from the Tribunal to the Court of Appeal would be on a point of law only.

17. The Administration expects that a start-up period of about 12 to 18 months would be required before the Board would be in a position to provide deposit protection. It would take into consideration the prevailing economic environment

and the views of the banking industry in determining when to commence the scheme. Clause 1(2) of the Bill would allow the Secretary for Financial Affairs and the Treasury to commence different parts of the enacted Ordinance on different dates.

Public Consultation

18. Public consultation has been conducted in late 2000 and in March 2002. According to the Administration, the results of the first public consultation indicated that there was broad public support for establishing a DPS in Hong Kong. The detailed proposals on the structure of the DPS, which were the subject of the second public consultation, were generally supported by the parties consulted. The Hong Kong Association of Banks has made some specific suggestions in respect of the proposed scheme. The Administration does not appear to have accepted all of them.

Consultation with LegCo Panel

19. The Financial Affairs Panel (FA Panel) was consulted on the legislative proposal at its meeting held on 6 January 2003.

20. While the FA Panel supported the proposed DPS in general, some members expressed the following concerns/views:

(a) The proposal to exempt an overseas bank that has a comparable scheme in the bank's home jurisdiction that protects deposits taken by its Hong Kong office would encourage depositors to move their deposits to overseas banks;

(b) As contributions towards the DPS Fund would be based on the "CAMEL rating" of banks, lower rated banks might be forced to undertake businesses with higher risks in order to recover the higher cost involved;

(c) There would be the problem of moral hazard associated with the scheme and banks might increase charges to customers to recover the cost for the scheme; and

(d) The proposal of appointing Hong Kong Monetary Authority (HKMA) as the agent for day to day administration of the scheme would undermine the credibility and independence of the scheme. There would be conflict for HKMA as the regulator of banks to take up the role. In the event of a large bank failure, HKMA might not be able to deploy adequate staff to take up the necessary duties.

21. With reference to (a), HKMA has advised that as the DPS in Hong Kong would basically be a protection scheme for small depositors, it would not be likely that small depositors would be lured to move their deposits to overseas banks.

22. With reference to (b), HKMA has pointed out that there was support from the public consultation to adopt a differential system for assessment of contributions. As banks would try to improve their risk-management and asset quality with a view to obtaining a higher CAMEL rating in order to lower payments to the Fund, the proposed contribution mechanism would help reduce the potential moral hazard risks.

23. With reference to (c), HKMA has advised that how banks charged their clients would be a commercial decision. It was envisaged that depositors would have a wider choice in banking service after implementation of the DPS.

24. With reference to (d), HKMA has advised that it would not be cost-effective for the DPS to maintain a staff level that was required to handle the workload in the event of a bank failure but otherwise not needed. The problem of role conflict could be addressed by functional separation between bank regulation and administration of the DPS. In the event of a large bank failure, HKMA could outsource some of the work and engage external professionals.

Conclusion

25. The Legal Service Division is seeking clarification from the Administration on a number of legal and drafting matters. The Bill signifies an important step in the protection of depositors. It may also alter the legal and business environment in which the banking industry operates. Members may wish to form a Bills committee to study the provisions of the Bill in detail.

Prepared by

KAU Kin-wah
Assistant Legal Adviser
Legislative Council Secretariat
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