

Dated 13 May 2010

To the Subcommittee to Study Issues Arising from
Lehman Brothers-related Minibonds and
Structured Financial Products of the Legislative Council

**RESPONSE TO THE SUBCOMMITTEE'S LETTER DATED 7 MAY 2010 FROM
MR HUNG PI-CHENG, BENJAMIN, EXECUTIVE DIRECTOR AND CHIEF EXECUTIVE OFFICER,
STANDARD CHARTERED BANK (HONG KONG) LIMITED (SCBHK)**

FOLLOW-UP TO THE HEARING ON 7 MAY 2010

1. **Regarding the internal process for approval to distribute Lehman Brothers(LB)-related equity linked notes (ELNs) in Hong Kong, please provide the following information:**

- (a) **Which levels of management staff were involved in the decision-making process and the decisions made by each level;**
- (b) **the names of the relevant departments and the names and titles of the persons responsible for making the decisions;**

1.1 As set out in paragraphs 8.2 to 8.5 of the Written Statement of Mr. Hung Pi Cheng Benjamin dated 29 April 2010 (the "Written Statement"), the approval process involved GWM based in Singapore and HKGWM in Hong Kong. The level of management staff involved & the decisions made by each level is illustrated in the following table:-

Management Staff	Department	Decisions Involved
Global Product Head, Wealth Management & Bancassurance Bryan Henning	GWM	<ul style="list-style-type: none">• Product provider approval• Signing of Global Distribution Agreement with Lehman Brothers• Product programme approval
Head, Investment and Treasury Products Chew Sutat / Senior Manager Structured Products Eugene Neo	GWM	<ul style="list-style-type: none">• Product provider evaluation• Product evaluation approval
Head, Wealth Advisory & Product Distribution Chew Leng Hock	GWM	<ul style="list-style-type: none">• Product risk classification• Product approval code issuance
General Manager, Wealth Management Mary Huen	HKWM	<ul style="list-style-type: none">• Product programme approval
Head, Retail Treasury Wealth Management Charles Wong	HKWM	<ul style="list-style-type: none">• Product programme approval• Product evaluation
Head of Consumer Banking, Hong Kong Tan Kong Khoon (succeeded by Benjamin Hung in 2006)	SCB HK	<ul style="list-style-type: none">• Product programme approval
Group Head, Business & Operational Risk Dominic Luk	Group Business & Operational Risk	<ul style="list-style-type: none">• Product programme approval
Legal Adviser, Hong Kong Doris Ma	Legal & Compliance	<ul style="list-style-type: none">• Product programme approval
Head of Operations & Technology Trevor Haeger	Systems and Operations	<ul style="list-style-type: none">• Product programme approval
Head of Credit, CBHK John Byrne	Credit	<ul style="list-style-type: none">• Product programme approval
Regional Head of Market Risk Management, Asia (ALM) Patrick Ma	Market Risk	<ul style="list-style-type: none">• Product programme approval

Head of Global Markets, NEA Patrick Gillot	Global Markets	• Product programme approval
Chief Financial Officer, HK, China, NEA Julian Fong	Finance	• Product programme approval

Note: Product Programme approval names & designation per W30(C) item 6 Annex 1

(c) a flow chart to illustrate in detail the process in (a) and (b); and

1.2 Please see item 1 enclosed.

(d) whether any separate approval was required for the distribution of each of the series of the LB ELNs in Hong Kong.

1.3 As set out in paragraphs 8.5 and 9 of the Written Statement, HKWM will first conduct its own due diligence on the product features and terms. Upon satisfactory result of the due diligence HKWM will submit the completed product evaluation form together with the relevant term sheet to GWM for approval. Each individual series of LB ELN was separately reviewed and approved.

2. **It is noted from Item 3 to W30(C) that GWM entered into the Distribution Agreement and there was a Letter Agreement dated 2 August 2006 between SCB and Lehman Brothers Commercial Corporation Asia Limited. Please provide the corporation profile of Lehman Brothers Commercial Corporation Asia Limited, and explain the company's relationship with the LB product team and the Issuer and the Guarantor of LB ELNs.**

2.1 Lehman Brothers Commercial Corporation Asia Limited (LBCCA) was a wholly owned subsidiary of Lehman Brothers Holdings Inc., the Guarantor of LB ELNs.

2.2 LBCCA was the distributing agent of LB ELNs, which were issued by Lehman Brothers Treasury Co BV.

2.3 LBCCA was based in Hong Kong and was responsible for interfacing with local distributors including SCBHK. The local LB product team also provided management, service delivery and on the ground support.

3. **From August 2006 to September 2008 (prior to the collapse of LB), how many customers of LB ELNs had requested for early redemption of the notes, and how many of them had been able to sell the notes?**

3.1 Based on the Bank's records, from August 2006 to September 2008, there were a total of 40 queries for unwinding LB ELNs and 2 had proceeded to execution.

4. **As stated in paragraph 18.2 of W30(C), all series of LB ELN were risk rated as "F", unless they were principal protected in which case they were given a "P" risk rating. Please provide a copy of the offer documentation of a principal-protected LB ELN sold by SCBHK.**

4.1 A copy of the relevant offer documentation in respect of Lehman Brothers 2-Year HKD/US Performance Gap Principal Guaranteed Note – Series 1 (5+11+2388), a principal-protected LB ELN, are enclosed as item 2.

5. **As stated by Mr Benjamin HUNG at the hearing held on 7 May 2010, apart from the Information Package of the LB ELN, there was not any other marketing material provided by the bank's staff to customers. Please confirm:**
- (a) **whether there was any other marketing material in addition to the Information Package; and**
 - (b) **whether the note tabled by Ms Audrey EU (as per attached) was a marketing material given by SCBHK to the sales staff or to the customers.**
- 5.1 There was no other offer documentation in additional to the Information Package.
- 5.2 As explained by Mr. Hung Pi Cheng Benjamin at the hearing of the Subcommittee to study Issues Arising from Lehman brothers-related Minibonds and Structured Financial Products of the Legislative Council on 7 May 2010, the note tabled by Ms. Audrey Eu was not a marketing material given by SCBHK to its sales staff or to its customers.
6. **Please provide the name(s) of the Head(s) of GWM and the staffing structure of GWM during the period August 2006 to June 2008.**
- 6.1 The staff structure of GWM during the period August 2006 to June 2008 is enclosed as Item 3
7. **As stated in paragraph 7.1 of W30(C), between August 2006 and June 2008, SCBHK distributed two types of LB ELNs: one using the authorization procedure under the Securities and Futures Ordinance (SFO) (Cap. 571) and the other using "Minimum Investment Offer Exemption" (i.e. through private placement) under the Companies Ordinance (CO) (Cap. 15). Please provide the following information/documentation:**
- (a) **how SCBHK had come to its decision to distribute LB ELNs in Hong Kong through the two different procedures as specified in paragraph 7.1 of W30(C)?**
- 7.1 The CO "Minimum Investment Offer Exemption" was introduced on 3 December 2004 following the passing of the Companies (Amendment) Bill 2003 unanimously on 9 July 2004 by LegCo. As stated in the Financial Secretary's Budget Speech in 2002, one of the aims of the Bill was to increase liquidity by attracting more financial product issuers to Hong Kong, as well as capital and investors from the Mainland and overseas.
- 7.2 Whether a particular structured note was offered to the market via the "Minimum Investment Offer Exemption" was fundamentally a decision of the issuer and not the distributors.
- 7.3 The CO "Minimum Investment Offer Exemption" resulted in an increase in investors' interest and as market demand grew, more products became available in the market. To meet the growing market demand, the Bank reviewed its DSSPP and approved the offering of debt securities, including ELN, to retail customers pursuant to the CO "Minimum Investment Offer Exemption".
- 7.4 ELNs distributed using the procedure under CO, generally attracted higher market demand than those distributed under SFO (Retail Notes) for the following reasons:
- (a) Pricing - The procedure under the CO "Minimum Investment Offer Exemption" offered better market pricing with higher coupon payout rates and yields. For Retail Notes, which usually involved a longer offering period of 2 to 3 weeks, issuers had to build in a risk premium to secure the customer coupon, and hence

the market pricing was usually less favorable when compared with notes distributed under the CO procedure.

- (b) Flexibility - The CO procedure also afforded greater flexibility in terms of underlying securities as issuers could determine the most appropriate structure and underlying assets based on the latest market conditions. For example, an increase in the banks' reserve rate in China could affect the pricing of Chinese banks and so an issuer may take this factor into consideration when deciding on the underlying basket of stocks. On the other hand for Retail Notes, the choice of underlying stocks would have already been determined, hence pricing could be off-market.
- 7.5 During the relevant period, the Bank launched 90 LB ELN (152 tranches in multiple currency) using CO "Minimum Investment Offer Exemption" and 6 tranches of LB Retail Notes. From May 2007, LB stopped offering Retail Notes to the Bank, however the Bank continued to offer Retail Notes issued by other providers.
- (b) *the respective total sales value of each of the aforesaid two types of LB ELNs during the period August 2006 and 5 June 2008;*
- 7.6 The total sales value are as follows:
- | | |
|-------------------------|-----------------------------|
| CO (Private Placement): | about HK\$5,195m (US\$666m) |
| SFO (Retail Notes): | about HK\$44m (US\$5.66m) |
- (c) *in a tabular form, the names of each series of LB ELNs distributed under each of the two procedures; and*
- 7.7 Please see item 4 enclosed.
- (d) *copy of the offer documents and marketing materials of the last series of LB ELN which were authorized under SFO and distributed by SCBHK.*
- 7.8 A copy of the relevant offer documentation and marketing materials in respect of Pyxis Equity-Linked Notes Series 19 (offer period until 20 December 2006) is enclosed as item 5. As explained during the earlier hearings, the amount outstanding pertaining to this Series accounted for less than 1% of the total sales value of outstanding LB ELNs, involving 18 customers.

Response to the Subcommittee's letter dated 7 May 2010 from
Mr Hung Pi-Cheng, Benjamin, Executive Director and Chief Executive Officer of
Standard Chartered Bank (Hong Kong) Limited

Enclosures

Item	Description
1	Flow chart on process for approval to distribute LB ELNs
2	Offer documentation in respect of a principal-protected LB ELN sold by the Bank
3	Organisation chart of GWM during the period August 2006 to June 2008
4	Table setting out the names of each series of LB ELNs distributed under the CO and SFO by the Bank
5	Offer documentation and marketing materials in respect of the last series of LB ELN authorised under SFO sold by the Bank