

立法會
Legislative Council

LC Paper No. LS57/09-10

**Paper for the House Committee Meeting
on 23 April 2010**

**Legal Service Division Report on
Deposit Protection Scheme (Amendment) Bill 2010**

I. SUMMARY

- 1. Object of the Bill** To amend the Deposit Protection Scheme Ordinance (Cap. 581) (the Ordinance) to improve depositor protection and operating efficiency under the Deposit Protection Scheme (the Scheme)
- 2. Comments**

 - (a) The Bill proposes to expand the scope of application of the Ordinance to cover secured deposits.
 - (b) The limit of protection of the Scheme is proposed to increase from \$100,000 to \$500,000.
 - (c) New powers are conferred on the Hong Kong Deposit Protection Board (the Board) to streamline the operation of the Scheme and improve the efficiency of making compensation to depositors.
- 3. Public Consultation** According to paragraph 18 of the LegCo Brief, the Board consulted the public in two phases in 2009. It also approached interested parties such as industry associations and the Consumer Council for comments.
- 4. Consultation with LegCo Panel** The proposals were discussed by the Panel on Financial Affairs on 1 June 2009 and 1 February 2010. Panel members raised various concerns.
- 5. Conclusion** Members may decide whether to study the policy aspects of the Bill in detail.

II. REPORT

Object of the Bill

The Deposit Protection Scheme (Amendment) Bill 2010 (the Bill) seeks to amend the Deposit Protection Scheme Ordinance (Cap. 581) (the Ordinance) to enhance the protection for depositors under the Deposit Protection Scheme (the Scheme) and to improve the operating efficiency of the Scheme.

LegCo Brief Reference

2. File Ref.: B9/2/2C issued by the Financial Services and the Treasury Bureau dated 7 April 2010.

Date of First Reading

3. 21 April 2010.

Background

4. The Ordinance was enacted in May 2004 and the Board was formed in July 2004 to establish and administer the Scheme. The Scheme commenced operation in September 2006. The salient features of the Scheme are summarized below:

- (a) Unless exempted by the Board, all licensed banks are Scheme members from whom contributions are collected and paid into the Deposit Protection Scheme Fund (the Fund). The current target fund size of the Fund is 0.3% of the total amount of all relevant deposits;
- (b) Compensation not exceeding \$100,000 may be paid to each depositor of a Scheme member (the failed Scheme member) in respect of which a winding up order has been made or the Monetary Authority (MA) has served a notice on the Board that compensation should be paid from the Fund;
- (c) Under section 1 of Schedule 1 to the Ordinance, certain types of deposit, such as time deposits for a term exceeding five years, structured deposits and secured deposits, are not protected by the Scheme; and
- (d) The Scheme will borrow from the Exchange Fund to pay depositors any compensation payable in respect of a failed Scheme member. The Scheme will seek reimbursement from the liquidation of the failed Scheme member for the compensation paid to depositors. The cost of borrowing from the Exchange Fund, any compensation paid that cannot be recovered from the liquidation and the administrative cost incurred by the Scheme will be charged to the Fund.

5. On 14 October 2008, the Financial Secretary announced the use of the Exchange Fund to guarantee full repayment of all customer deposits held with authorized institutions in Hong Kong. The guarantee is due to expire at the end of 2010.

6. According to paragraph 2 of the LegCo Brief, the Board completed a review of the Scheme and consulted the public on its findings by two phases in 2009. Following the review, the Board proposes a number of enhancements to the Scheme for addressing the latest developments in the international and local financial markets, in particular, for meeting the public expectation for better deposit protection. These include raising the protection limit from \$100,000 to \$500,000, and extending the Scheme to deposits secured for supporting other banking and financial services under an integrated account.

Comments

7. The Bill seeks to amend the Ordinance to implement the proposals concluded from the above review of the Scheme. The proposed amendments are summarized in the following paragraphs.

Enhancing the level and scope of protection

8. Clause 3 of the Bill seeks to amend the definition of "deposit" under the Ordinance to include deposits subject to any security (including any form of encumbrance, charge, mortgage, pledge, lien and right of set off) referable to the provision of any banking or financial services so that such deposits would be protected by the Scheme.

9. Clause 4(1) and (2) propose to amend section 27 of the Ordinance to raise the limit of compensation under the Scheme to \$500,000 for each depositor. According to paragraph 4 of the LegCo Brief, this will fully cover about 90% of depositors in Hong Kong, on a par with the higher end of international standards. To tie in with the proposed increase in the Scheme protection limit, clause 8 seeks to amend section 38 of the Ordinance so that the right to which the Board may subrogate upon making a payment of compensation to a depositor, in so far as it relates to the interest accrued on the payment, is to be determined on the basis of the new protection limit of \$500,000.

Reducing Scheme members' additional annual costs due to the increased protection limit

10. According to paragraphs 6 and 7 of the LegCo Brief, raising the protection limit and protecting secured deposits will increase the aggregate amount of deposits protected by the Scheme, which will result in a higher level of contribution payable by the banks. In order to eliminate any incentive for banks to pass on the added cost to depositors, clause 13 proposes a number of measures to mitigate any additional costs which may otherwise be incurred by Scheme members due to the increased protection limit:

- (a) A new definition of "amount of relevant deposits" will allow Scheme members to report, for contribution assessment purposes, the net amount¹ of relevant deposits after deducting relevant liabilities owed by depositors;
- (b) The target fund size would be adjusted from 0.3% to 0.25%²; and
- (c) The percentages for calculating build-up levies payable by Scheme members of different MA supervisory ratings would be reduced by 65%³.

Streamlining the operation of the Scheme to increase operating efficiency

11. The Bill also seeks to streamline the operation of the Scheme by introducing the following changes:

- (a) Clause 4(5) seeks to empower the Board to make reasonable estimates of the value of annuities and future and contingent liabilities and the amount of interest accrued on deposits or liabilities under specified circumstances to expedite the payment of compensation to depositors. If the estimated amount paid is later found to exceed the amount of compensation to which the depositor would otherwise have been entitled, clause 7 proposes to enable the Board to recover any excess amount from the depositor;
- (b) Clause 6 proposes to enable the Board to make interim payments of different amounts to different depositors or different classes of depositors;
- (c) Clause 10 seeks to give the Board additional powers to make rules for the disclosure, acknowledgement, description and representation of protected and non-protected deposits; and
- (d) Clause 12 proposes to allow members of the Board to conduct meetings and approve written resolutions by electronic means.

Consequential and other amendments

12. The Bill also introduces consequential amendments as a result of the proposed increase in the Scheme protection limit. The Schedule to the Bill seeks to amend section 265 of the Companies Ordinance (Cap. 32) to increase the maximum amount of depositors' priority claims in a bank liquidation from \$100,000 to \$500,000, and to adopt the definitions of "deposit" and "depositor" in the Ordinance in lieu of those in the Banking Ordinance (Cap. 155).

¹ This net amount is proposed to be subject to an upper limit of \$500,000 for each depositor.

² Under the new protection limit of \$500,000, the contributions to be collected and accumulated in the Fund to meet the payout expenses of the Scheme are estimated to be \$2.8 billion, which is approximately 0.25% of the total amount of relevant deposits: see paragraph 6 of the LegCo Brief.

³ The proposed reduction of the percentages for calculating build-up levies is due to the projected doubling in size of the amount of relevant deposits: see paragraph 7 of the LegCo Brief.

13. Other amendments relate to transitional provisions and related matters.

14. The Legal Service Division has sought clarification from the Administration on certain technical issues, including the clarity of the proposed consequential amendments to section 265 of Cap. 32 and the Chinese text of certain provisions. In response to our enquiries, the Administration has agreed to introduce amendments to improve the drafting of the relevant provisions.

Commencement

15. If enacted, the Bill will come into operation as follows:

- (a) The provision giving the Board additional rule-making powers will come into operation on the day the Bill is published in the Gazette as an Ordinance;
- (b) the new definitions of "deposit" and "amount of relevant deposits" will come into operation on 20 October 2010 for the purpose only of submitting returns and reports under section 48(2) and (3) of the Ordinance to enable the target fund size and build-up levies to be calculated for the year of 2011; and
- (c) the other provisions of the Bill will come into operation on 1 January 2011.

Public Consultation

16. According to paragraph 18 of the LegCo Brief, the Board conducted a two-phased public consultation on the proposals in April to June and August to October 2009. It has also approached interested parties, including industry associations, the Consumer Council and the Hong Kong Institute of Certified Public Accountants, for comments. There is general support from the public and the parties consulted, and their comments have been taken into account where appropriate. For further details, Members may refer to the Administration's paper on the review of the deposit protection scheme issued in January 2010 (LC Paper No. CB(1)978/09-10(04)) for the meeting of the Panel on Financial Affairs (the Panel) held on 1 February 2010.

Consultation with LegCo Panel

17. The Panel discussed the Administration's proposals to enhance the Scheme at its meetings on 1 June 2009 and 1 February 2010. Panel members expressed various concerns. These include the appropriateness of raising the protection limit to \$500,000, the impact of customers' practice of splitting deposits between different banks on the effectiveness of the Scheme, the types of deposits covered / not covered by the Scheme, disclosure requirements regarding the protection status of deposits, the target fund size

and investment strategy of the Fund, and whether the implementation of the proposed enhancements to the Scheme could dovetail with the lifting of the full deposit guarantee scheduled to expire at the end of 2010. Members may refer to the minutes of these meetings (LC Papers Nos. CB(1)2562/08-09 and CB(1)1493/09-10) for further details.

Conclusion

18. The Legal Service Division is considering the Administration's reply to the technical issues raised in relation to the Bill. Subject to Members' views as to whether to form a Bills Committee to study the policy aspects of the Bill, a further report will be issued in due course.

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