立法會
Legislative Council

LC Paper No. CB(1)1493/09-10
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Panel on Financial Affairs

Minutes of meeting
held on Monday, 1 February 2010 at 10:00 am
in the Chamber of the Legislative Council Building

Members present	**:**	Hon CHAN Kam-lam, SBS, JP (Chairman) Hon Albert HO Chun-yan Ir Dr Hon Raymond HO Chung-tai, SBS, S.B.St.J., JP Hon James TO Kun-sun Dr Hon Philip WONG Yu-hong, GBS Hon Emily LAU Wai-hing, JP Hon Vincent FANG kang, SBS, JP Hon Jeffrey LAM Kin-fung, SBS, JP Hon Andrew LEUNG Kwan-yuen, SBS, JP Hon WONG Ting-kwong, BBS, JP Hon KAM Nai-wai, MH Hon Starry LEE Wai-king Dr Hon LAM Tai-fai, BBS, JP Hon Paul CHAN Mo-po, MH, JP Hon CHAN Kin-por, JP Hon Mrs Regina IP LAU Suk-yee, GBS, JP
Members absent	**:**	Hon Ronny TONG Ka-wah, SC (Deputy Chairman) Dr Hon David LI Kwok-po, GBM, GBS, JP Hon Abraham SHEK Lai-him, SBS, JP Hon CHIM Pui-chung

Public officers attending	:	Agenda Item IV Mr Norman CHAN, SBS, JP Chief Executive Hong Kong Monetary Authority Mr Peter PANG, JP Deputy Chief Executive (Development) Hong Kong Monetary Authority Mr Eddie YUE, JP Deputy Chief Executive (Monetary) Hong Kong Monetary Authority Mr Arthur YUEN, JP Deputy Chief Executive (Banking) Hong Kong Monetary Authority Agenda Item V & VI Mr CHENG Yan-chee, JP Deputy Secretary for Financial Services and the Treasury (Financial Services)
Attendance by invitation	:	Agenda Item V Mr Raymond LI, JP Chief Executive Officer Hong Kong Deposit Protection Board Mr Colin POU Deputy Chief Executive Officer Hong Kong Deposit Protection Board Agenda Item VI Mr Keith LUI Executive Director (Supervision of Markets) Securities and Futures Commission

Mr Rico LEUNG
Senior Director (Supervision of Markets)
Securities and Futures Commission

Mr Derrick FUNG
Head of Clearing Division
Hong Kong Exchanges and Clearing Limited

Mr Allan TONG
Chairman
Federation of Share Registrars Limited

Clerk in attendance: Ms Anita SIT
Chief Council Secretary (1)5

Staff in attendance : Mr Noel SUNG
Senior Council Secretary (1)4

Mr Fred PANG
Council Secretary (1)5

Ms Haley CHEUNG
Legislative Assistant (1)8

Action

I Confirmation of minutes of meeting and matters arising

(LC Paper No. CB(1)941/09-10 — Minutes of the special meeting on 19 November 2009

LC Paper No. CB(1)976/09-10 — Minutes of the meeting on 7 December 2009)

The minutes of the meetings held on 19 November 2009 and 7 December 2009 were confirmed.

II Information papers issued since the last meeting

(LC Paper No. CB(1)899/09-10 — Article entitled "Hong Kong Mortgage Corporation - Past its Use - By Date" (English version only) as published in Best Practice (Vol. I, No. 3)

LC Paper No. CB(1)1027/09-10(01) — Administration's paper on fourth quarterly report of 2009 on Employees Compensation Insurance — Reinsurance Coverage for Terrorism)

2. Members noted the information papers issued since the last regular meeting on 4 January 2010.

III Date of next meeting and items for discussion

(LC Paper No. CB(1)978/09-10(01) — List of outstanding items for discussion

LC Paper No. CB(1)978/09-10(02) — List of follow-up actions

LC Paper No. CB(1)994/09-10(01) — Panel Chairman's letter dated 22 January 2010 to the Secretary for Financial Services and the Treasury concerning the interruption of dissemination of Hang Seng Indexes (Chinese version only)

LC Paper No. CB(1)994/09-10(02) — Hon James TO and Hon KAM Nai-wai's joint letter dated 25 January 2010 concerning the interruption of dissemination of Hang Seng Indexes (Chinese version only)

LC Paper No. CB(1)1034/09-10(01) — Administration's written response to the Panel Chairman's letter dated 22 January 2010)

Meeting on 1 March 2010

3. Members noted that the Administration had proposed two discussion items for the next regular meeting scheduled for 1 March 2010, as follows:-

(a) Review of the Trustee Ordinance and related matters; and

(b) Budget of the Securities and Futures Commission (SFC) for the financial year of 2010-2011.

4. Referring to his letter to the Secretary for Financial Service and the Treasury (SFST) and the letter from Mr James To and Mr KAM Nai-wai regarding the suspension of dissemination of Hang Seng family of indexes on 22 January 2010, the Chairman said that he had communicated with Hang Seng Indexes Company Limited (HSIL) and had requested the company to provide a report on the incident to the relevant regulatory authorities as soon as possible and make a copy of the report available to the Panel. HSIL had indicated that it might complete the report in about a week.

5. Mr James TO requested that the issue be discussed at the next Panel meeting on 1 March 2010, as by that time HSIL should have completed its report and the regulatory authorities should have come up with remedial actions. He declared that he was holding a small number of the shares of the Hang Seng Bank Limited.

6. Mrs Regina IP remarked that since practitioners in the information technology sector had also raised concern about the incident, a joint Panel meeting might be held with the Panel on Information Technology and Broadcasting to discuss the issue.

7. Dr Philip WONG said that although the Hang Seng indexes were useful references for investors, the indexes were only one of the considerations of investors in making their investment decisions. When the dissemination of Hang Seng indexes was suspended, no one had an unfair advantage over others. He did not consider that the incident was relevant to the terms of reference of the Panel.

8. Mr Jeffrey LAM said that the suspension of the dissemination of the Hang Seng indexes lasted for about half an hour and this was the first time such an incident occurred in the Hong Kong stock market, although similar incidents had happened in overseas stock markets before. As far as he understood, the incident was caused by problems with computer formula and not by human errors or computer virus. During the suspension period, HKICL had disseminated the index information to the concerned parties through e-mails, and the suspension had not had a significant impact on the market. He would suggest that the Panel consider whether and how it should follow up the matter after the investigation report was available. Mr WONG Ting-kwong shared Mr LAM's view and said that the Panel should wait for the investigation report and deal with other more important issues first.

9. Ms Emily LAU said that since Members belonging to the Democratic Party as well as Members belonging to the Democratic Alliance for Betterment and Progress of Hong Kong were very concerned about the incident, and the Administration also indicated in its letter to the Chairman that the Administration was highly concerned about the incident, it was appropriate for the Panel to discuss the incident. She supported the suggestion of including an agenda item on the incident for the next Panel meeting.

10. The Chairman suggested and members agreed that an item on the incident be included in the agenda for the next Panel meeting on 1 March 2010.

IV Briefing on the work of the Hong Kong Monetary Authority

(LC Paper No. CB(1)978/09-10(03) — Hong Kong Monetary Authority (HKMA)'s paper on its work

LC Paper No. CB(1)1034/09-10(02) — HKMA's press release of the investment results of the Exchange Fund in 2009)

Briefing by the Chief Executive, the HKMA

11. At the invitation of the Chairman, Chief Executive, Hong Kong Monetary Authority (CE/HKMA) gave a PowerPoint presentation on the economic environment of and the risks facing Hong Kong and the work of HKMA. He highlighted the following points in the briefing:

(a) Real GDP rebounded strongly by 3.5% in the second quarter of 2009, reversing the decline in the previous four consecutive quarters. The economy continued to improve in the third quarter of 2009, though at a slower pace of 0.4%. Slower growth in the third quarter mainly reflected persistently weak external demand. Domestic demand remained buoyant mainly due to massive inventory restocking spurred by optimism of businesses on retail sales. Recent economic indicators suggested local economic activities remained strong in the fourth quarter.

(b) The unemployment rate declined to 4.9% in December 2009 from a three-year high of 5.4% in August. Recent job market surveys showed a slight pick-up in hiring sentiment. Deflationary pressure gradually receded.

(c) Economic recovery was expected to continue and inflationary pressure might remain moderate, although the economy was still affected by a number of uncertainties, such as the uncertainty on the strength and sustainability of recovery in the advanced countries, the difficulty of overseas authorities in timing the exit strategies and the pressure of international capital flows on asset markets.

(d) Faced with tight credit conditions resulting from the global financial crisis, local corporations and residents repatriated funds from abroad to meet liquidity needs. The fact that Hong Kong's banking sector remained robust throughout the global financial crisis and the introduction of the full deposit guarantee might also have attracted safe-haven inflows of capital to Hong Kong. As a result, Hong Kong dollar loans decreased while Hong Kong dollar deposits increased.

Loans resumed small growth in the second quarter of 2009. Credit crunch apparently was not the main reason for fund inflows.

(e) Overseas funds continued to flow into the Hong Kong dollar, probably prompted by a search for higher returns and optimism about better economic outlook for Hong Kong and the Mainland. Equity investments accounted for a substantial portion of the inflows. Fund raising activities in the Hong Kong stock market were buoyant in 2009, with more than $500 billion raised through Initial Public Offerings (IPOs), rights issues and placements, of which $340 billion was raised by companies on the Mainland. As much as $300 billion raised by Mainland companies might still be held as Hong Kong dollar deposits at the end of 2009. When the funds raised were exchanged into other currencies, the Hong Kong dollars held by these companies would decrease. Since the interest-rate spread between the Hong Kong dollar and US dollar was considerably narrower than in 2006 and 2007 when the stock market was just as active, carry trades were no longer attractive and could not provide a counteracting force against the pressure of fund inflows into the Hong Kong dollar.

(f) A large part of the inflows into the Hong Kong dollar since the second quarter of 2009 was equity-related of which $340 billion was raised by Mainland corporations. The pressure of capital inflows might persist in 2010 if the equity market continued to be buoyant, equity fund-raising remained active and US interest rates remained low. If capital flows reversed resulting in strong outflows from the Hong Kong dollar, asset prices might fall and interest rate would go up according to the Currency Board system. These might have an impact on the financial markets and investors. The public should be alert to these risks.

(g) Investors should not take a one-sided bet against the US-dollar, since the movements for the exchange rate could be very volatile in the short run. Exchange rates were affected by many factors and could go either way, and market expectation of its movements might also change easily. The current and expected government debt situation in the US was no worse than that of other countries, particularly Japan. The International Monetary Fund (IMF) expected that general government debt in the US would be 108% of its GDP in 2014, which was much lower than Japan's current level of around 200%, and comparable to Euro-4 (99%) and the UK (98%). The outlook for the US economy was also no worse than that for other major economies because the effects of the global financial crisis were widespread and many major economies would need time to recover. When US-dollar interest rates rose or if the market expected the US dollar to strengthen, US-dollar funded carry trades would be unwound. The public should be alert to the risk of a reversal in capital flows, which could lead to volatilities in

Hong Kong dollar interest rates and could have a large impact on the economy and asset prices.

(h) Investment income of the Exchange Fund for 2009 (excluding valuation changes in the Strategic Portfolio) amounted to $106.7 billion. Most of the asset classes of the Exchange Fund recorded investment gains in the year. The fixed rate for calculating the payment to the Treasury for 2009 was 6.8%. Based on the fixed rate, the Exchange Fund paid $33.5 billion to the Fiscal Reserves for 2009. The Accumulated Surplus increased by $72.8 billion in 2009.

(i) The HKMA was implementing a number of measures put forward by the Basel Committee, including the planned issue of the finalized version of the "Guideline on A Sound Remuneration System" in the first quarter of 2010, reviewing the proposals on the enhancement of global capital and liquidity standards, and formulating proposals to enhance the liquidity regulatory framework. The Hong Kong Deposit Protection Board (HKDPB) aimed to submit legislative proposals to LegCo in the second quarter of 2010 to raise the deposit protection coverage to $500,000, so that the enhanced scheme could be implemented before the expiry of the full deposit guarantee by the end of 2010.

(j) At the end of 2009, more than 24 400 eligible customers (about 98%) of the Lehman Brothers Minibonds had accepted the repurchase offers. In mid-January 2010, about 80% of all Lehman Brothers-related complaints had been handled or resolved. The HKMA aimed to substantially complete the investigation of the remaining cases by the end of March 2010.

(k) The HKMA was reviewing the Hong Kong Association of Banks' response to the consultation of SFC on proposals to enhance protection for the investing public. The HKMA was also assisting the Government in preparing for the launch of the consultation on proposals to enhance investor education and establish a financial dispute resolution system. An independent consultant jointly commissioned by HKMA and SFC completed a report on the implementation of the mystery shopping programme in December 2009. The programme would be implemented in 2010.

(l) Renminbi trade settlement business in Hong Kong was on a steady rise. The HKMA had been actively promoting the further development of renminbi business in Hong Kong. The HKMA and the People's Bank of China were analyzing some of the ideas put forward during the visit of a delegation of the Hong Kong Association of Banks to Shanghai and Beijing in November 2009. In December 2009, the Chief Executive of the HKSAR relayed a message from Premier Wen Jia-bao about the various areas in which the Mainland would support the development of renminbi business in Hong Kong. The HKMA would follow up with the Mainland authorities.

(*Post-meeting note*: CE/HKMA's speaking note (LC Paper No. CB(1)1052/09-10(01)) was circulated to members on 2 February 2010 (Chinese version) and 9 February 2010 (English version) respectively.)

Discussion

Capital flows

12. Mrs Regina IP, Ir Dr Raymond HO and Mr Paul CHAN expressed concern about the impact of the inflows and subsequent outflows of large amount of capital on local asset prices and the overall economy. Mr CHAN asked whether HKMA would consider establishing a mechanism to collate and disclose statistics on the inflows/outflows of capital so that the market and the public could be aware of the capital movements and be alert to the impact on asset prices.

13. CE/HKMA responded that Hong Kong, as an open economy, did not restrict flows of capital; the measures that the Government could deploy to counteract the movement of capital were therefore limited. Such movement of capital, however, was subject to market force, e.g. when there was a difference in the interest rates of the US and Hong Kong dollars. At present, the HKMA already provided information on the Aggregate Balance of Hong Kong dollars held by banks on real time basis. Given that Hong Kong had an open economy, it was impossible for the HKMA to identify the sources of the capital inflows or forecast the timing of the inflows/outflows of capital, although HKMA's analysis showed that the recent large inflows of capital were not for speculative purposes. As such, it would be difficult for HKMA to collate comprehensive and accurate information regarding the sources and channels of capital inflows into and outflows from Hong Kong. The HKMA would continue to closely monitor the situation, and where possible, would endeavour to collate and provide an analysis of relevant information.

Exit from the quantitative easing policy

14. Ir Dr Raymond HO enquired about the strategies adopted by the major economies to exit from the "quantitative easing" policy. CE/HKMA replied that the "quantitative easing" policy was introduced by governments around the world as a contingency measure to meet the challenges of the global financial crisis, and was expected to be withdrawn when the economy in individual countries had stabilized. It was, however, impossible to ascertain at this stage whether the global economy would continue to stabilize and recover. As far as Asian countries were concerned, the threat of inflation was not imminent, rather the threat of an asset bubble arising from large inflows of capital required close attention by the governments.

Property market, mortgage loans and inflation

15. While noting that HKMA had to rely on the information provided by the relevant sector in analyzing the impact of Mainland capital on the local property market, Ms Emily LAU opined that in view of the close correlation between the property market and Hong Kong's economy, the HKMA should establish a system for collating and analysing the information related to the property market, and in future, CE/HKMA's briefing should include an analysis of the property market.

16. CE/HKMA responded that as Hong Kong had an open economy, the HKMA did not possess detailed information regarding the sources of the capital flowing into the property market, and therefore had difficulty in obtaining relevant data for analyzing the impact of investments in the property market from people outside Hong Kong, including those from the Mainland. HKMA had obtained information about the property market from sources in the property sector and relevant government departments, such as the Census and Statistics Department. Based on the rough estimate of a property agent, in 2009, about 10% of the residential units were purchased by people from the Mainland, and the amount of investment put into the property market by these people was impossible to be ascertained. CE/HKMA said that HKMA would try to include an analysis of the property market in future briefings for the Panel if it could secure more relevant data from reliable sources.

17. Mr Jeffrey LAM enquired about the impact of the recent measures of the Mainland authorities to tighten bank credit and the property market on Hong Kong's economy and Hong Kong enterprises' investments in the Mainland. He also pointed out that while HKMA had warned against a possible asset-price bubble and requested the banks to be prudent in their risk management, some banks continued to introduce attractive mortgage loan schemes. In this regard, he asked whether HKMA would introduce further measures to guard against imprudent lending in the banking sector.

18. CE/HKMA responded that the financial and banking systems in Asian countries had performed better than those in the US and European countries during the global financial crisis. In face of a large inflow of capital into Asia and the Mainland, the Central Government had to take steps to ensure the stability of the financial and banking systems, which should also be beneficial to Hong Kong's economy. CE/HKMA pointed out that on 23 October 2009, the HKMA issued guidelines to Authorized Institutions (AIs) on lowering the loan-to-value (LTV) ratio of luxury properties to 60%, and reminded AIs to exercise prudence in assessing the risks involved in mortgage loans for small and medium sized residential units. HKMA would continue to conduct on-site examinations to ensure compliance with the guidelines. The Deputy Chief Executive (Banking)/HKMA (DCE(B)/HKMA) added that HKMA had recently commenced a new round of on-site examinations to AIs, and reminded them to be prudent in valuation of properties and assessing the borrowers' repayment ability and not to exceed the specified LTV ratios in granting mortgage loans.

19. Mr Paul CHAN enquired whether HKMA had assessed the inflationary impact of the surge in asset prices, and about the estimated inflation rate in 2010. CE/HKMA responded that based on the assessment of the International Monetary

Fund and other experts, the inflationary rate of Hong Kong in 2010 would be moderate, i.e. at about 1.5%, and should not be a cause for concern.

Exchange Fund

20. Mrs Regina IP expressed concern about the impact of the continued weakening of the US dollar on the Exchange Fund, as the investment benchmark of the Exchange Fund contained a substantial allocation to US dollar-denominated assets. Given the economic situation in the US, there was concern about the possible collapse of the US dollar. CE/HKMA responded that the trend of the US-dollar exchange rate could be viewed differently from short-term and long-term perspectives. The US-dollar exchange rate could be very volatile in the short term, say in three to five years, whereas the trend of the exchange rate for a longer term, e.g. in the past thirty to fifty years, could be different. Recent market speculation was that the US dollar would remain weak in the foreseeable future. The US-dollar exchange rate might become volatile when there was a reversal of the flow of capital, change in interest rates and the need of investors to seek a safe haven for capital, etc.

21. Mr Paul CHAN remarked that the market generally anticipated gradual depreciation of the US dollar and appreciation of Renminbi. He enquired whether investments of the Exchange Fund had included Renminbi, and the percentage of such investment. In response, CE/HKMA said that currently, the currency and asset mix of the Exchange Fund did not include Renminbi or Renminbi-denominated assets. However, the HKMA would consider investing in different markets, including the Mainland market, with a view to enhancing the returns of Exchange Fund and protecting its purchasing power in the long run, bearing in mind that the primary objective of the Exchange Fund was to maintain monetary stability.

Trade financing

22. Mrs Regina IP expressed concern that despite the large inflows of capital, bank lending to enterprises remained at a low level, which was not conducive to supporting economic growth. CE/HKMA responded that the Government had introduced the loan guarantee schemes to ease the credit crunch faced by small and medium sized enterprises (SMEs), which to a certain extent had helped sustaining the economy and consumer confidence in spending. Data available to HKMA indicated that about 28 000 SMEs had benefited from the loan guarantee schemes, with loans amounting to around $70 billion.

Reform of the regulatory regime

23. Mr Andrew LEUNG pointed out that as a result of the global financial crisis, governments in the US and Europe had introduced a number of reform measures to tighten the control of the banking sector. He enquired whether and how Hong Kong would follow the footsteps of the US and European governments and the possible impact of such enhanced regulatory measures on the local banking sector, especially the medium and smaller sized banks. He also asked what measures HKMA would take to assist the medium and smaller sized banks in coping with tightened regulatory standards and the impact of the lifting of the full deposit guarantee at the end of 2010.

24. CE/HKMA said that the financial and banking sectors of Hong Kong had remained sound and robust in face of the challenges of the global financial crisis, with the capital adequacy ratio of banks maintained at a high level of above 16%. Reform of the regulatory regime for the financial and banking sectors was a hot topic in the international community after the outbreak of the global financial crisis, and the US government had introduced an array of reform measures which would have far reaching effect on the US and other major economies. HKMA had participated in the international deliberation of the reform measures and formulation of some of these measures. For instance, the HKMA had conducted a consultation exercise on the control of the remuneration of senior executives of banks in 2009, and aimed to introduce the revised guidelines in the first quarter of 2010. HKMA was also reviewing the proposals on enhancement of capital and liquidity standards having regard to their impact on the banking sector.

Lehman Brothers Minibonds Incident

25. Noting that by the end of 2009, about 24 400 complainants relating to the Lehman Brothers Minibonds Incident had reached settlement with the banks, Mr WONG Ting-kwong enquired about the situation of complaints relating to sales of structured financial products other than Lehman Brothers Minibonds.

26. DCE(B)/HKMA responded that 80% of the complaints relating to Lehman Brothers had been dealt with; the majority of these cases had been resolved between the relevant AIs and the complainants under the Lehman Brothers Minibond Repurchase Scheme. For the remaining complaints, the HKMA had completed the investigation of about 3 500 cases, and disciplinary actions were being taken on some of these cases. Investigation into the remaining cases was still in progress.

27. Mr KAM Nai-wai expressed concern that so far HKMA had taken disciplinary action in respect of only one complaint regarding mis-selling of structured financial products. Noting with concern that the complainants would not be informed of the outcome of the cases until completion of the procedures for disciplinary cases, Mr KAM enquired when the complainants would be informed of the result of the investigations, and when the disciplinary actions would be completed.

28. CE/HKMA responded that HKMA had to follow, step by step, the procedures laid down in the relevant legislation for investigation of complaints against the AIs in order to ensure the fairness of the process to the complainants and to the subjects of the complaints. The HKMA could only disclose details of the disciplinary actions taken against an AI or a bank staff after completion of the disciplinary procedures. He stressed that HKMA had made every effort to expedite the investigation of the complaints. DCE(B)/HKMA supplemented that while appreciating the anxiety on the part of the complainants, the HKMA had to ensure that the investigations were carried out properly in accordance with the prescribed procedures. The HKMA would make the best effort to complete investigation of the complaint cases as soon as possible, but could not provide a timetable for completion of the cases where disciplinary actions were involved, as the timing and duration for dealing with any appeals were beyond the control of HKMA.

Deposit protection

29. Mr James TO expressed concern about the impact of the scheduled lifting of the full deposit guarantee by the end of 2010 on the stability of the banking system. He enquired, apart from the stress tests, what measures HKMA had taken to ensure the stability of AIs, taking into account the risks which might arise from liquidity problems of some European countries. He opined that the enhanced deposit guarantee scheme should be implemented before the full deposit protection was lifted. Dr Philip WONG echoed Mr TO's concern, and asked why Hong Kong would co-ordinate only with the Singapore and Malaysian governments, but not other countries, over the arrangements for lifting of the full deposit guarantee.

30. CE/HKMA responded that the full deposit guarantee was an extraordinary measure introduced under exceptional circumstances. The expiry time for the full deposit guarantee was announced when the contingency measure was launched. The relevant authorities in Hong Kong, Singapore and Malaysia would co-ordinate over the exit arrangements for full deposit guarantee as they introduced similar arrangements and would withdraw the guarantee in their respective jurisdictions on the same date. Co-ordination among the three parties would ensure that there would not be a large outflow of capital from one place to another. Meanwhile, the HKDPB had proposed to increase the ceiling for deposit protection from $100,000 to $500,000, which would provide full protection to a great majority of the deposit accounts in Hong Kong. The Administration aimed to introduce the Bill relating to the enhanced deposit protection scheme into Legislative Council (LegCo) in the second quarter of 2010 so that the enhancements could take effect when the full deposit guarantee expired. As regards the bank accounts with large deposits, the depositors concerned, as in the case before the implementation of full deposit guarantee, needed to assess the risks involved in where to place their deposits. CE/HKMA further said that the stress test would assess the overall risk management of AIs, taking into account the risk of assets held by AIs relating to European countries with liquidity problems.

Provision of banking services

31. Mr KAM Nai-wai expressed concern that as reported in the mass media, some banks had rejected requests from ethnic minority groups for opening bank accounts, allegedly on the instruction of HKMA.

32. DCE(B)/HKMA said that HKMA had clarified that it had not issued any guideline to AIs suggesting to them to stop providing banking services for ethnic minority groups. HKMA had contacted the relevant association assisting the customers concerned and would look into the cases upon receipt of the information from the organization.

33. Ms Emily LAU expressed concern about the impact of the closure of banks' branches on the public. DCE(B)/HKMA responded that HKMA and the Hong Kong Association of Banks had previously (in June 2009) updated the Panel about the situation on provision of banking services to the public, and the AIs had been regularly reminded to meet the expectations of the public. While the number of bank branches had dropped between 2001 and 2006, the number of bank branches had rebounded between 2006 and 2009. At the request of Ms Emily LAU and Mr James TO, DCE(B)/HKMA undertook to provide updated information on the provision of banking services, including but not limited to statistics on the number of bank branches and ATMs provided in recent years.

(*Post-meeting note*: The HKMA's response was circulated to members vide LC Paper No. CB(1)1221/09-10(01) on 24 February 2010.)

34. Mr Albert HO remarked that the existing regulatory regime emphasized on the importance of the stability of the financial and banking system, and there was a need to strengthen the protection for bank customers' interests. Measures should be in place to guard against discrimination against ethnic minority groups, arbitrary closure of customers' accounts by the banks, abusive tactics used by debt collection companies employed by AIs, and imposition of excessive charges or fees. In his report on the "Review of HKMA's work on banking stability", the consultant Mr David CARSE also raised the issue about the role of HKMA in protection of the interests of bank customers. Mr HO sought CE/HKMA's view on the issue.

35. CE/HKMA responded that the protection of banks' customers involved protection of depositors and buyers of financial products sold at the banks. The maintenance of the stability of the banking system was instrumental in the protection of the interest of bank customers. In addition, the HKMA also monitored the operation of the AIs, and would take steps to deal with particular issues. For instance, in response to the media reports that ethnic minority groups had encountered difficulty in opening bank accounts, the HKMA had enquired into the matter and explained its stance to the media. DCE(B)/HKMA supplemented that if there were problems arising from unsatisfactory banking services, the credibility of the individual bank concerned or the banking sector would be adversely affected. If an AI was found to have breached any supervisory guidelines, the HKMA would certainly take action to rectify the situation.

Octopus card

36. Mr WONG Ting-kwong enquired about the progress on the discussion on the reciprocate arrangement for use of the Octopus card and similar cards in the Pearl River Delta region. CE/HKMA responded that the HKMA had been working closely with Mainland authorities to expand the network of outlets in Shenzhen where the Octopus card could be used, and make reciprocate arrangements in Hong Kong for use of the electronic money cards issued in Shenzhen. Discussion was in progress to issue a unified electronic money card which could be used in both Hong Kong and Shenzhen. In the medium and long run, the aim was to develop a common card reader so that card-holders could use different electronic money cards in the Pearl River Delta region.

Budget of HKMA

37. While pointing out that the budget of SFC was presented to the Panel each year for information and comments, Mrs Regina IP and Ms Emily LAU questioned why, as a key regulatory body funded by public money, the HKMA did not present its budget to the Panel.

38. CE/HKMA remarked that SFC presented its budget to the Panel based on a legislative requirement. As far as accountability and transparency were concerned, CE/HKMA would, at the briefing for the Panel in May every year, answer questions raised by members about its Annual Report, which contained the annual budget of the HKMA. CE/HKMA added that he would relay Mrs IP and Ms LAU's views on the budget arrangement to the Financial Secretary.

V. Review of the Deposit Protection Scheme

(LC Paper No. CB(1)978/09-10(04)	—	Administration's paper on review of the Deposit Protection Scheme
LC Paper No. CB(1)977/09-10	—	Background brief on review of the Deposit Protection Scheme prepared by the Legislative Council Secretariat)

Briefing by the Administration

39. The Chief Executive Officer, Hong Kong Deposit Protection Board (CEO/HKDPB) briefed members, through a Powerpoint presentation, on the outcome of the public consultation and review of the Deposit Protection Scheme (DPS). The Deputy Secretary for Financial Services and the Treasury (Financial Services) (DS(FS)) briefed the Panel on the legislative proposals and timetable for taking forward the enhancements to the DPS concluded in the review.

(*Post-meeting note*: The notes of the Powerpoint presentation (LC Paper No. CB(1)1051/09-10(02)) was issued to members vide a lotus notes e-mail on 1 February 2010.)

Investment and expenditure of the DPS Fund

40. In reply to Mrs Regina IP's enquiry about the target size of the DPS Fund, CEO/HKDPB advised that as a result of raising the deposit protection limit to $500,000, the target size of the DPS Fund would increase from about $1.3 billion to about $2.8 billion. He explained that the DPS Fund was not intended for use to pay compensation to depositors. When a Scheme member (i.e. a licensed bank) fell bankrupt, HKDPB would borrow from the Exchange Fund under a standby liquidity facility to pay compensation to depositors. HKDPB would seek reimbursement from the liquidation of the failed Scheme member for the compensation paid to depositors.

41. Mrs Regina IP expressed concern that the Hong Kong Monetary Authority (HKMA) was responsible for the investment of the DPS Fund. She opined that private investment agencies should be allowed to participate in the investment of the Fund, which would help the development of fund management business in Hong Kong. CEO/HKDPB pointed out that the DPS Fund was not part of the Exchange Fund and therefore was not subject to the investment benchmark of the Exchange Fund. The kinds of financial products that the DPS Fund might invest in were specified in the relevant provisions of the DPS Ordinance (Cap. 581), which were limited in scope. For example, the DPS Fund might invest in Exchange Fund Bills and US Treasury Bills. The investment strategy was decided by the HKDPB. Mrs Regina IP maintained her view that the DPS Fund should not be managed solely by HKMA.

42. Noting that the DPS Fund amounted to about $670 million and $1.3 billion in 2008 and 2009 respectively, and that the investment return of DPS Fund was only about $14 million and $4 million in 2008 and 2009 respectively, Mr Paul CHAN expressed grave concern about the low investment return of the DPS Fund. CEO/HKDPB responded that the low investment returns of the DPS Fund were mainly due to the limitations on investment specified in the DPS Ordinance. As the Fund was set up for the purpose of protecting bank deposits, its money could not be placed with banks. The investment strategy for the DPS Fund could be reviewed but had to be within the limits specified in the legislation.

(*Post-meeting note*: The Administration advised after the meeting that the DPS Fund amounted to about $960 million in 2009 and the investment return of the DPS Fund in 2008 and 2009 amounted to $15 million and $6 million respectively.)

43. Mr Paul CHAN enquired about the annual expenditure of about $50 million of the HKDPB, about $25 million of which was for hiring of services. CEO/HKDPB explained that the HKDPB maintained only a small number of core staff. In order to

ensure that HKDPB could efficiently and effectively deal with payment of compensation to depositors in case of bankruptcy of a Scheme member, the Board had engaged relevant service providers, such as accountancy firms, a call centre, an advertisement agency etc, to carry out annual mock exercises to test the capabilities of the service providers. This arrangement of hiring of services could save the expenses for employing a large number of permanent staff.

44. At the requests of Mr Paul CHAN and Mrs Regina IP, CEO/HKDPB agreed to provide the following information:

(a) measures to be taken by HKDPB to enhance the investment return of the DPS Fund; and

(b) details of the expenditure (about $50 million a year) of the HKDPB and ways to reduce its expenditure.

(*Post-meeting note*: The Administration's response was circulated to members vide LC Paper No. CB(1)1221/09-10(02) on 24 February 2010.)

Lifting of full deposit guarantee

45. Noting that HKMA had been in liaison with the authorities in Singapore and Malaysia on the arrangements for lifting the full deposit guarantee, Mrs Regina IP enquired whether similar arrangements would be made with other countries, as many people held deposit accounts with large amount of foreign currencies such as Australian and New Zealand dollars. Mr Albert HO shared Mrs IP's concern. Mr HO remarked that if the timing for lifting the full deposit guarantee in Hong Kong was not synchronized with other countries, there might be an outflow of large amount of capital from Hong Kong to countries with full deposit guarantee.

46. CEO/HKDPB responded that the temporary full deposit guarantee arrangement was introduced by the Financial Secretary amid the global financial crisis in late 2008. As Hong Kong, Singapore and Malaysia had introduced full deposit guarantee at about the same time and planned to discontinue the arrangement after 2010, a tripartite liaison group had been set up to co-ordinate the work of the regulatory authorities concerned. He believed that, in devising a feasible approach for lifting the full deposit guarantee, the Financial Secretary would take into consideration the international practice.

47. In relation to the concern of Mrs Regina IP about the possible impact of the lifting of the full deposit guarantee after 2010, the Chairman requested and CEO/HKDPB agreed to provide information about the deposit protection arrangements in other countries, including but not limited to Australia and New Zealand.

(*Post-meeting note*: The Administration's response was circulated to members vide LC Paper No. CB(1)1221/09-10(02) on 24 February 2010.)

48. Ms Emily LAU expressed concern on whether the implementation of the proposed enhancements to the DPS could dovetail with the lifting of full deposit guarantee so as to prevent outflow of large amount of capital. In this connection, she urged the Administration to introduce the amendment Bill into the Legislative Council (LegCo) as early as possible so as to allow sufficient time for members to scrutinize the proposals and enable timely implementation of the Bill.

49. CEO/HKDPB responded that the revised DPS and the full deposit guarantee were two separate schemes to reinforce confidence in the Hong Kong banking system. HKDPB would make the best effort to take forward the proposed enhancements to the DPS so that the revised Scheme could dovetail with the lifting of the full deposit guarantee. DS(FS) supplemented that the Administration aimed to introduce the amendment Bill into LegCo in the second quarter of 2010.

The moral hazard issue

50. Mr Albert HO enquired whether and how the "moral hazard" factor had been taken into account in formulating the proposal to raise the deposit protection limit to $500,000. CEO/HKDPB responded that "moral hazard" was one of the major concerns in reviewing the DPS. The proposed deposit protection limit of $500,000 was considered suitable based on the average per capita income of Hong Kong, and similar arrangements in countries like the US. As a result of the revised deposit protection limit, over 90% of the depositors would be fully protected, but only about 20% of the total amount of bank deposits would be covered by the revised DPS. The "moral hazard" risk was considered acceptable based on international standard.

51. Mr Albert HO enquired whether the revised DPS would cover deposits in foreign currencies, swap accounts, and deposit accounts held in overseas branches of banks in Hong Kong. CEO/HKDPB said that foreign currency deposit accounts and swap accounts were protected under the revised DPS. Off-shore deposits would not be protected as they were subject to the protection of relevant deposit protection schemes in the respective countries.

Improving efficiency in making compensation payments

52. In response to Ms Emily LAU and Mrs Regina IP's enquiry on the need for legitimizing HKDPB members' participation in Board meetings while they were overseas, CEO/HKDPB said that the proposal was only a technical amendment, as during the mock tests, the HKDPB had the experience of not having the required quorum to convene a meeting when some members were in other countries. The proposed legislative amendment aimed at enhancing the efficiency of the HKDPB in making compensation payments.

VI Development of a scripless securities market

(LC Paper No. CB(1)978/09-10(05) — Administration's paper on development of a scripless securities market)

Briefing by Securities and Futures Commission

53. The Executive Director (Supervision of Markets), Securities and Futures Commission (ED(SM)/SFC) and the Senior Director (Supervision of Markets), SFC (SD(SM)/SFC) briefed members, with the aid of a PowerPoint presentation, on the arrangements for development of a scripless securities market in Hong Kong as proposed by the Working Group on Scripless Securities Market.

(*Post-meeting note*: The notes of the Powerpoint presentation (LC Paper No. CB(1)1051/09-10(03)) were issued to members vide a lotus notes e-mail on 1 February 2010.)

Accuracy and safety of the shareholders' information

54. Mrs Regina IP enquired about the development of scripless securities markets in other places. Noting that under the current proposal, the existing paper-based regime would co-exist with the new scripless regime at the initial stage, she asked about the anticipated duration of the dual system. She expressed concern about the technical arrangements to ensure the accuracy and safety of the shareholders' information in the Central Clearing and Settlement System (CCASS) in a scripless environment, as arguments might arise if there were discrepancies between the computer records and shareholders' own records and there could be computer system failures.

55. In response, ED(SM)/SFC said that reference had been made to the arrangements in the United Kingdom (UK) and Australia in drawing up the proposed operational model, as the securities market in the US was still paper based. The UK stock market still maintained a dual system although the scripless arrangements had been introduced for 14 years. Since nearly nine million shareholders, including many elderly persons, still held share certificates, the UK authority has not yet made

a decision on whether to implement a fully scripless securities market. In Australia, the stock market was turned into a fully scripless securities market in 1999, with the support of the market. Many market participants in Hong Kong had expressed their wish to maintain the status quo. Hopefully the transitional period for implementing a fully scripless securities market would be shorter than that in the UK. As regards the accuracy of the scripless shareholders records, the regulatory authority and the HKEx would ensure that the records in the CCASS would be accurately maintained, and back-up systems would be established for safe storage of the records.

Enhanced corporate governance and transparency

56. Mrs Regina IP expressed concern as to how corporate governance and transparency of the trading system could be enhanced if shareholders were allowed to hold their shares in the CCASS under the name of their brokers, or in the name of a trust fund. Mrs IP asked whether market participants in Hong Kong preferred higher or lower shareholder transparency.

57. ED(SM)/SFC responded that investors held diverse views regarding shareholder transparency. Accounts held under the name of a trust would only show the name of the trust fund but not the names of individual shareholders. In the UK, many investors still preferred to hold their shares under their brokers' names. The proposed operational model could provide investors with more choices and enhance investor protection.

Administrative arrangements and fee level

58. Mr Paul CHAN said that he supported the direction of developing a scripless securities market, and the proposed phased approach, as many investors, especially the elderly ones, preferred to hold share certificates which gave them a stronger sense of security. He also supported that investors would be allowed to hold their personal accounts under the scripless system so that corporate communications and corporate action services could be carried out directly and more efficiently. He enquired about the arrangements in respect of the shares used as collaterals and kept by brokers on behalf of shareholders. He opined that the administrative charges under the scripless regime should not be higher than the current level.

59. ED(SM)/SFC replied that the scripless regime would include arrangements to cater for situations where banks or brokers held shares provided by clients for collateral purposes. The detailed administrative procedures and fee schedules for CCASS and the share registrars would be worked out after the consultation exercise, and the fee level would be reasonable and set having regard to the acceptance of market participants.

60. At the request of Mr Paul CHAN, ED(SM)/SFC undertook to provide, in tabular form, information on the arrangements for implementing a scripless securities market in the UK and Australia, and the proposed arrangements in Hong Kong.

(*Post-meeting note*: The Administration's response was circulated to members vide LC Paper No. CB(1)1221/09-10(03) on 24 February 2010.)

Consultation

61. The Chairman said that Members belonging to the Democratic Alliance for Betterment and Progress of Hong Kong supported the development of a scripless securities market. As such development would bring about significant changes to the ways investors handle their shares and conduct transactions, he urged the relevant parties to conduct extensive consultation with market participants on the detailed arrangements.

VII Any other business

62. There being no other business, the meeting ended at 12:44 pm.

Council Business Division 1
Legislative Council Secretariat
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