

**立法會**  
**Legislative Council**

LC Paper No. CB(1)2037/10-11  
(These minutes have been seen  
by the Administration)

Ref : CB1/PL/FA/1

**Panel on Financial Affairs**

**Minutes of meeting**  
**held on Monday, 7 March 2011 at 10:45 am**  
**in Conference Room A of the Legislative Council Building**

**Members present** : Hon CHAN Kin-por, JP (Deputy Chairman)  
Hon Albert HO Chun-yan  
Dr Hon David LI Kwok-po, GBM, GBS, JP  
Hon James TO Kun-sun  
Hon Emily LAU Wai-hing, JP  
Hon Vincent FANG kang, SBS, JP  
Hon LEE Wing-tat  
Hon WONG Ting-kwong, BBS, JP  
Hon Ronny TONG Ka-wah, SC  
Hon CHIM Pui-chung  
Hon KAM Nai-wai, MH  
Hon Starry LEE Wai-king, JP  
Hon Mrs Regina IP LAU Suk-ye, GBS, JP

**Member attending** : Hon WONG Kwok-hing, MH

**Members absent** : Hon CHAN Kam-lam, SBS, JP (Chairman)  
Ir Dr Hon Raymond HO Chung-tai, SBS, S.B.St.J., JP  
Dr Hon Philip WONG Yu-hong, GBS  
Hon Abraham SHEK Lai-him, SBS, JP  
Hon Jeffrey LAM Kin-fung, SBS, JP  
Hon Andrew LEUNG Kwan-yuen, GBS, JP  
Dr Hon LAM Tai-fai, BBS, JP  
Hon Paul CHAN Mo-po, MH, JP

**Public officers attending** : Agenda Item III  
Miss Mandy WONG  
Principal Assistant Secretary for Financial Services  
and the Treasury (Financial Services)

**Attendance by invitation** : Agenda Item III  
Mr Andrew WAN  
Chief Financial Officer and Senior Director,  
Corporate Affairs  
Securities and Futures Commission  
  
Mr Leo LEE  
Director of Finance and Administration,  
Corporate Affairs  
Securities and Futures Commission

Agenda Items IV and V

Mr Peter PANG, JP  
Executive Director  
Hong Kong Mortgage Corporation Limited

Mr James LAU, Jr., JP  
Chief Executive Officer  
Hong Kong Mortgage Corporation Limited

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

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

Ms Clara LO  
Legislative Assistant (1)10

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As the Chairman could not attend the meeting, the Deputy Chairman chaired the meeting.

**I Confirmation of minutes of meeting and matters arising**

(LC Paper No. CB(1)1336/10-11 — Minutes of meeting on 3 January 2011)

2. The minutes of the meeting held on 3 January 2011 were confirmed.

**II Date of next meeting and items for discussion**

(LC Paper No. CB(1)1458/10-11(01) — List of outstanding items for discussion

LC Paper No. CB(1)1458/10-11(02) — List of follow-up actions)

Meeting in April 2011

3. Members agreed to discuss the following items proposed by the Administration at the next regular meeting scheduled for 4 April 2011:
  - (a) Regulation of Mandatory Provident Fund intermediaries;
  - (b) Consultancy study on Risk-based Capital Framework for Insurance Business in Hong Kong; and
  - (c) Progress report on the work of the Financial Reporting Council.

Follow-up to joint meeting of the Panel on Financial Affairs and Panel on Transport

4. Mr James TO enquired about the up-to-date position of the proposal to set up a subcommittee to follow-up the issues raised at the joint meeting of the Panel on Financial Affairs and Panel on Transport on 28 February 2011. The Clerk to the Panel said that given the proposal, the Panels should decide whether the proposed subcommittee should be formed, and if formed, the terms of reference, areas of work to be covered, and the time frame for completing the work of the subcommittee. Under the existing quota system for subcommittees on policy issues, activation of the proposed subcommittee would require approval of the House Committee. The Secretariat was liaising

with the Chairmen of the two Panels with a view to arranging another joint Panel meeting to work out the details of the proposal.

5. Ms Emily LAU remarked that she agreed holding another joint Panel meeting to decide the matter. While she supported the setting up of a subcommittee to follow up the issues raised at the joint Panel meeting, she understood that the workload of the Secretariat had been extremely heavy. She would therefore request the Secretary General to review the manpower situation and make available manpower resources to cope with the work of the new subcommittee.

### **III Budget of the Securities and Futures Commission for the financial year of 2011-2012**

(LC Paper No. CB(1)1458/10-11(03) — Administration's paper on "Securities and Futures Commission Budget for the Financial Year 2011-12"

LC Paper No. CB(1)1446/10-11 — Background brief on the annual budgets of the Securities and Futures Commission prepared by the Legislative Council Secretariat)

#### Briefing by Administration and Securities and Futures Commission

6. The Principal Assistant Secretary for Financial Services and the Treasury (Financial Services) (PAS(FS)) remarked that the Government supported in principle the proposed budget of the Securities and Futures Commission (SFC) for 2011-2012. The Government noted that SFC had projected a surplus in its budget for 2011-2012, and as in the past years, SFC did not request for appropriation from the Legislative Council.

7. At the invitation of the Chairman, the Chief Financial Officer and Senior Director, Corporate Affairs, Securities and Futures Commission (CFO&SD/SFC) briefed members on SFC's budget for 2011-2012, by highlighting the salient points in the paper.

## Discussion

### *Levies and fees*

8. Given that SFC had a reserve of about \$6,700 million and a surplus of about \$700 million in 2010-2011, Mr James TO was of the view that SFC should reduce the level of levies and fees, and should not be responsible for funding the Investor Education Council (IEC) and Financial Dispute Resolution Centre (FDRC). Mr TO opined that in view of the large reserve and surplus, SFC was tempted to increase its staff establishment. While appreciating the need for SFC to increase the salaries of certain grades of existing staff in order to retain them, Mr TO queried the justification for the proposed 61 new posts and the budgeted increase of staff expenses.

9. PAS(FS) responded that the levy on securities transactions had been reduced from 0.004% to 0.003% in 2010-2011. In 2009-2010, in order to help relieve the cost burden on intermediaries amidst the economic downturn, SFC gave a waiver of the annual licence fees for over 37 000 intermediaries, including licensed corporations, registered institutions, responsible officers and representatives, for one year from 1 April 2009.

### *Regulatory and enforcement work*

10. Mr KAM Nai-wai expressed disappointment at the enforcement work of SFC. Mr KAM opined that the enforcement work of SFC lacked transparency. Unlike the Hong Kong Monetary Authority (HKMA) which reported on a weekly basis the progress of its work on Lehman Brothers-related cases, SFC had not disclosed the progress of its investigations on complaints relating to the Lehman-Brothers Minibonds Incident. Instead, SFC had only announced the settlements reached between financial institutions and investors of Lehman Brothers-related retail structured products. Mr KAM remarked that complainants had been advised that SFC was short of manpower in dealing with complaints, despite that there was an increase of 28 and 10 staff in the Enforcement Division of SFC in 2009-2010 and 2010-2011 respectively. Mr KAM enquired whether SFC had invoked the powers under section 107 of the Securities and Futures Ordinance (Cap. 571) (SFO) to instigate proceedings against financial institutions and their staff for mis-selling of Lehman brothers Minibonds.

11. CFO&SD/SFC responded that the provision of manpower for the Enforcement Division, which currently had 125 staff, was based on the estimated workload of the Division. For 2011-2012, SFC had proposed an increase of 15 staff for the Division. If and when necessary, more staff would be proposed for the Division to meet the increase in workload.

12. CFO&SD/SFC further advised that unlike the mode of investigation adopted by HKMA and Police, SFC had adopted a "top down" approach in dealing with the complaints relating to Lehman Brothers-related retail structured products, with a view to securing the largest compensation for the investors concerned within the shortest time. For instance, a settlement agreement had been reached with the Standard Chartered Bank in the previous week to make a payment of about \$1.5 billion to about 2 200 investors. SFC had met the complainants of the Lehman Brother-related retail structured products on an individual basis.

13. Noting that SFC proposed an increase of 15 staff for the Enforcement Division in 2011-2012, Ms Starry LEE enquired whether SFC had any performance pledge for its enforcement work. CFO&SD/SFC replied that SFC had laid down performance pledges, e.g. for handling applications for authorisation for issue of investment products, and handling of enquiries from investors, and the performance pledges, together with the compliance results in the past three years, were published in SFC's annual reports.

14. Ms Emily LAU enquired about the justifications for the proposal to create 15 additional posts in the Enforcement Division. PAS(FS) responded that the number of criminal charges laid by SFC had increased by over 40% last year, in addition to various civil proceedings against directors of listed companies, as well as proceedings before the Market Misconduct Tribunal.

15. Noting that SFC would be the licensing authority for credit rating agencies, Ms Starry LEE enquired about the improvements that would be brought about by the licensing system, in comparison with situation before the global financial crisis. Mrs Regina IP enquired about the steps to be taken to enhance regulation of credit rating agencies and sale of hedge funds.

16. PAS(FS) responded that at present, there were nine types of regulated activities that were subject to the licensing and registration requirements under the SFO. In line with international developments, the Government proposed to subject credit rating agencies to the regulatory regime under the SFO by introducing a Type 10 regulated activity, i.e. providing credit rating services. The relevant subsidiary legislation was being scrutinised by the Legislative Council. In the proposed Budget, the Licensing Department would be given six additional people to handle the significant growth in the number of applications and duties arising from the new regulatory requirement for credit rating agencies.

17. Mr Albert HO expressed concern that despite the large number of complaints concerning the mis-selling of Lehman Brothers Minibonds by

financial institutions, SFC recorded a surplus of about \$700 million in 2010-2011. Mr HO opined that SFC recorded a surplus in 2010-2011 mainly because it had adopted a "top down" approach to seek settlements between banks and complainants, instead of investigating and taking enforcement actions on individual complaint cases, in which there was prima facie evidence of mis-selling of structured products by financial institutions. Many complainants criticised that SFC's enforcement actions were selective, targeting at the small financial institutions rather than the large ones. The public was also dissatisfied that SFC refused to disclose whether a particular case was being investigated or substantiated, or the progress of its investigations under the pretext of secrecy. Mr HO was dissatisfied that SFC even refused to meet complainants and Legislative Council Members to discuss the progress of the investigation of the complaints, in the guise of maintaining its independence. Mr HO pointed out that the levies collected by SFC were authorized by the Legislature and the Government, and were public money, and SFC should be accountable for the use of the levies. Mr HO expressed disappointment at the lack of transparency of the operation of SFC. For instance, SFC had disclosed some of the information of the Citic Pacific case only after Legislative Council Members repeatedly raised questions on the case. Mr HO was dissatisfied that in reply to some complainants in cases where concrete evidence of mis-selling of investment products existed, SFC stated that it had its own strategy in investigation of complaints in view of the lack of manpower. There was not an effective review mechanism in SFC to review individual complaint cases and the actions taken by SFC. He was of the view that the arrogant attitude of SFC could hardly meet the expectations of the public.

18. CFO&SD/SFC responded that SFC fully understood that the levies for funding the SFC were public money, and had exercised vigilant control over the expenditure of the Commission. For 2011-2012, SFC aimed to make use of its financial resources to enhance the protection of investors, including the establishment of the IEC which would help improve investors' knowledge about different investment instruments and their risks. SFC had met Legislative Council Members and answered their queries upon request. In addition to the "top down" approach in handling complaints relating to the Lehman Brothers-related retail structured products, SFC had interviewed individual complainants in the investigation process. Given the high evidence threshold for prosecution actions under section 107 of SFO and the large number of complaints, SFC had to adopt an approach most suitable for handling the cases. PAS(FS) supplemented that the Process Review Panel of SFC circulated its reports to the Legislative Council on an annual basis. The Government had also given replies to Members' questions raised at Legislative Council meetings about the progress of the investigation into the Citic Pacific case, and prosecution cases under section 107 of SFO. On the transparency

issue, SFC had also given details on its enforcement and prosecution actions in its enforcement reporters, quarterly and annual reports, and daily press releases.

19. Mr James TO echoed Mr HO's concern regarding investigation of the Lehman Brothers-related investment product cases. Mr TO expressed dissatisfaction that while recording a surplus in its budget, SFC had adopted a "top down" approach in seeking settlements between financial institutions and complainants, claiming that it lacked the manpower resources to investigate into individual cases. Mr TO opined that SFC should continue to investigate into complaint cases where the complainants and the financial institutions concerned had not reached settlement, and if appropriate, SFC should carry out criminal investigation into the cases by invoking the powers under section 107 of SFO.

20. PAS(FS) responded that the then acting Secretary for Financial Services and the Treasury had already, in her reply to Members' questions at a previous Council meeting, given explanation as to why SFC could not categorically undertake to initiate criminal proceedings under section 107 of SFO as requested by investors of Lehman Brothers-related investment products.

#### *Staff turnover and recruitment*

21. In response to Ms Starry LEE's enquiry about the turnover rate of senior and middle level staff in SFC, CFO&SD/SFC stated that SFC had to compete with organizations such as major accounting firms and other corporations for staff with relevant accounting or legal expertise and regulatory experience. The highest turnover rate, ranging from a single digit figure to as high as 25%, was recorded at the junior and middle manager level and a strategic pay adjustment had been proposed for 2011-2012 in order to mitigate the loss of experienced staff and reduce the staff turnover rate.

22. Ms Emily LAU was concerned about the high staff turnover rate of SFC, which stood at about 13 to 14% in 2007, and stood as high as 25% in 2010 for junior and middle level staff.

23. CFO&SD/SFC responded that SFC had closely monitored the staff turnover situation, and reviewed the staff remuneration packages annually in comparison with those in the private sector, with a view to retaining and recruiting adequate qualified middle and lower ranking managers. Apart from review of salaries, SFC also introduced measures to further improve human resource management, such as providing subsidies for staff to attend job-related training courses. Through a graduate trainee programme, SFC had successfully recruited about 30 fresh graduates in the past two years, with a



view to filling the middle and junior manager posts. A part-time staff programme would also be implemented to meet the temporary increases in workload.

*Professional and other expenses*

24. Noting that "Professional and other expenses" would increase by 28.8% in 2011-2012, Ms Starry LEE enquired about the types of services to be outsourced. CFO&SD/SFC responded that the professional and other expenses included payments for legal advice and expert advice in areas of investigation of misconduct and complaints cases, supervision of intermediaries and regulation of new financial products. The lower expenses in 2010-2011 were mainly due to savings in legal fees arising from legal costs recovered in the year.

*Centralised strategy and risk team*

25. Ms Starry LEE enquired about the work of the centralised Strategy and Risk team. CFO&SD/SFC remarked that the centralised Strategy and Risk team would comprise a small number of staff including a director, a senior manager and a manager, and would be responsible for strategy and risk management.

*Investors Education Council*

26. Noting that SFC included a provision of \$10 million as the start-up cost and \$27 million for the operation of the IEC for the first half year, Ms Regina IP enquired, given that since SFC had been performing investor education work in the past, whether the existing staff responsible for investor education work would be transferred to the new IEC.

27. PAS(FS) responded that currently SFC could only carry out investor education work relating to securities and futures according to the SFO. The IEC would provide comprehensive investor education to the public of Hong Kong covering a wide spectrum of financial services such as banking service, insurance service and provident funds. The SFO would be amended accordingly to empower SFC to provide education beyond the scope of securities and futures. IEC would be set up as a company wholly-owned by SFC. A non-executive director of SFC, recommended by the SFC Board and endorsed by the Financial Secretary, will become the Chairman of IEC. The Board of Directors of IEC would include representatives of different regulatory bodies and market people. CFO&SD/SFC supplemented that the existing staff in the External Relations Department responsible for investor education would be transferred to the IEC.

*Staff secondment/attachment arrangements*

28. Ms Emily LAU enquired about the staff secondment/attachment arrangements between SFC and the Government.

29. PAS(FS) remarked that at present, a Senior Administrative Officer had been seconded to SFC while two officers from SFC were working in the Financial Services and the Treasury Bureau through an attachment programme. CFO&SD/SFC added that staff attachment had also been arranged between SFC and its counterparts in the Mainland.

*Office premises*

30. Ms Emily LAU remarked that SFC should consider leasing offices in districts with lower office rentals than those in Central, and enquired if SFC had any plan in this regard. CFO&SD/SFC responded that the leases of SFC's offices in Chater House and Li Po Chun Chambers would expire in 2013 and early 2012 respectively, and SFC would review its accommodation needs in due course.

*Resources for new initiatives*

31. In response to Mr Albert HO's enquiry as to whether provisions had been included in SFC's budget for implementation of new initiatives, CFO&SD/SFC replied that the Budget for 2011-2012 had not included provisions for new initiatives requiring legislative amendments, such as the statutory codification of the disclosure requirements for price sensitive information of listed companies.

*Authorization of structured products*

32. The Deputy Chairman remarked that some relevant parties had expressed concern that the process for SFC to authorize the issue of structured products had taken a long time, on an average of about nine months, after the Lehman Brothers Minibonds Incident. The Deputy Chairman enquired whether SFC would consider and discuss with the parties concerned about ways to streamline the authorization process, and/or increase its manpower resources for dealing with the applications.

33. CFO&SD/SFC responded that in view of the complexity of the structured products pending authorization, the significant increase in applications and the need to carefully assess the risks of the structured products, SFC had proposed additional staff resources for the Policy, China and Investment Products Division in order to expedite the authorization process.

*Representation of the Administration/SFC for discussion of SFC's budget*

34. Mr James TO remarked that in the discussion of SFC's annual budget, members had expressed concern about the strategy of SFC in handling complaints, especially the "top down" approach in dealing with complaints involving Lehman Brothers-related investment products. Mr TO pointed out that SFC's interviews with the complainants did not involve taking of any statements from the complainants for investigation purpose. In view that the Government was represented by the relevant Directors of Bureaux and heads of departments in Legislative Council meetings for discussion of the Government budget, Mr TO opined that, with due respect to the Government and SFC officers attending the meeting, the Chairman and Chief Executive Officer of SFC should attend the meeting to answer members' questions regarding SFC's budget.

35. Mr LEE Wing-tat and Mr KAM Nai-wai shared Mr James TO's view and suggested that the Chairman and the Chief Executive Officer of SFC should be invited to attend another Panel meeting for further discussion of SFC's budget. Mr KAM said that if the Chairman and Chief Executive Officer of SFC declined to attend the Panel meeting for further discussion of SFC's budget, he would move a motion to reprimand the two officers. Mr LEE opined that there was a lack of transparency, and checks and balances in the operation of SFC, taking into account the fact that the directors of SFC were appointed by the Government and SFC's budget was approved by the Financial Secretary.

*Motion moved by Mr James TO*

36. Mr James TO moved the following motion:

"本事務委員會將召開特別會議，繼續討論證券及期貨事務監察委員會2011-2012財政年度預算，並邀請證券及期貨事務監察委員會主席及行政總裁出席會議。"

**(Translation)**

"That this Panel will convene a special meeting to continue the discussion on the budget of the Securities and Futures Commission for the financial year of 2011-2012, and invite the Chairman and Chief Executive Officer of the Securities and Futures Commission to attend the meeting."

37. Mrs Regina IP remarked that if members were dissatisfied with SFC's procedures in investigating complaints and/or taking enforcement actions under section 107 of SFO, rather than the proposed budget, the issues could be pursued separately with SFC, instead of further discussion of the budget. Mrs IP remarked that the procedures for dealing with SFC's budget were much better than that for the HKMA budget, which was not subject to discussion by the Panel. The Deputy Chairman and Mr WONG Ting-kwong expressed concurrence with Mrs IP.

38. Mr KAM Nai-wai and Mr James TO opined that members' concerns about SFC's approach and arrangements for investigation and enforcement work were related to the proposals in the budget.

39. The Chairman put Mr James TO's motion to vote. Of the members present, seven voted for and two members voted against the motion. The Chairman declared the motion passed.

*(Post-meeting note: The motion was circulated to members vide LC Paper No. CB(1)1518/10-11 on 8 March 2011. Members were informed vide LC Paper No. CB(1)1571/10-11 on 14 March 2011 that a special Panel meeting would be held on 28 March 2011 to continue discussion of the item.)*

#### **IV Reverse Mortgage Pilot Scheme**

(LC Paper No. CB(1)1458/10-11(04) — Administration's paper on "Reverse Mortgage Pilot Scheme"

LC Paper No. CB(1)1456/10-11 — Background Brief on Reverse Mortgage Pilot Scheme prepared by the Legislative Council Secretariat)

*(Post-meeting note: The Powerpoint notes prepared by Hong Kong Mortgage Corporation Limited (HKMC) (LC Paper No. CB(1)1513/10-11(01)) were issued to Members by a Lotus Notes e-mail on 7 March 2011.)*

40. Mr LEE Wing-tat commented that less people would be interested in joining the Reverse Mortgage Pilot Scheme (the "Scheme") if the Scheme was operated strictly on prudent commercial principles, as the primary objective of banks and intermediaries was to make profits out of the Scheme leading to

lower annuity payments to the elderly. Mr LEE opined that the Government should play a bigger role in the Scheme so as to encourage the elderly to join the Scheme.

41. The Executive Director, HKMC (ED/HKMC) responded that according to an opinion survey conducted in 2010, around 44% of the respondents supported the introduction of reverse mortgage in Hong Kong and almost a quarter of the respondents indicated that they would consider participating in the Scheme based on the proposed annuity payment arrangements. The Scheme would be operated on prudent commercial principles in order to ensure its sustainability. In order to encourage the elderly to join the Scheme, HKMC had introduced certain enhancements to the Scheme under which a single borrower of a reverse mortgage loan would receive a higher monthly annuity than two joint borrowers. Based on overseas experience, the reverse mortgage applicants were on average about 70 years old. According to the annuity table, a 70-year-old couple who had a property of \$2.5 million and chose a life-annuity plan would receive a monthly annuity payment of \$7,000. If the applicant was a 70-year-old singleton, he would receive a monthly annuity payment of \$7,750. If the property was valued at the maximum amount of \$8 million at origination, the monthly annuity payment for a 70-year-old on a 10-year plan or a life-annuity plan would be \$40,800 and \$24,800 respectively.

42. Mr WONG Kwok-hing said that the elderly had expressed concern that the Scheme was not backed by the Government, and that they might not receive any payment if the bank concerned went bankrupt during a financial crisis. The elderly were also concerned that the monthly annuity payment would not be adjusted according to the inflation rate, and thus the real value of the annuity payment would diminish over time due to inflation. Mr WONG pointed out that if a borrower had to first withdraw from the Scheme in order to re-join it based on an increased value of the mortgaged property, the borrower would have to pay a high administrative fee. As such, it would be difficult for an elderly to decide whether he should re-mortgage his property in face of inflation.

43. ED/HKMC responded that based on overseas experience, if the monthly annuity payment was adjusted annually according to the inflation rate, the initial monthly annuity payment would be set at a much lower level. The reverse mortgage schemes in other countries seldom included the inflation factor, as it might affect the attractiveness of the scheme. If the property price went up, say as a result of inflation, a borrower could refinance with a new reverse mortgage based on the higher property price and receive a higher annuity payment. ED/HKMC pointed out that HKMC was a corporation

wholly-owned by the Exchange Fund, and would provide insurance coverage for the Scheme against the risk of shortfall in property price.

44. In response to Mr Ronny TONG's enquiry about the average return rate of reverse mortgages, ED/HKMC remarked that loan to valuation ratio for individual reverse mortgages varied and was subject to a number of factors, such as the age of the borrower, the term of annuity payment that the borrower chose, the value of the underlying property and the interest rate level. The Chief Executive Officer, HKMC (CEO/HKMC) supplemented that as an example, loan to valuation ratio for a 60-year-old borrower who chose a life-annuity plan would be about 70%.

45. Mrs Regina IP pointed out that when HKMC was established in 1997, the Legislative Council was advised that the core mission of HKMC was to promote wider home ownership in Hong Kong, and yet HKMC had extended its business to providing reverse mortgage, loan guarantee for small and medium sized enterprises (SMEs) and other high risk investments. Mrs IP opined that HKMC should be reprimanded for failing to consult the Legislative Council before widening its scope of business. Mrs IP was concerned that since HKMC provided insurance coverage for the reverse mortgage scheme, it might have to provide funding support to the banks for the reverse mortgage payments during an economic downturn. Mrs IP was of the view that the Government should continue to consider the establishment of a comprehensive retirement scheme for the populace, despite the implementation of the Scheme. Mrs IP enquired about the estimated number of participants of the Scheme. Mrs IP and Ms Emily LAU enquired how the participants of the Scheme would be affected if their mortgaged properties were subject to compulsory sale for redevelopment.

46. ED/HKMC responded that the operation of HKMC, as a limited company, was governed by the Board of Directors of the corporation. The formulation of the reverse mortgage arrangements was difficult, in view of the risk factors involved, namely the volatility of property price, the changing interest rate level and the life expectancy of the borrowers. The proposed annuity payment arrangements had taken into account the risk factors of the Scheme. Given the ageing population, more and more old people in Hong Kong would be interested in joining the Scheme. Based on the findings of the opinion survey conducted in 2010, about a quarter of the respondents expressed interest in joining the Scheme. ED/HKMC added that the participation in the Scheme would not affect the position of the elderly concerned in the event that the mortgaged property was subject to compulsory sale for redevelopment, as participants were free to withdraw from the Scheme at any time.

47. Ms Emily LAU noted that while HKMC stated in paragraph 6 of its paper that the Scheme would not involve any Government subsidy, HKMC would act as the insurer for the Scheme to bear the risk of shortfall in property price. Ms LAU enquired about the rate of insurance payment to be borne by the borrowers. Ms LAU also enquired whether overseas governments played a greater role in similar reverse mortgage schemes.

48. ED/HKMC responded that the upfront insurance premium was 0.28% of the property price, which would be collected for seven years between the fourth and tenth years of the reverse mortgage, amounting to a total of about 2% of the property price. There was also a monthly insurance premium charged at 1.25% p.a. on the outstanding mortgage loan. In addition, a counselling fee would be charged for the counselling service provided to the elderly. The purpose of the counselling service was to enable the elderly and their family members to understand their rights and obligations before taking out a reverse mortgage. HKMC was in discussion with the Law Society of Hong Kong to work out the arrangements, including setting the fee level as low as possible. CEO/HKMC supplemented that in the case of the United States which was the pioneer in reverse mortgage schemes, the upfront insurance fee and the monthly insurance premium were also set at 2% and 1.25% p.a. respectively, i.e. the same rates proposed for the Scheme in Hong Kong.

## V SME Financing Guarantee Scheme

(LC Paper No. CB(1)1458/10-11(05) — Administration's paper on "The SME Financing Guarantee Scheme"

LC Paper No. CB(1)1457/10-11 — Background brief on SME Financing Guarantee Scheme prepared by the Legislative Council Secretariat)

### Briefing by Hong Kong Mortgage Corporation

49. CEO/HKMC briefed members, through a Powerpoint presentation, on the SME Financing Guarantee Scheme (SFGS) launched by HKMC on 1 January 2011.

(*Post-meeting note:* The presentation notes (LC Paper No. CB(1)1513(10-11(02))) were issued to Members by a Lotus Notes e-mail on 7 March 2011.)

## Discussion

50. Mrs Regina IP remarked that SMEs had expressed concern that the insurance premium charged under the SFGS was too high, e.g. an SME had to pay a total premium of about \$400,000 for a loan guarantee of \$12 million. Mrs IP enquired how the level of insurance premium was set, and whether consideration would be given to reducing the premium level.

51. ED/HKMC responded that SMEs had to consider whether they could obtain credit facilities without joining the SFGS, and the overall cost in obtaining continuous financing facilities from banks. ED/HKMC pointed out that under the SFGS, some banks were willing to offer more favourable interest rates for the loans granted to SMEs.

52. Mr Albert HO enquired, given that the most difficult period of the credit crunch faced by SMEs was almost over, about the rationale for HKMC to be involved in the traditional business of banks in providing loans to SMEs. Mr HO enquired about the respective functions of the SFGS and the Hong Kong Export Credit Insurance Corporation. Mrs Regina IP shared Mr HO's concern, and pointed out that when HKMC introduced the reverse mortgage pilot scheme and the SFGS, HKMC had diverted from its core businesses. Mrs IP opined that the Government should review the role of HKMC if the private sector was prepared to provide mortgage insurance, in order to avoid competition between the public and private sectors for business opportunities.

53. ED/HKMC responded that one of the core missions of HKMC was to provide support to the banks in risk management in order to ensure the stability of the financial sector. SMEs usually lacked the required collateral to obtain loans from banks to support their business. The SFGS would enable SMEs to obtain loans from banks even during a credit crunch. The SFGS was introduced as a pre-cautionary measure to mitigate the risk exposure for banks at times of market volatility, and had proved to be useful as evidenced by the large number of applications so far received from SMEs. ED/HKMC stressed that HKMC was not involved in granting loans to SMEs but, through the SFGS, performed the role of a guarantor for SMEs in obtaining loans from banks. CEO/HKMC supplemented that under the SFGS, banks were free to accept a guarantee coverage of 50%, 60% or 70% for the loans granted to SMEs. CEO/HKMC pointed out that while the SFGS provided loan guarantee for SMEs, the Hong Kong Export Credit Insurance Corporation provided insurance coverage for local exporters against risks in the importing countries. The Trade and Industry Department also provided funds to support SMEs in the innovation and development of new products. ED/HKMC added that HKMC welcomed private companies to provide mortgage insurance for banks. Given that some private financial institutions providing mortgage insurance



had been downgraded during the global financial crisis in 2008 and hence ceased their insurance business in Hong Kong, there was a need for HKMC to provide a continuous mortgage insurance service to the market.

54. In response to Mr Albert HO's enquiry about the default rate under the Special Loan Guarantee Scheme, CEO/HKMC responded that since the loan guarantee period for most of the loans granted under the Special Loan Guarantee Scheme had yet to expire, the final default rate was not known. However, based on the preliminary figures provided in the report prepared by the Trade and Industry Department, the default rate in the initial stage was about 0.25% in terms of value.

55. The Deputy Chairman was concerned that there was no ceiling for the total guarantee commitment under the whole SFGS, although the HKMC was a limited company. The Deputy Chairman enquired whether an overall ceiling should be set for the scheme internally.

56. CEO/HKMC responded that although there was not an overall ceiling for the SFGS, and the maximum credit amount for each SME was \$12 million, the actual guarantee amount for each SME would be set based on risk assessment of individual companies. The HKMC also provided risk capital backing for exposure due to SME loan guarantee.

57. Mr WONG Ting-kwong remarked that SMEs generally welcomed the SFGS as it enabled SMEs to obtain loans from banks to continue and/or expand their business, especially when some SMEs lacked the required collateral to support their loan applications. Mr WONG suggested that, drawing reference from the government of Dongguan city, consideration could be given to setting up a loan guarantee corporation to assist the SMEs, jointly funded by the Government and the private sector.

58. ED/HKMC responded that HKMC would consider Mr WONG's suggestion.

## **VI Any other business**

59. There being no other business, the meeting ended at 12:55 pm.