

立法會

Legislative Council

LC Paper No. CB(1)999/14-15

Ref. : CB1/PL/FA

Report of the Panel on Financial Affairs for submission to the Legislative Council

Purpose

This report gives an account of the work of the Panel on Financial Affairs ("the Panel") for the 2014-2015 legislative session. It will be tabled at the meeting of the Legislative Council ("LegCo") of 24 June 2015 in accordance with Rule 77(14) of the Rules of Procedure of LegCo.

The Panel

2. The Panel was formed by a resolution passed by LegCo on 8 July 1998 and as amended on 20 December 2000, 9 October 2002, 11 July 2007 and 2 July 2008 for the purpose of monitoring and examining government policies and issues of public concern relating to financial and finance matters. The terms of reference of the Panel are set out in **Appendix I**.

3. For the 2014-2015 session, the Panel comprised 18 members, with Hon CHAN Kin-por and Hon Christopher CHEUNG Wah-fung elected as Chairman and Deputy Chairman respectively. The membership list of the Panel is in **Appendix II**.

Major work

Macro economy

4. During the 2014-2015 session, the Panel continued to provide a forum for Members of LegCo to exchange views with the Financial Secretary ("FS") on matters relating to macro economic issues. On the economic outlook for 2015, the Panel noted at the meeting on 1 June 2015 that for 2015 as a whole, the gross domestic product growth was forecast to be 1-3%, while the forecast

rates of headline and underlying consumer price inflation were 3.2% and 2.7% respectively. The global economic growth was slow on entering 2015, particularly so in the United States ("US") and Europe. The Mainland economy expanded steadily further, but it would still face downward pressures in the near term. Looking ahead, global economic growth was likely to remain moderate and uneven. The lacklustre external environment, coupled with a strong US dollar, would continue to constrain Hong Kong's export performance. While the steady job and income conditions should render support to local consumption, the slowdown in inbound tourism, if persisted, would reduce the domestic growth momentum, and was a cause for concern.

5. Some members expressed concern that the slowdown in inbound tourism and retail sales in recent months might persist for some time in view of the prevailing political environment and the recent replacement of the "multiple-entry" endorsement by the "one trip per week" endorsement for permanent residents of Shenzhen under the Individual Visit Scheme. FS assured members that the Government would stay vigilant to the potential impacts of the future development in inbound tourism and various external uncertainties on the economy and labour market in the period ahead.

6. Members also expressed concern about increasing volatilities in the Hong Kong stock market in recent months. With closer integration between the stock markets of Mainland and Hong Kong and given the differences between the respective regulatory regimes, members highlighted the need for the relevant regulators of Hong Kong, notably the Securities and Futures Commission ("SFC"), to step up co-ordination and co-operation with their Mainland counterparts in supervisory and enforcement matters with a view to enhancing protection for investors in the markets.

7. Members noted with concern the continuous rise in local property prices which had reached levels beyond the affordability of most households. As the demand side management measures and countercyclical measures were gradually losing their effects, members urged the Government to step up its efforts in increasing land and housing supply and consider other effective measures. FS acknowledged that the risks of a housing market bubble were still prominent, and the Government was alive to the possible impact of such risks on the macro-economy and the stability of the financial systems. The Government would spare no effort in increasing land and housing supply, and would closely monitor the development of the property market. If necessary, the Government would take further appropriate measures to maintain stable and healthy development of the property market.

Monetary affairs

8. The Panel continued to receive regular briefings by the Chief Executive of the Hong Kong Monetary Authority ("HKMA") and his colleagues on the work of HKMA. At these briefings, HKMA provided information on the global/regional/local financial and economic conditions, assessment of risk to Hong Kong's financial stability, banking supervision, development of the financial market and Hong Kong as an offshore Renminbi centre, and performance of the Exchange Fund ("EF").

The Exchange Fund

9. The Panel noted that the investment income of EF for 2014 amounted to \$44.7 billion, and the investment income for the first quarter of 2015 was \$6.6 billion. The fixed rates for calculating the payment to the fiscal reserves placed with EF were 3.6% and 5.5% for 2014 and 2015 respectively.

10. Some members expressed concern that the investment returns of EF in 2014 had continued to decline and the investment income of EF payable to the fiscal reserves placed with EF had further decreased. In particular, they noted that EF had recorded successive substantial investment losses in foreign exchange over the past five quarters, and enquired if HKMA would review the investment strategy of EF to enhance the stability of EF's investment income and avert further deterioration in the income from foreign exchange.

11. HKMA responded that it had been diversifying part of EF's investment for some years into a greater variety of asset classes housed under the Long-Term Growth Portfolio ("LTGP") and would expand the LTGP investments incrementally in a prudent manner with a view to yielding greater returns in the medium and long term. As assets in EF were held in different currencies, their investment return, when denominated in Hong Kong Dollar, would fluctuate due to cyclical movements of the US Dollar against other currencies. Taking into account the high risks associated with the unpredictable market conditions, it was considered appropriate to continue to adopt a diversified currency mix in order to even out foreign exchange losses and gains over the longer term, instead of adjusting the strategy and portfolio in response to changes in the foreign exchange market. As regards the fee payable to the fiscal reserves placed with EF, HKMA advised that the current arrangement with the Government whereby the return was calculated based on the average annual rate of return of EF's Investment Portfolio over the past six years had already taken into account the need to ensure a stable investment return for the fiscal reserves in the medium to long term.

Interest rate risks on liquidity flow and the property market

12. With the prospective rise in the Hong Kong interest rates along with normalization of the US interest rates in the near future, some members expressed concern that a potentially massive and abrupt liquidity drain from Hong Kong would soon occur. Moreover, the divergent monetary policies of major economies might cause greater volatilities in the currency markets and hence greater uncertainties in fund flows.

13. HKMA advised that the pace of US interest rate rise was still uncertain. Under the Currency Board arrangements which underpinned the Linked Exchange Rate ("LER") system, the Monetary Base of Hong Kong Dollar would expand or contract in response to capital inflow or outflow respectively. Any net inflow of funds into Hong Kong would be retained for holding high quality and short-term US Dollar-denominated debt securities with high liquidity in the Backing Portfolio of EF, which would help counteract the effects of liquidity outflow, if occurred. Besides, as it would take time for fund flows to adjust fully in response to interest rate changes, it was not expected that the anticipated liquidity drain would take place abruptly. With the LER system in place, HKMA envisaged that the exchange rate of Hong Kong Dollar against the US Dollar would remain stable in spite of currency volatilities and potential fund outflows.

14. Members expressed concern about the continuous rise in local residential property prices in spite of the demand side management measures implemented by the Government in the past few years. On the other hand, the potential interest rate rise might result in major consolidation of flat prices and adverse impacts on mortgage loan borrowers. The Panel noted that HKMA had introduced the seventh round of countercyclical prudential measures in late February 2015 on property mortgage to safeguard banking and financial stability, and to minimize the potential interest rate shock on mortgage loan borrowers. HKMA would monitor the developments and adjust its prudential supervisory measures in tandem with the property market cycles.

Resolution regime for financial institutions in Hong Kong

15. The Administration launched the second stage of public consultation in January 2015 on establishing an effective resolution regime for non-viable "too-big-to-fail" financial institutions ("FIs") in Hong Kong ("the resolution regime") to enhance the resilience of the local financial sector and meet new international standards set by the Financial Stability Board. The Panel was briefed on the details at the meeting on 2 March 2015.

16. The Panel discussed a number of issues relating to the resolution regime, including the scope of FIs captured by the regime, compliance costs,

governance arrangements and safeguards, protection of interests of employees and interface of the regime with the corporate insolvency regime. On the Administration's intention to proceed on the basis of an ex post funding model for meeting resolution costs, some members expressed concern about the potential moral hazard associated with this model, i.e. the failing FI was not required to contribute to the resolution costs upfront, but the surviving FIs were to pay the costs of resolving the failing FI. There was a view that all FIs captured by the resolution regime should duly bear their risk of failure by making contributions before a resolution. Some other members stressed the need to minimize compliance costs on FIs under the resolution regime, taking into account the cumulative compliance costs arising from the series of international regulatory reform initiatives implemented since the financial crisis in 2008.

17. The Administration advised that the resolution regime would only be used where an "in-scope" FI was assessed to be non-viable, and that its failure could pose systemic risks to the stability of the wider financial system. While the ex post funding model could give rise to moral hazard, the majority of respondents to the public consultation favoured this model as it would be inefficient to establish a fund with ex ante contributions which would not be utilized until a resolution was triggered. Moreover, there would be difficulties in determining the amount of provision from FIs in advance of a resolution as it was not possible to predict likely resolution costs in advance. Under the ex post funding arrangement, individual FIs, large or small, would need to make ex post contributions to the resolution costs of other FIs at some point in time. As regards the potential compliance costs on FIs, the Administration envisaged that the impact would be commensurate with the scale and complexity of the operations of individual FIs. The Administration would review various on-going regulatory requirements regularly and identify room for streamlining or removing those requirements where appropriate.

Securities and futures market

Budget of the Securities and Futures Commission for the financial year of 2015-2016

18. The Panel discussed the proposed budget of SFC for the 2015-2016 financial year at the meeting on 2 February 2015. Members noted with concern the continued operating deficit of SFC estimated for 2015-2016 and considered it unhealthy for SFC to continue to deploy its reserves to meet operating deficits in the long run, in particular as SFC could only adopt conservative strategies for the investment of its reserves. They urged SFC to actively consider measures to increase its income, such as imposing special levies on northbound trading under the Shanghai-Hong Kong Stock Connect ("S-HK SC"), and to reduce its recurrent expenditure by relocating some of its

non-location-bound back offices to districts of lower rentals, and/or acquiring its own office premises.

19. SFC explained that levies on securities transactions and futures and options contracts were SFC's main source of income. Following past reductions in the levy rates, the levy income indeed could not fully cover SFC's annual expenditure. Under SFC's latest assessment, SFC's reserves would be reduced in five years' time to below twice of its estimated operating expenses for a financial year. Unless there would be substantial improvement in the market turnover in future, it was likely that SFC would continue to incur annual operating deficit of some \$400 million and need to rely on its reserves to meet the funding gap. While SFC had no plan at this stage to impose levy on northbound trading under S-HK SC, it would explore related issues in the upcoming review of the implementation of S-HK SC. As the first exit option for the Cheung Kong Center office premises would be in 2017, SFC would explore various options, including whether to acquire office premises and/or to relocate all or part of its office premises to areas outside of Central.

Shanghai-Hong Kong Stock Connect

20. With the implementation of S-HK SC in November 2014, some members urged the Administration and SFC to strengthen investor education in respect of S-HK SC, particularly enhancing investors' awareness of the risks associated with trading through the system and the regulatory differences between Hong Kong and the Mainland in respect of listed entities. SFC stressed that it attached importance to investor education in the implementation of S-HK SC, and had deployed substantial resources in this area. The Investor Education Council had launched investor education programmes in respect of S-HK SC through various channels and implemented related initiatives in collaboration with the Mainland authorities.

21. Members noted the upward trend of the market turnover in southbound trading under S-HK SC and the record-high trading volumes of the Hong Kong stock market in April 2015, and expressed concerns about the associated risks on financial stability. The Administration explained that interconnection of equity markets between Hong Kong and Shanghai under S-HK SC would naturally result in greater interactions between the two markets. Changes and new dynamics in Hong Kong's equity market would emerge and market participants should understand and adapt to the new market characteristics, including greater market volatilities as a result of the stock connect and increasing fund flows between the Mainland and Hong Kong. As regards the impacts of a rallied stock market on financial stability, the Administration pointed out that SFC and HKMA would continue to be vigilant in exercising their respective regulatory roles in light of market developments, including capital flows, stock trading volumes and price volatilities, etc.

Securities and Futures (Amendment) Bill 2015

22. The Panel discussed on 13 April 2015 the legislative proposals under the prospective Securities and Futures (Amendment) Bill 2015 to allow SFC to provide supervisory assistance to regulators outside Hong Kong and to refine certain provisions in the Securities and Futures Ordinance (Cap. 571) ("SFO"). Members stressed the need to guard against collection and disclosure of excessive information and enhance the existing safeguards on information exchange with overseas regulators.

23. SFC stressed that it was mindful of the need to avoid obtaining excessive information or disclosing information without adequate safeguards, and the scope of information exchange under the Bill would be confined to providing supervisory assistance only. A number of existing safeguards, including those pertaining to legal professional privilege and privilege against self-incrimination, would be codified into SFO through the proposed legislative amendments while additional safeguards would be included, such as written statement from the requesting regulator to confirm, among others, that it had not been able and would not be able to obtain the information by any other reasonable means, and undertaking that it would not use the information in any legal proceedings unless with SFC's prior consent.

24. Members emphasized that SFC should put in place a mechanism for a licensed corporation ("LC") to appeal against SFC's decision to provide information relating to the LC requested by a regulator outside Hong Kong, similar to the existing appeal mechanism provided for exchange of tax information under the Inland Revenue Ordinance (Cap. 112). The Administration and SFC advised that in view of the narrow and confined scope of information exchangeable under the proposals, the legal safeguards in place, and overseas experiences, it was not considered necessary to provide for the suggested appeal mechanism. In fact, an appeal mechanism was also not provided for under the existing arrangements for SFC to exercise supervisory powers or provide assistance relating to enforcement-related requests from regulators outside Hong Kong. Members were unconvinced of the explanations given and strongly requested the Administration and SFC to duly consider the suggestion of providing an appeal mechanism. In response, the Administration agreed to further consider the suggestion.

First phase of implementation of the over-the-counter derivatives regulatory regime

25. The Securities and Futures (Amendment) Ordinance 2014 was enacted on 26 March 2014 to provide for a regulatory framework for the over-the-counter ("OTC") derivatives market in Hong Kong that enabled

mandatory reporting, clearing and trading of OTC derivatives transactions, and introduced a record keeping obligation to supplement the implementation of the said obligations. At the meeting on 5 January 2015, the Administration and SFC consulted the Panel on the legislative proposals for implementing the first phase of the OTC regulatory regime which would be covered in the Securities and Futures (OTC Derivative Transactions – Reporting and Record Keeping Obligations) Rules ("Reporting Rules") to be made by SFC.¹

26. The Panel discussed a number of related issues including the scope of reportable OTC derivatives transactions, reporting requirements and overseas practices, grace period for reporting and complete backloading of historical transactions, retention period of OTC derivatives transaction records, and penalties for breaches.

27. Members noted that under the legislative proposals, authorized institutions, approved money brokers and LCs which were small players in the OTC derivatives market would be exempted from reporting the transactions where they were a counterparty to (except if they had conducted transactions in Hong Kong on behalf of an affiliate), with a view to avoiding unreasonable compliance costs on market participants if they only occasionally engaged in such transactions or the impact of the transactions was relatively insignificant. On the definition of "small players", HKMA advised that under the proposals, an entity would be considered a small player if the aggregate gross notional value of its outstanding OTC derivatives transactions did not exceed US\$30 million.

28. Some members emphasized the need to avoid disclosure of confidential and sensitive particulars during the sharing of data collected by HKMA via the Hong Kong Trade Repository for regulatory and market surveillance purposes. HKMA advised that it would adhere to international standards whereby public disclosure of the data collected via trade repositories would be made in summary form according to the OTC derivatives product/transaction types without showing the particulars of individual transactions.

Development of the financial services industry in Hong Kong

Work of the Financial Services Development Council

29. The Panel received a briefing on the work progress of the Financial Services Development Council ("FSDC") at the meeting on 13 April 2015. On

¹ The Administration gazetted and tabled before LegCo in May 2015 the Securities and Futures (Amendment) Ordinance 2014 (Commencement) Notice 2015, the Securities and Futures (OTC Derivative Transactions – Reporting and Record Keeping Obligations) Rules, and the Securities and Futures (Stock Markets, Futures Markets and Clearing Houses) Notice to implement the first phase of the OTC regulatory regime.

human capital initiatives for the financial services industry, some members suggested attracting Mainland talents knowledgeable in the Mainland market or overseas talents with global perspective and familiar with international regulatory standards and practices to Hong Kong, as well as relaxing the restriction on enterprises in recruiting financial experts from the Mainland and overseas so as to meet the present gap in manpower supply in the industry. Some other members suggested FSDC consider collaborating with the Education Bureau to develop relevant curricula and programmes for training local financial experts and setting up a task force to co-ordinate the work in this area. Members also stressed the need to enhance the understanding among young people of the career opportunities in the middle and back office positions in the industry.

30. The Administration advised that it attached great importance to nurturing local talents in meeting the needs and continuous development of the Hong Kong financial market. In the 2015-2016 Budget, FS had earmarked \$100 million for running a three-year pilot scheme for the development of human capital, initially for the insurance and asset management sectors. In order to enhance graduates' understanding of the career options and prospects in the financial services industry, in particular the jobs and duties of middle and back office positions available, FSDC would continue to arrange career talks at universities to provide graduates with more information in the industry and the jobs offered as well as how they should prepare themselves for seeking jobs in the industry.

31. Members made various suggestions on the possible areas of research to be undertaken by FSDC to further promote Hong Kong as an international financial centre. The suggested areas of studies included the development of green finance in Hong Kong, the feasibility of shortening the current stock trading and settlement cycle from T+2 to T+1, and preparatory measures that Hong Kong should take to capitalize various new developments such as the establishment of Free Trade Zones in the Mainland and the establishment of the Asian Infrastructure Investment bank.

32. On members' concern about the resources arrangement and mode of operation of FSDC in the longer term, the Administration advised that the financial and manpower arrangements for FSDC would be reviewed after the first three years of its operation in year 2016. Currently, there was no plan to develop FSDC into a statutory body.

Development of the asset management industry

33. To strengthen Hong Kong's status as a premier international asset management centre and develop Hong Kong into a full-service, all-round asset management hub, FS announced in his 2013-2014 Budget the proposal to

extend the profits tax exemption for offshore funds to include transactions in private companies which were incorporated outside Hong Kong. The Administration briefed the Panel on the related legislative proposal at the meeting on 5 January 2015.

34. The Panel noted that under the existing exemption provisions for offshore funds, non-resident entities were exempt from profits tax for profits derived from "specified transactions" carried out through or arranged by a "specified person" and "transactions incidental to the carrying out of the specified transactions". However, the current definition of "securities" did not include securities of a private company. As such, the legislative proposal sought to, among others, amend the definition of "securities" such that a transaction in securities in an eligible private company (i.e. the portfolio company) would not be excluded from the scope of "specified transactions". The proposal also specified the conditions that the offshore qualified private equity funds and the portfolio companies in question had to meet in order to qualify for profits tax exemption.²

35. While some members expressed support for the proposal, some other members questioned the need and usefulness to extend the profits tax exemption for offshore funds to private equity funds, noting that even without the proposed tax exemption, the total capital under management in private equity funds in Hong Kong had achieved substantial year-on-year increases in recent years. Members also sought information on the quantifiable targets to be met by the proposal. The Administration explained that all along, there were calls from the fund industry for providing clear tax exemption to transactions conducted by offshore private equity funds in respect of eligible overseas portfolio companies, taking into account similar measures/proposals by other jurisdictions (e.g. Singapore) in the region. It was therefore considered both necessary and worthwhile to strengthen the tax incentive measures in Hong Kong with a view to expanding its fund market and enhancing competitiveness amidst regional competition. While it would be difficult to quantify the targets or benefits, the current proposal was expected to attract more private equity fund managers to hire local asset management, investment and advisory services which would be conducive to further development of Hong Kong's asset management industry. This would in turn drive demand for other relevant professional services, such as accounting and legal services.

36. Some members queried the policy considerations for imposing restrictive qualifying conditions on the portfolio companies, given that the Administration's proposal was meant to extend profits tax exemption for

² The Administration introduced the Inland Revenue (Amendment) Bill 2015 into LegCo in March 2015 to extend the profits tax exemption for offshore funds to private equity funds. A Bills Committee has been formed to scrutinize the Bill. The Administration will resume the Second Reading debate on the Bill at the Council meeting of 8 July 2015.

offshore funds to private equity funds in respect of transactions in securities in eligible overseas portfolio companies, and the exemption relief must not benefit the portfolio companies directly. Besides, portfolio companies in question were already subject to profits tax and their dividends would only be distributed after payment of the profits tax. These members urged the Administration to consider, from a wider economic perspective, relaxing the conditions and/or waiving the conditions for certain types of portfolio company (e.g. high-technology and innovative companies). There was also a suggestion to relax the requirement if the portfolio company's income derived from Hong Kong did not exceed a specified income threshold.

37. The Administration advised that the current proposal was meant to extend profits tax exemption for offshore funds to include transactions in private companies which were incorporated or registered outside Hong Kong and did not hold any Hong Kong properties nor carry out any business in Hong Kong. The proposed qualifying conditions would serve as safe harbour within which the portfolio companies in question could be accepted as having met the policy objective. The Administration further advised that an asset threshold instead of income threshold was adopted as one of the qualifying conditions after taking into account the views gathered from the fund industry and the operational needs of such companies.

Proposal to attract enterprises to establish corporate treasury centres in Hong Kong

38. At the meeting on 1 June 2015, the Administration briefed the Panel on the legislative proposal to implement the initiatives announced in the 2015-16 Budget to attract multinational and Mainland enterprises to establish corporate treasury centres ("CTCs") in Hong Kong to perform treasury services for their group companies. Specifically, the Administration proposed to amend the Inland Revenue Ordinance (Cap. 112) ("IRO") to allow, under specified conditions, interest deductions under profits tax for CTCs, and to reduce the profits tax for specified treasury activities by 50%.

39. Members supported the legislative proposal in principle in view of the anticipated benefits in generating demand for local financial and professional services sectors and contributing to the development of headquarters economy for Hong Kong. Members enquired about the number of enterprises expected to be attracted to set up CTCs in Hong Kong by the proposal and promotional work conducted by the Administration in parallel in taking forward the initiative. Some members expressed concern that the proposal might have a side effect of aggravating the shortage of grade A offices and pushing up the rentals and prices of commercial properties.

40. Members stressed the need to include provisions in the future amendment bill to ensure that only companies genuinely carrying on CTC business would be qualified for the proposed tax concessions, as well as anti-avoidance provisions to avoid abuse of the concessions. Some members cautioned that the Administration should exercise care in drafting the amendment bill to avoid making the IRO excessively complicated so as not to undermine Hong Kong's simple taxation regime.

Pilot programme to enhance talent training for the insurance sector and the asset and wealth management sector

41. At the meeting on 1 June 2015, the Administration briefed the Panel on a proposed three-year pilot programme to enhance talent training for the insurance sector and the asset and wealth management sector. The Panel noted that the financial services industry was the fastest growing economic sector in terms of manpower requirements during the period from 2012 to 2022, and there was broad consensus in the industry that manpower shortage was particularly acute in the insurance sector and the asset and wealth management sector. The proposed pilot programme would include promotion and education initiatives, internship programme for undergraduate students, and financial incentive schemes for professional training etc. for the two sectors. The Administration planned to seek approval from the Finance Committee for the proposed commitment of \$100 million for rolling out the programme in early 2016.

42. While members did not raise any objection to the proposal, some members were of the view that the industry and the two sectors in particular had the responsibility to promote public awareness of the wide range of career opportunities and prospects in their sectors and provide relevant training to enhance the competency and professionalism of the in-service practitioners. Some members also questioned the efficacy of the proposed internship programme with the internship period ranging from four to eight weeks. They noted that internship programmes in overseas countries usually last for about 10 weeks in order to allow university students to gain a better understanding of the operation of the financial services industry.

43. A member opined that there might be a mismatch in the demand and supply of manpower in the two sectors, as it was observed that quite a number of university graduates were willing to take up the front line positions in the sectors but few of them were interested in the middle and back office positions. In this regard, some members suggested that the Administration should provide university students with more information in the two sectors so that they could better prepare themselves for seeking jobs in these sectors during the undergraduate level.

Mandatory Provident Fund System

Review of the adjustment mechanism for the minimum and maximum levels of relevant income for Mandatory Provident Fund mandatory contributions

44. The Administration and the Mandatory Provident Fund Schemes Authority ("MPFA") briefed the Panel on 2 March 2015 on the review of adjustment mechanism for the minimum level of relevant income ("Min RI Level") and maximum level of relevant income ("Max RI Level") for MPF mandatory contributions, and MPFA's proposal to introduce an automatic mechanism for adjustment of the two levels ("the proposed mechanism") once every two years based on statutory benchmarks and calculation formula to replace the existing discretionary adjustment mechanism, with a review frequency of at least once every four years.

45. Members in general supported adopting 55% of Median Earnings of all employed persons as the benchmark for adjusting the Min RI Level as it would capture the income trend more closely including changes in the Statutory Minimum Wage.

46. On the benchmark for adjusting the Max RI Level based on 90th Percentile Earnings with a prescribed limit of \$5,000 for each increase, some members conveyed the serious concern of the business sector that the proposal would no longer give MPFA the flexibility to take into account other factors not explicitly set out in the legislation when determining the Max RI Level. The proposal would also result in increased MPF contributions by some employees. These members urged the Administration and MPFA to duly consult the business sector, labour unions and employees in the relevant income group on the proposed mechanism. Some other members however expressed concern that the prescribed limit of \$5,000 for each increase would "suppress" the Max RI Level resulting in a continued gap between the proposed benchmark and the Max RI Level.

47. The Administration and MPFA explained that a fully-automatic adjustment mechanism in accordance with the proposed adjustment benchmarks would ensure adjustment of both the Min and Max RI Levels be made promptly in line with economic developments without delay which might be caused by lengthy debate after each review on whether the adjustments should be implemented fully. Moreover, trustees and employers would be able to plan early for prospective adjustments as the outcomes of each review exercise would be more predictable. The Administration further pointed out that the magnitude of adjustment of the Max RI Level would depend on the data of the prevailing 90th Percentile Earnings at the time of review. While an upward adjustment, if any, of the Max RI Level would mean increased MPF contributions by some employees and their employers, there was the merit of

accumulating more retirement benefits in the longer term. As a matter of policy, it was necessary to set the Max RI Level such that the earnings of any employee or a self-employed person in excess of which would not be subject to mandatory contributions.

48. The Panel noted that the public consultation conducted by MPFA on the subject ended on 5 March 2015. Subject to the views collected, MPFA would submit a concrete proposal for amending the statutory adjustment mechanism for the Min and Max RI Levels to the Government by end of 2015.

Automatic exchange of financial account information in tax matters

49. In October 2014, the Government indicated to the Global Forum on Transparency and Exchange of Information for Tax Purposes Hong Kong's support for implementing automatic exchange of financial account information in tax matters ("AEOI") on a reciprocal basis with appropriate partners which could meet relevant requirements on protection of privacy and confidentiality of information exchanged and ensuring proper use of the data. At the meeting on 3 November 2014, the Panel was briefed on the possible legal framework to enable AEOI.

50. Members exchanged views with the Administration on issues including the benefits of AEOI and compliance costs, consistency of reporting standard for local and overseas financial institutions, and safeguards to protect privacy and confidentiality of information exchanged. Some members considered that Hong Kong should uphold its responsibility in international tax cooperation to implement AEOI, and pointed out that Hong Kong might lose its competitiveness if it did not keep in pace with the international trend of moving towards AEOI. Some other members however opined that the financial benefits for Hong Kong and its taxpayers arising from crackdown on tax evasion cases by way of AEOI would be limited given that the tax regime of Hong Kong was simple and territorial-based.

51. The Administration advised that over 90 jurisdictions, which adopted either territorial-based tax regime or global taxation had already publicly committed to the implementation of AEOI in 2017 or 2018. In view of the increasing aspirations of the international community for AEOI as a more efficient mode of international tax cooperation and a new global standard, it was necessary for Hong Kong to put in place the required legal framework for effecting AEOI. Otherwise, Hong Kong might run the risk of being labeled as an uncooperative jurisdiction or a "tax haven", which in turn would undermine its position and competitiveness as an international business and financial centre.

52. Members stressed that the Inland Revenue Department should identify AEOI partners carefully, strike a proper balance between tax transparency and protection of data privacy, and prevent fishing expedition by AEOI partners in tax information exchange. The Administration advised that AEOI involved only transmission of information pertaining to overseas tax residents who had opened an account in the financial institutions in Hong Kong to a jurisdiction, which was Hong Kong's partners of Comprehensive Avoidance of Double Taxation Agreements ("CDTA") or tax information exchange agreements ("TIEAs") and signed a Competent Authority Agreement with Hong Kong. The scope of information to be reported covered financial holders' personal data and financial data (e.g. interest, dividends, account balance/value). Similar to the safeguards available in the existing exchange of information mechanism for CDAs or TIEAs, the AEOI standard contained specific rules on the confidentiality of the information exchanged, including ensuring that the information exchanged should be foreseeably relevant. The Administration emphasized that it would identify appropriate AEOI partners which could meet relevant requirements on protection of privacy and confidentiality of information exchanged and ensuring proper use of data.

53. The Panel noted that the Administration would continue to keep close liaison with relevant stakeholders on the AEOI matter to ensure that their concerns were well addressed when drawing up the relevant legislative proposals, and would further consult Members before submitting the relevant Bill to LegCo.

Other work

54. During the 2014-2015 legislative session, the Panel also discussed with the Administration on the following subjects:

- (a) proposed revision of fees and charges for services under the Customs and Excise Department;
- (b) proposed enhancements to the Deposit Protection Scheme;
- (c) establishment proposal for staffing support to implement regulatory reforms for the insurance industry;
- (d) funding proposal on consultancy services for the proposed Joint-user Government Office Building in Cheung Sha Wan;
- (e) briefing by the Secretary for Financial Services and the Treasury on the relevant policy initiatives in the Chief Executive's 2015 Policy Address; and

(f) briefing by the Financial Reporting Council on its work in 2014.

55. From October 2014 to June 2015, the Panel held a total of eight meetings.

Council Business Division 1
Legislative Council Secretariat
18 June 2015

Legislative Council

Panel on Financial Affairs

Terms of Reference

1. To monitor and examine Government policies and issues of public concern relating to financial and finance matters.
2. To provide a forum for the exchange and dissemination of views on the above policy matters.
3. To receive briefings and to formulate views on any major legislative or financial proposals in respect of the above policy areas prior to their formal introduction to the Council or Finance Committee.
4. To monitor and examine, to the extent it considers necessary, the above policy matters referred to it by a member of the Panel or by the House Committee.
5. To make reports to the Council or to the House Committee as required by the Rules of Procedure.

**Legislative Council
Panel on Financial Affairs**

Membership list for 2014 - 2015 session

Chairman Hon CHAN Kin-por, BBS, JP

Deputy Chairman Hon Christopher CHEUNG Wah-fung, SBS, JP

Members Hon Albert HO Chun-yan
Hon James TO Kun-sun
Hon CHAN Kam-lam, SBS, JP
Hon Abraham SHEK Lai-him, GBS, JP
Hon WONG Kwok-hing, BBS, MH
Hon Jeffrey LAM Kin-fung, GBS, JP
Hon Andrew LEUNG Kwan-yuen, GBS, JP
Hon WONG Ting-kwong, SBS, JP
Hon Ronny TONG Ka-wah, SC
Hon Starry LEE Wai-king, JP
Hon Mrs Regina IP LAU Suk-ye, GBS, JP
Hon James TIEN Pei-chun, GBS, JP
Hon NG Leung-sing, SBS, JP
Hon Kenneth LEUNG
Hon Dennis KWOK
Hon SIN Chung-kai, SBS, JP

(Total : 18 members)

Clerk Ms Connie SZETO

Legal Adviser Mr YICK Wing-kin