

立法會
Legislative Council

LC Paper No. CB(1)1179/15-16
(These minutes have been seen
by the Administration)

Ref : CB1/BC/5/15/2

Bills Committee on Financial Institutions (Resolution) Bill

**Minutes of the eighth meeting on
Monday, 18 April 2016, at 2:30 pm
in Conference Room 3 of the Legislative Council Complex**

- Members present** : Hon CHAN Kam-lam, SBS, JP (Chairman)
Hon Albert HO Chun-yan
Hon Andrew LEUNG Kwan-yuen, GBS, JP
Hon WONG Ting-kwong, SBS, JP
Hon Cyd HO Sau-lan, JP
Hon CHAN Kin-por, BBS, JP
Hon NG Leung-sing, SBS, JP
Hon Kenneth LEUNG
Hon Dennis KWOK
Hon Christopher CHEUNG Wah-fung, SBS, JP
Hon SIN Chung-kai, SBS, JP
- Public officers attending** : Mr James H. LAU Jr., JP
Under Secretary for Financial Services & the Treasury
- Ms Karen Deborah KEMP, JP
Executive Director (Banking Policy)
Hong Kong Monetary Authority
- Mr Ben PLANT
Senior Manager (Banking Policy) (Resolution) 1
Hong Kong Monetary Authority

Mr PENG Si Yun, Lawrence
Senior Assistant Law Draftsman, Law Drafting
Division
Department of Justice

Mr Manuel NG
Senior Government Counsel, Law Drafting Division
Department of Justice

Mr Eugene GOYNE
Senior Director (Enforcement)
Securities and Futures Commission

Mr Tony CHAN
Ag Assistant Commissioner of Insurance (Policy and
Development)
Office of the Commissioner of Insurance

Clerk in attendance : Ms Connie SZETO
Chief Council Secretary (1)4

Staff in attendance : Mr YICK Wing-kin
Assistant Legal Adviser 8

Miss Sharon LO
Senior Council Secretary (1)9

Ms Sharon CHAN
Legislative Assistant (1)4

Action

I Meeting with the Administration

Matters arising from previous meetings

(LC Paper No. CB(1)799/15-16(01) — List of follow-up actions arising
from the discussion at the meeting
on 31 March 2016

Action

LC Paper No. CB(1)799/15-16(02) — Administration's response to issues raised at the meeting on 31 March 2016)

Clause-by-clause examination of the Bill

(LC Paper No. CB(3)165/15-16 — The Bill

LC Paper No. CB(1)381/15-16(01) — Marked-up copy of the Bill prepared by the Legal Service Division (Restricted to members only)

File Ref: B&M/2/1/27C — Legislative Council Brief

LC Paper No. LS15/15-16 — Legal Service Division Report

LC Paper No. CB(1)289/15-16(01) — Background brief on Financial Institutions (Resolution) Bill prepared by the Legislative Council Secretariat)

Discussion

The Bills Committee deliberated (Index of proceedings attached at **Appendix**).

Clause-by-clause examination of the Bill

2. The Bills Committee scrutinized clauses 74 to 100 of and Schedules 2 and 6 to the Bill.

Admin Follow-up actions to be taken by the Administration

Schedule 3 – Stamp duty exemption for securities transfer instruments

3. According to the Inland Revenue Department, any "sale or purchase" of Hong Kong stock under the securities transfer instruments (i.e. Schedule 3 to the Bill) would be subject to stamp duty under the Stamp Duty Ordinance (Cap. 117), and stamp duty exemption might be granted to the instruments on a case-by-case basis. Members were of the views that the Bill should provide certainty on stamp duty exemption for the securities transfer instruments to facilitate smooth conduct of resolution, especially for carrying out the

Action

stabilization options with transfers to a bridge institution and to a temporary public ownership company which would involve government ownership. Stamp duty exemption for the instruments would be justified recognizing the purpose of the transfers was to protect financial stability and integrity of the financial system. The Administration was requested to consider and respond to members' views.

Clauses 83 and 84 – Suspension of obligations and excluded obligations

4. Clause 83 enabled a resolution authority, in a Part 5 instrument, to suspend obligations of a within scope financial institution ("FI") to make a payment or delivery arising under a contract to which the FI or its subsidiary was a party. Clause 84 set out the excluded obligations (e.g. end of year payment and terminal payment) from a suspension under Clause 83. Members were concerned that the provisions might have effect allowing the FI to make payment for the remuneration to senior officers of the FI who had/might have contributed to the non-viability of the FI (e.g. the acts of the officers involved excessive risk taking). The Administration was requested to:

- (a) consider adding relevant provisions in the Bill to address members' concern;
- (b) provide Hong Kong Monetary Authority ("HKMA")'s guidelines to authorized institutions ("AIs") on the governance and control arrangements for AIs' remuneration systems, and explain how the guidelines could enable HKMA or an AI to defer payment of variable remuneration to the AI's senior management to address possible subsequent problems on the AI arising from misbehaviour of the AI's senior management;
- (c) clarify the coverage of the excluded obligations "end of year payment" and "terminal payment" in Clause 84(1)(c); and
- (d) consider the need to revise the terms in (c) above to better reflect the remuneration systems in the financial services industry.

Clause 95 – Appointment of appointing person

5. To decide whether any pre-resolution shareholder and pre-resolution creditor of an FI was eligible for compensation under the "no creditor worse off than in liquidation" principle, Clause 96 provided for the appointment of an independent valuer for making a valuation in relation to a failing FI. Clause 95 provided for the appointment by the Financial Secretary ("FS") of a person

Action

(i.e. the appointing person) to be responsible for appointing the independent valuer under Clause 96. Some members expressed concern about the proposal for FS to appoint an appointing person who in turn would be responsible for appointing the independent valuer. They considered that the independent valuer should be appointed by FS direct so that FS would take direct responsibility in making such appointment. The Administration was requested to:

- (a) review the relevant provisions to address members' concern; and
- (b) provide information on the appointment mechanisms for independent valuer adopted by overseas jurisdictions in their resolution regimes.

6. Clause 95(6) provided that the resignation of an appointing person would only take effect when the relevant notice was published in the Gazette. However, Clause 95(3) only required FS to publish a notice in the Gazette on the appointment of an appointing person. It was unclear when the appointment of an appointing person would take effect. The Administration was requested to:

- (a) clarify when the appointment of an appointing person would take effect;
- (b) review the relevant provisions in Clause 95 to remove the ambiguity; and
- (c) review the need of Clause 95(7) on the validity of the acts of an appointing person despite there had been defects in the appointment process.

Drafting issue

7. In the light of comments by the legal adviser to the Bills Committee, the Administration was requested to review the wording of clause 81(5) as the Chinese text "大致上相類" seemed to have different meaning from the English text "substantially similar to".

(Post-meeting note: The Administration's written responses were issued vide LC Paper Nos. CB(1)860/15-16(04) and CB(1)909/15-16(01) on 29 April and 13 May 2016 respectively.)

Action

II Any other business

Date of next meeting

8. The Chairman reminded members that the next two meetings would be held on 19 April 2016 at 10:45 am, and 3 May 2016 at 10:45 am respectively.

9. There being no other business, the meeting ended at 4:28 pm.

Council Business Division 1
Legislative Council Secretariat
26 August 2016

Proceedings of the Bills Committee on Financial Institutions (Resolution) Bill
Eighth meeting on Monday, 18 April 2016, at 2:30 pm
in Conference Room 3 of the Legislative Council Complex

Time Marker	Speaker	Subject(s)	Action Required
000705 – 000754	Chairman	Introductory remarks	
000755 – 002037	Chairman Administration Mr NG Leung-sing Mr CHAN Kin-por	<p>Briefing by the Administration on its written response to the issues arising from the meeting held on 31 March 2016 [LC Paper No. CB(1)799/15-16(02)]</p> <p>The Chairman was of the view that the Bill should set out clearly the conditions under which stamp duty exemption would be granted for the securities transfer instruments issued pursuant to the powers in the Bill as such transfers were conducted for the purpose of protecting financial stability.</p> <p>The Administration explained that —</p> <p>(a) the Stamp Duty Ordinance (Cap. 117) ("SDO") did not specify conditions for exemption of stamp duty, and exemption would be considered and granted for the securities transfer instruments on a case-by-case basis taking into account the merits of each case;</p> <p>(b) stamp duty exemption might be granted if the securities were transferred to a temporary public ownership ("TPO") company or a bridge institution ("BI"); and</p> <p>(c) when determining whether stamp duty exemption would be granted, the Inland Revenue Department would take into consideration factors such as the policy objectives, the cost effectiveness, the read-across implications, and the risk of fiscal evasion.</p> <p>The Chairman, Mr NG and Mr CHAN were of the view that the Bill should provide certainty on stamp duty exemption for the securities transfer instruments to facilitate smooth conduct of resolution and to avoid ambiguity. They pointed</p>	

Time Marker	Speaker	Subject(s)	Action Required
		<p>out that the purpose of the transfers, whether transferring to a commercial purchaser, a TPO company or BI, was to protect financial stability and the integrity of the financial system, hence equal treatment should be given to all securities transfer instruments regardless of the scale or complexity of the resolution. They added that the financial implications in terms of the government revenue forgone would be insignificant and the risk of fiscal evasion would be low, given the rare and emergency nature of resolution.</p> <p>The Administration agreed to further study the stamp duty exemption policy in the context of resolution to address members' concerns, taking into account the implications to the implementation of SDO.</p>	<p>The Administration to take action as paragraph 3 of the minutes</p>
002038 – 002748	Chairman Administration Mr Albert HO	<p>In response to Mr HO, the Administration advised that Committee Stage Amendments ("CSAs") would be introduced to remove the text in parenthesis (i.e. "(including a restriction requiring the sanction of the Court, or the approval of a regulatory body, for a transfer)") from section 4(3) of Schedule 3, section 4(3) of Schedule 4 and section 3(2) of Schedule 6. The proposed CSAs sought to clarify that there was no intention for the resolution regime to exclude the ability of any persons affected by acts of a resolution authority ("RA") to seek judicial review of those acts.</p>	
<p>Clause-by-clause examination of the Bill</p>			
002749 – 002957	Chairman Hong Kong Monetary Authority ("HKMA")	<p>Schedule 6 Bail-in Instruments</p> <p>Members did not raise any questions.</p>	
002958 – 003802	Chairman Administration HKMA Mr Albert HO Assistant Legal Adviser 8 ("ALA8")	<p><i>Subdivision 7 — Protected Arrangements</i></p> <p><u>Clause 74 – Interpretation</u></p> <p><u>Clause 75 – Regulations relating to protected arrangements</u></p>	

Time Marker	Speaker	Subject(s)	Action Required
		<p><i>Subdivision 8 — Deferral of Requirements</i></p> <p><u>Clause 76 – Deferral of requirements under Banking Ordinance</u></p> <p><u>Clause 77 – Deferral of requirements under Securities and Futures Ordinance</u></p> <p><u>Clause 78 – Deferral of requirements under section 8 of Insurance Companies Ordinance</u></p> <p>In reply to Mr HO, the Administration confirmed that applications for deferral of requirements would only be made to the Monetary Authority, the Securities and Futures Commission and the Insurance Authority.</p> <p><i>Division 2 — Power to Direct Continued Performance of Essential Services</i></p> <p><u>Clause 79 – Power to direct residual financial institution</u></p> <p><u>Clause 80 – Effect of direction under section 79</u></p> <p><u>Clause 81 – Power to direct affiliated operational entity</u></p> <p>ALA8 pointed out that the Chinese text "大致上相類" in clause 81(5) seemed to have different meaning from the English text "substantially similar to". The Administration agreed to review the wording.</p> <p><u>Clause 82 – Offences related to directions</u></p>	<p>The Administration to take action as paragraph 7 of the minutes</p>
<p>003803 – 010332</p>	<p>Chairman Administration HKMA Office of the Commissioner of Insurance ("OCI") Mr Albert HO Mr Dennis KWOK Mr SIN Chung-kai</p>	<p><i>Division 3 — Suspension of Obligations</i></p> <p><u>Clause 83 – Suspension of obligations</u></p> <p><u>Clause 84 – Excluded obligations</u></p> <p><u>Clause 85 – When obligation falls due</u></p> <p>In response to Mr HO's enquiry, HKMA said that the definition of "protected deposit" used in the Bill was the same as that used in the Deposit Protection Scheme Ordinance (Cap. 581) ("DPSO") with the definition in clause 2(1)</p>	

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		<p>making specific reference to the DPSO definition. This definition covered any deposit that was held with a DPS Scheme member, which deposit was not explicitly excluded from the definition under section 1 of Schedule 1 to DPSO, and meant the total amount of that deposit (i.e. <u>not</u> limited by the maximum protected amount under DPSO, currently \$500,000).</p> <p>Mr HO sought details regarding the excluded obligations under clause 84(1)(f). OCI advised that —</p> <ul style="list-style-type: none"> (a) the Administration was undertaking preparatory work to establish a Policyholders' Protection Fund ("PPF") to enhance protection of policyholders' interests in the event of the insolvency of an insurer; (b) PPF would focus on individual policyholders and cover both life insurance and non-life insurance; (c) a levy would be collected from the insurance industry for the establishment of PPF; and (d) obligations under a policy of insurance in respect of any claim for compensation under a scheme protected by PPF were excluded obligations under clause 84(1)(f) and as such a suspension of obligations under clause 83 could not be used to prevent payment to relevant policyholders seeking compensation from PPF. <p>Mr KWOK sought clarification on whether an RA could suspend the payment of remuneration (e.g. bonuses or executive pay) to the senior officers of a failing FI who had/might have contributed to the non-viability of the FI, and whether such payment would be regarded as employment benefits which the FI was obliged to pay (i.e. excluded obligations under clause 84). While an RA might apply to the Court for a clawback order against the officers of an FI, Mr KWOK cast doubt on the effectiveness of the clawback order as when the order was granted, the officer might have already left Hong Kong or become bankrupt, and as a result the money</p>	

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		<p>might not be traceable.</p> <p>HKMA advised that —</p> <ul style="list-style-type: none"> (a) the temporary suspension under clause 83 was intended to be a short (two business days) suspension which could temporarily suspend payment or restrict actions that could be taken against the failing FI under a contract during the crucial initial stabilization period of the FI in resolution; (b) the suspension would be imposed at the discretion of the RA with a view to meeting the resolution objectives, including to preserve continuity of critical financial services; (c) whether an FI in resolution would have a contractual obligation to pay any form of remuneration would depend upon the terms of any relevant employment contract; (d) if an officer, as defined under Part 8 of the Bill, of an FI was found to have materially contributed to the non-viability of the FI, the RA could apply to the Court for a clawback order against that officer; and (e) as a supervisory measure, HKMA had already issued a Supervisory Policy Manual ("SPM") module (designed to implement the FSB's Principles for Sound Compensation Practices and their corresponding Implementation Standards) which, amongst other things, sets out HKMA's expectation that the variable remuneration for the senior management of an authorized institution ("AI") should take into account the AI's performance over the longer term to restrain excessive short-term risk-taking. The SPM module also established that AIs should defer payment of all or part of employees' variable remuneration to more accurately reflect risk and risk outcomes. Hence AIs might withhold all or part of the variable remuneration of an officer if the payment was not justified by the performance of the FI (e.g. when the FI became, or was likely to become, non-viable 	

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		<p>in the context of the conditions for resolution under the resolution regime proposed to be established by the Bill).</p> <p>Mr KWOK and Mr HO stressed the need to empower RAs or the relevant regulators to suspend the payment of variable remuneration to the senior officers of the failing FI, in particular if the officers had/might have contributed to the non-viability of the FI (e.g. the acts of the officers were unlawful or involved excessive risk taking or misconduct). Mr KWOK also requested the Administration to provide HKMA's guidelines to AIs on the governance and control arrangements for AIs' remuneration systems, and explain how the guidelines could enable HKMA or an AI to defer payment of variable remuneration to the AI's senior management to address possible subsequent problems on the AI arising from misbehaviour of the AI's senior management.</p> <p>Mr HO requested the Administration to provide supplementary information on the coverage of the excluded obligations "end of year payment" and "terminal payment" in clause 84(1)(c).</p> <p>Mr SIN said that instead of "end of year payment", the term "variable pay", "bonus" or "performance payment" was more commonly used in the financial services industry. He requested the Administration to review the term "end of year payment" to better reflect the remuneration systems in the financial services industry.</p>	<p>The Administration to take action as paragraph 4(a) and (b) of the minutes</p> <p>The Administration to take action as paragraph 4(c) and (d) of the minutes</p>
010333 – 011253	Chairman Administration HKMA Mr SIN Chung-kai Mr Albert HO	<p><i>Division 4 – Default Event Provisions</i></p> <p><u>Clause 86 – Interpretation</u></p> <p><u>Clause 87 – Application of Division</u></p> <p><u>Clause 88 – Qualifying contracts</u></p> <p><u>Clause 89 – Events to be disregarded</u></p> <p><u>Clause 90 – Suspension of termination rights</u></p> <p><u>Clause 91 – Limitations on suspension</u></p>	

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		<p><u>Clause 92 – Rules relating to suspension of termination rights</u></p> <p><i>Division 5 — General</i></p> <p><u>Clause 93 – Functions of resolution authority</u></p> <p>In reply to Mr SIN, the Administration explained that "section 10 entity" referred to one or more entities that might be appointed by an RA under section 10 of the Bill to assist it in the performance of its functions as an RA or a lead RA under the Bill. To facilitate the orderly resolution of an FI, the securities of the FI might need to be transferred to an RA or a section 10 entity on application of the bail-in stabilization option to facilitate the write-down and conversion of the FI's liabilities and the transfer of shares to written-down debtholders.</p>	
<p>011254 – 014200</p>	<p>Chairman Administration HKMA Mr SIN Chung-kai Mr Kenneth LEUNG Mr Albert HO ALA8</p>	<p>Part 6</p> <p>Compensation</p> <p><i>Division 1 — Preliminary</i></p> <p><u>Clause 94 – Interpretation</u></p> <p><i>Division 2 — Independent Valuer</i></p> <p><u>Clause 95 – Appointment of appointing person</u></p> <p><u>Clause 96 – Appointment of independent valuer</u></p> <p><u>Clause 97 – Access to relevant information</u></p> <p>Schedule 2 Appointment Criteria for Independent Valuer</p> <p>Mr SIN asked whether it was a requirement under the Financial Stability Board ("FSB")'s "Key Attributes of Effective Regimes for Financial Institutions" ("KAs") to appoint an independent valuer for making a valuation in relation to a failing FI in order to decide if any pre-resolution creditor or pre-resolution shareholder of the FI was eligible for compensation under the "no creditor worse off</p>	

Time Marker	Speaker	Subject(s)	Action Required
		<p>than in liquidation" ("NCWOL") principle.</p> <p>The Administration and HKMA advised that the FSB's KAs only established the NCWOL principle underpinning resolution regimes. The KAs did not set standards or requirements in respect of the appointment of a valuer to perform the NCWOL valuation nor any procedures governing the valuation. The proposal in the Bill provided for a valuation process that was independent and impartial. A similar approach was adopted by the United Kingdom in its Banking Act 2009.</p> <p>Mr LEUNG asked whether there would be guidelines and procedures, including the appointment criteria, to facilitate the appointment of an independent valuer.</p> <p>The Administration said that Schedule 2 to the Bill listed out the appointment criteria which a person must meet in order to be eligible for appointment as an independent valuer. The Administration noted that the provisions provided flexibility to compile a list of persons with the relevant expertise who would be eligible to be appointed as an independent valuer in order to facilitate the making of such an appointment.</p> <p>Mr LEUNG urged the Administration to compile such a list before any resolution taken place.</p> <p>The Administration further said that it would introduce a CSA to remove section 4(c) in Schedule 2 in light of the significant practical difficulties of identifying fully, and on an ex ante basis, each and every current and former shareholder and creditor of an FI in the course of appointing an independent valuer. Absent the removal of this provision, an appointing person could effectively be restricted from identifying any suitable candidates for appointment as an independent valuer. The same change was proposed to be made to clause 37(2)(iii).</p>	

Time Marker	Speaker	Subject(s)	Action Required
		<p>Mr SIN and Mr HO expressed grave concern about the proposal for the Financial Secretary ("FS") to appoint an appointing person who in turn would be responsible for appointing the independent valuer. They considered that the independent valuer should be appointed by FS direct so that FS would take direct responsibility in making such appointment. They requested the Administration to review the relevant provisions and provide information on the appointment mechanisms for an independent valuer adopted by overseas jurisdictions in their resolution regimes.</p> <p>Mr HO sought clarification on whether the appointment of an appointing person would only take effect when the relevant notice of appointment was published by FS in the Gazette as he noted that clause 95(3) only required FS to publish a notice in the Gazette on the appointment of an appointing person whereas clause 95(6) explicitly provided that the resignation of an appointing person would only take effect when the relevant notice was published in the Gazette. He requested the Administration to review the relevant provisions in Clause 95 to remove any ambiguity.</p> <p>In reply to ALA8, the Administration clarified that the defect in the appointment of the appointing person under clause 95(7) referred to the procedural defect and such defect would not affect the acts of an appointing person. Mr HO suggested the Administration to review the need of Clause 95(7).</p> <p>The Chairman sought clarification on whether the appointing person had to report to FS after appointing the independent valuer.</p> <p>The Administration replied in the affirmative and said that FS had to approve the remuneration and allowances to be paid to the independent valuer and must cause notice of the appointment of an independent valuer to be published in the Gazette.</p>	<p>The Administration to take action as paragraph 5 of the minutes</p> <p>The Administration to take action as paragraph 6(a) and (b) of the minutes</p> <p>The Administration to take action as paragraph 6(c) of the minutes</p>

Time Marker	Speaker	Subject(s)	Action Required
014201 – 014753	Chairman Administration Mr Albert HO	<p><u>Clause 98 – Revocation of appointment of independent valuer</u></p> <p>In reply to Mr HO, the Administration advised that —</p> <p>(a) details regarding the establishment, powers, sittings, etc. of the Resolution Compensation Tribunal ("RCT") were provided in Part 7 of the Bill;</p> <p>(b) the person appointed as an independent valuer could be an assessor, accountant, forensic accountant, etc. provided they met the appointment criteria in Schedule 2; and</p> <p>(c) whether the independent valuer was guilty of serious misconduct under clause 98(1)(c) would be determined by RCT.</p>	
014754 – 015800	Chairman Administration HKMA Mr Albert HO	<p><u>Clause 99 – Appointment of new valuer</u></p> <p><u>Clause 100 – Use of information</u></p> <p>In response to Mr HO, the Administration and HKMA confirmed that —</p> <p>(a) the documents, records or accounts which needed to be provided to the independent valuer could only be used for the purpose of performing a NCWOL valuation;</p> <p>(b) the independent valuer could sub-contract individual parts of the valuation (e.g. the real estate portfolio of the FI) to other service providers (e.g. an estate surveyor) where necessary, to support an effective valuation; and</p> <p>(c) the secrecy requirements under clause 100 which applied to the independent valuer also applied to other persons who assist the independent valuer to perform his/her functions under the Bill.</p>	

Time Marker	Speaker	Subject(s)	Action Required
015801 – 015821	Chairman	Date of next meeting	

Council Business Division 1
Legislative Council Secretariat
26 August 2016