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**Bills Committee on Bank of Communications (Hong Kong) Limited
(Merger) Bill**

Background brief

Purpose

This paper provides background information on the Bank of Communications (Hong Kong) Limited (Merger) Bill which is a Member's bill introduced by Hon CHAN Chun-ying into the Legislative Council ("LegCo") in April 2017 ("the 2017 Merger Bill"). It also summarizes the major views and concerns expressed by Members when the Panel on Financial Affairs ("FA Panel") was briefed on the subject and during deliberation of the Bank of Communications (Hong Kong) Limited (Merger) Bill in 2016 which was a Member's bill introduced into LegCo by the then Hon NG Leung-sing in the Fifth LegCo ("the 2016 Merger Bill").

Background

Bank mergers in Hong Kong

2. To implement a bank merger, acquisition or transfer of business (collectively referred to as "merger") in Hong Kong, the institutions concerned must first obtain the relevant supervisory approvals of the Monetary Authority under the Banking Ordinance (Cap. 155) ("BO"). In addition, they should find a legally effective way to transfer the existing assets and liabilities to a new entity or to the institution which remains after the merger. Currently, there is no common international practice in effecting transfer of banking business. Mergers in Hong Kong involving locally-incorporated banks are normally effected by private legislation with the approval of LegCo.

Bank of Communications (Hong Kong) Limited (Merger) Bill

3. The 2017 Merger Bill is a Member's bill introduced by Hon CHAN Chun-ying with the consent of the Chief Executive.¹

4. The purpose of the 2017 Merger Bill is to provide for the transfer of the activities, assets and liabilities which constitute the retail banking business and private banking business of Bank of Communications Co., Ltd. ("BCOM") located in Hong Kong, currently operated through a branch in Hong Kong (i.e. BCOM, Hong Kong Branch) to Bank of Communications (Hong Kong) Limited ("BCOM (Hong Kong)"). BCOM (Hong Kong) is a wholly-owned subsidiary within the Bank of Communications group of companies of which BCOM is the ultimate holding company. BCOM (Hong Kong) is incorporated in Hong Kong and holds a full banking licence under BO.

5. After the proposed transfer, BCOM (Hong Kong) will carry on the retail and private banking businesses (except for a limited range of excluded property and liabilities) while BCOM, Hong Kong Branch would continue to carry on its corporate banking business and other businesses (excluding the retail and private banking businesses that are being carried out by BCOM, Hong Kong Branch on the day of the transfer).

6. The 2017 Merger Bill is substantially the same as the 2016 Merger Bill and is generally similar to previously enacted bank merger ordinances in Hong Kong. The 2016 Merger Bill received its First Reading at the LegCo meeting of 22 June 2016. A Bills Committee was formed to study the 2016 Merger Bill, and resumption of the Second Reading debate on the Bill was included in the agenda of the LegCo meeting of 13 July 2016. However, the relevant agenda item was not reached at the Council meeting and was lapsed upon the prorogation of the Fifth LegCo on 16 July 2016.

7. The 2017 Merger Bill was published in the Gazette on 21 and 28 April 2017 and received its First Reading at the LegCo meeting of 24 May 2017. The 2017 Merger Bill provides for the vesting in BCOM (Hong Kong) of the undertakings of BCOM, Hong Kong Branch on the appointed day to be decided by the directors of BCOM (Hong Kong) in consultation with the Hong Kong Monetary Authority ("HKMA"), and for other related purposes. The Bill contains a number of supplementary provisions relating to the effect

¹ The President has ruled that the Bill relates to Government policies within the meaning of Rule 51(4) of the Rules of Procedure and requires the written consent of the Chief Executive for its introduction. The Chief Executive gave consent for the Bill to be introduced into the Legislative Council by a letter dated 7 April 2017.

of the vesting in relation to trusts and wills; the accounting treatment of Bank of Communications, Hong Kong Branch; taxation arrangements; relationship with customers, borrowers, employees and other parties; mandatory provident fund scheme; evidence; interests in land and certain saving provisions.

8. The main provisions of the 2017 Merger Bill are explained in paragraph 9 of the LegCo Brief dated 28 April 2017 issued by Hon CHAN Chun-ying, and paragraphs 9 to 17 of the Legal Service Division Report on the Bill (LC Paper No. LS66/16-17). The 2017 Merger Bill, if passed, would come into operation on the day when it is published in the Gazette.

Major views and concerns expressed by Members

9. Hon CHAN Chun-ying and BCOM, Hong Kong Branch briefed FA Panel on the draft 2017 Merger Bill at the meeting on 5 December 2016. The major views and concerns expressed by Members at the FA Panel meeting on 5 December 2016 and during scrutiny of the 2016 Merger Bill are summarized in the ensuing paragraphs.

Benefits of the proposed merger

10. Noting that after the proposed business transfer, the retail and private banking businesses would be carried out by BCOM (Hong Kong), whereas the corporate banking business and other businesses would remain in BCOM, Hong Kong Branch, Members enquired how the proposed business transfer would benefit the development of the banks in the future.

11. BCOM, Hong Kong Branch pointed out that the proposed business transfer demonstrated the bank's long-term commitment to Hong Kong and its customers, employees and business partners by expanding and intensifying the retail and private banking businesses in Hong Kong in response to the growing demand for a variety of banking and financial services. The proposed business transfer was in line with the rising trend for international financial institutions to transfer their retail banking businesses to locally-incorporated subsidiaries. BCOM (Hong Kong) would be a licensed bank incorporated in Hong Kong with a corporate governance structure consisting mainly of the board of directors, board committees and senior management in accordance with requirements under BO. The governance of BCOM (Hong Kong) would be increasingly localized to interact with customers, employees and other business partners. Hence, strengthening the internal governance of the bank and enhancing the transparency of its operation.

12. Some Members expressed concern about possible difference in the regulatory standards and requirements applicable to BCOM, Hong Kong Branch and BCOM (Hong Kong), for example, in relation to securities business.

13. HKMA advised that BCOM, Hong Kong Branch and BCOM (Hong Kong) would be subject to the same regulatory requirements when engaging in securities business and/or other regulated activities as defined under the Securities and Futures Ordinance (Cap. 571). Foreign banks in Hong Kong might carry out their banking businesses in the form of a locally-incorporated subsidiary or a branch. Although BCOM, Hong Kong Branch was a non-locally incorporated bank, it was still required to comply with the capital standards promulgated by the Basel Committee on Banking Supervision at the Head Office level. HKMA would continue to co-ordinate closely with the China Banking Regulatory Commission to ensure that BCOM, Hong Kong Branch would meet the relevant regulatory standards on an on-going basis.

Vesting of undertakings in Bank of Communications (Hong Kong) Limited

Scope of banking businesses to be transferred

14. Some Members raised concern as to whether the retail banking business and private banking business to be transferred to BCOM (Hong Kong) as well as the relevant exclusions (i.e. property and liabilities to be excluded from the proposed business transfer) were clearly defined in the 2016 Merger Bill.

15. BCOM, Hong Kong Branch advised that customers were classified into retail, private, corporate or institutional customers when they opened accounts with the bank. This would form a clear basis for determining which customer accounts should be transferred. The bank would make reference to, among other things, its books and records concerned, to determine whether certain businesses were part of the retail or private banking business, etc. Besides, as set out in the relevant definitions of the 2016 Merger Bill, only those property, reserves and liabilities of BCOM, Hong Kong Branch which related in whole to private banking business, or in whole to retail banking business, or in whole to the retail banking business and private banking business, would be transferred.

Excluded property and liabilities

16. Pursuant to the definition of "excluded property and liabilities" in the 2016 Merger Bill and the draft 2017 Merger Bill, BCOM might specify, on or before the appointed day,² by a resolution or resolutions of its board of directors, or by a certificate given by an authorized person of BCOM, certain property and liabilities of the retail or private banking business of BCOM, Hong Kong Branch to be excluded from the proposed business transfer. Members expressed concern about the power conferred to BCOM for designating such exclusions. There was also concern that the power might give rise to possible loopholes for BCOM to manipulate the scope of transfer or exclusion, and undermine the certainty of whether certain customers/accounts would be transferred to BCOM (Hong Kong).

17. HKMA explained that the purpose of providing BCOM with the power to designate such exclusions was to allow flexibility for it to retain certain selected customer accounts with BCOM, Hong Kong Branch whom were considered appropriate to be retained by the Branch. Provisions of similar nature were also found in previous bank merger ordinances. BCOM, Hong Kong Branch supplemented that BCOM would exercise the said power only in very limited cases. For instance, there might be some selected customers requesting to retain their accounts with BCOM, Hong Kong Branch and whom were appropriate to be retained by the Branch. Some contracts between BCOM, Hong Kong Branch and certain counterparties (e.g. service providers) which, for the sake of clarity and to avoid uncertainty, should be clearly specified that they would not be transferred to BCOM (Hong Kong). Also, for some foreign law governed contracts, steps were required to be taken under the relevant foreign law to individually transfer the contract to BCOM (Hong Kong).

Impact on customers

Notification to existing customers about the proposed business transfer

18. Members were concerned about how BCOM, Hong Kong Branch would ensure that its existing customers, in particular the dormant account holders and account holders residing outside Hong Kong, would be duly informed of the proposed business transfer, and how the personal data of customers would be protected during the transfer process.

² The board of directors of Bank of Communications (Hong Kong) Limited ("BCOM (Hong Kong)") may determine an appointed day upon which the merger will take effect and that such appointed day must be notified by both BCOM (Hong Kong) and Bank of Communications, Hong Kong Branch in the Gazette.

19. BCOM, Hong Kong Branch advised that there would be a two-month notification period prior to the appointed day. The bank would issue letters of notification to its existing customers and set up a designated hotline to answer enquiries and provide assistance to the customers. The bank would also contact the holders of relevant dormant accounts³ and account holders residing outside Hong Kong if they did not respond to the bank within the two-month notification period. To ensure protection for the dormant account holders, a matching escrow account would be maintained by BCOM (Hong Kong) upon transferring of relevant dormant accounts from BCOM, Hong Kong Branch.

20. As regards the transfer of personal data, BCOM, Hong Kong Branch emphasized that the business transfer should not result in a breach of any duty of confidentiality or a contravention of the Personal Data (Privacy) Ordinance (Cap. 486) or the data protection principles. BCOM, Hong Kong Branch had consulted the relevant government departments and the Privacy Commissioner for Personal Data on the relevant provisions and related arrangements, and the latter had not raised any issues of concerns.

Capital base and financial soundness of Bank of Communications (Hong Kong) Limited

21. Given that BCOM, Hong Kong Branch was a branch of BCOM which was a nationwide state-owned commercial bank well established in the Mainland with a huge capital size, whereas the BCOM (Hong Kong) would only be a subsidiary of BCOM established in Hong Kong with its capital size and financial soundness yet to be established, some Members were concerned whether the proposed business transfer would have an impact on the existing customers of BCOM, Hong Kong Branch. Members also sought information on the capital base and financial soundness of BCOM (Hong Kong) in examining how far the newly established subsidiary could provide sufficient protection for customers' interests.

22. BCOM, Hong Kong Branch emphasized that all relevant contracts and agreements (including long-term contracts) made with, given to or addressed to BCOM, Hong Kong Branch with respect to the retail and private banking businesses would be transferred to BCOM (Hong Kong) upon the transfer. The rights and liabilities under these contracts and agreements would be adequately protected in accordance with law. With a more transparent mode of operation and stringent controls under Hong Kong's regulatory regime, customers' assets and interests would be better protected after the transfer.

³ Accounts which do not have any transactions within 24 months.

23. Regarding the capital adequacy of BCOM (Hong Kong), HKMA advised that the bank would be subject to the same statutory minimum capital adequacy ratio ("CAR") for locally-incorporated banks and minimum share capital level for licensed banks, which were set at 8% and \$300 million respectively. The CARs of locally-incorporated banks usually exceeded the statutory minimum level due to the need to meet other regulatory requirements under BO, and commercial considerations such as enhancing customers' confidence in the banks. When considering the banking licence application in respect of BCOM (Hong Kong), HKMA had examined the bank's business plan, and considered that it could meet the statutory minimum share capital requirement for locally-incorporated banks. BCOM (Hong Kong) had to continuously observe the regulatory requirements on capital adequacy after the granting of banking licence.

24. Upon Members' request at the FA Panel meeting on 5 December 2016, BCOM, Hong Kong Branch provided supplementary information showing the financial soundness of BCOM (Hong Kong) and information relevant to the operation of the retail and private banking businesses of BCOM (Hong Kong) in order to ensure proper protection to customers' interests during the transfer. The supplementary information is hyper-linked in the **Appendix**.

Impact on employees

25. Some Members expressed concern about the possible impacts of the proposed business transfer on existing employees of BCOM, Hong Kong Branch. They enquired if the business transfer would fully recognize the years of services of existing employees and preserve their rights and accrued benefits under their employment contracts, and whether their promotion prospects would be affected.

26. BCOM, Hong Kong Branch stressed that the terms and conditions of employment contracts with BCOM (Hong Kong) would be in line with those with BCOM, Hong Kong Branch. All relevant contracts of employment of BCOM, Hong Kong Branch would be transferred upon the business transfer and deemed for all purposes to be a single continuing employment. The accrued benefits of existing employees, including their years of services, would also be fully recognized. Following the transfer of business, BCOM, Hong Kong Branch and BCOM (Hong Kong) would continue to expand their businesses, and the relevant employees were expected to have a better career prospect after the transfer.

Views expressed by a member of the public

27. A member of the public who identified himself as a customer of BCOM, Hong Kong Branch wrote to FA Panel in January and February 2017 expressing concern that BCOM, Hong Kong Branch had not conducted public consultation nor provided details to its customers on the proposed business transfer.

28. Hon CHAN Chun-ying has sought the views of the Legal Services Division of LegCo Secretariat ("LSD") and BCOM, Hong Kong Branch on the matter. LSD pointed out that there was no requirement under the existing laws or Rules of Procedure of inviting public views in respect of bills introduced by Members. As a matter of practice, the relevant Bills Committee (if formed) would decide whether public views should be invited.

29. BCOM, Hong Kong Branch has explained in its letter to Hon CHAN Chun-ying dated 7 February 2017 that when the legislative process for the 2016 Merger Bill commenced in June 2015, BCOM had issued a formal announcement through the website of Hong Kong Exchanges and Clearing Limited informing the public of the proposed transfer of undertakings. As mentioned in paragraph 19 above, the bank would issue letters of notification to its existing customers prior to the appointed day and set up a designated hotline to answer enquiries and provide assistance to the customers. Any individual customers who do not wish to maintain accounts with BCOM (Hong Kong) will have the option of closing their accounts through normal procedures.

Latest development

30. At the House Committee meeting on 26 May 2017, Members agreed to form a Bills Committee to study the 2017 Merger Bill.

Relevant papers

31. A list of relevant papers with hyperlinks is in the **Appendix**.

List of relevant papers

Date	Event	Paper/Minutes of meeting
6 July 2015	Meeting of the Panel on Financial Affairs	Information Note (LC Paper No. CB(1)1034/14-15 (01)) Minutes (paragraphs 3-20) (LC Paper No. CB(1)1258/14-15)
16 November 2015	President's ruling on the Bank of Communications (Hong Kong) Limited (Merger) Bill intended to be introduced by Hon NG Leung-sing	President's ruling (LC Paper No. CB(3)143/15-16)
22 June 2016	Bank of Communications (Hong Kong) Limited (Merger) Bill was introduced into the Legislative Council	The Bill Legislative Council Brief Legal Service Division Report (LC Paper No. LS24/15-16)
8 July 2016	The Bills Committee on Bank of Communications (Hong Kong) Limited (Merger) Bill submitted its report to the House Committee	Report (LC Paper No. CB(1)1111/15-16)

Date	Event	Paper/Minutes of meeting
5 December 2016	Meeting of the Panel on Financial Affairs	<p>Information Note (LC Paper No. CB(1)190/16-17(02))</p> <p>Background brief (LC Paper No. CB(1)190/16-17(03))</p> <p>Minutes (paragraphs 4-17) (LC Paper No. CB(1)497/16-17)</p> <p>Supplementary information provided by Bank of Communications Co., Ltd. Hong Kong Branch (LC Paper No. CB(1)358/16-17(02))</p>
January and February 2017	Emails from a member of the public on the proposed Bank of Communications (Hong Kong) Limited (Merger) Bill	<p>Email dated 15 January 2017 (LC Paper No. CB(1)441/16-17(01)) <i>(restricted to Members, no hyperlink is provided)</i></p> <p>Email dated 1 February 2017 (LC Paper No. CB(1)545/16-17(01)) <i>(restricted to Members, no hyperlink is provided)</i></p> <p>Letter dated 18 January 2017 from Hon CHAN Chun-ying to Legal Service Division (Chinese version only) (LC Paper No CB(1)566/16-17(01))</p> <p>Reply dated 24 January 2017 from Legal Service Division to Hon CHAN Chun-ying (LC Paper No CB(1)566/16-17(02))</p> <p>Letter dated 7 February 2017 from Bank of Communications Co., Ltd. Hong Kong Branch to Hon CHAN Chun-ying (English version only) <i>(restricted to Members, no hyperlink is provided)</i> (LC Paper No CB(1)566/16-17(03))</p>

Date	Event	Paper/Minutes of meeting
24 May 2017	Bank of Communications (Hong Kong) Limited (Merger) Bill was introduced into the Legislative Council	<u>The Bill</u> <u>Legislative Council Brief</u> <u>Legal Service Division Report</u> (LC Paper No. LS66/16-17)