香港存款保障委員會
HONG KONG DEPOSIT PROTECTION BOARD

Enhancements to the Deposit Protection Scheme in Hong Kong

Consultation Conclusions

February 2024

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Executive Summary

1. On 13 July 2023, the Hong Kong Deposit Protection Board (HKDPB) issued a consultation paper [1] inviting public comments on a number of policy recommendations aimed at enhancing the Deposit Protection Scheme (DPS or the Scheme), covering (i) the protection limit; (ii) the levy system; (iii) deposit protection arrangements in the event of a bank merger; and (iv) the representation regime in respect of the display of the DPS membership sign and the negative disclosure requirements on non-protected deposits.

2. By the end of the consultation period on 12 October 2023, the HKDPB received a total of 33 written submissions from the general public, a consumer protection organisation, the banking industry and professional bodies. A list of respondents is at **Annex**.

3. In order to solicit more views from the general public, the HKDPB had also commissioned the Hong Kong Institute of Asia-Pacific Studies of the Chinese University of Hong Kong to conduct a public opinion survey on the key proposed enhancements to the DPS via telephone interview during the consultation period. Around 1,000 Hong Kong residents aged 18 years old or above and having bank accounts were randomly selected and successfully interviewed.

4. Based on the written submissions received and the findings of the public opinion survey, the respondents generally welcomed and supported the proposed enhancements to the DPS. Meanwhile, the HKDPB is aware of mixed views within the banking industry on the appropriate level of protection limit, and some Scheme members also provided comments on the implementation details of some proposals. The HKDPB has carefully considered the comments received. A summary of major comments received and the HKDPB's response are set out in Chapter 1 of this document.

5. The HKDPB would like to thank all respondents for their time and effort in reviewing the policy recommendations and providing us with their valuable comments.

6. The Panel on Financial Affairs of the Legislative Council in general supported the policy recommendations on DPS enhancements at its meeting on 30 October 2023. An amendment bill will be prepared based on the consultation conclusions as set out in Chapter 1, for submission to the Legislative Council in the next few months. The way forward is set out in Chapter 2 of this document.

[1] Consultation Paper on the Enhancements to the Deposit Protection Scheme in Hong Kong (https://www.dps.org.hk/en/download/consultation/Consultation_Paper_on_DPS_Enhancements_Eng_(final).pdf)

Chapter 1

Comments Received and Response of the HKDPB

I. Protection Limit and Target Fund Size

> Question 1:
>
> ***Do you agree with the proposal to increase the protection limit of the DPS from the current HK$500,000 to HK$800,000, at which the target size of the DPS Fund will remain at 0.25% of total protected deposits?***

Protection Limit

Major comments received

7. The findings of the public opinion survey conducted by the Hong Kong Institute of Asia-Pacific Studies of the Chinese University of Hong Kong indicated that close to 80% of survey respondents agreed with the proposed increase in the protection limit to HK$800,000. Similarly, relatively more individual submissions which commented on the protection limit agreed with increasing the protection limit to HK$800,000. Some others suggested a higher protection limit of HK$1 million, while there are also proposals for unlimited protection limit or a lower protection limit, say HK$750,000.

8. A consumer protection organisation welcomed the proposed increase of the protection limit to HK$800,000, citing that the proposed increase would more than make up for the loss in the actual degree of protection caused by inflation and would increase protection for depositors in real terms. Furthermore, it would allow more than 92% of depositors to receive full protection, above the international guidance of at least 90%. It also advised that in the long run, Hong Kong should strive for a higher protection limit and coverage level, and that future reviews need to be timely and should give extra consideration to the impact of inflation and consider ways to meet the challenge that a large proportion of total deposits remain unprotected.

9. Relevant professional bodies generally supported the proposal to raise the protection limit to HK$800,000. Specifically, they considered that the costs and benefits of raising the protection limit have been reasonably balanced at the level of HK$800,000. A respondent also agreed that the DPS represents only one piece in the jigsaw in terms of building trust and confidence in the banking system, and would suggest a more extensive review of the DPS at some point in the future to

ensure that it remains fit for purpose and takes into consideration any significant new developments in corresponding schemes elsewhere around the world.

10. Views were mixed amongst the Scheme members on the appropriate level of protection limit. Banks in support of HK$800,000 pointed out that if the protection limit were to be raised to HK$1 million, the additional effectiveness would be insignificant due to the relatively large portion of high net worth individuals in the depositor base, while at the same time this would create a more significant financial impact on banks and there might be potential cost pass-through to bank customers. Moreover, they considered it more appropriate to raise the protection limit in a prudent and progressive manner than drastically to HK$1 million to avoid any unnecessary speculation about the status of banking stability in Hong Kong. This would also leave room for further uplift in the future should circumstances so warrant. Some other banks, however, argued that banking deposits in Hong Kong have been growing at a slower pace than some other markets and that raising the protection limit by a larger extent to HK$1 million would enhance Hong Kong's attractiveness and competitive edge as a regional banking hub. They highlighted that many retail banks offering "premier" banking services for the mass affluent market adopt HK$1 million as the minimum threshold to qualify for such services, and thus recommended raising the protection limit to match that threshold. They also viewed the coverage ratio by deposit value as a more useful indicator, and noted that the ratio for Hong Kong is lower than that in some economies. Besides, they expected that the proposed protection limit of HK$800,000 would take effect in 2025 and stay until at least 2030 since the next review would only take place in five years. Given such a timeframe, they suggested increasing the protection limit to HK$1 million in one go or through a phase-in arrangement.

11. Separately, a few proposals which involve more fundamental changes to the design of the DPS were received. A respondent proposed introducing coinsurance, i.e. insuring only a fraction (say 80%) of individual deposits within the protection limit to reduce the risk of moral hazard and impart a degree of responsibility on insured depositors, while another respondent suggested offering fractional deposit insurance (say 80% protection) to individual deposits above the protection limit to better mitigate systemic risks.

The HKDPB's response

12. We are pleased to note that there is broad support amongst the general public as well as key stakeholder groups for the proposed increase of the protection limit to HK$800,000. It is understandable that some members of the public may prefer a higher or even unlimited protection limit, and some banks would also favour a higher protection limit in order to better attract affluent customers. However, we are mindful that the primary objective of the DPS is to protect small depositors and maintain their confidence in banks even in times of rumours, thereby reducing the likelihood of a rumour-driven bank run and underpinning banking stability in

Hong Kong. Moreover, capital flows into or out of a jurisdiction are affected by a host of factors such as the economic outlook, investment opportunities, the soundness of the banking system, interest rate levels, etc. While deposit protection may be one of the many factors in consideration, the DPS is indeed not designed as a tool to compete for depositors or deposit funds.

13. The protection limit of HK$800,000 is considered more appropriate at this stage because it can suitably strike a balance between enhancing protection to depositors and keeping additional costs at manageable levels. At the protection limit of HK$800,000, over 92% of depositors will be fully covered by the DPS, building in a reasonable buffer above the benchmark of 90% as recommended by the International Association of Deposit Insurers (IADI). The 60% increase in the protection limit will also more than compensate for the cumulative inflation over time, hence translating into around 20% increase in the real value of deposit protection. In terms of the costs involved, the potential loss to the DPS can still be accommodated under the current target size of the DPS Fund which is set at 0.25% of total protected deposits, so its monetary amount would only grow moderately from the existing HK$6.3 billion to HK$8.2 billion. As the costs are manageable, coupled with the aspirations of banks to maintain their competitiveness, the likelihood of such costs being passed onto bank customers should be minimised.

14. Concerning the coverage ratio by deposit value, the IADI recommends leaving a substantial amount of deposits exposed to market discipline in order to limit the risk of moral hazard, and does not specify such coverage ratio. This coverage ratio is expected to rise to over 25% in Hong Kong at the protection limit of HK$800,000. While it is comparatively lower than the corresponding ratio in some jurisdictions, it is worth noting that a protection limit of HK$800,000, by amount, is significantly higher than the prevailing levels in many other Asian economies, while comparable to those in the UK and the EU economies.[2] In fact, the structure of the depositor base plays a key role in determining this ratio. For Hong Kong, which is a small, open economy and at the same time an international financial centre and a regional asset and wealth management hub, there is a significant proportion of high net worth individuals and large corporates placing deposits in the banking system. The sheer deposit size of these customers substantially determines the coverage ratio by deposit value in Hong Kong.

15. On the alternative proposal of introducing coinsurance, we are aware that coinsurance was highlighted as one of the key reasons for the massive deposit

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Protection limit	United States	Germany	United Kingdom	Hong Kong	Canada	Japan	Mainland China	Singapore	Malaysia	South Korea
In USD terms	250,000	110,376	108,190	102,420	75,451	70,874	70,170	56,833	54,390	38,599
HK$ equivalent	1,952,750	862,150	845,070	800,000	589,350	553,600	548,100	443,925	424,838	301,500

Note: Based on exchange rates as at end-December 2023. Apart from the US and Canada which provide deposit protection on a "per account category" basis, all other jurisdictions provide deposit protection on a "per depositor per bank" basis.

withdrawals that triggered the collapse of Northern Rock in the UK during the Global Financial Crisis in 2008. Having learnt from that episode, the IADI made it clear in its Core Principles that deposit insurers should not incorporate coinsurance[3]. As regards the provision of fractional deposit insurance to deposits above the protection limit, it is in essence close to offering full deposit protection, which will not only entail a high risk of moral hazard but also impose a heavy financial burden on the banking industry which may ultimately be passed onto customers.

16. The banking stress events that happened in other parts of the world last year clearly demonstrated that bank runs and bank failures could still happen despite having very high protection limits and coverage ratios in place. This is because deposit protection is only one element of the entire financial safety net. Other important building blocks of the financial safety net, which include a robust banking supervisory framework, sound risk management by banks and an effective resolution regime, also play an important role in enhancing depositor confidence and contributing to financial stability.

17. Having regard to reasons stated in the above paragraphs, we will proceed to prepare legislative amendments to enhance the protection limit to HK$800,000. As always, we will closely monitor international developments and review the effectiveness of the DPS, including the protection limit, from time to time. Since the landscape of deposit insurance globally is expected to remain uncertain in the coming years, we fully agree with some stakeholders' comments that future reviews of the DPS should be timely. Subject to the legislative process, we aim to put the new protection limit into effect within this year and commence the next review three years after its implementation (i.e. 2027) with the target of completing the review exercise in the following year. In the next review of the protection limit, we will maintain dialogue with relevant stakeholders when considering whether there is a need to further enhance deposit protection having regard to the latest international and local developments as well as the relevant guiding principles and indicators, in order to ensure the effectiveness of the DPS in protecting depositors and maintaining banking stability in Hong Kong as intended.

[3] Core Principle 8, Essential Criteria 4.

Target Fund Size

Major comments received

18. Some Scheme members suggested that the HKDPB review the target fund size to see if a lower target fund size (for example, 0.23% of total protected deposits) would be sufficient to cover the potential loss to the DPS Fund.

The HKDPB's response

19. We had commissioned an external consultant in 2021-2022 to conduct an in-depth review of the target size of the DPS Fund to ensure that it would be sufficient to cover the potential loss[4] through-the-cycle, taking into account variations in the underlying parameters such as credit rating, asset recovery rates, protected deposit growth and so forth. This approach is in line with the recommendation of the International Monetary Fund (IMF) in its 2021 Financial Sector Assessment Program (FSAP) report on Hong Kong that the HKDPB should adopt more conservative assumptions when reviewing the target fund size. The findings of the review indicated that the potential loss to the DPS Fund could rise to close to 0.25% of total protected deposits if the protection limit is raised to HK$800,000.

20. In fact, the existing 0.25% target fund size in Hong Kong is lower than many major jurisdictions (for example, 2% in the US, 0.8% in the UK and 0.3% in Singapore). As such, we consider it appropriate to keep the existing target fund size at 0.25% of total protected deposits.

[4] Potential loss to the DPS comprises (i) shortfall loss when the DPS fails to fully recover the compensation paid to depositors from the liquidation the DPS; and (ii) financing cost (i.e. interest expense) on the borrowing from the Exchange Fund to fund the payment of compensation to depositors.

II. Levy System

Question 2:

Do you agree with the proposal to keep the levy rates unchanged while broadening the circumstances under which the build-up levy becomes chargeable again to cover the situation where the protection limit is raised regardless of whether the target fund size as a percentage of protected deposits is changed or not?

Major comments received

21. Some Scheme members expressed reservations about the proposal of switching back to the build-up levy once the protection limit is raised, mainly due to concerns about the additional financial burden on the industry. They suggested that the HKDPB consider extending the timeframe for reaching the target fund size and continue applying the expected loss levy rates, which are lower than the build-up levy rates, after the increase in protection limit to alleviate their financial burden. They also cited that the financial impact on the industry should also include other costs incurred in the implementation of proposed enhancements to the DPS, for example, the cost of system changes.

22. Meanwhile, a consumer protection organisation considered it desirable to reduce the time needed for the DPS Fund to reach the new target fund size and therefore supported the proposal to switch back to the build-up levy. It also noted that Hong Kong’s existing levy rates are lower than some other economies and there should be room to increase the levy rates.

23. Major professional bodies were also supportive of the proposal of switching back to the build-up levy to cater for a higher protection limit. In particular, a respondent pointed out that keeping the build-up levy rates unchanged provides stability and predictability for Scheme members, while broadening the circumstances under which the build-up levy becomes chargeable allows for a more flexible and adaptable funding mechanism for the DPS, which would help ensure that the DPS Fund can adequately cover the increased protection limit.

The HKDPB’s response

24. In terms of policy, we consider it justifiable to charge the build-up levy again once the protection limit is raised. After the protection limit is raised to HK$800,000, the target fund size will once again exceed the actual fund size and this calls for invoking the build-up levy to help build up the DPS Fund to reach the new target fund size. Expected loss levy, on the other hand, is not designed for the build-up phase of the target fund size. Should banks be allowed to continue paying the

lower expected loss levy rates, the time required to reach the new target fund size would be unduly prolonged to at least 10 years. A protracted build-up period would have negative implications on the credibility of the DPS and public confidence in the Scheme. In fact, the IMF had recommended in its 2021 FSAP report on Hong Kong that the flexibility of annual levies should be increased to allow the DPS Fund to reach its target fund size within a shorter timeframe.

25. With proposed switching back to the build-up levy starting from 2025, the expected loss levy to be applied in 2024[5] is only temporary. In order to assess the financial impacts of the proposed increase in the protection limit, we consider it appropriate to assume that the existing build-up levy rates remain applicable before and after the proposed increase in the protection limit. The results showed that annual contributions payable by the industry would increase by HK$153 million in total (or 26%) if the protection limit is raised to HK$800,000 from HK$500,000, while the timeframe for reaching the new target fund size should be around three years.[6]

26. It is also worthy to note that the existing build-up levy rates in Hong Kong are already among the lowest when compared to other major economies (0.0175%-0.049% in Hong Kong as compared to 0.075%-0.333% in Canada, 0.03%-0.24% in Malaysia, 0.025%-0.08% in Singapore, and 0.025%-0.42% in the US).

27. Given the above considerations, we will proceed to prepare legislative amendments to allow the HKDPB to charge the build-up levy upon an increase in the protection limit until the new target fund size is reached.

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[5] Expected loss levy is charged in 2024 because the target fund size based on the protection limit of HK$500,000 was reached last year.

[6] It should be noted that such estimates are based on the current balance sheets of banks, without taking into account future developments such as future deposit growth rates, so the actual time required for reaching the target fund size could be longer.

III. Deposit Protection Arrangements in the Event of Bank Merger

Question 3: ***Do you support the proposal to introduce enhanced arrangements for depositor protection for a limited period of time in the event of a bank merger? If so, do you agree with the proposed key features of the enhanced arrangements?***

Major comments received

28. Respondents generally supported our proposal to provide temporary enhanced protection to depositors affected by bank mergers. A consumer protection organisation also considered that the proposed six-month grace period or, for protected time deposits maturing after the end of the proposed six-month period, until their original maturity dates, are acceptable lengths of time. It also commented that the Scheme members involved in a merger or acquisition should provide timely notifications through effective channels or means to affected depositors about the enhanced coverage.

29. Some Scheme members sought clarifications on technical details, for example, the definition of the date of merger or acquisition, when the six-month grace period would commence, whether the enhanced coverage would apply in the event of an entity spin-off, and how the enhanced protection limit is determined under different scenarios. There were also enquiries on whether there would be any impact on the amount of levy due to the enhanced protection limit, and any new requirements on data retention and record keeping for Scheme members involved in a merger or acquisition.

The HKDPB's response

30. We are pleased to note the general support for this proposal. As mentioned in the consultation paper, Scheme members involved in a merger or acquisition should notify affected depositors of the enhanced protection as soon as practicable after obtaining relevant approval(s) of the merger or acquisition. Scheme members also have to ensure that the channels or means for such notifications are effective (for example, written notice, e-mail and/or SMS message).

31. Regarding the definition of the date of merger or acquisition, we understand that banks concerned would normally appoint a date on which a merger or acquisition takes effect or becomes effective (for example, the deposits and other assets/liabilities are transferred to the acquiring bank), and it is known as the date of merger or acquisition. The grace period will last for six months starting from the date of merger or acquisition. The proposed enhanced deposit protection will

also apply to the case where there is an acquisition of a Scheme member's deposit-taking business from another Scheme member due to an entity spin-off.

32. As to the basis for calculation of the enhanced protection limit, we see merits to further simplify it in order to facilitate public understanding of the arrangements. Simply put, we propose that for those depositors having existing protected deposits with two or more Scheme members involved in the merger or acquisition, each affected depositor will have an additional coverage for his or her protected deposit transferred from each merging Scheme member up to the standard protection limit for a limited period of time, on top of the standard protection limit available at the acquiring Scheme member[7]. This calculation basis is easier to understand and more similar to the existing approach adopted under the Financial Institutions (Resolution) Ordinance.

33. In relation to the determination of levy amount, our intention is to continue to calculate the amount of protected deposits and hence the levy amount based on the standard protection limit, rather than the enhanced protection limit, if any, in view that the enhanced deposit protection arrangements are only temporary.

34. The purpose of requiring Scheme members to retain relevant deposit records and information as of the date of merger or acquisition for a certain period of time is to facilitate the HKDPB to calculate the enhanced compensation amount to affected depositors in the payout in case the consolidated Scheme member fails after the merger or acquisition. We will conduct a separate industry consultation in the first half of 2024 on the retention of additional information by the relevant Scheme members for the purpose of this proposal.

35. Given the general support for the proposed enhanced protection to depositors affected by bank mergers, we will proceed to prepare legislative amendments to reflect this proposal, with refinements to the basis for calculation of the enhanced protection limit as explained above.

[7] For example, assume that Bank A merges with Bank B and all deposits in Bank A are transferred to Bank B on the date of merger, and that the standard protection limit is HK$500,000. If a depositor has HK$500,000 at Bank A and HK$500,000 at Bank B, the depositor will be entitled to a maximum compensation of HK$1 million at the consolidated Bank B (i.e. HK$500,000 at Bank A + HK$500,000 at Bank B). If another depositor has HK$200,000 at Bank A and HK$300,000 at Bank B, the depositor will be entitled to a maximum compensation of HK$700,000 at the consolidated Bank B (i.e. HK$200,000 at Bank A + HK$500,000 at Bank B).

IV. Requirements under the Representation Rules[8]

(a) Display of DPS membership sign (the Sign) on digital channels

Question 4: ***Do you support the proposal to require Scheme members to display the DPS membership sign on their digital channels in addition to their physical branches? If so, do you agree with the specific proposed arrangements?***

Requirements for the Display of the Sign

Major comments received

36. The majority of respondents agreed on the importance of displaying the Sign on the digital channels of Scheme members. In particular, a respondent considered that this proposal has several benefits, including allowing depositors to quickly identify which banks are members of the DPS and understand the level of protection available to them, and promoting transparency and clarity by making sure depositors get the same information regardless of the channel they use. The findings of the public opinion survey also indicated that around 84% of respondents agreed with the Board's proposal to require banks to display the Sign on their digital channels.

37. Scheme members raised some implementation comments about this proposal. They pointed out that the digital channels of international banks for corporate or private banking customers usually cover banking services across multiple markets, rather than solely the banking business in Hong Kong. Displaying the Sign on these channels may cause confusion to customers that their deposits placed with the overseas offices of the Scheme member are also protected by the DPS. Moreover, as not all products shown on digital channels are protected under the DPS, the display of the Sign on digital channels may cause potential confusion to customers that all products shown on the digital channels are protected. They also sought clarifications on whether the requirement would be applied to (i) digital channels not related to deposit-taking business, for example, Stored Value Facility (SVF), credit card and securities trading; and (ii) social media platforms.

The HKDPB's response

38. As it has been a global trend to deliver banking services via digital channels, more and more jurisdictions also require their scheme members to display membership

[8] The Deposit Protection Scheme (Representation on Scheme Membership and Protection of Financial Products under Scheme) Rules.

sign on their digital channels. The key objective of our proposal is to facilitate depositors to quickly identify whether a bank is a member of the DPS and the level of protection accorded to them when they visit the bank's website or mobile app, similar to when they visit the bank's physical branches. This is expected to help enhance public confidence in the banking system, which will benefit both depositors and the banking industry at large.

39. We fully agree with the views that the requirement should only apply to digital banking platforms related to Scheme members' banking business in Hong Kong. Therefore, if a Scheme member is incorporated outside Hong Kong and shares the home page of a digital banking platform with its overseas head office or other branches / affiliates, it will not be required to display the Sign on that platform so as to avoid creating confusion to customers. Besides, according to our proposal, the Sign is required to be embedded with a hyperlink to the homepage of the HKDPB's website, so customers can visit the website of the HKDPB to understand more about the DPS, for example, what types of deposits are protected and what are not. This arrangement will help provide more clarity on information about depositor protection.

40. We would also like to clarify that Scheme members will not be required to display the Sign on digital channels not related to deposit-taking activities, for example, dedicated mobile apps for SVF, credit card and securities trading, as well as social media platforms.

Display Arrangements of the Sign

Major comments received

41. Some Scheme members sought guidance from the HKDPB on the size and location of the Sign to be displayed on digital channels. They also commented that the space on mobile apps is generally more limited compared to websites to show the Sign in a reasonable size and with clarity on the page after login.

42. A consumer protection organisation was of the view that the implementation of the requirement should take into consideration the possibility of customers becoming indifferent or irritated by seeing the Sign in every single instance of logging in, hence defeating the purpose of informing customers.

The HKDPB's response

43. We note that the layout design of website and mobile app vary from bank to bank. It is therefore important to ensure that the proposed requirement is proportionate and practicable, and more flexibility should be provided to Scheme members in the implementation. Having regard to practices in some jurisdictions, we are

prepared to allow Scheme members to display the Sign on either the home page or the page immediately after customer login at each relevant digital banking platform. Scheme members also have the discretion to decide on the size and location of the Sign displayed on the relevant pages, provided that the Sign is reasonably visible to depositors visiting the platform.

(b) Negative disclosure requirements for private banking customers (PB customers)

Question 5:

Do you support the proposal to treat PB customers in the same way as institutional customers in terms of the negative disclosure requirements?

Major comments received

44. Respondents generally welcomed and supported the proposed streamlining of the negative disclosure requirement for PB customers so as to better balance consumer protection and regulatory burden. A respondent commented that this proposal will promote fairness and consistency between institutional clients and PB customers who are equally sophisticated.

45. Some Scheme members sought clarifications on implementation details, for example, the definition of "PB customers" in our context, whether a Scheme member may treat deposit products of the same nature as the same product for the purpose of the streamlined negative disclosure, and in what document the annual reminders should be contained.

46. A consumer protection organisation suggested setting an appropriate duration, for example three years, for the validity of the one-off disclosure, and requiring another disclosure to PB customers and acknowledgement from them to renew the validity after this period.

The HKDPB's response

47. We are pleased with the general support for the proposal. In terms of the operational arrangements, PB customers generally refer to customers of the private banking business of Scheme members in Hong Kong. In practice, we understand that banks would follow the relevant circulars issued by the Hong Kong Monetary Authority (HKMA) from time to time regarding the criteria for classifying a customer as a PB customer.

48. It is acceptable for Scheme members to treat deposit products of the same type / nature as the same product in their negative disclosure to PB customers under the streamlined approach, even though the individual products may entail different terms and conditions. This is similar to the existing practice for institutional customers. The same applies to annual reminders to customers.

49. Under the streamlined approach, Scheme members are required to provide annual reminders to PB customers that the products concerned are not protected by the DPS. While Scheme members have the discretion to determine in what document the reminder statement should be contained, the statement must be clearly legible enough to be brought to the attention of the customers. With the arrangement of annual reminders, it is considered not necessary to impose a validity period for the one-time disclosure for now. Nonetheless, we will continue to monitor the effectiveness of this arrangement and review from time to time whether any further refinements are needed.

V. Other comments

Broadening the Applicability of DPS

Major comments received

50. A consumer protection organisation made the following suggestions regarding the scope of the DPS:

(a) The DPS should cover not only licensed banks, but also restricted licensed banks (RLBs) and deposit-taking companies (DTCs). From a customer protection point of view, customers of the other two types of deposit-taking institutions should similarly be accorded the same kind of protection, as long as the nature of the deposits are similar to those covered by the DPS.

(b) Noting that structured deposits are not covered by the DPS and the HKDPB had set triggers for reviewing their protection status, in terms of the share of small depositors holding these deposits amongst all depositors, it would be desirable for the HKDPB to provide periodic updates on this statistic and whether it had reached the review trigger. Moreover, consumer education would be necessary to help depositors understand that structured deposits are not covered by the DPS.

(c) Out of financial stability considerations and by extension protection of financial consumers, the HKMA and the HKDPB should consider carefully what kind of financial safety net to provide to stablecoin holders in the upcoming regulatory regime for stablecoins.

(d) Given the prevalence of SVF, the HKMA and the HKDPB should keep in view ways to enhance protection for funds held in SVF. In any case, as long as the float and SVF deposits are unprotected by the DPS, related authorities should provide educational reminders to ensure consumers understand this and remind consumers to consider carefully the need to transfer funds into SVF accounts and pay close attention to the account balance.

The HKDPB's response

51. We thank the respondent for the views expressed on broadening the scope of the DPS with a view to enhancing consumer protection. Currently, both RLBs and DTCs are not members of the DPS. Due to restrictions on the amount and / or tenor of deposits they can take, ordinary retail depositors only have very limited access to these two types of institutions. Their main sources of funding are intragroup funding and corporate deposits. As of November 2023, the amount of customer deposits placed at RLBs and DTCs only made up around 0.2% of total

customer deposits in the whole banking system. We will continue to monitor the latest developments on this front and review the membership of the DPS if needed.

52. Structured deposits are more akin to investment, rather than deposits. As such, the practice in some other economies is also to exclude them from the scope of deposit insurance. In fact, the proportion of small depositors holding structured deposits in Hong Kong remains very small. As of the fourth quarter of 2021 (which is the latest statistics available), the number of small depositors holding structured deposits only accounted for 0.01% of total depositors. As such, there is no strong case for bringing structured deposits under the protection of the DPS at this stage. In the HKDPB's publicity materials, we have also made it clear that structured deposits are not protected by the DPS. To promote transparency, we will provide updated statistics regarding the holding of structured deposits among small depositors in the HKDPB's annual report in the future.

53. While stablecoins is a kind of virtual asset and purports to maintain a stable value with reference to a specified asset or a pool or basket of assets, it is not similar to deposits, and thus we do not have plans to cover them under the DPS at this stage. That said, the Government and the HKMA are conducting a public consultation on the implementation of a regulatory regime for stablecoin issuers which will, among others, impose a host of requirements on the quality and sufficiency of reserve assets held by stablecoin issuers to ensure the robustness of the stabilisation and redemption mechanisms.

54. In view of the specific character of SVF as an electronic surrogate of coins and banknotes, which is akin to a means of payment rather than a means of savings, the HKMA's regulatory regime for SVF draws a clear distinction between users' float and deposits with banks. Under the SVF regulatory regime, SVF licensees are required to put in place adequate risk management for managing the float to ensure that there will always be sufficient funds for the redemption of the stored value that remains on the facility. We note that the protection and management of float is one of the major licensing criteria and regulatory focus of the HKMA in the supervision of SVF licensees. We have also drawn the attention of the public that SVF is not covered by the DPS in our ongoing publicity and community education campaigns where applicable.

Increasing Cooperation and Information Exchange with Other Deposit Insurers

Major comments received

55. A consumer protection organisation commented that increasing cooperation and exchanging information with other deposit insurers can enable the HKDPB to provide on-the-ground information and support to members of the public who have offshore deposits and may be affected by bank closures outside Hong Kong. It can

also facilitate the HKDPB to stay abreast of latest international developments in deposit insurance.

The HKDPB's response

56. We fully agree with the comments on the importance of maintaining close cooperation and exchanging information with other deposit insurers. The HKDPB has entered into Memoranda of Understanding or other formal arrangements with several overseas deposit insurers to facilitate regular exchange of information on latest deposit insurance developments. Furthermore, the HKDPB, as a member of IADI, actively participates in conferences and events organised by IADI to exchange views on deposit insurance issues and keep up with the latest international developments in deposit insurance.

Promoting Public Awareness

Major comments received

57. A consumer protection organisation stressed the importance of promoting public awareness of the DPS and its main features, so that the public can enjoy peace of mind when depositing in banks and would not be easily swayed to make a run on the bank when there are rumours or signs of bank failures. It was pleased to note that the HKDPB had devoted much efforts to various publicity and educational initiatives, and further suggested that the HKDPB consider cooperating with banks and law enforcement agencies to carry out anti-fraud educational initiatives based on the theme of "deposit protection".

The HKDPB's response

58. We thank the respondent for recognising our efforts over the years on promoting public awareness and understanding of the DPS. We will continue our promotional and educational efforts to raise public awareness of the DPS, including the protection limit and coverage, and will explore opportunities to collaborate with relevant organisations in these initiatives.

Relaxation of Negative Disclosure Requirements for Retail Customers

Major comments received

59. Some Scheme members suggested that similar streamlined negative disclosure arrangement could also be adopted for retail customers who possess trading experience in non-protected products.

The HKDPB's response

60. We are of the view that the existing transaction-based negative disclosure regime is suitable for retail customers who are generally less sophisticated than PB customers and should therefore continue to receive an appropriate degree of protection.

Maintenance of List of Protected Deposit Products by Scheme Members

Major comments received

61. A consumer protection organisation suggested that Scheme members be required to publish and maintain a list of all protected financial products on their website. This will facilitate the clarity, transparency and understanding of the protection status of financial products for consumers.

The HKDPB's response

62. Currently, when a customer opens an account with a Scheme member for placing protected deposit, the Scheme member is required to notify the customer that the deposit is protected by the DPS. A Scheme member is also required to make a negative disclosure and obtain the customer's acknowledgement before each transaction of non-protected deposits. In addition, with the proposed requirement for Scheme members to display the Sign on their digital channels, customers may click the hyperlink embedded in the DPS logo to access the HKDPB's website and understand which types of deposits are protected by the DPS. We believe that these arrangements can help facilitate customers' understanding of the protection status of their deposits. We will monitor the effectiveness of these arrangements and review whether any further measures are needed in the future.

Enhanced Protection for Temporary High Balances

Major comments received

63. A consumer protection organisation suggested that the HKDPB consider providing time-limited enhanced protection to depositors facing life events which may result in depositors suddenly ending up with an account balance far exceeding the protection limit (e.g. inheritance and real estate transactions), so that those depositors can have time to make arrangements to maximise deposit protection such as divesting the sums in multiple banks.

The HKDPB's response

64. As explained in the consultation paper, the proposed enhanced deposit protection in the event of a bank merger or acquisition aims to align with the IADI Core Principles to strengthen the effectiveness of the DPS in maintaining banking stability. We understand that an arrangement to provide temporary enhanced protection to depositors facing life events is not specifically required by the IADI, because it is unlikely that a large group of customers would be affected at the same time which may have implications on banking stability. Nevertheless, we will keep in view international practice and market developments, and review the necessity of providing such additional protection to depositors in the future.

<u>Transition Period for Implementing the Proposed Enhancements</u>

Major comments received

65. Scheme members asked for a transition period of at least 12 months after the proposed enhancements are confirmed and the relevant guidance is available so that they can have sufficient time to implement necessary system changes and amend relevant operational procedures / disclosures.

The HKDPB's response

66. We note that there are expectations from the public for an early implementation of enhancements to the DPS. At the same time, we appreciate that Scheme members have to carry out necessary preparatory work in order to implement the enhancements, some of which may involve certain system changes. Having regard to the industry's feedback, the HKDPB plans to implement the proposed DPS enhancements in two phases. The first phase will focus on implementing the enhanced protection limit and other measures which are expected to take a shorter period of preparatory work. Subject to the legislative process, the first phase is targeted to take effect in the fourth quarter of 2024. The second phase will cover other enhancement measures and is targeted to come into force in early 2025 so as to provide more time to Scheme members for relevant preparatory work.

Chapter 2

Way Forward

67. As the next step, we will work closely with the Government on a bill to amend the DPS Ordinance and the Representation Rules. The amendment bill will reflect the final policy proposals on DPS enhancements as discussed in Chapter 1 of this document. Our target is to introduce the amendment bill into the Legislative Council in the next few months and implement the enhancements in phases between the fourth quarter of 2024 and early 2025 as elaborated in paragraph 66.

68. In parallel, we will continue to closely monitor international developments and engage with the banking industry along the way. As discussed in paragraph 17, in view of the fast evolving landscape of deposit insurance at the international level in the next few years, we plan to conduct the next review of the protection limit three years after the enhanced limit of HK$800,000 is put into effect, with the aim of completing the review exercise in the following year to ensure the DPS can keep up with international best practice.

Annex – List of Respondents

(in alphabetical order)

1. Benedict Tse
2. Billy Mok
3. Cheng Chun Fong
4. Cheung
5. Consumer Council
6. Daniel Chan
7. Dominic Tang
8. Fred
9. Ho Lok Sang
10. Ho Wai Hung
11. Hong Kong Institute of Certified Public Accountants
12. Hui Ying
13. Institute of Financial Planners of Hong Kong
14. Joyce Y. L. Li
15. Judith Rogers
16. Ms Kwok
17. Lau On Lap
18. Lee Tung Yeung
19. Leon G. Tong
20. Leung FC
21. Li Chi Kin
22. Mark Shnaidman
23. Poon Sau Hing

24. Private Wealth Management Association

25. Richard Arthur

26. So Yuk Fan

27. The Hong Kong Association of Banks

28. Timothy Wong

29. Wilkinson & Grist

30. William Leung, GBS, JP

31. 林太太

32. 傅先生

33. 劉小姐