**File Ref: B9/2/2C**

# LEGISLATIVE COUNCIL BRIEF

Deposit Protection Scheme Ordinance
(Chapter 581)

# DEPOSIT PROTECTION SCHEME (AMENDMENT) BILL 2010

## INTRODUCTION

At the meeting of the Executive Council on 30 March 2010, the Council **ADVISED** and the Chief Executive **ORDERED** that the Deposit Protection Scheme (Amendment) Bill 2010 ("the Bill"), at **Annex A**, should be introduced into the Legislative Council ("LegCo") to provide for the implementation of enhancement proposals concluded from a review of the Deposit Protection Scheme ("DPS") conducted by the Hong Kong Deposit Protection Board ("the Board") in 2009.

A

## JUSTIFICATIONS

### Enhancements of the DPS

2. In the light of relevant developments in international and local financial markets since the outbreak of the global financial crisis in 2007, and experience gained from operating the DPS since 2006, the Board completed a review of the DPS and conducted public consultations on the findings thereof by two phases in 2009.

3. The review concluded that the existing design features of the DPS in Hong Kong are already in substantial compliance with international best practices. Nevertheless, the review identified a number of enhancements to the DPS for addressing the latest developments in the international and local financial markets, in particular, for meeting heightened public expectation for better deposit protection. The major enhancement proposals concluded in the review include raising the DPS protection limit from HK$100,000 to HK$500,000, improving the clarity of the coverage of the DPS by protecting secured deposits and introducing cost mitigating measures to eliminate any potential for the cost of providing better protection being transferred to depositors.

4. After considering the costs and benefits of raising the DPS protection limit to various levels up to HK$1,000,000, and the result of the consultation on the possible options, the Board decided to raise the DPS protection limit from HK$100,000 to HK$500,000. This will bring the level of deposit protection in Hong Kong closer to those in other major markets in absolute terms, and fully cover about 90% of depositors, which is on a par with the higher end of international standards. Raising the limit to above HK$500,000 is expected to add little to effectiveness, but will bring about disproportionately higher cost and higher level of

moral hazard. To effect this enhancement, all references to HK$100,000 in the Deposit Protection Scheme Ordinance ("DPSO") (Cap. 581) will need to be changed to HK$500,000.

5. In addition to raising the DPS protection limit, the result of the consultation also supported the Board's recommendation of expanding DPS coverage to include secured deposits. This will help remove the uncertainties surrounding the protection status of a deposit being taken as a security by banks, or subject to any forms of encumbrance, for supporting the other banking and financial services provided by banks, most commonly under an integrated account. The improved clarity of the coverage of the DPS brought about by this enhancement is expected to help foster stronger confidence in the DPS. To effect this enhancement, the definition of deposit[1] in the DPSO will need to be revised by adding to it deposits subject to any security referable to the provision of any banking or financial services.

6. Raising the DPS protection limit and protecting secured deposits will increase the amount of deposits in the industry protected by the DPS ("protected deposits"). The aggregate contribution payable by members of the DPS ("Scheme members") which made up the DPS Fund is set as a percentage of the amount of protected deposits held with the members. Thus, an increase in the amount of protected deposits will in turn raise the total amount of contributions payable by Scheme members. However, it is estimated that the amount of funds required to be accumulated (in the DPS Fund) for meeting the cost of making compensation to depositors will grow at a pace slightly slower than the growth of the amount of protected deposits. The target size of the DPS Fund, though it will increase in absolute terms, will decrease slightly as a percentage of the total amount of deposits protected. It is estimated that, under the new protection limit of HK$500,000, the amount of contributions to be collected and accumulated in the DPS Fund to meet the payout expenses of the DPS will amount to HK$2.8 billion, which is equivalent to about 0.25% of the total amount of relevant deposits. Hence, we suggest that the target fund size of the DPS Fund be revised from the current 0.3% of the total amount of relevant deposits to 0.25%.

7. In order to eliminate any incentive for banks to pass the additional cost to depositors, the Board, after consulting the banking industry, proposed keeping the annual contribution payable by the industry at its current level. To achieve this objective, the Board

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Note (1) Currently, the DPSO refers to the definition of "deposit" in section 2(1) of Banking Ordinance (Cap. 155) in defining a deposit eligible for protection under the DPS. That section defines "deposit" to mean:

**"(a) a loan of money –**

**(i) at interest, at no interest or at negative interest; or**

**(ii) repayable at a premium or repayable with any consideration in money or money's worth; but**

**(b) does not include a loan of money –**

(i) upon terms involving the issue, by any company, of debentures or other securities in respect of which a prospectus has been registered under the Companies Ordinance (Cap. 32);

**(ii) upon terms referable to the provision of property or services; or**

(iii) by one company to another (neither company being an authorized institution) at a time when one is a subsidiary of the other or both are subsidiaries of another company,

and reference in this Ordinance to the taking or making of a deposit shall be construed accordingly"

According to the definition of "deposit" in the DPSO, a deposit does not include a loan of money upon terms referable to the provision of property or services.

recommended cutting the annual contribution rates of Scheme members by 65%, in the light of the estimate that the amount of relevant deposits in the industry will more than double in size after the protection limit is raised. With this proposed measure, we estimate that the DPS Fund will reach its target size by 2018. In addition, the Board recommended allowing Scheme members to report their amounts of relevant deposits for contribution assessment purposes on a net deposit basis (i.e. after deducting the liabilities of depositors to Scheme members from their relevant deposits). This is to reflect the basis on which compensation under the DPS is determined (under the DPSO, the compensation to which a depositor is entitled is calculated by deducting his liabilities from the aggregate of his protected deposits with the failed Scheme member). The aforesaid changes can be effected by adjusting the target size of the DPS Fund in terms of the percentage of the aggregate of the amount of relevant deposits maintained with the relevant Scheme members and the rates for charging annual contribution on members, and by allowing members to report relevant deposits on a net deposit basis for contribution assessment purposes in the DPSO.

8. As the Board relies heavily on subrogating into the priority claims of depositors with failed Scheme members to recover the compensation it pays to depositors, consequential amendments to the provisions on priority claims of depositors in the Companies Ordinance ("CO") (Cap. 32) will have to be made to effect the enhanced deposit protection under the DPS. Specifically, the definition of deposit and the limit on priority claims of depositors in the CO will have to be amended to link them to their counterparts in the DPSO.

**Other amendments to the DPSO**

9. Based on the experience gained from payout rehearsals and simulation tests conducted since the inception of the DPS, the Board has identified a number of enhancements to the DPSO that can help expedite the process of making compensation to depositors in a payout. To this end, the Bill will cover the following amendments -

(a) amending the proceedings of the Board to allow Board members to participate in meetings and conduct business of the Board legitimately through electronic means while they are overseas, so as to ensure that swift resolutions can be passed by the Board on time critical matters in a payout;

(b) amending the provisions relating to the calculation, limit and recovery of compensation to empower the Board to make reasonable estimations on the amount of accrued interest on complex interest-bearing products and the value of annuities and future and contingent liabilities to avoid delays in making compensation payment to depositors due to the need to perform precise calculations; and

(c) articulating the existing power of the Board to determine the amount of interim payments applicable to different depositors or different classes of depositors in order to speed up the payment of compensation to depositors.

10. In addition, the Bill provides for the making of additional rules by the Board on the representation, disclosure and acknowledgement requirements relating to deposits and other financial products, which include requiring Scheme members to make positive disclosures to confirm the protection status of a deposit to depositors, on top of the negative

disclosures on non-protected deposits already in place. The detailed disclosure rules will be made under the new powers to be introduced under this Bill and tabled for negative vetting by LegCo upon the passage of the Bill in due course.

## OTHER OPTIONS

11. The Board has consulted the public and other interested parties extensively during the review of the DPS. There is general support from the public and the parties consulted, and their comments have been taken into account where appropriate. Given the considerable benefits of enhancing the protection to depositors under the DPS and improving its operating efficiency, the Board considers it highly desirable to adopt the proposed amendments in this Bill, and putting them into legislation through amending the DPSO and CO is the only means of achieving these policy objectives.

## THE BILL

12. The proposed amendments to the DPSO and CO covered under the Bill, in general terms, provide for the enhancement of protection to depositors under the DPS and improvement in the operation of the DPS.

13. The main provisions of the Bill are as follows –

(a) **Clause 3** amends the definition of "deposit" in section 2(1) of the DPSO to expand the coverage of the DPS so that deposits subject to any security referable to the provision of any banking or financial services will be protected by the DPS;

(b) **Clause 4** amends section 27 of the DPSO to raise the limit on the total amount of compensation for each depositor under the DPS to HK$500,000 and to provide for the Board to determine the amount of accrued interests and the values of annuities and future and contingent liabilities of depositors under specified circumstances;

(c) **Clauses 5 and 7** amend sections 35 and 37 of the DPSO respectively to harmonise the maximum amount of compensation that can be paid to depositors and the amount of excessive payment that can be recovered from depositors with the expanded power of the Board to determine accrued interests and values of annuities and future and contingent liabilities under section 27 of the DPSO;

(d) **Clause 6** amends section 36 of the DPSO to articulate the Board's power to apply differential treatments to depositors when making interim payments;

(e) **Clause 9** amends section 48 of the DPSO to empower the Board to obtain information required for the assessment of contributions payable by Scheme members on a net deposit basis;

(f) **Clause 10** amends section 51 of the DPSO to empower the Board to make additional rules prescribing the representation, disclosure and acknowledgement requirements relating to protected and non-protected deposit products;

(g) **Clause 11** adds a new section 56 to the DPSO to put it beyond doubt that the increased DPS protection limit under section 27 of the DPSO will take effect only if compensation under the DPS is triggered on a day on or after the date on which the Bill commences operation;

(h) **Clause 12** amends Schedule 2 to the DPSO to allow members of the Board to conduct meetings and approve a resolution in writing through electronic means regardless of whether they are in Hong Kong;

(i) **Clause 13** amends Schedule 4 to the DPSO to allow Scheme members to report amount of relevant deposits for contribution assessment purposes after deducting liabilities owed by depositors; adjust the specified percentage for calculating the target fund size of the DPS Fund to 0.25%; and reduce the percentages for charging annual build-up levies on Scheme members by 65%; and

(j) **Section 2 of the Schedule** amends section 265 of the CO to link the limit on priority claims of depositors in a bank liquidation to the limit on amount of compensation under section 27 of the DPSO and to adopt the definitions of "deposit" and "depositor" in the DPSO.

14. The Board's tentative target is to implement the enhancements to the DPS on the start of 2011 so that the public may enjoy the benefits of an enhanced DPS when the full deposit guarantee expires by the end of 2010 (see paragraph 23 below).

## LEGISLATIVE TIMETABLE

15. The relevant legislative timetable is as follows –

| | |
|---|---|
| Publication in the Gazette | 9 April 2010 |
| First Reading and commencement of Second Reading debate | 21 April 2010 |
| Resumption of Second Reading debate, committee stage and Third Reading | to be notified |

## IMPLICATIONS OF THE PROPOSAL

16. The Bill is in conformity with the Basic Law, including the provisions concerning human rights. It has no productivity, environmental, financial, sustainability or civil service implications. The amendments proposed in the Bill will not affect the current binding effect of the DPSO.

B

17. The economic implications are set out at **Annex B**.

## PUBLIC CONSULTATION

18. The Board has conducted extensive public consultations on the enhancement proposals in two phases, in April - June and August - October 2009. It has proactively approached interested parties for comments, including industry associations[2], statutory advisory committees[3], Consumer Council, Standing Committee on Company Law Reform, Hong Kong Institute of Certified Public Accountants, Law Society of Hong Kong and Hong Kong Bar Association. The Board also gathered public responses to the key proposals during its regular opinion surveys on public attitude towards the DPS. The comments collected in the consultations together with the Board's responses to them have been published on its website. Generally speaking, the results of the consultations and the findings of the opinion surveys indicated that the enhancement proposals identified in the review received broad support from the public and the interested parties. The Board has taken into account the comments collected in finalising the Bill, for example, the reduction of the annual contribution rates required for keeping annual contribution of Scheme members unchanged at the current level.

19. The Board briefed the LegCo Panel on Financial Affairs on the enhancement proposals identified in the first phase of the review on 1 June 2009, and the results of the second phase of the review and the legislative plan for taking forward the enhancement proposals on 1 February 2010. Members of the Panel were supportive of the proposed amendments and requested that the Bill be introduced into LegCo as soon as possible.

## PUBLICITY

20. We will issue a press release upon the gazettal of the Bill on 9 April 2010. We will also arrange a spokesman to answer media and public enquiries.

## BACKGROUND

21. The DPSO was enacted in May 2004. It provides for the establishment of the DPS in Hong Kong with a compensation limit of HK$100,000 per depositor per bank. The DPS Fund with a target fund size of 0.3% of the total amount of relevant deposits is being built up through the collection of contributions from Scheme members. As at end March 2009, the DPS Fund (expressed in terms of assets) totaled HK$963 million, representing about 0.18% of the relevant deposits.

22. The Board was formed in July 2004 to establish and administer the DPS. The DPS has started providing deposit protection since September 2006.

23. On 14 October 2008, the Government announced the use of the Exchange Fund to guarantee repayment of all customer deposits held with authorized institutions in Hong Kong

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Notes [2] These include The Hong Kong Association of Banks and The DTC Association (The Hong Kong Association of Restricted Licence Banks and Deposit-taking Companies).

[3] These include the Banking Advisory Committee and the Deposit-taking Companies Advisory Committee.

following the principles of the DPS. The guarantee took immediate effect and will remain in force until the end of 2010.

**ENQUIRIES**

24. For any enquiries relating to the brief, please contact Miss Natalie Li, Principal Assistant Secretary for Financial Services and the Treasury (Financial Services) at 2529 0121, or Mr Colin Pou, Head (Deposit Protection Scheme), Hong Kong Monetary Authority at 2878 1903.

**Financial Services and the Treasury Bureau**
**7 April 2010**

**Annex A**

# DEPOSIT PROTECTION SCHEME (AMENDMENT) BILL 2010

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# A BILL

To

Amend the Deposit Protection Scheme Ordinance to increase the protection for depositors under the Deposit Protection Scheme; to reduce the additional annual costs incurred by Scheme members as a result of the increased protection; to facilitate the calculation and payment of compensation under the Scheme; to adjust accordingly the rights and remedies to which the Hong Kong Deposit Protection Board may be subrogated if it makes a payment of compensation; to allow meetings and other business of the Board to be conducted by electronic means; to confer additional rule-making powers on the Board; and to provide for consequential and related matters.

Enacted by the Legislative Council.

## PART 1

## PRELIMINARY

**1. Short title**

This Ordinance may be cited as the Deposit Protection Scheme (Amendment) Ordinance 2010.

**2. Commencement**

(1) Subject to subsections (2) and (3), this Ordinance comes into operation on 1 January 2011.

(2) Sections 3, 9 and 13 come into operation on 20 October 2010 for the purpose only of submitting returns and reports under section 48(2) and (3) of the Deposit Protection Scheme Ordinance (Cap. 581) to enable calculations to be made under Schedule 4 to that Ordinance for the year of 2011.

(3) Section 10 comes into operation on the day on which this Ordinance is published in the Gazette.

# PART 2

## AMENDMENTS TO DEPOSIT PROTECTION SCHEME ORDINANCE

**3. Section 2 amended (Interpretation)**

Section 2(1) of the Deposit Protection Scheme Ordinance (Cap. 581) is amended, in the definition of "deposit", by repealing everything after "to it" and substituting "in the definition of "deposit" in section 2(1) of the Banking Ordinance (Cap. 155) except that, despite paragraph (*b*)(ii) of that definition, it includes a loan of money referred to in paragraph (*a*) of that definition that is subject to any security (including any form of encumbrance, charge, mortgage, pledge, lien and right of set off) referable to the provision of any banking or financial services;".

**4. Section 27 amended (Entitlement to compensation: general)**

(1) Section 27(1) is amended by repealing "$100,000" and substituting "$500,000".

(2) Section 27(2) is amended by repealing "$100,000" and substituting "$500,000".

(3) Section 27(4)(*a*) is amended by repealing "and" at the end.

(4) Section 27(4)(*b*) is amended –

(*a*) by adding ", subject to paragraph (*c*)," before "with regard to the valuation";

(*b*) by repealing the full stop and substituting a semicolon.

(5) Section 27(4) is amended by adding –

"(*c*) the Board may determine the value of annuities and future and contingent liabilities by making an estimate that is reasonable and appropriate in the circumstances of the case if the Board considers that –

(i) there is uncertainty as to the value of the annuities and future and contingent liabilities;

(ii) the time required to ascertain the value of the annuities and future and contingent liabilities would be so long as to unduly delay the payment of compensation to the person entitled to the compensation; or

(iii) the costs and expenses that would be incurred in the calculation made to ascertain the value of the annuities and future and contingent liabilities would, having regard to the likely difference between the ascertained value and the estimated value of the annuities and future and contingent liabilities, outweigh the benefits of making the calculation; and

(*d*) the Board may determine the amount of interest accrued on deposits, or liabilities, by making an estimate that is reasonable and appropriate in the circumstances of the case if the Board considers that –

(i) there is uncertainty as to the entire amount of interest so accrued;

(ii) the time required to ascertain the entire amount of interest so accrued would be so long as to unduly delay the payment of compensation to the person entitled to the compensation; or

(iii) the costs and expenses that would be incurred in the calculation made to ascertain the entire amount of interest so accrued would, having regard to the likely difference between the ascertained amount and the estimated amount of the interest, outweigh the benefits of making the calculation.".

**5. Section 35 substituted**

Section 35 is repealed and the following substituted –

"**35. Maximum amount of compensation payable to a depositor**

The amount of compensation payable to a depositor of a failed Scheme member in accordance with this Ordinance is not to exceed –

(*a*) the amount in respect of which the depositor would, on the winding up of the failed Scheme member, be entitled to priority under section 265(1)(*db*) of the Companies Ordinance (Cap. 32); or

(*b*) where an estimate has been made under section 27(4)(*c*) or (*d*) as a result of which the specified amount of compensation to which the depositor is entitled as referred to in section 27(1) or (2) is greater than the amount referred to in paragraph (*a*), that specified amount subject to the limit prescribed in section 27(1) or (2).".

**6. Section 36 amended (Interim payment)**

(1) Section 36 is amended by renumbering it as section 36(1).

(2) Section 36 is amended by adding –

"(2) The Board may, under subsection (1), make interim payments of different amounts to different depositors, or different classes of depositors, as the Board considers appropriate.".

**7. Section 37 amended (Recovery of payment by Board)**

Section 37 is amended by adding –

"(5) For the purposes of subsection (1), a reference to the amount of compensation payable to the depositor in accordance with this Ordinance does not include, where an estimate has been made under section 27(4)(*c*) or (*d*)

as a result of which the amount of compensation paid to the depositor ("the paid amount") is greater than the amount of compensation that would have been paid to the depositor if the estimate had not been made ("the entitled amount"), the difference between the paid amount and the entitled amount.".

**8. Section 38 amended (Subrogation)**

Section 38(6)(*a*) is amended by repealing "$100,000" and substituting "$500,000".

**9. Section 48 amended (Power of Board to obtain information)**

Section 48(2) is amended by repealing everything after ", returns" and substituting –

"showing –

(*a*) the amount of relevant deposits, within the meaning of section 1 of Schedule 4, maintained with the Scheme member;

(*b*) the amount of relevant liabilities, within the meaning of section 1 of Schedule 4, owed by depositors to the Scheme member (if any); and

(*c*) the breakdown of those relevant deposits and liabilities (if any).".

**10. Section 51 amended (Power of Board to make rules)**

(1) Section 51(1)(*d*) is repealed and the following substituted –

"(*d*) requiring a Scheme member to make known to the public under specified circumstances that it is a member of the Scheme or will cease to be a member of the Scheme, and prescribing the manner in which the requirement is to be complied with;".

(2) Section 51(1) is amended by adding –

"(*da*) requiring a Scheme member –

(i) to make known to the public under specified circumstances as to whether a deposit or any other financial product offered by the Scheme member is or is not a protected deposit; or

(ii) to obtain under specified circumstances an acknowledgment from any person placing or holding a deposit with, or investing in or holding any other financial product offered by, the Scheme member of having received a notification from the Scheme member as to whether the deposit or financial product is or is not a protected deposit,

and prescribing the manner in which the requirement is to be complied with;".

(3) Section 51(1) is amended by adding –

"(*db*) imposing restrictions on Scheme members relating to the descriptions or representations of any financial product as a deposit or a specified kind of deposit;".

**11. Section 56 added**

The following is added –

"**56. Transitional provisions in relation to Deposit Protection Scheme (Amendment) Ordinance 2010**

(1) The amendments made to this Ordinance by the Deposit Protection Scheme (Amendment) Ordinance 2010 ( of 2010) ("the amending Ordinance") do not apply if a specified event within the meaning of section 22(1) has occurred before the commencement of section 4 of the amending Ordinance, in which case the limit on the total amount of compensation to which a depositor may be entitled is the limit prescribed in

section 27 before it is amended by that section 4 even though the payment of compensation is made after the commencement of that section 4.

(2) Rules made under section 51(1)(*da*) as added by section 10(2) of the amending Ordinance –

(*a*) may provide that any requirement imposed by those rules applies in relation to a deposit or any other financial product that is in existence at the commencement of those rules; and

(*b*) may prescribe the manner in which the requirement in relation to the deposit or financial product is to be complied with.

(3) Rules made under section 51(1)(*db*) as added by section 10(3) of the amending Ordinance may provide that those rules, in so far as they relate to the imposition of restrictions on Scheme members relating to the descriptions or representations of any financial product as a structured deposit, do not have effect in relation to any financial product that was being described or represented as a structured deposit immediately before the commencement of those rules.".

**12. Schedule 2 amended (Provisions relating to Board)**

(1) Section 2(4) of Schedule 2 is amended –

(*a*) by repealing "absent from Hong Kong or is for any other reason" and substituting ", due to absence from Hong Kong or for any other reason,";

(*b*) by repealing "absence or".

(2) Section 2(5) of Schedule 2 is amended –

(*a*) by repealing ", other than the Chairman, is absent from Hong Kong or is for any other reason" and substituting "(other than the Chairman) is, due to absence from Hong Kong or for any other reason,";

(*b*) by repealing "absence or".

(3) Section 5(1) of Schedule 2 is amended by adding ", and in such manner (including by electronic means)," after "times and places".

(4) Section 5(2) of Schedule 2 is amended by repealing "meetings of the Board is 4" and substituting "a meeting of the Board is 4 members present at the meeting".

(5) Section 5 of Schedule 2 is amended by adding –

"(5) A member of the Board is to be regarded as being present at a meeting of the Board, even though the member does not attend the meeting in person, if –

(*a*) the member participates in the meeting by telephone, video conferencing or other electronic means; and

(*b*) the member is able to communicate with the other members attending or present at the meeting and they are able to communicate with that member.

(6) A member who participates in a meeting of the Board by telephone, video conferencing or other electronic means may cast a vote by the same electronic means.

(7) Subsection (4)(*a*) and (*c*) applies even though the Chairman of the Board participates in the meeting by telephone, video conferencing or other electronic means.".

(6) Section 6 of Schedule 2 is repealed and the following substituted –

"6. **Transaction of business by circulation of papers**

(1) The Board may transact any of its business by circulation of papers.

(2) A resolution in writing which is approved in writing by a majority of the members of the Board is as valid and effectual as

if it had been duly passed at a meeting of the Board by the votes of the members of the Board so approving the resolution.

(3) A facsimile or an electronically transmitted document that bears the signature of a member of the Board is to be regarded as having been approved in writing by that member.

(4) To avoid doubt, a reference to circulation of papers in this section includes circulation of information by electronic means.".

**13. Schedule 4 amended (Contributions to Fund)**

(1) Schedule 4 is amended by repealing "[ss. 2, 15 & 54]" and substituting "[ss. 2, 15, 48 & 54]".

(2) Section 1(1) of Schedule 4 is amended by repealing the definition of "amount of relevant deposits" and substituting –

""amount of relevant deposits" (有關存款款額), in relation to a Scheme member, means, subject to subsection (2), the aggregate amount held by all depositors of the Scheme member, being the sum arrived at by adding up any of the following amounts held by each of the depositors of the Scheme member –

(*a*) the amount by which the amount of all relevant deposits held by one person, as a depositor, with the Scheme member in that person's own right exceeds the amount of relevant liabilities owed by the person to the Scheme member (if any), up to a limit of $500,000;

(*b*) the amount by which the amount of all relevant deposits held by a depositor, as a bare trustee under one bare trust, with the Scheme member exceeds the amount of

relevant liabilities owed by the depositor, as the bare trustee under that bare trust, to the Scheme member (if any), up to a limit of $500,000;

(*c*) the amount by which the amount of all relevant deposits held by a depositor with the Scheme member in one client account exceeds the amount of relevant liabilities owed by the depositor to the Scheme member under that client account (if any), up to a limit of $500,000; or

(*d*) the amount by which the amount of all relevant deposits held by a depositor, as a trustee under one trust, with the Scheme member exceeds the amount of relevant liabilities owed by the depositor, as the trustee under that trust, to the Scheme member (if any), up to a limit of $500,000;".

(3) Section 1(2) of Schedule 4 is repealed and the following substituted –

"(2) In the definition of "amount of relevant deposits" –

(*a*) a reference to a relevant deposit –

(i) includes a portion of the deposit; and

(ii) does not include any interest accrued on the deposit;

(*b*) for the purposes of paragraph (*a*) of that definition, if a relevant deposit is held by a depositor consisting of 2 or more persons –

(i) subject to subparagraph (ii), each of the 2 or more persons is deemed to have an equal share in the deposit

unless the contrary is proved to the satisfaction of the Board; and

(ii) if the 2 or more persons carry on business in partnership, those persons are a single and continuing body of persons as distinct from the persons who may from time to time be the members of the partnership;

(*c*) for the purposes of paragraphs (*b*) and (*d*) of that definition, if a relevant deposit is held by a depositor consisting of 2 or more persons, those persons are a single and continuing body of persons as distinct from the persons who may from time to time be the bare trustees or trustees;

(*d*) a reference to the amount of relevant liabilities owed by a depositor to a Scheme member is any amount the Scheme member may specify, being an amount within the range of 0% to 100% of the liabilities, other than future or contingent liabilities, owed by the depositor to the Scheme member ("relevant liabilities"), but does not include any interest accrued on the relevant liabilities;

(*e*) for the purposes of paragraph (*a*) of that definition, if a relevant liability owed by a person (being a depositor, or being one of the persons whom a depositor consists of) to a Scheme member forms part of a liability

owed by 2 or more persons to the Scheme member –

(i) subject to subparagraph (ii), each of the 2 or more persons is deemed to have an equal share in the liability unless the contrary is proved to the satisfaction of the Board; and

(ii) if the 2 or more persons carry on business in partnership, those persons are a single and continuing body of persons as distinct from the persons who may from time to time be the members of the partnership; and

(*f*) for the purposes of paragraphs (*b*) and (*d*) of that definition, if a relevant liability is owed by a depositor, consisting of 2 or more persons, to a Scheme member, those persons are a single and continuing body of persons as distinct from the persons who may from time to time be the bare trustees or trustees.".

(4) Section 2(3) of Schedule 4 is amended by repealing "0.3%" and substituting "0.25%".

(5) Section 3(5) of Schedule 4 is amended, in column 2 of the Table –

(*a*) by repealing "0.05%" and substituting "0.0175%";

(*b*) by repealing "0.08%" and substituting "0.028%";

(*c*) by repealing "0.11%" and substituting "0.0385%";

(*d*) by repealing "0.14%" and substituting "0.049%".

# PART 3

## CONSEQUENTIAL AND RELATED AMENDMENTS

**14. Consequential and related amendments**

The enactments specified in the Schedule are amended as set out in that Schedule.

## SCHEDULE [s. 14]

## CONSEQUENTIAL AND RELATED AMENDMENTS

### Companies Ordinance

1. **Section 227E amended (Proof of debts)**

(1) Section 227E(1) of the Companies Ordinance (Cap. 32) is amended, in the Chinese text, by repealing "存戶" and substituting "存款人".

(2) Section 227E is amended by adding –

"(4) In subsection (1), the expressions "deposit" (存款) and "depositor" (存款人) have the same meaning as in section 265(6).".

2. **Section 265 amended (Preferential payments)**

(1) Section 265(1)(*db*)(i) is amended by repealing "$100,000" and substituting "the limit on the total amount of compensation to which a depositor is entitled as prescribed in section 27(1) of the Deposit Protection Scheme Ordinance (Cap. 581)".

(2) Section 265(1)(*db*)(ii) is amended by repealing "$100,000" and substituting "the limit on the total amount of compensation to which a depositor is entitled as prescribed in section 27(1) of the Deposit Protection Scheme Ordinance (Cap. 581)".

(3) Section 265(1)(*db*)(iii) is amended by repealing "$100,000" and substituting "the limit on the total amount of compensation to which a depositor is

entitled as prescribed in section 27(1) of the Deposit Protection Scheme Ordinance (Cap. 581)".

(4) Section 265(1)(*db*)(iv) is amended by repealing "$100,000" and substituting "the limit on the total amount of compensation to which a depositor is entitled as prescribed in section 27(2) of the Deposit Protection Scheme Ordinance (Cap. 581)".

(5) Section 265(5J)(*b*) is amended by repealing "$100,000" and substituting "the limit on the total amount of compensation to which a person is entitled as prescribed in section 27(1) of the Deposit Protection Scheme Ordinance (Cap. 581)".

(6) Section 265(5J) is amended by repealing "be $100,000." and substituting "be that limit prescribed in section 27(1) of the Deposit Protection Scheme Ordinance (Cap. 581).".

(7) Section 265(6) is amended, in the definition of "deposit" and "depositor", by repealing "Banking Ordinance (Cap. 155)" and substituting "Deposit Protection Scheme Ordinance (Cap. 581)".

(8) Section 265 is amended by adding –

"(11) The Schedule to the Deposit Protection Scheme (Amendment) Ordinance 2010 ( of 2010) applies in the case of a winding up where the relevant date occurred before the commencement of that Schedule but the specified event within the meaning of section 22(1) of the Deposit Protection Scheme Ordinance (Cap. 581) occurs on or after the commencement of that Schedule.".

## Explanatory Memorandum

The main object of this Bill is to amend the Deposit Protection Scheme Ordinance (Cap. 581) ("the Ordinance") to increase the protection for depositors under the Deposit Protection Scheme ("the Scheme").

**Part 1 – Preliminary**

2. Clauses 1 and 2 provide respectively for the short title and the commencement of the Bill when enacted.

**Part 2 – Amendments to Deposit Protection Scheme Ordinance**

3. Clause 3 seeks to expand the product coverage of the Scheme. It amends the definition of "deposit" in section 2(1) of the Ordinance to include a loan of money subject to any security referable to the provision of any banking or financial services, so that those secured deposits will be protected under the Scheme.

4. On the other hand, clause 4 provides for a higher protection limit under the Scheme. It amends section 27 of the Ordinance to raise the limit on the total amount of compensation to which a depositor is entitled under the Scheme from $100,000 to $500,000. Correspondingly, clause 8 amends section 38 of the Ordinance so that the right to which the Hong Kong Deposit Protection Board ("the Board") may subrogate upon making a payment of compensation to a depositor, in so far as it relates to the interest accrued on the payment, is to be determined on the basis of this new protection limit of $500,000.

5. Under the amended section 27 of the Ordinance, the Board may also determine the value of annuities and future and contingent liabilities, and may determine the amount of interest accrued on deposits or liabilities, by making an estimate in certain circumstances (for instance, to avoid undue delay in the payment of compensation to a depositor).

6. Clause 5 replaces section 35 of the Ordinance by a new provision, accordingly, which seeks to adjust the maximum amount of compensation that may be paid to a depositor in the case that an estimate has been made by the Board to determine the value of annuities and future and contingent liabilities, or the amount of interest accrued on deposits or liabilities, for the purpose of calculating the amount of compensation payable to the depositor. Clause 7 then amends section 37 of the Ordinance to enable the Board to recover from a

depositor any amount paid in excess to the depositor because of an over-estimation of the amount of compensation to which the depositor is entitled.

7. Clause 6 amends section 36 of the Ordinance to make it clear that the Board may make different amounts of interim payments to different depositors or different classes of depositors.

8. Clause 13 seeks to reduce the additional annual costs incurred by Scheme members as a result of the increased protection under the Scheme by –

(*a*) amending section 1 of Schedule 4 to the Ordinance to allow any amount of the relevant liabilities owed by a depositor to a Scheme member to be deducted from that depositor's relevant deposits (but the net amount for each depositor is not to exceed $500,000) in calculating, for the purposes of contributions assessment under that Schedule, the aggregate amount of relevant deposits maintained with that Scheme member;

(*b*) amending section 2 of Schedule 4 to the Ordinance to lower the specified percentage, from 0.3% to 0.25%, for calculating the target fund size of the Deposit Protection Scheme Fund; and

(*c*) amending section 3 of Schedule 4 to the Ordinance to reduce the percentages specified for calculating the build-up levies payable by Scheme members each year.

9. Clause 9 amends section 48 of the Ordinance to empower the Board to require Scheme members to submit returns showing the amounts of relevant deposits maintained with and relevant liabilities owed to those members and the breakdown of those amounts.

10. Besides, clause 10 amends section 51 of the Ordinance to provide further powers for the Board to make rules concerning the notifications and the acknowledgments of notifications as to whether a deposit or any other financial product is or is not protected under the Scheme, and also to make rules

concerning the restrictions on describing or representing any financial product as a deposit or a specified kind of deposit.

11. Clause 12 amends Schedule 2 to the Ordinance to allow meetings and other business of the Board to be conducted by electronic means, whether the members of the Board are in Hong Kong or not.

12. Clause 11 adds a new section 56 to the Ordinance, which deals with transitional provisions.

**Part 3 – Consequential and Related Amendments**

13. Clause 14 and the Schedule deal with consequential and related amendments. In particular, section 265 of the Companies Ordinance (Cap. 32) is amended so that the preferential payment for a depositor, in case of the winding up of a bank, is not to exceed the limit on the total amount of compensation to which the depositor is entitled as prescribed in section 27 of the Ordinance as amended by clause 4 (i.e. $500,000).

**Annex B**

On economic implications, the proposed increase in the DPS protection limit and expansion of DPS coverage, through strengthening the explicit protection on depositors' bank deposits, could enhance the stability of the local banking system against volatility in the external environment. While the total cost required for providing protection will increase correspondingly, with the implementation of the cost mitigating measures, the annual contribution payable by Scheme members is expected to remain unchanged at the current level. This will help eliminate any incentive for Scheme members to pass the cost of providing additional protection to depositors.

2. Moreover, the enhancements to improve the operating efficiency of the DPS in determining and making compensation to depositors are expected to contribute to savings in administrative cost in a payout. The increase in regulatory or compliance cost associated with the additional disclosure requirements, if any, may be offset by reduction in the cost of handling customer enquiries resulting from improved clarity of the coverage of the DPS.

3. By and large, the proposals will enhance the DPS as a part of the financial infrastructure of Hong Kong, and will help strengthen Hong Kong's status as an international financial centre.