

The Banking Amendment Bill 1995 was published in the Gazette on 10 February 1995. The Bill proposes to amend the Banking Ordinance to make the Monetary Authority the licensing authority for all types of authorised institutions. It also proposes to define more clearly the scope, objectives and powers of an Adviser or Manager appointed under the Banking Ordinance to take control of a problem authorised institution.

Introduction

The Banking Amendment Bill 1995 incorporates a number of changes which are designed to improve the legal framework within which the authorisation and prudential supervision of authorised institutions is conducted in Hong Kong. The Bill has two main objectives. The first is to make the HKMA responsible for the authorisation, revocation and suspension of all three types of authorised institutions. The second is to define more clearly the scope, objectives and powers of an Adviser or Manager appointed under the Banking Ordinance to take control of an authorised institution. A number of other provisions in the Ordinance also need revision in the light of practical experience of the operation of the Ordinance.

Authorisation, suspension and revocation of licence/registration

The three-tier structure of authorised institutions in Hong Kong consists of licensed banks, restricted licence banks (rlbs) and deposit-taking companies (dtcs). At present, each of them is licensed or registered by a different designated authority. In the case of licensed banks the relevant authority is the Governor in Council (ExCo); those for rlbs and dtcs are the Financial Secretary (FS) and the HKMA respectively. The powers to revoke and suspend also rest with the respective designated authorities, except that the current legislation does not provide for the suspension of a licensed bank.

A review of the licensing, suspension and revocation provisions in the Ordinance has been conducted. As a result, it has been concluded that the Ordinance should be amended:

- (a) to establish the HKMA as the authority responsible for the authorisation, suspension and revocation of all three types of authorised institutions. This

would also include new powers to suspend a licensed bank;

- (b) to improve the checks and balances in the authorisation procedures by more clearly distinguishing the administrative and appellate functions; and
- (c) to improve the transparency in the authorisation arrangements by setting out more clearly the criteria which will be used for the authorisation, and revocation, of all three types of institutions.

Apart from freeing ExCo's timetable and thus enabling it to focus on important policy and strategic issues, the assumption by the HKMA of full responsibility for authorisation matters would be in line with its central banking role of maintaining the general stability of the banking system and with the practice of central banks in other leading financial centres.

The proposed transfer of powers from ExCo and the FS to the HKMA would improve the checks and balances of the authorisation provisions in the Ordinance. ExCo, the FS and the HKMA would play distinctive roles under the revised structure: the HKMA would be responsible for administering all authorisation matters, the FS would provide a check as the HKMA would be required to consult him on important authorisation decisions such as suspension and revocation, and ExCo would act as the appellate body for hearing appeals against decisions made by the HKMA.

It is also important that the HKMA should be seen to operate within clearly defined statutory criteria for authorisation, suspension and revocation. The review provided an opportunity to consolidate and expand the existing criteria which are fragmented and, in some cases, inconsistent as between licensed banks and rlbs/dtcs.

The criteria for authorisation are set out in the new Seventh Schedule to the Ordinance. The core elements are common to all types of authorised institutions. These relate to such matters as adequacy of home supervision, ownership, management, financial soundness and prudent conduct. Adequacy of financial disclosure has been added as a new criterion for locally incorporated institutions. In general, these criteria define the “fitness and propriety” of applicants. In addition, there are certain criteria which apply specifically to licensed banks such as a minimum size (US\$16 billion of total assets) for overseas applicants and close association and identification with Hong Kong for local applicants.

The authorisation criteria are of a continuing nature. Failure to meet them by existing authorised institutions would mean that the HKMA’s powers of revocation would become exercisable (although there is discretion on their use). Additional grounds for revocation are also contained in the new Eighth Schedule. These would include the provision of false or misleading information to the HKMA or breach of a condition attached to an authorisation or registration.

In circumstances where the HKMA’s power to revoke became exercisable, it is proposed that it should also have the power to suspend the authorisation of the institution. This power, which already exists in respect of rlbs and dtcs, would be extended to apply also to licensed banks. This would enhance the means available to the HKMA for dealing with banking crises.

Because of the importance of the criteria set out in the Seventh and Eighth Schedules, it is proposed that they would be subject to change only by ExCo. ExCo would therefore retain overall policy responsibility for the authorisation regime.

Powers to take control of an authorised institution under Part X of the Ordinance

The existing powers of the HKMA under Part X of the Ordinance to appoint a Manager to take control of a problem authorised institution are broadly expressed but, arguably, too vague.

Broadly speaking, the powers of control have two main objectives:

- (a) to allow the HKMA, through a Manager, to control the affairs, business and

property of a troubled institution so that it can be nursed back to health, perhaps as a prelude to sale; and

- (b) to enable the HKMA to take quick action to safeguard the assets and maintain the fabric of the business until a liquidator can be appointed.

For Managers to discharge their responsibilities effectively, it is important that their scope, objectives and powers be clearly specified in the Ordinance. The Insurance Companies legislation has been taken as a model in revising the relevant provisions in the Ordinance. In respect of the scope of the Manager, it is proposed to clarify that the appointment would be made in relation to the “affairs, business and property”, rather than simply “business”, of an authorised institution. In the case of an authorised institution incorporated outside Hong Kong, the scope of the Manager would be confined to as much of the institution’s affairs and business as are carried on, or managed, in or from Hong Kong and property of the institution located in, or managed from, Hong Kong, or which is an asset of the Hong Kong branch.

It is proposed that when the HKMA gives a direction to appoint a Manager to take over control of an authorised institution, it should specify in the direction the objectives with which the Manager is required to comply. This is intended to clarify the broad purpose of the Manager’s appointment, e.g. safeguarding the interests of depositors.

Subject to the objectives specified by the HKMA in its direction, it is proposed that the Manager should be given the power to do everything necessary to manage the affairs, business and property of the institution. The new Ninth Schedule describes the specific powers of the Manager which include, amongst others, the power to enter into contracts on behalf of the institution, and to dispose of the business or property of the institution.

The Managers would in effect be acting as the controller of the institution. To perform that role, provisions in the Ordinance need to establish their authority over the board, management and shareholders of the institutions. In respect of the senior management and the board, it is proposed that the appointment of the chief executive, and

also the directors in the case of a locally incorporated institution, shall be revoked unless the HKMA's direction specifies otherwise and that the Manager would be empowered to appoint persons to fill such vacancies.

In respect of the shareholders, the proposed provisions specify that in the case of a locally incorporated institution, no meeting of the institution may be held and no resolution may be passed at a meeting of the institution except with the consent of the Manager. In the case of an overseas incorporated authorised institution, where resolutions are proposed that may adversely affect the conduct of his powers, the Manager may object to the resolution. Any resolutions passed in spite of the Manager's objection shall be invalid.

The proposed amendments provide that the High Court may, on application of the Manager or members of the institution, approve or refuse to approve a resolution that has been moved but not passed at the general meeting of a locally incorporated institution, or which is purported to have been passed but invalidated in the case of an overseas institution. This is to provide an opportunity for an aggrieved party to seek a ruling from the High Court. Among other things, this would enable the Manager to present a resolution at a general meeting of shareholders, for example, to approve a capital reconstruction of the institution and the issue of new shares; and to seek the approval of the Court if the shareholders failed to approve the resolution.

Miscellaneous amendments

The opportunity is taken to amend other provisions in the Ordinance to bring them in line with current requirements.

(a) Publication of audited balance sheet

The definition of "audited annual accounts" will be amended in the proposed section 60(8) so that, in relation to an authorised institution, it means that those accounts consist of the institution's balance sheet, profit and loss account and, where the auditor expresses an opinion on the cashflow of the institution in his report, its cashflow statement, together with any notes thereon. This is to clarify that the

cashflow statement should be published when one is prepared and audited.

The publication requirement is relegated to the new Tenth Schedule which will only be subject to change by the FS. This is to provide for future need to allow authorised institutions to publish abridged accounts. The amount of financial disclosure will be enhanced substantially and it may be burdensome to require publication of the full audited accounts in future.

(b) Returns and information to be submitted to the HKMA

New section 63(2A) empowers the HKMA to obtain information from the holding company of an AI, and the subsidiary of any such holding company in addition to any subsidiaries of the institution. The proposed new section will bring the HKMA's power of consolidated supervision more into line with international practice.

(c) Limitations on advances by authorised institutions

Section 81 limits the size of an authorised institution's financial exposure to a counterparty. It is proposed that an institution's exposure to multilateral development banks would be exempted from this section as they are normally supported by their respective member governments. The definition of multilateral development banks provided in the Third Schedule will be adopted.

Credit-exposures to the buyers of flats under the Home Ownership Scheme (HOS) and Private Sector Participation Scheme (PSPS), which are guaranteed by the Housing Authority (HA), are presently calculated as contingent liabilities of the latter and therefore subject to a limit under this section.

Such loans have proved to be rather prudent business. Default rates have been extremely low and no authorised institution has suffered any loss from them. It is proposed therefore to grant a

specific exemption under this section in respect of exposure to the HA resulting from loans to individual borrowers under the HOS and PSPS.

(d) Limitations on advances to directors, etc of a bank

Section 83 limits the amount of unsecured facilities an authorised institution can extend to directors, etc. The Bill will extend its limitations to include unsecured facilities granted to minority shareholder controllers.

(e) Restriction on use of bank name

Section 97 governs the use of banking names and description. It is proposed to substitute all references to "title" by "name" as the existing use of the two words interchangeably in the section has caused confusions in interpretation.

Section 97(1B) is intended to grant exemption for certain companies to use the word "bank" to indicate their connection with a bank. This has also caused confusion and not eliminated the need for seeking approval in many cases. The sub-section is to be repealed and substituted by a guideline. It is not

intended that the basic policy on banking names and description would be changed.

(f) Liquidity ratio

Section 102(3) currently restricts the calculation of liquidity to apply only to an authorised institution's principal place of business in Hong Kong and its local branches. The proposed amendment will allow the HKMA to require the liquidity ratio of an authorised institution to be calculated on a consolidated basis.

(g) Official secrecy

Section 120 provides for the confidential treatment of information obtained by the HKMA in the exercise of its functions under the Ordinance and the circumstances in which it may be disclosed. The purpose of the amendment is to remove the existing impediments to the disclosure of information within the HKMA even though it is in the public interest to do so, e.g. where such information would help the HKMA in his function of maintaining the stability and integrity of the monetary and financial systems of Hong Kong. ☞

– Prepared by the Banking Policy Department