

Press release

LCQ7: Deposit Protection Scheme

Wednesday, March 11, 2009

Following is a question by the Hon Wong Yuk-man and a written reply by the Secretary for Financial Services and the Treasury, Professor K C Chan, in the Legislative Council today (March 11):

Question:

Under the Deposit Protection Scheme and the Government's full guarantee measure implemented since October last year for customer deposits held in all authorised institutions in Hong Kong, deposits which are not protected include time deposits with a maturity exceeding five years, structured deposits, secured deposits, bearer instruments, offshore deposits and other financial products such as bonds, stocks, warrants, funds and insurance policies. The deposits of customers of integrated accounts who have applied for secured overdraft facility may not be protected, even if the amount of such facility is small. The Hong Kong Monetary Authority (HKMA) has thus required banks to inform their customers in writing before May 31, 2009 which deposits are not protected. In this connection, will the Government inform this Council:

- (a) of the reasons for time deposits with a maturity exceeding five years not being protected;
- (b) of the reasons for stocks kept in banks not being protected;
- (c) what measures HKMA has to sanction banks which do not follow its guideline to issue notice before May 31, 2009 to their customers who are not under protection; and
- (d) whether it has assessed, in the event of a bank failure before May 31, 2009, if their customers who have applied for secured overdraft facility but have never received the aforesaid written notice will have their deposits protected?

Reply:

President,

The Administration's response to the question is as follows:

(a) and (b) The types of eligible deposits covered by the Deposit Protection Scheme (DPS) launched since September 2006 and the Full Guarantee Measure which involves the use of the Exchange Fund to guarantee customer deposits held with all Authorised Institutions in Hong Kong from October 14, 2008 to end 2010 (Full Guarantee Measure) are the same. The Hong Kong Monetary Authority (HKMA) has conducted a consultancy study and two rounds of public consultation when formulating the details of DPS. The Deposit Protection Scheme Ordinance, which was passed by the Legislative Council in May 2004, has clearly set out the legal framework of DPS, including the types of eligible deposits covered by DPS.

Under the Deposit Protection Scheme Ordinance, time deposits with a maturity exceeding five years and stocks kept in banks are not eligible deposits. One of the policy objectives of DPS and Full Guarantee Measure is for the Hong Kong Deposit Protection Board (HKDPB) to provide compensation to the affected depositors as soon as possible under the relevant legal framework in case of bank failure, so as to avoid affecting the liquidity of the depositors. Compared with various types of eligible deposits, the liquidity of time deposits with a maturity exceeding five years is relatively lower. As such, time deposits with a maturity exceeding five years are not categorised as eligible deposits upon prudent balance of relevant factors, including the policy objectives of and resource consideration concerning DPS and Full Guarantee Measure. This arrangement is in line with the types of deposits covered by the priority payment scheme applicable to depositors under the Companies Ordinance. In addition, DPS and Full Guarantee Measure aim at protecting deposits but not other financial products held in banks' custody. Generally speaking, since stocks kept in banks remain the asset of the relevant clients and will not be used to repay banks' creditors in case of liquidation of the banks, such stocks have not been regarded as eligible deposits.

(c) HKMA issued a guideline in December 2008 requesting banks to write to depositors holding unprotected deposits again by the end of May 2009 to set out which deposits held by these depositors are not protected under DPS and Full Guarantee Measure. HKMA has closely monitored the implementation of the guideline and will continue to do so. In case of non-compliance with the guideline, HKMA will request banks to promptly rectify the situation and carry out appropriate regulatory actions if necessary.

(d) Collateralised deposits held by depositors are not eligible deposits under DPS and Full Guarantee Measure. Depositors can enquire the relevant banks concerning whether their deposits have been pledged. In case their deposits have been pledged, depositors can take appropriate actions, such as requesting the banks to cancel the charge on the deposits, so that the relevant deposits can be regarded as eligible deposits under DPS and Full Guarantee Measure. According to HKMA's understanding, while the arrangements under the contractual terms of different banks may vary, automatic offering of credit facilities to customers holding integrated accounts and charging all deposits under the relevant accounts for credit facilities are not a common practice among banks in general. A major bank which has adopted this practice has already changed the arrangement and notified affected customers in February 2009.

Under DPS, relevant banks are required to make representation to depositors concerning their membership and protection status of their products according to the Deposit Protection Scheme (Representation on Scheme Membership and Protection of Financial Products under Scheme) Rules. As mentioned above, HKMA issued a guideline in December 2008 requesting banks to write to depositors holding unprotected deposits again by the end of May 2009 to set out which deposits held by these depositors are not protected under DPS and Full Guarantee Measure. HKMA and HKDPB have been closely monitoring the implementation of the aforesaid representation requirements. They will continue to do so and carry out appropriate follow-up actions when necessary.

Ends