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Information Note
Legislative Council Panel on Financial Affairs
Special Meeting on 19 June 2001

The Bank of East Asia, Limited Bill

Introduction

1. This note informs Members of the Administration's views on The Bank of East Asia, Limited Bill (the Bill).

General

2. The Administration is of the view that the Bill relates to Government policies for the purpose of Article 74 of the Basic Law. The Chief Executive has given consent for the Bill to be introduced into the Legislative Council. Specifically, the Bill relates to policies in respect of —

(a) bank merger; and

(b) taxation.

Bank merger

3. The Bill seeks to transfer the undertaking of United Chinese Bank Limited (UCB) to the Bank of East Asia, Limited (BEA), effecting a merger between the two banks.

4. In view of the above, the Bill relates to government policy on bank mergers. It is the Government's policy to support consolidation of the banking sector in Hong Kong, which should improve its competitiveness and contribute to systemic stability in the longer term. As part of this policy, the Administration tries to promote and facilitate bank mergers where reasonable proposals are submitted for consolidation. This is, however, always subject to the overriding aim to promote the stability of the banking system and to provide an appropriate degree of protection to depositors in the merged institutions and to depositors generally.

5. As regards this particular case, the Administration considers that the proposed merger will help promote stability of the banking sector.

Taxation

6. The Bill, as currently drafted, contains several clauses (in particular clause 8) which have the effect of deeming the BEA (the surviving entity) as one and the same as the UCB in law; and allowing any profits and losses of the UCB to be treated as the profits and losses of the BEA from the beginning of the financial year of the merger.

7. Section 19C(4) of the Inland Revenue Ordinance, which governs the set-off of losses incurred by a corporation, provides that where a corporation in any year of assessment sustains a loss in that trade, the amount of that loss shall be set off against the assessable profits of the same corporation for that year of assessment, and to the extent not so set off, shall be carried forward and set off against the same corporation's assessable profits for subsequent years of assessment. In other words, this is a specific provision against loss set-off between separate corporations. The clear legal effect is that when a corporation is liquidated or ceases to exist upon merger, the loss it incurred would lapse.

10. The Government's policy is to have regard to the status of the surviving entity under operation of law (whether foreign or local) when deciding whether or not the surviving entity may carry forward the assessed losses of the merging entities.

11. As the Bank of East Asia, Limited Bill deems the surviving entity as one and the same as the merging entities and if the Bill is enacted, the Government would implement the provisions in the enacted Ordinance, including allowing the surviving entity, for tax assessment purpose, to carry forward any losses accumulated by any of the merging entities, in accordance with Section 19C(4) of the Inland Revenue Ordinance.

12. The same would apply to other merger bills, if they carry similar provisions deeming the surviving entity as one and the same as the merging entities, and if the bills are enacted by the Legislative Council. The same would also apply if the surviving entity is domiciled in a

jurisdiction where the law deems the surviving entity as one and the same as the merging entities (e.g. the legal concept of universal succession which many civil law countries in Europe have adopted). Then applying the principle under private international law, the Government must accept this status of the surviving entity. And in accordance with the provisions in section 19(C)(4) of the Inland Revenue Ordinance, the surviving entity would be allowed to carry forward the assessed losses of the merging entities for tax assessment purposes.

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