

For Information

Legislative Council Panel on Financial Affairs

**Sale of Loans under the Home Starter Loan Scheme and
the Sandwich Class Housing Loan Scheme
to the Hong Kong Mortgage Corporation Limited**

PURPOSE

This paper informs Members of the arrangements in connection with a proposed sale to the Hong Kong Mortgage Corporation Limited (HKMC) of loans granted to home-buyers under the Home Starter Loan Scheme (HSLs) and the Sandwich Class Housing Loan Scheme (SCHLS) (collectively, the “Schemes”).

BACKGROUND

2. In 1993 and 1997, the Finance Committee approved the provision of \$2 billion and \$1.38 billion respectively to the Hong Kong Housing Society (HKHS), as an agent of the Government, to implement the SCHLS which aims to provide the sandwich class families with one-off, up-front loans to meet their down-payments and related home purchase expenses. Six phases of the scheme were introduced from August 1993 to October 1997. Over 5 700 families have been granted a total amount of \$2.7 billion in loans under this scheme.

3. In 1998, the Finance Committee approved the creation of a \$18 billion commitment for the HKHS to implement and administer the HSLs (as an agent of the Government) in order to provide similar loan assistance to first-time home buyers. Applications for the scheme were closed on 31 March 2002. Over 33 000 loans with a total amount of \$14.8 billion have been granted under this scheme. A summary of the key terms and

conditions of the Schemes is at **Annex**.

4. As at the end of October 2003, there were about 36 000 outstanding loans under the Schemes with a total outstanding principal balance plus any capitalised interest accrued during the repayment holiday of some \$15.7 billion. All of the properties involved are domestic properties located in Hong Kong.

5. As part of the asset disposal programme announced in the 2003-04 Budget, we plan to dispose of the loans under the Schemes (the “Loans”). A one-off capital revenue of about \$10.9 billion will be realised within the current financial year. The remaining balance of about \$4.8 billion will be set aside as Deferred Consideration (see paragraph 9 below).

SALE TO HKMC

6. We plan to sell the Loans to the HKMC instead of other authorized institutions licensed or registered under the Banking Ordinance because the properties that are acquired by the borrowers with the assistance of the Loans are mortgaged to some authorized institutions. These institutions are subject to the regulatory limit of lending not more than 70% of the value of the property to the owner without mortgage insurance. It would not be feasible to structure a tender to cater for this limitation on one hand and to maximize the proceeds to the Government on the other. Selling these Loans to the HKMC will avoid this problem altogether.

MINIMISED IMPACT ON LOAN BORROWERS

7. The HKHS is the agent of the Government in implementing and administering the Schemes. The Government is the beneficial owner of the Loans and the Legal/Equitable Second Charges executed by the borrowers in favour of the HKHS (the “Mortgages”). A key objective of the Government in this sale is to minimize the impact, if any, on the

borrowers. We have agreed in principle with the HKMC that the sale would take the form of an equitable assignment of the Loans and the Mortgages by way of a declaration of trust to be made by the Government in favour of the HKMC. Under this form of sale, the Government will pass only the beneficial interests in the Loans and the Mortgages to the HKMC while the HKHS retains all the legal interests in the Loans and the Mortgages. This form of sale will enable the HKHS to retain the legal right to continue to administer all the rules and regulations of the Schemes, thus preserving their key terms and conditions. The rights and obligations of the borrowers under the Schemes will not be prejudiced as a result of the proposed sale.

KEY TERMS OF THE SALE

8. Other key terms and conditions of the sale are summarised below and in paragraphs 9 and 10 –

- (a) Loans to be sold : Subject mortgages must originate under the Schemes and be secured by second legal charges executed in favour of the HKHS on residential properties in Hong Kong.
- (b) Selling price : At par (i.e. the outstanding principal balance of the Loans as at the relevant settlement date plus any capitalised interest on the Loans accrued during the repayment holiday).
- (c) Interest payable to the HKMC : The HKMC will receive, on a monthly basis, interest calculated at a market-based rate with reference to 3-month Hong Kong Dollar HIBOR (the “HKMC Rate”) on the aggregate outstanding principal of the Loans acquired by the HKMC.
- (d) Settlement : The HKMC will acquire the Loans and the Mortgages in phases. It is currently

scheduled that completion of the sale of all Loans and Mortgages will take place before the end of this financial year.

- (e) Repayment : After the HKMC has acquired the relevant from borrowers HKHS will remit the repayments from borrowers in relation to these Loans to the HKMC on a monthly basis.

9. To preserve the Government's existing obligation to meet any borrower's default and the HKHS's servicing fees (paragraph 11 below), the HKMC will set aside a currently estimated sum of \$4.8 billion (the "Deferred Consideration") for the purpose. The Deferred Consideration, plus interest to be accrued on a monthly basis ("Accrued Interest") will also be used to meet any shortfall in the HKMC's interest receipts¹.

10. If the Deferred Consideration and the Accrued Interest exceed Government's obligations as described in paragraph 9 above, the Government will be entitled to payment of the surplus. The Government has the discretion to determine the amount and timing for withdrawal of the surplus. However, if the Deferred Consideration and the Accrued Interest are insufficient to meet Government's obligations in paragraph 9, the Government will be required to pay the HKMC the difference.

POST-SALE ARRANGEMENTS

11. After the sale of the Loans to the HKMC, the Loans will continue to be serviced/administered by the HKHS. The HKHS will

¹ Under the Schemes, the borrowers have to repay interest on the outstanding principal balance of their loans at the rate of 2% or 3.5% per annum. On the other hand, the HKMC will receive interest on the outstanding principal balance of the Loans at the HKMC Rate (paragraph 8(c)). A shortfall in the HKMC's interest receipt will arise if the interest received from borrowers falls short of the interest payable to HKMC.

continue to enforce/administer the terms and conditions of the Schemes. The servicing fees that the HKHS charges for administering the Schemes in accordance with the servicing requirements of the Government will be met in the manner set out in paragraph 9. The HKMC will pay the HKHS any additional servicing fees arising from any additional service requirements of the HKMC or the HKMC's change in service requirements.

12. Subject to formal approval of the sale and purchase by the two sides and satisfactory completion and execution of all legal documents, we expect to complete the first phase of the sale in December 2003.

Treasury Branch
Financial Services and the Treasury Bureau
November 2003

Home Starter Loan Scheme (HSLs)

The eligibility criteria, terms and conditions under the loan scheme vary with phases. Salient features of the latest phase of the loan scheme which are relevant to this purchase are as follows:

Lender	Hong Kong Housing Society as the Government's agent.
Development Type	A residential property in Hong Kong with age less than 30 years.
Eligibility	<ul style="list-style-type: none"> • Monthly household income not exceeding \$50,000 for family applicants and \$20,000 for singletons; • Applicants must not be authorised tenants/occupants of public rental units, nor have enjoyed any Government funded home ownership assistance; • Disposal assets not exceeding \$1 million for family applicants and \$0.35 million for singletons; • Not owned domestic property in Hong Kong for the past ten years; and • Applicants must have resided in Hong Kong for at least seven years.
Number of family members	At least two directly related members for family applicants.
Mortgage Terms	Second legal charge.
Maximum loan amount	Maximum loan of \$600,000 for family applicants and \$300,000 for singletons or 30% of the flat price, whichever is the lower.
Interest Rate	2% p.a. for those with income not more than \$25,000 per month, 3.5% p.a. for those with income between \$25,001 and \$50,000 per month.
Repayment	120 monthly instalments starting from the fourth year after the loan is made.
Resale	<ul style="list-style-type: none"> • Within the first three years, repay all outstanding loan plus price appreciation (if any) of flat; • After three years, repay all outstanding loan plus an administrative fee.

Sandwich Class Housing Loan Scheme (SCHLS)

The eligibility criteria, terms and conditions under the loan scheme vary with phases. Salient features of the latest phase of the loan scheme which are relevant to this purchase are as follows:

Lender	Hong Kong Housing Society as the Government's agent.
Development Type	A residential property in Hong Kong with price less than \$3.3 million and age less than 20 years.
Eligibility	<ul style="list-style-type: none"> • Monthly household income between \$30,001 and \$60,000; • Applicants must not be authorised tenants/occupants of public rental units, nor have enjoyed any Government funded home ownership assistance; • Disposal assets not exceeding \$1.2 million; • Not owned domestic property in Hong Kong for the past five years; and • Applicants must have resided in Hong Kong for at least seven years.
Number of family members	At least two directly related members.
Mortgage Terms	Second legal charge.
Maximum loan amount	Maximum loan of \$550,000 or 25% of the flat price, whichever is the lower.
Interest Rate	2% p.a.
Repayment	120 monthly instalments starting from the fourth year after the loan is made.
Resale	<ul style="list-style-type: none"> • Within the first three years, repay all outstanding loan plus price appreciation of flat (if any); • After three years, repay all outstanding loan plus an administrative fee.