

# **Report on the Case of Mr James Lau's Property Transactions in 2010**

## **Introduction**

On 7 July 2016, media reports began to emerge concerning two property transactions by Mr James Lau, former Executive Director of the Hong Kong Monetary Authority (“HKMA”) and Chief Executive Officer of the Hong Kong Mortgage Corporation (“HKMC”) until his retirement in December 2012, shortly before the announcement of the second round of macro-prudential measures for property mortgage loans by the HKMA on 13 August 2010. There were concerns that Mr Lau might have access to and used “privileged” or “insider” information on these tightening measures for personal gains or benefits. More specifically, for these two properties, Mr Lau took out two 70% loan-to-value (“LTV”) mortgage loans, which would have exceeded the maximum LTV ratio by 10% (or around HK\$1.6 million) had the transactions taken place after 13 August 2010. Moreover, it has transpired that while Mr Lau had declared the two property transactions, he did not declare the two mortgage loans as required by the HKMA rules. This has given rise to the question of whether there was a conflict of interest. In response to press enquiries, the HKMA and Mr Lau issued separate responses on 7 July 2016 (see Annexes A and B respectively).

## **Findings**

2. On 8 July 2016, the Governance Sub-Committee (“GSC”) of the Exchange Fund Advisory Committee decided to look into the case. A task force (“Task Force”) comprising three GSC members was set up to review the documents of the HKMA, such as notes of the Chief

Executive's Committee (CEC) meetings and internal emails, to see if there is evidence to suggest there was a conflict of interest. In addition, the Task Force also interviewed Mr Lau on 21 July 2016. The findings of the GSC are summarised below:

- (a) Having reviewed the notes of the CEC meetings prior to the launch of the second round of macro-prudential measures for property mortgage loans and the internal emails of the HKMA, the available evidence suggests that Mr James Lau only became aware of the imminent launch of the measures on 29 July 2010, which was after the provisional Sale and Purchase ("S&P") agreements for the two properties were signed on 21 and 25 July 2010 respectively. In other words, the evidence suggests that he did not participate in the formulation of the HKMA's tightening measures and that he had no prior knowledge of the measures when the decisions to purchase the two properties were made.
- (b) In view of (a), there does not appear to be a conflict of interest issue even though the purchases were very close to the date of launch of the measures.
- (c) Mr Lau declared the purchase of these two properties after the completion dates. The dates of completion of the two transactions (i.e. 31 August and 29 October 2010 respectively), instead of the dates of signing the provisional S&P agreements, were reported by Mr Lau as the dates of transactions for reporting purpose. These two declarations, other than that for Lucky Court which was late by 1 working day, were strictly speaking not in breach of the declaration requirements, which did not specify at that time the definition of "transaction date" (N.B. it was not until November 2012 that the "transaction date"

was defined as the date of signing the provisional S&P agreement).

- (d) Mr Lau said he had not reported the two mortgage loans because of “oversight” on his part. There has been concern expressed in the media reports whether this could have been because of some unusually favourable terms of these loans. In this regard, we noted that Mr Lau had received three loan offers from three different banks, all with broadly comparable terms. Furthermore, we can find no evidence to suggest that the terms of the two loans were out of line with what would have been generally available to customers in the same customer segment of the bank. On the 70% LTV, the HKMA announcement on 13 August 2010 stated clearly that those transactions with the provisional S&P agreements signed on or before that date would not be affected by the new measures (i.e. a lower maximum LTV of 60% instead of 70%). So the LTV level of Mr Lau’s mortgage loans was in line with what was generally available to all other property buyers who signed a provisional S&P agreement on or before 13 August 2010.
- (e) Given the senior position held by Mr Lau in the HKMA and HKMC, he should have had the sensitivity and taken the care to understand and comply with the relevant declaration requirements for taking out mortgage loans. Mr Lau had clearly breached the declaration rules. The Management is of the view that, had he remained an HKMA staff member, a warning would have been given to him for his failure to declare the loans, with the proviso that any further breach of the investment restriction or declaration rules would lead to disciplinary actions being instituted against him. The GSC concurs with the Management’s view.

- (f) It has also been suggested that Mr Lau, even though he had no prior knowledge of the second-round measures when he bought the two properties, should, of his own accord or be told by the HKMA to, unwind the two property transactions once he became aware of the launch of the tightening measures. We believe that it would be highly inappropriate to do so because this is tantamount to making use of “privileged” or “insider” information, whether or not such move would result in actual gains for Mr Lau (which would have been hard to foretell as the market reactions to the tightening measures were uncertain).
  
- (g) There is scope for further refinements to the declaration rules and forms in light of practical experience. For example, the declaration form for property transactions could include a box indicating the means of financing the purchase and reminding the staff member that any related mortgage loan, if taken, will need to be declared as well. Another suggestion is to require the staff member to declare whether a given loan is secured by any underlying assets.

### **Relevant Facts and Information on the Case**

3. The facts and information relevant to the case and considered by the GSC are set out in the ensuing paragraphs.

#### *Avoidance of Conflict of Interest and Declaration Requirements*

4. Integrity of the HKMA and its staff is key to maintaining and safeguarding public trust and confidence in the HKMA. The HKMA

Code of Conduct provides guidelines and advice on the main issues that may have a bearing on the integrity of the HKMA and its staff. The Code sets out clearly that it is the responsibility of every staff member to be alert to and avoid engaging in situations that may lead to an actual or perceived conflict of interest and that the staff member should report any conflict to the supervisor. Under this overarching principle, the HKMA Administrative Guidelines on Rules on Restrictions on Investments by HKMA Staff provides more specific rules regarding staff's investments and the related declaration requirements. These rules and requirements are refined from time to time in the light of practical experiences, expansion of the HKMA's functions, as well as the changing circumstances.

5. The declaration requirements are designed to help the Management to monitor staff's compliance with the investment rules. They provide a tool for the Management to assess whether a staff member is engaged in overly active trading which may affect the discharge of his daily duties, is taking excessive risks or holding positions beyond his financial means, is undertaking investment activities which may pose conflict of interests with his duties in the HKMA or involve misuse of privileged information for financial gains. It is the responsibility of a staff member to report his investments within the specified period.

6. The declaration requirements have evolved over time. Insofar as property transactions and mortgage loans are concerned, the declaration requirements in effect during 2010 were that, for staff at Senior Manager level or above, details of property transactions should be reported "within 7 days of the transactions". All staff are also required to report to the Chief Executive of the HKMA ("CE/MA") all the loan facilities exceeding HK\$100,000 obtained from banks within 7 days.

7. In November 2012, the reporting period regarding property transactions was clarified by replacing “*within 7 days of the transaction*” with “*within 7 calendar days upon the signing of the provisional sale and purchase agreement*”. An additional restriction was introduced, requiring staff involved in the formulation and development of prudential measures regarding property mortgage loans to seek prior permission for the purchase and sale of property in Hong Kong.

#### *Protection of Confidentiality*

8. According to the HKMA Management, staff members are required to comply with strict rules to protect confidential or market sensitive information. Such information includes numerous items of bank-specific information that flow through the HKMA in its conduct of banking supervisory functions. Apart from the statutory official confidentiality provisions such as section 120 of the Banking Ordinance, the HKMA has all along adopted the practice of “need to know” by imposing Chinese walls within the HKMA. A staff member cannot access institution-specific files and information unless there is a legitimate functional need to do so. This will help materially reduce the risk of sensitive information being leaked from within the HKMA. The same principle applied, and is still applicable, to the formulation and development of specific prudential measures for property mortgage loans since October 2009. Only a small core group of HKMA officers were involved on a strictly need-to-know basis and they were, and are still, bound by the confidentiality rules. The prudential measures had not been discussed in the CEC meetings, which are attended by all Executive Directors (EDs) or above with the Administrative Assistant to CE/MA as the secretary. Based on internal records and staff’s recollections, paragraphs 9-12 below outline the process leading to the launch of the

second-round measures and the involvement of staff at various stages.

*Launch of the Second Round of Prudential Measures on 13 August 2010*

9. The first round of prudential measures was introduced on 23 October 2009. After its introduction, the HKMA closely monitored the developments of the property market and banks' implementation of the first-round measures. Throughout the first half of 2010 there were discussions from time to time between CE/MA and Deputy CE (Banking), sometimes involving the ED in charge of banking supervision (ED(BS)), about the developments of the property market and the possible shape of the new prudential measures if and when they were needed. A small support team of four banking staff at Division Head, Senior Manager and Manager level provided specific information as required but did not take part in such discussions. Towards the end of July 2010, CE/MA considered that a second round of measures might be warranted in view of the latest market conditions. On 29 July 2010 he convened an internal meeting including his three deputies, at which the specific prudential measures were deliberated and confirmed. At the same meeting, it was also decided that the HKMC should be asked to consider making appropriate adjustments to its Mortgage Insurance Programme (MIP).

10. Immediately after the meeting, a DCE emailed Mr James Lau, CEO/HKMC (who was on leave 22-30 July 2010), informing him that the HKMA would announce a tightening package very soon and inviting HKMC to consider tightening the MIP. The specific prudential measures to be introduced by the HKMA were not disclosed in this email. This was the first time Mr Lau was informed of the HKMA's plan to launch the second round of prudential measures without the details.

11. On 13 August 2010, the HKMA announced the second round of measures which included lowering the maximum LTV ratio for non-self-occupied properties to 60%. On the same day, HKMC also announced amendments of certain features of the MIP.

12. The Task Force has reviewed the notes of the CEC meetings (of which Mr Lau was a member) during the period from January to August 2010. The notes indicate that the prudential measures for property mortgage loans were not discussed by CEC at these meetings. The Task Force has also reviewed the email sent to Mr Lau on 29 July 2010 as referred to in paragraph 10 above. The Task Force was provided with a list of HKMA officials who took part in the small group discussions leading to the second round of prudential measures and the preparation of the announcement. We are satisfied that the evidence suggests that staff involvement was on a “need-to-know” basis and that Mr Lau was not involved until 29 July 2010.

#### *Mr Lau’s Property Transactions and Related Declarations*

13. On 10 September 2010, Mr Lau made a declaration to CE/MA regarding the purchase of a property at “Lucky Court” for HK\$9.98 million, quoting 31 August 2010 as the “Date of Purchase” and reporting the purpose of purchase as “Investment”.

14. On 8 November 2010, Mr Lau submitted a second declaration regarding the purchase of another property at “Mandarin Court” for HK\$6.18 million, quoting 29 October 2010 as the “Date of Purchase” and reporting the purpose of purchase as “Investment”.



15. The HKMA has not received any declaration made by Mr Lau regarding any mortgage loans for the two properties.

16. On 6 July 2016, the HKMA received a media enquiry regarding the two property transactions. A land search was then conducted on the two properties. Land Registry records reveal the following information:

<b>Date of</b>	<b>Mandarin Court</b>	<b>Lucky Court</b>
Provisional sale and purchase agreement	21 July 2010	25 July 2010
Sale and purchase agreement	4 August 2010	4 August 2010
Assignment (completion date)	29 October 2010	31 August 2010
Mortgage (loan drawdown date)	29 October 2010	31 August 2010

17. The Task Force reviewed the two declarations made by Mr Lau and the Land Registry records. The Task Force also reviewed copies, provided by Mr Lau, of the mortgage loan offers from three banks – Bank A, Bank B and Standard Chartered Bank (Hong Kong) Limited (SCB HK) – and the final loan agreements formally signed with SCB HK.

18. The loan offers were received between 5 August and mid-August 2010, on the basis of 70% LTV ratio. The key terms are summarised as below:

- (a) Bank A offered H+0.7%, capped by P-2.7% (P being 5%), plus cash rebate equivalent to 0.85% of loan amount;
- (b) Bank B offered H+0.7%, capped by P-2.75% (P being 5%), plus cash rebate of 1%;
- (c) SCB HK first offered H+0.65% (capped by P-3%) for Mandarin Court; and H+0.7% (capped by P-2.95%) for Lucky Court. SCB HK's prevailing Prime Rate then was 5.25%, slightly

higher than the 5% quoted by Bank A and Bank B. The interest rate for Lucky Court was subsequently revised down from H+0.7% to H+0.65%, capped by P-3%, tallying with the rates for Mandarin Court. For both mortgages SCB HK also offered cash rebate capped by 1%.

19. HKMA has obtained confirmation from SCB HK that the mortgage terms offered to Mr Lau were also available to SCB HK's Priority Banking customers (Mr Lau being in this category) at that time.

20. On 21 July 2016, the Task Force interviewed Mr Lau. Mr Lau was asked to elaborate on the circumstances leading to the property transactions and his failure to report the loans. The interview with Mr Lau has not revealed any information that would alter the facts and findings set out above.

**Governance Sub-Committee of  
the Exchange Fund Advisory Committee**

**29 July 2016**

**HKMA's response to media enquiries on Mr James Lau's case on 7 July 2016**

金管局的一些員工可能會因工作需要而處理一些市場敏感資料,因此,金管局的《行為守則》要求員工必須防範可能引起利益衝突的情況,並對員工的投資和申報訂立具體的指引。

金管局推行的物業按揭貸款審慎監管措施屬於市場敏感資料,故在措施制定的過程小心處理,僅限於少數有直接工作需要的同事才參與。所有參與同事在整個過程須恪守保密要求。有關措施的制定不在總裁委員會討論。

就2010年8月13日推出的新一輪措施,按揭證券公司總裁劉怡翔先生並無參與或得悉金管局制定有關措施的內部討論。他於2010年7月29日才首次獲告知金管局正計劃推出新一輪措施,而按揭證券公司需要考慮對其推行的按揭保險計劃作適當的修訂。

因應傳媒在7月6日的查詢,我們檢視了劉先生的申報紀錄。他在2010年有兩宗購買物業的申報,交易日期分別為2010年8月31日和10月29日。根據我們初步了解,這兩個物業的臨時買賣合約是在2010年7月21日和25日簽訂,早於他在7月29日首次獲告知金管局計劃推出新一輪措施。

根據金管局在2010年當時的規定,劉先生須在「房地產交易」(transaction)後7天內向總裁申報。

2012年11月,金管局進一步釐清有關申報規定,將「房地產交易」明確訂為「簽訂臨時買賣合約」。同時,亦要求所有參與制訂物業按揭貸款審慎監管措施的員工在香港買賣房地產前須先行獲得批准。

我們並無收到劉先生關於該兩個物業承造按揭貸款的申報。我們會就

此向劉先生進一步了解和跟進。

以下為劉怡翔先生在 2010 年兩宗購買物業申報的補充資料：

交易日期	申報日期
2010年8月31日	2010年9月10日
2010年10月29日	2010年11月8日

關於劉先生兩個物業承造按揭貸款未有申報的事宜,我們會在完成跟進後適當交代。

(English translation)

Some staff of the Hong Kong Monetary Authority (HKMA) may need to process market-sensitive information in the course of their work. Therefore, the HKMA's Code of Conduct stipulates that its staff must guard against any situations that may involve a conflict of interest. The HKMA also has specific guidelines on its staff's investment activities and their declarations of investments.

Prudential measures on property mortgage loans launched by the HKMA are regarded as market-sensitive information. The process of their formulation is thus always handled carefully, with the participation limited to only a very small number of staff whose work is directly related. The staff involved must keep the matter confidential during the whole process. The formulation of the aforesaid measures is not discussed by the Chief Executive's Committee.

Regarding the new round of prudential measures introduced on 13 August 2010, Mr. James Lau, then Chief Executive Officer of the Hong Kong Mortgage Corporation (HKMC), was not involved in, or had knowledge of, any internal discussions in the HKMA on the formulation of the measures. It was not until 29 July 2010 when Mr. Lau was first informed of the HKMA's plan to introduce another round of prudential measures and that the HKMC would need to consider making appropriate adjustments to its mortgage insurance programme.

In response to media enquiries on 6 July 2016, we reviewed the records of Mr. Lau's declaration. In 2010, he made two declarations for the acquisition of two properties. The transaction dates were 31 August and 29 October 2010 respectively. According to our preliminary understanding, the provisional sale and purchase agreements for the two properties were signed respectively on 21 July and 25 July 2010, both earlier than 29 July 2010 when he was first informed of the impending introduction of another round of prudential measures.

According to applicable HKMA rules in force in 2010, Mr. Lau was required to declare to the Chief Executive within seven days after any "property transaction".

The relevant rules were refined in November 2012, with "property transaction" clearly referring to "the signing of the provisional sale and purchase agreement". Besides, a new rule was introduced to require all staff involved in the formulation of prudential measures on property mortgage loans to obtain prior permission for any property transactions in Hong Kong.

We did not receive any declaration from Mr. Lau on the mortgage loan arrangements for the two said properties. We will follow up with Mr. Lau to obtain further information.

Below is the supplementary information on Mr. Lau's acquisition of two properties in 2010:

<u>Date of transaction</u>	<u>Date of declaration</u>
31 August 2010	10 September 2010
29 October 2010	8 November 2010

We will provide update as appropriate after following up on the case regarding Mr. Lau's failure to declare the mortgage loan arrangements for the two said properties.

**James Lau's response to media enquiries on 7 July 2016**

本人及家人在2010年7月份先後購置兩個住宅單位作投資用途,分別於2010年7月21日及25日簽訂臨時買賣合約,並獲銀行承造非自住物業的七成按揭。

本人當時擔任按揭證券公司總裁和金管局總裁委員會成員,就2010年8月13日金管局推出的新一輪措施,我並無參與或得悉金管局制定有關措施的內部討論。我是於2010年7月29日才首次獲告知按揭證券公司需要考慮適當修訂按揭保險計劃,至於新一輪措施的其他內容,我並不知悉。

本人簽訂兩個物業的臨時買賣合約是在2010年7月21日和25日,早於7月29日首次獲告知金管局計劃推出新一輪措施,而我亦已在完成有關買賣交易後作出申報,但因疏忽之故,沒有申報就有關物業已承造按揭。

本人須強調,在處理有關物業買賣的事宜上,並不涉及利益衝突,亦沒有因公職而獲取任何金錢回報或個人利益。

(English translation)

In July 2010, my family and I made two acquisitions of residential property units for investment purpose. The provisional sale and purchase agreements were signed on 21 July and 25 July 2010 respectively, and we obtained mortgage loans at a loan-to-value ratio of 70% for non-owner-occupied properties from a bank.

At the time, I was Chief Executive Officer of the Hong Kong

Mortgage Corporation (HKMC) and a member of the Chief Executive's Committee of the Hong Kong Monetary Authority (HKMA). I was not involved in or had knowledge of the internal discussions in the HKMA on the new round of prudential measures for residential mortgage loans introduced on 13 August 2010. I was first informed on 29 July 2010 that the HKMC would need to consider making appropriate adjustments to its mortgage insurance programme. I, however, had no knowledge of other contents of the new round of prudential measures.

I signed the provisional sale and purchase agreements for the two properties on 21 July and 25 July 2010 respectively, before 29 July 2010, the day I was first informed of the HKMA's plan to introduce a new round of prudential measures. I made investment declarations after the two property transactions were completed, but out of oversight I did not declare the mortgages taken on the properties concerned.

I must stress that there was no conflict of interest in my property transactions. Neither did I have any monetary or personal gains because of my public duties.