

Comment piece: Regulatory challenges in Hong Kong

local knowledge - global solutions

This comment piece looks at the regulatory challenges in Hong Kong

Introduction



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“The Singapore and Hong Kong regulatory environments are the most mature and stable in their regions but despite this, banks still have a number of

onerous regulatory reporting requirements to meet.”

Hong Kong Monetary Authority (HKMA)

The regulators in Hong Kong include:

- Hong Kong Monetary Authority (HKMA): The government authority in Hong Kong responsible for maintaining monetary and banking stability.
- Hong Kong Deposit Protection Board (DPS): An independent statutory body formed under section three of the Deposit Protection Scheme Ordinance (Cap. 581), responsible for maintaining a deposit protection scheme (DPS) in Hong Kong.
- Securities and Futures Commission (SFC): An independent non-governmental statutory body outside the civil service, responsible for regulating Hong Kong's securities and futures markets.

Bank licenses

One of the three types of authorized institutions in Hong Kong are licensed under the Banking Ordinance (also called Three-tier Banking System)

1. Licensed banks are the only institutions permitted to carry on banking business in Hong Kong. This term is often used interchangeably with the bank

2. A restricted licence bank may take time, call or notice deposits from members of the public in amounts of HK\$500,000 and above without restriction on maturity. Restricted licence banks generally engage in activities such as merchant banking and capital market operations.
3. Deposit-taking companies are restricted to taking deposits of HK\$100,000 or more with an original term to maturity of at least three months. These companies are mostly owned by, or otherwise associated with, banks. They engage in a range of specialised activities, including consumer finance, trade finance and securities business.

Many returns need to be submitted within 14 days from the reporting date. The many manual processes within banks required to complete these reports mean that users are spending more time completing the reports as opposed to the value adding task of analysing the results.

Three of the reports are especially difficult:

1. Large exposure returns
2. Liquidity reports
3. Maturity Profile reports

Large exposure returns

This return collects information on authorized institutions' large exposures to banks, non-bank entities and connected parties during the reporting quarter

It requires banks to:

- Aggregate both direct and indirect exposure by bank, non bank and connected party group on a daily basis
- Accumulate the daily group exposure data
- Find out which groups have the highest top 10 exposure during the quarter

The process is highly complex and time consuming. Banks usually spend a lot of time in compiling this report.

Liquidity reports

This return captures information on institutions' liquidity ratio and funding sources. Authorized institutions need to comply the minimum liquidity ratio as stipulated in the Banking Ordinance (current minimum liquidity ratio is 15%).

It requires banks to:

- Compute liquidity ratio on every Wednesday and month end. Liquidity ratio refers to the ratio of total liquefiable assets over total qualifying liabilities
- Identify all liquefiable assets which generally refers to assets mature or readily realizable within 1 month
- Identify all qualifying liabilities which generally refers to liabilities mature and likely to crystallize within 1 month
- Special processing requires to offset the eligible loan under liquefiable assets vs. pledged deposits under qualifying liabilities and net amount be reported accordingly
- HKMA has its own maturity band definition which is not the same as normal business convention. E.g. one month from reporting date of 28 Feb 2010 is 28 Mar 2010.

During the financial crisis or for those banks that the regulator deemed to require additional monitoring were requested by the HKMA to submit the liquidity return on a weekly or even a daily basis.

Maturity Profile reports

This return collects information on the maturity profile of assets and liabilities of authorized institutions

It requires banks to:

- Split the assets and liabilities into different product nature
- Identify the actual or projected cash flow and slotted into different maturity bucket according to the actual or estimated maturity date
- Ensure the total outstanding reported for each line items tied back to the Balance Sheet

- HKMA has its own maturity band definition which is not the same as normal business convention. E.g. one month from reporting date of 28 Feb 2010 is 28 Mar 2010.

Coverage processing

In many regulatory reports, it requires banks to identify the amount of secured and unsecured exposures.

The key difficulties encountered by banks are:

1. The calculation of secured and unsecured exposures is a very challenging task for banks with complex exposures to coverage relationships. E.g. A single collateral can cover multiple exposures or multiple collaterals are shared by multiple exposures. The logistic of offsetting of the exposures vs. collateral can be highly complex
2. Recognition of eligible collateral varies from country to country e.g. some countries only recognize guarantee received from bank or government as eligible collateral while other countries may have a more loosened criteria.

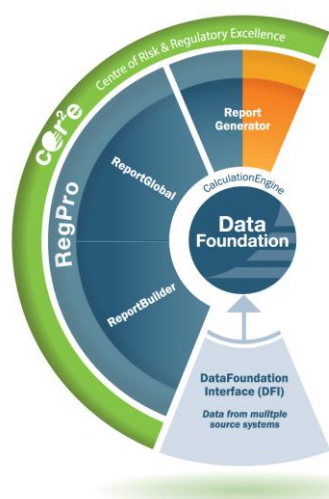
FRSGlobal coverage processing module performs offset of the highest risk weighted exposure against the most secured collateral to mitigate the credit risk of the reporting institution. At the same time, it allows flexibility of inclusion of only those eligible collaterals as per country specific reporting requirements.

FRSGlobal: RegPro

FRSGlobal RegPro solutions enable financial institutions to address major regulatory and compliance requirements locally and globally:

- Global compliance rules (e.g. Basel II, SOX, MiFID)
- Statutory (e.g. IFRS)
- Statistical (e.g. Bank of England)
- Prudential (e.g. Basel II)
- Transactional (e.g. MiFID)

This is achieved by leveraging a common DataFoundation to harness financial intelligence across an enterprise, while maintaining the country-specific requirements of local regulators.



- ReportGenerator: generating reports from the ReportGlobal module and/or those defined by the user using ReportBuilder
 - ReportBuilder: for non-technical users to build their own reports for internal or external consumption
 - ReportGlobal: fully defined regulatory reports for a selection of more than 40 countries
- Automated end-to-end production of regulatory reports
 - Timely and accurate regulatory reporting
 - The ability to keep up with changing local requirements while maintaining global consistency Increased management control
 - Cost-effective operations
 - Consolidated financial reporting and analysis

Benefits of RegPro:

- Multi-lingual, multi-currency support
- Drill-up and drill-down between data and report level
- Extensive variance analysis
- Orphan detection
- Ability to make adjustments
- Fully audited environment
- Detailed security mechanism
- One solution for global regulatory reporting

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