

Registered Institutions (“RIs”) are required to implement the following recommendations in accordance with the timetable specified

	Recommendations¹	Requirement and Implementation Timetable	Detailed Guidance on Implementation (Timeline of implementation follows the original timetable unless otherwise stated)
5	<p>“Health-warnings” should be attached to retail structured products with embedded derivatives or to retail derivative products generally.</p>	<p>RIs should include a “health warning” statement, printed in reasonable font size, to all existing derivative products and structured products with embedded derivatives that are being sold to investors. RIs should draw investors’ attention to the “health warning” statement when selling such products to them.</p> <p>Immediately</p>	<p>After consultation with the Securities and Futures Commission (SFC), a health warning statement with the following wording will be included in the marketing materials and offering documents of all structured investment products:</p> <p><i>“This is a structured product involving derivatives. The investment decision is yours but you should not invest in the [product name/type] unless the intermediary who sells it to you has explained to you that the product is suitable for you having regard to your financial situation, investment experience and investment objectives.”</i></p> <p><i>“此乃涉及金融衍生工具的結構性產品。投資決定是由閣下自行作出的，但閣下不應投資在該《產品名稱/類型》，除非中介人於銷售該產品時已向閣下解釋經考慮閣下的財務情況、投資經驗及目標後，該產品是適合閣下的。”</i></p> <p>For existing marketing materials and offering documents of structured products already authorized by the SFC, the health warning statement may be included on a separate sheet attaching to the materials. When the remaining printed stocks of these materials have been used up and need to be replenished, the health warning statement should be incorporated into the newly printed materials and a copy of the revised materials should be submitted to the SFC for record. The above is subject to due compliance with the relevant requirements under the SFO</p>

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		<p>or the Companies Ordinance and applicable SFC codes and guidelines.</p> <p>The requirement applies equally to phone banking transactions where the health warning statement should be provided verbally over the phone during the sales process and audio recorded for audit trail purposes.</p> <p>Notes:</p> <ol style="list-style-type: none"> 1. The definition of structured investment product (for the purposes of the health warning requirement) is an investment product with embedded derivatives that fall within the coverage of the Securities and Futures Ordinance. By this definition, stock trading is deemed to be excluded. 2. The wording of the health warning statement for structured investment products stated above was finalised in consultation with the SFC. The health warning statement is meant to be a warning to investors. Where an investor insists on buying a product despite a risk mismatch to his investment appetite or investment objectives, banks must demonstrate and prove that it has during the selling process complied with all applicable laws and regulations including the SFC’s Code of Conduct e.g. they have properly conducted suitability assessment and clearly explained the risk to the investors, with adequate documentation and evidence to demonstrate that this has been done.

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			<p>3. The HKMA and SFC are working on Key Facts Statements which should be provided by the product issuer and RIs respectively. These will be released in due course for market consultation. When the Key Facts Statements are finalised and introduced, the HKMA will consider whether there is still a need for a separate health warning statement.</p> <p>4. Some RIs may wish to apply the above health warning statement to investment products which are not structured products. In such circumstances, RIs may suitably replace the words “structured product involving derivatives” in the first sentence of the health warning statement with words like “investment product” which would provide more accurate description of the relevant investment product while keeping the rest of the health warning statement intact.</p>
12	To provide further protection for investors, the assessment of a customer’s risk profile be separated from the sales process and be carried out by non-sales staff and that the customer be provided with a copy of the risk profile and asked	RIs should put in place appropriate structure and procedures for the separation of risk assessment and sales process. Also adequate records (including audio records) must be maintained as evidence of the risk assessment process and confirmation of agreement to the risk assessment by the investor.	<p>The HKMA expects that the assessment of a customer’s risk profile should be carried out by non-sales staff. However, in situations where this is not practicable, an independent review must be performed on the risk assessments conducted by sales staff. The independent review should satisfy the following criteria:</p> <ul style="list-style-type: none"> • 100% check on risk assessments with customers graded above the medium risk category • 100% check on risk assessments involving vulnerable

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<p>to confirm his agreement that the risk profile is accurate. Mandatory requirements to audio record the assessment process should be introduced.</p>	<p>As soon as possible but no later than end of March 2009.</p>	<p>customers graded above the lowest risk category</p> <ul style="list-style-type: none"> • Sample check (at least 20%) on risk assessments of all other customers graded above the lowest risk category • The independent review should cover <u>all</u> sales staff who have performed assessment of customers’ risk profile • In case exceptions are noted with the risk assessments performed by a sales staff, the RI should perform a more comprehensive review on the risk assessments performed by that staff. <p>As part of its ongoing supervision, the HKMA will collect from RIs details of exceptions identified in independent reviews and will assess the effectiveness of independent reviews performed by RIs.</p> <p>In consultation with the SFC, it is considered that the independent non-sales staff performing the customer risk profiling does not have to be a relevant individual provided that the staff will not be involved in any activities that will fall within the definition of the various types of regulated activities and on the basis that:</p> <ul style="list-style-type: none"> (i) the staff will only perform the customer risk profiling process, i.e. ask the customer to provide information for completion of a standardised questionnaire, record the answers (e.g. inputting into system) and inform the customer of the resultant risk rating assigned by the system as well as the

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			<p>corresponding allocation among different asset classes (but not specific products); and</p> <p>(ii) the staff will not induce client to deal in securities and will not talk about specific investment products with client.</p> <p>On the same basis, it is considered that the staff responsible for conducting the independent review for cases where the risk profiling is done by sales staff would not be required to be registered as relevant individual.</p> <p>Customers should be provided with a copy of the risk profile and asked to confirm his/her agreement that the risk profile is accurate. The assessment process should be audio recorded and the audio records should be retained for seven years.</p> <p>Timeline for implementation of the audio recording requirement will follow that of Recommendation 13.</p>
13	The regulatory requirements at point of sale should be reviewed with a view to introducing mandatory requirements for the audio-recording of	RIs should ensure adequate records and audit trail (including audio records) are in place to show that due selling process is being followed for all investors.	<p>The audio records should be retained for seven years.</p> <p>Given the system changes required in implementing this recommendation, the HKMA is prepared to allow RIs more time to set up the audio-recording system but full implementation of this recommendation should be achieved by end of June 2009. Individual</p>

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	the sales process and ancillary arrangements.	As soon as possible but no later than end March 2009.	RIs requiring more lead time for implementation due to technical difficulties should liaise with their usual HKMA contact directly with justifications for requiring a longer lead time.
14	Where the continuous review by a registered institution of the risk ratings of the investment products it sells results in a higher risk rating being attributed to a product, the institution should disclose this to customers to whom it recommended and sold the product.	This is a requirement in the HKMA circular of 28 October.	<p>RIs should notify customers directly of the higher risk rating through monthly statement or a separate letter. The HKMA notes that this may necessitate system changes by RIs and some RIs might need more time to comply with this recommendation. In any case, RIs are expected to achieve full implementation of this recommendation as soon as practicable but no later than 30 June 2009. Individual RIs requiring more lead time for implementation due to technical difficulties should liaise with their usual HKMA contact directly with justifications for requiring a longer lead time. Before this is done, RIs should, as an immediate and interim measure, take appropriate actions to alert customers of the higher risk rating and provide a channel (e.g. website or dedicated telephone line) through which the customer could access the relevant information.</p> <p>RIs have no further obligation to make the disclosure to a customer who has closed his/her account or has the relevant investment product transferred to another bank’s account.</p>
15	In cases of sales of investment products where there is a risk mismatch	Adequate documentation of the investor’s reasons, understanding and agreement to the risk mismatch,	Bank staff has a heightened responsibility in ensuring that the suitability requirements are met and that risks are clearly explained to investors in the selling process. Whenever a product with a risk rating higher than

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<p>between the risk rating applied to the product and the customer’s risk profile, full and complete documentation should be retained of the reasons why the customers made the investment decision, the sales process should be audio-recorded, and endorsement should be sought from supervisory staff within the institution.</p>	<p>and seeking of supervisor’s endorsement, are existing requirements. To enhance audit trail, RIs should take steps to have relevant discussions with the investors audio- recorded.</p> <p>Adequate Documentation and supervisor’s endorsement to be implemented immediately</p> <p>Audio recording – as soon as possible but no later than end March 2009.</p>	<p>the customer’s risk tolerance level is sold to the customer, the bank staff should ensure the following: (i) remind the customer of the risk mismatch and that the product may not be suitable for him/her; (ii) document the reasons of any product recommendations as well as the reasons of the customer’s choice of products; (iii) the customer should sign his/her acknowledgement of the risk mismatch; and (iv) the full conversation should be appropriately audio-recorded. In the event of inconsistent answers given by a customer, the bank staff should seek clarification from the customer and document the reasons given by the customer. Endorsement should be sought from supervisory staff within the institution.</p> <p>Timeline for implementation of the audio recording requirement will follow that of Recommendation 13.</p>
<p>17 A mystery shopper programme be instituted periodically by the HKMA (as well as by registered institutions themselves) to test sales processes, and a pilot programme of customer surveys be commissioned by the HKMA to gauge whether</p>	<p>RIs should put in place appropriate “mystery shopper” programme to test sales procedures.</p> <p>As soon as possible but no later than end March 2009.</p>	<p>RIs are expected to put in place appropriate “mystery shopper” programme as soon as possible.</p> <p>The HKMA and SFC will jointly develop an external “mystery shopper” programme and will further work out the timeframe of the pilot programme of customer surveys.</p>

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such surveys can provide information useful for the examination of specific issues in the context of the longer-term customer relationship.		
18 Remuneration structures for staff engaged in AIs’ securities business be subject to greater focus in the HKMA’s on-site examinations and off-site surveillance of AIs’ securities business.	RIs should have adequate procedures and controls to ensure that frontline sales staff are not remunerated with bonuses calculated solely on the basis of financial performance but that other factors (including adherence to best practices guidelines and code of conduct) are in fact taken into account. Immediate	RIs are expected to implement this improvement measure immediately in case they have not already done so.

¹ The recommendation numbers are those referred to in paragraphs 8.1 to 8.50 of the HKMA’s Report.