



HONG KONG MONETARY AUTHORITY
香港金融管理局

Our Ref.: B10/1C

24 August 2015

The Chief Executive
All Authorized Institutions

Dear Sir/Madam,

Practice note on credit risk management for loans to the corporate sector

The Hong Kong Association of Banks and the Asia Pacific Loan Market Association met with the HKMA on 17 August 2015 to discuss the implementation of the above Practice Note. Major issues discussed are provided in the enclosed frequently asked questions and answers (FAQs) for AIs' information.

If your institution has questions on this letter, please contact Ms Denise Tai at 2878 1589.

Yours faithfully,

Henry Cheng
Executive Director (Banking Supervision)

Encl.

FAQs on the Implementation of the Practice Notes on Credit Risk Management for Loans to the Corporate Sector

Q1 What are the purposes of the Practice Note?

A1 The HKMA issues Practice Note and Guiding Paper from time to time. They aim at promoting sound risk management practices in the banking industry. This particular Practice Note elaborates the practical aspects of credit risk management principles stipulated in the HKMA Supervisory Policy Manual, taking into account good credit risk management practices that the HKMA identified in the course of its on-going supervision. As such, the Practice Note does not constitute new regulatory requirements and AIs will continue to be assessed on the basis of whether their systems of controls commensurate with the complexity and scale of their business. AIs should not regard the Practice Note as an exhaustive list of good practices that caters for all bank-specific circumstances. AIs can, having regard to their own specific circumstances (e.g. financial strength, risk profile, risk appetite) adopt alternative practices, provided that they can demonstrate to the HKMA that such alternative practices provide similar degree of effectiveness in managing the relevant risks.

Q2 Is the HKMA preparing to revise the Practice Note?

A2 Yes, the HKMA intends to bring the Practice Note up-to-date regularly so as to share with the industry good practices that cater for the evolving and emerging risks to the banking industry. In order to ensure that industry views can be appropriately taken into account, the HKMA considers it critical to for the industry to establish a credit risk management committee to work together with the HKMA in enhancing and updating the Practice Note. In this regard, the HKMA is discussing with relevant industry associations and will inform AIs of the development in due course.

Q3 Can a particular type of loan be scoped out from the Practice Note?

A3 The HKMA does not view the implementation of the Practice Note as a scoping issue. As explained in the answer to Q1, the Practice Note does not constitute new supervisory requirements on AIs. It only provides guidance in respect of good risk management practices. AIs should have put in place effective risk management practices with or without the issuance of the Practice Note, and they are encouraged to carefully study the Practice Note with a view to further enhancing their current practices where applicable. As indicated in paragraph 18 of the Practice Note, the HKMA is ready to consider alternative practices currently adopting or will be adopted by AIs that are equally effective in managing the relevant risks.

Q4 Can the implementation date of the Practice Note be deferred?

A4 Prudent and effective internal systems and practices for managing credit risk is one of the core requirements stimulated in the HKMA Supervisory Policy Manual and other relevant documents. Improvement in AIs' risk management practices is an on-going process, and AIs should have already put in place robust practices to comply with such requirements even without the issuance of the Practice Note. As such, implementation date is not an issue. Nevertheless, for the avoidance of doubt, the HKMA has taken out the implementation date from the Practice Note to better reflect the ongoing nature of the subject.

Q5 Can the HKMA clarify the scope of responsibility of AIs' compliance function?

A5 The HKMA notes that AIs may have varying structure in respect of how business, compliance, risk management, and internal audit functions interact and coordinate. For the avoidance of doubt, the HKMA sets out its expectations of the role of "compliance function" rather than that of "compliance department" or "compliance officer". AIs will normally optimise its systems of control by putting in place different control processes and check steps in all three lines of defence. The HKMA takes a holistic approach in reviewing the effectiveness of the relevant controls, focusing on whether there are clear gaps resulting in deficiencies in avoiding, detecting, and reporting cases of non-compliance.