

Process Review Committee

Annual Report to the Financial Secretary 2020-2021

I. GENERAL INFORMATION

Background of establishment

1.1 The Payment Systems and Stored Value Facilities Ordinance (“PSSVFO”) empowers the Monetary Authority (“MA”) to designate and oversee clearing and settlement systems (“CSSs”) that are material to the monetary or financial stability of Hong Kong or to its functioning as an international financial centre or having regard to matters of significant public interest. The purpose of the PSSVFO is, among other things, to promote the general safety and efficiency of designated CSSs.

1.2 To date, six CSSs have been designated under the PSSVFO. They are:

- (a) the Central Moneymarkets Unit (“CMU”)
- (b) the Hong Kong Dollar Clearing House Automated Transfer System (“HKD CHATS”)¹
- (c) the US Dollar Clearing House Automated Transfer System (“USD CHATS”)
- (d) the Euro Clearing House Automated Transfer System (“EUR CHATS”)
- (e) the Renminbi Clearing House Automated Transfer System (“RMB CHATS”)²
- (f) the Continuous Linked Settlement (“CLS”) System

1.3 The system operators (“SOs”) and settlement institutions (“SIs”) of the designated CSSs are set out in the following table:

¹ Including the Faster Payment System (“FPS”) which was launched on 17 September 2018 as extensions of the HKD CHATS and RMB CHATS respectively to provide 7 x 24 real-time clearing and settlement services for HKD and RMB retail payment transactions.

² The FPS also supports RMB transactions. See footnote 1.

Table 1:

Designated CSS	System operator	Settlement institution
CLS System	CLS Bank	CLS Bank
CMU	HKMA	Nil
HKD CHATS	HKICL*	HKMA
USD CHATS		The HongKong and Shanghai Banking Corporation Limited
EUR CHATS		Standard Chartered Bank (Hong Kong) Limited
RMB CHATS		Bank of China (Hong Kong) Limited

* The Hong Kong Monetary Authority (HKMA) and the Hong Kong Association of Banks each own 50% of the Hong Kong Interbank Clearing Limited (HKICL)

1.4 The HKMA is the owner/operator of HKD CHATS and the CMU, and has a 50% stake in the HKICL, which is the system operator of the four CHATS systems and provides computer support to the CMU. Of the six designated CSSs, the CLS System is the only one in which the HKMA does not have an interest. The CLS System is subject to the supervision of the Federal Reserve Bank of New York (“FRBNY”) and is exempted under section 11 of the PSSVFO from certain requirements under the Ordinance. FRBNY leads a CLS Oversight Committee with representatives from all of the jurisdictions (including Hong Kong) whose currencies are members of the CLS system, and the HKMA exercises oversight of CLS through participation in this committee. The HKMA exercises on-going oversight of the five local designated CSSs: the CMU, HKD CHATS, USD CHATS, EUR CHATS and RMB CHATS. Some of these designated CSSs have established links with overseas payment or securities settlement systems to facilitate cross-border transactions, for example, the payment-versus-payment (“PvP”) and the delivery-versus-payment (“DvP”) links between USD CHATS and RENTAS³ in Malaysia, the PvP link between USD CHATS and BI-RTGS⁴ in Indonesia, the PvP link between USD CHATS and BAHTNET⁵ in Thailand, and the DvP link between HKD CHATS and

³ RENTAS is the RTGS clearing and settlement system for inter-bank fund transfer and scripless securities trading in Malaysia.

⁴ BI-RTGS is the RTGS clearing and settlement system for inter-bank fund transfer in Indonesia.

⁵ BAHTNET is the RTGS clearing and settlement system for large value fund transfer between financial institutions or other organisations in Thailand.

BOJ-NET JGB Services⁶ in Japan. Although these overseas systems are not overseen by the HKMA, the HKMA oversees these external links in cooperation with the respective home overseers.

1.5 The HKMA has implemented a number of measures to address the potential or perceived conflict of interest arising from the HKMA being the SO or SI of certain CSSs and also the overseer of designated CSSs. These include a clear segregation of duties within the HKMA and the promotion of transparency in the designation and oversight processes. In addition, the Process Review Committee (“PRC”), a non-statutory committee, was established by the Chief Executive of the Hong Kong Special Administrative Region (“CE/HKSAR”) in December 2004 to review the processes and procedures adopted by the HKMA in applying oversight standards on designated CSSs to ensure that the same set of standards is applied to all designated CSSs, whether or not the HKMA has an interest in them.

Scope of work and terms of reference

1.6 The terms of reference of the PRC are:

- (a) to review and advise the HKMA upon the adequacy of the HKMA’s internal operational procedures and guidelines for applying the standards set under the PSSVFO to those designated systems in which the HKMA has a legal or beneficial interest;
- (b) to receive and consider periodic reports from the HKMA on all completed or discontinued files in respect of alleged non-compliance of the PSSVFO by those designated systems in which the HKMA has a legal or beneficial interest; and
- (c) to submit annual reports and, if appropriate, special reports on designated systems in which the HKMA has a legal or beneficial interest, to the Financial Secretary.

⁶ BOJ-NET JGB Services is the Japanese government securities settlement system in Japan.

1.7 The PRC has agreed that, in discharging its functions, it should focus on whether there were any discrepancies in the HKMA’s oversight of designated CSSs in which the HKMA has an interest, as compared with other systems. In other words, the PRC would review the processes and procedures adopted by the HKMA to ensure that the same oversight standards were applied to all designated CSSs. The PRC also agreed that its scope could be expanded in future if the HKMA had a legal or beneficial interest in a designated retail payment system (“RPS”) or a licensed stored value facility (“SVF”) under the PSSVFO. This is consistent with the policy intention of the establishment of the PRC in 2004. So far, the HKMA had not acquired any interest in any designated RPS or licensed SVF under the PSSVFO.

1.8 The Financial Secretary may cause the reports submitted by the PRC to be published, subject to relevant confidentiality requirements.

Membership of the PRC

1.9 The PRC is in its sixth term of service. Members of the PRC are appointed by the CE/HKSAR in their personal capacity for a three-year term from 1 December 2019 to 30 November 2022. The membership of the PRC as at 30 November 2021 was:

Chairman

Professor Francis Chin Yuk-lun

Emeritus and Honorary Professor
Department of Computer Science
The University of Hong Kong

Members

Ms Annie Chan Wai-hing

Managing Director
Annie Chan & Associates Limited

Mr Jack Chan

Chairman, China
Regional Managing Partner, Greater China
EY

Ms Sabita Prakash
Managing Director
Asia Debt Management Hong Kong Limited

Mr Michael Shue
Managing Director - Trust Services
Tricor Services Limited

II. HIGHLIGHTS OF THE WORK OF THE PRC

2.1 This is the 17th Annual Report of the PRC, which covers the work of the Committee from 1 December 2020 to 30 November 2021. This is also the second annual report for the current term of the PRC.

Meetings held and major deliberations of the PRC

2.2 The PRC held two meetings in 2021. At the first meeting in June 2021, Members reviewed the regular report covering the oversight activities of the HKMA from December 2020 to March 2021 and were briefed on the oversight activities conducted by the HKMA from April to June 2021. In particular, Members discussed and noted how the HKMA handled abnormal events encountered by the designated CSSs, the implications of these events and the follow-up actions taken.

2.3 During the meeting in June 2021, Members noted that the operations of the designated CSSs continued to remain safe and efficient under COVID-19. More granular information and analysis about the underlying causes of the past incidents were shared with Members who noted that the incidents were generally different in nature and most of them were beyond the control of the designated CSSs. Members were briefed on a thematic review on risk management framework (RMF) of a designated CSS and noted that the review result is generally satisfactory with recommendations proposed to further strengthen the RMF by refining its risk appetite categories and documentation of risk management lifecycle.

2.4 At the second meeting held in December 2021, Members reviewed the regular report covering the period from July to September 2021 and was briefed on the oversight activities conducted by the HKMA from October to November 2021. During the meeting, Members were briefed on the FPS system relocation and upgrade incident, and the way that the incident was handled. Members also discussed the drafting of the Committee's 17th Annual Report to be submitted to the Financial Secretary.

2.5 As agreed by Members, regular reports covering the HKMA's oversight

activities were sent to Members for review by circulation between meetings. If Members have questions about the reports, they may raise them with the Secretary of the Committee. Subject to the agreement of the Chairman, the questions will be discussed at the next regular meeting or, if needed, at a special meeting. During 2021, four regular reports had been circulated to Members for review. Members noted that the HKMA had met the performance benchmarks for oversight activities.

Comments and recommendations of the PRC

2.6 The format of the regular report and the accompanying oversight activities management reports were designed based on suggestions from Members. During the year, Members reviewed four regular reports and 36 accompanying oversight activities management reports covering the period from December 2020 to November 2021. Statistics showing the oversight activities contained in each regular report under the review of the PRC are summarised below:

Table 2: Oversight activities of HKMA under the review of PRC from December 2020 to November 2021

HKMA's oversight activities conducted during the quarter	1st Regular Report (Dec- Mar)	2nd Regular Report (Apr-Jun)	3rd Regular Report (Jul-Sep)	4th Regular Report (Oct-Nov)
Processing of monthly return submitted by SO/SI	24	18	18	12
Granting approval to changes in operating rules	4	8	0	1
Vetting of changes in particulars of SO/SI	10	7	3	5
Reviewing of ad-hoc information submitted by SO/SI	73	39	37	27
Conducting on-site examinations	0	0	0	0
Handling of abnormal events/ production incidents	12	6	3	10
Handling of possible	0	0	0	0

contravention cases				
Holding of meetings with management of SO/SI	6	0	0	0

2.7 At the meeting in November 2021, Members discussed the draft 2020 - 2021 PRC Annual Report. Members agreed to adopt the same publication approach as previous annual reports, and comments from Members were incorporated in the Report. The PRC would propose to the Financial Secretary that the annual report be published in its entirety and be posted on the website of the HKMA for wider dissemination to the public in the interests of promoting transparency and accountability.

III. CONCLUSION AND WAY FORWARD

3.1 The PRC reviewed four regular reports and 36 accompanying oversight activities management reports covering the period from December 2020 to November 2021. No complaints were received from the SOs and SIs. The review covered, among other things, submissions by the HKMA on its processing of 72 monthly returns and 25 cases of changes in particulars; granting of approvals to 13 changes in operating rules; handling of 31 abnormal events; reviewing of 176 submissions of ad-hoc information; and holding of 6 meetings with the management of the SOs and the SIs.

3.2 The PRC was not aware of any cases where the HKMA had not followed duly the internal operational procedures, or where the HKMA had not been procedurally fair in carrying out its oversight activities across different designated systems.

3.3 The PRC will continue to review the processes and procedures adopted by the HKMA in overseeing the existing designated CSSs and, where appropriate, any additional designated systems or licensed SVF under the PSSVFO in which the HKMA has a legal or beneficial interest.