



HONG KONG MONETARY AUTHORITY  
香港金融管理局

Our ref: B1/21C  
B1/15C  
B9/124C

6 July 2017

The Chief Executive  
All authorized institutions

Dear Sir/Madam,

**Supervisory Policy Manual module RE-1 “Recovery Planning” – further guidance for overseas-incorporated AIs with branch operations in Hong Kong and smaller locally-incorporated AIs**

I am writing to inform you of the third “wave” of implementation of the Supervisory Policy Manual module RE-1 “Recovery Planning” (SPM RE-1)<sup>1</sup> and provide further guidance to authorized institutions (AIs) covered in this wave.

As provided in SPM RE-1, all AIs are expected to develop and maintain a recovery plan commensurate with the nature, scale, significance and complexity of their operations. To date the majority of locally incorporated licensed banks have prepared recovery plans and submitted their plans to the Hong Kong Monetary Authority (HKMA) via two separate “waves”. The third “wave” of implementation of SPM RE-1 will cover overseas-incorporated AIs with branch operations in Hong Kong (branches) and smaller, less complex locally-incorporated AIs (smaller AIs). AIs in this latest wave will be individually notified of the timeline for submitting recovery plans and related information to the relevant Banking Supervision Department case teams.

To facilitate the development of recovery plans, a set of further guidance is provided at [Annex](#). This further guidance should be read in conjunction with SPM RE-1.

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<sup>1</sup> <http://www.hkma.gov.hk/media/eng/doc/key-functions/banking-stability/supervisory-policy-manual/RE-1.pdf>

Should you have any questions regarding this circular and the guidance, please do not hesitate to contact Ms Echo Chan at [ewhchan@hkma.gov.hk](mailto:ewhchan@hkma.gov.hk) and Mr Leo Lai at [lchlai@hkma.gov.hk](mailto:lchlai@hkma.gov.hk).

Yours sincerely,

Daryl Ho  
Executive Director (Banking Policy)

Encl

cc: Ms Eureka Cheung, FSTB  
Mr Yue Yi, Chairman, The Hong Kong Association of Banks  
Mr Lee Huat Oon, Acting Chairman, The DTC Association

**Guidance on SPM RE-1 for overseas-incorporated AIs with branch operations in Hong Kong and smaller locally-incorporated AIs****a) Scope of application (SPM RE-1 section 1.4)**

For a branch with significant operations in the context of operations of the banking sector in Hong Kong including the provision of significant or critical functions in Hong Kong,<sup>1</sup> in most cases a local recovery plan, drawing on the group recovery plan as appropriate, will need to be prepared alongside its group plan. The local recovery plan should be tailored for local operations and include Hong Kong specific information. If a branch has limited operations locally in the context of the wider group, there may be considerable reliance on group plan and actions.<sup>2</sup> However, the branch should demonstrate to the HKMA how the group recovery plan and options may be applied effectively to address stress events that pose a risk to the branch's viability.<sup>3</sup> If the HKMA is not satisfied that the group plan is sufficient for the Hong Kong operations, the HKMA may request the branch to incorporate Hong Kong specific information in the group plan. Branches should discuss the proposed local and group procedures with the HKMA.

If a foreign banking group has both a banking subsidiary and a branch operation in Hong Kong, it is preferable that one single plan be produced covering both operations considering the potential financial, operational and managerial interaction between the banking subsidiary and the branch and the need for a coordinated response by the banking subsidiary and the branch for the operations in Hong Kong in crisis.

In all cases, it would not be considered appropriate, for example, if a banking

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<sup>1</sup> Critical functions, according to paragraph 1.1.5 of SPM RE-1, are functions performed by a financial institution for individuals or corporates in circumstances where disruption to the provision of such functions, caused by the failure of the financial institution, is considered likely to have adverse effects on financial stability or on the functioning of the real economy

<sup>2</sup> Paragraph 1.4.12 of SPM RE-1, Branches may also rely on, where appropriate, regional recovery plans and recovery planning process and frameworks

<sup>3</sup> The essential considerations include, but are not limited to: (i) demonstrating how recovery actions at the group level may be triggered by the occurrence of severe stress events in Hong Kong; (ii) describing the process for activating the recovery plan for the AI, specifying the local Hong Kong management's role and involvement in the recovery planning process; and (iii) illustrating how the recovery options are expected to restore the financial soundness and viability of operations in Hong Kong

subsidiary and a branch solely rely on the group plan where the group plan does not adequately reflect the group's local operations or market specificities. If there is a divergence in the direction of the local plan and the group plan, the AI should consider the materiality of the issue. The AI may consult the HKMA on its proposed steps to resolve the matter.

For smaller AIs, with relatively fewer and simpler business, the recovery options will tend to be less complex and potentially easier to implement. Accordingly, a simpler recovery plan may be sufficient to meet the HKMA's requirements. AIs should at a minimum, demonstrate that their recovery plan covers the key elements set out in this guidance.

**b) Governance structure and oversight (SPM RE-1 section 2.2)**

*Development, review, approval and ongoing maintenance of recovery plan*

For branches, regardless of significance of the operations, local senior management should have a key role in the governance of recovery planning to ensure that local specificities are taken into account.<sup>4</sup> Personnel from the local Hong Kong management may be assigned responsibility for delivering elements of the recovery plan and to act as the main point of contact for the HKMA regarding recovery planning matters.<sup>5</sup> It may also be helpful if there is a process established to enable the head office to oversee the development of the Hong Kong specific elements of the recovery plan.

For a branch with significant operations in the context of the operations of the banking sector in Hong Kong, at the initial formulation of the branch's recovery plan, the governance body at the Head/Regional Office overseeing the Hong Kong operations, the local Hong Kong management and, where appropriate, the Board of Directors of the AI should be involved in the review and approval of the recovery plan. Thereafter the branch, together with the Head Office/Regional Office, may assess the best approach for ongoing annual reviews and approvals of the branch's recovery plan (such as delegating the review to an appropriate committee, etc.).

For smaller AIs, where the key metrics have not changed materially year on year, the AI's board may decide at the annual review of the recovery plan that

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<sup>4</sup> Paragraph 2.2.4 of SPM RE-1

<sup>5</sup> Paragraph 2.2.2 of SPM RE-1

the information, plans and triggers from the previous year are still appropriate. The AI should notify the HKMA once the review is complete and the AI will be expected to demonstrate to the HKMA's satisfaction that such an approach is appropriate for their recovery planning purposes.

#### *Monitoring process for triggering a recovery plan*

Branches and smaller AIs may consider leveraging existing systems to meet the monitoring and escalation requirements in respect of recovery triggers.<sup>6</sup> The monitoring process should be embedded in the risk management framework and delegation of roles and responsibilities should be clearly identified.

#### *Activating a recovery plan*

Branches and smaller AIs may leverage existing reporting and coordination functions to escalate trigger events, assess the AI's viability and coordinate the crisis management process. In any case, documented procedures for activating a recovery plan should be in place, specifying the individuals involved in the activation of the recovery plan (branches should do so at both group and branch level<sup>7</sup>).

#### **Menu of recovery options (SPM RE-1 section 2.3)**

AIs should include complete disposal or full sale as options, which should specify the conditions for execution and steps taken.<sup>8</sup>

For branches, recovery options may largely reflect group recovery options with the group being responsible for executing recovery options.<sup>9</sup> Nevertheless, branches should consider the credibility and effectiveness of group recovery options to restoring the financial soundness and viability of the local operations. Branches should outline the conditions for execution of recovery options, such as the steps, estimated time and implementation risks (e.g. cross border considerations) as well as associated risks from options not executed by the group that may, directly or indirectly, impact the branch.

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<sup>6</sup> Paragraphs 2.2.6 and 2.2.7 of SPM RE-1

<sup>7</sup> Paragraphs 2.2.8 and 2.2.9 of SPM RE-1

<sup>8</sup> Paragraph 2.3.6 of SPM RE-1

<sup>9</sup> Paragraph 2.3.7 of SPM RE-1

To the extent that a branch has any local recovery options that are independent from the group, it should detail the interaction between recovery options at the local level and the group’s overall recovery planning process, including activation and escalation mechanisms. A branch with significant operations may also consider the feasibility of independent, local recovery options if appropriate.

For smaller AIs, the range of recovery options could be limited, particularly if the AI has few lines of business (e.g. a part disposal may not be a credible recovery option as it may imperil the AI’s viability) or other available measures may not be able to return the AI to a viable position in the case of a severe crisis. The AI, in preparing its recovery plan, will still need to consider a range of appropriate recovery options that it may effectively deploy.

**c) Recovery triggers (SPM RE-1 section 2.4)**

Branches and smaller AIs may wish to develop recovery triggers based on their existing internal early warning indicators (“EWIs”), generally embedded in their risk management frameworks.<sup>10</sup> Such triggers should be carefully calibrated to the risks facing the AI and should allow the AI sufficient time to take corrective action. Branches and smaller AIs should alert the HKMA of an occurrence (or the expected occurrence) of a trigger event, as well as the subsequent triggering of a recovery plan, if any, as it relates directly or indirectly to the viability of the AI’s or branch’s operations in Hong Kong.<sup>11</sup>

Generally recovery triggers comprise a mix of qualitative and quantitative (liquidity and capital) triggers that are most relevant to the AI.<sup>12</sup> For branches, it may only be practicable to develop quantitative triggers around liquidity requirements. Branches may wish to consider whether it would be feasible to develop more granular recovery triggers around its existing liquidity framework.

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<sup>10</sup> Paragraph 2.4.3 of SPM RE-1, EWIs are generally used for risk management purposes, but may form a useful ‘foundation’ on which to develop recovery triggers

<sup>11</sup> Paragraph 2.2.11 of SPM RE-1

<sup>12</sup> Paragraph 2.4.3 of SPM RE-1

**d) Stress scenarios and stress testing (SPM RE-1 section 2.6)**

In conducting stress testing and constructing stress scenarios specific to Hong Kong operations, branches may rely on the existing group recovery framework if appropriate. However, a branch should assess the suitability of the group recovery stress scenarios for recovery planning purposes, particularly whether the stress scenarios appropriately test the risks and vulnerabilities in the context of its Hong Kong operations.<sup>13</sup> If the group recovery stress scenarios are not appropriate for the local context or are not sufficiently severe to support effective recovery planning at the local level, the branch should consider developing at least one stress scenario which will sufficiently test the branch's ability and mechanism to respond to a stress event.

It is recognised that smaller AIs may have limited capacity to produce the full range of scenarios specified in SPM RE-1.<sup>14</sup> Smaller AIs may consider conducting one stress test based on an appropriate stress scenario which is most reflective of the AI's risk profile and its operations. Smaller AIs may also use qualitative assessments to complement simple sensitivity and scenario analyses of specific risks for recovery planning purposes.

**e) Communication plan (SPM RE-1 section 2.10)**

Local communication needs must be considered to effectively support local management in crisis and to assist with coordination between the group and branch staff. Where a branch relies on a group communication plan, local management should demonstrate that the group communication plan is locally applicable. The branch should consider documenting key stakeholders involved in local communication and interactions with the group communication plan.

**End**

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<sup>13</sup> Paragraphs 1.4.11, 1.4.12, 2.6.5, and 2.6.6 of SPM RE-1

<sup>14</sup> Paragraph 2.6.4 of SPM RE-1