



**CB(1)145/09-10(04)**

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23 October 2009

By e-mail: [yhcheung@legco.gov.hk](mailto:yhcheung@legco.gov.hk)

Ms Rosalind Ma  
Clerk to Panel  
Legislative Council  
Legislative Council Building  
6 Jackson Road  
Hong Kong

Dear Ms Ma

Panel on Financial Affairs  
Meeting to be held on 2 November 2009

Thank you for your letter addressed to our Chairman dated 15 October 2009.

During the past months, the Hong Kong Association of Banks (HKAB) has assisted, through its Retail Banking Taskforce on Sale of Investment Products, the Hong Kong Monetary Authority (HKMA) in the implementation of the audio recording requirements and other measures to enhance the distribution process of investment products to the retail investing public (Enhanced Measures). As summarised in Annex 1, most of the Enhanced Measures have been implemented by the retail banking sector for a short period of time. In particular, the full implementation of the measures to physically segregate retail investment activities from ordinary banking business activities at bank branches (Physical Segregation Measures) across the retail banking sector was required by 2 October 2009.

It is understandable that both banks and their customers need time to adjust to the enhanced distribution process. HKAB will endeavour to facilitate this process by collecting feedback through member banks and raising and discussing any issues identified with the HKMA as the Enhancement Measures are being fully rolled out. This continuous dialogue between the HKMA and the industry should also facilitate the overall review of the enhanced distribution process in light of working experience. Pending this comprehensive review, HKAB is studying the proposals, including those relating to the audio recording requirement of the sales process, set out in the consultation paper released by the Securities and Futures Commission (SFC) on 25 September 200

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*Chairman* The Hongkong and Shanghai Banking Corporation Ltd  
*Vice Chairmen* Standard Chartered Bank (Hong Kong) Ltd  
Bank of China (Hong Kong) Ltd  
*Secretary* Jennifer Cheung

主席 香港上海匯豐銀行有限公司  
副主席 渣打銀行(香港)有限公司  
中國銀行(香港)有限公司  
秘書 張學欣



regarding pre-sale documentation, disclosure at the point of sale and after, selling practices and post-sale cooling-off period. We anticipate that HKAB will provide comments to the SFC on the consultation paper on behalf of members by 31 December 2009.

Given that the Enhanced Measures are only introduced for a short period of time as explained above, HKAB does not intend to participate in the upcoming Panel meeting on 2 November 2009 but hopes that the information provided in the Annex to be useful for discussion by the Panel.

Yours sincerely

A handwritten signature in black ink, appearing to be "Jennifer Cheung", is written over a horizontal line.

Jennifer Cheung  
Secretary

Enc.

**Circular of Hong Kong Monetary Authority (HKMA) dated 9 January 2009 to all Authorised Institutions (AIs) titled “Report of the HKMA on Issues Concerning the Distribution of Structured Products Connected to Lehman Group Companies” (HKMA 09JAN09 Circular)**

**Summary of Progress of Implementation by Retail Banking Sector**

Implementation Progress	Reference Document
Retail Banking Taskforce on Sale of Investment Products of HKAB (Retail Banking Taskforce) discussed and agreed with the HKMA on the implementation details of Recommendations 5, 10, 11 12, 13, 14, 15, 17 and 18 set out in HKMA 09JAN09 Circular applicable to investment products that fall within the scope of regulated activities under the Securities and Futures Ordinance (SFO).	Agreed implementation details are documented in the circular of the HKMA issued to all AIs dated 25 March 2009 (HKMA 25MAR09 Circular) (See Attachment 1)  Attachment 1.pdf
HKAB informed members of the public of the new banking practice of audio recording the process of conducting customer risk profile assessment and the sales of investment products to retail investors, in line with the audio recording requirement of 25MAR09 HKMA Circular.	HKAB press release dated 19 June 2009 (See Attachment 2). Visit <a href="http://www.hkab.org.hk/DisplayWhatsNewsAction.do?ss=1&amp;id=1068&amp;lang=en">http://www.hkab.org.hk/DisplayWhatsNewsAction.do?ss=1&amp;id=1068&amp;lang=en</a> to view the video clip mentioned in the press release.  Attachment 2.pdf
Retail banking Taskforce discussed and agreed with the HKMA on the distribution of investment products which are not regulated by the SFO, given the requirements of the HKMA 25MAR09 circular.	Agreed details are documented in the circular of the HKMA issued to all AIs dated 13 July 2009 (See Attachment 3).  Attachment 3.doc
HKAB informed members of the public that with effect from 30 September 2009, banks would enhance the signage systems at their branches in order to make “investment corners” distinct from the general banking halls, with illustrative examples of “investment corners” and the same areas before enhancements at real branch settings.	HKAB press release dated 25 September 2009 (See Attachment 4). Visit <a href="http://www.hkab.org.hk/DisplayWhatsNewsAction.do?ss=1&amp;id=1085&amp;lang=en">http://www.hkab.org.hk/DisplayWhatsNewsAction.do?ss=1&amp;id=1085&amp;lang=en</a> to view the illustrative examples of “investment corners” mentioned in the press release.  Attachment 4.pdf
HKAB informed members of the public that the initial launch of the Physical Segregation Measures	HKAB press release dated 2 October 2009 (See Attachment 5).

by member banks was generally smooth on 2 October 2009, the first business day whereby full implementation of the Physical Segregation Measures across the retail banking sector was required.



Attachment 5.pdf



HONG KONG MONETARY AUTHORITY  
香港金融管理局

Banking Supervision Department

銀行監理部

Our Ref.: B1/15C

25 March 2009

The Chief Executive  
All Authorized Institutions

Dear Sir/Madam,

**Implementation of recommendations in the HKMA's Report on Issues Concerning the Distribution of Structured Products Connected to Lehman Brothers ("the HKMA's Report")**

Further to my circular of 9 January 2009 requesting all Registered Institutions (RIs) to implement a number of recommendations in the HKMA's Report, the HKMA and the Hong Kong Association of Banks (HKAB) have, through the Retail Banking Taskforce on Sale of Investment Products established by the HKAB, further discussed and worked out the implementation details for these recommendations. All RIs are expected to implement these recommendations according to the implementation details set out in the two Annexes to this letter. The HKMA will in due course conduct onsite examination to review RIs' implementation of these recommendations.

If you have any questions on the above, please get in touch with your usual supervisory contact at the HKMA.

Yours faithfully,

Nelson Man  
Executive Director  
(Banking Supervision)

Encl.

c.c. Chairman, Hong Kong Association of Banks  
Chairman, The Deposit-taking Companies Association

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

Recommendations <sup>1</sup>	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>

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

Recommendations <sup>1</sup>	Requirement and Implementation Timetable	Detailed Guidance on Implementation (Timeline of implementation follows the original timetable unless otherwise stated)
		<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"> <li>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.</li> <li>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.</li> </ol>

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

	<b>Recommendations<sup>1</sup></b>	<b>Requirement and Implementation Timetable</b>	<b>Detailed Guidance on Implementation</b> (Timeline of implementation follows the original timetable unless otherwise stated)
			<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"> <li>• 100% check on risk assessments with customers graded above the medium risk category</li> <li>• 100% check on risk assessments involving vulnerable</li> </ul>

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

Recommendations <sup>1</sup>	Requirement and Implementation Timetable	Detailed Guidance on Implementation (Timeline of implementation follows the original timetable unless otherwise stated)
<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"> <li>• Sample check (at least 20%) on risk assessments of all other customers graded above the lowest risk category</li> <li>• The independent review should cover <u>all</u> sales staff who have performed assessment of customers' risk profile</li> <li>• 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.</li> </ul> <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> <ol style="list-style-type: none"> <li>(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</li> </ol>

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

Recommendations	Requirement and Implementation Timetable	Detailed Guidance on Implementation (Timeline of implementation follows the original timetable unless otherwise stated)
		<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>
<p>13 The regulatory requirements at point of sale should be reviewed with a view to introducing mandatory requirements for the audio-recording of</p>	<p>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>	<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>

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

Recommendations <sup>1</sup>	Requirement and Implementation Timetable	Detailed Guidance on Implementation (Timeline of implementation follows the original timetable unless otherwise stated)
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

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

Recommendations <sup>1</sup>	Requirement and Implementation Timetable	Detailed Guidance on Implementation (Timeline of implementation follows the original timetable unless otherwise stated)
<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>

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

Recommendations <sup>1</sup>	Requirement and Implementation Timetable	Detailed Guidance on Implementation (Timeline of implementation follows the original timetable unless otherwise stated)
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 to 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.

<sup>1</sup> The recommendation numbers are those referred to in paragraphs 8.1 to 8.50 of the HKMA's Report.

Registered Institutions are required to formulate a plan on how to implement the following recommendations for discussion with the HKMA by the end of March 2009

Recommendations	Implementation plan agreed by the HKMA and the banking industry
<p><b>Recommendation 10</b></p> <p>AIs, which are registered institutions, continue to be permitted to undertake securities business (including selling investment products to retail customers), but steps should be taken to ensure clearer differentiation between traditional deposit-taking activities and retail securities business, including:</p> <ul style="list-style-type: none"> <li>- physical segregation of AIs' retail securities business from their ordinary banking business</li> <li>- a requirement that staff involved in selling investment products to retail customers should not be involved in ordinary banking business</li> <li>- a requirement that AIs make clear, through physical signs and warnings, the distinction between deposits and investments and particularly the risks attached to the latter</li> <li>- a requirement that there be complete information separation between a retail customer's deposit accounts and his investment accounts and a</li> </ul>	<p>Following discussions with the Retail Banking Taskforce on Sale of Investment Products ("the Retail Banking Taskforce") of the Hong Kong Association of Banks (HKAB), the HKMA sets out below the implementation arrangement for this recommendation:</p> <ol style="list-style-type: none"> <li>1. RIs will set up designated "investment corner" with proper "signage" in the banking hall away from the general banking area. All sales of investment products must be conducted in the investment corner by qualified staff. Staff in the investment corner may provide full banking services to customers provided that the customer has provided consent for the RI to access and utilise his/her deposit information for investment and wealth management purposes.</li> <li>2. For existing active investment customers, banks are not required to seek positive consent from these customers for accessing and utilising their deposit information in the investment corner. However, banks should notify these customers of the new segregation arrangement and provide them with an option to refuse the bank's utilisation of their deposit information for sales/solicitation by the bank staff in the investment corner.</li> <li>3. For (i) existing inactive investment customers, (ii) existing customers who have previously lodged complaints alleging mis-selling of investment products by the RI and (iii) new customers, the RI will need to seek specific consent from these customers prior to offering full banking services at the investment corner.</li> <li>4. RIs should ensure that a robust system is in place to ensure that both customers and</li> </ol>

Recommendations	Implementation plan agreed by the HKMA and the banking industry
<p>prohibition on an AI's making use of deposit-related information to target and channel retail customers into investment activities.</p>	<p>bank staff are aware of the differentiation between the designated "investment corner" and the general banking area, and there will be procedures in place to ensure that customers will not be lured into the "investment corner" but use it only at their own initiatives.</p> <p>5. RIs may continue to display marketing materials at bank halls as they are doing currently. However, as this may be considered as part of the solicitation process, care must be taken to handle follow-up enquiries and/or sales to persons who are not yet a customer of the bank to avoid breaching the cold-calling rules. If customers, after reading the marketing materials, want to know more about the investment products or show interests to buy them, then normal suitability procedures must be conducted (as set out in SFC Code of Conduct 5.1 and 5.2 and FAQs on suitability obligations), and under the new segregation arrangement, should be done at the investment corner.</p> <p>6. The "physical segregation" requirement would not be applicable to general phone banking on the basis that (i) it will be audio recorded and (ii) complicated and high risk investment products will not be marketed or solicited to customers through this channel. For the avoidance of doubt, phone banking between relationship managers and their customers will follow all procedures applicable to the investment corner.</p> <p>7. Taking into account the time needed for operation and system changes, RIs are expected to achieve implementation by 30 September 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. For the purpose of consent seeking, customers who open investment accounts on or after RI's implementation of this segregation arrangement will be considered "new customers".</p>
<p><b>Recommendation 11</b></p> <p>- the above forms of segregation should apply to AIs' insurance activities and other investment</p>	<p>The HKMA and the HKAB's Retail Banking Taskforce agree that the above arrangement will apply to RIs' insurance activities and other investment activities, except for the following list of general insurance and traditional life insurance products on the basis that customers could generally distinguish them from deposit products and</p>

Recommendations	Implementation plan agreed by the HKMA and the banking industry
<p>activities.</p>	<p>that cooling-off period applies for traditional life insurance products. For life insurance products, RIs should include the following risk disclosure statement:</p> <p><u>Specimen Warning Statement</u></p> <p><i>"[Plan name] is an insurance plan with a savings element. Part of the premium pays for the insurance and related costs. If you are not happy with your policy, you have a right to cancel it within the cooling off period and obtain a refund of any premiums paid. A written notice should be received by us within the cooling off period (that is, 21 days from the date of the application, 14 days from the date of issue of the policy, or 5 days from the date of delivery of the policy/a notice (informing you/your representative about the availability of the policy and expiry date of the cooling-off period), whichever is later). After the expiration of the cooling off period, if you cancel the policy before the end of the term, the projected total cash value may be less than the total premium you have paid."</i></p> <p><u>List of general insurance and traditional life insurance products that may be sold outside the investment corner</u></p> <p>(a) General Insurance</p> <ul style="list-style-type: none"> <li>▪ Accident</li> <li>▪ Sickness</li> <li>▪ Land vehicles</li> <li>▪ Fire and natural forces</li> <li>▪ Damage to property</li> <li>▪ Motor vehicle liability</li> <li>▪ General liability</li> <li>▪ Credit</li> <li>▪ Miscellaneous financial loss</li> <li>▪ Legal expenses</li> </ul> <p>(b) Traditional Life Insurance Products</p> <ul style="list-style-type: none"> <li>▪ Life and annuity (including endowment)</li> <li>▪ Permanent health</li> </ul>

<b>Recommendations</b>	<b>Implementation plan agreed by the HKMA and the banking industry</b>
	<ul style="list-style-type: none"><li data-bbox="1227 308 1870 343">▪ Retirement scheme management (except MPF products)</li></ul>



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Press Release

**New Audio Recording Requirement Pertaining to Sales of Investment Products**

19 June 2009 - This video clip explains the practice of banks to audio record the process of conducting customer risk profile assessment and the sales of investment products to retail investors. This practice aligns with the audio recording requirement of the circular of the Hong Kong Monetary Authority issued to All Authorised Institutions dated 25 March 2009 regarding the sales of investment products.

<http://www.hkab.org.hk/DisplayWhatsNewsAction.do?ss=1&id=1068&lang=en>

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新聞稿

2009年6月19日

**零售銀行於進行投資產品銷售時之錄音要求**

此短片說明客戶在銀行進行風險狀況評估時及於整個銷售過程中將會進行錄音。此乃因應香港金融管理局於2009年3月25日所發出之通告要求所有註冊機構實施之錄音要求。

<http://www.hkab.org.hk/DisplayWhatsNewsAction.do?lang=b5&id=1068&ss=1>

*Chairman* The Hongkong and Shanghai Banking Corporation Ltd  
*Vice Chairmen* Standard Chartered Bank (Hong Kong) Ltd  
Bank of China (Hong Kong) Ltd  
*Secretary* Jennifer Cheung

主席 香港上海匯豐銀行有限公司  
副主席 渣打銀行(香港)有限公司  
中國銀行(香港)有限公司  
秘書 張學欣

Our Ref.: B1/15C

13 July 2009

The Chief Executive  
All authorized institutions

Dear Sir/Madam,

**Selling of Investment Products**

In the current low interest rate environment, depositors are likely to have an increased interest in looking for enhanced return from investment products. This circular reminds authorized institutions (AIs) that they should exercise due care in marketing and selling investment products to customers.

***Investment products regulated under the Securities and Futures Ordinance (SFO)***

For sale of investment products that fall within the scope of regulated activities under the SFO, AIs are reminded again that they must have effective controls and procedures to ensure compliance with the requirements of the SFO, the Code of Conduct for Persons Licensed by or Registered with the Securities and Futures Commission and the questions and answers on suitability obligations dated 8 May 2007 issued by the Securities and Futures Commission (SFC), and all other relevant requirements of the SFC and the Hong Kong Monetary Authority (HKMA). These include the requirements set out in the HKMA circular of 25 March 2009 on the "Implementation of Recommendations in the HKMA Report on Issues Concerning the Distribution of Structured Products Connected to Lehman Brothers" (the HKMA circular).

***Investment products not regulated by the SFO***

Many AIs also distribute investment products which are not regulated by the SFO, such as currency and interest rate linked deposits and derivatives. Similar to SFO-regulated investment products, these products involve investment risks to the customers and are often not principal-protected. AIs selling these products must ensure the suitability of their recommendations and/or solicitation for the customers.

Apart from ensuring suitability, AIs should also clearly disclose, among other things, the following key facts and risks to the customers when marketing and selling investment products that are not regulated by the SFO:

- these products are NOT equivalent to time deposits and are NOT protected deposits under the Deposit Protection Scheme in Hong Kong
- where applicable, the fact that these products are not principal-protected
- explanation of the nature of these products and whether they include any embedded derivatives and/or leverage, and the key risks of the investment

### Attachment 3

including any risk of substantial losses to their investments

- any disclosure of the maximum expected return of the investment must be accompanied by **equally** prominent and clear warning that the investor is subject to the risk of loss to his investment
- the "health warning" as set out in the HKMA circular, if they are structured products

AIs should conduct the above procedures inside the investment corner, and for audit trail purposes, must maintain adequate records to demonstrate that they have conducted appropriate suitability assessment and evidence that they have made the above disclosures, including audio recording as required in the HKMA circular.

For products that are relatively simple, such as non-leveraged foreign currency linked deposits of major currencies<sup>1</sup>, non-leveraged interest rate linked deposits and non-leveraged gold linked deposits, the HKMA is prepared to allow some operational flexibility in complying with the risk disclosure requirements for roll-over and repeated transactions. For these products, AIs should conduct the suitability assessment and make a full disclosure of the key facts and risks as set out above inside the investment corner at the time of the first transaction of each type of products. For roll-over transactions and repeated transactions (within six months of the previous transaction) of the same product, AIs may provide the customer with leaflets or other written materials disclosing the key product facts and risks in lieu of orally repeating the full risk disclosure provided that the customer confirms that he/she continues to be fully aware of the risks of the product and the AI maintains proper records (such as audio recording) to evidence that this is the case. In cases where the roll-over transactions or repeated transactions are made by telephone instructions, AIs must ensure and maintain audio records to prove that the customers continue to understand the key risks of these transactions. For roll-over and repeated transactions occurring more than six months after the previous transaction, if the customer has represented to the AI that he/she understands the risks of these products and insisted to waive the full risk disclosure, the AI may upon the customer's request, waive the full disclosure of the risks but the AI should ensure that the customer's representation and request are properly audio recorded as evidence. AIs are reminded that this operational flexibility does not discharge them from the obligation of ensuring the suitability of the product to the customer in every transaction.

For marketing materials of all investment products that are not regulated by the SFO, the HKMA expects AIs to follow standards similar to those issued by the SFC on marketing materials, including the enhanced disclosure requirements as set out in the SFC's circular of 3 October 2008 to issuers of retail investment products and the SFC's letter of 5 December 2008 to issuers of SFC-authorized Collective Investment Schemes. In particular, marketing materials must be clear, fair and

present a balanced picture with adequate and prominent risk disclosure in compliance with all applicable regulations. Financial or other incentives (e.g. gifts) to invest in a product should not be used or presented in a way that is likely to divert or mislead investors' focus from the proper consideration of the product.

***Investment products sold through private placement***

Currently, product issuers may distribute investment products through the "private placement" channel only if the distribution meets the prescribed exemptions under the Companies Ordinance (CO)<sup>2</sup>. A prospectus is not required in respect of products sold through a private placement and the associated marketing materials are not required to be authorized by the SFC. These requirements are designed to ensure the provision of adequate information to investors and thereby offer them a measure of protection. Accordingly, AIs must be satisfied that the use of the private placement channel for distributing investment products is appropriate and justified. In particular, AIs must be careful when dealing with schemes involving recurrent series of substantially similar products with minimal changes in product features and ensure that these schemes fully meet the prescribed exemptions for private placement. Further, as the offering documents of investment products distributed through the private placement channel are not required to be authorized by the SFC, the HKMA will look to AIs that distribute these products to ensure that the offering documents contain full and clear disclosure of product nature and risks. To enhance investor protection, the HKMA and Hong Kong Association of Banks' Retail Banking Task Force have agreed that investment products sold through private placement should be distributed only to professional investors, or to retail investors with a minimum investment in the product of not less than HK\$500,000.

If you have any questions on the above, please get in touch with your usual supervisory contact at the HKMA.

Yours faithfully,

Nelson Man  
Executive Director  
(Banking Supervision)

c.c. Chairman, Hong Kong Association of Banks  
Chairman, The Deposit-taking Companies Association

<sup>1</sup> For the purpose of this circular letter, major currencies refer to US dollar, Euro, UK Pound Sterling, Australian dollar, New Zealand dollar, Canadian dollar, Swiss Franc, and Japanese Yen.

<sup>2</sup> The distribution must, amongst others, meet one of the following criteria in order to be qualified as private placements exempt from the issue of a prospectus under the Companies Ordinance

- to not more than 50 persons;
- with a minimum denomination of HK\$500,000;
- with a maximum size of HK\$5 million; or
- to professional investors



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## Press Release

### **Retail banks implement new measures to physically segregate retail securities business activities from ordinary banking business at branches**

25 September 2009 – With effect from 30 September 2009, members of The Hong Kong Association of Banks (HKAB) will enhance the signage systems at their branches in order to make “investment corners” distinct from the general banking halls. The enhanced signage systems aim to provide members of the public with a clearer physical differentiation between traditional deposit-taking activities and retail securities activities (see illustrative examples of “investment corners” and the same areas before enhancement).

The above arrangement aligns with the recommendations set out in the circular of the Hong Kong Monetary Authority issued to all Authorised Institutions dated 25 March 2009 regarding the sale of investment products.

For further enquiries relating to this press release, please contact Ms Jennifer Cheung, Secretary of HKAB at 2521 1169.

The Hong Kong Association of Banks

新聞稿

2009年9月25日

### **零售銀行實行新措施以分隔分行零售證券業務及一般銀行業務**

香港銀行公會(公會)的會員銀行由 2009 年 9 月 30 日起將優化分行內的指示系統，分隔銀行大堂及投資專區。新指示系統可讓市民更容易識別辦理傳統的接受存款業務及零售證券業務的不同區域。(新指示系統推出前及推出後的分行內佈置，見附圖例子)。

以上安排為配合香港金融管理局於 2009 年 3 月 25 日向所有認可機構發出的通告內列載有關銷售投資產品的建議。

查詢新聞稿詳情，請致電 2521 1169 聯絡香港銀行公會秘書張學欣小姐。

香港銀行公會

*Chairman* The Hongkong and Shanghai Banking Corporation Ltd }  
*Vice Chairmen* Standard Chartered Bank (Hong Kong) Ltd  
 Bank of China (Hong Kong) Ltd  
*Secretary* Jennifer Cheung

主席 香港上海匯豐銀行有限公司  
 副主席 渣打銀行(香港)有限公司  
 中國銀行(香港)有限公司  
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## Press Release

### **Smooth launch of new measures to physically segregate retail investment activities from ordinary banking business activities at branches (Physical Segregation Measures)**

2 October 2009 – The Hong Kong Association of Banks (HKAB) observes that the launch of the Physical Segregation Measures by member banks has been generally smooth today, the first business day whereby full implementation of the Physical Segregation Measures across the retail banking sector is required.

Over the past months, the retail banking sector has taken a number of steps to enhance their distribution of investment products, in line with the various recommendations and implementation timelines set out in the circular of the Hong Kong Monetary Authority (HKMA) to all Authorised Institutions dated 25 March 2009. On behalf of the industry, HKAB will continue to liaise closely with the HKMA in a bid to further streamline the distribution process for investment products under the enhanced regulatory framework going forward.

For further enquiries relating to this press release, please contact Ms Jennifer Cheung, Secretary of HKAB at 2521 1169.

The Hong Kong Association of Banks

新聞稿

2009年10月2日

### **零售銀行順利落實分隔分行零售投資業務及一般銀行業務的新措施(實體分隔措施)**

香港銀行公會(公會)表示，零售銀行界在新措施實行的首個營業日(2009年10月2日)須全面落實實體分隔措施。一般而言，銀行會員認為整體運作暢順。

在過去數月，零售銀行界按香港金融管理局於2009年3月25日向所有認可機構發出的通告內列載有關銷售投資產品的建議，採納了一系列措施，以優化投資產品的銷售過程。公會將繼續代表業界與香港金融管理局緊密聯系，致力提升符合新規管下的投資產品的銷售過程。

查詢新聞稿詳情，請致電 2521 1169 聯絡香港銀行公會秘書張學欣小姐。

香港銀行公會

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 Bank of China (Hong Kong) Ltd  
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 秘書 張學欣

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