



HONG KONG MONETARY AUTHORITY
香港金融管理局

Circulars

08 Sep 2009

Simplified arrangements for selling of renminbi sovereign bonds

Our Ref.: B1/15C

8 September 2009

The Chief Executive
All Registered Institutions

Dear Sir / Madam,

Simplified arrangements for selling of renminbi sovereign bonds

The Ministry of Finance of the Central Government has announced a plan to issue renminbi (RMB) sovereign bonds in Hong Kong on 28 September 2009. Given that this is the first issue of RMB sovereign bonds in Hong Kong, the co-arrangers of the issue expect that it will attract high levels of interest from the investing public. Since registered institutions (RIs) are required, as part of the enhanced procedures for conducting regulated activities, to implement physical segregation between their retail securities business and ordinary banking business conducted at bank branches commencing on 1 October 2009, the co-arrangers are concerned that there may be a degree of confusion potentially resulting in queues of customers at bank branches applying for the RMB sovereign bonds because both the bank staff and customers are not yet familiar with the new arrangements.

As the suitability requirements are principle based, RIs should tailor their own selling or advisory procedures according to the risk level of the investment products and the investors' profiles. For products having features and risks which are not difficult for an average investor to understand, the suitability requirement can be achieved under simplified procedures. On that premise, the co-arrangers have proposed some simplified arrangements for the selling of RMB sovereign bonds. The Securities and Futures Commission (SFC) has been consulted in the process of formulating the simplified arrangements and agrees that, in respect of the selling of RMB sovereign bonds, these arrangements if properly implemented would be consistent with the principles of the suitability requirements in the Code of Conduct for Persons Licensed by or Registered with the SFC (the Code of Conduct). The Hong Kong Monetary Authority (HKMA) therefore considers the simplified arrangements for the selling of RMB sovereign bonds as set out in this circular appropriate.

Client risk profiling process

Client risk profiling should be conducted as usual except that audio recording is not required. This arrangement applies only to the selling of RMB sovereign bonds. If the RI

intends to sell other investment products to the customer, then the client risk profiling should be audio recorded before such transactions are conducted.

Simplified selling process

As always, RIs are required to provide a clear explanation of the product nature and risks to the customers during the selling process. In cases where there is no risk mismatch¹, the selling process need not be audio recorded. To facilitate risk disclosure, the co-arrangers will prepare a standardised risk disclosure statement which will be provided to the distributors. RIs should also ask their customers to sign a declaration form which includes all the information included in the standardised risk disclosure statement to confirm the customers' understanding and acceptance of the nature of the product and the risks involved.

Before making any recommendation or solicitation to clients, RIs are expected to have considered each client's personal circumstances such as his/her financial situation, investment objectives/ experience/ knowledge/ horizon and risk tolerance, and comply with the suitability requirements under the Code of Conduct.

Having considered the above, the following procedures should apply:

- For transactions involving tenor mismatch² and/or, where applicable, high asset concentration³, RIs should ensure that the customers understand the mismatch and/or high asset concentration and the risks involved. If the customer accepts the risks and chooses to proceed with the subscription, the RI should ask the customer to sign a declaration to indicate his/her understanding and acceptance of the risks and the tenor mismatch and/or high asset concentration, and provide the customer with a written record of reasons why the customer considers the product risk is acceptable; and
- When selling the product to vulnerable customers⁴, RIs are required to arrange for another frontline staff member to witness the transaction and help ensure that the customer understands the nature and risks of the product. The RI should also provide the customer with a written record of reasons why the customer considers the product risk is acceptable.

For transactions involving risk mismatch, RIs should follow the normal selling procedures, including audio recording of the selling process.

Selling through non-designated areas in branches

Where necessary, selected counters in the general banking area of branches may be designated, on a temporary basis, for handling transactions relating to the sale of RMB sovereign bonds during the subscription period. RIs should ensure that such counters are equipped with proper signage, indicating that they are designated for handling the RMB sovereign bonds subscription. The counters should be manned by relevant individuals with adequate training and knowledge about the nature and risks of the product. Such counters should not handle transactions involving risk mismatch if they are not equipped with audio recording facilities. RIs should put in place adequate procedures and controls, and effective management supervision, to ensure proper client risk profiling and selling processes at such counters.

Selling through other distribution channels

In general, regulatory requirements are technology neutral. RIs providing securities services through different channels should ensure clients are equally provided with the same disclosure information and all regulatory requirements are complied with.

Internet banking is one of the possible distribution channels for the RMB sovereign bonds. Where this channel is used, the RI should ensure that appropriate disclosure of the risks and features of RMB sovereign bonds is provided on the Internet for the customers to read. The RI should also ensure an updated customer risk profile is in place. For transactions involving risk mismatch, RIs should ask the customers to subscribe to the product through other channels such as branches or phone banking.

In addition, the following requirements should be satisfied if the Internet transactions involve vulnerable customers, tenor mismatch and/or high asset concentration:

- Vulnerable customers should be given a clear explanation (e.g. through displaying a warning page) that they may either (i) subscribe to the product at branches so that additional safeguards (e.g. having the selling process witnessed by an additional frontline staff member) can be applied, or (ii) proceed with the transaction through Internet banking but with the subscription subject to an off-line review by the RI to ensure adequate suitability assessment taking into account the customer's risk profile and the transaction details (e.g. any unreasonably high asset concentration, or tenor mismatch). In the latter cases, the RI should ask the customer to provide the reason why he or she considers the product risk is acceptable. The RI should also follow up with the customer if any possible suitability issues are observed during the off-line review process; and
- For transactions involving other customers, if any tenor mismatch and/or high asset concentration is involved, RIs should display a warning statement to explain clearly to the customer the mismatch and/or high asset concentration and the risks involved. If the customer accepts the risks and chooses to proceed with the subscription, the RI should ask the customer to provide the reason why he or she considers the product risk is acceptable and acknowledge (e.g. by clicking a check box) his/her understanding and acceptance of the risks. The RI should conduct an off-line review of the subscription requests and follow up with the customer if any possible suitability issues are observed.

For the avoidance of doubt, phone banking is also an acceptable distribution channel for the RMB sovereign bonds but the normal audio recording requirement remains applicable.

If you have any questions on this letter, please feel free to contact Mr Shu-Pui Li at 2878-1826 or Ms Alice Lee at 2878-1603.

Yours faithfully,

Karen Kemp
Acting Deputy Chief Executive

¹ Risk mismatch means that the product risk rating is higher than the client risk tolerance level.

² Tenor mismatch means that the product tenor is longer than the client's intended investment tenor.

³ The RI should use its internal definition of "high asset concentration", where applicable.

⁴ Vulnerable customers include the elderly (i.e. aged 65 or above), the visually impaired and the uneducated (or those with only an elementary or relatively low level of education).

c.c. SFC (Attn: Mr Stephen Po, Senior Director of Intermediaries Supervision Department)

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