HONG KONG MONETARY AUTHORITY
香港金融管理局

Our Ref : S4/3C
B1/15C
B1/21C

4 June 2010

The Chief Executive
All locally incorporated authorized institutions

Dear Sir / Madam,

Supervisory Policy Manual ("SPM")
<u>Module CA-G-5 : Supervisory Review Process ("SRP") (Revised)</u>

I am writing to inform you that, following consultation with the two industry Associations, the Monetary Authority ("MA") is issuing today a revised version of the above-mentioned SPM module as a statutory guideline by notice in the Gazette under section 16(10) of the Banking Ordinance.

In July 2009, the Basel Committee on Banking Supervision issued a package of enhancements to the Basel II framework, including supplemental Pillar 2 guidance to address the weaknesses in risk management practices revealed by the recent global financial crisis. The supplemental guidance covers, in particular, risk management principles in respect of firm-wide risk oversight, risk concentration, off-balance sheet exposures, securitization and associated reputation risk, valuation of financial instruments, liquidity risk management and firm-wide stress-testing as well as compensation practices. To further enhance its SRP framework, the HKMA has incorporated the relevant supplemental Pillar 2 guidance into the above-mentioned SPM module and made corresponding refinements to the SRP scoring system.

Many of the enhancements set out in the revised module are based on risk management principles and concepts that have already been embedded in various supervisory guidelines issued by the HKMA. Given that these enhancements are crucial for effective capital and risk management, locally incorporated authorized institutions ("AIs") are expected to implement the enhancements without delay if they have not already done so. Nevertheless, if an individual AI needs more time to complete system and process changes for implementing specific requirements, it may discuss and agree with the HKMA an implementation plan and timetable for the requirements concerned.

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On-line access to the SPM module is available to AIs under the icon for "Supervisory Policy Manual" on the HKMA's public (http://www.info.gov.hk/hkma) and private (http://www.stet.finnet.hk/index.htm) websites.

Should you have any questions relating to the module, please contact Ms Rita Yeung at 2878 1388 or Ms Polly Yan at 2878 1528.

Yours faithfully,

Rose Luk
Acting Executive Director (Banking Policy)

Encl.

c.c. The Chairman, Hong Kong Associations of Banks
The Chairman, The DTC Association
FSTB (Attn : Ms Natalie Li)