HONG KONG MONETARY AUTHORITY
香港金融管理局

Banking Policy Department 銀行政策部

Our Ref.: B9/92C

29 October 2009

Mr Peter Wong
Chairman
The Hong Kong Association of Banks
Room 525, 5/F
Prince's Building
Central
Hong Kong

Dear Mr Wong,

Consultation on Guideline on a Sound Remuneration System (Guideline)

I am writing to seek the Association's comments on the attached draft Guideline on a Sound Remuneration System.

The HKMA has developed this Guideline on the basis of the recommendations[1] issued by the Financial Stability Board (FSB), which have been endorsed by the G20 as an international standard on sound remuneration practices. This Guideline serves to provide broad guidance on the governance and control arrangements for, and operations of, authorized institutions' (AIs) remuneration systems. It is intended to apply to all AIs, including both locally incorporated AIs and local branches of foreign banks, given its relevance to AIs' risk management and internal control systems generally and the need to ensure a level playing field.

The Guideline sets out key principles on a sound remuneration system, covering the following areas:-

(i) **Governance** – formulation of remuneration policy; board oversight (including the establishment of a remuneration committee); and the role of risk control functions (including, but not limited to, risk management, financial control, compliance, and internal audit) in respect of an AI's remuneration system.

[1] These refer to the *Principles for Sound Compensation Practices* and *Implementation Standards* issued by the FSB in April 2009 and September 2009 respectively, and they are available on the FSB website www.financialstabilityboard.org/.

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(ii) **Structure of remuneration** – proportionate balance of fixed and variable remuneration; use of instruments for variable remuneration; and exceptional use of guaranteed minimum bonuses.

(iii) **Measurement of performance for variable remuneration** – pre-determined criteria for performance measurement; adjustments to performance assessment in respect of current and potential risks and the overall performance of an AI and relevant business units; and the exercise of judgement in the process of determining variable remuneration.

(iv) **Alignment of remuneration payouts to the time horizon of risks** – deferment of variable remuneration (including minimum vesting period and pre-defined performance conditions); claw-back provision and restriction on hedging exposures in respect of the unvested portion of deferred remuneration.

(v) **Adequate disclosure on remuneration** – disclosure in respect of the design and implementation of remuneration systems; and aggregate quantitative information on remuneration broken down by senior management and by other employees whose activities could have a material impact on the risk exposure of an AI.

The HKMA intends to issue the Guideline in the form of a supervisory policy manual module by the end of this year. Upon issuance of the final Guideline, the HKMA expects all AIs to take prompt action to implement the Guideline with a view to achieving full compliance within 2010. AIs should apply the principles set out in the Guideline to the remuneration payable by them for the performance year 2009 as far as reasonably possible, taking into account the lead time required for making any necessary changes to their remuneration systems (including policies, structures, internal systems, and employment contracts).

As the development of international standards and best practices on remuneration within banks is still evolving, this Guideline may require modification. The HKMA will continue to monitor developments and will make changes to the Guideline as appropriate, having regard to local circumstances.

I would be grateful if your members' comments on the attached draft Guideline could reach us by **30 November 2009**.

I am writing in similar terms to the Chairman of The DTC Association.

Yours sincerely,

Karen Kemp
Executive Director (Banking Policy)

Encl.

c.c. FSTB (Attn. Miss Natalie Li)