



香港存款保障委員會
HONG KONG DEPOSIT
PROTECTION BOARD

Our Ref.: D1/1C

13 November 2007

The Chief Executive
All Scheme members

Dear Sir/Madam,

Compliance Review Program for the Information System Guideline

I am writing to inform you of the arrangements to be adopted by the Hong Kong Deposit Protection Board for reviewing Scheme members' compliance with the Guideline on Information Required for Determining and Paying Compensation (the IS Guideline).

To ensure that the Board can determine and pay compensation to depositors efficiently in a payout, the Board issued the IS Guideline in February 2006. The IS Guideline sets out the requirements in accordance with which Scheme members should maintain their information systems and make information relevant to determining compensation of depositors available to the Board. Scheme members with no more than 500,000 deposit accounts should have already achieved full compliance with the IS Guideline before 31 August 2006. Those with more than 500,000 deposit accounts are expected to be in full compliance by the end of this year.

To ensure compliance of Scheme members with the standards set out in the IS Guideline, the Board will commence conducting compliance reviews on Scheme members in 2008. The details of the Compliance Review Program to be implemented by the Board for reviewing Scheme members' compliance are set out in the attached information note. Scheme members chosen for a review will be informed at least two months before the date of commencement of the review.

If you have any questions on the Program, please do not hesitate to contact Mr Pierre Leung at 2878 8057 or Ms Anita Chan at 2878 8004.

Yours faithfully,

Raymond Li

Chief Executive Officer
Hong Kong Deposit Protection Board

Encl.

c.c. The Hong Kong Association of Banks (Attn: Secretary)

HONG KONG DEPOSIT PROTECTION BOARD

Compliance Review Program for the Information System Guideline

PURPOSE

This information note sets out the arrangements to be adopted by the Hong Kong Deposit Protection Board (the Board) for reviewing Scheme members' compliance with the Guideline on Information Required for Determining and Paying Compensation (the IS Guideline).

BACKGROUND

2. According to the Deposit Protection Scheme Ordinance (DPS Ordinance), when compensation under the DPS is triggered in respect of a Scheme member, the Board should determine the compensation entitlements of the depositors of the Scheme member and pay compensation to them as soon as practicable. To ensure that the Board can discharge its functions in this respect efficiently, the Board issued the IS Guideline on 8 February 2006 (which was subsequently gazetted on 16 June 2006) to specify the manner in which Scheme members should maintain information that is relevant to the determination of compensation in a payout and how they should make such information retrievable or available to the Board. According to the IS Guideline, Scheme members with 500,000 deposit accounts or less are required to achieve compliance with the IS Guideline by 31 August 2006, whereas other Scheme members are required to be in full compliance by the end of 2007. The Board will commence conducting reviews on Scheme members to verify their compliance status in 2008, after the last batch of Scheme members achieves full compliance with the IS Guideline.

COMPLIANCE REVIEW PROGRAM

3. According to section 48(1) of the DPS Ordinance, the Board may require a Scheme member to submit such information as it may require for the performance of its functions, and such information shall be submitted within such period and in such manner as the Board may specify. The Board will therefore formally require a Scheme member to submit information to the Board for conducting a compliance review under this section of the DPS Ordinance.

4. The requirements in the IS Guideline generally cover three areas:

- (i) availability of the required information, including the completeness and accuracy of the information;
- (ii) timeliness in making the required information retrievable or available; and
- (iii) format in which the required information is maintained or submitted to the Board.

5. The Board recognizes that a Scheme member's compliance with some of the requirements in the IS Guideline cannot be verified directly. For example, unlike in a payout, it will not be possible to call a halt to the normal operation of a Scheme member at any time to test whether it can mobilize all its resources to make the required information available to the Board within the specified timeframes. Compliance with such requirements can only be verified indirectly, say by verifying whether a system is in place to meet the relevant requirements if the DPS is triggered. The focus of the compliance review will therefore be placed on ascertaining the availability of the required information and compatibility of the information submitted by a Scheme member with the standards in the IS Guideline. In conducting a compliance review, the Board will mainly rely on information supplied by a Scheme member and will not access the information systems of the Scheme member to retrieve the required information.

6. The scope of work to be performed by the Board in each compliance area is set out in the following table:

Compliance areas	Scope of work for checking compliance of	
	Scheme members with no more than 10,000 deposit accounts	Scheme members with more than 10,000 deposit accounts
Availability of the required information	<ul style="list-style-type: none"> • obtain month-end position data and terms and conditions of all products (or a subset containing major products of which the Board deems sufficient), to ascertain whether the required information is available and can be retrieved in Hong Kong • compare the balances in the position data with accounting reports to ascertain the completeness of the information • examine the terms and conditions of major products to ascertain their protection or set-off status • verify the accuracy of the information in the position data by obtaining and reviewing source documents of a set of randomly selected positions 	
Timeliness in making the information retrievable and/or available	<ul style="list-style-type: none"> • substantiate whether a system and/or a set of processes is in place to make the required information retrievable and/or available to the Board within the specified timeframes 	

<p>Format in which the information is made retrievable and/or available</p>	<ul style="list-style-type: none"> examine the electronic files (e.g., database exports, native database files, dumps) obtained to establish whether the position and position-holder information can be retrieved in an electronic form 	<ul style="list-style-type: none"> examine the electronic files obtained to establish whether the position and position-holder information can be obtained in the specified formats
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In addition to the scope of work set out in the table above, the Board will also examine in each review whether a Scheme member has in place a mechanism to ensure that due regard will be given to meeting the requirements in the IS Guideline when new systems or new products are introduced by the Scheme member over time.

7. In the light of the resource constraints of the Board, it is expected that the Board will be able to conduct no more than six compliance reviews every year. A risk-based approach will be adopted by the Board to identify Scheme members to be subject to a compliance review. Selection of Scheme members will be made with reference to various factors such as the size and complexity of their information systems, in terms of data volume, variety and level of sophistication. Except where a significant change in those factors or a major system change is noted for a Scheme member, a Scheme member subject to a compliance review is not expected to be enrolled in another review until the Board has completed a cycle of checking on Scheme members of a comparable risk profile. Scheme members chosen for a review will be informed at least two months before the date of commencement of the review.

8. It is expected that, depending on a number of factors specific to the Scheme member involved, it will take 4 to 10 weeks to complete a compliance review. The Scheme member chosen will be requested to nominate representatives from their information systems, accounting and banking services departments to liaise with the Board on matters relating to the review, for example, where the balances in the position data do not agree with those in the accounting reports, to co-ordinate the relevant departments of the Scheme member to explain and resolve the discrepancies. However, it is not expected that these personnel will be required to devote significant amount of time throughout the compliance review.

SIMULATION TESTS

9. Among the six compliance reviews planned per annum, three of them will be conducted in conjunction with the simulation tests of the Board. In a simulation test, the position data obtained from a Scheme member will be uploaded to the information system developed by the Board for calculating compensation entitlements of depositors in a payout (the Payout System) to simulate calculation. It

is not anticipated that Scheme member personnel will be required to devote significantly more time to a compliance review that is conducted in conjunction with a simulation test if the position data provided to the Board is in compliance with the IS Guideline. According to the Board's experience in the simulation tests conducted so far, Scheme members may be consulted occasionally in relation to the format and contents of the position data to facilitate the uploading of the data to the Board's Payout System.

NON-COMPLIANCE AND REMEDIAL ACTIONS

10. After the completion of a compliance review, the Board will issue a letter to the Scheme member to advise on the findings of the review. Where non-compliance issues are identified in the review, the Scheme member will be required to establish an action plan to resolve such issues, and report to the Board upon completion of the plan. The Board may require the Scheme member to submit additional information to substantiate the completion of the relevant remedial actions.

INDEPENDENT AUDIT REVIEW

11. Where severe non-compliance issues are identified by the Board in a compliance review, the Board may require the Scheme member to undergo further review. Under section 48(4) of the DPS Ordinance, the Board may require a Scheme member to submit a report prepared by an auditor appointed by the Scheme member and approved by the Board as to whether or not, in the opinion of the auditor, the Scheme member has in place systems of control that are adequate to enable the Board to perform its functions.

12. For any weaknesses identified by the auditor, the Board will request the Scheme member to establish an action plan and to inform the Board of its course of actions under section 48(1) of the DPS Ordinance.

COMMENCEMENT OF COMPLIANCE REVIEW

13. To test the functioning of the Payout System, the Board commenced conducting simulation tests on the Payout System in 2006. Compliance checks on selected areas of the IS Guidelines were also performed in these tests. In the course of conducting the simulation tests, the Board noticed that, due to variations in the interpretation of some requirements in the IS Guideline, the data submitted by some Scheme members for testing could not fully meet the standards set out in the IS Guideline. To understand the pervasiveness of such phenomenon, the Board issued a survey (IT Survey) to Scheme members in October 2007 to collect information on certain technical issues relating to achieving compliance with the IS Guideline.

14. While the Board will formally embark on conducting compliance reviews on Scheme members in 2008, sufficient time will be given to Scheme members to make adjustments to their information systems to rectify non-compliance areas arising out of common misinterpretations of the IS Guideline as revealed in the IT Survey before such areas will be subject to review.

Hong Kong Deposit Protection Board
November 2007