HONG KONG (as of April 2014)

Annex I: Banks

Action to be taken	Responsible national authority	High-level description of approach to be taken, and necessary or contributory factors to assist implementation (e.g. changes in international standards)	Milestones and expected completion date (e.g. "end-2014" or "one year after new international standards agreed")
1. Reducing reliance on CRA ratings in laws and regulations (Principle I)			
Based on the findings from the stock-taking exercise, please describe the areas identified as needing change and those areas considered priorities, as well as the steps authorities intend to take to reduce reliance on CRA ratings in laws and regulations. In addition, authorities should describe the incentives put in place for market participants to develop their own independent credit assessment processes. Examples of incentives might include disclosure requirements relating to credit risk assessment practices or articulating clear supervisory expectations of the extent to which firms should perform their own due diligence before making lending decisions.			
a) Remove references to CRA ratings in laws and regulations relating to banks.	Hong Kong Monetary Authority ("HKMA")	The references to CRA ratings in laws and regulations relating to banks are all related to the regulatory capital and liquidity frameworks. Capital standards The regulatory capital framework, which is closely in line with the latest Basel capital	 Capital standards In accordance with the implementation

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		standards, is set out in the Banking (Capital) Rules[1]. The Basel Committee on Banking Supervision ("BCBS") is in the process of reviewing the standardized approach for credit risk, the securitization framework and the market risk framework with a view to developing proposals, among other things, to reduce undue reliance on CRA ratings in the regulatory capital framework. The HKMA will initiate legislative amendments to the Banking (Capital) Rules to implement proposals issued by the BCBS in this regard once the proposals are finalised. There are 26 authorized institutions* (AIs) using the standardized approach (this does not include AIs using the IRB approach that	timetable set by the BCBS. Rules amendments to be completed 15-17 months after the BCBS finalizes the revised standardized approach for credit risk (unless the BCBS specifies a longer timeline): ◆ Policy formulation and industry consultation: about 5 – 6 months

[1] The Banking (Capital) Rules can be assessed at the website of the Department of Justice of the HKSAR Government: http://www.legislation.gov.hk/blis_pdf.nsf/CurAllEngDoc/4FA16B5F7562DC69482575EE0045FB50/$FILE/CAP_155L_e_b5.pdf

Action to be taken	Responsible national authority	High-level description of approach to be taken, and necessary or contributory factors to assist implementation (e.g. changes in international standards)	Milestones and expected completion date (e.g. "end-2014" or "one year after new international standards agreed")
		have exposures exempted from the IRB approach and for which the risk-weights are determined by using the standardized approach). Their aggregate risk-weighted amount (RWA) for credit risk accounted for about 28% of the aggregate RWA for credit risk of all locally incorporated AIs (if the standardized RWA of the aforesaid IRB AIs are included, the percentage share will be about 33%). Out of the 21 locally incorporated licensed banks in Hong Kong, 11 are using the standardized approach in calculating their RWA for credit risk (this does not include licensed banks using the IRB approach that have exposures exempted from the IRB approach and for which the risk-weights are determined by using the standardized approach). These 11 banks in aggregate account for about 25% of the RWA of all locally incorporated licensed banks on a	◆ Law drafting and industry consultation: about 8 - 9 months ◆ Scrutiny by the Legislative Council: 2 months

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		consolidated basis. The HKMA does not expect that there will be significant change in the number of AIs using the standardized approach in the near future. * Hong Kong maintains a 3-tier system of deposit-taking institutions, namely, licensed banks, restricted licence banks and deposit-taking companies (collectively referred to as "authorized institutions"). The last two categories of institutions are subject to certain restrictions on deposit-taking. Liquidity standards For the purposes of implementing the Basel III liquidity standards, the HKMA will be removing the Fourth Schedule to the Banking Ordinance (BO) on liquidity and replacing it with a set of Banking (Liquidity) Rules.	Liquidity standards Effective from 1 January 2015

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		CRA references will however be retained in the Banking (Liquidity) Rules once produced as these Rules will reflect the Basel III Liquidity Coverage Ratio which itself includes CRA references. As for the intended approach to modify the existing Liquidity Ratio prescribed in the Banking Ordinance, please refer to item 3.2(b).	
b) Develop alternative standards of credit assessment, where needed, for the purpose of replacing references to CRA ratings in laws and regulations relating to banks.	HKMA	Capital standards The HKMA intends to adopt the measures to be issued by the BCBS for reducing reliance on CRA ratings in the regulatory capital framework in item 1(a) above.	Capital standards Please see 1(a) above
2. Reducing market reliance on CRA ratings (Principle II)			
a) Enhance supervisory processes and procedures to assess the adequacy of banks' own credit assessment processes and incentivise market participants to develop internal risk	HKMA	As identified in the stock-taking exercise, overall, banks in Hong Kong do not tend to place particularly strong reliance on CRA	For existing regulatory requirements:

Action to be taken	Responsible national authority	High-level description of approach to be taken, and necessary or contributory factors to assist implementation (e.g. changes in international standards)	Milestones and expected completion date (e.g. "end-2014" or "one year after new international standards agreed")
management capabilities.		ratings in their credit risk assessment processes. This is in part due to the fact that generally only large corporations, in particular large listed companies and their debt instruments, are likely to have ratings both locally and regionally. For clients / counterparties which have CRA ratings, banks would normally use such information as reference just to supplement their internal credit risk assessments of these clients / counterparties. In addition, supervisory guidelines are in place encouraging / requiring banks to have their own internal risk management capabilities and not to rely unduly on the credit assessment of, and credit ratings assigned by, external credit rating agencies[2].	Ongoing supervisory process. For any new / enhanced international standards to be adopted into the local framework: Upon promulgation of the new standards, the HKMA will conduct reviews or examinations, usually within 12 to

[2] For example, as stipulated in the Supervisory Policy Manual module on "Counterparty Credit Risk Management (CR-G-13)" (para. 4.3), banks are required to "conduct their own due diligence on their counterparties and the quality of exposures underlying the transactions based on sufficient credit information", and "care should be taken not to rely unduly on the credit assessment of, and credit ratings assigned by, external credit rating agencies". Regarding requiring banks to have their own internal risk management capabilities, see Supervisory Policy Manual modules CR-G-2 "Credit approval, review and records" (e.g. paragraph 2.2), CR-G-3 "Credit administration, measurement and monitoring" (e.g. paragraph 2.3), and CR-G-5

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		The adequacy of banks' own credit assessment processes has been covered in the regular risk-based and/or thematic onsite examinations and offsite review of banks' credit risk management. As and when new international standards or enhancements to existing international standards are adopted into the HKMA's regulatory framework, the HKMA will include supervision of banks' compliance with the new or enhanced standards into its onsite examinations and offsite reviews as	24 months depending on the complexity of the new standards, to assess whether banks are in compliance with the new standards.

"Country risk management" (e.g. paragraph 3.6). These guidelines can be found via the web-link: http://www.hkma.gov.hk/eng/key-functions/banking-stability/supervisory-policy-manual.shtml.

Action to be taken	Responsible national authority	High-level description of approach to be taken, and necessary or contributory factors to assist implementation (e.g. changes in international standards)	Milestones and expected completion date (e.g. "end-2014" or "one year after new international standards agreed")
		appropriate.	
b) Require or incentivise market participants to disclose information about their internal credit risk assessment processes.	HKMA	Hong Kong incorporated banks have been required under the Banking (Disclosure) Rules to make public disclosures in line with the Pillar 3 disclosure requirements prescribed by the BCBS. These include disclosure of information on credit risk assessment processes, covering the policies, procedures and controls banks use for identifying, measuring, monitoring, and controlling their principal risks (including credit risk). The HKMA will update these disclosure standards in line with the changes ultimately made by the BCBS to the standardized approach for credit risk, the securitization framework and the market risk framework as mentioned in item 1(a).	In accordance with BCBS's implementation timetable for standards mentioned in item 1(a).
3.2 Prudential supervision of banks (Principle III.2)			
a) Enhance supervisory oversight of banks to ensure they develop adequate internal credit	HKMA	As mentioned in item 2(a) above, the adequacy of banks' own credit assessment	For existing regulatory

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assessment processes that avoid mechanistic reliance on CRA ratings (differentiating where appropriate between banks subject to the internal ratings-based (IRB), Standardised Approach of other capital regime).		process is covered in the regular onsite examinations and offsite review of banks' credit risk management. Following the issuance of any new international standards or the enhancement of existing standards to be adopted into the local regime, the HKMA will consider performing specific thematic examinations or focussing on the new, enhanced areas as part of its risk-based examinations on the credit risk assessment processes of banks. For banks using the IRB approach, the HKMA would have a higher expectation of their internal credit assessment processes with little reliance being placed on CRA ratings. While the subject areas would also be covered in the regular risk-based or thematic onsite examinations of these banks, the IRB specialized team would also conduct additional reviews in its IRB examinations to ensure the IRB banks meet supervisory	requirements: Ongoing supervisory process. For any new / enhanced international standards to be adopted into the local framework: Upon promulgation of the new standards, the HKMA will conduct reviews or examinations, usually within 12 to 24 months depending on the complexity of the

Action to be taken	Responsible national authority	High-level description of approach to be taken, and necessary or contributory factors to assist implementation (e.g. changes in international standards)	Milestones and expected completion date (e.g. "end-2014" or "one year after new international standards agreed")
		expectations.	new standards, to assess whether banks are in compliance with the new standards.
b) Revise CRA ratings in other prudential supervisory policies (e.g. relating to liquidity requirements) to reduce reliance on CRA ratings.	HKMA	To supplement existing supervisory guidelines on credit risk management, the HKMA is in the process of developing supervisory guidance on credit risk transfer to, among other things, strengthen the requirements on banks' internal credit risk assessment of structured products with a view to reducing undue reliance on CRA ratings. Taking the opportunity of the implementation of the Basel III liquidity standards, the HKMA is reviewing the existing statutory liquidity ratio (which will continue to apply to those banks in Hong Kong not made subject to the Liquidity Coverage Ratio	End-2014

Action to be taken	Responsible national authority	High-level description of approach to be taken, and necessary or contributory factors to assist implementation (e.g. changes in international standards)	Milestones and expected completion date (e.g. "end-2014" or "one year after new international standards agreed")
		("LCR")), including whether, and the extent to which, CRA ratings should be adopted as a factor for defining liquefiable assets. The modification to the existing liquidity ratio is targeted to be completed by January 2015. If the Basel Committee issues further guidance on possible ways to reduce reliance on CRA ratings in the course of supervision (e.g. to use market-based indicators for defining eligible liquid assets for the LCR), the HKMA will make reference to such guidance for enhancing the local liquidity framework.	

Annex II: Central bank operations

Action to be taken	Responsible national authority	High-level description of approach to be taken, and necessary or contributory factors to assist implementation (e.g. changes in international standards)	Milestones and expected completion date (e.g. "end-2014" or "one year after new international standards agreed")
3. Application of the basic principles to particular financial market activities (Principle III)			
Based on the findings from the stock-taking exercise, please describe the areas identified as needing changes, including which areas are considered priorities, and the steps authorities intend to take to reduce reliance on CRA ratings in central bank policies and operations.			
On FX reserves management, the HKMA has made on-going efforts to reduce the reliance on CRA ratings. Specifically, based on the past experience in early 2013 to adopt an internal credit scoring system to evaluate the credit-worthiness of sovereign issuers, the HKMA in November 2013 implemented a new credit policy on counter-parties with a view to strengthening the credit assessment framework by incorporating a wider spectrum of variables and indicators in the in-house scoring system.			

Action to be taken	Responsible national authority	High-level description of approach to be taken, and necessary or contributory factors to assist implementation (e.g. changes in international standards)	Milestones and expected completion date (e.g. "end-2014" or "one year after new international standards agreed")
3.1 Central bank operations (Principle III.1)			
a) Reduce reliance on CRA ratings in central bank policies (such as investments, asset management frameworks, and conventional and unconventional operations), including the decision to accept or reject an instrument as collateral or for outright purchase and in determining haircuts.	HKMA	Under the currency board arrangements, HKMA does not conduct any open market operations. Meanwhile, for the provision of overnight HKD liquidity through Discount Window, the HKMA only accepts Exchange Fund Bills and Notes (EFBNs) as collateral. Since all EFBNs are part of the HKD monetary base and fully backed by USD reserves, this arrangement is consistent with the currency board principles. For these reasons, no action is required to be taken to reduce reliance on CRA ratings in relation to central bank's daily market operations.	

Action to be taken	Responsible national authority	High-level description of approach to be taken, and necessary or contributory factors to assist implementation (e.g. changes in international standards)	Milestones and expected completion date (e.g. “end-2014” or “one year after new international standards agreed”)
		In case of any repos to provide HKD funding under Lender of Last Resort (LoLR) or in times of a dysfunctional money market, the haircuts on securities are determined with reference to a number of factors, including but not limited to credit ratings. The HKMA maintains the discretion in adjusting haircuts as appropriate. The haircut table is not publicly disclosed and as such they would not induce strong reliance on CRA ratings by private sector.	

Action to be taken	Responsible national authority	High-level description of approach to be taken, and necessary or contributory factors to assist implementation (e.g. changes in international standards)	Milestones and expected completion date (e.g. "end-2014" or "one year after new international standards agreed")
		For LoLR support, the eligible collateral ranges from investment-grade securities to non-rated assets such as mortgage loans and bank placements. If needed, discretion can be exercised to accept non investment-grade securities. For term repos, the HKMA accepts securities of acceptable credit quality as collateral. In determining the eligibility of a security as collateral for LoLR support/term repos, the HKMA will take into account a wide range of factors, including but not limited to credit ratings, the type of securities, the type of issuers, maturity, issue size, denomination currency, etc.	

Action to be taken	Responsible national authority	High-level description of approach to be taken, and necessary or contributory factors to assist implementation (e.g. changes in international standards)	Milestones and expected completion date (e.g. "end-2014" or "one year after new international standards agreed")
		On FX reserves management, the HKMA in early 2013 strengthened its internal credit risk management framework with the adoption of an in-house credit scoring system to evaluate the credit-worthiness of sovereign issuers. In assessing the credit of a sovereign, the HKMA takes into account CRA ratings and other important credit information including its market-based probability of default (PD) and a wide spectrum of key macroeconomic and financial variables in the internal credit scoring system. The HKMA then assigns relative weights to all these factors, thus forming a comprehensive analysis of the relative default risk of the sovereign issuers.	N/A

Action to be taken	Responsible national authority	High-level description of approach to be taken, and necessary or contributory factors to assist implementation (e.g. changes in international standards)	Milestones and expected completion date (e.g. “end-2014” or “one year after new international standards agreed”)
		Since then, the HKMA has stepped up efforts to further reduce reliance on the use of CRA ratings in managing FX reserves. Specifically, the HKMA in November 2013 implemented a new internal credit assessment framework for financial institutions. Similar to sovereigns, the framework is based on an expanded number of determining factors including PD and relevant financial metrics together with the country risk and operating environment. The HKMA plans to assess the feasibility of extending the use of PD for other types of entities such as corporates, taking into account the required resources in developing and maintaining the internal scoring systems.	On-going

Action to be taken	Responsible national authority	High-level description of approach to be taken, and necessary or contributory factors to assist implementation (e.g. changes in international standards)	Milestones and expected completion date (e.g. "end-2014" or "one year after new international standards agreed")
b) Adjust policies for imposing risk control measures (including haircuts) on financial instruments to align with the FSB Principles on CRA ratings.	HKMA	N/A (to FX reserves management)	N/A
c) Develop the central bank's internal credit risk assessment capabilities and use of alternative measures of creditworthiness.	HKMA	See item 3.1(a) above.	See item 3.1(a) above

Annex III: Insurance/Reinsurance Companies[3]

Action to be taken	Responsible national authority	High-level description of approach to be taken, and necessary or contributory factors to assist implementation (e.g. changes in international standards)	Milestones and expected completion date (e.g. "end-2014" or "one year after new international standards agreed")
1. Reducing reliance on CRA ratings in laws and regulations (Principle I)			
Based on the findings from the stock-taking exercise, please describe the areas identified as needing change and those areas considered priorities, as well as the steps authorities intend to take to reduce reliance on CRA ratings in laws and regulations. In addition, authorities should describe the incentives put in place for market participants to develop their own independent credit assessment processes. Examples of incentives might include disclosure requirements relating to credit risk assessment practices or articulating clear supervisory expectations of the extent to which firms should perform their own due diligence before making lending or investment decisions.			

[3] Answers in this section should relate to the prudential regulation of insurance companies and reinsurance companies. Laws and regulations relating to insurance companies in their capacity as institutional investors should be included in the section entitled "Investment Funds Management."

Action to be taken	Responsible national authority	High-level description of approach to be taken, and necessary or contributory factors to assist implementation (e.g. changes in international standards)	Milestones and expected completion date (e.g. "end-2014" or "one year after new international standards agreed")
Since the introduction of the FSB Principles for Reducing Reliance on CRA Ratings, the Insurance Authority ("IA") has actively reviewed if there are any areas / reference in law and regulations about CRA ratings that can be removed or replaced with suitable alternatives accordingly. Based on IA's review, it is found that references of CRA ratings in Regulation and Guidance Notes are minimal and not likely to result in sole or mechanistic reliance on such ratings. This is consistent with the views of the International Association of Insurance Supervisors ("IAIS") that CRA ratings usually have a lesser role to play in the management of the risk of an insurer and they are never sole input for investment and reinsurance portfolio management of insurers. The IA has published Guidance Notes in relation to asset management and corporate governance of authorised insurers, outlining the requirements of internal risk management policies and procedures. The IA requires that insurers' board of directors and senior management assume full responsibility for risk management and control of investment and reinsurance portfolio management. While keeping in view of the international developments and the guidance on this subject matter to be developed by the IAIS, the IA is in the process of developing a Risk-based Capital ("RBC") framework which will examine, among others, in detail the situation of using CRA ratings in relevant law, regulation and guidance, and propose measures to reduce such reliance where appropriate. In addition, on the basis that the existing references of CRA ratings in Regulation and Guidance Notes have already been not in sole or mechanistic reliance on such ratings in the insurance industry, the IA has conducted a study on the development of the proposed RBC framework, which is built upon the Insurance Core Principles promulgated by the IAIS. The IA considers that the capital adequacy and supervisory framework will be geared towards a spectrum of factor-based approach. As such, with the proposed RBC framework putting more references to the significance of various risk factors, the emphasis of CRA ratings will relatively be reduced to a large extent.			
a) Remove references to CRA ratings in laws and regulations relating to insurance/reinsurance companies.	IA	References are to be removed, where appropriate, upon the enactment of the RBC framework.	3-5 years as such action is part of the RBC development

Action to be taken	Responsible national authority	High-level description of approach to be taken, and necessary or contributory factors to assist implementation (e.g. changes in international standards)	Milestones and expected completion date (e.g. "end-2014" or "one year after new international standards agreed")
b) Develop alternative standards of credit assessment, where needed, for the purpose of replacing references to CRA ratings in laws and regulations relating to insurance/reinsurance companies.	IA	It is to be considered during the development of the RBC framework in Hong Kong; and pending with IAIS' development of guidance regarding formulation and disclosure of appropriate risk assessment practices by financial institutions.	See item 1(a) above
2. Reducing market reliance on CRA ratings (Principle II)			
a) Enhance supervisory processes and procedures to assess the adequacy of insurers'/reinsurers' own credit assessment processes and incentivise market participants to develop internal risk management capabilities.	IA	The IA has published Guidance Notes in relation to asset management and corporate governance of the authorised insurers, outlining the requirements of internal risk management policies and procedures.	On-going
b) Require or incentivise market participants to disclose information about their internal credit risk assessment processes.	IA	The IA will keep close watch on the development by international standard setting bodies of guidance regarding formulation and disclosure of appropriate risk assessment practices by financial institutions.	To follow the timeline as set and agreed by the FSB and/or the IAIS in implementing the policy recommendations.

Annex IV: Investment Funds Management
(including collective investment schemes, alternative investment schemes, occupational retirement schemes)

Action to be taken	Responsible national authority	High-level description of approach to be taken, and necessary or contributory factors to assist implementation (e.g. changes in international standards)	Milestones and expected completion date (e.g. "end-2014" or "one year after new international standards agreed")
1. Reducing reliance on CRA ratings in laws and regulations (Principle I)			
Based on the findings from the stock-taking exercise, please describe the areas identified as needing change and those areas considered priorities, as well as the steps authorities intend to take to reduce reliance on CRA ratings in laws and regulations. In addition, authorities should describe the incentives put in place for market participants to develop their own independent credit assessment processes. Examples of incentives might include disclosure requirements relating to credit risk assessment practices.			
During the stocktaking exercise, the Securities and Futures Commission ("SFC") did not identify any areas requiring change. SFC reviewed whether there is a reliance on CRA rating in our authorisation of publicly offered collective investment schemes (CIS) and SFC submitted that for CIS offered to the public in Hong Kong, there is no requirement under the primary legislation, the Securities and Futures Ordinance or the applicable SFC product codes and guidelines that these products must be rated by CRA. The only references to CRA rating for publicly offered CIS in the regulations are in the Code on Unit Trusts and Mutual Funds (UT Code) but these references are purely disclosure based and they do not constitute reliance. Furthermore, the credit rating information is only disclosable where it is applicable. For example, if a CIS is holding collateral, we ask that the description of the holdings of collateral should include; the value of the CIS (by percentage) secured / covered by collateral with breakdown by asset class/nature and credit ratings. The disclosure of the credit rating is only one part of the disclosure requirement and is only applicable to a CIS if it is holding collateral. The purpose of these types of disclosure requirements is to provide more information to investors. We do not mandate any form of reliance (mechanical or otherwise) on CRA ratings.			

Action to be taken	Responsible national authority	High-level description of approach to be taken, and necessary or contributory factors to assist implementation (e.g. changes in international standards)	Milestones and expected completion date (e.g. "end-2014" or "one year after new international standards agreed")
a) Remove references to CRA ratings in laws and regulations for investment funds management.	SFC	N/A. CRA rating is only one of many factors to be considered.	N/A
b) Develop alternative standards of credit assessment, where needed, for the purpose of replacing references to CRA ratings in laws and regulations for investment funds management.	SFC	N/A. Please see item 1(a) above. The SFC will keep in view the outcome from the International Organization of Securities Commissions (IOSCO)'s relevant work in reducing reliance on CRA ratings.	N/A
2. Reducing market reliance on CRA ratings (Principle II)			
a) Enhance supervisory processes and procedures to assess the adequacy of market participants' own credit assessment processes.	SFC	N/A. Investment processes are discussed with investment managers and alternative investment managers during the course of supervision of the SFC-licensed firms. The SFC will keep in view the outcome from the IOSCO's relevant work in reducing reliance on CRA ratings.	N/A

Action to be taken	Responsible national authority	High-level description of approach to be taken, and necessary or contributory factors to assist implementation (e.g. changes in international standards)	Milestones and expected completion date (e.g. "end-2014" or "one year after new international standards agreed")
3. Application of the basic principles to particular financial market activities (Principle III.3)			
a) Establish, as appropriate, supervisory review of internal limits and investment policies of investment managers and institutional investors.			
a. Insurance companies (in their capacity as institutional investors)	IA	The IA has published Guidance Notes in relation to asset management and corporate governance of the authorised insurers, outlining the requirements of internal risk management policies and procedures. The IA may also periodically request the insurers to submit specified information such as limits to credit, market and other risks and conduct on-site inspections and discussion with the insurers.	On-going

Action to be taken	Responsible national authority	High-level description of approach to be taken, and necessary or contributory factors to assist implementation (e.g. changes in international standards)	Milestones and expected completion date (e.g. "end-2014" or "one year after new international standards agreed")
b. Investment managers (i.e. managers of collective investment schemes).	SFC	N/A. Investment processes are discussed with investment funds managers during the course of supervision. In respect of reviewing the internal limits and investment policies, SFC considers whether the firm's risk management practice is commensurate with the risk profile of the firm, whether the firm has appropriate resources and whether there is appropriate management governance. The SFC will keep in view the outcome from the IOSCO's relevant work in reducing reliance on CRA ratings.	N/A

Action to be taken	Responsible national authority	High-level description of approach to be taken, and necessary or contributory factors to assist implementation (e.g. changes in international standards)	Milestones and expected completion date (e.g. "end-2014" or "one year after new international standards agreed")
c. Alternative investment managers (e.g. hedge funds, endowments).	SFC	N/A. Investment processes are discussed with alternative funds managers during the course of supervision. In respect of reviewing the internal limits and investment policies, SFC considers whether the firm's risk management practice is commensurate with the risk profile of the firm, whether the firm has appropriate resources and whether there is appropriate management governance. The SFC will keep in view the outcome from the IOSCO's relevant work in reducing reliance on CRA ratings.	N/A

Action to be taken	Responsible national authority	High-level description of approach to be taken, and necessary or contributory factors to assist implementation (e.g. changes in international standards)	Milestones and expected completion date (e.g. "end-2014" or "one year after new international standards agreed")
d. Managers of occupational retirement schemes.	Mandatory Provident Fund Authority ("MPFA")	Presently, as set out in MPF legislation, investment managers and trustees of MPF funds must consider the statutory minimum standards based on CRA credit ratings, among other things, when investing for these funds. Investment compliance monitoring is discussed with trustees and managers of the schemes / funds during the course of supervision in assessing proper compliance with legislative requirements as well as the investment objectives and policy of the funds as set out in the governing rules of the schemes / funds. In the absence of an alternative credit assessment framework for relevant securities at this stage, no change is proposed. A broader review of investment regulation, including reliance on CRA, may be undertaken in the longer-term.	Ongoing

Action to be taken	Responsible national authority	High-level description of approach to be taken, and necessary or contributory factors to assist implementation (e.g. changes in international standards)	Milestones and expected completion date (e.g. "end-2014" or "one year after new international standards agreed")
b) Require changes to internal limits and investment policies.			
a. Insurance companies (in their capacity as institutional investors)	IA	The IA will keep in view of the international development on guidance for formulation and disclosure of appropriate risk assessment practices by financial institutions. Having that said, the IA is empowered by the Insurance Companies Ordinance to take regulatory intervention in respect of operations of insurance companies in Hong Kong for the protection of interests of policyholders.	On-going
b. Investment managers (i.e. managers of collective investment schemes).	SFC	N/A. Certain investors may impose investment restrictions by reference to CRA ratings. The SFC will keep in view the outcome from the IOSCO's relevant work in reducing reliance on CRA ratings.	N/A

Action to be taken	Responsible national authority	High-level description of approach to be taken, and necessary or contributory factors to assist implementation (e.g. changes in international standards)	Milestones and expected completion date (e.g. "end-2014" or "one year after new international standards agreed")
c. Alternative investment managers (e.g. hedge funds, endowments).	SFC	N/A. SFC is not aware that CRA ratings were used in setting internal limits or investment policies of managers. Managers perform their own credit analysis in making investment decisions. The SFC will keep in view the outcome from the IOSCO's relevant work in reducing reliance on CRA ratings.	N/A
d. Managers of occupational retirement schemes.	MPFA	Non-compliance with MPF investment requirements may constitute breach of the MPF legislation or MPF investment code and appropriate disciplinary actions may be taken by the MPFA in respect of the breach. In the absence of an alternative credit assessment framework for relevant securities at this stage, no change is proposed.	Ongoing
c) Incentivise compliance with the CRA Principles.			

Action to be taken	Responsible national authority	High-level description of approach to be taken, and necessary or contributory factors to assist implementation (e.g. changes in international standards)	Milestones and expected completion date (e.g. "end-2014" or "one year after new international standards agreed")
a. Insurance companies (in their capacity as institutional investors)	IA	Please see item 3(a)(a) above.	On-going
b. Investment managers (i.e. managers of collective investment schemes).	SFC	N/A. SFC-licensed firms are subject to conduct of business standards, eg Management, Supervision and Internal Control Guidelines for Persons Licensed by or Registered with the Securities and Futures Commission (ICG) and Fund Manager Code of Conduct (FMCC) in which requirements on proper risk controls are set out. The SFC will require firms to put in place remedial measures to rectify any deficiencies identified during the course of supervision, including changes to internal limits and/or investment policies where appropriate. The SFC will keep in view the outcome from the IOSCO's relevant work in reducing reliance on CRA ratings.	N/A

Action to be taken	Responsible national authority	High-level description of approach to be taken, and necessary or contributory factors to assist implementation (e.g. changes in international standards)	Milestones and expected completion date (e.g. "end-2014" or "one year after new international standards agreed")
c. Alternative investment managers (e.g. hedge funds, endowments).	SFC	N/A. Please see item 3(c)(b) above.	N/A
d. Managers of occupational retirement schemes.	MPFA	N/A. CRA credit rating is only one of the criteria/factors being considered.	Ongoing
d) Strengthen supervisory oversight to assess whether investments managers and institutional investors have made changes to the role that CRA ratings play in investment mandates, thresholds and triggers.			
a. Insurance companies (in their capacity as institutional investors)	IA	N/A. CRA ratings usually have a lesser role to play in the management of the risk of an insurer and they are never sole input for investment and reinsurance portfolio management of insurers.	N/A

Action to be taken	Responsible national authority	High-level description of approach to be taken, and necessary or contributory factors to assist implementation (e.g. changes in international standards)	Milestones and expected completion date (e.g. "end-2014" or "one year after new international standards agreed")
b. Investment managers (i.e. mangers of collective investment schemes).	SFC	N/A. Certain investors may impose investment restrictions by reference to CRA ratings. Investment managers are able to conduct their own credit assessment, but may still prefer rated securities for different reasons, such as reducing the amount of internal analytical work, liquidity, etc. The SFC will keep in view the outcome from the IOSCO's relevant work in reducing reliance on CRA ratings.	N/A
c. Alternative investment managers (e.g. hedge funds, endowments).	SFC	N/A. Hedge fund mandates generally do not carry prescriptive rating criteria. Alternative investment managers rely on their own internal credit analysis in making investment decisions. The SFC will keep in view the outcome from the IOSCO's relevant work in reducing reliance on CRA ratings.	N/A

Action to be taken	Responsible national authority	High-level description of approach to be taken, and necessary or contributory factors to assist implementation (e.g. changes in international standards)	Milestones and expected completion date (e.g. "end-2014" or "one year after new international standards agreed")
d. Managers of occupational retirement schemes.	MPFA	Internal limits and investment policies of trustees / managers for compliance with legislative requirements are reviewed regularly as part of the supervisory process. In the absence of an alternative credit assessment framework for relevant securities at this stage, no change is proposed.	Ongoing

Annex V: Collateral Policies for Central Counterparties (CCPs)

Action to be taken	Responsible national authority	High-level description of approach to be taken, and necessary or contributory factors to assist implementation (e.g. changes in international standards)	Milestones and expected completion date (e.g. "end-2014" or "one year after new international standards agreed")
Based on the findings from the stock-taking exercise, please describe the areas identified as needing change and those areas considered priorities, as well as the steps authorities intend to take to reduce reliance on CRA ratings in laws and regulations. In addition, authorities should describe the incentives put in place for market participants to develop their own independent credit assessment processes. Examples of incentives might include disclosure requirements relating to credit risk assessment practices or articulating clear supervisory expectations of the extent to which CCPs should perform their own due diligence.			

The reference to CRA ratings by Hong Kong Securities Clearing Company ("HKSCC") Limited, HKFE4 Clearing Corporation Limited and SEHK5 Options Clearing House Limited, is fairly limited. The only reference to CRA ratings in the rules and procedures is in relation to the admission criteria of General Clearing Participant ("GCP") of HKSCC and it is one of the four admission criteria.

There is no CRA rating reference to collateral policies in the rules and procedures of the above clearing houses.

References to CRA ratings in the counterparty risk management policies are made in the following areas for central counterparties ("CCPs"):

1) Bank Guarantee ("BG") acceptance and limits (currently under review - intention is to phase out BG from the list of admissible collateral)

2) Foreign government securities admission

3) Settlement bank eligibility criteria

In each of the above areas, the three CCPs do not rely solely on CRA ratings to assess creditworthiness. There are other criteria to supplement the assessment. For example, market depth and size of the foreign government securities is one of the criteria to assess in their admission while in considering the on-going eligibility of a settlement bank its history of operational reliability are also assessed.

Whilst credit quality as determined by CRAs is an investment criteria stated in the investment policy of the CCPs, it is not the only criteria in the investment decision process. In addition, the CCPs are in the process of establishing its own "credit library" whereby fundamental credit analysis will be done in-house to supplement external analysis.

The initial plan of the HKSCC is to review the appropriateness of the existing admission criteria including the reference to CRA ratings for GCP in 2015. HKSCC will consider whether to incorporate other financial and non-financial information of an applicant as a supplement or replacement of CRA ratings in the admission requirement.

Action to be taken	Responsible national authority	High-level description of approach to be taken, and necessary or contributory factors to assist implementation (e.g. changes in international standards)	Milestones and expected completion date (e.g. "end-2014" or "one year after new international standards agreed")
1. Reducing reliance on CRA ratings in laws and regulations (Principle I)			
a) Remove references to CRA ratings in laws and regulations relating to collateral policies for CCPs.	N/A.	N/A.	N/A.
b) Develop alternative standards of credit assessment, where necessary, for the purpose of replacing references to CRA ratings in laws and regulations relating to collateral policies for CCPs.	N/A.	N/A.	N/A.
2. Reducing market reliance on CRA ratings (Principle II)			
a) Enhance supervisory processes and procedures to assess the adequacy of CCPs' own credit	N/A.	N/A.	N/A.

[4] Hong Kong Futures Exchange Limited
[5] The Stock Exchange of Hong Kong Limited

Action to be taken	Responsible national authority	High-level description of approach to be taken, and necessary or contributory factors to assist implementation (e.g. changes in international standards)	Milestones and expected completion date (e.g. "end-2014" or "one year after new international standards agreed")
assessment processes.			
3. Application of the basic principles to particular financial market activities (Principle III)			
3.1 Central counterparties and private sector margin agreements (Principle III.4a)			
a) Conduct stress tests or estimate the procyclical effect, on the overall margin requirements for the CCP participants, of a sudden downgrade of the credit ratings of some widely used securities.	N/A.	N/A.	N/A.
b) Assess the reliance on credit ratings in the investment policy of the CCP.	N/A.	N/A.	N/A.
c) Review private sector margin agreements to ensure compliance with the Principle.	N/A.	N/A.	N/A.
d) Require changes to private sector margin agreements.	N/A.	N/A.	N/A.
e) Incentivise compliance with the CRA Principles.	N/A.	N/A.	N/A.

Annex VI: Securities Issuance (debt and equity, whether public issuance or private placement), including asset-backed securities and corporate debt

Action to be taken	Responsible national authority	High-level description of approach to be taken, and necessary or contributory factors to assist implementation (e.g. changes in international standards)	Milestones and expected completion date (e.g. "end-2014" or "one year after new international standards agreed")
Based on the findings from the stock-taking exercise, please describe the areas identified as needing change and those areas considered priorities, as well as the steps authorities intend to take to reduce reliance on CRA ratings in laws and regulations. In addition, authorities should describe the incentives put in place for market participants to develop their own independent credit assessment processes. Examples of incentives might include disclosure requirements relating to credit risk assessment practices.			

Action to be taken	Responsible national authority	High-level description of approach to be taken, and necessary or contributory factors to assist implementation (e.g. changes in international standards)	Milestones and expected completion date (e.g. "end-2014" or "one year after new international standards agreed")
Eligibility of Issuers/ Guarantors for non-collateralised listed structured products An issuer is allowed to issue non-collateralised structured products if it meets one of the four criteria set out in Rule 15A.13 (1) of the Hong Kong Stock Exchange Listing Rules. Having a credit rating which is one of the top three investment grades awarded by a credit rating agency recognised by the Hong Kong Stock Exchange is one of the criteria. In addition, the Listing Rules also require the issuers to have net assets of HK$2 billion and adequate risk management systems and procedures. There are no requirements to disclose an issuer's credit rating in respect of public offerings of shares and debt securities. For listed structured products, the credit rating of the issuer and/or the guarantor is required to be disclosed in the listing documents. For non-collateralised listed structured products, the issuers are also required to include in their listing documents and marketing materials that the listed structured products are uncollateralised and investors are relying on an issuers' credit worthiness when investing in a particular issuer's structured products. The cost and resources implications for developing (and monitoring the use of) alternative standards of assessment for the purpose of replacing references to CRA ratings are substantial. **Unlisted structured investment products ("SIP")** For SIP, the references to credit rating by CRAs are identified in three areas: (i) eligibility of issuers/guarantors; (ii) criteria for collateral; and (iii) disclosure requirements in offering documents/advertisements.			

- *Eligibility of Issuers/ Guarantors*

Pursuant to the Code on Unlisted Structured Investment Products ("SIP Code"), in order to satisfy the core eligibility requirements as an issuer/guarantor for a SIP, an entity shall, among other things, either (i) be a Regulated Entity (i.e. a bank or licensed corporation); or (ii) have a credit rating which is one of the top three investment grades awarded by at least one rating agency of international standing and reputation which is acceptable to the Commission. Such eligibility requirements are in line with the requirements for issuers of listed structured products pursuant to the Listing Rules. It is one of the two means by which an entity may meet the eligibility requirements under the SIP Code as an issuer/ guarantor. Currently, all issuers/ guarantors are banking entities i.e. they do not rely on their credit ratings to be eligible.

- *Criteria for collateral*

In accordance with the SIP Code, where a SIP is collateralised, the collateral shall meet a number of criteria. One of the criteria is that the collateral shall have a credit rating which is one of the top three investment grades awarded by at least one rating agency of international standing and reputation which is acceptable to the Commission. Please note that credit rating is only one of the many criteria to be met by the collateral. The costs (in terms of time, resources and reputational risk) of changing the use of CRA ratings to a direct assessment are substantial, and no alternative provisions in regulations have been identified and can safely be implemented at this stage. Further, issuers of SIP may not have the necessary data, capacity and resources to make their own credit assessment of collateral issued by a third-party issuer and, even if they do, a potential issue of independent objectivity/ upward biases may come into question. Currently, no SIP is collateralised.

- *Disclosure requirements in offering documents/advertisements*

Pursuant to the SIP Code, credit rating is required to be disclosed in offering documents and advertisements for an unlisted structured investment product only if the issuer/guarantor relies on its credit rating so as to meet the eligibility requirements or where the product is collateralised. Where a credit rating is disclosed in an offering document/ advertisement, it shall be accompanied by some information on the source of the credit rating; the meaning of the credit rating and an appropriate warning to the effect that the credit rating (i) is not a recommendation, (ii) is not necessarily an indication of liquidity or volatility, and (iii) may be downgraded if the credit quality of the relevant entity or asset or obligation declines. These warning statements are required to be added so as to *reduce* any mechanistic reliance on CRA ratings by issuers. Currently, no SIP is rated.

1. Reducing reliance on CRA ratings in laws and regulations (Principle I)			
a) Remove references to CRA ratings in laws and regulations related to securities issuance.	N/A	N/A.	N/A
b) Develop alternative standards of credit assessment, where necessary, for the purpose of replacing references to CRA ratings in laws and regulations relating to securities issuance.	N/A	N/A.	N/A
2. Reducing market reliance on CRA ratings (Principle II)			
a) Enhance supervisory processes and procedures to assess the adequacy of market participants own credit assessment processes.	N/A	N/A.	N/A
3. Application of the basic principles to particular financial market activities (Principle III)			
3.1 Central counterparties and private sector margin agreements (Principle III.5a)			
a) Review the role of credit rating in disclosures by issuers of securities.	N/A	N/A.	N/A
b) Reduce the role of credit ratings in disclosures by issuers of securities (list the steps to take).	N/A	N/A.	N/A

Annex VII: Securities Firms (broker-dealers)

Action to be taken	Responsible national authority	Milestones to be met (e.g. changes in international standards)	Milestones and expected completion date (e.g. "end-2014" or "one year after new international standards agreed")
Based on the findings from the stock-taking exercise, please describe the areas identified as needing change and those areas considered priorities, as well as the steps authorities intend to take to reduce reliance on CRA ratings in laws and regulations. In addition, authorities should describe the incentives put in place for market participants to develop their own independent credit assessment processes.			
1. Reducing reliance on CRA ratings in laws and regulations (Principle I)			
a) Remove references to CRA ratings in laws and regulations relating to securities firms.	SFC	N/A. Assessment conducted during peer review did not result in any proposed changes to legislations or regulations. CRA rating is only one of many factors to be considered. The SFC will keep in view the outcome from the IOSCO's and Basel Committee for Banking Supervision (BCBS)'s relevant work in reducing reliance on CRA ratings.	N/A

Action to be taken	Responsible national authority	Milestones to be met (e.g. changes in international standards)	Milestones and expected completion date (e.g. "end-2014" or "one year after new international standards agreed")
b) Develop alternative standards of credit assessment, where necessary, for the purpose of replacing references to CRA ratings in laws and regulations relating to securities firms.	SFC	N/A, please see item 1(a) above.	N/A
2. Reducing market reliance on CRA ratings (Principle II)			
a) Enhance supervisory processes and procedures to assess the adequacy of securities firms' own credit assessment processes.	SFC	N/A. Lending practices are discussed with securities firms which provide financing to clients in assessing the business conduct of the SFC-licensed firms. Likewise, internal credit assessment processes of SFC-licensed investment bank subsidiaries are reviewed during the course of supervision where appropriate. The SFC will keep in view the outcome from the IOSCO's relevant work in reducing reliance on CRA ratings.	N/A