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HKMA consultation begins on review of Three-Tier Banking System

Simon Deane and Sally Lau

On 26 June 2023, the Hong Kong Monetary Authority (“**HKMA**”) issued a consultation paper for a review of Hong Kong’s three-tier banking system.

The current banking system in Hong Kong has three-tiers, comprising of licensed banks (“**LBs**”), restricted licence banks (“**RLBs**”) and deposit-taking companies (“**DTCs**”). This structure has been in place now for four decades and aimed to strike a balance between making entry into the banking system as flexible as possible and protection of small depositors.

Starting from the premise that the three-tier system has become more complex than necessary to achieve the aforesaid balance and that the market share of DTCs has dwindled over time, the HKMA proposes to simplify the three-tier structure into two tiers by merging DTCs into the RLB sector and to replace the three-tier structure with a two-tier banking system.

Further, the HKMA proposes to:-

- (a) discontinue the authorization of new DTCs, and invite and encourage existing DTCs to upgrade themselves into the second-tier (i.e. RLBs) or LBs, within a transition period of 5 years; and
- (b) keep the requirements for the second-tier institutions unchanged, including the minimum capital requirement (i.e. HK\$100 million) and the minimum deposit size requirement (i.e. HK\$500,000), subject to suitable transitional arrangements for existing depositors of DTCs.

The HKMA is of the view that the proposed replacement of the three-tier structure will not have a significant impact on banking stability nor on market dynamics.

The consultation will last until 25 September 2023. Interested parties are welcome to submit their views to the HKMA on or before the deadline.

For the press release, please see [here](#). To access a full copy of the consultation paper, please see [here](#).

HKMA announces Major Enhancements on Protection of Payment Card Customers

Simon Deane and Michelle Ng

The HKMA issued guidance to authorized institutions (“AIs”) which are payment card issuers to enhance protection of payment card customers on 20 June 2023. These AIs are expected to strengthen protection in four areas namely:

- (a) empowerment: enhancing management of card-not-present transactions, suspension and reactivation of cards, credit limits and over-the-limit facilities, as well as encouraging reports of unauthorised transactions;
- (b) support, communication and education: aiming to strengthen the identification, follow-up and precautionary measures for suspicious transactions;
- (c) unauthorised transaction handling and security measures: providing for a pragmatic and transparent investigation process in relation to unauthorised transactions, as well as additional authentication and fraud detection tools; and
- (d) responsible borrowing: providing reminders to cardholders of financial implications of repayment practices, credit limit and cash advance transactions.

The HKMA and the industry will continue to engage with other relevant stakeholders including telecommunication companies to explore the use of technology in bolstering cardholder protection. Relevant AIs are expected to take steps as soon as practicable. They should have complied with the requirements by the end of June 2023, and by the end of 2023 for those involving system changes.

The HKMA circular is available [here](#). To view the details of the enhancement measures, please click [here](#).

Hong Kong Deposit Protection Board consults on enhancements to the Deposit Protection Scheme

Simon Deane and Natalie Chan

On 13 July 2023, the Hong Kong Deposit Protection Board issued a consultation paper (“**Consultation Paper**”) on some proposed enhancements to the Deposit Protection Scheme (“**DPS**”). The Consultation Paper contains a number of policy recommendations on enhancing protection of depositors in Hong Kong, following a comprehensive review which was initiated in 2021. DPS protects the deposits of both personal and corporate depositors held with licensed banks in Hong Kong (not with the other types of AI), but does not protect the deposits of AIs, foreign banks or persons/companies related to a DPS scheme member.

One of the key enhancements is to increase the protection limit from the current HK\$500,000 to HK\$800,000 per depositor. This will expand the coverage of protected depositors from the current 89% to 92%, in line with an international standard with a reasonable buffer. Under this proposal, the deposits in the banking system that are protected will also be increased by 26% to HK\$3.3 trillion, making up 25% of the total deposits in the banking system.

Another key enhancement relates to the merger of licensed banks which are both scheme members of the DPS. In cases where the depositors have deposits with more than one scheme members which are in the process of merging, each affected depositor will be entitled to compensation in respect of his/her protected deposits up to HK\$800,000 with each relevant scheme member during a grace period of six months upon the bank merger, as if the merger had not occurred.

For more information on the Consultation Paper, please see [here](#).

Launch of bank-to-bank information sharing platform (FINEST)

Simon Deane and Jennifer Lok

The Financial Intelligence Evaluation Sharing Tool (“**FINEST**”), a bank-to-bank information sharing platform developed by the Hong Kong Association of Banks (“**HKAB**”) in partnership with the Hong Kong Police Force (“**HKPF**”) and the HKMA, launched its pilot phase on 20 June 2023. FINEST provides a secure and efficient platform for sharing data relating to suspected financial crimes among banking institutions.

The aim of this bank-to-bank information sharing initiative is to facilitate the detection and prevention of financial crime across the banking sector, thereby helping to mitigate fraud and money laundering risks.

The pilot phase of FINEST focuses on corporate data, and involves the participation of five domestic systemically important AIs (D-SIBs), namely Bank of China (Hong Kong) Limited, Standard Chartered Bank (Hong Kong) Limited, The Hongkong and Shanghai Banking Corporation Limited, Hang Seng Bank Limited and Industrial and Commercial Bank of China (Asia) Limited. It is expected that more banks will join FINEST in phases, and the scope of information to be shared will be further expanded, e.g. to cover personal accounts, in the future.

Please click the links for the press releases from the HKMA ([link](#)), HKAB ([link](#)) and HKPF ([link](#)).

HKMA issues consultation on timeline for implementing Basel III final reform package

Simon Deane and Crystal Choi

On 4 August 2023, the HKMA wrote to the banking industry to consult on the timeline for implementing the Basel III final reform package.

The HKMA proposes that the implementation of the Basel III final reform package will start from a date no earlier than 1 July 2024, covering the revised standards on credit risk, operational risk and output floor as a minimum regulatory requirement, and the revised standards on market risk and credit valuation adjustment (“**CVA**”) risk as a reporting-only requirement. The revised market risk and CVA risk standards will take effect as minimum regulatory requirements on a date no earlier than 1 January 2025. The implementation dates of the revised disclosure requirements will follow those of their associated policy standards.

The consultation period for the proposed timelines ends on 4 September 2023 and the HKMA is working towards releasing the final set of rules by October 2023 for statutory consultation as required under the Banking Ordinance (Cap. 155).

The letter from the HKMA is available [here](#).

Want to know more?

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