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Self-Governance and State Regulation

Code of Banking Practice

In addition to a code of conduct proclaimed by individual banks, Hong Kong and Australia each have a code of banking practice issued by the respective banking associations. In order to appreciate the banking situation in Hong Kong, it is worthwhile to look at the Hong Kong Association of Banks (HKAB) and to examine its role and its relationship with the Hong Kong Monetary Authority (HKMA), which has the exclusive power to approve the establishment of licensed banks, restricted banks and deposit-taking companies, but the focus in this monograph is only on licensed banks. Once a bank receives a license to operate, it has a statutory obligation to become a member of the HKAB, which has traditionally had a pivotal role in the establishment of banking practices and guidelines. The locally established banks are entitled to select their own representatives, whereas the foreign banks have to choose representatives according to their geographical grouping. The HKAB has three permanent members, namely the Hong Kong Bank (HSBC), the Standard Chartered Bank and the Bank of China, each of which rotates annually as chair of the HKAB. These three are not only the largest banks in Hong Kong but also have a notable statutory function, namely as officially designated note issuers of the Hong Kong currency, which is a unique privilege held only by central banks in other countries.

Until the relatively recent establishment of the HKMA, which subsumed the previous Commissioner of Banking, the HKAB had a much broader unofficial role. Not only did the three permanent members issue the currency, but they also effectively established the interest rates, and thus the HKAB was referred to as a banking cartel. The HKMA has endeavoured to break up the interest-setting cartel by stipulating that market forces must determine interest rates. Despite this measure, the three permanent members remain the largest banks, continue to be the
official note issuers and dominate monetary trading, so they exert considerable influence on interest rate movements and are effectively the market makers.

These permanent members perform another key role, which is normally carried out by the central bank of the country, namely as the official clearing banks: HSBC and HKMA for US dollars, HSBC for HK dollars and Bank of China for PRC RMB (Chinese renminbi). In its role of US dollar clearing, HSBC cooperates closely with the Federal Reserve Bank of the United States.

Together with the Deposit Taking Companies Association, the HKAB has also issued the Code of Banking Practice (COBP), which is intended:

(a) to promote good banking practices by setting out the minimum standards which institutions should follow in their dealings with personal customers;
(b) to increase transparency in the provision of banking services so as to enhance the understanding of customers of what they can reasonably expect of the services provided by the institutions;
(c) to promote a fair and cordial relationship between institutions and their customers;
(d) through the above, to foster customer confidence in the banking system.¹

The HKMA fully endorses the COBP-recommended practices and standards and expects all banks to take active steps to ensure full compliance with the COBP, which some senior bankers believe actually emanates from the Authority. It believes that the COBP will help to further enhance the transparency and quality of banking services in Hong Kong as well as Hong Kong’s status as an international financial centre. As part of its regular supervision and to set up the monitoring of banks’ compliance with the COBP, the HKMA has required all banks to commission their internal audit departments or other equivalent units to conduct an annual self-assessment of their compliance with the COBP. The self-assessment results are required to be submitted in the standard template to the HKMA by the timeline as imposed by the HKMA. The self-assessment aims to encourage banks to rectify any weaknesses identified at an early stage. Where non-compliance areas are identified during the self-assessment process, banks should specifically provide the details, remedial plan and target completion date. The HKMA closely monitors banks’ progress in implementing the rectification plans. The self-assessment results also enable the HKMA to analyse the compliance