

CORPORATE GOVERNANCE

Whether the DPS can be effective in promoting banking stability depends to a large extent on the confidence of the public in the DPS to honour its commitments when a bank failure occurs. Apart from putting in place an efficient payout infrastructure and engendering a high level of public awareness and understanding of the DPS, public perception of the integrity of the Board is also critical to building up confidence in the DPS. The Board is therefore fully aware that it must subscribe to sound corporate governance practices in administering the DPS. Given the nature of the Board and the functions of the DPS, the corporate governance structure of the Board shares the characteristics of both a public organisation and a deposit insurer.

COMPOSITION AND PROCEEDINGS OF THE BOARD

The Board is an independent statutory body formed under the DPS Ordinance. It is, however, subject to the oversight of the Financial Secretary who is responsible for approving the Board's annual budget and tabling the Board's annual report to the Legislative Council.

The functions and composition of the Board are defined by the DPS Ordinance and, as such, the Board shall comprise between six to nine members, all of whom are non-executive members. Except for the two ex-officio members, all other members are appointed for a fixed, but renewable term. These members are appointed mainly because they possess professional or occupational experience relevant to the operation of the DPS.

The proceedings of the Board are governed by the relevant provisions in the DPS Ordinance. The Board meets three to four times every year to deliberate policy issues crucial to the operation and development of the DPS. In 2007-08, the Board met three times. On average, over 75% of members were present at each meeting.

Under the DPS Ordinance, the Board may appoint committees to assist in performing its functions. An Investment Committee comprising members with experience and expertise in banking and investment matters has been formed to advise the Board on the investment of the DPS Fund. The Chairman and a majority of the members of the Committee are also members of the Board.

EXECUTIVE MANAGEMENT

Pursuant to section 6 of the DPS Ordinance, the Board shall perform its functions through the MA unless otherwise directed by the Financial Secretary. This means the MA, acting as the executive arm of the Board, is responsible for managing the day-to-day operation of the DPS and assisting the Board in developing and implementing corporate policies and strategies.

The powers that can be exercised by the Board in administering the DPS are detailed in the DPS Ordinance. The Board has established clear guidelines on the division of responsibilities between the Board, the Management Team and other supporting divisions of the HKMA, and between the posts of the Chairman and the Chief Executive Officer, which have been separated in

line with good corporate governance practice. In general, strategic decisions relating to the operation and development of the DPS and those decisions requiring an exercising of the Board's powers under the DPS Ordinance have to be taken by the Board. The Management Team, on the other hand, is responsible for maintaining the day-to-day operation of the DPS according to the policies and principles endorsed by the Board.

INTERNAL CONTROLS AND AUDITS

Assisted by the Internal Audit Division (IAD) of the HKMA, which is a division independent of the department in the HKMA supporting the Board, the Management Team performs an annual assessment of the risks inherent in different operational areas of the Board, and evaluates whether appropriate controls are in place to safeguard the Board against the potential risks identified. The findings of the risk assessment will form the basis for the IAD to formulate its annual plan for auditing the operation of the DPS.

The IAD performs an annual audit of the DPS to ensure that the various internal control procedures of the Board have been properly adhered to, especially on activities posing a relatively high level of risk to the Board. The IAD will report its findings directly to a meeting of the Board. The IAD reported satisfactory results on the audit conducted in 2007.

The appointment of the external auditor of the DPS Fund requires the approval of the Financial Secretary. The external auditor is responsible for auditing the annual statement of accounts of the

DPS Fund prepared by the Board. The external auditor will report its findings directly to the Board. The external auditor for the year under review was PricewaterhouseCoopers (PwC). Apart from auditing the statement of accounts for 2007-08, PwC did not offer any non-audit service to the Board.

CONFLICTS OF INTEREST AND CODE OF CONDUCT

In line with the good corporate governance standards applicable to deposit insurers, government representatives, including those of the HKMA, account for only a minority of the members of the Board. This allows the government and the banking supervisor to contribute to the operation of the DPS from the public administration and financial regulatory perspectives, but prevents the Board from overtly exposing itself to the influence of the government and other financial safety-net players. The Management Team assigned by the HKMA to assist the Board is not responsible for banking supervisory matters. The operation of the Board is insulated from the influence of the banking industry as no employees or directors of banks and banks' related companies can be appointed as a Board member.

The Board has established clear guidelines and procedures for disclosing interests and avoiding conflicts of interest. The relevant guidelines and procedures are set out in the DPS Ordinance and the Codes of Conduct for members and staff of the Board. Board members are required to register in writing their personal interests when

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they first join the Board or its committees, and annually thereafter, to the secretary of the Board. The register of Members' interests is kept by the secretary and is available for public inspection. Senior staff members of the Board are required to make a declaration to the Chairman of the Board annually. Specific procedures are available on how members and staff of the Board should report their interests and be excused from a decision-making process.

COMMUNICATION AND TRANSPARENCY

The Board is committed to open communication with the public and other stakeholders. It has set up an enquiry hotline to answer questions from the public, and maintains a website to facilitate access to information on different aspects of the DPS operations. In 2007-08, the website registered close to 100,000 visits. The Board also publishes an annual report.



APPEAL MECHANISM

Certain decisions made by the Board and the MA under the DPS Ordinance can be the subject of an appeal to the Deposit Protection Appeals Tribunal. The Tribunal is chaired by a High Court judge appointed by the Chief Executive. Members of the Tribunal are appointed by the Financial Secretary from a panel of six people appointed by the Chief Executive.

REGULAR REVIEW OF THE CORPORATE GOVERNANCE STRUCTURE

The Board has set a policy of reviewing its corporate governance structure regularly to ensure that it continues to adhere to sound corporate governance standards, despite any expansion or change in the scope of the Board's operation driven by the development of the DPS. The review conducted by the Board in 2007-08 indicates the governance structure remains in substantial compliance with the best practices adopted by comparable public organisations and other deposit insurers. In between reviews, refinements will be made as and when necessary as the Board gains experience with operating the DPS.