

Financial Institutions (Resolution) (Contractual Recognition of Suspension of Termination Rights—Banking Sector) Rules

(Cap. 628 sub. leg. C)

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(Cap. 628, section 92)

(Enacting provision omitted—E.R. 1 of 2022)

[27 August 2021]

Part 1

Preliminary

1. *(Omitted as spent—E.R. 1 of 2022)*

2. **Interpretation**

In these Rules—

covered contract (受涵蓋合約)—

- (a) in relation to a covered entity that is an authorized institution incorporated in Hong Kong or an HK holding company, means a financial contract entered into by the covered entity that—
 - (i) is governed by non-Hong Kong law; and
 - (ii) contains a termination right exercisable by a counterparty other than an excluded counterparty; or
- (b) in relation to a covered entity that is a related company of an authorized institution incorporated in Hong Kong,

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means a financial contract entered into by the covered entity that—

- (i) is governed by non-Hong Kong law;
- (ii) contains a termination right exercisable by a counterparty other than an excluded counterparty; and
- (iii) contains an obligation of the covered entity that is guaranteed or otherwise supported by an authorized institution incorporated in Hong Kong, or an HK holding company, that is a group company of the covered entity;

covered entity (受涵蓋實體) means—

- (a) an authorized institution incorporated in Hong Kong;
- (b) an HK holding company; or
- (c) a related company of an authorized institution incorporated in Hong Kong;

excluded counterparty (獲豁免對手方), in relation to a contract, means a counterparty to the contract that is—

- (a) a financial market infrastructure;
- (b) the Monetary Authority;
- (c) the Government;
- (d) the government of a non-Hong Kong jurisdiction; or
- (e) the central bank of a non-Hong Kong jurisdiction;

financial contract (金融合約) means a contract listed in Part 2 of the Schedule or any combination of such contracts, other than a contract or combination of contracts for short-term inter-bank borrowing with an original maturity of 3 months or less;

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group company (集團公司), in relation to a covered entity, means a body corporate that is a member of the same group of companies as the covered entity;

HK holding company (香港控權公司) means an entity that is a holding company incorporated in Hong Kong of an authorized institution incorporated in Hong Kong, but is not itself an authorized institution;

initial day (起始日), in relation to a covered entity, or a covered contract entered into by it, means—

- (a) the day on which these Rules come into operation; or
- (b) if it is not a covered entity on that day—the later day on which it becomes a covered entity;

initial period (起始期間), in relation to a covered contract, means the period set out in rule 5(3);

related company (關連公司), in relation to an authorized institution incorporated in Hong Kong, means a group company of the authorized institution that is not itself an authorized institution incorporated in Hong Kong or an HK holding company;

resolution authority (處置機制當局) means the resolution authority in relation to a banking sector entity;

Note—

Under section 2(1) of the Ordinance, the resolution authority in relation to a banking sector entity is the Monetary Authority.

suspension of termination rights provision (暫停終止權條文) means a term or condition (made, or evidenced, in writing) of a covered contract to the effect that the parties to the contract agree in a legally enforceable manner that, despite any other term or condition of the contract or any other agreement, arrangement or understanding, the parties (other than an excluded counterparty) will be bound by a suspension of a

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termination right in relation to the contract imposed by the resolution authority under section 90(2) of the Ordinance;

termination right (終止權), in relation to a covered contract, means—

- (a) a right to terminate the contract;
 - (b) a right to accelerate, close out, set off or net obligations, or any similar right that suspends, modifies or extinguishes an obligation of a party to the contract; or
 - (c) a right to prevent an obligation from arising under the contract.
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Requirement for Covered Contracts to Contain Suspension of Termination Rights Provision

- 3. Requirement on covered entity for covered contracts to contain suspension of termination rights provision**
- (1) A covered entity must ensure that a suspension of termination rights provision is contained in a covered contract that is—
 - (a) entered into by the covered entity on or after the initial day; or
 - (b) entered into by the covered entity before the initial day but—
 - (i) renewed on expiry of its term on or after that day (irrespective of whether the renewal is automatic or requires any action on the part of the covered entity or any counterparty to the contract); or
 - (ii) materially amended on or after that day (irrespective of whether the amendment is automatic or requires any action on the part of the covered entity or any counterparty to the contract).
 - (2) Subject to subrule (3), if a contract is not a covered contract when it is entered into but becomes a covered contract at a time on or after the initial day (*relevant time*), the contract is taken for the purposes of this rule to be a covered contract entered into when it becomes a covered contract.
 - (3) Subrule (2) does not apply—
 - (a) if—

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- (i) the contract becomes a covered contract falling within paragraph (a) of the definition of **covered contract** in rule 2, because a party to the contract becomes an authorized institution incorporated in Hong Kong or an HK holding company; and
 - (ii) immediately before the relevant time, the contract would have been a covered contract falling within paragraph (a) of that definition, but for the party not being an authorized institution incorporated in Hong Kong or an HK holding company; or
- (b) if—
- (i) the contract becomes a covered contract falling within paragraph (b) of that definition, because—
 - (A) the entity (**Entity A**) that guarantees or otherwise supports an obligation of a party to the contract (**Entity B**) becomes an authorized institution incorporated in Hong Kong, or an HK holding company, that is a group company of Entity B; or
 - (B) in the case that Entity A is, immediately before the relevant time, an authorized institution incorporated in Hong Kong or an HK holding company—Entity B becomes a related company of Entity A, or becomes a related company of an authorized institution incorporated in Hong Kong that is a group company of Entity A; and
 - (ii) immediately before the relevant time, the contract would have been a covered contract falling within paragraph (b) of that definition, but for the absence of the circumstance mentioned in subparagraph (i).

- (4) For the purposes of subrule (1)(b)(ii) but without limiting that subrule, a covered contract is materially amended if an amendment is made to the contract to create a new right or obligation of a party to the contract.
- (5) A failure of a covered entity to comply with subrule (1) in relation to a covered contract does not affect any power of the resolution authority under section 90(2) of the Ordinance to suspend a termination right under the contract.

4. When covered entity must comply

Subject to rule 5, a covered entity must—

- (a) comply with rule 3(1) in relation to a covered contract when the contract is entered into, renewed or materially amended (as the case requires); and
- (b) continue to comply with that rule throughout the term or remaining term of the contract (as the case requires), including the term or remaining term of the contract as renewed or materially amended.

5. Initial period for compliance

- (1) This rule applies if, in the following period, a covered entity enters into a covered contract, or a covered contract entered into by a covered entity is renewed or materially amended—
 - (a) the initial period for the contract; or
 - (b) if the initial period is extended under rule 6(1)—subject to any variation under rule 6(2) or any condition imposed under rule 6(3), the initial period so extended.
- (2) The covered entity must—
 - (a) comply with rule 3(1) in relation to the covered contract by the end of the period specified in subrule (1); and

- (b) continue to comply with that rule throughout the term or remaining term of the contract (as the case requires), including the term or remaining term of the contract as renewed or materially amended.
- (3) The initial period for a covered contract is—
 - (a) the period of 24 months beginning on the initial day, for a contract where there are no counterparties other than—
 - (i) an authorized institution; or
 - (ii) a financial institution (other than an authorized institution) that is a global systemically important bank on the initial day; or
 - (b) the period of 30 months beginning on the initial day, for any other contract.
- (4) Any excluded counterparties to a covered contract are to be ignored for the purposes of subrule (3)(a).

6. Resolution authority may extend initial period

- (1) The resolution authority may, by written notice served on a covered entity, extend the initial period for a covered contract or a class of covered contract, if satisfied that it is prudent to do so.
- (2) The resolution authority may, by written notice served on a covered entity, vary or revoke an extension under subrule (1), if satisfied that it is prudent to do so.
- (3) The resolution authority may do the following, if satisfied that it is prudent to do so—
 - (a) in a notice under subrule (1) or (2), impose conditions on an extension;

- (b) by written notice served on a covered entity, vary or revoke any conditions of, or impose further conditions on, an extension.
- (4) In determining whether it is prudent to extend the initial period, vary or revoke an extension, impose a condition on an extension or vary or revoke a condition of an extension, the resolution authority may take into account—
 - (a) any strategies devised by the resolution authority under section 13(1)(a) or (2)(a) of the Ordinance for securing an orderly resolution of—
 - (i) if the covered entity is an authorized institution incorporated in Hong Kong—the covered entity or an HK holding company of the covered entity;
 - (ii) if the covered entity is an HK holding company—the covered entity or an authorized institution incorporated in Hong Kong that is a subsidiary of the covered entity; or
 - (iii) if the covered entity is a related company of an authorized institution incorporated in Hong Kong—an authorized institution incorporated in Hong Kong, or an HK holding company, that is a group company of the covered entity; and
 - (b) any other matters the resolution authority considers relevant.

7. Resolution authority may exempt covered entity from requirements

- (1) The resolution authority may, by written notice served on a covered entity, exempt the covered entity from compliance with rule 3(1) for a covered contract or a class of covered contract, if satisfied that it is prudent to do so.

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- (2) The resolution authority may, by written notice served on a covered entity, vary or revoke an exemption under subrule (1), if satisfied that it is prudent to do so.
- (3) The resolution authority may do the following, if satisfied that it is prudent to do so—
 - (a) in a notice under subrule (1) or (2), impose conditions on an exemption;
 - (b) by written notice served on a covered entity, vary or revoke any conditions of, or impose further conditions on, an exemption.
- (4) In determining whether it is prudent to exempt a covered entity, vary or revoke an exemption, impose a condition on an exemption or vary or revoke a condition of an exemption, the resolution authority may take into account—
 - (a) any strategies devised by the resolution authority under section 13(1)(a) or (2)(a) of the Ordinance for securing an orderly resolution of—
 - (i) if the covered entity is an authorized institution incorporated in Hong Kong—the covered entity or an HK holding company of the covered entity;
 - (ii) if the covered entity is an HK holding company—the covered entity or an authorized institution incorporated in Hong Kong that is a subsidiary of the covered entity; or
 - (iii) if the covered entity is a related company of an authorized institution incorporated in Hong Kong—an authorized institution incorporated in Hong Kong, or an HK holding company, that is a group company of the covered entity;

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- (b) any risks to the stability and effective working of the financial system of Hong Kong, including to the continued performance of critical financial functions, that may be posed by the non-viability of—
 - (i) if the covered entity is an authorized institution incorporated in Hong Kong—the covered entity;
 - (ii) if the covered entity is an HK holding company— an authorized institution incorporated in Hong Kong that is a subsidiary of the covered entity; or
 - (iii) if the covered entity is a related company of an authorized institution incorporated in Hong Kong—an authorized institution incorporated in Hong Kong that is a group company of the covered entity; and
 - (c) any other matters the resolution authority considers relevant.
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Part 3

Compliance and Enforcement

8. Systems of control and record keeping

A covered entity must at all times—

- (a) have adequate systems of control in place to ensure compliance by it with—
 - (i) rule 3(1); and
 - (ii) any conditions of an extension under rule 6 or of an exemption under rule 7; and
- (b) keep sufficient records to demonstrate compliance by it with—
 - (i) rule 3(1);
 - (ii) any conditions of an extension under rule 6 or of an exemption under rule 7; and
 - (iii) paragraph (a).

Note—

Under section 158 of the Ordinance, the resolution authority may require a controlled entity or a third party entity to provide information or produce records or documents that the resolution authority reasonably requires in connection with the performance of its functions under the Ordinance. Section 159 of the Ordinance provides for related offences. A covered entity is a controlled entity within the meaning of those sections (see sections 2(1) and 154 of the Ordinance).

9. Resolution authority may require covered entity to provide legal opinion

The resolution authority may require a covered entity to provide to the resolution authority an opinion acceptable to the resolution authority from counsel or a solicitor that a suspension of

termination rights provision contained in a covered contract in compliance with rule 3(1) is legally enforceable.

10. Requirement to notify resolution authority of failure to comply

If, in relation to a covered contract, a covered entity fails to comply with rule 3(1) in accordance with rule 4 or 5(2) (as the case requires), the covered entity must—

- (a) as soon as practicable notify the resolution authority in writing; and
- (b) provide particulars to the resolution authority on request.

11. Rectification plans

- (1) If, in relation to a covered contract, a covered entity fails to comply with rule 3(1) in accordance with rule 4 or 5(2) (as the case requires), the resolution authority may, by written notice served on the covered entity, require the covered entity to—
 - (a) propose, within the period specified in the notice, a plan acceptable to the resolution authority to rectify the failure; and
 - (b) implement the plan.
- (2) The covered entity must specify in a plan proposed in response to a notice served on it under subrule (1) a period within which it proposes to rectify the failure.
- (3) The resolution authority may, by written notice served on the covered entity, extend the period for the covered entity to rectify the failure, if satisfied that it is prudent to do so.
- (4) The service of a notice on a covered entity under subrule (1) or (3), does not affect any power of the resolution authority under section 14 of the Ordinance in relation to—

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- (a) if the covered entity is an authorized institution incorporated in Hong Kong—the covered entity or an HK holding company of the covered entity;
 - (b) if the covered entity is an HK holding company—the covered entity or an authorized institution incorporated in Hong Kong that is a subsidiary of the covered entity; or
 - (c) if the covered entity is a related company of an authorized institution incorporated in Hong Kong—an authorized institution incorporated in Hong Kong, or an HK holding company, that is a group company of the covered entity.
- (5) A covered entity commits an offence and is liable on conviction to a fine at level 2 if the covered entity, without reasonable excuse, fails to—
- (a) propose a plan in compliance with a requirement imposed on the covered entity under subrule (1)(a); or
 - (b) implement a plan proposed in compliance with that requirement within the period specified in the plan or, if the period is extended under subrule (3), within the period so extended.
- (6) If a covered entity commits an offence under subrule (5), an officer of the covered entity also commits an offence under that subrule if the officer—
- (a) authorized or permitted the commission of the offence by the covered entity; or
 - (b) was knowingly concerned in any way (whether by act or omission) in the commission of the offence by the covered entity.

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- (7) An officer who commits an offence under subrule (5) is liable on conviction to a fine at level 2 and to imprisonment for 6 months.
 - (8) An officer of a covered entity may commit an offence under subrule (5) whether or not the covered entity has been prosecuted for, or found guilty of, an offence under that subrule.
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Schedule

[r. 2]

Financial Contracts

Part 1

Interpretation

1. Interpretation

In this Schedule—

financial accommodation (財務通融) has the meaning given by section 1 of Part 1 of Schedule 1 to the Securities and Futures Ordinance (Cap. 571);

transferable securities (可轉讓證券) has the meaning given by section 2(1) of the Financial Institutions (Resolution) (Protected Arrangements) Regulation (Cap. 628 sub. leg. A).

Part 2

Financial Contracts

1. Securities contracts, that is—

- (a) contracts for the purchase, sale or loan of a transferable security or a group or index of transferable securities;
- (b) repurchase or reverse purchase transactions on a transferable security or a group or index of transferable securities; or

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- (c) securities margin financing transactions, that is, transactions for providing financial accommodation in order to facilitate—
 - (i) the acquisition of transferable securities; or
 - (ii) (if applicable) the continued holding of those securities,
whether or not those or other securities are pledged as security for the accommodation.
- 2. Commodities contracts, that is—
 - (a) contracts for the purchase, sale or loan of a commodity or a group or index of commodities; or
 - (b) repurchase or reverse purchase transactions on a commodity or a group or index of commodities.
- 3. Derivatives contracts, that is, financial instruments the value of which is determined by reference to the price or value of, or changes in the price or value of, at least one underlying asset, financial instrument, index, rate or thing of any kind designated in the instrument and includes forwards contracts, futures contracts, options contracts and swap agreements.
- 4. Contracts for the purchase, sale or delivery of Hong Kong currency or any other currency.
- 5. Contracts of a similar nature to a contract listed in item 1, 2, 3 or 4.
- 6. Master or other agreements in so far as they relate to a contract listed in item 1, 2, 3, 4 or 5.