

Hong Kong: Mandatory Reference Checking Scheme for Banks

In brief

The Hong Kong Monetary Authority (HKMA) recently released its Consultation Conclusions Paper ("**Consultation Conclusions**") on Implementation of Mandatory Reference Checking Scheme ("**MRC Scheme**") to Address the "Rolling Bad Apples" Phenomenon.¹ The proposal will be implemented in two phases. In view of the feedback during the consultation process, the Consultation Conclusions have revised the scope of personnel to be covered in the MRC Scheme from the initial proposal. Modifications and refinements to certain operational details of the MRC Scheme, as well as the implementation timetable will be led by an industry working group (IWG) to be established by the Hong Kong Association of Banks. We discuss the key aspects of the Consultation Conclusions and the employment ramifications in more detail below.

In this issue

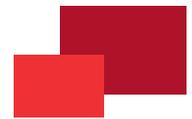
- [In depth](#)
- [Implementation timeline](#)
- [Next Steps](#)

In depth

We summarise the currently proposed MRC Scheme as follows:

<p>What financial institutions will be covered under the MRC Scheme?</p>	<ul style="list-style-type: none"> • The MRC Scheme will only be applicable to HKMA regulated Authorised Institutions (AIs) planning to enter into a new employment relationship with prospective personnel ("recruiting AIs"), who will be required to approach all former and current employers of the prospective personnel which are also AIs ("reference providing AIs").
<p>Which personnel will be covered under Phase 1?</p>	<ul style="list-style-type: none"> • Directors approved under section 71 of the Banking Ordinance (BO). • Chief Executives (CEs) and Alternative Chief Executives (ACEs) approved under section 71 of the BO. • Managers appointed under section 72B of the BO. • Executive Officers (EOs) approved under section 71C of the BO. • Responsible Officers appointed under the Insurance Ordinance (IO) or the Mandatory Provident Fund Schemes Ordinance (MPFSO).
<p>Which additional personnel will be covered under Phase 2?</p>	<ul style="list-style-type: none"> • Staff of an AI licensed or registered to carry out regulated activities under the Securities and Futures Ordinance (SFO), IO or MPFSO, which cover relevant individuals, Insurance Authority licensed technical representatives and Mandatory Provident Fund Schemes Authority registered subsidiary intermediaries. • Any other roles that may subsequently be added by the IWG.

¹ Consultation Conclusions Paper on Implementation of Mandatory Reference Checking Scheme to Address the "Rolling Bad Apples" Phenomenon (hkma.gov.hk)



<p>What information will "reference providing AIs" need to provide to "recruiting AIs"?</p>	<p>The details of the scope of information to be provided are subject to further consideration by the IWG.</p> <p>In principle, the HKMA agrees that reportable information should be confined to that which is material or serious in nature and should generally fall within the below categories:</p> <ol style="list-style-type: none"> i. Breach of legal or regulatory requirements relating to the BO, IO, MPFSO and SFO. ii. Incidents which cast serious doubts on honesty, integrity or matters of a similar nature. iii. Misconduct reports filed with the HKMA - this should cover those filed against an individual regardless of whether the report is filed specifically with the HKMA or with other relevant authorities and copied to the HKMA. iv. Internal or external disciplinary actions arising from conduct matters - internal disciplinary actions should include actions that are taken by the AI against the relevant employee as a result of misconduct on the part of that employee. This may include, for example, internal warnings (either written or verbal form); financial penalty involving remuneration; and suspension and dismissal as a result of misconduct. External disciplinary actions refer to those taken by regulatory bodies, industry associations and professional bodies against the individual during their employment with the reference providing AI. v. Any other additional information relevant to the fit and proper assessment - this would cover information about incidents or matters that (1) occurred, or existed within the specified period before the date of the reference request; or between the date of the reference request and the date the reference providing AI provides the reference; and (2) is related to misconduct that is of a material or serious nature.
<p>Will there be any further clarification of the scope of the information to be included in the reference?</p>	<p>The HKMA has proposed that the IWG shall:</p> <ul style="list-style-type: none"> • prepare guidance on the types of ongoing investigations to be included and the types of exemptions that should apply; • set out more specific criteria for the types of investigations or reviews to be included; and • deliberate on and provide more practical guidance with examples on what constitutes "reportable information".
<p>Will there be a standard form template to facilitate responses for the purposes of the MRC Scheme?</p>	<p>The HKMA has suggested that the IWG may take the lead to develop or revise an industry standard template.</p>
<p>What period of time will the MRC Scheme cover?</p>	<p>Employment records will need to be retained for seven years for the purposes of the MRC Scheme, subject to further deliberation by the IWG.</p>
<p>How long will reference providing AIs have to respond to a request from a recruiting AI?</p>	<ul style="list-style-type: none"> • Reference providing AIs will have one month, commencing from the day that the MRC request is made by the recruiting AI, to respond to a request. • The HKMA notes that refinements to the response time can be considered by the IWG having regard to industry feedback and operational experience.
<p>What if there are difficulties for a reference providing AI providing information or a recruiting AI cannot obtain a response from a reference providing AI?</p>	<ul style="list-style-type: none"> • Reference providing AIs may provide interim responses and should also explain the reasons for the difficulties in responding. • Recruiting AIs will be considered to have discharged their obligations if they do not receive a response within a month from a reference providing AI or any longer period mutually agreed between both parties.



<p>Is there any enforcement mechanism to address failure by a reference providing AI to respond to requests?</p>	<ul style="list-style-type: none"> In cases where there are repeated failures by a reference providing AI to respond, this should be brought to the attention of the IWG and may be followed up by the HKMA.
<p>What if the individual refuses to consent or withdraws consent to the MRC process?</p>	<ul style="list-style-type: none"> The recruiting AI should consider the reasons for the refusal to provide consent and whether it casts doubt on the fitness and propriety of the individual. If an AI decides to proceed to employ an individual without conducting MRC, the justifications for such exemption should be documented. Where prospective personnel withdraw their consent, the recruiting AI should inform the reference providing AI as soon as possible so that the reference providing AI can cease providing the MRC information. The HKMA welcomes the IWG to determine a standardised notification template which could be used by recruiting AIs when an individual withdraws consent.
<p>Can an AI still employ prospective employees/ continue to employ a recently hired individual after being informed of misconduct?</p>	<ul style="list-style-type: none"> Recruiting AIs are strongly encouraged to complete all the MRC processes before on-boarding prospective employees. With the exception of positions that require regulatory approvals, an AI will retain the discretion whether to proceed with, or terminate, a proposed offer of employment or ongoing employment of an individual after becoming aware of negative information. The AI should take into consideration factors including the competence of the individual, relevant regulatory requirements and the likelihood of the individual committing misconduct again in the new working environment. AIs should document the factors that were considered as part of the decision to proceed with a proposed offer of employment or maintain ongoing employment.
<p>Should prospective employees be informed of, and given an opportunity to respond to any negative information?</p>	<ul style="list-style-type: none"> Yes. Subject to any legal or regulatory prohibition preventing the prospective employees from being made aware of the information, they should be provided with procedural fairness and an opportunity to address the information that has been obtained. The HKMA has noted that it would be appropriate for the IWG to consider the practical issues associated with such a process in more detail taking into account the Privacy Commissioner for Personal Data's view.
<p>Can AIs outsource the MRC process to external service providers?</p>	<ul style="list-style-type: none"> Yes provided that the AI remains ultimately responsible for ensuring compliance with the relevant supervisory requirements applicable to outsourcing. The Consultation Conclusions note that in particular, AIs should have contractual arrangements and relevant controls in place to safeguard the security and storage of data leakage if outsourcing is used.

Implementation timeline

The IWG is responsible for facilitating the operation of the MRC Scheme and will determine the timeline for implementation, which is still to be confirmed. The IWG is currently anticipated to provide operational details of the MRC Scheme within 6 months from the date of issue of the Consultation Conclusions (i.e. by 3 November 2021), and may consult further with the HKMA on the detailed implementation timeline. A review of the implementation of Phase 1 of the MRC Scheme is to be conducted two years after its implementation.



Next Steps

Whilst the final requirements for the MRC Scheme remain to be determined and published, AIs should nevertheless commence preparation for its implementation by taking actions including:

- continuing to observe the output of the IWG to determine the nature and extent of any potential refinements that are proposed to the MRC Scheme;
- determining how the MRC Scheme requirements differ to any existing internal reference checking procedures and what changes will need to be made to existing recruiting processes and procedures including offers of employment;
- determining how the MRC Scheme requirements may impact internal investigation processes;
- confirming the current policies regarding the collection and provision of information regarding prospective / former personnel (including any legal and regulatory constraints) and whether escalation to and approval from head office may be required to implement a differentiated Hong Kong specific policy enabling compliance with the MRC Scheme;
- considering whether the AI has adequate carve outs for compulsory regulatory disclosures (such as those required under the MRC Scheme) in confidentiality agreements entered into with employees e.g. in settlement agreements etc.;
- determining what, if any, changes need to be made to existing privacy information consents to facilitate future compliance with the MRC Scheme requirements and how any additional consents will be obtained; and
- considering how and where the information required to be kept and disclosed pursuant to the MRC Scheme is stored and ensuring it is readily accessible by appropriate personnel.

To discuss how our experience can assist you, or if you have any questions on any of the matters above, please do not hesitate to liaise with your usual contact at Baker McKenzie or the lawyers listed in this Alert.

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