

Operational Resilience

Summary of updates on OR-2, revised OR-1, and revised TM-G-2

April 2023



HKMA SPM Modules:
**OR-2, Revised
OR-1, and
TM-G-2**

The Basel Committee on Banking Supervision (BCBS) issued *Principles for Operational Resilience (POR)* and *Revised Principles for Sound Management of Operational Risk* in March 2021. To implement these, the Hong Kong Monetary Authority (HKMA) issued a new SPM module OR-2 on “Operational Resilience” and a revised version of the SPM module TM-G-2 on “Business Continuity Planning” on 31st May 2022, as well as a revised SPM module OR-1 on “Operational Risk Management” on 25th July 2022. The new modules provide consistent guidance on how AIs should address operational resilience and are required to be implemented in accordance with the timelines provided by the HKMA.



What is Operational Resilience?

Operational resilience has been a regulatory concern for over a decade since the 2008 financial crisis and has risen to the top of the regulatory agenda and has now been brought into even sharper focus by the COVID-19 pandemic worldwide.

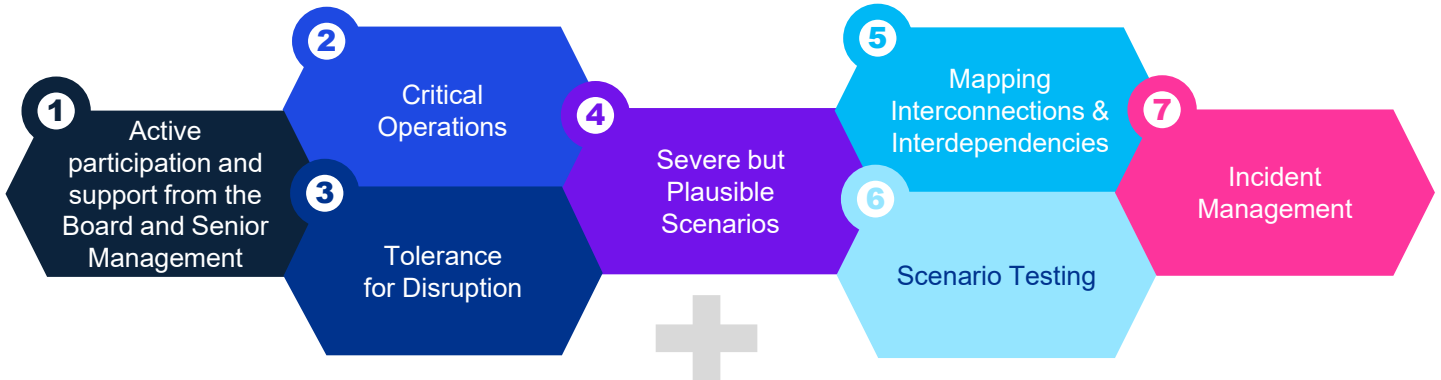
Definition of Operational Resilience

“Operational Resilience is the ability of a bank to deliver critical operations through disruption. It enables a bank to identify and protect itself from threats and potential failures, respond and adapt to, as well as to recover and learn from disruptive events in order to minimise their impact on the delivery of critical operations through disruption.”



Key components to consider when building the Operational Resilience framework

To develop a holistic operational resilience framework, AIs should consider the following components as detailed in OR-2 and leverage the other HKMA guidance and policies which are detailed below.








Risk management areas including but not limited to:

<p>OR-1</p> <p>Operational risk management</p> <p>Issued in Nov 2005 Revised in Jul 2022</p>	<p>TM-G-2</p> <p>Business continuity planning and testing</p> <p>Issued in Dec 2002 Revised in May 2022</p>	<p>SA-2</p> <p>Third-party dependency management</p> <p>Issued in Dec 2001</p>	<p>TM-G-1</p> <p>ICT including cyber security</p> <p>Issued in Jun 2003</p>
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Revised OR-1 Key Updates









Following consultation with the industry, the HKMA issued a revised version of the SPM module **OR-1 on Operational Risk Management** on 25 July 2022. KPMG analysed and identified the following changes:

New Requirements	 Operational Risk Management Framework (ORMF)	<p>Became more prescriptive on components to be included in an appropriate ORMF:</p> <ul style="list-style-type: none"> • Specific aspects of operational risk management to consider <ul style="list-style-type: none"> ○ Change management ○ Information and communication technology ○ Business continuity management and disaster recovery plan • Disclosure: 3 general disclosure principles that AIs are expected to follow so that its stakeholder can better assess their operational risk exposure and management
	 Risk Appetite and tolerance statement	<ul style="list-style-type: none"> • Required AIs to prepare a forward-looking statement that articulates the nature, types and levels of operational risk that the bank is willing to assume • The statement needs to be approved and periodically reviewed by the Board
	 Group Level	<ul style="list-style-type: none"> • Required AIs to also cover their subsidiaries and related entities in their ORMF • Subsidiaries and related entities may rely on their group's ORMF and Risk appetite and tolerance statement after considering the operation's size, nature and complexity
New Terms	 Three lines of Defense	<ul style="list-style-type: none"> • Adopted the Three Lines of Defense model to structure the roles and responsibilities of respective functions and ensure the components within the ORMF is fully integrated into the overall risk management process.
Timeline	 Implementation Timeline	<ul style="list-style-type: none"> • Within 18 months from 25 July 2022 (i.e. no later than 25 January 2024) • Specific guidance that links ORMF of an AI to its operational resilience are exempted from this deadline and shall follow the timeline set out in OR-2



TM-G-2 Key Updates

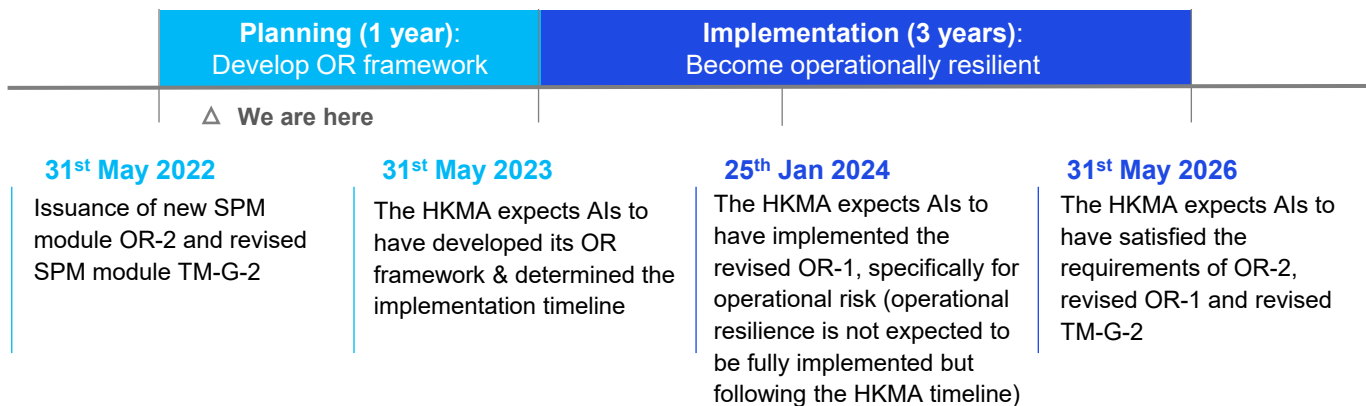
Following consultation with the industry, the HKMA issued a revised version of the SPM module **TM-G-2 Business Continuity Planning** on 31st May, 2022. KPMG analysed and identified the following changes:

New Definitions align to OR-2	 Critical Operations	<ul style="list-style-type: none"> • Critical operation activities, processes, and services performed by an AI • Supporting assets (including people, technology, information and facilities) necessary for the delivery of such activities and services
	 Tolerance for Disruption	<ul style="list-style-type: none"> • Situations that would result in significant disruptions, and while unlikely to occur, remain probable
	 Severe but Plausible Scenario	<ul style="list-style-type: none"> • Maximum level of significant disruption to a critical operation that an AI can accept
Scope	 Forward-looking Business Continuity Plan	<ul style="list-style-type: none"> • Validate for a range of severe but plausible scenarios • Identify critical operations, key internal and external dependencies supporting these critical operations • Incorporate business impact analysis, recovery strategies, testing, training and awareness, communication strategies and crisis management • Consistent with AIs' operational resilience framework and its recovery and resolution plans
Highlights & Other Considerations	 Broader concerns	<ul style="list-style-type: none"> • Consider tolerance for disruption during BIA time-frame assessment • Consider severe but plausible scenarios in BCP development and testing
	 Lessons learnt from COVID-19	<ul style="list-style-type: none"> • Consider work-from-home arrangements and split-team arrangements to enable teams to stand in for each other where needed
	 BCP Testing Frequency	<ul style="list-style-type: none"> • Consider factors affecting testing frequency: (1) Potential impact of disruption (2) AI's complexity (3) Changing operating environment
	 Crisis Management Process	<ul style="list-style-type: none"> • Clear internal decision-making process and criteria for activation of the BCP and / or alternate sites • Process to establish roles and responsibilities for managing disruptions • Clear guidance for succession of authority in the event of a disruption



Actions needed from AIs

The HKMA will engage in active discussions with AIs to review the suitability of their proposed timelines.



Failure to implement OR-2 properly may lead to ...

- Difficulties in obtaining the HKMA approval for the launch of new products
- Impact on the bank's ability to meet the Authorisation Criteria under the Banking Ordinance



Actions needed from AIs to fulfil OR-2 requirements

To start with...

- ✓ Assess and review design of **current functional operating models** and identify existing capabilities to be leveraged

To rally the troops...


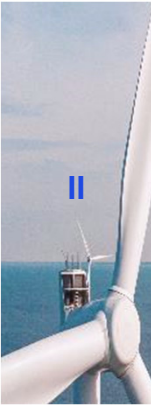


- ✓ Build growth strategy and PMO office
- ✓ Tone from the top and raise awareness

To enable technology in the solution



How KPMG can help?

KPMG's innovative approach consists of 2 phases (i.e., planning and implementation) to deliver a seamless solution for complying with HKMA's regulatory expectations within the required timeframe.

Planning	 <p>Current State Assessment</p>	<ul style="list-style-type: none"> ✓ Perform gap analysis between the Bank's current state against the latest HKMA requirements on OR-2 ✓ Conduct workshops to validate the gaps identified, including our recommendations and suggested enhancement/remediation roadmap
	 <p>Operational Resilience Framework Development</p>	<ul style="list-style-type: none"> ✓ Propose criteria in determining critical operations based on size, nature and complexity of the AI's operations, and identify a list of critical operations ✓ Identify a list of severe but plausible scenarios that will impact critical operations ✓ Formulate a set of criteria in determining tolerance for disruptions and determine the tolerance for severe but plausible scenarios using time-based metrics ✓ Determine OR Strategies and Target Operating Model (TOM) ✓ Enhance the operational risk management framework based on the results of current state assessment
	 <p>Pilot</p>	<ul style="list-style-type: none"> ✓ Define pilot scope, purpose, test cases and metrics ✓ Perform pilot mapping and end-to-end testing on one of the critical operation to validate the operational resilience operating model
Implementation	 <p>Implementation Support</p>	<ul style="list-style-type: none"> ✓ Provide Operational Resilience implementation support on mapping, scenario testing and incident management ✓ Support the bank's transition of operational resilience into BAU and to fulfill HKMA's requirements

KPMG has a global, multi-disciplinary team with subject matter advisors who have significant depth and capability across the Resilience, Operational Risk, Business Continuity Plan / Business Continuity Management, Recovery and Resolution Planning, Cyber and Technology domains. We draw on this depth to ensure that our clients have access to the right perspectives as we collaborate on an Operational Resilience Programme that meets your needs.

Contact us

If you would like to further discuss the implications of the new Operational Resilience standard, please contact us:



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