Annex 2

Transition Disclosures Template

			Amounts subject to pre-Basel III treatment*
	CET1 capital: instruments and reserves		
1	Directly issued qualifying CET1 capital instruments plus any related share premium		
2	Retained earnings		
3	Disclosed reserves		
4	*Directly issued capital subject to phase out from CET1 capital (only applicable to non-joint stock companies)*	Not applicable	
	Public sector capital injections grandfathered until 1 January 2018	Not applicable	
5	Minority interests arising from CET1 capital instruments issued by consolidated bank subsidiaries and held by third parties (amount allowed in CET1 capital of the consolidation group)		
6	**CET1 capital before regulatory deductions**		
	CET1 capital: regulatory deductions		
7	Valuation adjustments		
8	Goodwill (net of associated deferred tax liability)		
#9	Other intangible assets (net of associated deferred tax liability)		
#10	Deferred tax assets net of deferred tax liabilities		
11	Cash flow hedge reserve		
12	Excess of total EL amount over total eligible provisions under the IRB approach		
13	Gain-on-sale arising from securitization transactions		
14	Gains and losses due to changes in own credit risk on fair valued liabilities		
15	Defined benefit pension fund net assets (net of associated deferred tax liabilities)		
16	Investments in own CET1 capital instruments (if not already netted off paid-in capital on reported balance sheet)		
17	Reciprocal cross-holdings in CET1 capital instruments		
#18	Insignificant capital investments in CET1 capital instruments issued by financial sector entities that are outside the scope of regulatory consolidation (amount above 10% threshold)		
#19	Significant capital investments in CET1 capital instruments issued by financial sector entities that are outside the scope of regulatory consolidation (amount above 10% threshold)		
20	Mortgage servicing rights (amount above 10% threshold)	Not applicable	
21	Deferred tax assets arising from temporary differences (amount above 10% threshold, net of related tax liability)	Not applicable	
22	Amount exceeding the 15% threshold	Not applicable	
23	of which: significant investments in the common stock of financial sector entities	Not applicable	
24	of which: mortgage servicing rights	Not applicable	
25	of which: deferred tax assets arising from temporary differences	Not applicable	
26	National specific regulatory adjustments applied to CET1 capital		
26a	Cumulative fair value gains arising from the revaluation of land and buildings (own-use and investment properties)		
26b	Regulatory reserve for general banking risks		
26c	Securitization exposures specified in a notice given by the Monetary Authority		
26d	Cumulative losses below depreciated cost arising from the institution's holdings of land and buildings		
26e	Capital shortfall of regulated non-bank subsidiaries		
26f	Capital investment in a connected company which is a commercial entity (amount above 15% of the reporting institution's capital base)		
27	Regulatory deductions applied to CET1 capital due to insufficient AT1 capital and Tier 2 capital to cover deductions		
28	**Total regulatory deductions to CET1 capital**		
29	**CET1 capital**		
	AT1 capital: instruments		
30	Qualifying AT1 capital instruments plus any related share premium		
31	of which: classified as equity under applicable accounting standards		
32	of which: classified as liabilities under applicable accounting standards		

33	*Capital instruments subject to phase out arrangements from AT1 capital*		
34	AT1 capital instruments issued by consolidated bank subsidiaries and held by third parties (amount allowed in AT1 capital of the consolidation group)		
35	*of which: AT1 capital instruments issued by subsidiaries subject to phase out arrangements*		
36	**AT1 capital before regulatory deductions**		
	AT1 capital: regulatory deductions		
37	Investments in own AT1 capital instruments		
38	Reciprocal cross-holdings in AT1 capital instruments		
#39	Insignificant capital investments in AT1 capital instruments issued by financial sector entities that are outside the scope of regulatory consolidation (amount above 10% threshold)		
40	Significant capital investments in AT1 capital instruments issued by financial sector entities that are outside the scope of regulatory consolidation		
41	National specific regulatory adjustments applied to AT1 capital		
41a	Portion of previous deductions applied 50:50 to core capital and supplementary capital, based on pre-Basel III treatment, which during transitional period remain subject to deduction from T1 capital		
i	of which: Excess of total EL amount over total eligible provisions under the IRB approach		
ii	of which: Capital shortfall of regulated non-bank subsidiaries		
iii	of which: Investments in own CET1 capital instruments		
iv	of which: Reciprocal cross holdings in CET1 capital instruments issued by financial sector entities		
v	of which: Capital investment in a connected company which is a commercial entity (amount above 15% of the reporting institution's capital base)		
vi	of which: Insignificant capital investments in CET1 capital instruments, AT1 capital instruments and T2 capital instruments issued by financial sector entities that are outside the scope of regulatory consolidation		
vii	of which: Significant capital investments in CET1 capital instruments, AT1 capital instruments and T2 capital instruments issued by financial sector entities that are outside the scope of regulatory consolidation		
42	Regulatory deductions applied to AT1 capital due to insufficient Tier 2 capital to cover deductions		
43	**Total regulatory deductions to AT1 capital**		
44	**AT1 capital**		
45	**Tier 1 capital (Tier 1 = CET1 + AT1)**		
	Tier 2 capital: instruments and provisions		
46	Qualifying Tier 2 capital instruments plus any related share premium		
47	*Capital instruments subject to phase out arrangements from Tier2 capital*		
48	Tier 2 capital instruments issued by consolidated bank subsidiaries and held by third parties (amount allowed in Tier 2 capital of the consolidation group)		
49	*of which: capital instruments issued by subsidiaries subject to phase out arrangements*		
50	Collective impairment allowances and regulatory reserve for general banking risks eligible for inclusion in Tier 2 capital		
51	**Tier 2 capital before regulatory deductions**		
	Tier 2 capital: regulatory deductions		
52	Investments in own Tier 2 capital instruments		
53	Reciprocal cross-holdings in Tier 2 capital instruments		
#54	Insignificant capital investments in Tier 2 capital instruments issued by financial sector entities that are outside the scope of regulatory consolidation (amount above 10% threshold)		
55	Significant capital investments in Tier 2 capital instruments issued by financial sector entities that are outside the scope of regulatory consolidation		
56	National specific regulatory adjustments		
56a	Add back of cumulative fair value gains arising from the revaluation of land and buildings (own-use and investment properties) eligible for inclusion in Tier 2 capital		
56b	Portion of previous deductions applied 50:50 to core capital and supplementary capital, based on pre-Basel III treatment, which during transitional period remain subject to deduction from Tier 2 capital		
i	of which: Excess of total EL amount over total eligible provisions under the IRB approach		
ii	of which: Capital shortfall of regulated non-bank subsidiaries		
iii	of which: Investments in own CET1 capital instruments		
iv	of which: Reciprocal cross holdings in CET1 capital instruments issued by financial sector entities		
v	of which: Capital investment in a connected company which is a commercial entity (amount above 15% of the reporting institution's capital base)		

vi	of which: Insignificant capital investments in CET1 capital instruments, AT1 capital instruments and Tier 2 capital instruments issued by financial sector entities that are outside the scope of regulatory consolidation	
vii	of which: Significant capital investments in CET1 capital instruments, AT1 capital instruments and Tier 2 capital instruments issued by financial sector entities that are outside the scope of regulatory consolidation	
57	**Total regulatory deductions to Tier 2 capital**	
58	**Tier 2 capital**	
59	**Total capital (Total capital = Tier 1 + Tier 2)**	
59a	Deduction items under Basel III which during transitional period remain subject to risk-weighting, based on pre-Basel III treatment	
i	of which: Mortgage servicing rights	
ii	of which: Defined benefit pension fund net assets	
iii	of which: Investments in own CET1 capital instruments, AT1 capital instruments and Tier 2 capital instruments	
iv	of which: Capital investment in a connected company which is a commercial entity	
v	of which: Insignificant capital investments in CET1 capital instruments, AT1 capital instruments and Tier 2 capital instruments issued by financial sector entities that are outside the scope of regulatory consolidation	
vi	of which: Significant capital investments in CET1 capital instruments, AT1 capital instruments and Tier 2 capital instruments issued by financial sector entities that are outside the scope of regulatory consolidation	
60	**Total risk weighted assets**	
	Capital ratios (as a percentage of risk weighted assets)	
61	CET1 capital ratio	
62	Tier 1 capital ratio	
63	Total capital ratio	
64	Institution specific buffer requirement (minimum CET1 capital requirement as specified in s.3A of the BCR plus capital conservation buffer plus countercyclical buffer requirements plus G-SIB or D-SIB requirements)	
65	*of which: capital conservation buffer requirement*	
66	*of which: bank specific countercyclical buffer requirement*	
67	*of which: G-SIB or D-SIB buffer requirement*	
68	CET1 capital surplus over the minimum CET1 requirement and any CET1 capital used to meet the Tier 1 and Total capital requirement under s.3A of the BCR	
	National minima (if different from Basel 3 minimum)	
69	National CET1 minimum ratio	Not applicable
70	National Tier 1 minimum ratio	Not applicable
71	National Total capital minimum ratio	Not applicable
	Amounts below the thresholds for deduction (before risk weighting)	
72	Insignificant capital investments in CET1 capital instruments, AT1 capital instruments and Tier 2 capital instruments issued by financial sector entities that are outside the scope of regulatory consolidation	
73	Significant capital investments in CET1 capital instruments issued by financial sector entities that are outside the scope of regulatory consolidation	
74	Mortgage servicing rights (net of related tax liability)	Not applicable
75	Deferred tax assets arising from temporary differences (net of related tax liability)	Not applicable
	Applicable caps on the inclusion of provisions in Tier 2 capital	
76	Provisions eligible for inclusion in Tier 2 in respect of exposures subject to the basic approach and the standardized (credit risk) approach (prior to application of cap)	
77	Cap on inclusion of provisions in Tier 2 under the basic approach and the standardized (credit risk) approach	
78	Provisions eligible for inclusion in Tier 2 in respect of exposures subject to the IRB approach (prior to application of cap)	
79	Cap for inclusion of provisions in Tier 2 under the IRB approach	
	Capital instruments subject to phase-out arrangements (only applicable between 1 Jan 2018 and 1 Jan 2022)	
80	*Current cap on CET1 capital instruments subject to phase out arrangements*	Not applicable

81	*Amount excluded from CET1 due to cap (excess over cap after redemptions and maturities)*	Not applicable	
82	*Current cap on AT1 capital instruments subject to phase out arrangements*		
83	*Amount excluded from AT1 capital due to cap (excess over cap after redemptions and maturities)*		
84	*Current cap on Tier 2 capital instruments subject to phase out arrangements*		
85	*Amount excluded from Tier 2 capital due to cap (excess over cap after redemptions and maturities)*		

Footnotes:

* This refers to the position under the Banking (Capital) Rules in force on 31 December 2012.

\# Indicates elements where a more conservative definition has been applied in the BCR relative to that set out in the Basel III capital standards.

Abbreviations:

CET1: Common Equity Tier 1

AT1: Additional Tier 1

Notes to the template

Row No.	Description	Hong Kong basis	Basel III basis
#9	**Other intangible assets (net of associated deferred tax liability)**		
	Explanation As set out in paragraph 87 of the Basel III text issued by the Basel Committee (December 2011), mortgage servicing rights (MSRs) may be given limited recognition in CET1 capital (and hence be excluded from deduction from CET1 capital up to the specified threshold). In Hong Kong, an AI is required to follow the accounting treatment of including MSRs as part of intangible assets reported in the AI's financial statements and to deduct MSRs in full from CET1 capital. Therefore, the amount to be deducted as reported in row 9 may be greater than that required under Basel III. The amount reported under the column "Basel III basis" in this box represents the amount reported in row 9 (i.e. the amount reported under the "Hong Kong basis") adjusted by reducing the amount of MSRs to be deducted to the extent not in excess of the 10% threshold set for MSRs and the aggregate 15% threshold set for MSRs, DTAs arising from temporary differences and significant investments in CET1 capital instruments issued by financial sector entities (excluding those that are loans, facilities or other credit exposures to connected companies) under Basel III.		
#10	**Deferred tax assets net of deferred tax liabilities**		
	Explanation As set out in paragraphs 69 and 87 of the Basel III text issued by the Basel Committee (December 2011), DTAs that rely on future profitability of the bank to be realized are to be deducted, whereas DTAs which relate to temporary differences may be given limited recognition in CET1 capital (and hence be excluded from deduction from CET1 capital up to the specified threshold). In Hong Kong, an AI is required to deduct all DTAs in full, irrespective of their origin, from CET1 capital. Therefore, the amount to be deducted as reported in row 10 may be greater than that required under Basel III. The amount reported under the column "Basel III basis" in this box represents the amount reported in row 10 (i.e. the amount reported under the "Hong Kong basis") adjusted by reducing the amount of DTAs to be deducted which relate to temporary differences to the extent not in excess of the 10% threshold set for DTAs arising from temporary differences and the aggregate 15% threshold set for MSRs, DTAs arising from temporary differences and significant investments in CET1 capital instruments issued by financial sector entities (excluding those that are loans, facilities and other credit exposures to connected companies) under Basel III.		
#18	**Insignificant capital investments in CET1 capital instruments issued by financial sector entities that are outside the scope of regulatory consolidation (amount above 10% threshold)**		
	Explanation For the purpose of determining the total amount of insignificant capital investments in CET1 capital instruments issued by financial sector entities, an AI is required to aggregate any amount of loans, facilities or other credit exposures provided by it to any of its connected companies, where the connected company is a financial sector entity, as if such loans, facilities or other credit exposures were direct holdings, indirect holdings or synthetic holdings of the AI in the capital instruments of the financial sector entity, except where the AI demonstrates to the satisfaction of the Monetary Authority that any such loan was made, any such facility was granted, or any such other credit exposure was incurred, in the ordinary course of the AI's business. Therefore, the amount to be deducted as reported in row 18 may be greater than that required under Basel III. The amount reported under the column "Basel III basis" in this box represents the amount reported in row 18 (i.e. the amount reported under the "Hong Kong basis") adjusted by excluding the aggregate amount of loans, facilities or other credit exposures to the AI's connected companies which were subject to deduction under the Hong Kong approach.		
	Significant capital investments in CET1 capital instruments issued by financial sector entities that are outside the scope of regulatory consolidation (amount above 10% threshold)		

#19	<u>Explanation</u> For the purpose of determining the total amount of significant capital investments in CET1 capital instruments issued by financial sector entities, an AI is required to aggregate any amount of loans, facilities or other credit exposures provided by it to any of its connected companies, where the connected company is a financial sector entity, as if such loans, facilities or other credit exposures were direct holdings, indirect holdings or synthetic holdings of the AI in the capital instruments of the financial sector entity, except where the AI demonstrates to the satisfaction of the Monetary Authority that any such loan was made, any such facility was granted, or any such other credit exposure was incurred, in the ordinary course of the AI's business. Therefore, the amount to be deducted as reported in row 19 may be greater than that required under Basel III. The amount reported under the column "Basel III basis" in this box represents the amount reported in row 19 (i.e. the amount reported under the "Hong Kong basis") adjusted by excluding the aggregate amount of loans, facilities or other credit exposures to the AI's connected companies which were subject to deduction under the Hong Kong approach.		
#39	**Insignificant capital investments in AT1 capital instruments issued by financial sector entities that are outside the scope of regulatory consolidation (amount above 10% threshold)**		
	<u>Explanation</u> The effect of treating loans, facilities or other credit exposures to connected companies which are financial sector entities as CET1 capital instruments for the purpose of considering deductions to be made in calculating the capital base (see note re row 18 to the template above) will mean the headroom within the threshold available for the exemption from capital deduction of other insignificant capital investments in AT1 capital instruments may be smaller. Therefore, the amount to be deducted as reported in row 39 may be greater than that required under Basel III. The amount reported under the column "Basel III basis" in this box represents the amount reported in row 39 (i.e. the amount reported under the "Hong Kong basis") adjusted by excluding the aggregate amount of loans, facilities or other credit exposures to the AI's connected companies which were subject to deduction under the Hong Kong approach.		
#54	**Insignificant capital investments in Tier 2 capital instruments issued by financial sector entities that are outside the scope of regulatory consolidation**		
	<u>Explanation</u> The effect of treating loans, facilities or other credit exposures to connected companies which are financial sector entities as CET1 capital instruments for the purpose of considering deductions to be made in calculating the capital base (see note re row 18 to the template above) will mean the headroom within the threshold available for the exemption from capital deduction of other insignificant capital investments in Tier 2 capital instruments may be smaller. Therefore, the amount to be deducted as reported in row 54 may be greater than that required under Basel III. The amount reported under the column "Basel III basis" in this box represents the amount reported in row 54 (i.e. the amount reported under the "Hong Kong basis") adjusted by excluding the aggregate amount of loans, facilities or other credit exposures to the AI's connected companies which were subject to deduction under the Hong Kong approach.		

Transition Disclosures Template - Explanatory Note

1. This template is substantially similar to the Capital Disclosures Template, except for the following modifications:

   - Modification 1: An "Amounts subject to pre-Basel III treatment" column has been added for an authorized institution ("AI") to report the amount of each regulatory deduction item that is still subject during the transitional period to either the previous 50/50 deduction treatment from core capital and supplementary capital or to risk-weighting under the pre-amended Banking (Capital) Rules ("BCR")[1]. The portion of the amount, which has already been transitioned to the new "Basel III treatment" under the amended BCR, will be reported under the main column alongside this additional column.

   - Modification 2: While the "Amounts subject to pre-Basel III treatment" column shows the amount of each regulatory deduction item that is subject to the "pre-Basel III treatment", it is also necessary to show how this amount is included in the calculation of an AI's regulatory capital. To this end, rows 41a, 56b and 59a are added with subdivisions under rows 41, 56 and 59 for an AI to show the amount of each item subject to "pre-Basel III treatment". An AI may add any further subdivisions under rows 41a, 56b and 59a as applicable.

2. The following examples illustrate how the above two modifications are intended to operate:

   Example for Modification 1

   In 2014, an AI is required to make a deduction from Common Equity Tier 1 ("CET1") capital of 20% of the amount which would previously have been deducted 50/50 from core capital and supplementary capital under the pre-Basel III treatment in accordance with the transitional arrangements set out in Schedule 4H of the BCR. Presuming an AI using the internal ratings-based approach to calculate its credit risk capital requirement has an excess of total EL amount over total eligible provisions ("shortfall of provisions") of $100mn, the AI is required to deduct $20mn (i.e. 20% of $100mn) from CET1 capital. For disclosure purposes, the AI will report $20mn in the first of the two empty cells in row 12 and report $80mn in the second of the two cells, indicating that the latter is yet to be subject to the "Basel III treatment" under the amended BCR. The sum of the two cells will be equal to the total amount of

[1] These refer to the version of the BCR in force on 31 December 2012.

regulatory deductions (i.e. $100mn) required.

Examples for Modification 2

Continuing from the above example, the pre-Basel III treatment requires that any shortfall of provisions is to be deducted from core capital and supplementary capital. For this purpose, 2 rows have been inserted after row 41 and row 56 respectively, to indicate that during the transitional period some shortfall of provisions will continue to be deducted equally from Tier 1 capital and Tier 2 capital. As such, the $80mn reported in the last cell of row 12 will be divided into two equal portions (i.e. $40mn each) and reported in row 41ai and row 56bi.

Now, presume that the AI currently risk-weights defined benefit pension fund net assets at 200%. In 2014, the defined benefit pension fund assets amount to $50mn and the amended BCR will ultimately require these to be deducted. However, the transitional arrangements set out in Schedule 4H of the BCR will only require the AI to deduct 20% of the assets in 2014. This means that the AI will report $10mn in the first cell in row 15 and $40mn in the second cell (the sum of the two cells is therefore equal to the total amount of regulatory deduction required). The AI will disclose in a subdivision row under row 59aii a figure of $80mn ($40mn x 200%).

Similarly, where an AI has insignificant capital investments in financial sector entities amounting to $110mn which are risk-weighted at 125% based on the pre-Basel III treatment, assume that of these investments, ultimately $100mn will be deducted from CET1 capital once the transitional arrangements are completed. In 2014, under the transitional arrangements in Schedule 4H of the BCR, the AI will need to deduct $20mn of the investments and report this in the first cell in row 18 and will report the remaining $80mn in the second cell. The AI will then make a disclosure in a row inserted under row 59 to indicate that such assets are risk-weighted at 125% during the transitional period, that is the AI will report a figure of $100mn in the row inserted under row 59, being the risk-weighted amount of such assets (i.e. $80mn x 125%).

3. Given that certain capital elements under the BCR carry a more conservative definition relative to those under the Basel III framework, an AI is required to separately disclose the impact of each of these different definitions in the "Notes to the template" to facilitate comparison by market participants of its capital position with banks in other jurisdictions. In this regard, an AI should make disclosures in accordance with those notes.