Financial Institutions (Resolution) (Loss-absorbing Capacity Requirements—Banking Sector) Rules

Note: *These draft Rules are prepared to assist in explaining the relevant policy proposals. They are not the final version for the legislative process if legislation is introduced for giving effect to the proposals.*

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(Made by the Monetary Authority under section 19(1) of the Financial Institutions (Resolution) Ordinance (Cap. 628))

Part 1

Preliminary

1. Commencement

These Rules come into operation on [date to be added].

2. Interpretation

(1) In these Rules—

Additional Tier 1 capital instrument ( )—

(a) in relation to an instrument issued by an authorized institution, has the meaning given by section 2(1) of the Ordinance; or

(b) in relation to an instrument issued by any other entity, has the meaning it would be given by section 2(1) of the Ordinance if the entity were an authorized institution;

annual reporting period ( ), in relation to a disclosure entity, means a financial year of the entity;

banking book ( )—

(a) in relation to an authorized institution, has the meaning given by section 2(1) of the Capital Rules; or

(b) in relation to any other entity, has the meaning it would be given by section 2(1) of the Capital Rules if the entity were an authorized institution;

capital adequacy ratio ( )—

(a) in relation to an authorized institution, has the meaning given by section 3 of the Capital Rules; or

(b) in relation to any other entity, has the meaning it would be given by section 3 of the Capital Rules if the entity were an authorized institution;

capital component ratio ( )—see rule 18;

capital consolidation group ( ) in relation to an authorized institution, means the authorized institution's consolidation group within the meaning of section 4 of the Capital Rules;

Capital Rules ( ) means the Banking (Capital) Rules (Cap. 155 sub. leg. L);

CET1 capital ( ), subject to rule 17—

(a) in relation to an authorized institution, has the meaning given by section 2(1) of the Capital Rules; or

(b) in relation to any other entity, has the meaning it would be given by section 2(1) of the Capital Rules if the entity were an authorized institution;

CET1 capital instrument ( )—

(a) in relation to an instrument issued by an authorized institution, has the meaning given by section 2(1) of the Capital Rules; or

(b) in relation to an instrument issued by any other entity, has the meaning it would be given by section 2(1) of the Capital Rules if the entity were an authorized institution;

classifiable entity ( )—see rule 4;

classification date ( ) in relation to an entity that is a resolution entity or material subsidiary, means—

(a) subject to paragraph (b), the date on which the classification of the entity as a resolution entity or material subsidiary takes effect; or

(b) if the entity has been declassified as a resolution entity or material subsidiary and later reclassified, the date on which the reclassification or, if the entity has been reclassified more than once, the latest reclassification, takes effect;

clean HK holding company ( ) means an HK holding company—

(a) the activities of which are limited to—

(i) issuing funding instruments;

(ii) holding funding instruments issued by its subsidiaries; and

(iii) any related ancillary activities; and

(b) the liabilities of which that are none of Additional Tier 1 capital instruments, Tier 2 capital instruments or non-capital LAC debt instruments, and that, on a winding up of the company, would rank equally with, or below, any Additional Tier 1 capital instruments, Tier 2 capital instruments or non-capital LAC debt instruments, do not exceed 5% of the sum of—

(i) the company's loss-absorbing capacity; and;

(ii) any items that would constitute loss-absorbing capacity but for section 1(1)(e) of Schedule 1 or section 1(1)(d) of Schedule 2;

consolidated basis ( )—

(a) subject to paragraph (b), when used in relation to the calculation of a LAC ratio—

(i) for a resolution entity or material subsidiary that is an authorized institution, means the basis set out in rule 15 on which the institution calculates that ratio; or

(ii) for a resolution entity or material subsidiary that is not an authorized institution, means the basis set out in rule 16 on which the resolution entity or material subsidiary calculates that ratio; or

(b) when used in relation to the Capital Rules, has the meaning it would have in those Rules if—

(i) a reference in those Rules to a consolidation group were a reference to a LAC consolidation group; and

(ii) in the case of an entity that is not an authorized institution, a reference in those Rules to an authorized institution were a reference to that entity;

counterparty credit risk ( )—

(a) in relation to an authorized institution, has the meaning given by section 2(1) of the Capital Rules; or

(b) in relation to any other entity, has the meaning it would be given by section 2(1) of the Capital Rules if the entity were an authorized institution;

disclosure entity ( ) means a resolution entity or a material subsidiary;

disclosure statement ( ) means a statement required to be prepared under rule 50(1)(a);

exposure measure ( )—

(a) in relation to a resolution entity or material subsidiary that is an authorized institution—

(i) for the purpose of calculating a LAC ratio on a solo or solo-consolidated basis, means the amount of the denominator determined under rule 14(3)(a), less any contribution to the denominator in respect of—

(A) items deducted from its loss-absorbing capacity in accordance with rule 38 or 40 (as the case requires); and

(B) items deducted from Tier 2 capital in accordance with the Capital Rules; or

(ii) for the purpose of calculating a LAC ratio on a consolidated basis, means the amount of the denominator determined under rule 15(3)(a), less any contribution to the denominator in respect of—

(A) items deducted from its loss-absorbing capacity in accordance with rule 38 or 40 (as the case requires); and

(B) items deducted from Tier 2 capital in accordance with the Capital Rules; or

(b) in relation to a resolution entity or material subsidiary that is an HK holding company or HK affiliated operational entity, for the purpose of calculating a LAC ratio on a consolidated basis, means the amount of the denominator determined under rule 16(3)(a), less any contribution to the denominator in respect of—

(i) items deducted from its loss-absorbing capacity in accordance with rule 38 or 40 (as the case requires); and

(ii) items deducted from Tier 2 capital in accordance with the Capital Rules;

external LAC debt instrument ( ) means an instrument that meets all the criteria set out in Schedule 1;

external LAC leverage ratio ( )—see rule 11;

external LAC risk-weighted ratio ( )—see rule 10;

external loss-absorbing capacity ( )—see rule 37;

external non-capital LAC debt instrument ( ) means an external LAC debt instrument that is not—

(a) an Additional Tier 1 capital instrument; or

(b) a Tier 2 capital instrument;

financial sector entity ( ) has the meaning given by section 35 of the Capital Rules;

funding instrument ( ) means any of the following—

(a) a CET1 capital instrument;

(b) an Additional Tier 1 capital instrument;

(c) a Tier 2 capital instrument;

(d) a non-capital LAC debt instrument;

(e) any other debt instrument;

HK affiliated operational entity ( ) means an entity that is an affiliated operational entity incorporated in Hong Kong of an authorized institution incorporated in Hong Kong, but is not itself an authorized institution or HK holding company;

HK holding company ( ) 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;

indirect holding ( )—

(a) in relation to an authorized institution, has the meaning given by section 35 of the Capital Rules; or

(b) in relation to any other entity, has the meaning it would be given by section 35 of the Capital Rules if the entity were an authorized institution;

interim reporting period ( ), in relation to a disclosure entity, means the first 6 months of the entity's financial year;

internal LAC debt instrument ( ) means an instrument that meets all the criteria set out in Schedule 2;

internal LAC leverage ratio ( )—see rule 13;

internal LAC risk-weighted ratio ( )—see rule 12;

internal LAC scalar ( )— see rule 26;

internal loss-absorbing capacity ( )—see rule 39;

internal non-capital LAC debt instrument ( ) means an internal LAC debt instrument that is not—

(a) an Additional Tier 1 capital instrument; or

(b) a Tier 2 capital instrument;

LAC consolidation group ( ), in relation to a resolution entity or material subsidiary, means—

(a) subject to paragraph (b)—

(i) for a resolution entity or material subsidiary that is an authorized institution—its capital consolidation group;

(ii) for a resolution entity or material subsidiary that is an HK holding company—the group consisting of the HK holding company and the capital consolidation group of its principal authorized institution; or

(iii) for a resolution entity or material subsidiary that is an HK affiliated operational entity—the group consisting of the HK affiliated operational entity and the capital consolidation group of its principal authorized institution; or

(b) if the resolution authority varies the group under rule 7, the group as varied from time to time;

LAC debt instrument ( ) means—

(a) an external LAC debt instrument; or

(b) an internal LAC debt instrument;

LAC instrument ( ) means—

(a) a CET1 capital instrument; or

(b) a LAC debt instrument;

LAC ratio ( )—

(a) in relation to a resolution entity, means its external LAC risk-weighted ratio or its external LAC leverage ratio; or

(b) in relation to a material subsidiary, means its internal LAC risk-weighted ratio or its internal LAC leverage ratio;

LAC requirement ( ) means a requirement under these Rules for—

(a) a resolution entity to maintain any of its LAC ratios at or above a specified minimum; or

(b) a material subsidiary to maintain any of its LAC ratios at or above a specified minimum;

leverage ratio ( ), in relation to an authorized institution, has the meaning given by section 3Y of the Capital Rules;

loss-absorbing capacity ( )—

(a) in relation to a resolution entity, means external loss-absorbing capacity;

(b) in relation to a material subsidiary, means internal loss-absorbing capacity; or

(c) in relation to an entity established or incorporated outside Hong Kong, means any liabilities or other financial resources that are recognized as being eligible to count towards a requirement under a regulatory regime in a non-Hong Kong jurisdiction that corresponds to a LAC requirement (including a requirement designed to reflect the principles set out in the TLAC term sheet), to the extent of that recognition;

material sub-group ( ), in relation to a material subsidiary, means the group consisting of—

(a) the material subsidiary; and

(b) all subsidiaries of the material subsidiary;

material subsidiary ( ) means an entity classified as a material subsidiary under rule 6;

minimum external LAC leverage ratio ( ) means the minimum external LAC leverage ratio for a resolution entity determined under Division 2 of Part 4;

minimum external LAC risk-weighted ratio ( ) means the minimum external LAC risk-weighted ratio for a resolution entity determined under Division 2 of Part 4;

minimum internal LAC leverage ratio ( ) means the minimum internal LAC leverage ratio for a material subsidiary determined under Division 3 of Part 4;

minimum internal LAC risk-weighted ratio ( ) means the minimum internal LAC risk-weighted ratio for a material subsidiary determined under Division 3 of Part 4;

minimum LAC ratio ( ) means any of the following—

(a) a minimum external LAC leverage ratio;

(b) a minimum external LAC risk-weighted ratio;

(c) a minimum internal LAC leverage ratio;

(d) a minimum internal LAC risk-weighted ratio;

modelled minimum external LAC leverage ratio ( ) means the modelled minimum external LAC leverage ratio for a material subsidiary determined under rule 25;

modelled minimum external LAC risk-weighted ratio ( ) means the modelled minimum external LAC risk-weighted ratio for a material subsidiary determined under rule 25;

non-capital LAC debt instrument ( ) means—

(a) an external non-capital LAC debt instrument; or

(b) an internal non-capital LAC debt instrument;

non-capital LAC liability ( ) means any of the following—

(a) a non-capital LAC debt instrument;

(b) a liability referred to in paragraph (c) of the definition of ***loss-absorbing capacity***, other than any such liability that is constituted by a regulatory capital instrument;

(c) any other liability that—

(i) is not constituted by a regulatory capital instrument; and

(ii) on a winding up of the issuer, would rank equally with, or below—

(A) an instrument referred to in paragraph (a); or

(B) a liability referred to in paragraph (b) that is recognized as being eligible to count towards a requirement under a regulatory regime in a

non-Hong Kong jurisdiction that corresponds to a LAC requirement other than by virtue of any provisions in such regulatory regime designed to reflect the principles set out in the antepenultimate or penultimate paragraphs of section 11 of the TLAC term sheet,

excluding any such other liability that, under a relevant regulatory regime, is excluded from bearing loss in a resolution of the issuer;

non-Hong Kong resolution entity ( ), in relation to a material subsidiary, means an entity established or incorporated in a non-Hong Kong jurisdiction where the preferred resolution strategy covering the material subsidiary contemplates the taking of a non-Hong Kong resolution action in relation to the entity;

preferred resolution strategy ( ), in relation to a classifiable entity, means—

(a) the resolution strategy notified to the entity under rule 3 as the preferred resolution strategy covering the entity; or

(b) if the resolution authority has not notified an entity under rule 3 and the entity is in the resolution group of another classifiable entity, the preferred resolution strategy notified to that other entity under rule 3;

principal authorized institution ( )—

(a) in relation to a resolution entity or material subsidiary that is an HK holding company—

(i) if it has only one subsidiary that is an authorized institution incorporated in Hong Kong, means that subsidiary; or

(ii) if it has more than one subsidiary that is an authorized institution incorporated in Hong Kong, means—

(A) subject to sub-subparagraph (B), the subsidiary authorized institution incorporated in Hong Kong that has the highest risk-weighted amount on a consolidated basis under the Capital Rules; or

(B) the authorized institution designated by the resolution authority under subrule (2); or

(b) in relation to a resolution entity or material subsidiary that is an HK affiliated operational entity—

(i) if it is an affiliated operational entity of only one authorized institution incorporated in Hong Kong, means that authorized institution; or

(ii) if it is an affiliated operational entity of more than one authorized institution incorporated in Hong Kong, means—

(A) subject to sub-subparagraph (B), the authorized institution incorporated in Hong Kong that has the highest risk-weighted amount on a consolidated basis under the Capital Rules; or

(B) the authorized institution designated by the resolution authority under subrule (2);

professional investor ( ) has the meaning given by section 1 of Part 1 of Schedule 1 to the Securities and Futures Ordinance (Cap. 571);

quarterly reporting period ( ), in relation to a disclosure entity, means the first, second, third or fourth 3-month period of a financial year of the entity;

regulatory capital instrument ( ) means—

(a) a CET1 capital instrument, Additional Tier 1 capital instrument or Tier 2 capital instrument; or

(b) an instrument that counts towards a requirement under a regulatory regime in a non-Hong Kong jurisdiction that corresponds to a requirement on an authorized institution to maintain minimum capital adequacy ratios under the Capital Rules;

resolution ( ) means—

(a) resolution as defined in section 2(1) of the Ordinance; or

(b) a process in a non-Hong Kong jurisdiction of a similar nature to resolution referred to in paragraph (a);

resolution authority ( ) means the resolution authority in relation to a banking sector entity;

Note—

Under section 2 of the Ordinance, the resolution authority in relation to a banking sector entity is the Monetary Authority;

resolution component ratio ( )—see rule 19;

resolution entity ( ) means an entity classified as a resolution entity under rule 5;

resolution group ( ), in relation to an entity that is covered by a preferred resolution strategy, means the group identified in that strategy as the resolution group of which the entity is a member;

resolution strategy ( ) means—

(a) a strategy devised by the resolution authority under section 13(1)(a) or 13(2)(a) of the Ordinance for securing the orderly resolution of a within scope financial institution or a holding company of a within scope financial institution; or

(b) a strategy of a similar nature to a strategy referred to in paragraph (a) devised or adopted by a non-Hong Kong resolution authority covering one or more group companies of a within scope financial institution;

reviewable decision ( ) means a decision of the resolution authority under these Rules that may be reviewed by the Resolvability Review Tribunal;

risk-weighted amount ( )—

(a) in relation to a resolution entity or material subsidiary that is an authorized institution—

(i) for the purpose of calculating a LAC ratio on a solo or solo-consolidated basis, means the amount of the denominator determined under rule 14(2)(a); or

(ii) for the purpose of calculating a LAC ratio on a consolidated basis, means the amount of the denominator determined under rule 15(2)(a)—

less any contribution to the relevant denominator in respect of items deducted from its loss-absorbing capacity in accordance with rule 38 or 40 (as the case requires);

(b) in relation to a resolution entity or material subsidiary that is an HK holding company or HK affiliated operational entity, for the purpose of calculating a LAC ratio on a consolidated basis, means the amount of the denominator determined under rule 16(2)(a), less any

contribution to the denominator in respect of items deducted from its loss absorbing capacity in accordance with rule 38 or 40 (as the case requires); or

(c) in relation to an authorized institution that is not a resolution entity or material subsidiary, means the amount of the denominator of its capital adequacy ratio as calculated under the Capital Rules on a solo, solo-consolidated or consolidated basis (as the case requires);

semi-annual reporting period ( ), in relation to a disclosure entity, means the first or second 6-month period of a financial year of the entity;

solo basis ( )—

(a) in relation to calculating a capital adequacy ratio, means the basis set out in section 29 of the Capital Rules; or

(b) in relation to calculating a LAC ratio, has the meaning that results in an equivalent approach in the calculation of the LAC ratio to that set out in section 29 of the Capital Rules for the calculation of a capital adequacy ratio;

solo-consolidated basis ( )—

(a) in relation to calculating a capital adequacy ratio, means the basis set out in section 30 of the Capital Rules; or

(b) in relation to calculating a LAC ratio, has the meaning that results in an equivalent approach in the calculation of the LAC ratio to that set out in section 30 of the Capital Rules for the calculation of a capital adequacy ratio;

solo-consolidated subsidiary ( ) has the meaning given by section 4 of the Capital Rules;

solo LAC scalar ( )—see rule 30;

synthetic holding ( )—

(a) in relation to an authorized institution, has the meaning given by section 35 of the Capital Rules; or

(b) in relation to any other entity, has the meaning it would be given by section 35 of the Capital Rules if the entity were an authorized institution;

Tier 1 capital ( ), subject to rule 17—

(a) in relation to an authorized institution, has the meaning given by section 2(1) of the Capital Rules; or

(b) in relation to any other entity, has the meaning it would be given by section 2(1) of the Capital Rules if the entity were an authorized institution;

Tier 2 capital ( ) subject to rule 17—

(a) in relation to an authorized institution, has the meaning given by section 2(1) of the Capital Rules; or

(b) in relation to any other entity, has the meaning it would be given by section 2(1) of the Capital Rules if the entity were an authorized institution;

Tier 2 capital instrument ( )—

(a) in relation to an instrument issued by an authorized institution, has the meaning given by section 2(1) of the Capital Rules; or

(b) in relation to an instrument issued by any other entity, has the meaning it would be given by section 2(1) of the Capital Rules if the entity were an authorized institution;

TLAC term sheet ( ) means the Total Loss-absorbing Capacity (TLAC) Term Sheet issued by the Financial Stability Board on 9 November 2015;

total capital ( ), in relation to an entity, means the sum of its Tier 1 capital and Tier 2 capital;

Total capital ratio ( )—

(a) in relation to an authorized institution, has the meaning given by section 2(1) of the Capital Rules; or

(b) in relation to any other entity, has the meaning it would be given by section 2(1) of the Capital Rules if the entity were an authorized institution and if a reference to Total capital in that section were a reference to total capital as defined in this rule;

trading book ( )—

(a) in relation to an authorized institution, has the meaning given by section 2(1) of the Capital Rules; or

(b) in relation to any other entity, has the meaning it would be given by section 2(1) of the Capital Rules if the entity were an authorized institution;

underlying exposures ( ) has the meaning given by section 2(1) of the Capital Rules.

(2) For the purposes of the definition of ***principal authorized institution*** in subrule (1), the resolution authority, by written notice served on a resolution entity or material subsidiary that is an HK holding company or HK affiliated operational entity, may designate a group company of the resolution entity or material subsidiary that is an authorized institution incorporated in Hong Kong as the principal authorized institution of the resolution entity or material subsidiary.

3. Preferred resolution strategy

The resolution authority, by written notice served on a classifiable entity, may identify a resolution strategy as the preferred resolution strategy covering the entity.

Part 2

Resolution Entities, Material Subsidiaries and LAC Consolidation Groups

4. What entities can be classified as resolution entities or material subsidiaries

(1) The following entities may be classified as a resolution entity or a material subsidiary under this Part—

(a) an authorized institution incorporated in Hong Kong;

(b) an HK holding company;

(c) an HK affiliated operational entity.

(2) For the purposes of these Rules, an entity referred to in subrule (1) is a ***classifiable entity*** ( ).

5. Resolution entities

(1) The resolution authority may, in accordance with rule 8, classify a classifiable entity as a resolution entity if there is a preferred resolution strategy covering the classifiable entity that contemplates the application of a stabilization option in respect of any assets, rights or liabilities of the classifiable entity.

(2) In considering whether to classify a classifiable entity as a resolution entity, the resolution authority may take into account—

(a) the preferred resolution strategy covering the classifiable entity; and

(b) any other matters the resolution authority considers relevant.

(3) The resolution authority, by written notice served on a resolution entity, may at any time declassify the entity as a resolution entity.

6. Material subsidiaries

(1) The resolution authority may, in accordance with rule 8, classify a classifiable entity as a material subsidiary if—

(a) the classifiable entity is in a resolution group but is not a resolution entity; and

(b) the resolution authority determines that the classifiable entity taken on its own, or together with any of its subsidiaries in the resolution group—

(i) contains more than 5% of the risk-weighted assets of the resolution group;

(ii) generates more than 5% of the total operating income of the resolution group;

(iii) contains more than 5% of the unweighted assets of the resolution group; or

(iv) is material to the provision of critical financial functions.

(2) The resolution authority, by written notice served on a material subsidiary, may at any time declassify it as a material subsidiary.

(3) In making a determination under subrule (1)(b), the resolution authority may draw on any information and make any assumptions the resolution authority considers appropriate, taking into account the following matters—

(a) the availability of data relating to the risk-weighted assets, total operating income and unweighted assets of

the classifiable entity and other members of the resolution group;

(b) the comparability of data referred to in paragraph (a), taking into account that the classifiable entity and other members of the resolution group—

(i) may not all be authorized institutions or be otherwise regulated in Hong Kong or in a non-Hong Kong jurisdiction; and

(ii) may not all be located in the same jurisdiction;

(c) any other matters the resolution authority considers relevant.

7. Variation of LAC consolidation groups

(1) The resolution authority may, in accordance with rule 8, vary the LAC consolidation group of a resolution entity or material subsidiary by—

(a) removing one or more subsidiaries of the resolution entity or material subsidiary from the group; or

(b) adding one or more subsidiaries of the resolution entity or material subsidiary to the group.

(2) The resolution authority may vary the LAC consolidation group of a resolution entity or material subsidiary under this rule only if the resolution authority is satisfied that it is prudent to do so.

(3) In determining whether it is prudent to vary the LAC consolidation group of a resolution entity or material subsidiary, the resolution authority may take into account—

(a) the extent to which the subsidiary to be removed or added is connected to the resolution entity or material subsidiary and the potential for the level of

connectedness to contribute to a risk of contagion between them;

(b) the preferred resolution strategy covering the resolution entity or material subsidiary; and

(c) any other matters the resolution authority considers relevant.

8. Procedure for classifying resolution entities and material subsidiaries and varying LAC consolidation groups

(1) If the resolution authority proposes to classify an entity as a resolution entity or material subsidiary, or vary the LAC consolidation group of an entity that is a resolution entity or material subsidiary, the resolution authority must serve a written notice on the entity—

(a) specifying the resolution authority's proposed classification or variation;

(b) specifying the grounds for the proposed classification or variation; and

(c) including a statement that the entity may, within 14 days (or a longer period allowed by the resolution authority), make written representations to the resolution authority on any matter specified in the notice.

(2) If representations are made in accordance with subrule (1)(c), the resolution authority, after considering the representations, may—

(a) serve a further written notice on the entity—

(i) confirming the proposed classification or variation; or

(ii) modifying the proposed classification or variation to take into account any of the representations; or

(b) decide not to make the proposed classification or variation.

(3) If no representations are made in accordance with subrule (1)(c), the resolution authority may serve a further written notice on the entity confirming the proposed classification or variation.

(4) The further written notice served under subrule (2)(a) or (3) has the effect of classifying the entity as a resolution entity or material subsidiary, or varying the LAC consolidation group, in accordance with its terms, on the date specified in the notice.

(5) For a variation of a LAC consolidation group that results in an increase in the amount of loss-absorbing capacity that a resolution entity or material subsidiary needs to maintain in order to meet its LAC requirements, the date referred to in subrule (4) must be at least 12 months after the date on which the further written notice is served under subrule (2)(a) or (3).

9. Notification of changes to LAC consolidation group or group activities

(1) A resolution entity must give written notice to the resolution authority of the following matters as soon as practicable after the resolution entity is aware of the matter or ought to be aware of the matter—

(a) a subsidiary ceasing to be a member of the resolution entity's LAC consolidation group, other than as a result of the resolution authority removing the subsidiary from the group under rule 7(1)(a);

(b) a subsidiary becoming a member of the resolution entity's LAC consolidation group, other than as a result

of the resolution authority adding the subsidiary to the group under rule 7(1)(b);

(c) the principal activities of a subsidiary referred to in paragraph (b);

(d) any significant change to the principal activities of the resolution entity or any of its subsidiaries (including a subsidiary referred to in paragraph (b)).

(2) A material subsidiary must give written notice to the resolution authority of the following matters as soon as practicable after the material subsidiary is aware of the matter or ought to be aware of the matter—

(a) a subsidiary ceasing to be a member of the material subsidiary's LAC consolidation group, other than as a result of the resolution authority removing the subsidiary from the group under rule 7(1)(a);

(b) a subsidiary becoming a member of the material subsidiary's LAC consolidation group, other than as a result of the resolution authority adding the subsidiary to the group under rule 7(1)(b);

(c) the principal activities of a subsidiary referred to in paragraph (b);

(d) any significant change to the principal activities of the material subsidiary or any of its subsidiaries (including a subsidiary referred to in paragraph (b))

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Part 3

LAC Ratios

Division 1—External LAC Ratios for Resolution Entities

10. External LAC risk-weighted ratio

A resolution entity's external LAC risk-weighted ratio is the ratio, expressed as a percentage, of the resolution entity's external loss-absorbing capacity to its risk-weighted amount on either a solo or solo-consolidated basis, or a consolidated basis, determined in accordance with these Rules.

11. External LAC leverage ratio

A resolution entity's external LAC leverage ratio is the ratio, expressed as a percentage, of the resolution entity's external loss-absorbing capacity to its exposure measure, on either a solo or solo-consolidated basis, or a consolidated basis, determined in accordance with these Rules.

Division 2—Internal LAC Ratios for Material Subsidiaries

12. Internal LAC risk-weighted ratio

A material subsidiary's internal LAC risk-weighted ratio is the ratio, expressed as a percentage, of the material subsidiary's internal loss-absorbing capacity to its risk-weighted amount on either a solo or solo-consolidated basis, or a consolidated basis, determined in accordance with these Rules.

13. Internal LAC leverage ratio

A material subsidiary's internal LAC leverage ratio is the ratio, expressed as a percentage, of the material subsidiary's internal loss-absorbing capacity to its exposure measure, on either a solo or solo-consolidated basis, or a consolidated basis, determined in accordance with these Rules.

Division 3—Solo, Solo-consolidated and Consolidated Basis for Calculating LAC Ratios

14. Solo or solo-consolidated basis for calculating LAC ratios for resolution entities or material subsidiaries that are authorized institutions

(1) This rule applies to a resolution entity or material subsidiary that is an authorized institution.

(2) In calculating its external or internal LAC risk-weighted ratio (as the case requires) on a solo or solo-consolidated basis, the resolution entity or material subsidiary must—

(a) determine the denominator of its capital adequacy ratio as calculated under the Capital Rules on a solo or solo-consolidated basis;

(b) determine its risk-weighted amount on a solo or solo-consolidated basis;

(c) determine its external or internal loss-absorbing capacity on a solo or solo-consolidated basis; and

(d) determine its external or internal LAC risk-weighted ratio in accordance with these Rules on a solo or solo-consolidated basis.

(3) In calculating its external or internal LAC leverage ratio (as the case requires) on a solo or solo-consolidated basis, the resolution entity or material subsidiary must—

(a) determine the denominator of its leverage ratio as calculated under the Capital Rules on a solo or solo-consolidated basis;

(b) determine its exposure measure on a solo or solo-consolidated basis;

(c) determine its external or internal loss-absorbing capacity on a solo or solo-consolidated basis; and

(d) determine its external or internal LAC leverage ratio in accordance with these Rules on a solo or solo-consolidated basis.

15. Consolidated basis for calculating LAC ratios for resolution entities or material subsidiaries that are authorized institutions

(1) This rule applies to a resolution entity or material subsidiary that is an authorized institution.

(2) In calculating its external or internal LAC risk-weighted ratio (as the case requires) on a consolidated basis with reference to its LAC consolidation group, the resolution entity or material subsidiary must—

(a) subject to subrule (4), determine the denominator of its capital adequacy ratio as it would be calculated under the Capital Rules on a consolidated basis with reference to its LAC consolidation group;

(b) determine its risk-weighted amount on a consolidated basis with reference to its LAC consolidation group;

(c) determine its external or internal loss-absorbing capacity on a consolidated basis with reference to its LAC consolidation group; and

(d) determine its external or internal LAC risk-weighted ratio in accordance with these Rules on a consolidated basis with reference to its LAC consolidation group.

(3) In calculating its external or internal LAC leverage ratio (as the case requires) on a consolidated basis with reference to its LAC consolidation group, the resolution entity or material subsidiary must—

(a) determine the denominator of its leverage ratio as it would be calculated under the Capital Rules on a consolidated basis with reference to its LAC consolidation group;

(b) determine its exposure measure on a consolidated basis with reference to its LAC consolidation group;

(c) determine its external or internal loss-absorbing capacity on a consolidated basis with reference to its LAC consolidation group; and

(d) determine its external or internal LAC leverage ratio in accordance with these Rules on a consolidated basis with reference to its LAC consolidation group.

(4) For the purposes of subrule (2)(a)—

(a) in determining the contribution made to the denominator of its capital adequacy ratio by exposures of any entity that is a member of the LAC consolidation group of the resolution entity or material subsidiary but not a member of the capital consolidation group of the resolution entity or material subsidiary and that is not an authorized institution, the resolution entity or material subsidiary

must, unless otherwise agreed in writing by the resolution authority, use the methodology that would apply if that entity were an authorized institution using the prescribed approaches in relation to calculation of capital adequacy ratios referred to in Part 2 of the Capital Rules which do not require the Monetary Authority to be satisfied as to any matter, or require any consent of or consultation with the Monetary Authority under that Part; and

(b) in determining the contribution made to the denominator of its capital adequacy ratio by exposures of—

(i) any entity that is a member of the capital consolidation group of the resolution entity or material subsidiary; or

(ii) any entity that is a member of the LAC consolidation group of the resolution entity or material subsidiary but not a member of the capital consolidation group of the resolution entity or material subsidiary and that is an authorized institution,

the resolution entity or material subsidiary must, unless otherwise agreed in writing by the resolution authority, use the methodologies that are being applied to that entity under the Capital Rules in determining the contribution made to the denominator of the applicable capital adequacy ratio.

16. Consolidated basis for calculating LAC ratios for resolution entities or material subsidiaries that are not authorized institutions

(1) This rule applies to a resolution entity or material subsidiary that is—

(a) an HK holding company; or

(b) an HK affiliated operational entity.

(2) In calculating its external or internal LAC risk-weighted ratio (as the case requires) on a consolidated basis with reference to its LAC consolidation group, the resolution entity or material subsidiary must—

(a) subject to subrule (4), determine the denominator of its capital adequacy ratio as that ratio would be calculated under the Capital Rules on a consolidated basis with reference to its LAC consolidation group if the resolution entity or material subsidiary were an authorized institution;

(b) determine its risk-weighted amount on a consolidated basis with reference to its LAC consolidation group;

(c) determine its external or internal loss-absorbing capacity on a consolidated basis with reference to its LAC consolidation group; and

(d) determine its external or internal LAC risk-weighted ratio in accordance with these Rules on a consolidated basis with reference to its LAC consolidation group.

(3) In calculating its external or internal LAC leverage ratio (as the case requires) on a consolidated basis with reference to its LAC consolidation group, the resolution entity or material subsidiary must—

(a) determine the denominator of its leverage ratio as that ratio would be calculated under the Capital Rules on a consolidated basis with reference to its LAC consolidation group if the resolution entity or material subsidiary were an authorized institution;

(b) determine its exposure measure on a consolidated basis with reference to its LAC consolidation group;

(c) determine its external or internal loss-absorbing capacity on a consolidated basis with reference to its LAC consolidation group; and

(d) determine its external or internal LAC leverage ratio in accordance with these Rules on a consolidated basis with reference to its LAC consolidation group.

(4) For the purposes of subrule (2)(a)—

(a) in determining the contribution made to the denominator of its capital adequacy ratio by exposures of—

(i) the resolution entity or material subsidiary; or

(ii) any entity that is a member of the LAC consolidation group of the resolution entity or material subsidiary but not a member of the capital consolidation group of the principal authorized institution of the resolution entity or material subsidiary and that is not an authorized institution,

the resolution entity or material subsidiary must, unless otherwise agreed in writing by the resolution authority, use the methodology that would apply if the resolution entity or material subsidiary or that entity were an authorized institution using the prescribed approaches in relation to calculation of capital adequacy ratios referred to in Part 2 of the Capital Rules which do not require the

Monetary Authority to be satisfied as to any matter, or require any consent of or consultation with the Monetary Authority under that Part; and

(b) in determining the contribution made to the denominator of its capital adequacy ratio by exposures of—

(i) any entity that is a member of the capital consolidation group of the principal authorized institution of the resolution entity or material subsidiary; or

(ii) any entity that is a member of the LAC consolidation group of the resolution entity or material subsidiary but not a member of the capital consolidation group of the principal authorized institution of the resolution entity or material subsidiary and that is an authorized institution,

the resolution entity or material subsidiary must, unless otherwise agreed in writing by the resolution authority, use the methodologies that are being applied to that entity under the Capital Rules in determining the contribution made to the denominator of the applicable capital adequacy ratio.

17. Consolidated basis for calculating capital

For the purpose of determining a resolution entity's or material subsidiary's CET1 capital, Tier 1 capital and Tier 2 capital on a consolidated basis with reference to its LAC consolidation group, the Capital Rules apply as if a reference in the Capital Rules to its consolidation group were a reference to its LAC consolidation group.

Part 4

Determination of Minimum LAC Ratios

Division 1—Capital Component Ratio and Resolution Component Ratio

18. Capital component ratio

(1) For a resolution entity that is an authorized institution the membership of whose LAC consolidation group is the same as its capital consolidation group, the capital component ratio is equal to—

(a) the minimum Total capital ratio that the entity is required to maintain on a consolidated basis in respect of its capital consolidation group under the Capital Rules; or

(b) if that minimum is varied under section 97F of the Banking Ordinance (Cap. 155), that minimum as so varied.

(2) Subject to subrule (4), for a resolution entity that is an authorized institution the membership of whose LAC consolidation group is different from its capital consolidation group, the capital component ratio is equal to—

(a) the minimum Total capital ratio that the entity is required to maintain in respect of its capital consolidation group under the Capital Rules; or

(b) if that minimum is varied under section 97F of the Banking Ordinance (Cap. 155), that minimum as so varied.

(3) Subject to subrule (4), for a resolution entity that is an HK holding company or HK affiliated operational entity, the capital component ratio is equal to—

(a) the minimum Total capital ratio that the entity's principal authorized institution is required to maintain on a consolidated basis in respect of its capital consolidation group under the Capital Rules; or

(b) if that minimum is varied under section 97F of the Banking Ordinance (Cap. 155), that minimum as so varied.

(4) The resolution authority may, in accordance with rule 20, vary the capital component ratio for a resolution entity referred to in subrule (2) or (3) if satisfied that it is prudent to do so to reflect the difference in composition of the resolution entity's LAC consolidation group and the capital consolidation group referred to in subrule (2) or (3) (as the case requires).

(5) To avoid doubt, from time to time the resolution authority may, subject to subrule (4), further vary the capital component ratio for a resolution entity referred to in subrule (2) or (3).

19. Resolution component ratio

(1) Subject to subrules (2) and (7), a resolution entity's resolution component ratio is equal to its capital component ratio.

(2) The resolution authority may, on the resolution authority's volition or on a resolution entity's application, in accordance with rule 20, vary a resolution entity's resolution component ratio if satisfied that it is prudent to do so.

(3) For the purposes of subrule (2), a resolution entity may, within the relevant period, apply in writing to the resolution authority, requesting a variation—

(a) to reduce its resolution component ratio; or

(b) to reduce an increase to its resolution component ratio that would apply to it as a result of a variation made under section 97F of the Banking Ordinance (Cap. 155).

(4) An application under subrule (3) must specify—

(a) the reduction requested; and

(b) the grounds for the reduction requested.

(5) In determining whether it is prudent to vary a resolution entity's resolution component ratio (including whether to accept a resolution entity's application for variation under subrule (3)), the resolution authority may take into account—

(a) any stabilization options expected to be applied under the preferred resolution strategy covering the resolution entity;

(b) any risks to resolvability related to the fact that there may be entities that are in the resolution entity's resolution group but not in its LAC consolidation group, and whose assets are therefore not otherwise taken into account when determining the resolution entity's LAC requirements; and

(c) any other matters the resolution authority considers relevant.

(6) To avoid doubt, from time to time the resolution authority may, subject to subrule (2), further vary the resolution component ratio for a resolution entity.

(7) If a resolution entity's capital component ratio has increased as a result of the exercise by the Monetary Authority of the power of variation under section 97F of the Banking Ordinance (Cap. 155), the corresponding increase in the resolution entity's resolution component ratio under subrule

(1) takes effect 12 months after the increase in the capital component ratio.

(8) In this rule—

relevant period ( )—

(a) in relation to subrule (3)(a), means the period of 14 days beginning on the date on which the further written notice classifying the resolution entity under rule 8(2)(a) or (3) (as the case requires) was served; or

(b) in relation to subrule (3)(b), means the period of 14 days beginning on the date on which the increase in the resolution entity's capital component ratio, mentioned in subrule (7), takes effect.

20. Procedure for varying capital component ratio or resolution component ratio

(1) If the resolution authority proposes to vary a resolution entity's capital component ratio or resolution component ratio, the resolution authority must serve a written notice on the resolution entity—

(a) specifying the resolution authority's proposed variation;

(b) specifying the grounds for the proposed variation; and

(c) including a statement that the resolution entity may, within 14 days (or a longer period allowed by the resolution authority), make written representations to the resolution authority on any matter specified in the notice.

(2) If the resolution authority proposes not to vary a resolution entity's resolution component ratio following the resolution entity's application under subrule 19(3), the resolution

authority must serve a written notice on the resolution entity—

(a) specifying the resolution authority's proposed decision not to vary the resolution component ratio;

(b) specifying the grounds for the proposed decision; and

(c) including a statement that the resolution entity may, within 14 days (or a longer period allowed by the resolution authority), make written representations to the resolution authority on any matter specified in the notice.

(3) If representations are made in accordance with subrule (1)(c), the resolution authority, after considering the representations, may—

(a) serve a further written notice on the resolution entity—

(i) confirming the proposed variation; or

(ii) modifying the proposed variation to take into account any of the representations; or

(b) decide not to make the proposed variation.

(4) If representations are made in accordance with subrule (2)(c), the resolution authority, after considering the representations, may serve a further written notice on the resolution entity—

(a) confirming the proposed decision not to make any variation to the resolution component ratio; or

(b) notifying the resolution entity of the variation, as determined by the resolution authority.

(5) If no representations are made in accordance with subrule (1)(c), the resolution authority may serve a written further notice on the resolution entity confirming the proposed variation.

(6) If no representations are made in accordance with subrule (2)(c), the resolution authority may serve a written further notice on the resolution entity confirming the proposed decision not to vary the resolution component ratio.

(7) Subject to subrule (8), the further written notice served under subrule (3)(a), (4)(b) or (5) has the effect of varying the capital component ratio or the resolution component ratio, in accordance with its terms, on the date specified in the notice.

(8) For a variation of a resolution entity's capital component ratio or resolution component ratio that results in an increase in any of its minimum LAC ratios the date referred to in subrule (7) must be at least 12 months after the date on which the further written notice is served under subrule (3)(a) or (5).

(9) The following decisions of the resolution authority are reviewable decisions—

(a) a decision to vary a resolution entity's resolution component ratio;

(b) a decision not to vary a resolution entity's resolution component ratio following an application made under rule 19(3).

Division 2—Minimum External LAC Ratios for Resolution Entities

21. Minimum external LAC risk-weighted ratio

(1) Subject to subrule (2), the minimum external LAC risk-weighted ratio for a resolution entity is equal to the sum of its capital component ratio and its resolution component ratio.

(2) The resolution authority, by written notice served on a resolution entity that is a global systemically important bank, may increase the resolution entity's minimum external LAC

risk-weighted ratio to reflect the minimum TLAC requirements set out in the TLAC term sheet.

Note—

The TLAC term sheet sets out minimum risk-weighted ratios of 16% and 18% from certain dates for global systemically important banks.

22. Minimum external LAC leverage ratio

(1) Subject to subrule (2), the minimum external LAC leverage ratio for a resolution entity is determined in accordance with the following formula—

$$\left(1+\frac{\text{resolution component ratio}}{\text{capital component ratio}}\right)\times 3\%$$

(2) The resolution authority, by written notice served on a resolution entity that is a global systemically important bank, may increase the resolution entity's minimum external LAC leverage ratio to reflect the minimum TLAC requirements set out in the TLAC term sheet.

Note—

The TLAC term sheet sets out minimum leverage ratios of 6% and 6.75% from certain dates for global systemically important banks.

Division 3—Minimum Internal LAC Ratios for Material Subsidiaries

23. Minimum internal LAC risk-weighted ratio

A material subsidiary's minimum internal LAC risk-weighted ratio is equal to the material subsidiary's modelled minimum external

LAC risk-weighted ratio multiplied by the material subsidiary's internal LAC scalar.

24. Minimum internal LAC leverage ratio

A material subsidiary's minimum internal LAC leverage ratio is equal to the material subsidiary's modelled minimum external LAC leverage ratio multiplied by the material subsidiary's internal LAC scalar.

25. Modelled minimum external LAC risk-weighted ratio and modelled minimum external LAC leverage ratio

(1) Subject to subrule (2), a material subsidiary's modelled minimum external LAC risk-weighted ratio and modelled minimum external LAC leverage ratio are equal to the minimum external LAC risk-weighted ratio and minimum external LAC leverage ratio, respectively, that would apply to the material subsidiary if it were a resolution entity, determined in accordance with Divisions 1 and 2 as if a reference in those Divisions to a resolution entity were a reference to the material subsidiary.

(2) In determining whether it is prudent to vary the resolution component ratio applicable to a material subsidiary for the purpose of determining its modelled minimum external LAC risk-weighted ratio or modelled minimum external LAC leverage ratio, the resolution authority, instead of the matters referred to in rule 19(5), may take into account—

(a) any stabilization options expected to be applied should the material subsidiary be put into resolution;

(b) the preferred resolution strategy covering the material subsidiary;

(c) any risks to resolvability related to the fact that there may be entities that are in the material subsidiary's material sub-group but not in its LAC consolidation group, and whose assets are therefore not otherwise taken into account when determining the material subsidiary's LAC requirements; and

(d) any other matters the resolution authority considers relevant.

26. Internal LAC scalar

(1) Subject to subrule (2), a material subsidiary's internal LAC scalar is 75%.

(2) The resolution authority may, in accordance with rule 27, increase a material subsidiary's internal LAC scalar if satisfied that it is prudent to do so.

(3) In determining whether it is prudent to increase a material subsidiary's internal LAC scalar, the resolution authority may take into account—

(a) the preferred resolution strategy covering the material subsidiary;

(b) the likely availability of additional financial resources within the material subsidiary's resolution group that could be expected to be deployed to restore to viability any authorized institution in the material subsidiary's material sub-group; and

(c) any other matters the resolution authority considers relevant.

(4) The maximum percentage to which the resolution authority may increase a material subsidiary's internal LAC scalar under subrule (2) is—

(a) 90% where the preferred resolution strategy covering the material subsidiary envisages all internal loss-absorbing capacity issued by the material subsidiary being issued directly to an entity that is not incorporated in Hong Kong; or

(b) 100% where the preferred resolution strategy covering the material subsidiary envisages some or all internal loss-absorbing capacity issued by the material subsidiary being issued directly to an entity that is incorporated in Hong Kong.

(5) To avoid doubt, from time to time the resolution authority may, subject to subrule (4), further increase a material subsidiary's internal LAC scalar, or revoke or reduce a previous increase.

27. Procedure for increasing internal LAC scalar

(1) If the resolution authority proposes to increase a material subsidiary's internal LAC scalar, the resolution authority must serve a written notice on the material subsidiary—

(a) specifying the resolution authority's proposed increase;

(b) specifying the grounds for the proposed increase; and

(c) including a statement that the material subsidiary may, within 14 days (or a longer period allowed by the resolution authority), make written representations to the resolution authority on any matter specified in the notice.

(2) If representations are made in accordance with subrule (1)(c), the resolution authority, after considering the representations, may—

(a) serve a further written notice on the material subsidiary—

(i) confirming the proposed increase; or

(ii) modifying the proposed increase to take into account any of the representations; or

(b) decide not to make the proposed increase.

(3) If no representations are made in accordance with subrule (1)(c), the resolution authority may serve a further written notice on the material subsidiary confirming the proposed increase.

(4) Subject to subrule (5), the further written notice served under subrule (2)(a) or (3) has the effect of increasing the internal LAC scalar, in accordance with its terms, on the date specified in the notice.

(5) The date referred to in subrule (4) must be at least 12 months after the date on which the further written notice is served under subrule (2)(a) or (3).

Division 4—Requirements to Maintain Minimum LAC Ratios

28. Requirement for resolution entities to maintain minimum external LAC ratios

(1) Subject to rule 36, at all times after the relevant period, a resolution entity must have—

(a) an external LAC risk-weighted ratio that is not less than its minimum external LAC risk-weighted ratio, calculated on a consolidated basis with reference to its LAC consolidation group; and

(b) an external LAC leverage ratio that is not less than its minimum external LAC leverage ratio, calculated on a

consolidated basis with reference to its LAC consolidation group.

(2) Subject to rule 36, at all times after the relevant period, a resolution entity that is an authorized institution must, in addition to complying with subrule (1), have—

(a) an external LAC risk-weighted ratio that is not less than its minimum external LAC risk-weighted ratio multiplied by its solo LAC scalar, calculated on a solo basis or, if the authorized institution has been granted an approval under section 28(2)(a) of the Capital Rules, a solo-consolidated basis with reference to the subsidiaries specified in the approval; and

(b) an external LAC leverage ratio that is not less than its minimum external LAC leverage ratio multiplied by its solo LAC scalar, calculated on a solo basis or, if the authorized institution has been granted an approval under section 28(2)(a) of the Capital Rules, a solo-consolidated basis with reference to the subsidiaries specified in the approval.

(3) In this rule—

relevant period ( ), in relation to a resolution entity, means—

(a) the period of 24 months immediately following the classification date for the resolution entity; or

(b) any longer period notified to the resolution entity by the resolution authority under rule 31.

29. Requirement for material subsidiaries to maintain minimum internal LAC ratios

(1) Subject to rule 36, at all times after the relevant period, a material subsidiary must have—

(a) an internal LAC risk-weighted ratio that is not less than its minimum internal LAC risk-weighted ratio, calculated on a consolidated basis with reference to its LAC consolidation group; and

(b) an internal LAC leverage ratio that is not less than its minimum internal LAC leverage ratio, calculated on a consolidated basis with reference to its LAC consolidation group.

(2) Subject to rule 36, at all times after the relevant period, a material subsidiary that is an authorized institution must, in addition to complying with subrule (1), have—

(a) an internal LAC risk-weighted ratio that is not less than its minimum internal LAC risk-weighted ratio multiplied by its solo LAC scalar, calculated on a solo basis or, if the authorized institution has been granted an approval under section 28(2)(a) of the Capital Rules, a solo-consolidated basis with reference to the subsidiaries specified in the approval; and

(b) an internal LAC leverage ratio that is not less than its minimum internal LAC leverage ratio multiplied by its solo LAC scalar, calculated on a solo basis or, if the authorized institution has been granted an approval under section 28(2)(a) of the Capital Rules, a solo-consolidated basis with reference to the subsidiaries specified in the approval.

(3) In this rule—

relevant period ( ), in relation to a material subsidiary, means—

(a) the period of 24 months immediately following the classification date for the material subsidiary; or

(b) any longer period notified to the material subsidiary by the resolution authority under rule 31.

30. Solo LAC scalar

(1) Subject to subrule (2), the solo LAC scalar for a resolution entity or material subsidiary that is an authorized institution is 100%.

(2) The resolution authority, by written notice served on a resolution entity or material subsidiary, may reduce the solo LAC scalar for the resolution entity or material subsidiary if satisfied that it is prudent to do so.

(3) In determining whether it is prudent to reduce a solo LAC scalar for a resolution entity or material subsidiary, the resolution authority may take into account—

(a) the extent to which the solo LAC scalar being set at 100% would result in the resolution entity or material subsidiary having to maintain a greater amount of loss-absorbing capacity than required to meet its LAC requirements on a consolidated basis;

(b) the extent to which the solo LAC scalar being set at 100% would impact on the quantity and availability of non-pre-positioned loss-absorbing capacity; and

(c) any other matters the resolution authority considers relevant.

(4) For the purposes of this rule, the non-pre-positioned loss-absorbing capacity of a resolution entity or material subsidiary is the amount of loss-absorbing capacity that the resolution entity or material subsidiary needs to maintain to meet its LAC requirements on a consolidated basis, less—

(a) the amount of loss-absorbing capacity that the resolution entity or material subsidiary needs to maintain to meet

its LAC requirements on a solo basis, excluding any holdings referred to in paragraph (b); and

(b) any holdings by the resolution entity or material subsidiary of loss-absorbing capacity maintained by other members of its resolution group that those other members are required to maintain to meet any applicable LAC requirements.

(5) To avoid doubt, from time to time the resolution authority may further reduce the solo LAC scalar for a resolution entity or material subsidiary, or revoke or reduce a previous reduction.

(6) A revocation or reduction of a previous reduction of a solo LAC scalar for a resolution entity or material subsidiary takes effect on the date specified in the notice under subrule (2), which must be at least 12 months after the date on which the notice is served on the resolution entity or material subsidiary.

31. Extension of relevant period

The resolution authority may, by written notice served on a resolution entity or material subsidiary, extend the period after which the resolution entity or material subsidiary must meet a LAC requirement, if satisfied that it is prudent to do so.

32. Further LAC ratio requirement for certain G-SIBs designated before 2016

(1) This rule applies if—

(a) a resolution entity or material subsidiary that is an authorized institution or HK holding company is a global systemically important bank;

(b) the resolution entity or material subsidiary, or the group of companies of which it is a member, or another

member of that group (as the case may be) was designated as a global systemically important bank by the Financial Stability Board on or before 31 December 2015 and has been continuously so designated since its date of designation;

(c) the global systemically important bank is required by section 21 of the TLAC term sheet to meet minimum TLAC requirements from 1 January 2019; and

(d) the classification date for the resolution entity or material subsidiary is on or before 30 September 2021.

(2) Subject to rule 36, in addition to any requirement to maintain minimum LAC ratios under this Division, the resolution entity or material subsidiary must ensure that, at all times after the period of 3 months after its classification date, or any longer period notified in writing to the resolution entity or material subsidiary by the resolution authority—

(a) in the case of a resolution entity—

(i) its external LAC risk-weighted ratio calculated on a consolidated basis is not less than 16%; and

(ii) its external LAC leverage ratio calculated on a consolidated basis is not less than 6%; or

(b) in the case of a material subsidiary—

(i) its internal LAC risk-weighted ratio calculated on a consolidated basis is not less than 16% multiplied by its internal LAC scalar; and

(ii) its internal LAC leverage ratio calculated on a consolidated basis is not less than 6% multiplied by its internal LAC scalar.

Division 5—Minimum LAC Debt Requirement

33. Minimum LAC debt requirement for resolution entities

(1) Subject to rule 35—

(a) if a resolution entity is required by these Rules to meet a minimum external LAC risk-weighted ratio, or is subject to a requirement under rule 32, the external LAC risk-weighted ratio that it would have if its external loss-absorbing capacity was equal to the sum of its debt instruments must be no less than one-third of its minimum external LAC risk-weighted ratio; and

(b) if a resolution entity is required by these Rules to meet a minimum external LAC leverage ratio, or is subject to a requirement under rule 32, the external LAC leverage ratio that it would have if its external loss-absorbing capacity was equal to the sum of its debt instruments must be no less than one-third of its minimum external LAC leverage ratio.

(2) For the purposes of this rule, a debt instrument is an instrument—

(a) that is an external LAC debt instrument; and

(b) that evidences indebtedness (whether or not it is treated as debt or equity for accounting purposes).

34. Minimum LAC debt requirement for material subsidiaries

(1) Subject to rule 35—

(a) if a material subsidiary is required by these Rules to meet a minimum internal LAC risk-weighted ratio, or is subject to a requirement under rule 32, the internal LAC risk-weighted ratio that it would have if its internal loss-

absorbing capacity was equal to the sum of its debt instruments must be no less than one-third of its minimum internal LAC risk-weighted ratio; and

(b) if a material subsidiary is required by these Rules to meet a minimum internal LAC leverage ratio, or is subject to a requirement under rule 32, the internal LAC leverage ratio that it would have if its internal loss-absorbing capacity was equal to the sum of its debt instruments must be no less than one-third of its minimum internal LAC leverage ratio.

(2) For the purposes of this rule, a debt instrument is an instrument—

(a) that is an internal LAC debt instrument; and

(b) that evidences indebtedness (whether or not it is treated as debt or equity for accounting purposes).

35. Reduction of minimum LAC debt requirement

(1) The resolution authority, by written notice served on a resolution entity or material subsidiary, may reduce the minimum debt requirement under rule 33 or 34 for the resolution entity or material subsidiary to below one-third, if the resolution authority is satisfied that it is prudent to do so.

(2) In determining whether it is prudent to reduce the minimum debt requirement for a resolution entity or material subsidiary, the resolution authority may take into account—

(a) the total capital of the resolution entity or material subsidiary;

(b) the preferred resolution strategy covering the resolution entity or material subsidiary; and

(c) any other matters the resolution authority considers relevant.

(3) To avoid doubt, from time to time the resolution authority may further reduce the minimum debt requirement for a resolution entity or material subsidiary, or revoke or reduce a previous reduction.

(4) A reduction of a minimum debt requirement or revocation of a previous reduction takes effect on the date specified in the notice under subrule (1).

(5) For a revocation or reduction of a previous reduction of a minimum debt requirement for a resolution entity or material subsidiary, the date referred to in subrule (4) must be at least 12 months after the date on which the notice under subrule (1) is served on the resolution entity or material subsidiary.

Division 6—Suspension of LAC requirements

36. Suspension of LAC requirements following certain occurrences

(1) This rule applies if any of the following things occurs—

(a) a stabilization option is applied in respect of an asset, right or liability of a resolution entity or material subsidiary;

(b) any Additional Tier 1 capital instrument, Tier 2 capital instrument or internal non-capital LAC debt instrument of a resolution entity or material subsidiary is written down or converted into ordinary shares as contemplated in the terms and conditions of the instrument;

(c) a capital reduction instrument is made in respect of a resolution entity or material subsidiary; or

(d) anything is done in accordance with an agreement made, with the written consent of the resolution authority, between a resolution entity or material subsidiary and any of its creditors to write down, cancel, convert, change the form of or otherwise modify any of its LAC instruments.

(2) If the occurrence results in the resolution entity or material subsidiary failing to meet any of its LAC requirements, the resolution entity or material subsidiary is not required to meet any LAC requirement before the expiry of—

(a) the period of 24 months after the occurrence; or

(b) any longer period notified in writing to the resolution entity or material subsidiary by the resolution authority

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Part 5

Calculation of Loss-absorbing Capacity

37. Calculation of external loss-absorbing capacity of resolution entity

Subject to rule 42, a resolution entity's external loss-absorbing capacity is the sum of the following items, calculated in Hong Kong dollars, and after the deductions specified in rule 38 have been made in accordance with that rule—

(a) the total capital of the resolution entity less any contribution to the total capital from—

(i) any Additional Tier 1 capital instrument or Tier 2 capital instrument that is not an external LAC debt instrument;

(ii) where a resolution entity's external loss-absorbing capacity is being calculated on a consolidated basis, any regulatory capital instrument—

(A) that is not a CET1 capital instrument; and

(B) that is issued by a member of the resolution entity's LAC consolidation group other than the resolution entity;

(b) subject to paragraph (a), any portion of the resolution entity's Tier 2 capital instruments that are external LAC debt instruments that has been amortized in accordance with section 1(d) of Schedule 4C to the Capital Rules;

(c) external non-capital LAC debt instruments issued by the resolution entity.

38. Deductions from external loss-absorbing capacity

(1) A resolution entity must deduct from its external loss-absorbing capacity—

(a) the amount of any direct holdings, indirect holdings and synthetic holdings by the resolution entity of its own non-capital LAC liabilities, unless already derecognized under applicable accounting standards, calculated in accordance with Schedule 3;

(b) the amount of any direct holdings, indirect holdings and synthetic holdings by the resolution entity of non-capital LAC liabilities issued by a financial sector entity that is a group company that is not a member of the resolution entity's LAC consolidation group, calculated in accordance with Schedule 4;

(c) if the resolution entity is required to meet a minimum external LAC risk-weighted ratio or minimum external LAC leverage ratio on a solo basis, the amount of the resolution entity’s direct holdings of non-capital LAC liabilities issued by entities that are members of the resolution entity’s LAC consolidation group; and

(d) if the resolution entity is required to meet a minimum external LAC risk-weighted ratio or minimum external LAC leverage ratio on a solo-consolidated basis, the amount of the resolution entity’s direct holdings of non-capital LAC liabilities issued by entities, other than any solo-consolidated subsidiaries in relation to the resolution entity, that are members of the resolution entity’s LAC consolidation group.

(2) A resolution entity must include in the amount to be deducted under subrule (1) potential future holdings that the resolution entity could be contractually obliged to purchase.

39. Calculation of internal loss-absorbing capacity of material subsidiary

Subject to rule 42, a material subsidiary's internal loss-absorbing capacity is the sum of the following items, calculated in Hong Kong dollars, and after the deductions specified in rule 40 have been made in accordance with that rule—

(a) the total capital of the material subsidiary less any contribution to the total capital from—

(i) any Additional Tier 1 capital instrument or Tier 2 capital instrument that is not an internal LAC debt instrument;

(ii) any instrument that is not issued directly or indirectly to the resolution entity in the material subsidiary's resolution group; and

(iii) where a material subsidiary's internal loss-absorbing capacity is being calculated on a consolidated basis, any regulatory capital instrument—

(A) that is not a CET1 capital instruments; and

(B) that is issued by a member of the material subsidiary's LAC consolidation group other than the material subsidiary;

(b) subject to paragraph (a), any portion of any of the material subsidiary's Tier 2 capital instruments that are internal LAC debt instruments that has been amortized in accordance with section 1(d) of Schedule 4C to the Capital Rules;

(c) internal non-capital LAC debt instruments issued by the material subsidiary directly or indirectly to, and held

directly or indirectly by, the resolution entity in the material subsidiary's resolution group.

40. Deductions from internal loss-absorbing capacity

(1) A material subsidiary must deduct from its internal loss-absorbing capacity—

(a) the amount of any direct holdings, indirect holdings and synthetic holdings by the material subsidiary of its own non-capital LAC liabilities, unless already derecognized under applicable accounting standards, calculated in accordance with Schedule 3;

(b) the amount of any direct holdings, indirect holdings and synthetic holdings by the material subsidiary of non-capital LAC liabilities issued by a financial sector entity that is a group company that is not a member of the material subsidiary's LAC consolidation group, calculated in accordance with Schedule 4;

(c) if the material subsidiary is required to meet a minimum internal LAC risk-weighted ratio or minimum internal LAC leverage ratio on a solo basis, the amount of the material subsidiary's direct holdings of non-capital LAC liabilities issued by entities that are members of the material subsidiary's LAC consolidation group; and

(d) if the material subsidiary is required to meet a minimum internal LAC risk-weighted ratio or minimum internal LAC leverage ratio on a solo-consolidated basis, the amount of the material subsidiary's direct holdings of non-capital LAC liabilities issued by entities, other than any solo-consolidated subsidiaries in relation to the material subsidiary, that are members of the material subsidiary's LAC consolidation group.

(2) A material subsidiary must include in the amount to be deducted under subrule (1) potential future holdings that the material subsidiary could be contractually obliged to purchase.

41. Resolution authority may require evidence

(1) The resolution authority, by written notice served on a resolution entity, may require the resolution entity to provide to the resolution authority, within the time specified in the notice, evidence of a kind specified by the resolution authority that the resolution entity's external loss-absorbing capacity, or items claimed by the resolution entity to form part of its external loss-absorbing capacity, meet the requirements of these Rules.

(2) The resolution authority, by written notice served on a material subsidiary, may require the material subsidiary to provide to the resolution authority, within the time specified in the notice, evidence of a kind specified by the resolution authority that the material subsidiary's internal loss-absorbing capacity, or items claimed by the material subsidiary to form part of its internal loss-absorbing capacity, meet the requirements of these Rules.

(3) Without limiting the kinds of evidence the resolution authority may specify, the resolution authority may require the resolution entity to obtain, and provide to the resolution authority, independent legal advice acceptable to the resolution authority.

42. Requirement not to include, or to discontinue inclusion of, items in external or internal loss-absorbing capacity

(1) If the resolution authority is satisfied that it is prudent to do so, the resolution authority may, in accordance with rule 43—

(a) require a resolution entity—

(i) not to include an item in the calculation of its external loss-absorbing capacity; or

(ii) to discontinue the inclusion of an item in the calculation of its external loss-absorbing capacity; or

(b) require a material subsidiary—

(i) not to include an item in the calculation of its internal loss-absorbing capacity; or

(ii) to discontinue the inclusion of an item in the calculation of its internal loss-absorbing capacity.

(2) In considering whether it is prudent to require a resolution entity or material subsidiary not to include, or to discontinue the inclusion of, an item, the resolution authority may take into account—

(a) any matters that, in the opinion of the resolution authority, may undermine the ability of the item to absorb losses or otherwise contribute to an orderly resolution as contemplated by the preferred resolution strategy covering the resolution entity or material subsidiary; and

(b) any other matters the resolution authority considers relevant.

43. Procedure for imposing requirement not to include, or to discontinue inclusion of, items in external or internal loss-absorbing capacity

(1) If the resolution authority proposes to impose a requirement on a resolution entity or material subsidiary under rule 42, the

resolution authority must serve a written notice on the resolution entity or material subsidiary—

(a) specifying the resolution authority's proposed requirement;

(b) specifying the grounds for the proposed requirement; and

(c) including a statement that the resolution entity or material subsidiary may, within 14 days (or a longer period allowed by the resolution authority), make written representations to the resolution authority on any matter specified in the notice.

(2) If representations are made in accordance with subrule (1)(c), the resolution authority, after considering the representations, may—

(a) serve a further written notice on the resolution entity or material subsidiary—

(i) confirming the proposed requirement; or

(ii) modifying the proposed requirement to take into account any of the representations; or

(b) decide not to impose the proposed requirement.

(3) If no representations are made in accordance with subrule (1)(c), the resolution authority may serve a further written notice on the resolution entity or material subsidiary confirming the proposed requirement.

(4) The further written notice served under subrule (2)(a) or (3) has the effect of imposing the requirement on the resolution entity or material subsidiary in accordance with its terms, on the date specified in the notice

Part 6

Disclosure

44. When do disclosure requirements apply

A requirement on a disclosure entity to make a quarterly or semi-annual disclosure under this Part applies in relation to each quarterly reporting period or semi-annual reporting period (as the case requires) of the disclosure entity that ends at least 3 months after the classification date of the disclosure entity.

45. Key metrics—loss-absorbing capacity—quarterly disclosures

(1) A disclosure entity must disclose, for each quarterly reporting period—

(a) summary information on its loss-absorbing capacity; and

(b) an explanation of any material changes to its loss-absorbing capacity during the period, including the key drivers of those changes.

(2) In addition to subrule (1), a disclosure entity that is a material subsidiary in a resolution group a member of which is a non-Hong Kong resolution entity must disclose, for each quarterly reporting period, to the extent to which the disclosure entity can reasonably obtain the necessary information—

(a) summary information on the loss-absorbing capacity of the non-Hong Kong resolution entity; and

(b) an explanation of any material changes to the loss-absorbing capacity of the non-Hong Kong resolution entity during the period, including the key drivers of those changes.

46. Composition of loss-absorbing capacity—semi-annual disclosures

(1) A disclosure entity that is a resolution entity must disclose, for each semi-annual reporting period—

(a) a detailed breakdown of its external loss-absorbing capacity; and

(b) an explanation of any material changes to its external loss-absorbing capacity during the period, including the key drivers of those changes.

(2) A disclosure entity that is a material subsidiary must disclose, for each semi-annual reporting period—

(a) a detailed breakdown of its internal loss-absorbing capacity; and

(b) an explanation of any material changes to its internal loss-absorbing capacity during the period, including the key drivers of those changes.

47. Resolution entity—creditor ranking at legal entity level—semi-annual disclosures

A disclosure entity that is a resolution entity must disclose, for each semi-annual reporting period—

(a) information on the priority that creditors would enjoy on a winding up of the disclosure entity; and

(b) where appropriate, institution-specific or jurisdiction-specific information relating to creditor hierarchies on a winding up of the disclosure entity.

48. Material subsidiary—creditor ranking at legal entity level—semi-annual disclosures

A disclosure entity that is a material subsidiary must disclose, for each semi-annual reporting period—

(a) information on the priority that creditors would enjoy on a winding up of the disclosure entity; and

(b) where appropriate, institution-specific or jurisdiction-specific information relating to creditor hierarchies on a winding up of the disclosure entity.

49. Main features of regulatory capital instruments and of other non-capital LAC debt instruments—semi-annual disclosures

(1) A disclosure entity must disclose, for each semi-annual reporting period—

(a) the main features of its CET1 capital instruments, Additional Tier 1 capital instruments, Tier 2 capital instruments and non-capital LAC debt instruments (each referred to in this rule as a ***relevant instrument***); and

(b) a direct link to the relevant section of its internet website where the full terms and conditions of all relevant instruments can be found.

(2) Whenever—

(a) a relevant instrument—

(i) is issued and included in a disclosure entity's loss-absorbing capacity;

(ii) is repaid; or

(iii) ceases to be included in a disclosure entity's loss-absorbing capacity; or

(b) there is a redemption, conversion or write-down, or any other material change in the nature, of a relevant instrument issued by a disclosure entity,

the disclosure entity must, as soon as practicable, update the disclosure it has made under subrule (1) in order to reflect the changes arising from the event referred to in paragraph (a) or (b).

50. Medium of disclosure

(1) If a disclosure entity is required under these Rules to disclose information, it must make that disclosure by—

(a) preparing, in the Chinese and English languages, a statement—

(i) that, subject to subrule (2) and rule 54, is in the form exclusively of a standalone document or a discrete section of the entity's financial statements (***discrete section***); and

(ii) in which the information required to be disclosed is readily identifiable;

(b) subject to subrule (2) and rule 59, presenting the information required to be disclosed in the format, and using the standard disclosure templates or tables specified by the resolution authority; and

(c) complying with the other provisions of this rule applicable to or in relation to the statement.

(2) If the resolution authority permits in a specification under subrule (1)(b) and if all the conditions specified in subrule (3) are met, any part of the information required to be disclosed may be contained in a separate document that is signposted in the standalone document or the discrete section.

(3) The conditions are—

(a) that the disclosure entity signposts clearly, in the standalone document or the discrete section, the location where the information published elsewhere is published, providing, at a minimum, the following information—

(i) a reference to the format, templates and tables specified by the resolution authority to which the signposting relates;

(ii) the full title of the separate document in which the information is published;

(iii) a link to the relevant section of the entity's internet website where the separate document can be accessed (if applicable);

(iv) the page and paragraph number of the separate document where the information is located; and

(b) that the level of assurance on the reliability of data in the separate document is equivalent to, or greater than, the internal assurance level required for the information presented in the standalone document or the discrete section.

(4) For the purpose of these Rules, a reference to a disclosure entity making a disclosure to the general public includes the entity making the disclosure—

(a) on the entity's internet website or a section of the entity's internet website; or

(b) if approved by the resolution authority, on the internet website, or a section of the internet website, of a group company of the entity.

51. Timing of disclosure

(1) For disclosures under these Rules for a quarterly reporting period that ends otherwise than at the close of an interim or annual reporting period, the disclosure entity must publish the disclosure statement—

(a) if the disclosure entity publishes quarterly financial statements for the quarterly reporting period (***quarterly financial statements***) within 8 weeks after the end of the quarterly reporting period—concurrently with the publication of the quarterly financial statements; or

(b) if the disclosure entity does not publish quarterly financial statements within 8 weeks after the end of the quarterly reporting period—within that 8-week period.

(2) For disclosures under these Rules for a quarterly or semi-annual reporting period that ends at the close of an interim reporting period, the disclosure entity must publish the disclosure statement—

(a) if the disclosure entity publishes interim financial statements for the interim reporting period (***interim financial statements***) within 3 months after the end of the quarterly or semi-annual reporting period—

(i) concurrently with the publication of the interim financial statements; or

(ii) if a permission is given under subrule (4)—within the time permitted; or

(b) if the disclosure entity does not publish the interim financial statements within 3 months after the end of the quarterly or semi-annual reporting period—within that 3-month period.

(3) For disclosures under these Rules for a quarterly or semi-annual reporting period that ends at the close of an annual reporting period, the disclosure entity must publish the disclosure statement—

(a) if the disclosure entity publishes annual financial statements for the annual reporting period (***annual financial statements***) within 4 months after the end of the quarterly or semi-annual reporting period—

(i) concurrently with the publication of the annual financial statements; or

(ii) if a permission is given under subrule (4)—within the time permitted; or

(b) if the disclosure entity does not publish annual financial statements within 4 months after the end of the quarterly or semi-annual reporting period—within that 4-month period.

(4) Subject to subrule (5), the resolution authority may, by written notice served on a disclosure entity, permit the publication of a disclosure statement under subrule (2)(a) or (3)(a) at a time later than the publication of the interim financial statements or annual financial statements but within the following period after the end of the quarterly or semi-annual reporting period to which the disclosure statement relates—

(a) if subrule (2)(a) applies—3 months;

(b) if subrule (3)(a) applies—4 months.

(5) The resolution authority may give a permission under subrule (4) if the disclosure entity demonstrates to the satisfaction of the resolution entity that—

(a) concurrent publication under subrule (2)(a) or (3)(a) is not practicable or feasible, or will result in a delay in the publication of the relevant financial statements; and

(b) the proposed difference in time between the publication of the relevant financial statements and the publication of the disclosure statement is reasonable in all the circumstances of the case.

52. Location of disclosure statements

(1) Subject to subrules (2) and (3), a disclosure entity must—

(a) keep at least one copy of each of its disclosure statements (***relevant copy***) in its principal place of business in Hong Kong; and

(b) make a relevant copy available for inspection by the general public during the business hours of the disclosure entity at its principal place of business in Hong Kong.

(2) A disclosure entity must ensure that a relevant copy of a disclosure statement is available for inspection under subsection (1)(b) for at least 12 months beginning on the date of publication of the disclosure statement.

(3) If a disclosure entity does not have a principal place of business in Hong Kong that is accessible to the general public, the disclosure entity complies with subrule (1) and (2) if—

(a) those subrules are complied with by a group company of the disclosure entity that is an authorized institution that has a principal place of business in Hong Kong accessible to the general public; and

(b) the disclosure entity discloses the location of the principal place of business referred to in paragraph (a).

53. Further requirements for disclosure statements

(1) A disclosure entity must make it clear in its disclosure statement—

(a) which information contained in the statement has been audited; and

(b) which information contained in the statement has not been audited.

(2) A disclosure entity must ensure that when its disclosure statement is published—

(a) the statement contains all the disclosures required under these Rules to be made by the disclosure entity for the reporting period to which the statement relates; and

(b) the disclosures referred to in paragraph (a) are not false or misleading in any material respect.

(3) A disclosure entity—

(a) must establish and maintain an archive of all disclosure statements; and

(b) unless otherwise approved by the resolution authority, must establish and maintain the archive—

(i) on the disclosure entity's internet website; or

(ii) if an approval is given under rule 50(4)(b), on the internet website, or section of the internet website, of the disclosure entity's relevant group company.

(4) A disclosure entity must lodge a copy of its disclosure statement with the resolution authority before it publishes the statement.

(5) The resolution authority must ensure that each copy lodged with it under subrule (4) is kept with the register maintained under section 20 of the Banking Ordinance (Cap. 155).

54. Group disclosures and internet websites

(1) A disclosure entity may treat disclosures made by a group company of the disclosure entity (***group disclosures***) as being part of the disclosures the disclosure entity is required to make under these Rules (***entity disclosures***) if the disclosure entity demonstrates to the satisfaction of the resolution authority that—

(a) the group disclosures are not materially different from the entity disclosures;

(b) if the group company making the group disclosures is established or incorporated in a non-Hong Kong jurisdiction, the group disclosures are prepared in accordance with the prevailing banking supervisory standards relating to disclosure issued by the Basel Committee and adopted by the relevant banking supervisory authority of that group company (if any);

(c) the group disclosures provide a sufficient level of detail to permit third parties to form a considered view of the relevant aspects of the disclosure entity's loss-absorbing capacity;

(d) the disclosure statement of the disclosure entity contains a statement of the location where all the group disclosures can be found;

(e) the group disclosures are set out on an internet website of the group company that is accessible by the general public; and

(f) the disclosure entity has an internet website (or a section of an internet website) that—

(i) is specifically intended to be accessible by the general public in Hong Kong; and

(ii) contains a link to the section of the internet website setting out the group disclosures as referred to in paragraph (e).

(2) If a disclosure entity that is not an authorized institution does not have its own internet website, the disclosure entity complies with a requirement under these Rules to make information available, or to establish and maintain an archive, on its internet website if—

(a) a group company of the disclosure entity has an internet website (or a section of an internet website) specifically intended to be accessible by the general public in Hong Kong and the required information is made available, or the required archive is established and maintained, on that internet website (or section of that internet website); and

(b) the disclosure entity has demonstrated to the satisfaction of the resolution authority that making the information available, or establishing and maintaining the archive, on such an internet website (or a section of such an internet website) will not materially diminish the ease of access to, or utility of, the information or archive for the general public in Hong Kong.

55. Verification

(1) The board of directors (or a committee designated by the board) and the senior management of a disclosure entity must ensure that the information which the entity is required to disclose under these Rules is, before being disclosed, scrutinized and subjected to an internal review to ensure that the information is not false or misleading in any material respect.

(2) The internal review referred to in subrule (1) must be carried out by a disclosure entity's adequately qualified personnel who are independent of the entity's staff or management responsible for preparing the information required to be disclosed.

(3) A disclosure entity must ensure that one or more members of the senior management of the entity attest in writing that the disclosures made by the entity under these Rules have been prepared in accordance with the internal review and internal control processes approved by the entity's board of directors.

(4) The internal review and internal control processes applied to the information disclosed by a disclosure entity under these Rules for a reporting period that ends at the close of an interim or annual reporting period must be no less stringent than those applied to the information provided by the entity within the management discussion and analysis part of its financial statements.

(5) This rule does not apply in relation to any information that a disclosure entity is required to disclose under rule 45(2) in respect of a non-Hong Kong resolution entity.

56. Proprietary or confidential information

(1) A disclosure entity may, with the prior consent of the resolution authority, decline to disclose proprietary or confidential information the disclosure of which would otherwise be required under these Rules (***relevant requirement***) if the entity—

(a) discloses general information relating to the subject matter of the relevant requirement in its disclosure statement (whether or not under the relevant requirement); and

(b) includes a statement in that disclosure statement stating what information it has declined to disclose.

(2) In this rule—

proprietary or confidential information ( ), in relation to a disclosure entity, means information—

(a) that, if it became publicly available, would cause serious prejudice to the competitive position of the entity; or

(b) in respect of which the entity has legally binding obligations to its customers or other counterparties that prevent the entity from disclosing the information.

57. Materiality

(1) The senior management of a disclosure entity must ensure that a disclosure made by the entity under these Rules contains all the material information.

(2) In this rule—

material information ( ) means information—

(a) that is required to be disclosed under these Rules; and

(b) that, if it were not disclosed or were misstated, could change or influence the assessment or decision of a person relying on the disclosure concerned for the purposes of making investment or other economic decisions.

Part 7

Enforcement

Division 1—Notifiable Matters

58. Requirement to notify resolution authority of failure or likely failure to comply

If an entity that is subject to a requirement under these Rules fails to comply, or becomes aware that it is likely to fail to comply, with the requirement, the entity must—

(a) as soon as practicable notify the resolution authority; and

(b) provide particulars to the resolution authority on request.

Note—

Under section 19(4) of the Ordinance, failure to comply, without reasonable excuse, with this rule is an offence.

Division 2—Remedial Action

59. Requirement to take remedial action

(1) If an entity contravenes these Rules, the resolution authority may, in accordance with rule 60, require the entity to take remedial action specified by the resolution authority, within the period specified by the resolution authority, to remedy the contravention.

(2) The resolution authority may require an entity to take remedial action under subrule (1) if the resolution authority is satisfied, on reasonable grounds, that it is prudent to require the entity to take the action.

Note—

Under section 19(5) of the Ordinance, failure to comply, without reasonable excuse, with a requirement to take remedial action is an offence.

60. Procedure for requiring entity to take remedial action

(1) If the resolution authority proposes to require an entity to take remedial action, the resolution authority must serve a written notice on the entity—

(a) specifying the details of the proposed remedial action and proposed period in which it is to be taken;

(b) specifying the grounds for the proposed requirement to take remedial action; and

(c) including a statement that the entity may, within 14 days (or a longer period allowed by the resolution authority), make written representations to the resolution authority on any matter specified in the notice.

(2) If representations are made in accordance with subrule (1)(c), the resolution authority, after considering the representations, may—

(a) serve a further written notice on the entity—

(i) confirming the proposed requirement to take remedial action or the proposed period in which it is to be taken; or

(ii) modifying the proposed requirement or proposed period to take into account any of the representations; or

(b) decide not to require the entity to take remedial action.

(3) If no representations are made in accordance with subrule (1)(c), the resolution authority may serve a further written

notice on the entity confirming the proposed requirement to take remedial action or the proposed period in which it is to be taken.

(4) The further written notice served under subrule (2)(a) or (3) has the effect of requiring the entity to take remedial action in accordance with its terms, on the date specified in the notice.

(5) A decision of the resolution authority to require an entity to take remedial action is a reviewable decision.

Part 8

Review by Resolvability Review Tribunal

61. Application for review of reviewable decision

(1) A relevant entity that is aggrieved by a reviewable decision may, at any time within the period specified in subrule (3), apply to the Resolvability Review Tribunal for a review of the decision.

(2) An application for review must set out the grounds for the application and be accompanied by a copy of the relevant notice.

(3) The period specified for the purposes of subrule (1) is the period of 30 days beginning on the date on which the relevant notice was served on the relevant entity.

(4) Despite subrule (3), the Resolvability Review Tribunal, on the written application of any person, may by order extend the time within which an application for review may be made if satisfied that there is good cause for granting the extension.

(5) The making of an application to the Resolvability Review Tribunal for review of a reviewable decision operates as a stay of execution of the decision.

(6) In this rule—

relevant entity ( )—

(a) in relation to a decision to vary a resolution entity's resolution component ratio, means the resolution entity;

(b) in relation to a decision not to vary a resolution entity's resolution component ratio following an application made under rule 19(3), means the resolution entity; or

(c) in relation to a decision to require an entity to take remedial action, means the entity;

relevant notice ( )—

(a) in relation to a decision to vary a resolution entity's resolution component ratio, means the further written notice served under rule 20(3)(a) or (5) (as the case requires);

(b) in relation to a decision not to vary a resolution entity's resolution component ratio following an application made under rule 19(3), means the further written notice served under rule 20(4)(a) or (6) (as the case requires); or

(c) in relation to a decision to require an entity to take remedial action, means the further written notice served under rule 60(2)(a) or (3) (as the case requires).

62. Determination of application for review

(1) As soon as practicable after an application under rule 61(1) is received by it, the Resolvability Review Tribunal must send a copy of the application to the resolution authority.

(2) In reviewing a reviewable decision, the Resolvability Review Tribunal must ensure that the parties to the proceeding are given a reasonable opportunity of being heard.

(3) The standard of proof required to determine any question or issue before the Resolvability Review Tribunal is the standard of proof applicable to civil proceedings in a court of law.

(4) In determining a review of a reviewable decision, the Resolvability Review Tribunal may—

(a) confirm or set aside the decision; or

(b) remit the matter in question to the resolution authority with any direction that it considers appropriate, which may include a direction to make a fresh decision in respect of any matter specified by the Tribunal.

Schedule 1

[r. 2]

Qualifying Criteria to be Met to be an External LAC Debt Instrument

1. Qualifying criteria to be met to be an external LAC debt instrument

(1) An instrument qualifies as an external LAC debt instrument of a resolution entity only if the following criteria are met—

(a) the instrument is issued and fully paid up;

(b) subject to subsection (6), if issued in Hong Kong, the instrument is issued to a professional investor;

(c) the instrument is not secured;

(d) the instrument is not subject to—

(i) any set off or netting right; or

(ii) any other arrangement that legally or economically enhances the seniority of any claim under the instrument;

(e) the instrument has a remaining contractual maturity of at least 12 months or is perpetual;

(f) subject to subsection (2), the holder of the instrument has no right to accelerate the payment or repayment of future scheduled payments (coupon or principal) except in the event of a liquidation of the entity;

(g) subject to subsection (3), the liability constituted by the instrument does not fluctuate in value by reference to the

value of, or any fluctuation in the value of, one or more than one underlying asset, index, financial instrument, rate or thing designated in the instrument and does not otherwise have derivative-linked features;

(h) the liability constituted by the instrument does not arise other than through a contract;

(i) the instrument is either—

(i) subordinated to depositors and general creditors of the entity; or

(ii) issued by a clean HK holding company;

(j) the liability constituted by the instrument is not an excluded liability within the meaning of section 58(9) of the Ordinance;

(k) subject to subsection (4), the instrument is subject to the law of Hong Kong;

(l) subject to subsection (5), the terms and conditions of the instrument contain a provision that the holder of the instrument—

(i) acknowledges that the instrument is subject to being written-off, cancelled, converted, modified, or to having its form changed, in the exercise of powers under the Ordinance;

(ii) agrees to be bound by any such write-off, cancellation, conversion, modification or form change; and

(iii) acknowledges that the rights of the holder are subject to anything done in the exercise of those powers;

(m) subject to subsection (6)—

(i) the terms and conditions of the instrument contain a provision that the instrument is intended to qualify as a LAC debt instrument under these Rules; and

(ii) any prospectus, notice, circular, advertisement or brochure prepared by or for the issuer in relation to the instrument—

(A) discloses the risks inherent in the holding of the instrument, including the risks in relation to its subordination and the circumstances in which the holder may suffer loss as a result of the holding;

(B) contains a statement that the instrument is complex and high risk; and

(C) contains a statement that, in order to qualify as a LAC debt instrument under these Rules, if issued in Hong Kong the instrument must be issued to a professional investor;

(n) subject to subsection (6), the instrument is in a denomination of no less than—

(i) if denominated in Hong Kong dollars—HK$2,000,000;

(ii) if denominated in US dollars—US$250,000;

(iii) if denominated in Euros—200,000 Euros; or

(iv) if denominated in any other currency—the equivalent in that currency to HK$2,000,000 with reference to the relevant exchange rate on the date of issue;

(o) the instrument is not funded or guaranteed (directly or indirectly) by the resolution entity or another entity that

is in the same resolution group as the resolution entity, unless the resolution authority has agreed in writing that the instrument being so funded or guaranteed is not inconsistent with the preferred resolution strategy covering the resolution entity;

(p) subject to subsection (7), if the terms and conditions of the instrument contain one or more call options—

(i) to exercise a call option, the entity must have the prior consent of the resolution authority; and

(ii) the entity has not created, and has not done anything to create, an expectation at issuance that the call option will be exercised.

(2) Subsection (1)(f) does not apply to a right of the holder to require the resolution entity to redeem the instrument that is exercisable only on one or more dates specified as a date or dates certain in the instrument, but in that case the date of the contractual maturity of the instrument for the purpose of subsection (1)(e) is the date certain or, if more than one, the earliest of those dates.

(3) Subsection (1)(g) does not apply only because a coupon on the instrument is calculated by reference to a reference rate.

(4) Subsection (1)(k) does not apply if the resolution entity has obtained independent legal advice acceptable to the resolution authority that, under the governing law of the instrument, the application of resolution powers under the Ordinance, including the application of any stabilization option, in relation to the instrument or any liability constituted by the instrument, would be effective and enforceable on the basis of binding statutory provisions or legally enforceable contractual provisions.

(5) Subsection (1)(l) does not apply to an Additional Tier 1 capital instrument or Tier 2 capital instrument issued before the day on which Part 5 of the Ordinance came into operation.

(6) Subsection (1)(b), (m) and (n) does not apply to an Additional Tier 1 capital instrument or Tier 2 capital instrument issued before the day on which these Rules come into operation and subsection 1(b), (m)(ii) and (n) does not apply to an instrument issued to and held by a group company of the issuer.

(7) Subsection (1)(p) does not apply to an Additional Tier 1 capital instrument or Tier 2 capital instrument.

———————

Schedule 2

[r. 2]

Qualifying Criteria to be Met to be an Internal LAC Debt Instrument

1. Qualifying Criteria to be met to be an internal LAC debt instrument

(1) An instrument qualifies as an internal LAC debt instrument of a material subsidiary only if the following criteria are met—

(a) the instrument is issued and fully paid up;

(b) the instrument is not secured;

(c) the instrument is not subject to—

(i) any set off or netting right; or

(ii) any other arrangement that legally or economically enhances the seniority of any claim under the instrument;

(d) the instrument has a remaining contractual maturity of at least 12 months or is perpetual;

(e) subject to subsection (2), the holder of the instrument has no right to accelerate the payment or repayment of future scheduled payments (coupon or principal) except in the event of a liquidation of the material subsidiary;

(f) subject to subsection (3), the liability constituted by the instrument does not fluctuate in value by reference to the value of, or any fluctuation in the value of, one or more than one underlying asset, index, financial instrument,

rate or thing designated in the instrument and does not otherwise have derivative-linked features;

(g) the liability constituted by the instrument does not arise other than through a contract;

(h) the instrument is either—

(i) subordinated to depositors and general creditors of the material subsidiary; or

(ii) issued by a clean HK holding company;

(i) the liability constituted by the instrument is not an excluded liability within the meaning of section 58(9) of the Ordinance;

(j) subject to subsection (4), the instrument is subject to the law of Hong Kong;

(k) subject to subsection (5), the terms and conditions of the instrument contain a provision that the holder of the instrument—

(i) acknowledges that the instrument is subject to being written-off, cancelled, converted, modified, or to having its form changed, in the exercise of powers under the Ordinance;

(ii) agrees to be bound by any such write-off, cancellation, conversion, modification or form change; and

(iii) acknowledges that the rights of the holder are subject to anything done in the exercise of those powers;

(l) subject to subsection (6), the terms and conditions of the instrument contain a provision that the instrument is intended to qualify as a LAC debt instrument under these Rules;

(m) the instrument is not funded or guaranteed directly or indirectly by the material subsidiary or any subsidiary of the material subsidiary, unless the resolution authority has agreed in writing that the instrument being so funded or guaranteed is not inconsistent with the preferred resolution strategy covering the material subsidiary;

(n) subject to subsection (7), if the terms and conditions of the instrument contain one or more call options—

(i) to exercise a call option, the material subsidiary must have the prior consent of the resolution authority; and

(ii) the material subsidiary has not created, and has not done anything to create, an expectation at issuance that the call option will be exercised;

(o) the instrument is—

(i) an Additional Tier 1 capital instrument;

(ii) a Tier 2 capital instrument; or

(iii) an instrument that complies with section 2.

(2) Subsection (1)(e) does not apply to a right of the holder to require the material subsidiary to redeem the instrument that is exercisable only on one or more dates specified as a date or dates certain in the instrument, but in that case the date of the contractual maturity of the instrument for the purpose of subsection (1)(d) is the date certain or, if more than one, the earliest of those dates.

(3) Subsection (1)(f) does not apply only because a coupon on the instrument is calculated by reference to a reference rate.

(4) Subsection (1)(j) does not apply if the material subsidiary has obtained independent legal advice acceptable to the resolution authority that, under the governing law of the instrument, the

application of resolution powers under the Ordinance, including the application of any stabilization option, in relation to the instrument or any liability constituted by the instrument, would be effective and enforceable on the basis of binding statutory provisions or legally enforceable contractual provisions.

(5) Subsection (1)(k) does not apply to an instrument issued before the day on which Part 5 of the Ordinance came into operation.

(6) Subsection (1)(l) does not apply to an instrument issued before the day on which these Rules come into operation.

(7) Subsection (1)(n) does not apply to an Additional Tier 1 capital instrument or Tier 2 capital instrument.

2. Additional requirements for internal non-capital LAC debt instruments

(1) For the purposes of section 1(1)(o)(iii), an instrument complies with this section if—

(a) the terms and conditions of the instrument—

(i) contain a provision requiring the material subsidiary to ensure that the instrument will be either written down, or converted into ordinary shares, on the occurrence of the trigger event; or

(ii) if a notice has been served on the material subsidiary under subsection (3), comply with that notice; and

(b) at all times, the material subsidiary maintains all prior authorization necessary to immediately issue the relevant number of ordinary shares specified in the terms and conditions of the instrument (if any), and there are no impediments to the write-off or automatic conversion of

the instrument into ordinary shares of the material subsidiary, on the occurrence of the trigger event;

(c) before the instrument is issued, the material subsidiary submits to the resolution authority—

(i) a detailed description of the rationale for any specified conversion method set out in the terms and conditions of the instrument, including the computations of the indicative dilution of the material subsidiary's ordinary shares that would occur on the occurrence of the trigger event and the resulting ordinary shareholder structure; and

(ii) an explanation of why such a conversion method would help to ensure or maintain the viability of the material subsidiary; and

(d) for an instrument issued directly to a group company of the material subsidiary that is established or incorporated in a non-Hong Kong jurisdiction, the terms and conditions of the instrument identify—

(i) the jurisdiction of incorporation of the group company to which it is issued; and

(ii) the non-Hong Kong resolution authority in that jurisdiction (***home authority***).

(2) For the purposes of subsection (1), the trigger event is the occurrence of—

(a) the resolution authority notifying the material subsidiary in writing that the resolution authority is satisfied that—

(i) if the material subsidiary is an authorized institution—it has ceased, or is likely to cease, to be viable and there is no reasonable prospect that private sector action (outside of resolution) would

result in it again becoming viable within a reasonable period (in both cases, without taking into account the write-down or conversion into equity of any LAC debt instruments); or

(ii) if the material subsidiary is an HK holding company or HK affiliated operational entity—the relevant authorized institution has ceased, or is likely to cease, to be viable and there is no reasonable prospect that private sector action (outside of resolution) would result in it again becoming viable within a reasonable period (in both cases, without taking into account the write-down or conversion into equity of any LAC debt instruments); and

(b) for an instrument issued directly to a group company established or incorporated in a non-Hong Kong jurisdiction, the resolution authority notifying the material subsidiary in writing that—

(i) the resolution authority has notified the home authority of the resolution authority's intention to notify the material subsidiary under paragraph (a); and

(ii) the home authority—

(A) has consented to the write-down or conversion of the internal non-capital LAC debt instruments issued by the material subsidiary; or

(B) has not, within 24 hours after receiving notice under subparagraph (i), objected to the write-down or conversion of the internal non-

capital LAC debt instruments issued by the material subsidiary.

(3) The resolution authority may serve a written notice on a material subsidiary requiring that the terms and conditions of any or all instruments that are intended to be internal LAC debt instruments must specify which one only of writing down or conversion to ordinary shares will take place on the occurrence of the trigger event.

(4) In this section—

relevant authorized institution ( ), in relation to a material subsidiary that is an HK holding company or HK affiliated operational entity, means any authorized institution incorporated in Hong Kong—

(a) of which the material subsidiary is a holding company or affiliated operational entity (as the case requires); and

(b) that is in the same resolution group as the material subsidiary.

Schedule 3

[rr. 38 & 40]

Deduction of Holdings of Own Non-capital LAC Liabilities

1. Deduction of holdings of own non-capital LAC liabilities

(1) For the purposes of rules 38(1)(a) and 40(1)(a), a resolution entity or material subsidiary must, subject to subsections (2), (3) and (4)—

(a) calculate the amount of any direct holdings, indirect holdings or synthetic holdings of its own non-capital LAC liabilities to be deducted from its external or internal loss-absorbing capacity (as the case requires) on the basis of gross long positions (irrespective of whether the positions are booked in the banking book or the trading book); and

(b) make those deductions from its external or internal loss-absorbing capacity.

(2) A resolution entity or material subsidiary must calculate the amount of holdings of its own non-capital LAC liabilities on the basis of the net long position if the long and short positions are in the same underlying exposure and the short positions involve no counterparty credit risk.

(3) A resolution entity or material subsidiary must take the amount to be deducted for indirect holdings that take the form of holdings of index securities as the amount of holdings of

index securities that corresponds to the proportion of its own non-capital LAC liabilities included in the underlying index.

(4) A resolution entity or material subsidiary must net gross long positions in its own non-capital LAC liabilities resulting from holdings of index securities against short positions in its own non-capital LAC liabilities resulting from short positions in the same underlying index, including where those short positions involve counterparty credit risk.

Schedule 4

[rr. 38 & 40]

Deduction of Holdings of Other Non-capital LAC Liabilities

1. Deduction of holdings of other non-capital LAC liabilities

(1) For the purposes of rules 38(1)(b) and 40(1)(b), a resolution entity or material subsidiary must—

(a) calculate its aggregate holdings of non-capital LAC liabilities issued by financial sector entities to be deducted from its external or internal loss-absorbing capacity (as the case requires); and

(b) make those deductions from its external or internal loss-absorbing capacity.

(2) A resolution entity's or material subsidiary's aggregate holdings of non-capital LAC liabilities issued by financial sector entities must be calculated as follows—

(a) direct holdings, indirect holdings and synthetic holdings of non-capital LAC liabilities must be included;

(b) the net long positions in both the banking book and trading book must be included and, in this regard, the gross long position may be offset against a short position in the same underlying exposure if the maturity of the short position either matches the maturity of the long position or has a residual maturity of at least one year;

(c) underwriting positions held for 5 business days or less (or the longer period approved by the resolution authority) must be excluded;

(d) the resolution entity or material subsidiary may, with the prior consent of the resolution authority, temporarily exclude holdings of certain non-capital LAC liabilities where they have been created in the context of resolving or providing financial assistance to reorganize a distressed financial sector entity.

Monetary Authority

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Explanatory Note

[To be added]