Mechanism for calculating reduction in Regulatory Reserve (RR) and adjustment
to target rate of benchmark regulatory provision

The new target rate for calculation of the benchmark regulatory provision is calculated by subtracting 50% of the RR requirement as at 31 December 2019 from the existing target rate. Please refer to the following table for a numeric illustration of the calculation:

	End-Dec 2019			
Target rate (A)	Stages 1 & 2 loan provisions under HKFRS 9 as % of total loans (B)	RR requirement as % of total loans (A)-(B)= (C)	Reduction in 50% of RR requirement (C)/2=(D)	New target rate effective immediately (A)-(D)
1.06%	0.66%	0.40%	0.20%	0.86%

Note: In case (B) > (A), the existing target rate will not be changed.

With the new effective target rate, the determination of the level of RR that a locally incorporated AI is required to maintain will continue to follow the two-step approach set out in Annex II-C of the Completion Instructions for the Return of Capital Adequacy Ratio:

- **Step 1** – calculate the benchmark regulatory provision (benchmark) as the product of (i) target rate; and (ii) total loans and advances to non-banks;

- **Step 2** – compare the benchmark with the relevant portion of HKFRS 9 provisions (i.e. provisions made for total loans and advances to non-banks categorised into Stage 1 and Stage 2 under HKFRS 9).

(i) where the benchmark is greater than the relevant portion of HKFRS 9 provisions, the "shortfall" will continue to be earmarked from retained earnings and maintained as RR;

(ii) where, on the other hand, the benchmark is equal to or smaller than relevant portion of HKFRS 9 provisions so that there is no "shortfall" or an "excess" of accounting provisions, no RR will be required.