Annex 2

Transition Disclosures Template - Explanatory Note

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

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

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

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

   Example for Modification 1

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

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

Examples for Modification 2

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

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

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

3. Given that certain capital elements under the BCR carry a more conservative definition relative to those under the Basel III framework, an AI is required to separately disclose the impact of each of these different definitions in the "Notes to the template" to facilitate comparison by market participants of its capital position with banks in other jurisdictions. In this regard, an AI should make disclosures in accordance with those notes. Where appropriate, an AI should include additional description to substantiate the difference in cases where the standard description does not adequately explain the specific circumstances of the AI.