

Annex

DRAFT

Banking (Capital) (Amendment) Rules 2015

Banking (Capital) (Amendment) Rules 2015

(Made by the Monetary Authority under section 97C of the Banking Ordinance (Cap. 155) after consultation with the Financial Secretary, the Banking Advisory Committee, the Deposit-taking Companies Advisory Committee, The Hong Kong Association of Banks and The Hong Kong Association of Restricted Licence Banks and Deposit-taking Companies)

1. Commencement

These Rules come into operation on 1 January 2016.

2. Banking (Capital) Rules amended

The Banking (Capital) Rules (Cap. 155 sub. leg. L) are amended as set out in sections 3 to 28.

3. Section 3E amended (interpretation of Part 1B)

Section 3E(1), Chinese text, definition of ~~防護緩衝資本比率~~—

Repeal

“緩衝比率”

Substitute

“緩衝水平”.

4. Section 3Q amended (applicable JCCyB ratio for Hong Kong)

Section 3Q(9), Chinese text, after “銀行業”—

Add

“可能”.

5. Section 3U amended (D-SIB)

Section 3U, Chinese text—

Repeal

“重要性的”

Substitute

“重要性”.

6. Section 17 amended (authorized institution shall only use STM approach, IMM approach or approach used by parent bank to calculate its market risk)

(1) Section 17, heading—

Repeal

“, IMM approach or approach used by parent bank”

Substitute

“or IMM approach”.

(2) Section 17(1)(a)—

Repeal

“paragraphs (b) and (c)”

Substitute

“paragraph (b)”.

(3) Section 17(1)(b)—

Repeal the semicolon

Substitute a full stop.

(4) Section 17(1)—

Repeal paragraph (c).

(5) Section 17(2)—

Repeal

“any combination of the STM approach, the IMM approach and the approach used by its parent bank”

Substitute

“a combination of the STM approach and the IMM approach”.

7. Sections 20 and 21 repealed

Sections 20 and 21—

Repeal the sections.

8. Part 2, Division 7A heading amended (attachment of conditions to approvals granted under section 6(2)(a), 8(2)(a), 10B(2)(a), 18(2)(a), 20(2)(a) or 25(2)(a))

Part 2, Division 7A, heading—

Repeal

“, 20(2)(a)”.

9. Section 33A amended (attachment of conditions to approvals granted under section 6(2)(a), 8(2)(a), 10B(2)(a), 18(2)(a), 20(2)(a) or 25(2)(a))

(1) Section 33A, heading—

Repeal

“, 20(2)(a)”.

(2) Section 33A(1)—

Repeal

“, 20(2)(a)”.

(3) Section 33A(2)—

Repeal

“, 20(2)(a)”.

10. Section 34 amended (reviewable decisions)

(1) Section 34(1)—

Repeal

“Subject to subsection (2), a”

Substitute

“A”.

(2) Section 34—

Repeal subsection (2).

11. Section 56 amended (exceptions to section 55)

Section 56—

Repeal subsection (3).

12. Section 71 amended (off-balance sheet exposures)

Section 71(2), Table 11, item 1, definition of *excluded exchange rate contract*—

Repeal paragraph (a).

13. Section 74 amended (determination of risk-weights applicable to off-balance sheet exposures)

Section 74(2)(f)—

Repeal

“as 100%”

Substitute

“by reference to the risk-weight allocated to the relevant shares or securities”.

14. Section 79 amended (collateral which may be recognized for purposes of section 77(i)(i))

Section 79(1)(m)—

Repeal

“or securities firm”.

-
- 15. Section 82 amended (determination of risk-weight to be allocated to recognized collateral under simple approach)**
- (1) Section 82(2)(e), after “business days after”—
- Add**
- “the last time when the exposure was marked-to-market before”.
- (2) Section 82(2)(g)—
- Repeal**
- everything after “documentation”
- Substitute**
- “for repo-style transactions involving securities of the same type as those that are the subject matter of the transaction; and”.
- (3) Section 82(4)—
- Repeal paragraph (c).**
- 16. Section 100 amended (capital treatment of recognized guarantees and recognized credit derivative contracts)**
- Section 100—
- Repeal subsections (6), (7) and (8).**
- 17. Section 118 amended (off-balance sheet exposures)**
- Section 118(2), Table 15, item 1, definition of *excluded exchange rate contract*—
- Repeal paragraph (a).**
- 18. Section 121 amended (determination of risk-weights applicable to off-balance sheet exposures)**
- Section 121(2)(f)—

Repeal

“as 100%”

Substitute

“by reference to the risk-weight allocated to the relevant shares or securities”.

19. Section 139 amended (interpretation of Part 6)

(1) Section 139(1)—

Add in alphabetical order

“*ADC phase* (), in relation to commercial real estate, means the land acquisition, development or construction phase of the real estate;

HVCRE exposure () means a specialized lending of an authorized institution that falls within the description in section 143(1)(e);”.

(2) Section 139(3), after “Table 18”—

Add

“or 18A, whichever is applicable”.

20. Section 142 amended (classification of exposures)

(1) Section 142(1)(b)—

Repeal

“25”

Substitute

“26”.

(2) Section 142(1), Table 16, item 1, column 3—

Add

“(da) Specialized lending (high-volatility commercial real estate)”.

21. Section 143 amended (corporate exposures)

(1) Section 143(1)—

Repeal

“For”.

Substitute

“Subject to subsection (4A), for”.

(2) Section 143(1)(d)—

Repeal the full stop

Substitute a semicolon.

(3) Section 143(1)—

Add

“(e) an authorized institution’s specialized lending falls within high-volatility commercial real estate if the lending is the financing of commercial real estate that exhibits a higher loss rate volatility than other types of specialized lending, and falls within any of the following—

(i) a commercial real estate exposure secured by any commercial real estate located in Hong Kong of a type announced by the Monetary Authority under subsection (6) as sharing a higher volatility in portfolio default rate;

(ii) a commercial real estate exposure secured by any commercial real estate located in a jurisdiction outside Hong Kong of a type announced by the relevant banking supervisory authority of the

jurisdiction as sharing a higher volatility in portfolio default rate;

- (iii) an exposure that finances the ADC phase of—
 - (A) any commercial real estate of a type referred to in subparagraph (i) or (ii); or
 - (B) any other commercial real estate where there is uncertainty of repayment and the obligor in respect of the exposure does not have substantial equity at risk.”.

- (4) Section 143(3)—

Repeal

“subsection (4)”.

Add

“subsections (4) and (4A)”.

- (5) Section 143—

Add

“(4A) For the purposes of section 142(1) as read with Table 16, an authorized institution must classify all of its exposures to corporates that fall within the description in subsection (1)(e) as exposures that fall within the IRB subclass of specialized lending (high-volatility commercial real estate), whether or not the exposures may—

- (a) also fall within the description in any other paragraph of subsection (1); or
- (b) be classified as exposures that fall within the IRB subclass of small-and-medium sized corporates under subsection (3).”.

- (6) Section 143(5)—

Add

“(ba) the IRB subclass of specialized lending (high-volatility commercial real estate) under subsection (4A);”.

(7) Section 143—

Add

“(6) The Monetary Authority may categorize any type of commercial real estate located in Hong Kong as commercial real estate of a type sharing a higher volatility in portfolio default rate, and announce the categorization by—

- (a) notifying all authorized institutions in writing; and
- (b) posting a notification on the Monetary Authority’s website.

(7) For the purposes of subsection (1)(e)(iii)(B), there is uncertainty of repayment in respect of an exposure if the source of repayment at origination of the exposure is—

- (a) the future uncertain sale of the commercial real estate concerned; or
- (b) cash flows whose source of repayment is substantially uncertain.”.

22. Section 157 amended (provisions supplementary to section 156(2) and (5)—firm-size adjustments for small-and-medium sized corporates)

Section 157—

Add

“(5) If an authorized institution has an HVCRE exposure that may be classified as a corporate exposure that falls within the IRB subclass of small-and-medium sized corporates under section 143(3) but for the operation of

section 143(4A), the institution may also make a firm-size adjustment referred to in subsection (1) in respect of the exposure, and subsections (2), (3) and (4) apply accordingly.”.

23. Section 158 amended (provisions supplementary to section 156—risk-weights for specialized lending)

(1) Section 158(1)—

Repeal

“Where”

Substitute

“Subject to subsections (1A), (1B) and (1C), where”.

(2) Section 158(1), before “or section 157A”—

Add

“, section 157(5) in respect of HVCRE exposures that fall within that section”.

(3) Section 158—

Add

“(1A) If the specialized lending is an HVCRE exposure—

- (a) the value of 0.24 in the correlation (R) or correlation (ρ_{os}) in the risk-weight function specified in Formula 16 or 17 is to be replaced by a value of 0.30;
- (b) if section 157(1) or (5) is applicable, the value of 0.24 in the correlation (R) or correlation (ρ_{os}) in section 157(1) is to be replaced by a value of 0.30; and
- (c) if section 157A is applicable, a reference to Formula 16 or 17 in that section is a reference to the Formula as adjusted under paragraph (a) or (b).

-
- (1B) An authorized institution that falls within subsection (1)(b) must not use the advanced IRB approach to derive the risk-weighted amount of any of its HVCRE exposures if both of the following circumstances occur —
- (a) the institution has material income-producing real estate exposures; and
 - (b) the institution does not also use the advanced IRB approach to derive the risk-weighted amount of all of its reference exposures.
- (1C) If an authorized institution that started to use the advanced IRB approach to derive the risk-weighted amount of its HVCRE exposures at a time when the institution did not have any material income-producing real estate exposures subsequently becomes aware that the circumstances referred to in subsection (1B)(a) and (b) occur in respect of the institution, the institution must—
- (a) cease to use the advanced IRB approach to derive the risk-weighted amount of its HVCRE exposures after the expiry of a period of 6 months after the date on which the institution becomes so aware; or
 - (b) start to use the advanced IRB approach to derive the risk-weighted amount of all of its reference exposures before the expiry of that period.”.
- (4) Section 158(2)(c), after “Table 18”—
- Add**
- “or 18A, whichever is applicable,”.
- (5) Section 158(2)(d)—
- Repeal**

“subsection (3)”

Substitute

“subsections (3) and (4)”.

- (6) Section 158(2)(d), after “Table 18”—

Add

“or 18A, whichever is applicable.”.

- (7) Section 158(2), Table 18, heading—

Repeal

“for Specialized Lending”.

Add

“**Applicable to Specialized Lending other than HVCRE Exposures**”.

- (8) Section 158(2), after Table 18—

Add

“Table 18A

**Supervisory Rating Grades for Determination of Risk-weights
Applicable to HVCRE Exposures**

	Strong	Good	Satisfactory	Weak	Default
Credit quality grade	1	2	3	4	Not applicable
Risk-weight	95%	120%	140%	250%	0%”.

- (9) Section 158(3)—

Repeal

“its specialized lending” (wherever appearing)

Substitute

“its specialized lending (other than HVCRE exposures and specified ADC exposures)”.

(10) Section 158—

Add

“(4) An authorized institution may assign a risk-weight of 70% to its HVCRE exposure that falls into the supervisory rating grade of “strong” in Table 18A, and a risk-weight of 95% to its HVCRE exposure that falls into the supervisory rating grade of “good” in Table 18A, if—

- (a) the exposure has a remaining maturity of less than 2.5 years; or
- (b) the institution demonstrates to the satisfaction of the Monetary Authority that the institution’s credit underwriting criteria and the ability of the obligor in respect of the exposure to withstand other risk characteristics are substantially stronger than the corresponding criteria for the equivalent supervisory rating grade as referred to in subsection (2)(c)(i).

(5) In this section—

reference exposure () means a specialized lending falling within the description in section 143(1)(d) that—

- (a) falls within the IRB subclass of specialized lending under supervisory slotting criteria approach (income-producing real estate) under section 143(2);
- (b) falls within the IRB subclass of small-and-medium sized corporates under section 143(3); or

- (c) falls within the IRB subclass of other corporates under section 143(5);

specified ADC exposure () means an exposure—

- (a) that is a specialized lending that finances the ADC phase of commercial real estate;
- (b) in respect of which there is no uncertainty of repayment within the meaning of section 143(7); and
- (c) that would have fallen within section 143(1)(e)(iii)(B) had there been uncertainty of repayment within the meaning of section 143(7) in respect of the exposure.
- (6) For the purposes of this section, an authorized institution has material income-producing real estate exposures if the average aggregate EAD of its reference exposures over the past 12 months exceeds 5% of the institution’s capital base as determined under Part 3.”.

24. Section 200 amended (requirements for authorized institution using top-down approach to estimate probability of default, etc. of purchased receivables for default risk or dilution risk)

- (1) Section 200(b)—

Repeal

“and”.

- (2) Section 200(c)—

Repeal the full stop

Substitute

“; and”.

- (3) Section 200—

Add

“(d) in the case of default risk, have in place policies, systems and procedures to ensure compliance with paragraphs 493 to 499 in the document entitled “International Convergence of Capital Measurement and Capital Standards—A Revised Framework (Comprehensive Version)” published by the Basel Committee in June 2006.”.

25. Section 218 amended (provisions supplementary to section 214(2)—double default framework)

Section 218(2)(c)(i), after “approach”—

Add

“or for an HVCRE exposure which falls within section 158(2)”.

26. Section 220 amended (calculation of expected losses and eligible provisions for corporate, sovereign, bank and retail exposures)

(1) Section 220(4), after “Table 22”—

Add

“or 22A, whichever is applicable,”.

(2) Section 220(4), Table 22, heading, after “**Lending**”—

Add

“**other than HVCRE Exposures**”.

(3) Section 220(4), after Table 22—

Add

“Table 22A

Risk-weights for Determination of EL Amount of HVCRE Exposures

Strong	Good	Satisfactory	Weak	Default
5%	5%	35%	100%	625%”.

27. Schedule 4D amended (requirements to be met for minority interests and capital instruments issued by consolidated bank subsidiaries and held by third parties to be included in authorized institution’s capital base)

(1) Schedule 4D, section 3(1)—

Repeal

everything after “attributable to third parties”

Substitute

“calculated under subsections (1A), (1B) and (1C).”.

(2) Schedule 4D, section 3—

Add

“(1A) Where the subsidiary is incorporated in Hong Kong, the surplus CET1 capital of the subsidiary is calculated as the CET1 capital of the subsidiary less the lower of—

(a) the sum of the risk-weighted amount for credit risk, risk-weighted amount for market risk and risk-weighted amount for operational risk of the subsidiary, calculated on a solo basis or a solo-consolidated basis, as the case may be, multiplied by a percentage equal to the sum of—

(i) subject to subsection (2), the minimum CET1 capital ratio that the subsidiary must comply with, on a solo basis or a solo-consolidated basis, as the case may be, under sections 3A and 3B of these Rules and, if applicable, as varied by the Monetary Authority under

section 97F of the Ordinance (specified minimum ratio); and

- (ii) 2.5%; or
- (b) the portion of the sum of the risk-weighted amount for credit risk, risk-weighted amount for market risk and risk-weighted amount for operational risk of the authorized institution calculated on a consolidated basis, that relates to the subsidiary, multiplied by a percentage equal to the sum of—
 - (i) subject to subsection (2), the minimum CET1 capital ratio that the authorized institution must comply with, on a consolidated basis, under sections 3A and 3B of these Rules and, if applicable, as varied by the Monetary Authority under section 97F of the Ordinance (specified minimum ratio); and
 - (ii) 2.5%.
- (1B) Where the subsidiary is not incorporated in Hong Kong, the surplus CET1 capital of the subsidiary is calculated as the CET1 capital of the subsidiary less the portion of the sum of the risk-weighted amount for credit risk, risk-weighted amount for market risk and risk-weighted amount for operational risk of the authorized institution calculated on a consolidated basis, that relates to the subsidiary, multiplied by a percentage equal to the sum of—
 - (a) subject to subsection (2), the minimum CET1 capital ratio that the institution must comply with, on a consolidated basis, under sections 3A and 3B of these Rules and, if applicable, as varied by the Monetary Authority under section 97F of the Ordinance (specified minimum ratio); and

(b) 2.5%.

(1C) The amount of the surplus CET1 capital of the subsidiary that is attributable to third parties is calculated by multiplying the surplus CET1 capital of the subsidiary by the percentage of the CET1 capital instruments in the subsidiary that are held by third parties.”.

(3) Schedule 4D, section 3(2)—

Repeal

“subsection (1)(a)(i)(A) and (ii)(A)”

Substitute

“subsections (1A)(a)(i) and (b)(i) and (1B)(a)”.

(4) Schedule 4D, section 3(3)(b)—

Repeal

“subsection (1)(a)(i)(A) and (ii)(A)”

Substitute

“subsections (1A)(a)(i) and (b)(i) and (1B)(a)”.

(5) Schedule 4D, section 3(4)(b)—

Repeal

“subsection (1)(a)(i)(A) and (ii)(A)”

Substitute

“subsections (1A)(a)(i) and (b)(i) and (1B)(a)”.

(6) Schedule 4D, section 4(1)—

Repeal

everything after “attributable to third parties”

Substitute

“calculated under subsections (1A), (1B) and (1C).”.

(7) Schedule 4D, section 4—

Add

- “(1A) Where the subsidiary is incorporated in Hong Kong, the surplus Tier 1 capital of the subsidiary is calculated as the Tier 1 capital of the subsidiary less the lower of—
- (a) the sum of the risk-weighted amount for credit risk, risk-weighted amount for market risk and risk-weighted amount for operational risk of the subsidiary, calculated on a solo basis or a solo-consolidated basis, as the case may be, multiplied by a percentage equal to the sum of—
 - (i) subject to subsection (3), the minimum Tier 1 capital ratio that the subsidiary must comply with, on a solo basis or a solo-consolidated basis, as the case may be, under sections 3A and 3B of these Rules and, if applicable, as varied by the Monetary Authority under section 97F of the Ordinance (specified minimum ratio); and
 - (ii) 2.5%; or
 - (b) the portion of the sum of the risk-weighted amount for credit risk, risk-weighted amount for market risk and risk-weighted amount for operational risk of the authorized institution calculated on a consolidated basis, that relates to the subsidiary, multiplied by a percentage equal to the sum of—
 - (i) subject to subsection (3), the minimum Tier 1 capital ratio that the institution must comply with, on a consolidated basis, under sections 3A and 3B of these Rules and, if applicable, as varied by the Monetary Authority under

section 97F of the Ordinance (specified minimum ratio); and

(ii) 2.5%.

(1B) Where the subsidiary is not incorporated in Hong Kong, the surplus Tier 1 capital of the subsidiary is calculated as the Tier 1 capital of the subsidiary less the portion of the sum of the risk-weighted amount for credit risk, risk-weighted amount for market risk and risk-weighted amount for operational risk of the authorized institution calculated on a consolidated basis, that relates to the subsidiary, multiplied by a percentage equal to the sum of—

(a) subject to subsection (3), the minimum Tier 1 capital ratio that the institution must comply with, on a consolidated basis, under sections 3A and 3B of these Rules and, if applicable, as varied by the Monetary Authority under section 97F of the Ordinance (specified minimum ratio); and

(b) 2.5%.

(1C) The amount of the surplus Tier 1 capital of the subsidiary that is attributable to third parties is calculated by multiplying the surplus Tier 1 capital of the subsidiary by the percentage of the sum of the Tier 1 capital instruments in the subsidiary that are held by third parties.”.

(8) Schedule 4D, section 4(3)—

Repeal

“subsection (1)(a)(i)(A) and (ii)(A)”

Substitute

“subsections (1A)(a)(i) and (b)(i) and (1B)(a)”.

-
- (9) Schedule 4D, section 4(4)(b)—
- Repeal**
“subsection (1)(a)(i)(A) and (ii)(A)”
- Substitute**
“subsections (1A)(a)(i) and (b)(i) and (1B)(a)”.
- (10) Schedule 4D, section 4(5)(b)—
- Repeal**
“subsection (1)(a)(i)(A) and (ii)(A)”
- Substitute**
“subsections (1A)(a)(i) and (b)(i) and (1B)(a)”.
- (11) Schedule 4D, section 5(1)—
- Repeal**
everything after “attributable to third parties”
- Substitute**
“calculated under subsections (1A), (1B) and (1C)”.
- (12) Schedule 4D, section 5—
- Add**
- “(1A) Where the subsidiary is incorporated in Hong Kong, the surplus Total capital of the subsidiary is calculated as the Total capital of the subsidiary less the lower of—
- (a) the sum of the risk-weighted amount for credit risk, risk-weighted amount for market risk and risk-weighted amount for operational risk of the subsidiary, calculated on a solo basis or a solo-consolidated basis, as the case may be, multiplied by a percentage equal to the sum of—
- (i) subject to subsection (3), the minimum Total capital ratio that the subsidiary must comply

with, on a solo basis or a solo-consolidated basis, as the case may be, under sections 3A and 3B of these Rules and, if applicable, as varied by the Monetary Authority under section 97F of the Ordinance (specified minimum ratio); and

(ii) 2.5%; or

(b) the portion of the sum of the risk-weighted amount for credit risk, risk-weighted amount for market risk and risk-weighted amount for operational risk of the authorized institution calculated on a consolidated basis, that relates to the subsidiary, multiplied by a percentage equal to the sum of—

(i) subject to subsection (3), the minimum Total capital ratio that the institution must comply with, on a consolidated basis, under sections 3A and 3B of these Rules and, if applicable, as varied by the Monetary Authority under section 97F of the Ordinance (specified minimum ratio); and

(ii) 2.5%.

(1B) Where the subsidiary is not incorporated in Hong Kong, the surplus Total capital of the subsidiary is calculated as the Total capital of the subsidiary less the portion of the sum of the risk-weighted amount for credit risk, risk-weighted amount for market risk and risk-weighted amount for operational risk of the authorized institution calculated on a consolidated basis, that relates to the subsidiary, multiplied by a percentage equal to the sum of—

(a) subject to subsection (3), the minimum Total capital ratio that the institution must comply with,

on a consolidated basis, under sections 3A and 3B of these Rules and, if applicable, as varied by the Monetary Authority under section 97F of the Ordinance (specified minimum ratio); and

(b) 2.5%.

(1C) The amount of the surplus Total capital of the subsidiary that is attributable to third parties is calculated by multiplying the surplus Total capital of the subsidiary by the percentage of the sum of the Tier 1 capital instruments and Tier 2 capital instruments in the subsidiary that are held by third parties.”.

(13) Schedule 4D, section 5(3)—

Repeal

“subsection (1)(a)(i)(A) and (ii)(A)”

Substitute

“subsections (1A)(a)(i) and (b)(i) and (1B)(a)”.

(14) Schedule 4D, section 5(4)(b)—

Repeal

“subsection (1)(a)(i)(A) and (ii)(A)”

Substitute

“subsections (1A)(a)(i) and (b)(i) and (1B)(a)”.

(15) Schedule 4D, section 5(5)(b)—

Repeal

“subsection (1)(a)(i)(A) and (ii)(A)”

Substitute

“subsections (1A)(a)(i) and (b)(i) and (1B)(a)”.

28. Schedule 7 amended (standard supervisory haircuts for comprehensive approach to treatment of recognized collateral)

- (1) Schedule 7, section 1, Table, Part 1, item 5, columns 6 and 7—

Repeal

“not applicable”

Substitute

“25%”.

- (2) Schedule 7, section 1, Table, Part 1, item 7, column 2—

Repeal

“or securities firms”.

Monetary Authority

2015

Explanatory Note

These Rules are made by the Monetary Authority under section 97C of the Banking Ordinance (Cap. 155) to amend the Banking (Capital) Rules (Cap. 155 sub. Leg. L) (*principal Rules*).

2. The main purpose of the Rules is to amend the principal Rules to bring certain aspects of the principal Rules in conformity with the relevant standards issued by the Basel Committee on Banking Supervision in view of the assessment conducted by the Basel Committee in 2014/2015 on the extent of compliance of Hong Kong's capital standards with the Basel Committee's standards.
3. The Rules come into operation on 1 January 2016.