Banking (Capital) Rules

(Cap. 155 sub. leg. L)

Contents

Division 5A—Prescribed Approaches to Calculation of CVA Risk Capital Charge

Section		Page
	Division 2—IMM(CCR) Approach	

Division 8—Risk-weighting Requirements under SEC-ERBA

Banking (Capital) Rules

(Cap. 155, section 97C)

(Enacting provision omitted—E.R. 1 of 2012)

[1 January 2007] *L.N.232 of 2006*

(Format changes—E.R. 1 of 2012)

Part 1

Preliminary

1. *(Omitted as spent—E.R. 1 of 2012)*

2. Interpretation

(1) In these Rules— *(L.N. 167 of 2023)*

ABCP programme (ABCP計劃) has the meaning given by section 227(1); *(L.N. 222 of 2018)*

Additional Tier 1 capital (額外一級資本), in relation to an authorized institution, is to be construed in accordance with section 39; *(L.N. 156 of 2012)*

Additional Tier 1 capital instrument (額外一級資本票據) means any capital instrument that meets the qualifying criteria set out in Schedule 4B; *(L.N. 156 of 2012)*

affiliate (附屬成員) has the meaning given by section 35; *(L.N. 156 of 2012)*

approved internal assessment process (經批准內部評估程序), in relation to an authorized institution that has an IAA approval, means the institution's internal assessment process that is the subject of the IAA approval; *(L.N. 222 of 2018)*

approved trading desk (經批准交易桌), in relation to the IMA, means a trading desk referred to in section 322A(2)(b); *(L.N. 167 of 2023)*

asset sale with recourse (有追索權的資產出售), in relation to an authorized institution, means an off-balance sheet exposure to the credit risk of an asset sold under an asset sale transaction where the credit risk of the asset sold remains with the institution because the purchaser of the asset is entitled to sell the asset back to the institution within a specified period, or under specified circumstances, under the terms of the transaction; *(L.N. 175 of 2017)*

attachment point (起賠點), in relation to a tranche of a securitization transaction, means the threshold at which losses in the underlying exposures (within the meaning of section 227(1)) of the transaction would first be allocated to the tranche; *(L.N. 175 of 2017)*

back-testing (回溯測試), in relation to the use of an internal model by an authorized institution—

(a) where the internal model is used to calculate counterparty credit risk, means a process whereby the realized values of risk measures and the hypothetical changes based on static positions are compared with the values of the risk measures forecast by the model; or

(b) in any other case, means a process whereby the daily changes in the value of a portfolio of exposures of the institution are compared with the daily VaR generated from the institution's internal model applicable to that portfolio; *(L.N. 156 of 2012)*

bank (銀行) means—

(a) an authorized institution except an authorized institution the authorization of which is for the time being suspended under section 24 or 25 of the Ordinance; or

(b) subject to subsection (7), a financial institution (other than an authorized institution) incorporated outside Hong Kong—

(i) that is licensed or authorized to take deposits from the public of the jurisdiction in which it is incorporated or it has an establishment; and

(ii) that is either—

(A) an internationally active financial institution subject to appropriate prudential standards (including regulatory capital and liquidity requirements) and level of supervision in accordance with the Basel Framework; or

(B) a financial institution (other than an internationally active financial institution) subject to appropriate prudential standards determined by the banking supervisory authority of the jurisdiction in which it is incorporated that include at least a minimum regulatory capital requirement; *(L.N. 167 of 2023)*

bank subsidiary (銀行附屬公司) has the meaning given by section 35; *(L.N. 156 of 2012)*

banking book (銀行帳), in relation to an authorized institution, means the book consisting of—

(a) the institution's exposures in each of the instruments assigned to that book under section 281A(1) or 281B(4) or (8); and

(b) all of the institution's other on-balance sheet exposures and off-balance sheet exposures that are not assigned to the institution's trading book; *(L.N. 167 of 2023)*

Basel Framework (巴塞爾框架) means—

(a) the current Basel Framework; or

(b) other standards (including FAQs) for the regulation and supervision of banks published by the Basel Committee in or after 2006 that have been superseded by the current Basel Framework; *(L.N. 167 of 2024)*

basic approach (基本計算法) means the method of calculating an authorized institution's credit risk for non-securitization exposures set out in Part 5;

bond (債券) means an interest-bearing or zero-coupon debt security—

(a) which is an acknowledgment of a debt promising payment of a specified sum to the holder of the debt security; and

(b) which describes a time to maturity which is, or will become, definite;

BSC approach (BSC 計算法) means the basic approach;

business day (營業日), in relation to a country, means any day other than—

(a) a public holiday in that country; or

(b) a day on which the financial markets are not generally open for business in that country;

calendar quarter (季度) means a period of 3 consecutive calendar months ending on a calendar quarter end date;

calendar quarter end date (季度終結日) means the last day of March, June, September or December;

capital adequacy ratio (資本充足比率) has the meaning given by section 3; *(L.N. 156 of 2012)*

capital base (資本基礎)—see section 36; *(6 of 2018 s. 28)*

capital charge (資本要求), in relation to an authorized institution, means an amount of regulatory capital which the institution is required to hold for an exposure to a relevant risk which, if multiplied by 12.5, becomes the risk-weighted amount of that exposure for that risk;

CCF means a credit conversion factor;

CCP means a central counterparty; *(L.N. 156 of 2012)*

CCP-related transaction (CCP關聯交易)—see section 2AA; *(L.N. 44 of 2020)*

central counterparty (中央交易對手方), in relation to contracts traded in one or more than one financial market, means an entity which, for the purposes of clearing and settling trades in the contracts, interposes itself between the counterparties to the contracts by becoming the buyer to every seller and the seller to every buyer under the contracts; *(L.N. 156 of 2012)*

CET1 capital (CET1資本) means Common Equity Tier 1 capital; *(L.N. 156 of 2012)*

CET1 capital instrument (CET1資本票據)—

(a) in relation to a joint-stock company, means an ordinary share (including a voting ordinary share and an ordinary share ranking pari passu with a voting ordinary share in all respects except the absence of voting rights) that meets the qualifying criteria set out in Schedule 4A; or

(b) in relation to any entity other than a joint-stock company, means any capital instrument that is equivalent to an ordinary share in terms of loss absorption and meets the qualifying criteria set out in Schedule 4A; *(L.N. 156 of 2012)*

CET1 capital ratio (CET1資本比率) means Common Equity Tier 1 capital ratio; *(L.N. 156 of 2012)*

CIS exposure (CIS風險承擔) means an on-balance sheet exposure, or an off-balance sheet exposure, that is in the form of an equity investment in a collective investment scheme, or that has the same credit risk as an equity investment in the scheme, including such an exposure arising from—

(a) the holding of units or shares in the scheme; or

(b) a commitment to subscribe to the scheme's future capital calls; *(L.N. 54 of 2022)*

clean-up call (結清權) has the meaning assigned to it by section 227(1);

clearing client (結算客户)—see section 2AA; *(L.N. 44 of 2020)*

clearing intermediary (結算中介人)—see section 2AA; *(L.N. 44 of 2020)*

clearing member (結算成員), in relation to a CCP—

(a) means a member of, or a direct participant in, the CCP that is entitled to enter into a transaction with the CCP; or

(b) if—

(i) the CCP has a link to another CCP; and

(ii) a member of, or a direct participant in, that other CCP that is entitled to enter into a transaction with that other CCP is able to clear transactions through the CCP via the link,

means that other CCP; *(L.N. 156 of 2012)*

client within a multi-level client structure (多層客户結構內的客户)—see section 2AA; *(L.N. 44 of 2020)*

clients at levels higher than the institution (階級高於該機構的客户)—see section 2AA; *(L.N. 44 of 2020)*

collective investment scheme (集體投資計劃)—

(a) subject to paragraph (b), has the meaning assigned to it by Part 1 of Schedule 1 to the Securities and Futures Ordinance (Cap. 571);

(b) does not include a restricted collective investment scheme;

collective provisions (集體準備金), in relation to the exposures of an authorized institution, means provisions that—

(a) are held against future and presently unidentified losses; and

(b) are freely available to meet those losses when they materialize in future; *(L.N. 175 of 2017)*

commercial entity (商業實體) has the meaning given by section 35; *(L.N. 156 of 2012)*

commodity (商品)—

(a) in relation to the calculation of counterparty credit risk, means any of the following—

(i) any metal (including gold), energy, agricultural product or any other physical product;

(ii) any freight rate, climatic variable or other economic statistic (other than any measure of inflation); *(L.N. 167 of 2023)*

(b) in relation to the calculation of market risk capital charge and CVA risk capital charge, means—

(i) except in relation to the SSTM approach—any energy, freight, precious metal (including gold), non-precious metal, gaseous combustible, agricultural product or other physical product; or

(ii) in relation to the SSTM approach—any energy, freight, precious metal (other than gold), non-precious metal, gaseous combustible, agricultural product or other physical product; and *(L.N. 44 of 2020; L.N. 167 of 2023)*

(c) in relation to the calculation of credit risk (other than counterparty credit risk)—means any item falling within paragraph (a)(i) that is traded on an exchange; *(L.N. 167 of 2023)*

commodity-related derivative contract (商品關聯衍生工具合約), in relation to the calculation of market risk capital charge, has the meaning assigned to it by section 281; *(L.N. 167 of 2023)*

Common Equity Tier 1 capital (普通股權一級資本), in relation to an authorized institution, is to be construed in accordance with section 38; *(L.N. 156 of 2012)*

Common Equity Tier 1 capital ratio (普通股權一級資本比率), in relation to an authorized institution, means, subject to sections 29, 30 and 31, the ratio, expressed as a percentage, of the amount of the institution's CET1 capital to the sum of the institution's risk-weighted amount for credit risk, risk-weighted amount for market risk, risk-weighted amount for CVA risk, risk-weighted amount for operational risk and risk-weighted amount for sovereign concentration risk, as determined in accordance with these Rules; *(L.N. 156 of 2012; L.N. 222 of 2018; L.N. 167 of 2023)*

comprehensive approach (全面方法) has the meaning assigned to it by section 51(1); *(L.N. 137 of 2011)*

consolidated basis (綜合基礎) has the meaning assigned to it by section 4;

consolidation group (綜合集團) has the meaning assigned to it by section 4;

correlation trading portfolio (相關交易組合) has the meaning given by section 281; *(L.N. 137 of 2011)*

counter-guarantee (反擔保), in relation to an authorized institution, means a guarantee (or other undertaking) given by one party for the payment of money by a guarantor upon the guarantor being required to make payment under the terms of a guarantee given by the guarantor to the institution in relation to the exposure of the institution to a third party;

counterparty credit risk (對手方信用風險), in relation to a derivative contract or SFT entered into by an authorized institution with a counterparty, means the risk that the counterparty could default before the final settlement of the cash flows of the contract or transaction; *(L.N. 167 of 2023)*

country (國家) includes—

(a) subject to paragraph (b), any part of a country; and

(b) any jurisdiction except a restricted jurisdiction;

covered bond (資產覆蓋債券), in relation to the calculation of the risk-weighted amount for credit risk, means a bond issued by a bank or mortgage institution—

(a) that is subject to relevant laws or regulations specially designed to protect the holders of the bond; and

(b) the proceeds from the issue of which must, in conformity with those relevant laws or regulations, be invested in assets that—

(i) during the whole period of the validity of the bond, are capable of covering claims attached to the bond; and

(ii) in the event of the failure of the issuer of the bond, would be used on a priority basis for the reimbursement of the principal and payment of the accrued interest; *(L.N. 167 of 2024)*

credit conversion factor (信貸換算因數)—

(a) in relation to the determination of the credit equivalent amount (within the meaning of section 51(1), 105 or 139(1) as the case requires) of an off-balance sheet exposure of an authorized institution that is not a default risk exposure—means a percentage by which the principal amount (within the meaning of section 51(1), 105 or 139(1) as the case requires) of the exposure is multiplied as a part of the process for determining the credit equivalent amount of the exposure; or

(b) in relation to the determination of the amount of default risk exposure in respect of a derivative contract by using the current exposure method—means a percentage by which the notional amount of the derivative contract is multiplied as a part of the process for determining the amount of the exposure; *(L.N. 44 of 2020)*

credit default swap (信用違責掉期) means a credit derivative contract under which the protection buyer pays a fee to the protection seller in return for a payment by the protection seller in the event of a default (or similar credit event) by a reference entity;

credit derivative contract (信用衍生工具合約) means—

(a) a futures contract, forward contract, swap contract, option contract or similar derivative contract entered into by 2 parties with the intention to transfer credit risk in relation to a reference obligation from one party (***protection buyer***) to the other party (***protection seller***); *(L.N. 175 of 2017)*

(b) a long settlement transaction that falls within paragraph (a); or

(c) a long settlement transaction of which the counterparty credit risk profile and risk drivers are similar to those specific to a contract that falls within paragraph (a); *(L.N. 156 of 2012)*

credit enhancement (信用提升) has the meaning assigned to it by section 227(1);

credit-enhancing interest-only strip (提升信用的純利息份額) means an on-balance sheet asset of the originator of a securitization transaction that—

(a) represents a valuation of cash flows related to future margin income (being the gross finance charges and other income expected to be received by the SPE in the transaction in excess of the expenses, including interest payments, charge-offs, fees, and other expenses arising from the SPE, that are expected to be incurred under the transaction); and

(b) is subordinated to claims from other parties to the transaction in terms of the priority of payment or repayment; *(L.N. 175 of 2017)*

credit event (信用事件), in relation to a credit derivative contract, means an event specified in the contract which, if it occurs, obliges the protection seller to make a payment to the protection buyer;

credit-linked note (信用掛鈎票據) means a form of structured note with an embedded credit default swap which allows the issuer of the note (***protection buyer***) to transfer credit risk to the buyer of the note (***protection seller***);

credit protection (信用保障)—

(a) in relation to an exposure of an authorized institution, means the protection against the exposure afforded to the institution by—

(i) if the exposure is a non-securitization exposure—recognized credit risk mitigation; or

(ii) if the exposure is a securitization exposure—Part 7 credit risk mitigation (within the meaning of section 227(1)); or

(b) in any other case—means the protection provided by a party against a credit exposure incurred by another party; *(L.N. 175 of 2017)*

credit protection provider (信用保障提供者)—

(a) in relation to a guarantee which constitutes credit protection, means the guarantor under the guarantee; or

(b) in relation to a credit derivative contract which constitutes credit protection, means the protection seller under the contract;

credit quality grade (信用質素等級) means a grade represented by a numeral to which an ECAI rating is mapped in accordance with an LT ECAI rating mapping table or an ST ECAI rating mapping table; *(L.N. 167 of 2023)*

credit-related derivative contract (信用關聯衍生工具合約) means—

(a) a credit derivative contract; or

(b) a derivative contract (other than a credit derivative contract) where—

(i) the value of the contract is primarily driven by the credit risk of, or any change in the credit risk of, one or more than one underlying asset or financial instrument designated in the contract; and

(ii) the credit risk or the change may be measured in terms of one or more than one index or indicator of credit risk; *(L.N. 44 of 2020)*

credit risk (信用風險), in relation to an authorized institution, means the risk of loss arising from the change in the value of an on-balance sheet or off-balance sheet exposure of the institution due to—

(a) the change in the credit quality of the exposure concerned; or

(b) the failure of an obligor to meet the obligor's credit obligations to the institution or to the obligor's other creditors; *(L.N. 156 of 2012)*

credit risk components (信用風險組成部分) has the meaning assigned to it by section 139(1);

credit valuation adjustment (信用估值調整), in relation to the calculation by an authorized institution of CVA risk in respect of a counterparty, means an adjustment made by the institution to the default risk-free prices of OTC derivative transactions and SFTs to reflect the potential default of that counterparty; *(L.N. 167 of 2023)*

credit valuation adjustment risk capital charge (信用估值調整風險資本要求), in relation to the calculation by an authorized institution of CVA risk, means the amount of regulatory capital that the institution is required to hold for the CVA risk; *(L.N. 167 of 2023)*

CTP has the meaning given by section 281; *(L.N. 167 of 2023)*

currency mismatch (貨幣錯配), in relation to an exposure of an authorized institution—

(a) subject to paragraph (b), means that the exposure and the credit protection afforded to the exposure are denominated in different currencies;

(b) does not include a case in which the institution has, in respect of the exposure, entered into a hedging agreement and, under that agreement, the risk of foreign exchange loss to the institution arising from the fact that the exposure and the credit protection afforded to the exposure are denominated in different currencies is eliminated;

current Basel Framework (現行巴塞爾框架) means the consolidated Basel Framework launched by the Basel Committee in December 2019 comprising standards and the associated FAQs, as amended or supplemented from time to time, that are currently in force according to the Basel Committee's implementation timeline; *(L.N. 167 of 2023)*

current exposure (現行風險承擔), in relation to a derivative contract of an entity (***existing contract***), means the replacement cost that—

(a) would be incurred by the entity if it were required to enter into another derivative contract to replace the existing contract with another counterparty with substantially the same economic consequences for the entity; and

(b) is calculated by marking-to-market the existing contract, and—

(i) if the resultant value is positive for the entity—taking the resultant value of the contract; or

(ii) if the resultant value is zero or negative for the entity—taking the value of zero; *(L.N. 44 of 2020)*

current exposure method (現行風險承擔方法) means the method of calculating default risk exposures in respect of derivative contracts set out in Division 2A of Part 6A; *(L.N. 44 of 2020)*

CVA means a credit valuation adjustment; *(L.N. 156 of 2012)*

CVA loss (CVA損失), in relation to the calculation by an authorized institution of the outstanding default risk exposure to a counterparty, means the CVA (or a portion of the CVA) for the counterparty that has been recognized by the institution as an incurred write-down, where the amount of the incurred write-down is calculated—

(a) without taking into account any amount of debit valuation adjustments made for the netting sets with the counterparty that have been deducted from the CET1 capital of the institution under section 43(1)(h); and

(b) net of any amount of debit valuation adjustments made for the netting sets with the counterparty that have not been deducted from the CET1 capital of the institution under section 43(1)(h); *(L.N. 156 of 2012)*

CVA risk (CVA風險) means the risk of mark-to-market losses arising from changes in CVA values in response to changes in credit spreads of counterparties and market risk factors that drive the price of OTC derivative transactions and SFTs; *(L.N. 167 of 2023)*

CVA risk capital charge (CVA風險資本要求) means a credit valuation adjustment risk capital charge; *(L.N. 167 of 2023)*

debit valuation adjustment (債務估值調整), in relation to a netting set held by an authorized institution, means an adjustment to the valuation of the netting set to reflect the market value of the credit risk of the institution; *(L.N. 156 of 2012)*

debt-related derivative contract (債務關聯衍生工具合約) has the meaning assigned to it by section 281;

deductible holding (可扣減持有), in relation to an authorized institution, means—

(a) a direct holding, an indirect holding or a synthetic holding by the institution of a Type A deductible item;

(b) a potential future holding by the institution of a Type A deductible item that the institution could be contractually obliged to purchase;

(c) an indirect holding or a synthetic holding by the institution of a Type B deductible item; or

(d) a potential future holding by the institution of a Type B deductible item that the institution could be contractually obliged to purchase; *(L.N. 54 of 2022)*

default fund contribution (違責基金承擔), in relation to a clearing member of a CCP, means—

(a) the funded or unfunded contribution made by the clearing member to the CCP's mutualized loss-sharing arrangements; or

(b) the clearing member's underwriting of the CCP's mutualized loss-sharing arrangements; *(L.N. 156 of 2012)*

default risk exposure (違責風險的風險承擔), in relation to derivative contracts or SFTs entered into with a counterparty (***relevant trades***), means an exposure to the counterparty credit risk of the counterparty in respect of the relevant trades the amount of which is calculated by using— *(L.N. 167 of 2023)*

(a) the SA-CCR approach;

(b) the IMM(CCR) approach;

(c) the current exposure method; or

(d) any of the methods set out in Division 2B of Part 6A; *(L.N. 44 of 2020)*

delivery-versus-payment basis (貨銀對付形式)—

(a) in relation to a transaction that is not a foreign exchange transaction, means that the delivery of a thing under the transaction and the payment for the thing occur simultaneously; or

(b) in relation to a foreign exchange transaction, means that the transfer of all the currencies under the transaction occur simultaneously; *(L.N. 137 of 2011)*

derivative contract (衍生工具合約)—

(a) means a financial instrument (other than a bond, loan, share, note or structured financial instrument) the value of which is determined 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 as designated in the financial instrument;

(b) where a financial instrument which falls within paragraph (a) is embedded in or combined with, or forms part of, a bond, loan, share, note or structured financial instrument, means only the financial instrument which falls within paragraph (a);

(c) means a long settlement transaction that falls within paragraph (a); or *(L.N. 156 of 2012)*

(d) means a long settlement transaction of which the counterparty credit risk profile and risk drivers are similar to those specific to a contract that falls within paragraph (a); *(L.N. 156 of 2012)*

detachment point (止賠點), in relation to a tranche of a securitization transaction, means the threshold at which losses in the underlying exposures (within the meaning of section 227(1)) of the transaction would result in the total loss of principal for the tranche; *(L.N. 175 of 2017)*

dilution risk (攤薄風險) has the meaning assigned to it by section 139(1);

direct client (直接客户)—see section 2AA; *(L.N. 44 of 2020)*

direct credit substitute (直接信貸替代項目), in relation to an authorized institution, means an off-balance sheet exposure of the institution arising from an irrevocable transaction or instrument that carries the same credit risk to the institution as a direct extension of credit by the institution, including such an exposure arising from—

(a) a guarantee given by the institution;

(b) a standby letter of credit serving as a financial guarantee for a loan;

(c) an acceptance; or

(d) a credit protection sold under a credit derivative contract in the form of a total return swap or credit default swap booked in the institution's banking book; *(L.N. 175 of 2017)*

domestic currency exposure (本地貨幣風險承擔) means an exposure of an authorized institution which is—

(a) denominated in the local currency of the obligor in respect of the exposure; and

(b) funded by liabilities entered into by the institution in that currency;

domestic public sector entity (本地公營單位) means an entity specified in Part 1 of Schedule 1;

EAD has the meaning assigned to it by section 139(1);

early amortization provision (提早攤銷規定) has the meaning assigned to it by section 227(1);

ECAI means an external credit assessment institution;

ECAI issue specific rating (ECAI特定債項評級)—

(a) in relation to an exposure, subject to paragraphs (b) and (c), means a short-term credit assessment rating or long-term credit assessment rating that is assigned to the exposure by a Type A ECAI or a Type B ECAI;

(b) in relation to an exposure that is a securitization exposure, has the meaning given by section 227A; and

(c) in relation to an exposure in section 287, has the meaning given by section 287(11); *(L.N. 167 of 2023)*

ECAI issuer rating (ECAI發債人評級), in relation to any person (however described)—

(a) except in section 287, means a long-term credit assessment rating that is assigned to the person by a Type A ECAI or a Type B ECAI; and

(b) in section 287, has the meaning given by section 287(11); *(L.N. 167 of 2023)*

ECAI rating (ECAI 評級) means—

(a) an ECAI issuer rating; or

(b) an ECAI issue specific rating;

EE means expected exposure; *(L.N. 156 of 2012)*

effective EPE (有效 EPE) means effective expected positive exposure; *(L.N. 156 of 2012)*

effective expected positive exposure (有效預期正風險承擔), in relation to a netting set, means the amount calculated in accordance with section 226F; *(L.N. 156 of 2012; L.N. 44 of 2020)*

EL amount (EL額) has the meaning assigned to it by section 139(1);

eligible ABCP exposure (合資格ABCP風險承擔)—see section 15B; *(L.N. 222 of 2018)*

eligible covered bond (合資格資產覆蓋債券), in relation to the STC approach and the BSC approach, means a covered bond that meets all the conditions specified by the Monetary Authority under section 59D(4); *(L.N. 167 of 2023)*

eligible CVA hedge (合資格CVA對沖) means a hedge that falls within section 322U(1); *(L.N. 167 of 2023)*

end client (最終客户)—see section 2AA; *(L.N. 44 of 2020)*

equity-related derivative contract (股權關聯衍生工具合約) has the meaning assigned to it by section 281;

exception (例外情況), in relation to back-testing by an authorized institution, means an instance in which the daily losses in the value of a portfolio of exposures of the institution are above the daily VaR generated from the institution's internal model applicable to that portfolio;

exchange controls (外匯管制) means controls or restrictions imposed by the government of a country on the exchange of the currency of that country for the currency of another country;

exchange rate contract (匯率合約) means a futures contract, forward contract, swap contract, option contract or similar derivative contract the value of which is determined by reference to the value of, or any fluctuation in the value of—

(a) an underlying currency (excluding gold); or *(L.N. 44 of 2020)*

(b) an underlying currency index (being an index calculated by reference to a basket of currencies); *(L.N. 175 of 2017)*

expected exposure (預期風險承擔), in relation to a netting set, means the amount calculated in accordance with section 226H; *(L.N. 156 of 2012)*

exposure amount (風險承擔數額)—

(a) in relation to the STC approach, has the meaning given by section 51(1);

(b) in relation to the BSC approach, has the meaning given by section 105; and

(c) in relation to a securitization transaction, has the meaning given by section 227(1); *(L.N. 167 of 2023)*

external credit assessment institution (外部信用評估機構) means an institution that is on the list published on the Monetary Authority's website under section 4B(3); *(L.N. 167 of 2023)*

facility grade (融通等級) has the meaning assigned to it by section 139(1);

fair value (公平價值)—

(a) in relation to an asset, means the amount for which the asset could be exchanged between knowledgeable, willing parties in an arm's length transaction; or

(b) in relation to a liability, means the amount for which the liability could be settled between knowledgeable, willing parties in an arm's length transaction;

financial instrument (金融工具) includes a financial instrument in any one or more of the following forms—

(a) a written document;

(b) information recorded in the form of an entry in a book of account;

(c) information recorded (by means of a computer or otherwise) in a non-legible form but is capable of being reproduced in a legible form; *(L.N. 167 of 2023)*

financial sector entity (金融業實體) has the meaning given by section 35; *(L.N. 156 of 2012)*

first-to-default credit derivative contract (首先違責者信用衍生工具合約) means a credit derivative contract under which—

(a) the protection buyer obtains credit protection for a basket of exposures; and *(L.N. 137 of 2011)*

(b) the first default among the obligations specified in the contract for the purposes of determining whether a credit event has occurred triggers the credit protection and terminates the contract;

foreign public sector entity (非本地公營單位) means an entity specified by a relevant banking supervisory authority outside Hong Kong (whether by means of legislation or a public notice or otherwise) to be a public sector entity for the purposes of applying preferential risk-weighting treatment under capital adequacy standards formulated in accordance with—

(a) the document entitled “International Convergence of Capital Measurement and Capital Standards” published by the Basel Committee in July 1988; or *(L.N. 156 of 2012)*

(b) the Basel Framework; *(L.N. 167 of 2023)*

forward asset purchase (遠期資產購買), in relation to an authorized institution, means an off-balance sheet exposure to the credit risk of a loan, security or other asset (other than currency) that the institution has a contractually binding commitment to purchase from another party under a contract (including a put option contract written by the institution) on a specified future date; *(L.N. 175 of 2017)*

forward contract (遠期合約)—

(a) subject to paragraph (b), means a contract between two parties for the purchase or sale of a specified quantity of a specified commodity, currency, financial instrument or thing at a specified price on a specified future date;

(b) does not include a futures contract;

forward forward deposits placed (遠期有期存款), in relation to an authorized institution, means an off-balance sheet exposure to the credit risk of a party under an agreement between the institution and the party whereby the institution will place a deposit at a specified rate of interest with the party on a specified future date; *(L.N. 175 of 2017)*

foundation IRB approach (基礎 IRB 計算法) has the meaning assigned to it by section 139(1);

full basic CVA approach (完整基本CVA計算法) means the method of calculating an authorized institution’s CVA risk capital charge set out in Division 3 of Part 8A; *(L.N. 167 of 2023)*

futures contract (期貨合約) means a contract which is made under the rules or conventions of a futures exchange and traded on the exchange;

gain-on-sale (出售收益) has the meaning assigned to it by section 227(1);

general market risk (一般市場風險) has the meaning assigned to it by section 281;

group of companies (公司集團) has the meaning assigned to it by section 2(1) of the Companies Ordinance (Cap. 622); *(28 of 2012 ss. 912 & 920)*

guarantee (擔保) includes an indemnity;

haircut (扣減) means an adjustment to be applied to a credit protection or an exposure to take into account volatilities in value or exchange rates; *(L.N. 44 of 2020)*

higher level client (高階客户)—see section 2AA; *(L.N. 44 of 2020)*

home authority (監管母銀行當局), in relation to an authorized institution, means the banking supervisory authority responsible for supervising the parent bank of the institution; *(L.N. 156 of 2012)*

home jurisdiction (原屬司法管轄區), in relation to a Type B ECAI, means—

(a) the jurisdiction in which the Type B ECAI is incorporated; or

(b) another jurisdiction specified by the Monetary Authority in a restriction published under section 4B(3) for the Type B ECAI; *(L.N. 167 of 2023)*

IAA means the internal assessment approach; *(L.N. 222 of 2018)*

IAA approval (IAA批准) means an approval to use the IAA granted by the Monetary Authority under section 15C(2)(a); *(L.N. 222 of 2018)*

IMA means the internal models approach; *(L.N. 167 of 2023)*

IMM(CCR) approach (IMM(CCR)計算法) means the internal models (counterparty credit risk) approach; *(L.N. 156 of 2012)*

IMM(CCR) approval (IMM(CCR)批准) means an approval to use the IMM(CCR) approach granted by the Monetary Authority under section 10B(2)(a); *(L.N. 156 of 2012)*

IMM(CCR) risk-weighted amount (IMM(CCR) 風險加權數額) means the amount calculated under section 226D; *(L.N. 156 of 2012)*

impairment loss (減值損失), in relation to an exposure of an authorized institution, means the amount by which the carrying amount of the exposure exceeds the exposure's recoverable amount;

incorporated (成立為法團) includes established;

independent amount (獨立金額), in relation to a margin agreement associated with transactions between 2 counterparties that are not cleared by a CCP, means collateral posted by one counterparty to the other counterparty to mitigate the potential future exposure of the other counterparty to the first counterparty arising from the possible future change in the value of the transactions; *(L.N. 156 of 2012)*

indirect client (間接客户)—see section 2AA; *(L.N. 44 of 2020)*

indirect holding (間接持有) has the meaning given by section 35; *(L.N. 156 of 2012)*

inferred rating (推斷評級) has the meaning given by section 227(1); *(L.N. 222 of 2018)*

inflation derivative contract (通脹衍生工具合約) means a derivative contract the value of which changes in response to changes in one or more measures of inflation; *(L.N. 44 of 2020)*

insignificant LAC investment (非重大LAC投資) has the meaning given by section 35; *(L.N. 156 of 2012; L.N. 222 of 2018)*

insurance firm (保險商號)—

(a) means an entity—

(i) which is authorized and supervised by an insurance regulator pursuant to the law of a jurisdiction other than Hong Kong; and *(L.N. 167 of 2023)*

(ii) which is subject to supervisory arrangements regarding the maintenance of adequate capital to support its business activities comparable to those prescribed for authorized institutions under the Ordinance and these Rules; and

(b) includes an authorized insurer within the meaning of the Insurance Ordinance (Cap. 41); *(12 of 2015 s. 106)*

insurance regulator (保險規管當局) does not include a restricted insurance regulator;

interest rate contract (利率合約) means a futures contract, forward contract, swap contract, option contract or similar derivative contract the value of which changes in response to changes in interest rates; *(L.N. 175 of 2017)*

interest rate derivative contract (利率衍生工具合約) has the meaning assigned to it by section 281;

internal assessment approach (內部評估計算法) means the method, set out in section 266A, of determining the risk-weight of an eligible ABCP exposure by using the SEC-ERBA based on the internal credit rating of the exposure; *(L.N. 222 of 2018)*

internal assessment process (內部評估程序), in relation to an authorized institution, means a process used by the institution to assess the credit quality of its securitization exposures to ABCP programmes; *(L.N. 222 of 2018)*

internal capital (內部資本), in relation to an authorized institution, means the amount of capital which the institution holds and allocates internally as a result of the institution's assessment of the risks faced by the institution;

internal credit rating (內部信用評級), in relation to an authorized institution that has an IAA approval, means a credit rating which—

(a) is generated by the institution's approved internal assessment process; and

(b) is assigned to a securitization exposure to an ABCP programme; *(L.N. 222 of 2018)*

internal model (內部模式) means a model used by an authorized institution to measure the institution's credit risk or market risk; *(L.N. 167 of 2023)*

internal models approach (內部模式計算法) means the method of calculating an authorized institution's market risk capital charge set out in Divisions 13 of Part 8; *(L.N. 167 of 2023)*

internal models (counterparty credit risk) approach (內部模式(對手方信用風險) 計算法) means the method of calculating an authorized institution's default risk exposure set out in Division 2 of Part 6A; *(L.N. 156 of 2012)*

internal ratings-based approach (內部評級基準計算法) means the method of calculating an authorized institution's credit risk for non-securitization exposures set out in Part 6;

IPO means an initial public offering; *(L.N. 167 of 2023)*

IRB adoption class (IRB採用類別) means a class of exposures specified in Table 1AAB; *(L.N. 167 of 2023)*

IRB approach (IRB 計算法) means the internal ratings-based approach;

IRB class (IRB 類別) has the meaning assigned to it by section 139(1);

IRB pool (IRB組合) means a pool of underlying exposures of a securitization transaction classified as an IRB pool under section 16; *(L.N. 175 of 2017)*

IRB subclass (IRB 子類別) has the meaning assigned to it by section 139(1);

joint-stock company (合股公司) means a company that has issued ordinary shares, irrespective of whether the shares are held privately or publicly; *(L.N. 156 of 2012)*

LAC Rules (《LAC規則》) means the Financial Institutions (Resolution) (Loss-absorbing Capacity Requirements—Banking Sector) Rules (Cap. 628 sub. leg. B); *(L.N. 222 of 2018)*

LGD has the meaning assigned to it by section 139(1);

local currency (本地貨幣), in relation to a country, means the currency issued by the central government, the central bank, the monetary authority, or an authorized note-issuing bank, of that country;

long settlement transaction (長結算期交易), in relation to the calculation by an authorized institution of counterparty credit risk, means a transaction or contract where a counterparty undertakes to deliver a security, commodity or foreign currency amount against cash, other financial instruments or commodities, or vice versa, at a settlement or delivery date that is contractually specified in the transaction or contract as being more than the lower of—

(a) the market standard applicable to a transaction or contract of this type; and

(b) 5 business days after the date on which the counterparty enters into the transaction or contract; *(L.N. 156 of 2012; L.N. 44 of 2020)*

long-term ECAI issue specific rating (長期ECAI特定債項評級) means an ECAI issue specific rating that is a long-term credit assessment rating; *(L.N. 167 of 2023)*

loss given default (違責損失率) has the meaning given by section 139(1); *(L.N. 137 of 2011)*

lower level client (低階客户)—see section 2AA; *(L.N. 44 of 2020)*

LT ECAI rating mapping table (LT ECAI評級配對表) means a table made by the Monetary Authority under section 4B(2) that includes the mapping of ECAI issuer ratings and long-term ECAI issue specific ratings to credit quality grades; *(L.N. 167 of 2023)*

main index (主要指數) has the meaning assigned to it by section 51(1); *(L.N. 137 of 2011)*

margin agreement (保證金協議) has the meaning given by section 226A; *(L.N. 156 of 2012)*

margin lending transaction (保證金借貸交易), in relation to the calculation by an authorized institution of counterparty credit risk—

(a) subject to paragraph (b), means a transaction under which credit is extended in connection with the purchase, sale, carrying or trading of securities; *(L.N. 44 of 2020)*

(b) does not include a transaction under which the credit extended is—

(i) secured by securities; and

(ii) in connection with a matter other than the purchase, sale, carrying or trading of securities; *(L.N. 156 of 2012)*

margin period of risk (保證金風險期間) has the meaning given by section 226A; *(L.N. 156 of 2012)*

margin threshold (保證金門檻) has the meaning given by section 226A; *(L.N. 156 of 2012)*

market risk (市場風險), in relation to an authorized institution, means—

(a) interest rate risk, credit spread risk, equity risk, commodity risk, foreign exchange risk and default risk for trading book instruments; and

(b) commodity risk and foreign exchange risk for banking book instruments; *(L.N. 167 of 2023)*

market risk capital charge (市場風險資本要求) has the meaning assigned to it by section 281;

mark-to-market (按市價計值), in relation to any transaction, position, exposure or contract, means to revalue the transaction, position, exposure or contract, as the case may be, at current market price;

mark-to-model (按模式計值) means an approach to valuing an exposure, or a portfolio of exposures, where the value is benchmarked, extrapolated or calculated from an internal model based on a set of market data; *(L.N. 137 of 2011)*

material subsidiary (重要附屬公司) has the meaning given by rule 2(1) of the LAC Rules; *(L.N. 222 of 2018)*

minimum holding period (最短持有期), in relation to a collateral or any other thing held by an authorized institution, or by another person, for the institution's benefit (however described), means a period—

(a) that is reasonably likely to be required by the institution to realize the collateral or thing;

(b) that commences on the date of the default by the obligor giving rise to the right on the part of the institution to realize the collateral or thing; and

(c) that ends on the business day (being a day that is not a public holiday in any relevant market for the collateral or thing) on which the institution would be reasonably likely to be able to realize the collateral or thing; *(L.N. 44 of 2020)*

minimum transfer amount (最低轉移額) has the meaning given by section 226A; *(L.N. 156 of 2012)*

mixed pool (混合組合) means a pool of underlying exposures of a securitization transaction classified as a mixed pool under section 16; *(L.N. 175 of 2017)*

multi-level client structure (多層客户結構)—see section 2AA; *(L.N. 44 of 2020)*

net book value (淨帳面價值), in relation to any thing, means the thing's book value after deducting the amount of any allowance for impairment loss arising from an individual assessment of the thing for impairment loss;

nettable (可作淨額計算的), in relation to an exposure (however described) of an authorized institution, means that the exposure is subject to a recognized netting; *(L.N. 156 of 2012; L.N. 175 of 2017)*

netting set (淨額計算組合)—

(a) in relation to the calculation of the default risk exposure by using a method or approach other than the IMM(CCR) approach, means—

(i) a group of transactions with a counterparty that are subject to recognized netting; or

(ii) a transaction with a counterparty that is not subject to recognized netting or that is treated as if it were not subject to recognized netting; or

(b) in relation to the calculation of the default risk exposure by using the IMM(CCR) approach, means—

(i) a transaction falling within section 226J(1);

(ii) a group of transactions with a counterparty (other than a transaction falling within section 226J(1)) that are subject to recognized netting; or

(iii) a transaction with a counterparty (other than a transaction falling within section 226J(1)) that is not subject to recognized netting or that is treated as if it were not subject to recognized netting; *(L.N. 44 of 2020)*

non-capital LAC debt instrument (非資本LAC債務票據) has the meaning given by rule 2(1) of the LAC Rules; *(L.N. 222 of 2018)*

non-capital LAC debt resources (非資本LAC債務資源), in relation to an authorized institution, means the sum of all non-capital LAC debt instruments issued by the institution; *(L.N. 222 of 2018)*

non-capital LAC liability (非資本LAC負債) has the meaning given by rule 2(1) of the LAC Rules; *(L.N. 222 of 2018)*

non-securitization exposure (非證券化類別風險承擔) means an exposure that is not a securitization exposure; *(L.N. 167 of 2023)*

note issuance and revolving underwriting facilities (票據發行及循環式包銷融通), in relation to an authorized institution, means an off-balance sheet exposure of the institution arising from a facility provided in respect of the issue of debt securities by an issuer to the market where the institution and other underwriters under the facility are committed to—

(a) purchase any of those debt securities that cannot be placed in the market; or

(b) provide funding of an equivalent amount to the issuer; *(L.N. 175 of 2017)*

notional amount (名義數額), in relation to an off-balance sheet exposure, means the reference amount used to calculate payment obligation between the parties to the exposure; *(L.N. 44 of 2020)*

n^{th}-to-default credit derivative contract (n^{th}違責者信用衍生工具合約) has the meaning given by section 281; *(L.N. 137 of 2011)*

obligor (承擔義務人)—

(a) in relation to an exposure of an authorized institution in respect of a guarantee, means the guarantor under the guarantee;

(b) in relation to an exposure of an authorized institution in respect of a credit derivative contract, means the protection seller under the contract; or

(c) in relation to any other exposure of an authorized institution, means a person—

(i) to whom the institution has an exposure; and

(ii) who has the primary obligation to repay, pay or otherwise settle the exposure;

obligor grade (承擔義務人等級) has the meaning assigned to it by section 139(1);

offsetting transaction (抵銷交易)—see section 2AA; *(L.N. 44 of 2020)*

operational risk (業務操作風險), in relation to an authorized institution, means the risk of direct or indirect loss resulting from—

(a) inadequacies or failings in the processes or systems, or of the personnel, of the institution; or

(b) external events; *(L.N. 156 of 2012)*

option contract (期權合約) means a contract which gives the holder of the contract the option or right, exercisable at or before a specified time, to purchase or sell a specified quantity of a specified commodity, currency, financial instrument or thing at a specified price;

originating institution (發起機構) has the meaning assigned to it by section 227(1);

OTC derivative transaction means an over-the-counter derivative transaction;

outstanding default risk exposure (違責風險的未結清風險承擔), in relation to a counterparty with whom the transactions entered into by an authorized institution consist of not less than one derivative contract, means the greater of— *(L.N. 44 of 2020)*

(a) zero; or

(b) the difference between—

(i) the sum of the amounts of the default risk exposures across all netting sets with the counterparty; and *(L.N. 167 of 2023)*

(ii) the CVA loss in respect of that counterparty; *(L.N. 156 of 2012)*

over-the-counter derivative transaction (場外衍生工具交易) means a derivative contract that is not traded on an exchange; *(L.N. 156 of 2012; L.N. 44 of 2020)*

parent bank (母銀行), in relation to an authorized institution, means any holding company of the institution which is authorized as a bank in the overseas country in which the holding company is incorporated;

partly paid-up shares and securities (部分付款股份及證券), in relation to an authorized institution, means an off-balance sheet exposure to the credit risk of the shares or securities purchased from an issuer where— *(L.N. 175 of 2017)*

(a) only a part of the issue price or nominal face value of the shares or securities has been paid by the institution; and

(b) the institution will be required to pay the unpaid amount in the future; *(L.N. 175 of 2017)*

PD has the meaning assigned to it by section 139(1);

pool (組別), in relation to an authorized institution which uses the IRB approach, has the meaning assigned to it by section 139(1);

position (持倉), in relation to an authorized institution's calculation of market risk, has the meaning assigned to it by section 281;

positive current exposure (現行風險承擔正數), in relation to a transaction of an authorized institution in securities, foreign exchange or commodities that is outstanding after the settlement date in respect of the transaction, means the risk of loss to the institution on the difference between—

(a) the transaction valued at the agreed settlement price; and

(b) the transaction valued at the current market price; *(L.N. 167 of 2023)*

prior consent (事先同意) means prior consent in writing;

probability of default (違責或然率) has the meaning given by section 139(1); *(L.N. 137 of 2011)*

professional investor (專業投資者) has the meaning given by rule 2(1) of the LAC Rules; *(L.N. 222 of 2018)*

profit and loss attribution test (損益歸屬測試), in relation to the IMA, means a process comparing the daily changes in the value of a portfolio of exposures held by an approved trading desk for the most recent 250 trading days calculated by the internal models used for determining market risk capital charges and the front office systems, based on the following statistical metrics—

(a) the Spearman correlation metric;

(b) the Kolmogorov-Smirnov distribution test metric; *(L.N. 167 of 2023)*

property-holding shell company (持物業空殼公司) means a company which does not engage in any business activity except for the sole purpose of the buying, holding and selling of residential properties;

public sector entity (公營單位) means—

(a) a domestic public sector entity; or

(b) a foreign public sector entity;

qualifying CCP (合資格CCP) has the meaning given by section 226V(1); *(L.N. 51 of 2013)*

qualifying non-bank financial institution (合資格非銀行金融機構) means an entity (other than a bank)—

(a) that is a licensed corporation licensed and supervised by the Securities and Futures Commission (except a licensed corporation that has been licensed for Type 10 regulated activity (within the meaning of the Securities and Futures Ordinance (Cap. 571)));

(b) that is an authorized insurer or a designated insurance holding company within the meaning of the Insurance Ordinance (Cap. 41); or

(c) that is incorporated in a jurisdiction other than Hong Kong and is authorized by a regulator under the law of that jurisdiction to carry on financial activities in that jurisdiction, if the relevant banking supervisory authority in that jurisdiction—

(i) determines that the regulatory and supervisory standards imposed on the entity by its regulator are comparable to those (including capital and liquidity requirements) that are imposed on banks incorporated in that jurisdiction; or

(ii) has implemented capital standards consistent with the current Basel Framework and permits banks incorporated in that jurisdiction to treat exposures to the entity as exposures to a bank for the purpose of complying with the capital standards; *(L.N. 167 of 2023)*

rated (獲評級), in relation to a securitization exposure, has the meaning assigned to it by section 227(1);

rating system (評級系統) has the meaning assigned to it by section 139(1);

recognized credit risk mitigation (認可減低信用風險措施), in relation to a non-securitization exposure of an authorized institution, means the use by the institution of— *(L.N. 175 of 2017)*

(a) recognized netting;

(b) recognized collateral (within the meaning of section 51(1), 105 or 139(1), as the case requires);

(c) a recognized guarantee (within the meaning of section 51(1), 105 or 139(1), as the case requires); *(L.N. 156 of 2012; L.N. 175 of 2017)*

(d) a recognized credit derivative contract (within the meaning of section 51(1), 105 or 139(1), as the case requires); or *(L.N. 156 of 2012; L.N. 175 of 2017)*

(e) collateral received by the institution that may be included in the calculation mentioned in section 226BJ(1), (2) or (3) or the estimation mentioned in section 226H(2)(a), *(L.N. 156 of 2012; L.N. 44 of 2020)*

for the purposes of reducing the risk-weighted amount of the exposure pursuant to these Rules; *(L.N. 137 of 2011)*

recognized exchange (認可交易所) means—

(a) a recognized stock exchange; or

(b) a recognized futures exchange;

recognized futures exchange (認可期貨交易所) means a futures exchange specified in Part 2 of Schedule 1 to the Securities and Futures Ordinance (Cap. 571);

recognized netting (認可淨額計算)—

(a) in the case of the calculation of default risk exposure using the IMM(CCR) approach, means any netting done pursuant to—

(i) a valid bilateral netting agreement; or

(ii) a valid cross-product netting agreement; or

(b) in any other case, means any netting done pursuant to a valid bilateral netting agreement; *(L.N. 156 of 2012)*

recognized stock exchange (認可證券交易所) means a stock exchange specified in Part 3 of Schedule 1 to the Securities and Futures Ordinance (Cap. 571);

reduced basic CVA approach (簡化基本CVA計算法) means the method of calculating an authorized institution's CVA risk capital charge set out in Division 2 of Part 8A; *(L.N. 167 of 2023)*

reference entity (參照實體), in relation to a credit-related derivative contract, means the entity on whose credit status that contract is based; *(L.N. 44 of 2020)*

reference obligation (參照義務), in relation to a credit derivative contract, means the specified obligation of a specified reference entity in the contract, pursuant to which the basis for the settlement of the contract is determined;

regulatory capital (監管資本), in relation to an authorized institution, means the amount of capital the institution is required to hold in accordance with the Ordinance and these Rules in respect of its risk-weighted amount for each relevant risk;

regulatory capital arbitrage (監管資本套戥) has the meaning assigned to it by section 4;

regulatory deductible item (監管可扣減項目) means a Type A deductible item or a Type B deductible item; *(L.N. 54 of 2022)*

regulatory reserve for general banking risks (一般銀行業務風險監管儲備), in relation to an authorized institution, means that portion of the institution's retained earnings which, for the purposes of paragraph 9 of the Seventh Schedule to the Ordinance, is earmarked or appropriated to maintain adequate provision for losses which the institution will or may incur; *(L.N. 175 of 2017)*

relevant international organization (有關國際組織) means an international organization specified in Part 10 of Schedule 1;

relevant risk (有關風險), in relation to an authorized institution, means the credit risk, market risk, CVA risk, operational risk or sovereign concentration risk of the institution; *(L.N. 222 of 2018; L.N. 167 of 2023)*

repo-style transaction (回購形式交易) means a transaction entered into by a person whereby the person— *(L.N. 44 of 2020)*

(a) agrees to sell securities to a counterparty for a sum of money with a commitment to repurchase the securities at a specified price on a specified future date from the counterparty;

(b) lends securities to a counterparty and receives a sum of money or other securities from the counterparty in exchange as collateral;

(c) agrees to acquire securities from a counterparty for a sum of money with a commitment to resell the securities at a specified price on a specified future date to the counterparty; or

(d) borrows securities from a counterparty and provides a sum of money or other securities to the counterparty in exchange as collateral;

re-securitization exposure (再證券化類別風險承擔) has the meaning given by section 227(1); *(L.N. 137 of 2011)*

re-securitization transaction (再證券化交易) has the meaning given by section 227(1); *(L.N. 137 of 2011)*

resolution entity (處置實體) has the meaning given by rule 2(1) of the LAC Rules; *(L.N. 222 of 2018)*

restricted collective investment scheme (受限制集體投資計劃) means a collective investment scheme specified in Part 3 of Schedule 1;

restricted debt securities (受限制債務證券) means debt securities specified in Part 4 of Schedule 1;

restricted foreign public sector entity (受限制非本地公營單位) means a foreign public sector entity specified in Part 5 of Schedule 1;

restricted insurance regulator (受限制保險規管當局) means an insurance regulator specified in Part 6 of Schedule 1;

restricted jurisdiction (受限制司法管轄區) means a jurisdiction specified in Part 7 of Schedule 1;

restricted securities regulator (受限制證券規管當局) means a securities regulator specified in Part 8 of Schedule 1;

restricted sovereign (受限制官方實體) means a sovereign specified in Part 9 of Schedule 1;

revolving (循環)—

(a) for the purposes of Parts 4 and 6 and Schedule 6, and in relation to a facility granted by an authorized institution to an obligor, means that the obligor's outstanding balance under the facility is permitted to fluctuate based on the obligor's decisions to borrow and repay, up to a limit agreed with the institution; and

(b) for the purposes of Part 7, has the meaning given by section 227(1); *(L.N. 167 of 2023)*

risk category (風險類別), in relation to an authorized institution's calculation of market risk, has the meaning assigned to it by section 281;

risk class (風險類別)—

(a) in relation to the STM approach, means any of the following classes of risk to which an authorized institution's market risk exposures can be allocated—

(i) general interest rate risk;

(ii) credit spread risk (non-securitization);

(iii) credit spread risk (securitization: non-CTP);

(iv) credit spread risk (securitization: CTP);

(v) equity risk;

(vi) commodity risk;

(vii) foreign exchange risk;

(b) in relation to the IMA, means any of the following classes of risk to which an authorized institution's market risk exposures can be allocated—

(i) general interest rate risk;

(ii) credit spread risk;

(iii) equity risk;

(iv) commodity risk;

(v) foreign exchange risk; and

(c) in relation to the standardized CVA approach, means any of the following classes of risk to which an authorized institution's CVA risk exposures can be allocated—

(i) interest rate risk;

(ii) counterparty credit spread risk;

(iii) reference credit spread risk;

(iv) equity risk;

(v) commodity risk;

(vi) foreign exchange risk; *(L.N. 167 of 2023)*

risk-weighted amount (風險加權數額)—

(a) in relation to the calculation of the credit risk of a non-securitization exposure of an authorized institution, means the amount of the institution's exposure to credit risk calculated in accordance with Part 4, 5 or 6, or Division 4 of Part 6A, as the case requires; *(L.N. 156 of 2012)*

(b) in relation to the calculation of the credit risk of a securitization exposure of an authorized institution, means the amount of the institution's exposure to credit risk calculated in accordance with Part 7;

(c) in relation to the calculation of the market risk of an authorized institution, means the amount of the institution's exposure to market risk calculated in accordance with Part 8; *(L.N. 137 of 2011; L.N. 222 of 2018)*

(ca) in relation to the calculation of the CVA risk of an authorized institution, means the amount of the institution's exposure to CVA risk calculated in accordance with Part 8A; *(L.N. 167 of 2023)*

(d) in relation to the calculation of the operational risk of an authorized institution, means the amount of the institution's exposure to operational risk calculated in accordance with Part 9; or *(L.N. 222 of 2018)*

(e) in relation to the calculation of the sovereign concentration risk of an authorized institution, means the amount of the institution's exposure to sovereign concentration risk calculated in accordance with Part 10; *(L.N. 222 of 2018)*

risk-weighted amount for credit risk (信用風險的風險加權數額), in relation to an authorized institution, means the total risk-weighted amount of—

(a) the institution's non-securitization exposures to credit risk calculated in accordance with one or more of Parts 4, 5 and 6 and Division 4 of Part 6A, as the case requires; and *(L.N. 167 of 2023)*

(b) the institution's securitization exposures to credit risk calculated in accordance with Part 7;

risk-weighted amount for CVA risk (CVA風險的風險加權數額), in relation to an authorized institution, means—

(a) if the institution uses the approach set out in section 23C(1)(d)—the amount calculated by the institution under that approach; or

(b) in any other case—the amount calculated by the institution by multiplying the CVA risk capital charge by 12.5; *(L.N. 167 of 2023)*

risk-weighted amount for market risk (市場風險的風險加權數額), in relation to an authorized institution, means the total risk-weighted amount of the institution's exposures to market risk calculated in accordance with Part 8;

risk-weighted amount for operational risk (業務操作風險的風險加權數額), in relation to an authorized institution, means the risk-weighted amount of the institution's exposure to operational risk calculated in accordance with Part 9;

risk-weighted amount for sovereign concentration risk (官方實體集中風險的風險加權數額), in relation to an authorized institution, means the total risk-weighted amount of the institution's exposures to sovereign concentration risk calculated in accordance with Part 10; *(L.N. 222 of 2018)*

SA-CCR approach (SA-CCR計算法) means the standardized (counterparty credit risk) approach; *(L.N. 44 of 2020)*

SA-CCR risk-weighted amount (SA-CCR風險加權數額), in relation to a netting set of an authorized institution with a counterparty that contains one or more derivative contracts, means the product of—

(a) either one of the following amounts calculated by using the SA-CCR approach—

(i) if the institution calculates the credit risk for exposures to the counterparty by using the IRB approach—the outstanding default risk exposure in respect of the netting set; or

(ii) in any other case—the exposure amount of the default risk exposure in respect of the netting set; and

(b) the risk-weight applicable to the amount referred to in paragraph (a) determined in accordance with Part 4, 5 or 6 or Division 4 of Part 6A, as the case requires; *(L.N. 167 of 2023)*

SA-DRC has the meaning given by section 281; *(L.N. 167 of 2023)*

SA pool (標準組合) means a pool of underlying exposures of a securitization transaction classified as an SA pool under section 16; *(L.N. 175 of 2017)*

SEC-ERBA means the securitization external ratings-based approach; *(L.N. 175 of 2017)*

SEC-FBA means the securitization fall-back approach; *(L.N. 175 of 2017)*

SEC-IRBA means the securitization internal ratings-based approach; *(L.N. 175 of 2017)*

SEC-SA means the securitization standardized approach; *(L.N. 175 of 2017)*

second-to-default credit derivative contract (第二違責者信用衍生工具合約) means a credit derivative contract under which—

(a) the protection buyer obtains credit protection for a basket of exposures; and *(L.N. 137 of 2011)*

(b) the second default among the obligations specified in the contract for the purposes of determining whether a credit event has occurred triggers the credit protection and terminates the contract;

section 3C requirement (第3C條規定), in relation to an authorized institution, means a requirement in a notice under section 3C specifying the basis on which the capital adequacy ratio of the institution is to be calculated; *(L.N. 156 of 2012)*

securities financing transaction (證券融資交易) means—

(a) a repo-style transaction;

(b) a margin lending transaction;

(c) a long settlement transaction that falls within paragraph (a) or (b); or

(d) a long settlement transaction of which the counterparty credit risk profile and risk drivers are similar to those specific to a transaction that falls within paragraph (a) or (b); *(L.N. 156 of 2012)*

securities firm (證券商號)—

(a) means an entity (other than a bank)—

(i) that is authorized and supervised by a securities regulator under the law of a jurisdiction other than Hong Kong; and

(ii) that is subject to supervisory arrangements regarding the maintenance of adequate capital to support its business activities comparable to those prescribed for authorized institutions under the Ordinance and these Rules; and

(b) includes a licensed corporation that has been granted a licence to carry on a regulated activity by the Securities and Futures Commission; but

(c) does not include a credit rating agency that is authorized by a securities regulator outside Hong Kong or the Securities and Futures Commission to provide credit rating services; *(L.N. 167 of 2023)*

securities regulator (證券規管當局) does not include a restricted securities regulator;

securitization exposure (證券化類別風險承擔) means an exposure of a person to a securitization transaction, including such an exposure arising from—

(a) the purchase or repurchase of securitization issues;

(b) the provision of credit protection or credit enhancement to any of the parties to the transaction;

(c) the retention of one or more than one exposure to a tranche in the transaction;

(d) the provision of a liquidity facility (within the meaning of section 227(1)) or servicer cash advance facility (within the meaning of that section) for the transaction; or

(e) the obligation to acquire any investors' interest in the underlying exposures of the transaction if the transaction is subject to an early amortization provision; *(L.N. 175 of 2017)*

securitization external ratings-based approach (證券化外部評級基準計算法) means a method, set out in Division 8 of Part 7, of determining the risk-weight of a securitization exposure based on the ECAI issue specific rating, the inferred rating or the internal credit rating, as the case requires, of the exposure; *(L.N. 222 of 2018)*

securitization fall-back approach (證券化備選計算法) means the method of determining the risk-weight of a securitization exposure set out in Division 10 of Part 7; *(L.N. 175 of 2017)*

securitization internal ratings-based approach (證券化內部評級基準計算法) means the method of determining the risk-weight of a securitization exposure set out in Division 7 of Part 7; *(L.N. 175 of 2017)*

securitization issues (證券化票據) has the meaning assigned to it by section 227(1);

securitization standardized approach (證券化標準計算法) means the method of determining the risk-weight of a securitization exposure set out in Division 9 of Part 7; *(L.N. 175 of 2017)*

securitization transaction (證券化交易) has the meaning assigned to it by section 227(1);

senior management (高級管理人員), in relation to an authorized institution, includes the chief executives and managers of the institution;

SFT means a securities financing transaction; *(L.N. 156 of 2012)*

short-term ECAI issue specific rating (短期ECAI特定債項評級) means an ECAI issue specific rating that is a short-term credit assessment rating; *(L.N. 222 of 2018)*

significant LAC investment (重大LAC投資) has the meaning given by section 35; *(L.N. 156 of 2012; L.N. 222 of 2018)*

simplified standardized approach (簡化標準計算法) means the method of calculating an authorized institution's market risk capital charge set out in Divisions 2, 3, 4, 5, 6, 7, 8, 9 and 10 of Part 8; *(L.N. 167 of 2023)*

solo basis (單獨基礎) has the meaning assigned to it by section 4;

solo-consolidated basis (單獨—綜合基礎) has the meaning assigned to it by section 4;

solo-consolidated subsidiary (單獨—綜合附屬公司) has the meaning assigned to it by section 4;

sovereign (官方實體) means—

(a) the Government;

(b) the central government of a country;

(c) the central bank of a country;

(d) an authority of a country which performs in the country functions similar to the functions performed by the Monetary Authority; or

(e) a relevant international organization;

sovereign concentration risk (官方實體集中風險), in relation to an authorized institution—

(a) means the risk of large losses to the institution arising from obligors which are specified sovereign entities of a particular jurisdiction suddenly failing to meet their credit obligations to the institution or to other creditors of the obligors; and *(L.N. 167 of 2023)*

(b) includes the risk of other counterparties of the institution failing to meet their credit obligations to the institution as a result of the sudden failure referred to in paragraph (a); *(L.N. 222 of 2018)*

sovereign foreign public sector entity (屬官方實體的非本地公營單位) has the meaning assigned to it by section 51(1); *(L.N. 137 of 2011)*

SPE has the meaning assigned to it by section 227(1);

special purpose vehicle (特定目的工具) has the meaning given by section 35; *(L.N. 156 of 2012)*

specific provisions (特定準備金), in relation to an exposure of an authorized institution, means an allowance for impairment loss in respect of that exposure where—

(a) the institution reasonably considers that one or more than one event has occurred causing the impairment loss; *(L.N. 175 of 2017)*

(b) the event or events exist on the initial recognition of the exposure or occur after the exposure is originated or acquired by the institution; and *(L.N. 175 of 2017)*

(c) the allowance is assessed by the institution by reference to the impact that the event or events have on the cash flows in respect of the exposure insofar as that impact can be reliably estimated; *(L.N. 175 of 2017)*

specific risk (特定風險) has the meaning assigned to it by section 281;

specific wrong-way risk (特定錯向風險) has the meaning given by section 226A; *(L.N. 156 of 2012)*

specified sovereign entity (指明官方實體) has the meaning given by section 342(1); *(L.N. 222 of 2018)*

SSTM approach (SSTM計算法) means the simplified standardized approach; *(L.N. 167 of 2023)*

standard supervisory haircut (標準監管扣減) means a haircut set out in the Tables in section 1 of Schedule 7; *(L.N. 44 of 2020; L.N. 167 of 2023)*

standardized (counterparty credit risk) approach (標準(對手方信用風險)計算法) means the method of calculating default risk exposures in respect of derivative contracts set out in Division 1A of Part 6A; *(L.N. 44 of 2020)*

standardized (credit risk) approach (標準 (信用風險) 計算法) means the method of calculating an authorized institution's credit risk for non-securitization exposures set out in Part 4;

standardized CVA approach (標準CVA計算法) means the method of calculating an authorized institution's CVA risk capital charge set out in Division 4 of Part 8A; *(L.N. 167 of 2023)*

standardized (market risk) approach (標準 (市場風險) 計算法) means the method of calculating an authorized institution's market risk capital charge set out in Divisions 1A, 1B, 1C and 1D of Part 8; *(L.N. 167 of 2023)*

ST ECAI rating mapping table (ST ECAI評級配對表) means a table made by the Monetary Authority under section 4B(2) that includes the mapping of short-term ECAI issue specific ratings to credit quality grades; *(L.N. 167 of 2023)*

STC approach (STC 計算法) means the standardized (credit risk) approach;

STM approach (STM 計算法) means the standardized (market risk) approach;

stress-testing (壓力測試), in relation to an authorized institution, means the use by the institution of a risk management technique to evaluate the potential impact on the institution of a specific event, or movements in a set of financial variables, or both, under market conditions depicting various levels of market movement and financial distress;

swap contract (掉期合約) means a contract under which two parties agree to exchange assets, liabilities or cash flows according to specified terms over a specified period;

synthetic holding (合成持有) has the meaning given by section 35; *(L.N. 156 of 2012)*

synthetic securitization transaction (合成證券化交易) has the meaning assigned to it by section 227(1);

Tier 1 capital (一級資本), in relation to an authorized institution, is to be construed in accordance with section 37; *(L.N. 156 of 2012)*

Tier 1 capital ratio (一級資本比率), in relation to an authorized institution, means, subject to sections 29, 30 and 31, the ratio, expressed as a percentage, of the amount of the institution's Tier 1 capital to the sum of the institution's risk-weighted amount for credit risk, risk-weighted amount for market risk, risk-weighted amount for CVA risk, risk-weighted amount for operational risk and risk-weighted amount for sovereign concentration risk, as determined in accordance with these Rules; *(L.N. 156 of 2012; L.N. 222 of 2018; L.N. 167 of 2023)*

Tier 2 capital (二級資本), in relation to an authorized institution, is to be construed in accordance with section 40; *(L.N. 156 of 2012)*

Tier 2 capital instrument (二級資本票據) means any capital instrument that meets the qualifying criteria set out in Schedule 4C; *(L.N. 156 of 2012)*

title transfer (所有權轉移), in relation to collateral, means an outright transfer of the legal and beneficial ownership in the collateral from the collateral provider to the collateral taker;

Total capital (總資本), in relation to an authorized institution, means the sum of the institution's Tier 1 capital and Tier 2 capital; *(L.N. 156 of 2012)*

Total capital ratio (總資本比率), in relation to an authorized institution, means, subject to sections 29, 30 and 31, the ratio, expressed as a percentage, of the amount of the institution's Total capital to the sum of the institution's risk-weighted amount for credit risk, risk-weighted amount for market risk, risk-weighted amount for CVA risk, risk-weighted amount for operational risk and risk-weighted amount for sovereign concentration risk, as determined in accordance with these Rules; *(L.N. 156 of 2012; L.N. 222 of 2018; L.N. 167 of 2023)*

total EL amount (EL 總額) has the meaning assigned to it by section 139(1);

total eligible provisions (合資格準備金總額) has the meaning assigned to it by section 139(1);

total return swap (總回報掉期) means a credit derivative contract under which the protection buyer—

(a) agrees to pay the protection seller all cash flows which arise from a reference obligation together with any appreciation in the market value of the reference obligation; and

(b) receives, in return for that agreement, a spread over a specified index together with any depreciation in the value of the reference obligation during the term of the contract;

trade-related contingency (貿易關聯或有項目), in relation to an authorized institution, means an off-balance sheet exposure of the institution arising from a self-liquidating trade letter of credit—

(a) that has an original maturity below 1 year; and

(b) that is associated with the movement of goods,

including such an exposure arising from issuing or confirming a letter of credit, from acceptance on a trade bill or from shipping guarantee; *(L.N. 167 of 2023)*

trading book (交易帳), in relation to an authorized institution, means the book consisting of the institution's exposures in each of the instruments assigned to it under section 281A(4) or 281B(1); *(L.N. 167 of 2023)*

trading day (交易日) means a day on which a financial market is open for trading;

trading desk (交易桌), in relation to the calculation of an authorized institution's market risk capital charge, means a group of traders or trading accounts—

(a) set up by the institution to manage a portfolio of trading book positions in accordance with a well-defined business strategy; and

(b) operating within a clear risk management structure; *(L.N. 167 of 2023)*

traditional securitization transaction (傳統證券化交易) has the meaning assigned to it by section 227(1);

tranche (份額) has the meaning given by section 227(1); *(L.N. 137 of 2011; L.N. 222 of 2018; L.N. 167 of 2023)*

tranched credit protection (分份額信用保障) means a credit protection under which—

(a) a party transfers a portion of the credit risk of a securitization exposure or a non-securitization exposure in one or more than one tranche to one or more than one other party, and retains the remaining portion of the credit risk of the exposure; and

(b) the portion transferred and the portion retained are of different seniority; *(L.N. 175 of 2017)*

transaction-related contingency (交易關聯或有項目), in relation to an authorized institution, means an off-balance sheet exposure of the institution to a customer arising from an irrevocable obligation of the institution to pay a beneficiary when the customer fails to perform a contractual and non-financial obligation, including such an exposure arising from a performance bond, bid bond, warranty or standby letter of credit; *(L.N. 175 of 2017)*

transactor (交易者)—

(a) in relation to a revolving facility that has at least one scheduled repayment date during the previous 12 months, where all or part of the outstanding balance under the facility as at a predefined reference date is due for repayment at the succeeding scheduled repayment date (such as a credit card or charge card), means an obligor in respect of the facility who—

(i) has repaid in full the balance due under the facility at each scheduled repayment date for the previous 12 months; or

(ii) has no balance due under the facility over the previous 12 months; or

(b) in relation to an overdraft facility or a similar revolving facility that can be drawn and repaid at any time, means an obligor in respect of the facility who has not made any drawdown under the facility in the previous 12 months; *(L.N. 167 of 2023)*

Type A deductible item (A類可扣減項目), in relation to the calculation of the risk-weighted amount of a CIS exposure by an authorized institution, means—

(a) a CET1 capital instrument, an Additional Tier 1 capital instrument, or a Tier 2 capital instrument, issued by the institution or any other financial sector entity; or

(b) a capital instrument issued by a financial sector entity other than the institution that—

(i) is treated as a CET1 capital instrument under section 4(1)(c) of Schedule 4F or section 1(4)(d) of Schedule 4G;

(ii) is mapped to Additional Tier 1 capital under section 4(3) of Schedule 4F or section 1(6) of Schedule 4G; or

(iii) is mapped to Tier 2 capital under section 4(3) of Schedule 4F or section 1(6) of Schedule 4G; *(L.N. 54 of 2022)*

Type A ECAI (A類ECAI) means an ECAI other than a Type B ECAI; *(L.N. 167 of 2023)*

Type B deductible item (B類可扣減項目), in relation to the calculation of the risk-weighted amount of a CIS exposure by an authorized institution, means a non-capital LAC liability of the institution or any other financial sector entity; *(L.N. 54 of 2022)*

Type B ECAI (B類ECAI) means an ECAI the use for the purposes of these Rules of the credit assessment ratings issued by which is subject to one or more restrictions published by the Monetary Authority under section 4B(3); *(L.N. 167 of 2023)*

underlying exposures (組成項目)—

(a) in relation to a securitization transaction, has the meaning given by section 227(1); *(L.N. 54 of 2022)* (ab) in relation to a collective investment scheme, means—

(i) an on-balance sheet exposure of the scheme, including such an exposure arising from variation margin receivables in respect of transactions cleared by CCPs;

(ii) an exposure of the scheme to the underlying exposure of a derivative contract (within the meaning of section 226A), or to the asset underlying an SFT, where—

(A) the derivative contract or the SFT is entered into by the scheme; and

(B) if the scheme were an authorized institution, it would be required to hold regulatory capital in respect of the exposure to such an underlying exposure or asset under Part 4, 5, 6, 6A or 7, as the case requires;

(iii) a default risk exposure of the scheme arising from derivative contracts or SFTs entered into by the scheme; or

(iv) any other off-balance sheet exposure incurred by the scheme where, if the scheme were an authorized institution, it would be required to hold regulatory capital in respect of such an exposure under Part 4, 5, 6, 6A or 7, as the case requires; or *(L.N. 54 of 2022)*

(b) subject to paragraphs (a) and (ab), in relation to a derivative contract (including a credit derivative contract) for the calculation of an authorized institution's market risk, has the meaning given to the definition of ***underlying exposure*** by section 281; *(L.N. 137 of 2011; L.N. 54 of 2022)*

unrated (無評級), in relation to a securitization exposure, has the meaning assigned to it by section 227(1);

unsegregated collateral (無隔離抵押品), in relation to an authorized institution, means collateral that—

(a) is posted by the institution for—

(i) its transaction that is cleared by a CCP; or

(ii) a bilateral transaction entered into by the institution with a counterparty; and

(b) is not held on a bankruptcy remote basis; *(L.N. 44 of 2020)*

unspecified multilateral body (非指明多邊組織) means an entity (other than a multilateral development bank)—

(a) that is established by a group of countries to provide financing and professional advice for economic and social development projects;

(b) that has—

(i) a large sovereign membership;

(ii) its own independent legal and operational status; and

(iii) a mandate similar to the mandates of multilateral development banks; and

(c) a considerable number of the owners of which are also the owners of multilateral development banks; *(L.N. 167 of 2023)*

valid bilateral netting agreement (有效雙邊淨額結算協議), in relation to an authorized institution, means an agreement in respect of which the following conditions are satisfied—

(a) the agreement is in writing;

(b) the agreement creates a single legal obligation for all individual contracts or transactions covered by the agreement, and provides, in effect, that—

(i) the institution would have a single claim or obligation to receive or pay only—

(A) for derivative contracts—the net amount of the sum of the positive and negative mark-to-market values of the individual contracts covered by the agreement;

(B) for SFTs—the net amount of the sum of the gains and losses on the individual transactions (including the value of any collateral) covered by the agreement; or

(C) for other transactions giving rise to on-balance sheet exposures or liabilities—the net amount owed to or by the institution in respect of the individual transactions covered by the agreement; and

(ii) the institution would have the claim or obligation in the event that a counterparty to the agreement, or a counterparty to whom the agreement has been validly assigned, fails to comply with any obligation under the agreement due to default, insolvency, bankruptcy or similar circumstance; *(L.N. 175 of 2017)*

(c) the institution has been given independent legal advice in writing to the effect that in the event of a challenge in a court of law, including a challenge resulting from default, insolvency, bankruptcy, or similar circumstance, the relevant court or administrative authority would find the institution's exposure to be the net amount under— *(L.N. 156 of 2012)*

(i) the law of the jurisdiction in which the counterparty is incorporated or the equivalent location in the case of non-corporate entities, and if a branch of the counterparty is involved, then also under the law of the jurisdiction in which the branch is located;

(ii) the law which governs the individual contracts or transactions covered by the agreement; and *(L.N. 175 of 2017)*

(iii) the law which governs the agreement;

(d) the institution establishes and maintains procedures to monitor developments in any law relevant to the agreement and to ensure that the agreement continues to satisfy this definition;

(e) the institution manages the contracts or transactions covered by the agreement on a net basis; *(L.N. 175 of 2017)*

(f) the institution maintains in its files documentation adequate to support the netting of the contracts or transactions covered by the agreement; *(L.N. 175 of 2017)*

(g) the agreement is not subject to a provision that permits the non-defaulting counterparty to make only limited payment, or no payment at all, to the defaulter or the estate of the defaulter, regardless of whether or not the defaulter is a net creditor under the agreement; and *(L.N. 175 of 2017)*

(h) if the agreement covers the netting of SFTs—the agreement allows for prompt liquidation or setting-off of collateral on the occurrence of an event referred to in paragraph (b)(ii); *(L.N. 175 of 2017)*

valid cross-product netting agreement (有效跨產品淨額結算協議), in relation to an authorized institution's transactions with a counterparty that are covered by an IMM(CCR) approval, has the meaning given by section 226B; *(L.N. 156 of 2012)*

valuation adjustment (估值調整), in relation to an exposure of an authorized institution that is measured at fair value, means an adjustment made in accordance with section 4A; *(L.N. 137 of 2011)*

value-at-risk (風險值), in relation to a portfolio of exposures, means a measure of the worst expected loss on the portfolio resulting from market movement over a period of time at a given confidence level; *(L.N. 167 of 2023)*

VaR means value-at-risk.

(L.N. 156 of 2012; L.N. 175 of 2017; L.N. 222 of 2018; L.N. 44 of 2020; L.N. 54 of 2022; L.N. 167 of 2023)

(2) A reference in these Rules to a table or formula followed by a number is a reference to the table or formula, as the case may be, in these Rules bearing that number.

(3) Where, under a provision of these Rules, the prior consent of the Monetary Authority is required by an authorized institution in respect of any matter, the institution shall seek the prior consent by making an application in the specified form, if any, to the Monetary Authority.

(4) Where, under a provision of these Rules, the Monetary Authority is required to give notice of any matter to all authorized institutions incorporated in Hong Kong, or to a class of such institutions, it is sufficient compliance with that provision if the Monetary Authority publishes the notice in the Gazette.

(5) If any matter specified in a provision of these Rules is qualified by the word "adequate", "appropriate", "material", "prudent", "qualified", "relevant" or "robust", then, for

the purposes of assisting in ascertaining the nature of that qualification insofar as it relates to that matter, regard must be had to any guidelines or codes of practice issued under the Ordinance which are applicable to that provision. *(L.N. 222 of 2018)*

(6) A reference in these Rules to an exposure of an authorized institution to a guarantor arising in respect of a guarantee, or to a counterparty arising in respect of a credit derivative contract purchased by the institution, is an exposure for the purposes of these Rules whether or not any event has occurred which may give rise to a right to sue, or a claim on, the guarantor or the counterparty, as the case may be.

(7) A financial institution (other than an authorized institution) incorporated outside Hong Kong does not fall within paragraph (b) of the definition of ***bank*** in subsection (1) if—

(a) in the opinion of the Monetary Authority, the institution is not adequately supervised by the banking supervisory authority of the jurisdiction in which the institution is incorporated; or

(b) the licence or other authorization of the institution to take deposits from the public of the jurisdiction in which the institution is incorporated or it has an establishment is for the time being suspended. *(L.N. 167 of 2023)*

(E.R. 2 of 2012)

2AA. Interpretation: certain terms involving CCP and clients etc.

(1) In these Rules—

clearing intermediary (結算中介人), in relation to a CCP, means a party (including a clearing member of the CCP) who has a contractual relationship with another party (***clearing client***) that enables the clearing client to access the CCP.

(2) If a clearing client of a clearing intermediary in respect of a CCP enters into a transaction with the clearing intermediary in order to access the CCP but the clearing client does not do so for performing the function of a clearing intermediary in respect of the CCP, the clearing client is an end client.

(3) If a clearing intermediary in respect of a CCP is a clearing member of the CCP, the clearing client of the clearing intermediary is a direct client (regardless of whether the clearing client is an end client or not in respect of a transaction entered into with, or guaranteed by, the clearing intermediary). If a clearing intermediary in respect of the CCP is not a clearing member of the CCP, the clearing client of the clearing intermediary is an indirect client.

(4) If a clearing member of a CCP enters into a transaction with the CCP but the clearing member does not do so for performing the function of a clearing intermediary in respect of the CCP, the transaction is a CCP-related transaction.

(5) If a clearing member of a CCP acts on behalf of an end client in the capacity of a clearing intermediary in respect of the CCP—

(a) a transaction between the clearing member and the CCP is an offsetting transaction; and

(b) a transaction between the clearing member and the end client is a CCP-related transaction.

(6) If an end client accesses a CCP through at least 2 clearing intermediaries interposed between the CCP and the end client, then—

(a) all the interposed clearing intermediaries (other than a clearing member of the CCP) and the end client are referred to collectively as a multi-level client structure associated with the CCP and individually as a client within a multi-level client structure;

(b) where an authorized institution as a clearing intermediary within the multi-level client structure associated with the CCP provides clearing services to another clearing intermediary or the end client within the structure, that other clearing intermediary or the end client is a lower level client of the institution;

(c) where an authorized institution as a clearing intermediary or the end client within the multi-level client structure associated with the CCP receives clearing services from another clearing intermediary within the structure—

(i) that other clearing intermediary is a higher level client of the institution; and

(ii) the higher level client and any clearing intermediary within the structure at a level higher than the higher level client are clients at levels higher than the institution;

(d) the following transaction is an offsetting transaction if the transaction is entered into for enabling the end client to access the CCP—

(i) a transaction between the CCP and a clearing member of the CCP;

(ii) a transaction between a clearing member of the CCP and a direct client of the clearing member that is a clearing intermediary within the multi-level client structure associated with the CCP;

(iii) a transaction between an authorized institution and a higher level client or lower level client where both the institution and the client are clearing intermediaries; and

(e) the following transaction is a CCP-related transaction if the transaction is entered into for enabling the end client to access the CCP—

(i) a transaction between an authorized institution that is the end client and a higher level client;

(ii) a transaction between an authorized institution and a lower level client that is the end client.

(L.N. 44 of 2020)

2A. Application

These Rules apply to an authorized institution incorporated in Hong Kong.

(L.N. 128 of 2014)

Part 1A

Capital Adequacy Ratio

(L.N. 156 of 2012)

3. Interpretation of Part 1A

In this Part—

capital adequacy ratio (資本充足比率), in relation to an authorized institution, means the institution's—

(a) CET1 capital ratio;

(b) Tier 1 capital ratio; and

(c) Total capital ratio.

(L.N. 156 of 2012)

3A. *(Repealed L.N. 167 of 2023)*

3B. Minimum capital adequacy ratio applicable to authorized institutions

(L.N. 167 of 2023)

Subject to any section 3C requirement that applies to an authorized institution, the institution must not at any time— *(L.N. 167 of 2023)*

(a) have a CET1 capital ratio of less than 4.5%;

(b) have a Tier 1 capital ratio of less than 6%; or

(c) have a Total capital ratio of less than 8%.

(L.N. 156 of 2012)

3C. Monetary Authority may require authorized institution that has any subsidiary to calculate capital adequacy ratio on

unconsolidated or consolidated basis, etc.

(1) For the purposes of calculating the capital adequacy ratio of an authorized institution that has one or more than one subsidiary, the Monetary Authority may, by notice in writing given to the institution, require the capital adequacy ratio of the institution to be calculated—

(a) on an unconsolidated basis in respect of the institution;

(b) on a consolidated basis in respect of the institution and one or more of such subsidiaries; or

(c) on an unconsolidated basis in respect of the institution and on a consolidated basis in respect of the institution and one or more of such subsidiaries.

(2) An authorized institution must comply with the requirements of a notice given to it under subsection (1).

(L.N. 156 of 2012)

3D. Authorized institution must notify Monetary Authority of failure to have minimum capital adequacy ratio

If an authorized institution fails to comply with section 3B, or fails to have a capital adequacy ratio that is equal to or more than the ratio specified by the Monetary Authority in a notice served on the institution under section 97F(1) of the Ordinance, the institution must— *(L.N. 167 of 2023)*

(a) immediately notify the Monetary Authority of the failure; and

(b) provide the Monetary Authority with any particulars of the failure that the Monetary Authority requires.

(L.N. 156 of 2012)

Part 1B

Additional CET1 Capital Required to be Maintained before Distribution Payment Allowed

(Part 1B added L.N. 128 of 2014)

Division 1—General

3E. Interpretation of Part 1B

(1) In this Part—

buffer level (緩衝水平), in relation to an authorized institution, means the buffer level applicable to the institution under section 3G;

capital conservation buffer ratio (防護緩衝資本比率), in relation to the calculation of an authorized institution's buffer level, means the ratio set out in section 3M;

CB ratio (CB比率) means a capital conservation buffer ratio;

CCyB ratio (CCyB比率) means a countercyclical capital buffer ratio;

countercyclical capital buffer ratio (逆周期緩衝資本比率), in relation to the calculation of an authorized institution's buffer level, means the ratio calculated under section 3O;

distribution payment (分派付款), in relation to the making of a payment by an authorized institution—

(a) means—

(i) payment of dividends;

(ii) payment for purchase of the institution's own shares;

(iii) discretionary payment on Additional Tier 1 capital instruments;

(iv) discretionary bonus payment to the directors, senior management and employees of the institution; or

(v) any other payment that is in substance a distribution of the institution's CET1 capital; but

(b) does not include any payment that does not deplete the institution's CET1 capital;

domestic systemically important authorized institution (具本地系統重要性認可機構) means an authorized institution so designated under section 3U;

D-SIB means a domestic systemically important authorized institution;

earnings (溢利), in relation to an authorized institution, means the amount of the institution's profits calculated by—

(a) adding together—

(i) the institution's profits after taxation generated in a financial year out of which the institution may make a distribution payment; and

(ii) any distribution payment that has been made, and deducted from the institution's income, in the financial year; and

(b) subtracting from the sum calculated under paragraph (a) any additional tax that would have been reported if no distribution payment had been made in the financial year;

global systemically important authorized institution (具全球系統重要性認可機構) means an authorized institution so designated under section 3S;

G-SIB means a global systemically important authorized institution;

higher loss absorbency ratio (較高吸收虧損能力比率)—

(a) in relation to the calculation of a D-SIB's buffer level, means the ratio determined under section 3V; or

(b) in relation to the calculation of a G-SIB's buffer level, means the ratio determined under section 3T;

HLA ratio (HLA比率) means a higher loss absorbency ratio;

maximum distributable amount (最高可分派數額)—see section 3H;

net CET1 capital (淨CET1資本), in relation to an authorized institution, means the institution's CET1 capital less the amount from the CET1 capital that the institution requires for maintaining— *(L.N. 222 of 2018)*

(a) the minimum CET1 capital ratio, Tier 1 capital ratio and Total capital ratio set out in section 3B applicable to it as may be varied by the Monetary Authority under section 97F of the Ordinance; and

(b) the minimum external or internal LAC risk-weighted ratio (as the case requires) that the institution is required to maintain under the LAC Rules. *(L.N. 222 of 2018)*

(2) The net CET1 capital ratio for an authorized institution is determined in the same way as the institution's CET1 capital ratio under these Rules, except that the institution's net CET1 capital is used in place of the institution's CET1 capital for the determination.

(3) For the purposes of this Part—

(a) where an authorized institution creates an obligation to make a distribution payment, the institution is treated as making a distribution payment; and

(b) where an authorized institution intends to create an obligation to make a distribution payment, the institution is treated as intending to make a distribution payment.

Division 2—Constraints on Distribution Payment

3F. Distribution payment requirements

(1) *(Repealed L.N. 167 of 2023)*

(2) No distribution payment may be made by an authorized institution in a financial year unless all of the following provisions and requirement are complied with— *(L.N. 175 of 2017; L.N. 222 of 2018)*

(a) this section;

(b) if applicable, section 3J or 3K;

(c) section 3Z;

(d) if the institution is a resolution entity or material subsidiary and the payment is made on a day on which the institution must meet a LAC requirement—the LAC requirement. *(L.N. 222 of 2018)*

(3) Without affecting any requirement imposed on an authorized institution under any other Parts, subsection (4), (5) or (6) applies to the institution if it intends to make a distribution payment in a financial year (***relevant payment***).

(4) If an authorized institution's net CET1 capital ratio is above its buffer level, irrespective of whether the institution has earnings for the immediately preceding financial year, the institution may make the relevant payment.

(5) If an authorized institution's net CET1 capital ratio is equal to or below its buffer level, and the institution does not have earnings for the financial year immediately preceding the financial year in which notification of the relevant maximum

distributable amount is required to be made under section 3K(3)(a) (***year of notification***), the institution must not make the relevant payment.

(6) If an authorized institution’s net CET1 capital ratio is equal to or below its buffer level, and the institution has earnings for the financial year immediately preceding the year of notification, the institution may make the relevant payment, but the relevant payment must not exceed the greater of—

(a) zero; and

(b) the maximum distributable amount notified to the Monetary Authority under section 3K(3)(a) less the aggregate amount of any distribution payments that have been made in the year of notification.

(7) In subsection (2)—

LAC requirement (LAC規定) has the meaning given by rule 2(1) of the LAC Rules. *(L.N. 222 of 2018)*

3G. Buffer level

There is applicable to an authorized institution a buffer level that is expressed as a percentage and calculated according to the following formula—

(a) if the institution is a G-SIB or a D-SIB—

CB ratio + CCyB ratio + HLA ratio; or

(b) in any other case—

CB ratio + CCyB ratio.

3H. Maximum distributable amount

(1) The maximum distributable amount for an authorized institution is the product of—

(a) the institution’s earnings for the financial year immediately preceding the financial year in which notification under section 3K(3)(a) is made; and

(b) the maximum distribution percentage determined by reference to the quartile of the institution’s buffer level within which the institution’s net CET1 capital ratio falls, as listed in Table 1AA.

Table 1AA

Determination of Maximum Distribution Percentage for Calculation of Maximum Distributable Amount

Quartile of buffer level within which net CET1 capital ratio falls	Maximum distribution percentage
1st quartile (0% to 25% of buffer level)	0%
2nd quartile (more than 25% to 50% of buffer level)	20%
3rd quartile (more than 50% to 75% of buffer level)	40%
4th quartile (more than 75% to 100% of buffer level)	60%

(2) For the purposes of subsection (1)(b), an authorized institution must determine the quartile of the institution’s buffer level within which the institution’s net CET1 capital ratio falls as at the latest practicable date—

(a) which must be within 2 months before the date on which notification under section 3K(3)(a) is made; and

(b) for which the institution has the necessary data readily available for making the determination.

3I. Monetary Authority may require buffer level and maximum distribution percentage to be applied on unconsolidated or consolidated basis where there is subsidiary

(1) For the purposes of applying the buffer level and the maximum distribution percentage to an authorized institution that has one or more subsidiaries, the Monetary Authority may, by notice in writing given to the institution, require the buffer level and the maximum distribution percentage to be applied—

(a) on an unconsolidated basis in respect of the institution;

(b) on a consolidated basis in respect of the institution and one or more of the subsidiaries; or

(c) on an unconsolidated basis in respect of the institution and on a consolidated basis in respect of the institution and one or more of the subsidiaries.

(2) An authorized institution must comply with the requirements of a notice given to it under subsection (1).

3J. What authorized institution must do where net CET1 capital ratio above buffer level

(1) *(Repealed L.N. 167 of 2023)*

(2) If an authorized institution's net CET1 capital ratio is above its buffer level, and the institution intends to make a distribution payment that would result in its net CET1 capital ratio being equal to, or falling below, the buffer level, the institution must—

(a) consult the Monetary Authority before making the distribution payment; and

(b) submit to the Monetary Authority, within such period as the Monetary Authority may specify in writing (being a period reasonable in all the circumstances of the case), for approval a capital plan setting out the measures proposed to be taken by the institution, within such time frame as the Monetary Authority may specify, to manage and improve the institution's capital position.

3K. What authorized institution must do where net CET1 capital ratio not above buffer level

(1) *(Repealed L.N. 167 of 2023)*

(2) If an authorized institution's net CET1 capital ratio is equal to or below its buffer level, the institution must, on becoming aware of the fact, immediately notify the Monetary Authority and specify the quartile of the buffer level within which the net CET1 capital ratio falls.

(3) If an authorized institution's net CET1 capital ratio is equal to or below its buffer level, and the institution intends to make a distribution payment, the institution must—

(a) notify, within 1 month before making the distribution payment, the Monetary Authority of the maximum distributable amount for the institution;

(b) provide the Monetary Authority with any particulars that the Monetary Authority requires; and

(c) submit to the Monetary Authority, within such period as the Monetary Authority may specify in writing (being a period reasonable in all the circumstances of the case), for approval a capital plan setting out the measures proposed to be taken by the institution, within such time frame as the Monetary Authority may specify, to manage and improve the institution's capital position.

3L. Other requirements

(1) *(Repealed L.N. 167 of 2023)*

(2) An authorized institution must consult the Monetary Authority in advance if—

(a) the institution intends to raise capital in the private sector for putting itself into a position to make a distribution payment in excess of the maximum distributable amount that would have otherwise been applicable to the institution in the absence of such intended capital raising; and

(b) the amount of such intended capital would not result in any noticeable improvement in the capital position of the institution after the making of the distribution payment.

Division 3—CB Ratio

3M. CB ratio

The CB ratio for calculating an authorized institution's buffer level under section 3G is 2.5%.

(L.N. 167 of 2023)

Division 4—CCyB Ratio

3N. Interpretation of Division 4

In this Division—

advance announcement period (預告期), in relation to a JCCyB ratio, means the period—

(a) beginning on the date immediately after the date on which the ratio is announced; and

(b) ending on the effective date of the ratio;

applicable JCCyB ratio (適用JCCyB比率), in relation to a jurisdiction in which an authorized institution has private sector credit exposures, means—

(a) (where the jurisdiction is outside Hong Kong) an applicable JCCyB ratio as specified in section 3P; or

(b) (where the jurisdiction is Hong Kong) an applicable JCCyB ratio as specified in section 3Q;

effective date (生效日期), in relation to a JCCyB ratio or an applicable JCCyB ratio, means the date on which the ratio becomes effective;

JCCyB ratio (JCCyB比率), in relation to a jurisdiction outside Hong Kong in which an authorized institution has private sector credit exposures, means—

(a) a capital buffer level, expressed as a percentage, announced by the relevant authority of the jurisdiction for the purpose of implementing the provisions concerning the countercyclical capital buffer in the current Basel Framework; or *(L.N. 167 of 2023)*

(b) (if no such announcement has been made) 0%;

private obligor (私人承擔義務人) means an obligor that is not—

(a) a sovereign;

(b) a regional, provincial or municipal government;

(c) a public sector entity;

(d) a multilateral development bank; or

(e) a bank;

private sector credit exposures (私人機構信用風險承擔), in relation to an authorized institution, means—

(a) non-securitization exposures for which the institution calculates a risk-weighted amount for credit risk in accordance with Part 4, 5 or 6, or Division 4 of Part 6A, as the case requires; *(L.N. 167 of 2023)*

(b) securitization exposures for which the institution calculates a risk-weighted amount for credit risk in accordance with Part 7; or

(c) exposures for which the institution calculates a market risk capital charge in accordance with Part 8 for—

(i) SA-DRC under the STM approach;

(ii) default risk charge under the IMA; or

(iii) specific risk under the SSTM approach, *(L.N. 167 of 2023)*

to the extent that such exposures are to a private obligor only;

ultimate risk basis (最終風險基礎) means the allocation of private sector credit exposures to the jurisdiction where the risk ultimately lies to the best of an authorized institution's knowledge and information.

3O. CCyB ratio

(1) The CCyB ratio for calculating an authorized institution's buffer level under section 3G is calculated by the use of Formula 1A.

Formula 1A

Calculation of CCyB Ratio

$$CCyB = \frac{\sum_j (RWA_j \cdot AJCCyB_j)}{\sum_j RWA_j}$$

where—

CCyB = the institution's CCyB ratio for calculating its buffer level under section 3G;

RWA_j = the sum of—

(a) the risk-weighted amounts for credit risk that relate to the institution's private sector credit exposures in jurisdiction j calculated in accordance with— *(L.N. 167 of 2023)*

(i) Part 4, 5 or 6 or Division 4 of Part 6A; and

(ii) Part 7,

as the case requires; and

(b) the risk-weighted amount for market risk that relates to the institution's private sector credit exposures in jurisdiction j derived by multiplying by 12.5 the aggregate of the market risk capital charge calculated in accordance with Part 8 for— *(L.N. 167 of 2023)*

(i) SA-DRC under the STM approach;

(ii) default risk charge under the IMA; or

(iii) specific risk under the SSTM approach, as the case requires, but if the institution is exempted by the Monetary Authority under section 22(1) from calculating its market risk capital charge under section 17, this paragraph is to be disregarded; *(L.N. 167 of 2023)*

$AJCCyB_j$ = the applicable JCCyB ratio for jurisdiction j that is in effect on the latest practicable date referred to in section 3H(2) as at which the institution calculates its CCyB ratio for calculating its buffer level under section 3G.

(2) Subject to subsection (3), the jurisdiction in which an authorized institution is considered to have private sector credit exposures must be determined by the institution, where possible, on an ultimate risk basis.

(3) If, in relation to an authorized institution, it is not possible to determine under subsection (2) the jurisdiction in which the institution has private sector credit exposures, the jurisdiction is taken to be the jurisdiction where the exposures are booked.

3P. Applicable JCCyB ratio for jurisdiction outside Hong Kong

(1) This section applies in relation to a jurisdiction outside Hong Kong in which an authorized institution has private sector credit exposures (***non-Hong Kong jurisdiction***).

(2) *(Repealed L.N. 167 of 2023)*

(3) For this Part— *(L.N. 167 of 2023)*

(a) where a JCCyB ratio for a non-Hong Kong jurisdiction is 0% because of paragraph (b) of the definition of ***JCCyB ratio*** in section 3N—

(i) subject to subparagraph (ii), the applicable JCCyB ratio for the jurisdiction is 0%; or

(ii) if an announcement is at any time made by the Monetary Authority under subsection (4), the applicable JCCyB ratio is the one as announced by the Monetary Authority;

(b) where a JCCyB ratio announced for a non-Hong Kong jurisdiction is not more than 2.5%—

(i) subject to subparagraph (ii), the applicable JCCyB ratio for the jurisdiction is equal to the JCCyB ratio; or

(ii) if an announcement is at any time made by the Monetary Authority under subsection (4), the applicable JCCyB ratio is the one as announced by the Monetary Authority; or

(c) where a JCCyB ratio announced for a non-Hong Kong jurisdiction is more than 2.5%—

(i) subject to subparagraph (ii), the applicable JCCyB ratio is 2.5%; or

(ii) if an announcement is at any time made by the Monetary Authority under subsection (4), the applicable JCCyB ratio is the one as announced by the Monetary Authority.

(4) Where the Monetary Authority considers that the applicable JCCyB ratio for a non-Hong Kong jurisdiction under subsection (3)(a)(i), (b)(i) or (c)(i) is not sufficient to adequately bolster authorized institutions' resilience in view of the identified system-wide risks related to that jurisdiction, the Monetary Authority may announce, in accordance with subsection (11), the following to be the applicable JCCyB ratio— *(L.N. 167 of 2023)*

(a) (for subsection (3)(a) or (b)) a ratio higher than the JCCyB ratio but not more than 2.5%; or

(b) (for subsection (3)(c)) the JCCyB ratio.

(5) Subject to subsections (6), (7), (8) and (9), the effective date of a JCCyB ratio for a non-Hong Kong jurisdiction is taken to be the effective date of the applicable JCCyB ratio for the jurisdiction unless— *(L.N. 167 of 2023)*

(a) where the JCCyB ratio is higher than the previous one, the advance announcement period for the JCCyB ratio is less than 6 months or more than 12 months; or

(b) the Monetary Authority considers that, with a view to ensuring adequate resilience of authorized institutions, or the effective working of the banking system of Hong Kong, the effective date of the applicable JCCyB ratio should be different from that of the JCCyB ratio.

(6) For subsection (5), if a JCCyB ratio for the jurisdiction is 0% because of paragraph (b) of the definition of ***JCCyB ratio*** in section 3N, 1 January 2016 is taken to be the effective date of the JCCyB ratio for the jurisdiction.

(7) If an applicable JCCyB ratio for a non-Hong Kong jurisdiction is announced by the Monetary Authority under subsection (4), the Monetary Authority must announce, in accordance with subsection (11), the effective date of the applicable JCCyB ratio to be— *(L.N. 167 of 2023)*

(a) (where the announcement is made under subsection (4)(a) and the JCCyB ratio referred to in that subsection is 0% because of paragraph (b) of the definition of ***JCCyB ratio*** in section 3N) 12 months after the date of the announcement by the Monetary Authority, unless the Monetary Authority announces a different effective date under subsection (9); or

(b) (in any other case) a date not less than 6 months, and not more than 12 months, after the date of the announcement by the Monetary Authority.

(8) For subsection (5)(a), subject to subsection (9), the effective date of the applicable JCCyB ratio for the jurisdiction is taken to be— *(L.N. 167 of 2023)*

(a) (where the advance announcement period is less than 6 months) 6 months after the date of the announcement of the JCCyB ratio by the relevant authority of the jurisdiction; or

(b) (where the advance announcement period is more than 12 months) 12 months after the date of the announcement of the JCCyB ratio by the relevant authority of the jurisdiction.

(9) For subsections (5)(b) and (7)(a), the Monetary Authority may announce, in accordance with subsection (11), the effective date of the applicable JCCyB ratio for the jurisdiction to be a date— *(L.N. 167 of 2023)*

(a) (subject to paragraph (b)) not more than 12 months after the date of the announcement by the Monetary Authority; and

(b) (where the applicable JCCyB ratio is higher than the previous one) not less than 6 months after the date of the announcement by the Monetary Authority.

(10) *(Repealed L.N. 167 of 2023)*

(11) An announcement under subsection (4), (7) or (9) must be made by the Monetary Authority by—

(a) notifying all authorized institutions in writing; and

(b) posting a notification on the Monetary Authority's website.

3Q. Applicable JCCyB ratio for Hong Kong

(1) *(Repealed L.N. 167 of 2023)*

(2) The applicable JCCyB ratio for Hong Kong is the applicable JCCyB ratio announced by the Monetary Authority under subsection (3). *(L.N. 167 of 2023)*

(3) Subject to subsection (7), the Monetary Authority may announce, in accordance with subsection (10), a ratio of 0% or greater that the Monetary Authority considers prudent to be the applicable JCCyB ratio for Hong Kong. *(L.N. 167 of 2023)*

(4) In determining under subsection (3) whether a ratio is prudent, the Monetary Authority may take into account—

(a) the extent of risks for the financial system of Hong Kong; and

(b) any other matters the Monetary Authority considers relevant. *(L.N. 167 of 2023)*

(5)-(6) *(Repealed L.N. 167 of 2023)*

(7) The Monetary Authority may, after consulting the Banking Advisory Committee, the Deposit-taking Companies Advisory Committee, The Hong Kong Association of Banks and The DTC Association, announce, in accordance with subsection (10), a ratio of more than 2.5% to be the applicable JCCyB ratio if— *(L.N. 167 of 2023)*

(a) the latest applicable JCCyB ratio is 2.5% and has been in effect for a period of not less than 6 months;

(b) the Monetary Authority considers that the system-wide risks did not materially recede during the period; and

(c) the Monetary Authority considers it necessary to determine a ratio of more than 2.5% to be the applicable JCCyB ratio in order to protect authorized institutions from the expected consequences of the build-up of system-wide risks for the financial system of Hong Kong. *(L.N. 167 of 2023)*

(8) Where an applicable JCCyB ratio is higher than the previous one, the Monetary Authority must announce, in accordance with subsection (10), the applicable JCCyB ratio not less than 6 months, and not more than 12 months, before the effective date of the applicable JCCyB ratio.

(9) If the Monetary Authority considers that the system-wide risks are receding, or that the banking sector may be entering a period of stress, the Monetary Authority may reduce, by announcement in accordance with subsection (10), the applicable JCCyB ratio. *(L.N. 167 of 2023)*

(10) An announcement under subsection (3), (7), (8) or (9) must be made by the Monetary Authority by— *(L.N. 167 of 2023)*

(a) notifying all authorized institutions in writing; and

(b) posting a notification on the Monetary Authority's website.

3R. Distribution payments made after reduction of applicable JCCyB ratio

(1) An authorized institution must comply with subsection (2) if—

(a) a latest applicable JCCyB ratio for Hong Kong, or for a jurisdiction outside Hong Kong, is lower than the previous one; and

(b) the institution intends, within a period of 12 months after the effective date of the latest applicable JCCyB ratio, to use for making a distribution payment any of its earnings that would have been subject to constraint on distribution payments under this Part but for the lower applicable JCCyB ratio.

(2) For subsection (1), an authorized institution must—

(a) consult the Monetary Authority before making the payment; and

(b) provide the Monetary Authority with a written justification regarding the prudence of the intended distribution payment within the context of the institution’s capital planning.

Division 5—HLA Ratio

3S. G-SIB

The Monetary Authority may designate an authorized institution as a global systemically important authorized institution if, in the opinion of the Monetary Authority, the risks associated with the institution are such as to render the institution capable of having a significant impact on the effective working and stability of the global financial system were the institution to become non-viable.

3T. HLA ratio as applicable to G-SIB

(1) Subject to subsection (3) and section 3W, the Monetary Authority may, by reference to the degree of global systemic importance that the Monetary Authority assesses a G-SIB to bear, determine for the institution an HLA ratio as specified in subsection (2).

(2) The HLA ratio applicable to the G-SIB concerned must be not less than 1% and not more than 3.5%. *(L.N. 167 of 2023)*

(3) The Monetary Authority must notify the G-SIB concerned in writing of the HLA ratio determined for the institution, and the institution must apply, within 12 months from the notification, the HLA ratio to the calculation of its buffer level.

3U. D-SIB

The Monetary Authority may designate an authorized institution as a domestic systemically important authorized institution if, in the opinion of the Monetary Authority, the risks associated with the institution are such as to render the institution capable of having a significant impact on the effective working and stability of the banking or financial system of Hong Kong were the institution to become non-viable.

3V. HLA ratio as applicable to D-SIB

(1) Subject to subsection (3) and section 3W, the Monetary Authority may, by reference to the degree of domestic systemic importance that the Monetary Authority assesses a D-SIB to bear, determine for the institution an HLA ratio as specified in subsection (2).

(2) The HLA ratio applicable to the D-SIB concerned must be not less than 1% and not more than 3.5%. *(L.N. 167 of 2023)*

(3) The Monetary Authority must notify the D-SIB concerned in writing of the HLA ratio determined for the institution, and the institution must apply, within 12 months from the notification, the HLA ratio to the calculation of its buffer level.

3W. Where authorized institution being both G-SIB and D-SIB

If an authorized institution is designated under this Division as both a G-SIB and a D-SIB, the HLA ratio applicable to the institution is the higher of the following—

(a) the HLA ratio applicable to the institution as a G-SIB; and

(b) the HLA ratio applicable to the institution as a D-SIB.

3X. Where both authorized institution and its subsidiary being D-SIB

If an authorized institution is a subsidiary of a D-SIB, and the Monetary Authority also designates the institution as a D-SIB, the Monetary Authority may determine under section 3V(1) for the institution an HLA ratio that is different from the one determined for the D-SIB of which the institution is a subsidiary.

Part 1C

Leverage Ratio

(Part 1C added L.N. 175 of 2017)

3Y. Interpretation of Part 1C

In this Part—

exposure measure (風險承擔計量), in relation to an authorized institution, means its exposure measure determined in accordance with section 3ZB;

leverage ratio (槓桿比率), in relation to an authorized institution, means the ratio, expressed as a percentage, of its Tier 1 capital to its exposure measure.

3Z. Minimum leverage ratio for authorized institutions

(1) An authorized institution must not at any time have a leverage ratio of less than 3%.

(2) The ratio must be calculated on the same basis as that adopted for the calculation of capital adequacy ratio under Division 7 of Part 2.

3ZA. Authorized institution must notify Monetary Authority of failure to have minimum leverage ratio

An authorized institution that fails to comply with section 3Z must—

(a) on becoming aware of the failure, immediately notify the Monetary Authority of the fact; and

(b) if requested by the Monetary Authority to provide the particulars of the failure to the Monetary Authority—provide the particulars.

3ZB. Determination of exposure measure

(1) An authorized institution must determine its exposure measure in accordance with this section.

(2) The exposure measure is the sum of the following—

(a) the institution's on-balance sheet exposures, excluding those arising from derivative contracts or SFTs (other than collateral for derivative contracts or for SFTs recognized as an on-balance sheet asset under the applicable accounting standard);

(b) the institution's exposures arising from derivative contracts (other than collateral recognized as an on-balance sheet asset under the applicable accounting standard);

(c) the institution's exposures arising from SFTs (other than collateral recognized as an on-balance sheet asset under the applicable accounting standard); and

(d) the institution's off-balance sheet exposures (other than those falling within paragraph (b) or (c)).

(3) The amounts of the exposures mentioned in subsection (2)(a), (b), (c) and (d) are calculated by using the standard calculation methodology set out in the standard return template relating to leverage ratio specified by the Monetary Authority.

(4) The institution may deduct from the sum calculated under subsection (2) its on-balance sheet exposures (other than liability items) deducted from Tier 1 capital.

(5) If the institution is a note-issuing bank, in determining the institution's on-balance sheet exposures for the purposes of this section, certificates of indebtedness issued by the Financial Secretary under section 4 of the Exchange Fund Ordinance (Cap. 66) to, and held by, the institution must not be included.

(6) In this section—

note-issuing bank (發鈔銀行) has the meaning given by section 2 of the Legal Tender Notes Issue Ordinance (Cap. 65).

Part 2

Prescribed Approaches in relation to Calculation of Capital Adequacy Ratio

Division 1—General

4. Interpretation of Part 2

In this Part— *(L.N. 167 of 2023)*

consolidated basis (綜合基礎), in relation to the calculation of an authorized institution's capital adequacy ratio, means the basis set out in section 31 on which the institution calculates that ratio;

consolidation group (綜合集團), in relation to an authorized institution, means—

(a) the institution; and

(b) such subsidiaries of the institution as specified in a section 3C requirement given to the institution; *(L.N. 156 of 2012)*

regulatory capital arbitrage (監管資本套戥), in relation to an authorized institution, means the use by the institution of a combination of different calculation approaches or methods in respect of the institution's exposures with the intention of minimizing its regulatory capital by selectively choosing a given calculation approach or method for certain exposures predominantly to achieve a lower regulatory capital;

solo basis (單獨基礎), in relation to the calculation of an authorized institution's capital adequacy ratio, means the basis set out in section 29 on which the institution calculates that ratio;

solo-consolidated basis (單獨—綜合基礎), in relation to the calculation of an authorized institution's capital adequacy ratio, means the basis set out in section 30 on which the institution calculates that ratio;

solo-consolidated subsidiary (單獨—綜合附屬公司), in relation to an authorized institution, means a subsidiary of the institution specified in an approval granted to the institution under section 28(2)(a). *(L.N. 167 of 2023)*

(L.N. 167 of 2023)

4A. Valuation of exposures measured at fair value

(1) Where the exposures of an authorized institution are measured at fair value, for the purposes of calculating the risk-weighted amount of the exposures under one or more of Parts 4, 5, 6, 6A, 7, 8, 10 and 11, the institution must establish and maintain valuation systems, controls and procedures that are effective to ensure that the valuation of its exposures is prudent and reliable. *(L.N. 156 of 2012; L.N. 222 of 2018; L.N. 167 of 2023)*

(2) For the purposes of subsection (1), an authorized institution must make adjustments, where appropriate, to the valuation of its exposures that are measured at fair value to account for—

(a) the limitations of the valuation model or methodology and the data used by the institution in the valuation process;

(b) the liquidity of the institution's exposures; and

(c) other relevant factors that might reasonably be expected to affect the prudence and reliability of the valuation of the institution's exposures.

(3) To avoid doubt, adjustments made by an authorized institution in accordance with this section may exceed adjustments made

by the institution in accordance with the financial reporting standards adopted by the institution.

(L.N. 137 of 2011)

4B. Recognition of ECAIs

(1) A credit assessment rating assigned to a person or an exposure may be used by an authorized institution for the purposes of these Rules only where—

(a) the rating has been issued by an entity recognized by the Monetary Authority;

(b) the use of the rating is not for a purpose that is prohibited by a restriction published on the Monetary Authority's website under subsection (3);

(c) if the rating is assigned to an exposure, the exposure has not ceased to be outstanding; and

(d) the rating is for the time being neither withdrawn nor suspended by the entity that issued it.

(2) The Monetary Authority is to—

(a) determine with which of the credit quality grades, which are represented by the numerals 1 to 18, the relevant long-term credit assessment ratings issued by an entity falling within subsection (1)(a) are to be associated;

(b) determine with which of the credit quality grades, which are represented by the numerals 1 to 5, the relevant short-term credit assessment ratings issued by an entity falling within subsection (1)(a) are to be associated; and

(c) make tables to include the mappings determined under paragraphs (a) and (b).

(3) The Monetary Authority is to publish on the Monetary Authority's website—

(a) the list of entities that have been recognized under subsection (1)(a);

(b) any restrictions on the use of the credit assessment ratings issued by an entity that has been recognized under subsection (1)(a);

(c) the mapping tables made under subsection (2)(c); and

(d) any amendments made by the Monetary Authority from time to time to the list of entities, the restrictions or the mapping tables.

(L.N. 167 of 2023)

4C. Nomination of ECAIs to be used

(1) If an authorized institution is required under these Rules to determine the risk-weight attributable to an exposure in accordance with Part 4 or 7, the institution must nominate one or more ECAIs in accordance with this section.

(2) Subject to subsections (3) and (4), an authorized institution must nominate, for each of the ECAI ratings based portfolios relevant to it, one or more ECAIs the ECAI ratings issued by which the institution will use for the purposes of Part 4 or 7, in respect of—

(a) the ECAI ratings based portfolio concerned; or

(b) a certain type of exposures falling within the ECAI ratings based portfolio concerned.

(3) An authorized institution must not nominate an ECAI, or a group of ECAIs, for an ECAI ratings based portfolio unless, having regard to the obligors in respect of the exposures that fall within the portfolio and to the geographical regions where those exposures arise or may be required to be enforced, it can reasonably be concluded that the ECAI, or the group of ECAIs collectively, issues a range of ECAI ratings that—

(a) if the ECAI ratings will be used in respect of any exposure falling within that portfolio—provides a reasonable coverage for that portfolio; or

(b) if the ECAI ratings will be used in respect of a certain type of exposures falling within that portfolio—provides a reasonable coverage for those exposures.

(4) An authorized institution may nominate a Type B ECAI for an ECAI ratings based portfolio if the use of the ECAI ratings issued by the Type B ECAI for the purposes of Part 4 or 7 in respect of exposures falling within the ECAI ratings based portfolio is not prohibited by a restriction published on the Monetary Authority's website under section 4B(3).

(5) An authorized institution must give written notice to the Monetary Authority of a nomination under subsection (2) as soon as practicable after making the nomination.

(6) An authorized institution must not, in respect of an ECAI ratings based portfolio or a certain type of exposures falling within an ECAI ratings based portfolio, use, for the purposes of Part 4 or 7, the ECAI ratings of an ECAI unless—

(a) the ECAI has been nominated under subsection (2) in respect of that portfolio or type of exposures; and

(b) notice of that nomination has been given to the Monetary Authority under subsection (5).

(7) To avoid doubt, an authorized institution must, for the purposes of Part 4 or 7, treat as not having an ECAI rating any person or exposure that, although falling within an ECAI ratings based portfolio, does not have an ECAI rating assigned to it by an ECAI nominated under subsection (2) by the institution in respect of that portfolio or the type of exposures to which the exposure belongs.

(8) In this section—

ECAI ratings based portfolio (ECAI評級基準組合)—

(a) in relation to Part 4, has the meaning given by section 51(1);

(b) in relation to Part 7, means securitization exposures other than re-securitization exposures.

(L.N. 167 of 2023)

4D. Amendment of nomination

(1) An authorized institution may, with the prior consent of the Monetary Authority, amend a nomination made under section 4C(2) or further amend a nomination that has been amended previously under this section.

(2) Section 4C(3), (4), (5) and (6), with all necessary modifications, applies to a nomination to be amended, or amended, under this section as it applies to a nomination made under section 4C(2).

(L.N. 167 of 2023)

4E. Transitional provision in relation to nominations

(1) On and after the commencement date* of Part 3 of the Banking (Capital) (Amendment) Rules 2023, unless an authorized institution makes a new nomination under section 4C(2) for the following exposures, any nomination (and the corresponding notification to the Monetary Authority) or any amendment to a nomination (and the corresponding consent of the Monetary Authority) made in accordance with section 70 or 267(1)(a), as the case requires, as in force immediately before that date for those exposures remains in effect as if it were a nomination made under section 4C(2) or an amendment made under section 4D—

(a) sovereign exposures;

(b) public sector entity exposures;

(c) bank exposures;

(d) securitization exposures subject to the SEC-ERBA.

(2) To avoid doubt, a nomination made in accordance with section 70 as in force immediately before the commencement date of Part 3 of the Banking (Capital) (Amendment) Rules 2023 for the following exposures ceases to have effect on that date—

(a) securities firm exposures;

(b) corporate exposures.

(L.N. 167 of 2023)

Editorial Note:

* Commencement date: 1 January 2025.

Division 2—Prescribed Approaches to Calculation of Credit Risk for Non-securitization Exposures

5. Authorized institution shall only use STC approach, BSC approach or IRB approach to calculate its credit risk for non-securitization exposures

(1) Subject to section 16A, an authorized institution— *(L.N. 156 of 2012)*

(a) subject to paragraphs (b) and (c), shall use the STC approach to calculate its credit risk for non-securitization exposures;

(b) may use the BSC approach to calculate its credit risk for all of its non-securitization exposures only if it has the approval to do so under section 6(2)(a);

(c) may use the IRB approach to calculate its credit risk for non-securitization exposures only if it has the approval to do so under section 8(2)(a).

(2) Subsection (1) does not prevent an authorized institution from using any combination of the STC approach and IRB approach to calculate its credit risk for non-securitization exposures if that combination is expressly permitted by, and in accordance with, another provision of these Rules. *(L.N. 137 of 2011)*

(L.N. 167 of 2023)

6. Authorized institution may apply for approval to use BSC approach to calculate its credit risk for non-securitization exposures

(1) An authorized institution may apply to the Monetary Authority for approval to use the BSC approach to calculate its credit risk for all of its non-securitization exposures.

(2) Subject to subsection (3), the Monetary Authority shall determine an application under subsection (1) from an authorized institution by—

(a) granting approval to the institution to use the BSC approach to calculate its credit risk for all of its non-securitization exposures; or

(b) refusing to grant the approval.

(3) Without prejudice to the generality of subsection (2)(b), the Monetary Authority shall refuse to grant approval to an authorized institution to use the BSC approach to calculate its credit risk for all of its non-securitization exposures if any one or more of the requirements specified in section 7(a) are not satisfied with respect to the institution.

(4) *(Repealed L.N. 167 of 2023)*

(L.N. 167 of 2023)

7. Minimum requirements to be satisfied for approval under section 6(2)(a) to use BSC approach

An authorized institution which makes an application under section 6(1) to use the BSC approach shall demonstrate to the satisfaction of the Monetary Authority—

(a) that—

(i) at the end of the institution's financial year immediately preceding the date of the application, the institution and its consolidation group, if any, each had total assets, before deducting any specific provisions or collective provisions, of not more than $10 billion; and

(ii) there is no cause to believe that the use by the institution of the BSC approach to calculate its credit risk for all of its non-securitization exposures would not adequately identify, assess and reflect the credit risk of all of the institution's non-securitization exposures taking into account the nature of the institution's business. *(L.N. 167 of 2023)*

(b) *(Repealed L.N. 167 of 2023)*

8. Authorized institution may apply for approval to use IRB approach to calculate its credit risk for non-securitization exposures

(1) An authorized institution may apply to the Monetary Authority for approval to use the IRB approach for one or more IRB adoption classes to calculate its credit risk for non-securitization exposures.

(2) Subject to subsection (3) and section 9, the Monetary Authority shall determine an application under subsection (1) from an authorized institution by—

(a) granting approval to the institution to use the IRB approach for one or more IRB adoption classes to calculate its credit risk for non-securitization exposures; or

(b) refusing to grant the approval.

(3) Without prejudice to the generality of subsection (2)(b), the Monetary Authority shall refuse to grant approval to an authorized institution to use the IRB approach for one or more IRB adoption classes to calculate its credit risk for non-securitization exposures if any one or more of the requirements specified in Schedule 2 applicable to or in relation to the institution are not satisfied with respect to the institution.

(4) Where an authorized institution is granted an approval under subsection (2)(a) to use the IRB approach for one or more IRB adoption classes to calculate its credit risk for non-securitization exposures— *(L.N. 167 of 2023)*

(a) subject to sections 10(5)(a) and 12, the institution shall not, except with the prior consent of the Monetary Authority, use any approach other than the IRB approach to calculate its credit risk for non-securitization exposures within the IRB adoption class for which an approval is granted to use the IRB approach; and

(b) the institution shall not, without the prior consent of the Monetary Authority, make any significant change to any rating system which is the subject of the approval.

(L.N. 167 of 2023)

9. Circumstances in which Monetary Authority shall take into

account assessment outside Hong Kong of rating system used by authorized institution

(1) Where—

(a) an authorized institution uses a rating system which has been used by a bank incorporated outside Hong Kong to calculate the institution's credit risk for non-securitization exposures; and

(b) the bank is a member of a group of companies of which the institution is also a member,

the Monetary Authority shall, for the purposes of Schedule 2, take into account, insofar as is practicable and reasonable in all the circumstances of the case—

(c) subject to subsection (2), the assessment of the relevant banking supervisory authority of the bank as to the accuracy, verifiability, internal consistency and integrity of the rating system; and

(d) the appropriateness of the rating system for the purposes of assessing the credit risk characteristics of the institution's exposures.

(1A) In subsection (1)(a), a reference to a bank incorporated outside Hong Kong does not include a re-domiciled entity. *(14 of 2025 s. 178)*

(2) The Monetary Authority shall take into account the assessment referred to in subsection (1)(c) if, and only if, the Monetary Authority is satisfied that the capital adequacy standards adopted by the relevant banking supervisory authority for assessing credit risk under the IRB approach are not materially different from those set out in Part 6 and Schedule 2.

10. Measures which may be taken by Monetary Authority if authorized institution using BSC approach or IRB approach no

longer satisfies specified requirements

(1) Where—

(a) an authorized institution uses the BSC approach to calculate its credit risk for all of its non-securitization exposures; and

(b) the Monetary Authority is satisfied that—

(i) if the institution were to make a fresh application under section 6(1) for approval to use the BSC approach to calculate its credit risk for all of its non-securitization exposures, the approval would be refused by virtue of section 6(3); or

(ii) the institution has contravened a condition attached under section 33A(1) or (2) to its approval granted under section 6(2)(a), *(L.N. 137 of 2011)*

the Monetary Authority may, by notice in writing given to the institution, require the institution to use the STC approach to calculate its credit risk for all of its non-securitization exposures instead of the BSC approach.

(2) A notice given to an authorized institution under subsection (1) may require the institution to use the STC approach to calculate its credit risk for all of its non-securitization exposures, or such parts of its non-securitization exposures as specified in the notice, beginning on such date, or the occurrence of such event, as specified in the notice.

(3) An authorized institution shall comply with the requirements of a notice given to it under subsection (1).

(4) Where—

(a) an authorized institution uses the IRB approach to calculate its credit risk for non-securitization exposures; and

(b) the Monetary Authority is satisfied that—

(i) if the institution were to make a fresh application under section 8(1) for approval to use the IRB approach to calculate its credit risk for non-securitization exposures, the approval would be refused by virtue of section 8(3) (but, insofar as Schedule 2 is concerned, only section 1 of that Schedule is to be taken into account); or

(ii) the institution has contravened a condition attached under section 33A(1) or (2) to its approval granted under section 8(2)(a), *(L.N. 137 of 2011)*

the Monetary Authority may take one or more of the measures set out in subsection (5).

(5) The measures referred to in subsection (4) are that—

(a) the Monetary Authority may, by notice in writing given to the institution, require the institution to use the STC approach to calculate its credit risk for non-securitization exposures instead of the IRB approach in respect of its non-securitization exposures within all the IRB adoption classes for which an approval to use the IRB approach has been granted, or such parts of those non-securitization exposures as specified in the notice, beginning on such date, or the occurrence of such event, as specified in the notice;

(b) the Monetary Authority may, by notice in writing given to the institution, require the institution to—

(i) submit to the Monetary Authority a plan, within such period (being a period which is reasonable in all the circumstances of the case) as specified in the notice, which satisfies the Monetary Authority that, if it were implemented by the institution, the institution would cease to fall within subsection

(4)(b) within a period which is reasonable in all the circumstances of the case; and

(ii) implement the plan;

(c) the Monetary Authority may, by notice in writing given to the institution, advise the institution that the Monetary Authority is considering exercising the power under section 97F of the Ordinance to vary any capital requirement rule applicable to the institution, including by increasing all or any of the following—

(i) the institution's CET1 capital ratio;

(ii) the institution's Tier 1 capital ratio;

(iii) the institution's Total capital ratio; and *(L.N. 156 of 2012)*

(d) *(Repealed L.N. 167 of 2023)*

(e) the Monetary Authority may, by notice in writing given to the institution, require the institution to reduce its credit exposures in such manner, or adopt such measures, as specified in the notice which, in the opinion of the Monetary Authority, will cause the institution to cease to fall within subsection (4)(b) within a period which is reasonable in all the circumstances of the case, or will otherwise mitigate the effect of the institution falling within that subsection.

(6) An authorized institution shall comply with the requirements of a notice given to it under subsection (5)(a), (b) or (e).

(7) For the avoidance of doubt, it is hereby declared that—

(a) the requirements specified in Schedule 2 are also applicable to and in relation to an authorized institution using the IRB approach to calculate its credit risk in respect of the use by the institution of a rating system to which a significant change referred to in section 8(4)(b) relates (whether or not the institution has, in respect of that change, been given the prior consent referred to in section 8(4)(b)), and subsection (4)(b) and the other provisions of this section apply to the institution accordingly; and

(b) subsection (5)(c) does not operate to prejudice the generality of the circumstances in respect of which the Monetary Authority may exercise the power under section 97F of the Ordinance in the case of an authorized institution to which that subsection applies. *(L.N. 156 of 2012)*

(L.N. 167 of 2023)

10A. Authorized institution must only use SA-CCR approach etc. to calculate its counterparty credit risk

(L.N. 44 of 2020)

(1) Subject to subsections (2), (2A) and (5), an authorized institution must— *(L.N. 44 of 2020; L.N. 167 of 2023)*

(a) use the SA-CCR approach to calculate the institution's default risk exposures in respect of derivative contracts; and

(b) use the methods set out in Division 2B of Part 6A to calculate the institution's default risk exposures in respect of SFTs. *(L.N. 44 of 2020; L.N. 167 of 2023)*

(c) *(Repealed L.N. 167 of 2023)*

(2) An authorized institution may use the IMM(CCR) approach to calculate its default risk exposures in respect of derivative contracts, SFTs or long settlement transactions only if it has an IMM(CCR) approval for those contracts or transactions.

(2A) An authorized institution may use the current exposure method to calculate its default risk exposures in respect of derivative contracts if it uses the BSC approach to calculate its credit risk for non-securitization exposures. *(L.N. 44 of 2020)*

(2B) Despite subsection (2A), the Monetary Authority may, by written notice given to an authorized institution, require the institution to use the SA-CCR approach to calculate its default risk exposures if the Monetary Authority believes that, taking into account the nature of the institution's business, the use by the institution of the current exposure method would not adequately assess and reflect the counterparty credit risk incurred by the institution. *(L.N. 44 of 2020; L.N. 167 of 2023)*

(3)-(4) *(Repealed L.N. 167 of 2023)*

(5) Subsection (1) does not prevent an authorized institution from using—

(a) a combination of the SA-CCR approach and the IMM(CCR) approach; or

(b) a combination of the methods referred to in subsection (1)(b) and the IMM(CCR) approach,

to calculate the institution's default risk exposures if that combination is expressly permitted by, and in accordance with, another provision of these Rules.

(6) *(Repealed L.N. 167 of 2023)*

(7) An authorized institution must comply with the requirements of a notice given to it under subsection (2B). *(L.N. 167 of 2023)*

(8) Subsections (1), (2), (2A), (2B), (5) and (7) apply to an authorized institution regardless of whether the contracts or transactions concerned are booked in the institution's banking book or trading book. *(L.N. 167 of 2023)*

(L.N. 156 of 2012; L.N. 44 of 2020)

10B. Authorized institution may apply for approval to use IMM(CCR) approach to calculate its default risk exposures

(1) An authorized institution may apply to the Monetary Authority for approval to use the IMM(CCR) approach to calculate its default risk exposures in respect of contracts or transactions falling within any one or more of the following categories— *(L.N. 167 of 2023)*

(a) derivative contracts (other than long settlement transactions);

(b) SFTs (other than long settlement transactions);

(c) long settlement transactions.

(2) Subject to subsection (3), the Monetary Authority must determine an application under subsection (1) from an authorized institution by—

(a) granting approval to the institution to use the IMM(CCR) approach to calculate its default risk exposures in respect of—

(i) the categories of contracts or transactions specified in the application; or

(ii) any categories of contracts or transactions that the Monetary Authority specifies in the approval; or

(b) refusing to grant the approval (whether in whole or in part).

(3) Without limiting subsection (2)(b), the Monetary Authority must refuse to grant an approval to an authorized institution to use the IMM(CCR) approach if any one or more of the requirements specified in Schedule 2A applicable to or in relation to the institution are not satisfied with respect to the institution.

(4) Subject to subsections (5) and (7), an authorized institution that has an IMM(CCR) approval must use the IMM(CCR) approach to calculate its default risk exposures in respect of all contracts and transactions that are covered by the approval.

(5) Subject to subsection (6), the Monetary Authority may specify, in an IMM(CCR) approval granted to an authorized institution, a transitional period in which the institution is permitted to use the SA-CCR approach or the methods set out in Division 2B of Part 6A to calculate its default risk exposures for contracts or transactions in respect of a portion of its business that are covered by the IMM(CCR) approval. *(L.N. 44 of 2020)*

(6) The Monetary Authority may specify the transitional period referred to in subsection (5) only if the authorized institution concerned has submitted to the Monetary Authority a plan for fully implementing, within a period that is reasonable in all the circumstances of the case, the IMM(CCR) approach for all contracts or transactions covered by the IMM(CCR) approval.

(7) An authorized institution may choose to use the SA-CCR approach or the methods set out in Division 2B of Part 6A to calculate its default risk exposures for certain contracts or transactions that are covered by the IMM(CCR) approval if the institution demonstrates to the satisfaction of the Monetary Authority that its total default risk exposures to those contracts or transactions are immaterial. *(L.N. 44 of 2020)*

(8) An authorized institution that has an IMM(CCR) approval must, for contracts or transactions that are not covered by the IMM(CCR) approval, calculate its default risk exposures in respect of those contracts or transactions in accordance with section 10A(1).

(9) Where an authorized institution uses the IMM(CCR) approach to calculate its default risk exposures, the institution must not, without the prior consent of the Monetary Authority—

(a) make any significant change to any internal model that is the subject of the institution's IMM(CCR) approval; or

(b) switch to using the SA-CCR approach, the current exposure method or any of the methods set out in Division 2B of Part 6A. *(L.N. 44 of 2020)*

(10) Subject to section 10D, an approval granted under subsection (2)(a) before the commencement date* of Part 3 of the Banking (Capital) (Amendment) Rules 2023 for an authorized institution to use the IMM(CCR) approach to calculate its default risk exposures in respect of the categories of contracts or transactions specified in the approval remains in force on and after that date. *(L.N. 167 of 2023)*

(L.N. 156 of 2012)

Editorial Note:

* Commencement date: 1 January 2025.

10C. *(Repealed L.N. 167 of 2023)*

10D. Measures that may be taken by Monetary Authority if authorized institution using IMM(CCR) approach no longer satisfies specified requirements

(1) The Monetary Authority may take one or more of the measures set out in subsections (2), (3), (4), (5) and (6) in respect of an authorized institution that is using the IMM(CCR) approach if the Monetary Authority determines that—

(a) the institution no longer satisfies any one or more of the requirements specified in Schedule 2A applicable to or in relation to the institution;

(b) the institution has contravened a condition attached under section 33A(1) or (2) to its IMM(CCR) approval; or

(c) the institution fails to fully implement the IMM(CCR) approach within the period specified, under section 10B(6), in the IMM(CCR) approval.

(2) The Monetary Authority may, by notice in writing given to the authorized institution, require the institution to—

(a) use the SA-CCR approach or the methods set out in Division 2B of Part 6A, instead of the IMM(CCR) approach, to calculate its default risk exposures, *(L.N. 44 of 2020; L.N. 167 of 2023)*

(b) *(Repealed L.N. 167 of 2023)*

in respect of the contracts or transactions as specified in the notice, beginning on the date, or the occurrence of the event, specified in the notice.

(3) The Monetary Authority may, by notice in writing given to the authorized institution, require the institution to—

(a) submit to the Monetary Authority a plan, within the period specified in the notice (being a period that is reasonable in all the circumstances of the case), that satisfies the Monetary Authority that, if it were implemented by the institution, the institution would cease to fall within subsection (1) within a period that is reasonable in all the circumstances of the case; and

(b) implement the plan.

(4) The Monetary Authority may, by notice in writing given to the authorized institution, advise the institution that the

Monetary Authority is considering exercising the power under section 97F of the Ordinance to vary any capital requirement rule applicable to the institution, including by increasing all or any of the following—

(a) the institution's CET1 capital ratio;

(b) the institution's Tier 1 capital ratio;

(c) the institution's Total capital ratio.

(5) The Monetary Authority may, by notice in writing given to the authorized institution, require the institution to calculate its default risk exposures by the use of a higher α (within the meaning of section 226E(1)) specified in the notice.

(6) The Monetary Authority may, by notice in writing given to the authorized institution, require the institution to reduce its counterparty credit risk exposures in any manner, or to adopt any measures, specified in the notice that, in the opinion of the Monetary Authority, will cause the institution to cease to fall within subsection (1) within a period that is reasonable in all the circumstances of the case, or will otherwise mitigate the effect of the institution falling within that subsection.

(7) An authorized institution must comply with the requirements of a notice given to it under subsection (2), (3), (5) or (6).

(8) To avoid doubt—

(a) the requirements specified in Schedule 2A are also applicable to and in relation to an authorized institution using the IMM(CCR) approach in respect of an internal model to which a significant change referred to in section 10B(9)(a) relates (whether or not the institution has, in respect of that change, been given the prior consent referred to in that section) and the other provisions of this section apply accordingly; and

(b) subsection (4) does not operate to prejudice the generality of the circumstances in which the Monetary Authority may exercise the power under section 97F of the Ordinance in respect of an authorized institution to which that subsection applies.

(L.N. 156 of 2012)

Division 3—Specific Requirements relating to Use of IRB Approach

11. Adoption of IRB approach

(1) When an authorized institution applies to the Monetary Authority under section 8(1) for approval to use the IRB approach, the institution must—

(a) submit an implementation plan agreed with the Monetary Authority that specifies to what extent and when the institution intends to use the IRB approach to calculate its credit risk for non-securitization exposures; and

(b) subject to subsection (2), choose one or more IRB adoption classes set out in Table 1AAB for which the institution applies to use the IRB approach to calculate its credit risk for non-securitization exposures.

Table 1AAB

IRB Adoption Classes

Column 1 Item	Column 2 IRB adoption class	Column 3 IRB class covered	Column 4 IRB subclass covered
1.	Corporate—other than specialized lending	Corporate exposures	(a) Small and medium-sized corporates (b) Large corporates (c) Financial institutions treated as corporates (d) Other corporates
2.	Corporate—specialized lending	Corporate exposures	(a) Specialized lending (project finance) (b) Specialized lending (object finance) (c) Specialized lending (commodity finance)

Column 1 Item	Column 2 IRB adoption class	Column 3 IRB class covered	Column 4 IRB subclass covered
			(d) Specialized lending (income-producing real estate) (e) Specialized lending (high-volatility commercial real estate)
3.	Sovereign	Sovereign exposures	(a) Sovereigns (b) Sovereign foreign public sector entities (c) Multilateral development banks
4.	Bank	Bank exposures	(a) Banks (excluding covered bonds)

Column 1 Item	Column 2 IRB adoption class	Column 3 IRB class covered	Column 4 IRB subclass covered
			(b) Qualifying non-bank financial institutions
			(c) Public sector entities (excluding sovereign foreign public sector entities)
			(d) Unspecified multilateral bodies
			(e) Covered bonds
5.	Retail—qualifying revolving retail exposures	Retail exposures	(a) Qualifying revolving retail exposures (transactor)

Column 1 Item	Column 2 IRB adoption class	Column 3 IRB class covered	Column 4 IRB subclass covered
			(b) Qualifying revolving retail exposures (revolver)
6.	Retail—residential mortgages	Retail exposures	(a) Residential mortgages to individuals (b) Residential mortgages to property-holding shell companies
7.	Retail—others	Retail exposures	(a) Small business retail exposures (b) Other retail exposures to individuals

Column 1 Item	Column 2 IRB adoption class	Column 3 IRB class covered	Column 4 IRB subclass covered
8.	CIS	CIS exposures	CIS exposures
9.	Others	Other exposures	(a) Cash items (b) Other items

(2) An authorized institution must not choose only the IRB adoption class of "Others" to apply for the use of the IRB approach to calculate its credit risk for exposures falling within the IRB class of "Other exposures".

(3) Subject to section 12, if an authorized institution uses the IRB approach to calculate its credit risk for an IRB adoption class, the institution must use the IRB approach to calculate its credit risk for all exposures that fall within that IRB adoption class.

(4) In this section, the following expressions have the meanings given to them by section 139(1)—

(a) cash items;

(b) corporate;

(c) financial institution treated as corporate;

(d) specialized lending.

(L.N. 167 of 2023)

12. Exemption for exposures

(1) An authorized institution which has made an application

under section 8(1) to use, or which uses, the IRB approach to calculate its credit risk for non-securitization exposures (referred to in this section as ***relevant calculation***) may apply to the Monetary Authority to have such of its non-securitization exposures as specified in the application exempted from inclusion in the relevant calculation. *(L.N. 137 of 2011)*

(2) The Monetary Authority shall determine an application under subsection (1) from an authorized institution by— *(L.N. 167 of 2023)*

(a) exempting from inclusion in the relevant calculation—

(i) the exposures in an IRB adoption class which are specified in the application; or

(ii) the exposures falling within a business unit which are specified in the application,

if the institution demonstrates to the satisfaction of the Monetary Authority that—

(iii) it is not practicable for the institution to include the exposures referred to in subparagraph (i) or (ii), as the case may be, in the relevant calculation; and

(iv) the exemption will not materially prejudice the calculation of the institution's regulatory capital for credit risk; or

(b) refusing to grant the exemption.

(3) An authorized institution to which an exemption under subsection (2)(a) is granted—

(a) shall use the STC approach to calculate its credit risk for non-securitization exposures to which the exemption relates.

(b) *(Repealed L.N. 167 of 2023)*

(4) *(Repealed L.N. 167 of 2023)*

(5) Where—

(a) an authorized institution is granted an exemption (referred to in this subsection as ***existing exemption***) under subsection (2)(a); and

(b) the institution is at any time thereafter satisfied that if it were to make a fresh application under subsection (1) for an exemption (referred to in this subsection as ***new exemption***) in respect of the exposures to which the existing exemption relates, the new exemption would be, or may be, refused by virtue of subsection (2),

the institution shall, as soon as is practicable after it is so satisfied, give notice in writing to the Monetary Authority of the case.

(L.N. 167 of 2023)

13. Revocation of exemption under section 12

(1) Where—

(a) an authorized institution uses the STC approach to calculate its credit risk for certain non-securitization exposures to which an exemption under section 12(2)(a) relates; and

(b) the Monetary Authority is satisfied that, if the institution were to make a fresh application under section 12(1) for an exemption in respect of those non-securitization exposures, the exemption would be refused by virtue of section 12(2),

the Monetary Authority may take one or more of the measures set out in subsection (2).

(2) The measures referred to in subsection (1) are that—

(a) if the fresh application referred to in subsection (1)(b) would be refused by virtue of section 12(2), the Monetary Authority may, by notice in writing given to the institution, require the institution to—

(i) submit to the Monetary Authority a plan, within such period (being a period which is reasonable in all the circumstances of the case) as specified in the notice, which satisfies the Monetary Authority that, if it were implemented by the institution, the institution would be able to use the IRB approach to calculate its credit risk for those non-securitization exposures within a period which is reasonable in all the circumstances of the case; and

(ii) implement the plan; and

(b) *(Repealed L.N. 167 of 2023)*

(c) the Monetary Authority may, by notice in writing given to the institution, revoke the exemption on such date, or the occurrence of such event, as specified in the notice.

(3) An authorized institution shall comply with the requirements of a notice given to it under subsection (2)(a).

(4) For the avoidance of doubt, it is hereby declared that an authorized institution's compliance with a requirement referred to in subsection (2)(a) does not prejudice the generality of the Monetary Authority's power under subsection (2)(c).

(L.N. 167 of 2023)

14. *(Repealed L.N. 167 of 2023)*

Division 4—Prescribed Approaches to Calculation of Credit Risk for Securitization Exposures

15. Authorized institution must use SEC-IRBA, SEC-ERBA, SEC-SA or SEC-FBA to determine risk-weight of securitization exposure

(1) An authorized institution must use the SEC-IRBA to determine the risk-weight of a securitization exposure to a securitization transaction that is not a re-securitization exposure if—

(a) the pool of underlying exposures of the transaction is classified as an IRB pool; or

(b) all of the following conditions are met—

(i) the pool of underlying exposures of the transaction is classified as a mixed pool;

(ii) the institution is able to calculate the K_{IRB} in accordance with section 254(1) for at least 95% of the total nominal amount of the underlying exposures.

(2) If—

(a) an authorized institution is to determine the risk-weight of a securitization exposure to a securitization transaction; and

(b) the securitization exposure has—

(i) an ECAI issue specific rating issued by an ECAI nominated by the institution under section 4C for the purposes of Part 7; or *(L.N. 167 of 2023)*

(ii) if subparagraph (i) does not apply, an inferred rating,

then, subject to subsection (2B), the institution must use the SEC-ERBA to determine the risk-weight of the securitization exposure based on that rating if all of the conditions specified in subsection (2A) are met. *(L.N. 222 of 2018)*

(2A) The conditions specified for subsection (2) are—

(a) the securitization exposure is not a re-securitization exposure; and

(b) either—

(i) the pool of underlying exposures of the securitization transaction is classified as an SA pool; or

(ii) both of the following conditions are met—

(A) the pool of underlying exposures of the securitization transaction is classified as a mixed pool;

(B) the institution is unable to calculate the K_{IRB} in accordance with section 254(1) for at least 95% of the total nominal amount of the underlying exposures. *(L.N. 222 of 2018)*

(2B) If—

(a) an authorized institution having an IAA approval is to determine the risk-weight of a securitization exposure to a securitization transaction; and

(b) the securitization exposure—

(i) does not have an ECAI issue specific rating issued by an ECAI nominated by the institution under section 4C for the purposes of Part 7; but *(L.N. 167 of 2023)*

(ii) has an internal credit rating,

then, subject to subsection (2C), the institution may determine the risk-weight of the securitization exposure by using the SEC-ERBA based on the internal credit rating in accordance with section 266A if the securitization exposure is an eligible ABCP exposure and falls within a category of securitization exposures covered by the institution’s IAA approval. *(L.N. 222 of 2018)*

(2C) Subsection (2B) does not apply to an authorized institution in determining the risk-weight of a securitization exposure if—

(a) the institution’s IAA approval has attached to it under section 33A(1) or (2) any condition that prohibits the institution from using the IAA to determine the risk-weight of the exposure; or

(b) a notice issued by the Monetary Authority under section 15D has the effect of prohibiting the institution from using the IAA to determine the risk-weight of the exposure. *(L.N. 222 of 2018)*

(3) An authorized institution must use the SEC-SA to determine the risk-weight of a securitization exposure to a securitization transaction if—

(a) the securitization exposure is unrated and the pool of underlying exposures of the transaction is classified as an SA pool;

(b) all of the following conditions are met—

(i) the securitization exposure is unrated and the pool of underlying exposures of the transaction is classified as a mixed pool;

(ii) the institution is unable to calculate the K_{IRB} in accordance with section 254(1) for at least 95% of the total nominal amount of the underlying exposures; *(L.N. 222 of 2018)*

(c) the securitization exposure is a re-securitization exposure (whether rated or not); or *(L.N. 222 of 2018)*

(d) the institution is required to do so pursuant to a notice under section 15D given to it by the Monetary Authority. *(L.N. 222 of 2018)*

(4) Despite subsections (1), (2), (2B) and (3), an authorized institution must use the SEC-FBA to determine the risk-weight of a securitization exposure to a securitization transaction if— *(L.N. 222 of 2018)*

(a) any of the due diligence requirements in section 15A is not complied with in respect of the exposure or the transaction; *(L.N. 222 of 2018)*

(b) the institution is unable to use the SEC-IRBA, SEC-ERBA and SEC-SA to determine the risk-weight; or *(L.N. 222 of 2018)*

(c) the institution is required to do so pursuant to a notice under section 15D given to it by the Monetary Authority. *(L.N. 222 of 2018)*

(L.N. 175 of 2017)

15A. Due diligence requirements for using SEC-IRBA, SEC-ERBA or SEC-SA

(1) The due diligence requirements for the purposes of section 15(4)(a) are set out in subsections (2), (3) and (4).

(2) The authorized institution concerned must have a comprehensive understanding, on a continuous basis, of the risk characteristics of—

(a) the securitization exposure concerned (whether on-balance sheet or off-balance sheet); and

(b) the pool of underlying exposures of the securitization transaction that gave rise to the securitization exposure.

(3) The institution must be able to access the following information on a continuous basis and in a timely manner—

(a) if the transaction is not a re-securitization transaction—performance information on the underlying exposures (including issuer name and credit quality); and

(b) if the transaction is a re-securitization transaction—

(i) performance information on the underlying exposures (including issuer name and credit quality); and

(ii) information on the risk characteristics and performance of the underlying exposures of the original securitization transaction being re-securitized through the re-securitization transaction.

(4) The institution must have a thorough understanding of each structural feature of the transaction that has the potential to materially affect the performance of the securitization exposure referred to in subsection (2).

(L.N. 175 of 2017)

15B. Meaning of *eligible ABCP exposure*

For the purposes of these Rules, a securitization exposure of an authorized institution having an IAA approval (***specified exposure***) is an eligible ABCP exposure if all of the following criteria are met—

(a) the specified exposure is an exposure to an ABCP programme (***ABCP programme***);

(b) one of the following persons is the sponsor of the ABCP programme—

(i) the institution;

(ii) a member of a group of entities of which the ultimate holding company is the same as that of the institution;

(c) the ABCP programme has in place—

(i) adequate and prudent standards on the underwriting and structuring of asset purchase transactions; and

(ii) adequate and prudent policies, processes and structural features for assessing, controlling and mitigating risks associated with underlying exposures and other parties involved such as sellers of the underlying exposures and servicers;

(d) the sponsor of the ABCP programme has an adequate and prudent policy on selecting ECAIs to assign ECAI ratings to debt securities to be issued under the ABCP programme;

(e) there is an ECAI issue specific rating assigned to each of the debt securities with an original maturity of one year or less issued under the ABCP programme by an ECAI that has been nominated by the institution under section 4C for the purposes of Part 7; *(L.N. 167 of 2023)*

(f) the circumstances of the institution and the specified exposure are such that if all of the senior debt securities issued under the ABCP programme were held by the institution—

(i) the debt securities would be required by section 15 to be risk-weighted by the institution by using the SEC-ERBA based on the ECAI issue specific ratings of the debt securities if section 267(4) did not exist; or

(ii) if the debt securities would overlap with the specified exposure or other securitization exposures of the institution to the ABCP programme—the debt securities would be required by section 15 to be so risk-weighted if sections 239 and 267(4) did not exist;

(g) the specified exposure is not a re-securitization exposure;

(h) the specified exposure is backed by a pool of underlying exposures that is classified as an SA pool;

(i) the institution, if it did not have an IAA approval, would be required by section 15 to determine the risk-weight of the specified exposure by using the SEC-ERBA based on an inferred rating of the specified exposure (if such a rating is available) or by using the SEC-SA;

(j) the initial internal credit rating assigned to the specified exposure by the institution in accordance with the approved internal assessment process is at least equivalent to an ECAI issue specific rating that maps to—

(i) a credit quality grade of 1, 2, 3, 4, 5, 6, 7, 8, 9 or 10 in the LT ECAI rating mapping table made by the Monetary Authority under section 4B(2)(c) for securitization exposures; or

(ii) a credit quality grade of 1, 2 or 3 in the ST ECAI rating mapping table made by the Monetary Authority under section 4B(2)(c) for securitization exposures. *(L.N. 167 of 2023)*

(L.N. 222 of 2018)

15C. Authorized institution may apply for approval to use IAA to determine risk-weight of eligible ABCP exposure

(1) An authorized institution that has obtained the Monetary Authority's approval under section 8 to use the IRB approach to calculate its credit risk for non-securitization exposures may make an application to the Monetary Authority for approval to use the IAA to determine the risk-weights of its eligible ABCP exposures (***application***).

(2) Subject to subsection (3), the Monetary Authority must determine the application by—

(a) granting approval to the institution to use the IAA to determine the risk-weights of its eligible ABCP exposures falling within—

(i) the categories of securitization exposures specified in the application; or

(ii) any categories of securitization exposures that the Monetary Authority specifies in the approval; or

(b) refusing to grant the approval (whether in whole or in part).

(3) Without limiting subsection (2)(b), the Monetary Authority must refuse to grant an approval to an authorized institution to use the IAA unless the institution satisfies the Monetary Authority that the institution, and its internal assessment process that is the subject of the application, are subject to an appropriate governance and risk management framework (***framework***) which ensures at all times that—

(a) there is effective oversight of the internal assessment process and other related activities of the institution;

(b) the rating methodologies used for assessing the institution's securitization exposures to an ABCP programme are—

(i) prudent; and

(ii) appropriate to the characteristics of the ABCP programme;

(c) there are adequate and prudent policies, procedures and internal controls for ensuring that—

(i) the internal assessment process is risk-sensitive and robust; and

(ii) requirements under these Rules, for the time being in force in respect of the use of the IAA, are complied with; and

(d) there are regular and independent reviews conducted by qualified persons to assess the adequacy and validity of the internal assessment process and its outputs.

(4) An authorized institution having an IAA approval must not, without the prior consent of the Monetary Authority, make any significant change to the framework in respect of elements that are relevant to ensuring at all times that the descriptions in subsection (3)(a), (b), (c) and (d) are met.

(L.N. 222 of 2018)

15D. Measures that may be taken by Monetary Authority if authorized institution using IAA no longer satisfies specified requirements

(1) The Monetary Authority may take one or more of the measures set out in this section in respect of an authorized institution that has an IAA approval if the Monetary Authority determines that—

(a) the governance and risk management framework that the institution and its internal assessment process are subject to has ceased to be capable of ensuring at all times that the descriptions in section 15C(3)(a), (b), (c) and (d) are met, or the institution has contravened section 15C(4);

(b) the institution has contravened a condition attached under section 33A(1) or (2) to its IAA approval; or

(c) the institution has used the IAA to determine the risk-weight of a securitization exposure—

(i) that is not an eligible ABCP exposure; or

(ii) that is an eligible ABCP exposure but does not fall within a category of securitization exposures covered by the institution's IAA approval.

(2) The Monetary Authority may, by notice in writing given to the institution, require the institution to use the SEC-SA or the SEC-FBA, instead of the IAA, to determine the risk-weights of the securitization exposures or categories of securitization exposures specified in the notice, during the period or beginning on the date or on the occurrence of an event specified in the notice.

(3) The Monetary Authority may, by notice in writing given to the institution, require the institution to adopt one or more than one measure within the period specified in the notice (being a period that is reasonable in all the circumstances of the case) that, in the opinion of the Monetary Authority—

(a) will cause the institution to cease to fall within subsection (1) within a period that is reasonable in all the circumstances of the case; or

(b) will otherwise mitigate the effect of the institution falling within subsection (1).

(4) An authorized institution must comply with the requirements of a notice given to it under subsection (2) or (3).

(L.N. 222 of 2018)

16. Classification of underlying exposures

(1) An authorized institution must classify the pool of underlying exposures of a securitization transaction in accordance with this section.

(2) Subject to subsection (5), the institution must classify the pool of underlying exposures of a securitization transaction as an IRB pool if—

(a) all the underlying exposures in the pool are IRB underlying exposures; and

(b) the institution has all the data and information necessary for calculating the risk-weighted amounts of all the IRB underlying exposures in accordance with Part 6.

(3) The institution must classify the pool of underlying exposures of a securitization transaction as a mixed pool if—

(a) some or all of the underlying exposures in the pool are IRB underlying exposures; and

(b) the institution has all the data and information necessary for calculating the risk-weighted amounts of some, but not all, of the underlying exposures in the pool in accordance with Part 6.

(4) The institution must classify the pool of underlying exposures of a securitization transaction as an SA pool if—

(a) the institution uses, or if the underlying exposures were held directly by the institution, it would use, the STC approach or BSC approach to calculate the credit risk for all the underlying exposures in the pool;

(b) some or all of the underlying exposures in the pool are IRB underlying exposures, but the institution is unable to calculate the risk-weighted amount of any of the IRB underlying exposures in accordance with Part 6 due to a lack of necessary data and information;

(c) the securitization transaction is a re-securitization transaction; or

(d) the institution is required by a notice given to it under subsection (5) to do so.

(5) Even if the conditions in subsection (2)(a) and (b) are met, the Monetary Authority may, by notice in writing given to the institution, require it to classify the pool of underlying exposures as an SA pool if the Monetary Authority considers that the classification of the pool as an IRB pool would

result in a less prudent estimate of the capital charge for the institution's securitization exposure to the transaction given—

(a) the particular structure of the transaction; or

(b) the characteristics of the underlying exposures of the transaction.

(6) An authorized institution must comply with the requirement of a notice given to it under subsection (5).

(7) In this section—

IRB underlying exposures (IRB組成項目) means underlying exposures that fall, or would fall if they were held directly by the authorized institution concerned, within an IRB class or IRB subclass for which the institution has an approval granted under section 8 to use the IRB approach to calculate the credit risk.

(L.N. 175 of 2017)

Division 4A—Calculation of Credit Risk for Exposures to CCPs, etc.

(Division 4A added L.N. 156 of 2012)

16A. Authorized institution must use Division 4 of Part 6A to calculate its credit risk for exposures to CCPs, etc.

An authorized institution must calculate in accordance with Division 4 of Part 6A—

(a) its credit risk for exposures to CCPs in respect of derivative contracts and SFTs cleared by the CCPs and, if the institution is a clearing member of any CCP, its credit risk for exposures to that CCP arising from its default fund contributions to that CCP;

(b) its credit risk for exposures to clearing members in respect of CCP-related transactions and offsetting transactions; *(L.N. 44 of 2020)*

(c) its credit risk for exposures to direct clients, or higher level clients or lower level clients within multi-level client structures, in respect of CCP-related transactions and offsetting transactions; *(L.N. 44 of 2020)*

(ca) its credit risk for exposures to direct clients in respect of guarantees of the clients' performance under transactions or contracts cleared by CCPs; and *(L.N. 44 of 2020)*

(d) its credit risk for exposures to persons who hold the collateral posted by the institution in respect of transactions or contracts cleared by CCPs.

Division 5—Prescribed Approaches to Calculation of Market Risk Capital Charge

(L.N. 167 of 2023)

17. Authorized institution must use STM approach, SSTM approach or IMA to calculate its market risk capital charge

(1) An authorized institution (other than an authorized institution exempted under section 22(1))—

(a) subject to paragraphs (b) and (c), must use the STM approach to calculate its market risk capital charge;

(b) may use the SSTM approach to calculate its market risk capital charge if it has approval to do so under section 17A; and

(c) subject to sections 18(7), 19 and 19A, may use the IMA to calculate its market risk capital charge in respect of any trading desk for which it has an approval under section 18(2)(a).

(2) Subsection (1) does not prevent an authorized institution from using a combination of the STM approach and the IMA to calculate its market risk capital charge in accordance with another provision of these Rules that expressly permits that combination.

(3) An authorized institution must not use either of the following to calculate its market risk capital charge—

(a) a combination of the STM approach and the SSTM approach;

(b) a combination of the SSTM approach and the IMA.

(L.N. 167 of 2023)

17A. Approval for authorized institution to use SSTM approach to calculate its market risk capital charge

(1) An authorized institution may apply to the Monetary Authority for approval to use the SSTM approach to calculate its market risk capital charge.

(2) Subject to subsections (3) and (4), the Monetary Authority must determine an application from an authorized institution under subsection (1) by—

(a) granting approval to the institution to use the SSTM approach to calculate its market risk capital charge; or

(b) refusing to grant the approval.

(3) Subject to subsection (4), the Monetary Authority may grant approval to an authorized institution to use the SSTM approach to calculate its market risk capital charge if the institution demonstrates to the satisfaction of the Monetary Authority that—

(a) the institution's risk-weighted amount for market risk under the SSTM approach—

(i) does not exceed $1 billion on a permanent basis; and

(ii) does not exceed 2% of its total risk-weighted assets on a permanent basis;

(b) the aggregate notional amount of non-centrally cleared derivatives (including both banking book and trading book positions) does not exceed $6 trillion on a permanent basis;

(c) the institution is not a G-SIB, a D-SIB or a subsidiary of a G-SIB; and

(d) the institution does not hold a CTP.

(4) The Monetary Authority may refuse to grant approval to an authorized institution that meets the criteria set out in subsection (3) if the Monetary Authority considers that it is prudent to do so, having regard to the complexity and size of the risks in any of the institution's risk classes.

(5) The Monetary Authority must specify in an approval under this section the date on which the approval takes effect.

(6) If an approval under this section for an authorized institution is in effect, the institution must give written notice to the Monetary Authority if the institution—

(a) no longer on a permanent basis fulfils all of the criteria set out in subsection (3); or

(b) expects that any of those criteria will not be fulfilled.

(7) In this section—

D-SIB has the meaning given by section 3E(1);

G-SIB has the meaning given by section 3E(1).

(L.N. 167 of 2023)

17B. Revocation of approval for authorized institution to use SSTM

approach to calculate its market risk capital charge

The Monetary Authority may, by written notice given to an authorized institution, revoke an approval granted to the institution under section 17A if—

(a) the Monetary Authority is satisfied that, if the approval were not in effect and the institution were to make a fresh application under section 17A(1), that application would be refused; or

(b) the institution has given the Monetary Authority a notice under section 17A(6).

(L.N. 167 of 2023)

18. Approval for authorized institution to use IMA to calculate its market risk capital charge in respect of trading desks

(1) An authorized institution may apply to the Monetary Authority for approval to use the IMA to calculate its market risk capital charge in respect of any one or more trading desks.

(2) Subject to subsections (3), (4) and (5), the Monetary Authority must determine an application from an authorized institution under subsection (1) by—

(a) granting approval to the institution to use the IMA to calculate its market risk capital charge in respect of any one or more trading desks specified in the approval; or

(b) refusing to grant the approval.

(3) The Monetary Authority may grant approval to an authorized institution if, following the approval, at least 10% of its aggregate market risk capital charges will be based on positions held on trading desks referred to in the approval.

(4) The Monetary Authority must refuse to grant approval in respect of a trading desk that holds—

(a) securitization exposures; or

(b) equity investments in a collective investment scheme that cannot be looked through but are assigned to the trading book.

(5) The Monetary Authority must refuse to grant approval to an authorized institution if any one or more of the requirements in Schedule 3 applicable to the institution are not satisfied.

(6) The Monetary Authority must specify in an approval the date on which, or an event on the occurrence of which, the approval takes effect.

(7) An authorized institution that uses the IMA to calculate its market risk capital charge in respect of any one or more trading desks—

(a) must not, without the prior consent of the Monetary Authority, make any change to the core model documentation that is the subject of the approval granted to the institution;

(b) must also calculate its market risk capital charge using the STM approach in respect of each trading desk for which it uses the IMA; and

(c) must also calculate its market risk capital charge using the STM approach across all trading desks.

(8) In this section—

approval (批准) means an approval under subsection (2)(a);

core model documentation (核心模式文件) means the core model documentation referred to in section 1(1)(d)(i) of Schedule 3.

(L.N. 167 of 2023)

18A. *(Repealed L.N. 167 of 2023)*

19. Measures which may be taken by Monetary Authority if

authorized institution using IMA no longer satisfies specified requirements

(L.N. 167 of 2023)

(1) The Monetary Authority may take one or more of the measures set out in subsection (2) in relation to an authorized institution that uses the IMA to calculate its market risk capital charge in respect of one or more trading desks if the Monetary Authority is satisfied that—

(a) if the approval under section 18(2)(a) were not in effect and the institution were to make a fresh application under section 18(1)—the application would be refused because of section 18(5);

(b) the institution has contravened a condition attached under section 33A(1) or (2) to its approval under section 18(2)(a); or

(c) an internal model falls into the back-testing red zone referred to in item 7 of Table 32A. *(L.N. 167 of 2023)*

(2) The measures referred to in subsection (1) are that—

(a) the Monetary Authority may, by written notice given to the institution, require the institution to use the STM approach instead of the IMA to calculate its market risk capital charge in respect of the trading desks specified in the notice beginning on a date, or on the occurrence of an event, as specified in the notice; *(L.N. 167 of 2023)*

(b) the Monetary Authority may, by notice in writing given to the institution, require the institution to—

(i) submit to the Monetary Authority a plan, within such period (being a period which is reasonable in all the circumstances of the case) as specified in the notice, which satisfies the Monetary Authority that, if it were implemented by the institution, the institution would cease to fall within subsection (1)(a), (b) or (c) within a period which is reasonable in all the circumstances of the case; and

(ii) implement the plan;

(c) the Monetary Authority may, by notice in writing given to the institution, advise the institution that the Monetary Authority is considering exercising the power under section 97F of the Ordinance to vary any capital requirement rule applicable to the institution, including by increasing all or any of the following—

(i) the institution's CET1 capital ratio;

(ii) the institution's Tier 1 capital ratio;

(iii) the institution's Total capital ratio; *(L.N. 156 of 2012)*

(d) the Monetary Authority may, by notice in writing given to the institution, require the institution to calculate its market risk capital charge by the use of such higher multiplication factor as specified in the notice in accordance with section 322E(3); and

(e) the Monetary Authority may, by notice in writing given to the institution, require the institution to reduce its market risk exposures in such manner, or to adopt such measures, specified in the notice which, in the opinion of the Monetary Authority, will cause the institution to cease to fall within subsection (1)(a), (b) or (c) within a period which is reasonable in all the circumstances of the case, or will otherwise mitigate the effect of the institution falling within that subsection. *(L.N. 167 of 2023)*

(3) An authorized institution shall comply with the requirements of a notice given to it under subsection (2)(a), (b), (d) or (e).

(4) For the avoidance of doubt, it is hereby declared that—

(a) the requirements specified in Schedule 3 are also applicable to and in relation to an authorized institution using the IMA to calculate its market risk capital charge in respect of the use by the institution of an internal model to which a change of the core model documentation referred to in section 18(7)(a) relates (whether or not the institution has, in respect of that change, been given the prior consent required by that section), and subsection (1) and the other provisions of this section apply to the institution accordingly; and *(L.N. 167 of 2023)*

(b) subsection (2)(c) does not operate to prejudice the generality of the circumstances in respect of which the Monetary Authority may exercise the power under section 97F of the Ordinance in the case of an authorized institution to which that subsection applies. *(L.N. 156 of 2012)*

19A. Authorized institution that has approval to use IMA must use STM approach in certain circumstances

(1) This section applies if a trading desk in respect of which an authorized institution has an approval under section 18(2)(a)—

(a) no longer fulfils the back-testing requirements under section 322G(1); or

(b) at any time on or after the first anniversary of the day on which section 322G comes into operation*, is assigned to the red zone in the profit and loss attribution test under section 322G(3).

(2) The institution must use the STM approach to calculate its market risk capital charge in respect of the trading desk until the trading desk—

(a) has satisfied the back-testing requirements over the past 12 months; and

(b) has been reassigned to the green zone in the profit and loss attribution test.

(3) An authorized institution must give written notice to the Monetary Authority if the institution because of this section—

(a) switches from using the IMA to using the STM approach; or

(b) switches back from using the STM approach to using the IMA.

(4) Despite subsection (2), the Monetary Authority may permit an authorized institution to continue using the IMA to calculate its market risk capital charge in respect of a trading desk to which subsection (1) applies if the Monetary Authority is satisfied that there are the most extraordinary circumstances with systemic relevance.

(5) If the Monetary Authority permits under subsection (4) an authorized institution to continue using the IMA in respect of a trading desk, the institution must, as quickly as it is able, update its internal models to take into account the regime shift or significant market stress resulting from the circumstances referred to in that subsection.

(L.N. 167 of 2023)

Editorial Note:

* Operation date: 1 January 2025.

20-21. *(Repealed L.N. 212 of 2015)*

22. Exemption from section 17

(1) The Monetary Authority may, by notice in writing given to an authorized institution (other than an authorized institution

which uses the IRB approach to calculate its credit risk), exempt the institution from section 17 if the Monetary Authority is satisfied that— *(L.N. 137 of 2011)*

(a) the institution's market risk positions—

(i) never exceed 5% of its total on-balance sheet and off-balance sheet exposures; or

(ii) only sporadically exceed 5%, and never exceed 6%, of its total on-balance sheet and off-balance sheet exposures; and

(b) the institution's market risk positions—

(i) never exceed $50 million; or

(ii) only sporadically exceed $50 million and never exceed $60 million.

(2) For the purposes of subsection (1)—

(a) the amount of an authorized institution's market risk positions is calculated by aggregating—

(i) the institution's total gross (long plus short) positions in debt securities and debt-related derivative contracts;

(ii) the arithmetic mean of the institution's total long and total short positions in interest rate derivative contracts;

(iii) the institution's total gross (long plus short) positions in equities and equity-related derivative contracts;

(iv) the institution's total net open position in foreign exchange exposures as derived in section 296; and

(v) the institution's total gross (long plus short) positions in commodities and commodity-related derivative contracts; and

(b) an authorized institution's total on-balance sheet and off-balance sheet exposures are derived by—

(i) aggregating the institution's total liabilities, total assets less specific and collective provisions, and the principal amount (within the meaning of section 51(1)) of all of the institution's off-balance sheet exposures; and *(L.N. 137 of 2011)*

(ii) deducting therefrom the institution's paid-up capital, reserves (including current year's profit or loss) and perpetual or term subordinated debt.

(3) The date in relation to which an authorized institution's market risk positions are assessed for the purposes of subsection (1) is—

(a) subject to paragraphs (b) and (c), the calendar quarter end date of each of the 4 consecutive calendar quarters of the same calendar year;

(b) subject to paragraph (c), the calendar quarter end date of the consecutive calendar quarters, being not more than 4 consecutive calendar quarters, specified by the Monetary Authority by notice in writing given to the institution; or

(c) the date specified by the Monetary Authority by notice in writing given to the institution. *(L.N. 137 of 2011)*

(4) Where an authorized institution is exempted under this section from section 17, the institution—

(a) shall not, except with the prior consent of the Monetary Authority, include market risk in the calculation of its capital adequacy ratio;

(b) shall give notice in writing to the Monetary Authority of—

(i) an increase in its market risk positions which causes, or could reasonably be construed as potentially causing, whether by itself or in conjunction with any other event, the institution to cease to fall within subsection (1)(a) or (b); or

(ii) an intention to increase its market risk positions which will cause, or could reasonably be construed as potentially causing, whether by itself or in conjunction with any other event, the institution to cease to fall within subsection (1)(a) or (b);

(c) shall apply Part 4, 5 or 7, as the case requires, to calculate the credit risk for the institution's market risk positions except for its total net open position in foreign exchange exposures as derived in section 296.

(5) In this section, the following expressions have the respective meanings assigned to them by section 281—

(a) debt security; and

(b) equity.

23. Revocation of exemption under section 22

(1) Where—

(a) an authorized institution is exempted under section 22(1) from section 17; and

(b) either—

(i) the Monetary Authority is satisfied that, if the institution were not already so exempted, the exemption would be refused by virtue of the institution failing to satisfy the Monetary Authority as specified in section 22(1); or

(ii) the institution has given the Monetary Authority a notice referred to in section 22(4)(b), *(L.N. 137 of 2011)* the Monetary Authority may, by notice in writing given to the institution, revoke the exemption granted under section 22(1), beginning on such date, or the occurrence of such event, as specified in the notice.

(2) Section 17 applies to an authorized institution immediately upon the revocation under this section of an exemption under section 22(1).

23A. *(Repealed L.N. 167 of 2023)*

23B. *(Repealed L.N. 167 of 2023)*

Division 5A—Prescribed Approaches to Calculation of CVA Risk Capital Charge

(Division 5A added L.N. 167 of 2023)

23C. Approaches authorized institution must use to calculate its CVA risk capital charge

(1) An authorized institution—

(a) subject to paragraphs (c) and (d), must use the full basic CVA approach to calculate its CVA risk capital charge if the institution includes any eligible CVA hedge in the calculation of that charge;

(b) subject to paragraphs (c) and (d), may use the reduced basic CVA approach to calculate its CVA risk capital charge if the institution does not include any eligible CVA hedge in the calculation of that charge;

(c) may use the standardized CVA approach to calculate its CVA risk capital charge in respect of one or more transactions if the institution has approval to do so under section 23D; and

(d) subject to subsection (5), in the circumstances specified in subsection (2), may calculate its risk-weighted amount for CVA risk as the aggregate of—

(i) the IMM(CCR) risk-weighted amount of the transactions or contracts concerned that are covered by the IMM(CCR) approval;

(ii) the SA-CCR risk-weighted amount or CEM risk-weighted amount of the transactions or contracts concerned that are not covered by the IMM(CCR) approval;

(iii) the SA-CCR risk-weighted amount of the transactions or contracts concerned that fall within section 10B(5) or (7); and

(iv) the SFT risk-weighted amount of the SFTs that are not covered by the IMM(CCR) approval or that fall within section 10B(5) or (7).

(2) For the purposes of subsection (1)(d), the circumstances are that the total notional amount of the institution's OTC derivative transactions that are not cleared with a CCP does not exceed $1 trillion on a permanent basis.

(3) Subsection (1) does not prevent an authorized institution from using a combination of the reduced basic CVA approach and the standardized CVA approach, or a combination of the full basic CVA approach and the standardized CVA approach, to calculate its CVA risk capital charge for—

(a) different counterparties;

(b) different netting sets with the same counterparty; and

(c) different transactions within the same netting set, if—

(i) the netting set is split into 2 synthetic netting sets, where one is subject to the standardized CVA approach and the other is subject to the reduced basic CVA approach or the full basic CVA approach; and

(ii) the split—

(A) is consistent with the treatment of the legal netting set used by the institution for accounting purposes; or

(B) results from the fact that the approval under section 23D does not cover all transactions within the netting set.

(4) An authorized institution must not use any of the following to calculate its CVA risk capital charge or risk-weighted amount for CVA risk—

(a) a combination of the reduced basic CVA approach and the approach set out in subsection (1)(d);

(b) a combination of the full basic CVA approach and the approach set out in subsection (1)(d);

(c) a combination of the standardized CVA approach and the approach set out in subsection (1)(d).

(5) The Monetary Authority may, by written notice given to an authorized institution, prohibit the institution from using the approach set out in subsection (1)(d) to calculate its risk-weighted amount for CVA risk if the Monetary Authority considers that the CVA risk of the institution materially contributes to the overall risk of the institution.

(6) An authorized institution must comply with a notice given to it under subsection (5).

(7) In this section—

CEM risk-weighted amount (CEM風險加權數額) has the meaning given by section 106(7);

SFT risk-weighted amount (SFT風險加權數額) has the meaning given by section 52(9) or 106(7), as the case requires.

23D. Approval for authorized institution to use standardized CVA approach to calculate its CVA risk capital charge

(1) An authorized institution may apply to the Monetary Authority for approval to use the standardized CVA approach to calculate its CVA risk capital charge in respect of the types of transactions specified in the application.

(2) Subject to subsection (3), the Monetary Authority must determine an application from an authorized institution under subsection (1) by—

(a) granting approval to the institution to use the standardized CVA approach to calculate its CVA risk capital charge in respect of the transactions specified in the approval; or

(b) refusing to grant the approval.

(3) The Monetary Authority may only grant approval to an authorized institution if the institution demonstrates to the satisfaction of the Monetary Authority that the institution meets the requirements specified in Schedule 1B that are applicable to it.

(4) The Monetary Authority must specify in an approval the date on which, or the event on the occurrence of which, the approval takes effect.

(5) If an approval for an authorized institution under this section is in effect, the institution must give written notice to the Monetary Authority if the institution—

(a) no longer meets all of the requirements specified in Schedule 1B that are applicable to it; or

(b) expects that any of those requirements will not be met.

23E. Revocation of approval under section 23D

(1) The Monetary Authority may, by written notice given to an authorized institution, revoke an approval granted under section 23D, and require the institution, on and after the date specified in the notice or the occurrence of an event specified in the notice, to use another approach instead of the standardized CVA approach to calculate its CVA risk capital charge in respect of the transactions specified in the approval if—

(a) the Monetary Authority is satisfied that—

(i) if the approval were not in effect and the institution were to make a fresh application under section 23D(1), that application would be refused; or

(ii) the institution has contravened a condition attached under section 33A(1) or (2) to the approval; or

(b) the institution has given the Monetary Authority a notice under section 23D(5).

(2) An authorized institution must comply with a notice given to it under subsection (1).

Division 6—*(Repealed L.N. 167 of 2023)*

24-26. *(Repealed L.N. 167 of 2023)*

Division 7—Calculation of Capital Adequacy Ratio: Solo Basis, Solo-consolidated Basis and Consolidated Basis

27. Authorized institution shall calculate its capital adequacy ratio on solo basis, solo-consolidated basis or consolidated basis

(1) An authorized institution shall—

(a) calculate its capital adequacy ratio on a solo basis or, if it has the approval to do so under section 28(2)(a), calculate its capital adequacy ratio on a solo-consolidated basis; and

(b) subject to section 33, calculate its capital adequacy ratio on a consolidated basis.

(2) Subject to section 33, the Monetary Authority may, in a section 3C requirement, require an authorized institution to calculate its capital adequacy ratio on a consolidated basis in respect of a subsidiary of the institution (other than a subsidiary which is an insurance firm or securities firm) where— *(L.N. 156 of 2012)*

(a) more than 50% of the total assets or total income of the subsidiary relate to or arise from the carrying out of one or more than one relevant financial activity; or

(b) the Monetary Authority is satisfied that, after taking into account the nature of the business undertaken by the subsidiary, the institution should calculate its capital adequacy ratio on a consolidated basis in respect of that subsidiary if a relevant risk of the institution is to be adequately identified and assessed.

(3) In subsection (2)—

relevant financial activity (有關財務活動), in relation to a subsidiary of an authorized institution, means—

(a) an activity which is ancillary to a principal activity of the institution, including—

(i) owning and managing the institution’s property; and

(ii) performing information technology functions for the institution;

(b) lending, including—

(i) the provision of consumer or mortgage credit;

(ii) factoring;

(iii) forfaiting; and

(iv) the provision of guarantees and other financial commitments;

(c) financial leasing;

(d) money transmission services;

(e) issuing and administering a means of payment, including—

(i) credit cards;

(ii) travellers' cheques; and

(iii) bank drafts;

(f) trading for the subsidiary's own account, or for accounts of the subsidiary's customers, in—

(i) money market instruments;

(ii) foreign exchange;

(iii) financial instruments which are traded on an exchange;

(iv) OTC derivative transactions; or

(v) transferable securities;

(g) participating in securities issues, including the provision of services relating to the issues;

(h) the provision of—

(i) advice to undertakings on capital structure or industrial strategy, including any matter relating to capital structure or industrial strategy; or

(ii) advice and services relating to mergers and the purchase of undertakings;

(i) money broking; *(L.N. 128 of 2014)*

(j) portfolio management and the provision of advice in relation to portfolio management; or *(L.N. 128 of 2014)*

(k) custodial and safekeeping services. *(L.N. 128 of 2014)*

(4) An authorized institution which calculates its capital adequacy ratio on a consolidated basis shall give notice in writing to the Monetary Authority of any of the following matters as soon as is practicable after the institution is aware of the matter or ought to be aware of the matter—

(a) a member of the institution's consolidation group ceasing to be a subsidiary of the institution;

(b) a subsidiary of the institution becoming a member of its consolidation group;

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

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

28. Authorized institution may apply for approval to calculate its capital adequacy ratio on solo-consolidated basis

(1) An authorized institution may apply to the Monetary Authority for approval to calculate its capital adequacy ratio on a solo-consolidated basis instead of a solo basis in respect of such of its subsidiaries which are members of its consolidation group as specified in the application.

(2) Subject to subsection (3), the Monetary Authority shall determine an application under subsection (1) from an authorized institution by—

(a) granting approval to the institution to calculate its capital adequacy ratio on a solo-consolidated basis instead of a solo basis in respect of such subsidiaries of the institution as specified in the approval, and giving the institution a section 3C requirement to give effect to the approval; or *(L.N. 156 of 2012)*

(b) refusing to grant the approval.

(3) Without prejudice to the generality of subsection (2)(b), the Monetary Authority shall refuse to grant approval to an authorized institution to calculate its capital adequacy ratio on a solo-consolidated basis instead of a solo basis in respect of a subsidiary of the institution unless the institution demonstrates to the satisfaction of the Monetary Authority that—

(a) the subsidiary is wholly owned by, and managed as if it were an integral part of, the institution;

(b) the subsidiary is wholly financed by the institution such that the subsidiary has no depositors or other external creditors except external creditors for—

(i) audit fees;

(ii) company secretarial services; and

(iii) sundry operating expenses; and

(c) there are no regulatory, legal or taxation constraints on the transfer of the subsidiary's capital to the institution.

(4) Where—

(a) an authorized institution has been granted an approval under subsection (2)(a); and

(b) an event (referred to in this subsection as ***relevant event***) which could reasonably be construed as causing, or potentially causing, whether by itself or in conjunction with any other event, a subsidiary of the institution to fall outside subsection (3)(a), (b) or (c), occurs, the institution shall, as soon as is practicable after the relevant event occurs, give notice in writing to the Monetary Authority of the relevant event.

29. Solo basis for calculation of capital adequacy ratio

(1) An authorized institution shall in calculating its capital adequacy ratio on a solo basis—

(a) aggregate the institution's (including the institution's local branches' and overseas branches') risk-weighted amounts for—

(i) credit risk;

(ia) CVA risk; *(L.N. 167 of 2023)*

(ii) market risk; *(L.N. 222 of 2018)*

(iii) operational risk; and *(L.N. 222 of 2018)*

(iv) sovereign concentration risk; *(L.N. 222 of 2018)*

(b) deduct from the aggregate amount derived under paragraph (a)—

(i) that portion, as determined on a solo basis, of the total regulatory reserve for general banking risks and collective provisions of the institution apportioned to the STC approach or BSC approach, and to the SEC-ERBA, SEC-SA or SEC-FBA, which is not included in the Tier 2 capital of the institution; and *(L.N. 175 of 2017)*

(ii) the amount, as determined on a solo basis, of the net book value of the institution's reserves attributable to fair value gains arising from the revaluation of the institution's holdings of land and buildings, which is not included in the Tier 2 capital of the institution; and *(L.N. 156 of 2012)*

(c) determine the institution’s capital base, in accordance with Part 3, to reflect the fact that it is calculating its capital adequacy ratio on a solo basis.

(2) For the avoidance of doubt, it is hereby declared that—

(a) for the purposes of this section, an authorized institution shall risk-weight the exposures of an overseas branch of the institution in accordance with these Rules.

(b) *(Repealed L.N. 156 of 2012)*

(L.N. 156 of 2012)

30. Solo-consolidated basis for calculation of capital adequacy ratio

(1) Subject to subsection (2), an authorized institution shall in calculating its capital adequacy ratio on a solo-consolidated basis—

(a) aggregate the institution’s (including the institution’s local branches’ and overseas branches’) and its solo-consolidated subsidiaries’ risk-weighted amounts for—

(i) credit risk;

(ia) CVA risk; *(L.N. 167 of 2023)*

(ii) market risk; *(L.N. 222 of 2018)*

(iii) operational risk; and *(L.N. 222 of 2018)*

(iv) sovereign concentration risk; *(L.N. 222 of 2018)*

(b) deduct from the aggregate amount derived under paragraph (a)—

(i) that portion, as determined on a solo-consolidated basis, of the total regulatory reserve for general banking risks and collective provisions of the institution and its solo-consolidated subsidiaries apportioned to the STC approach or BSC approach, and to the SEC-ERBA, SEC-SA or SEC-FBA, which is not included in the Tier 2 capital of the institution and its solo-consolidated subsidiaries; and *(L.N. 156 of 2012; L.N. 175 of 2017)*

(ii) the amount, as determined on a solo-consolidated basis, of the net book value of the institution's and its solo-consolidated subsidiaries' reserves attributable to fair value gains arising from the revaluation of the institution's and its solo-consolidated subsidiaries' holdings of land and buildings, which is not included in the Tier 2 capital of the institution and its solo-consolidated subsidiaries; and *(L.N. 156 of 2012)*

(c) determine the capital base of the institution and its solo-consolidated subsidiaries, in accordance with Part 3, to reflect the fact that it is calculating its capital adequacy ratio on a solo-consolidated basis.

(2) For the avoidance of doubt, it is hereby declared that, for the purposes of this section, an authorized institution shall risk-weight the exposures of an overseas branch of the institution in accordance with these Rules.

(3) An authorized institution which calculates its capital adequacy ratio on a solo-consolidated basis shall ensure that, in calculating that ratio, the risk-weighting of a relevant risk does not include inter-company balances with, and transactions between, the institution and its solo-consolidated subsidiaries.

(4) *(Repealed L.N. 156 of 2012)*

31. Consolidated basis for calculation of capital adequacy ratio

(1) An authorized institution shall in calculating its capital adequacy ratio on a consolidated basis—

(a) aggregate the institution's consolidation group's (including the institution's local branches' and overseas branches') risk-weighted amounts for— *(L.N. 156 of 2012)*

(i) credit risk;

(ia) CVA risk; *(L.N. 167 of 2023)*

(ii) market risk; *(L.N. 222 of 2018)*

(iii) operational risk; and *(L.N. 222 of 2018)*

(iv) sovereign concentration risk; *(L.N. 222 of 2018)*

(b) deduct from the aggregate amount derived under paragraph (a)—

(i) that portion, as determined on a consolidated basis, of the total regulatory reserve for general banking risks and collective provisions of the institution's consolidation group apportioned to the STC approach or BSC approach, and to the SEC-ERBA, SEC-SA or SEC-FBA, which is not included in the Tier 2 capital of the institution's consolidation group; and *(L.N. 156 of 2012; L.N. 175 of 2017)*

(ii) the amount, as determined on a consolidated basis, of the net book value of the institution's consolidation group's reserves attributable to fair value gains arising from the revaluation of the institution's consolidation group's holdings of land and buildings, which is not included in the Tier 2 capital of the institution's consolidation group; and *(L.N. 156 of 2012)*

(c) determine the institution's consolidation group's capital base, in accordance with Part 3, to reflect the fact that it is calculating its capital adequacy ratio on a consolidated basis.

(2) It is hereby declared that, under the consolidated basis for the calculation of the capital adequacy ratio of an authorized institution, the institution shall ensure that—

(a) the risk-weighting of a relevant risk does not include the exposures of a subsidiary of the institution which is not a member of its consolidation group; and

(b) the risk-weighting of a relevant risk does not include inter-company balances with, and transactions between, members of its consolidation group.

(3) An authorized institution which calculates its capital adequacy ratio on a consolidated basis may, insofar as its market risk is concerned, offset market risk positions between members of its consolidation group if those market risk positions are monitored and managed on a group basis.

(4) For the avoidance of doubt, it is hereby declared that—

(a) for the purposes of this section, an authorized institution shall risk-weight the exposures of an overseas branch of the institution in accordance with these Rules. *(L.N. 156 of 2012)*

(b) *(Repealed L.N. 156 of 2012)*

32. Provisions supplementary to section 31

(1) Subject to subsection (2), an authorized institution which calculates its capital adequacy ratio on a consolidated basis shall do so using the same approach in calculating a relevant risk as it would be required to use if it were calculating that ratio on a solo basis.

(2) With the prior consent of the Monetary Authority, an authorized institution which calculates its capital adequacy ratio on a consolidated basis is not required to comply with subsection (1) if the institution demonstrates to the satisfaction of the Monetary Authority that it is not practicable for every

member of its consolidation group to use the same approach to calculate the relevant risk of the group on that basis.

(3)-(4) *(Repealed L.N. 167 of 2023)*

33. Exceptions to section 27

(1) Where—

(a) an authorized institution calculates its capital adequacy ratio on a consolidated basis; and

(b) a specified subsidiary calculates its capital adequacy ratio on a solo basis in accordance with the capital adequacy standards applicable in the jurisdiction in which it is incorporated, *(L.N. 167 of 2023)*

the institution may apply to the Monetary Authority for approval to risk-weight the exposures of that subsidiary (which may be all those exposures or a class thereof) in accordance with those standards instead of in accordance with these Rules. *(L.N. 137 of 2011; 14 of 2025 s. 179)*

(2) Subject to subsection (3), the Monetary Authority shall determine an application under subsection (1) from an authorized institution by—

(a) granting approval to the institution to risk-weight the exposures of the subsidiary specified in the application, or those exposures specified by the Monetary Authority in the approval, in accordance with the capital adequacy standards applicable in the jurisdiction where the subsidiary is incorporated instead of in accordance with these Rules, and giving the institution a section 3C requirement to give effect to the approval; or *(L.N. 156 of 2012; L.N. 167 of 2023)*

(b) refusing to grant the approval (whether in whole or in part). *(L.N. 137 of 2011)*

(3) Without prejudice to the generality of subsection (2)(b), the Monetary Authority shall refuse to grant approval to an authorized institution to risk-weight the exposures of a subsidiary which is a member of the institution's consolidation group in accordance with the capital adequacy standards applicable in the jurisdiction in which the subsidiary is incorporated instead of in accordance with these Rules unless the institution demonstrates to the satisfaction of the Monetary Authority that the use of those standards would not materially prejudice the calculation of the institution's capital adequacy ratio. *(L.N. 167 of 2023)*

(4) An authorized institution which calculates its capital adequacy ratio on a consolidated basis may apply to the Monetary Authority for approval to calculate that ratio by excluding one or more than one member from its consolidation group.

(5) Subject to subsection (6), the Monetary Authority shall determine an application under subsection (4) from an authorized institution by—

(a) granting approval to the institution to calculate its capital adequacy ratio by excluding from its consolidation group such members of the group as the Monetary Authority specifies and giving the institution a section 3C requirement to give effect to the approval; or *(L.N. 156 of 2012)*

(b) refusing to grant the approval.

(6) Without prejudice to the generality of subsection (5)(b), the Monetary Authority shall refuse to grant approval to an authorized institution to calculate its capital adequacy ratio by excluding from its consolidation group any member of the group unless the institution demonstrates to the satisfaction of the Monetary Authority that the inclusion of that member in the group—

(a) would be inappropriate or misleading; or

(b) is not practicable due to regulatory, legal or taxation constraints on the transfer of information necessary to enable the institution to calculate that ratio on a consolidated basis in respect of that member.

(7) In subsection (1)—

specified subsidiary (指明附屬公司), in relation to an authorized institution—

(a) means a subsidiary of the institution that is a member of the institution's consolidation group and is incorporated in a jurisdiction other than Hong Kong; but

(b) does not include a subsidiary of the institution that is a re-domiciled entity. *(14 of 2025 s. 179)*

Division 7A—Attachment of Conditions to Approvals Granted under Section 6(2)(a), 8(2)(a), 10B(2)(a), 15C(2)(a) or 18(2)(a)

(L.N. 156 of 2012; L.N. 212 of 2015; L.N. 222 of 2018; L.N. 167 of 2023)

33A. Attachment of conditions to approvals granted under section 6(2)(a), 8(2)(a), 10B(2)(a), 15C(2)(a) or 18(2)(a)

(L.N. 156 of 2012; L.N. 212 of 2015; L.N. 222 of 2018; L.N. 167 of 2023)

(1) Where the Monetary Authority grants an approval under section 6(2)(a), 8(2)(a), 10B(2)(a), 15C(2)(a) or 18(2)(a) to an authorized institution, the approval may be granted subject to any conditions that the Monetary Authority thinks proper to attach to the approval in any particular case. *(L.N. 156 of 2012; L.N. 212 of 2015; L.N. 222 of 2018; L.N. 167 of 2023)*

(2) Without limiting the generality of subsection (1), the Monetary Authority may at any time, by notice in writing

served on an authorized institution in respect of which the Monetary Authority has granted an approval under section 6(2)(a), 8(2)(a), 10B(2)(a), 15C(2)(a) or 18(2)(a) (whether before, on or after 1 January 2012), attach to the institution's approval any conditions (including attach by way of amending conditions already attached to the approval), or cancel any conditions attached to the approval, that the Monetary Authority thinks proper, with effect from— *(L.N. 156 of 2012; L.N. 212 of 2015; L.N. 222 of 2018; L.N. 167 of 2023)*

(a) subject to paragraph (b), the date of service of the notice; or

(b) such later date (if any) as is specified in the notice.

(Division 7A added L.N. 137 of 2011)

Division 8—Decisions to which Section 101B(1) of Ordinance Applies

34. Reviewable decisions

(1) A decision made by the Monetary Authority under section 6(2), 8(2), 10B(2), 15C(2), 18(2) or 33A(1) or (2) is a decision to which section 101B(1) of the Ordinance applies. *(L.N. 156 of 2012; L.N. 212 of 2015; L.N. 222 of 2018; L.N. 167 of 2023)*

(2) *(Repealed L.N. 212 of 2015)*

(L.N. 137 of 2011)

Part 3

Determination of Capital Base

(Part 3 replaced L.N. 156 of 2012)

Division 1—General

35. Interpretation of Part 3

In this Part—

affiliate (附屬成員), in relation to an authorized institution, means—

(a) an entity that—

(i) has a beneficial interest in, or controls, 20% or more of the total number of ordinary shares in the institution; or

(ii) is entitled to exercise, or control the exercise of, 20% or more of the voting power in the institution;

(b) an entity in which the institution or an entity falling within paragraph (a)—

(i) has a beneficial interest in, or controls, 20% or more of the total number of ordinary shares; or

(ii) is entitled to exercise, or control the exercise of, 20% or more of the voting power;

bank subsidiary (銀行附屬公司), in relation to an authorized institution, means a subsidiary of the institution that—

(a) is a bank or any other entity that is subject to substantially similar regulation and supervision as a bank; and

(b) is subject to consolidation under a section 3C requirement;

cash flow hedge (現金流對沖), in relation to a hedging relationship of an authorized institution, means a hedge of an exposure of the institution to variability in cash flows that—

(a) is attributable to—

(i) a particular risk associated with an asset or liability recognized on the institution's balance sheet; or

(ii) a highly probable uncommitted but anticipated future transaction; and

(b) could affect the institution's profit or loss;

commercial entity (商業實體) means any entity in the private sector, other than a financial sector entity;

connected company (有連繫公司), in relation to an authorized institution, means—

(a) a subsidiary, or the holding company, of the institution; or

(b) a company that falls within section 64(1)(b), (c), (d) or (e) of the Ordinance in respect of the institution;

financial sector entity (金融業實體) means an entity that is engaged predominantly in one or more of the following activities, whether by itself or through any of its subsidiaries—

(a) banking;

(b) securities business;

(c) insurance business;

(d) financial leasing;

(e) the issuance of credit cards;

(f) portfolio management;

(g) investment advisory services;

(h) custodial and safekeeping services;

(i) central clearing services;

(j) activities ancillary to banking;

(k) activities similar to any of the activities set out in any of paragraphs (a), (b), (c), (d), (e), (f), (g), (h) and (i);

indirect holding (間接持有), in relation to an authorized institution, means an exposure of the institution in respect of a capital instrument issued by, or a non-capital LAC liability of, a financial sector entity in circumstances where—

(a) the instrument or liability is not held by the institution directly; but

(b) a loss of value in the instrument or liability will result in a loss to the institution substantially equivalent to the loss in value of a direct holding; *(L.N. 222 of 2018)*

insignificant LAC investment (非重大LAC投資), in relation to an authorized institution, means an investment by the institution in a capital instrument issued by, or a non-capital LAC liability of, an entity that is neither of the following—

(a) an affiliate of the institution;

(b) an entity of which the institution owns more than 10% of the issued ordinary share capital; *(L.N. 222 of 2018)*

loss-absorbing capacity (吸收虧損能力) has the meaning given by rule 2(1) of the LAC Rules; *(L.N. 222 of 2018)*

reciprocal cross holding (互相交叉持有) means an arrangement—

(a) under which—

(i) an authorized institution holds capital instruments issued by, or non-capital LAC liabilities of, a financial sector entity; and

(ii) the entity also holds capital instruments issued by, or non-capital LAC liabilities of, the institution; and

(b) which is designed to artificially inflate the capital position or loss-absorbing capacity of the institution and the entity; *(L.N. 222 of 2018)*

retained earnings (保留溢利), in relation to an authorized institution, means the amount of profits and losses of the institution brought forward pursuant to prevailing accounting standards as at a particular date, and includes the institution's—

(a) unaudited profit or loss of the current financial year; and

(b) profit or loss of the immediately preceding financial year pending audit completion;

significant LAC investment (重大LAC投資), in relation to an authorized institution, means an investment by the institution in a capital instrument issued by, or a non-capital LAC liability of— *(L.N. 222 of 2018)*

(a) an affiliate of the institution; or

(b) an entity, other than an affiliate of the institution, of which the institution owns more than 10% of the issued ordinary share capital;

special purpose vehicle (特定目的工具), in relation to an authorized institution, means a company or any other entity—

(a) that is established by the institution for the sole purpose of raising capital for the institution; and

(b) that does not trade or conduct any business except raising capital for the institution;

synthetic holding (合成持有), in relation to an authorized institution, means an exposure of the institution to an instrument the value of which is directly linked to the value of— *(L.N. 222 of 2018)*

(a) the capital instruments issued by a financial sector entity; or

(b) the non-capital LAC liabilities of a financial sector entity. *(L.N. 222 of 2018)*

36. Determination of capital base

The capital base of an authorized institution is the sum of the institution's—

(a) Tier 1 capital; and

(b) Tier 2 capital.

Division 2—Tier 1 Capital

37. Tier 1 capital

The Tier 1 capital of an authorized institution is the sum of the institution's—

(a) CET1 capital; and

(b) Additional Tier 1 capital.

38. CET1 capital

(1) The CET1 capital of an authorized institution is the sum of the following capital items, calculated in Hong Kong dollars and after the deductions specified in Division 4 have been made in accordance with that Division—

(a) the institution's CET1 capital instruments except any such instruments that are issued by the institution by virtue of capitalizing any property revaluation reserves of the institution referred to in section 40(1)(d);

(b) the amount standing to the credit of the institution's share premium account (if any) resulting from the issue of the institution's CET1 capital instruments; *(28 of 2012 ss. 912 & 920 and L.N. 162 of 2013)*

(c) subject to subsection (2), the institution's retained earnings and other disclosed reserves;

(d) the applicable amount of minority interests arising from the CET1 capital instruments issued by the consolidated bank subsidiaries of the institution and held by third parties, that is recognized as CET1 capital of the institution on a consolidated basis, as calculated based on the requirements set out in sections 2(1) and 3 of Schedule 4D.

(2) An authorized institution must exclude from reserves or retained earnings, as the case requires, under subsection (1)(c)—

(a) cumulative cash flow hedge reserves that relate to the hedging of financial instruments that are not fair valued on the balance sheet (including projected cash flows);

(b) cumulative fair value gains or losses on liabilities of the institution that are valued at fair value and that result from changes in the institution's own credit risk except any debit valuation adjustments for derivative contracts arising from the institution's own credit risk referred to in section 43(1)(h);

(c) cumulative fair value gains arising from the revaluation of the institution's holdings of land and buildings (whether for the institution's own use or for investment purposes);

(d) cumulative fair value gains generated from any transaction or arrangement entered into between the institution and another member of the institution's consolidation group involving the disposal of land and buildings (whether for the institution's own use or for investment purposes) that are held by the institution, or that other member, unless otherwise approved by the Monetary Authority; and

(e) the institution's regulatory reserve for general banking risks. *(L.N. 175 of 2017)*

(3) To avoid doubt, any capital instruments issued to third parties through a special purpose vehicle must not be included in an authorized institution's CET1 capital.

39. Additional Tier 1 capital

(1) The Additional Tier 1 capital of an authorized institution is the sum of the following capital items, calculated in Hong Kong dollars and after the deductions specified in Division 4 have been made in accordance with that Division—

(a) the institution's Additional Tier 1 capital instruments;

(b) the amount standing to the credit of the institution's share premium account (if any) resulting from the issue of capital instruments that fall within paragraph (a); *(28 of 2012 ss. 912 & 920 and L.N. 162 of 2013)*

(c) the applicable amount of capital instruments issued by the consolidated bank subsidiaries of the institution and held by third parties, that is recognized as Additional Tier 1 capital of the institution on a consolidated basis, as calculated based on the requirements set out in sections 2(2) and 4 of Schedule 4D.

(2) If an authorized institution issues capital instruments to third parties through a special purpose vehicle and—

(a) the special purpose vehicle is consolidated with the institution;

(b) the capital instruments meet the qualifying criteria set out in Schedule 4B; and

(c) the only asset of the special purpose vehicle is its investment in the capital of the institution in a form that meets the qualifying criteria set out in Schedule 4B,

the capital instruments may be included in the Additional Tier 1 capital of the institution on a consolidated basis as if the institution itself had issued the capital instruments directly to the third parties.

(3) If an authorized institution issues capital instruments to third parties through a special purpose vehicle via a consolidated bank subsidiary of the institution and—

(a) the special purpose vehicle is consolidated with the bank subsidiary;

(b) the capital instruments meet the qualifying criteria set out in Schedule 4B; and

(c) the only asset of the special purpose vehicle is its investment in the capital of the bank subsidiary in a form that meets the qualifying criteria set out in Schedule 4B,

the institution may treat the capital instruments as if the bank subsidiary itself had issued the capital instruments directly to the third parties and, accordingly, may include the capital instruments in determining the applicable amount of the capital instruments to be included in the Additional Tier 1 capital of the institution on a consolidated basis, as calculated based on the requirements set out in sections 2(2) and 4 of Schedule 4D.

Division 3—Tier 2 Capital

40. Tier 2 capital

(1) The Tier 2 capital of an authorized institution is the sum of the following capital items, calculated in Hong Kong dollars and after the deductions specified in Division 4 have been made in accordance with that Division—

(a) the institution's Tier 2 capital instruments;

(b) the amount standing to the credit of the institution's share premium account (if any) resulting from the issue of capital instruments that fall within paragraph (a); *(28 of 2012 ss. 912 & 920 and L.N. 162 of 2013)*

(c) the applicable amount of Tier 2 capital instruments issued by the consolidated bank subsidiaries of the institution and held by third parties, that is recognized as Tier 2 capital of the institution on a consolidated basis, as calculated based on the requirements set out in sections 2(2) and 5 of Schedule 4D;

(d) subject to section 41, that part of the institution's reserves and retained earnings that is attributable to fair value gains arising from—

(i) the revaluation of the institution's holdings of land and buildings except land and buildings mortgaged to the institution to secure a debt;

(ii) the revaluation of the institution's share of the net asset value of any subsidiary of the institution to the extent that the value has changed as a result of the revaluation of the subsidiary's holdings of land and buildings except land and buildings mortgaged to the subsidiary to secure a debt; and

(iii) disposal of land and buildings (whether for the institution's own use or for investment purposes) referred to in section 38(2)(d);

(e) the shares issued by the institution through capitalizing that part of the institution's reserves and retained earnings that is attributable to fair value gains described in paragraph (d);

(f) the amount of the institution's regulatory reserve for general banking risks and collective provisions that may be included in its Tier 2 capital under section 42; *(L.N. 175 of 2017)*

(g) the amount of the excess of the institution's total eligible provisions over its total EL amount that may be included in its Tier 2 capital under section 42(3)(c). *(L.N. 175 of 2017)*

(2) If an authorized institution issues capital instruments to third parties through a special purpose vehicle and—

(a) the special purpose vehicle is consolidated with the institution;

(b) the capital instruments meet the qualifying criteria set out in Schedule 4C; and

(c) the only asset of the special purpose vehicle is its investment in the capital of the institution in a form that meets the qualifying criteria set out in Schedule 4C,

the capital instruments may be included in the Tier 2 capital of the institution on a consolidated basis as if the institution itself had issued the capital instruments directly to the third parties.

(3) If an authorized institution issues capital instruments to third parties through a special purpose vehicle via a consolidated bank subsidiary of the institution and—

(a) the special purpose vehicle is consolidated with the bank subsidiary;

(b) the capital instruments meet the qualifying criteria set out in Schedule 4C; and

(c) the only asset of the special purpose vehicle is its investment in the capital of the bank subsidiary in a form that meets the qualifying criteria set out in Schedule 4C,

the institution may treat the capital instruments as if the bank subsidiary itself had issued the capital instruments directly to the third parties and, accordingly, may include the capital instruments in determining the applicable amount of the capital instruments to be included in the Tier 2 capital of the institution on a consolidated basis, as calculated based on the requirements set out in sections 2(2) and 5 of Schedule 4D.

41. Provisions supplementary to section 40(1)(d)

(1) An authorized institution's reserves and retained earnings fall within that part of reserves and retained earnings referred to in section 40(1)(d) only if—

(a) the institution has a clearly documented policy on the frequency and method of revaluation of its holdings of land and buildings that is satisfactory to the Monetary Authority;

(b) the institution does not depart from that policy except after consultation with the Monetary Authority;

(c) subject to paragraph (d), any revaluation of the institution's holdings of land and buildings is undertaken by an independent professional valuer;

(d) in any case where the institution demonstrates to the satisfaction of the Monetary Authority that, despite all reasonable efforts, the institution has been unable to obtain the services of an independent professional valuer to undertake the revaluation of all or part of the institution's holdings of land and buildings, any revaluation of such holdings undertaken by a person who is not an independent professional valuer is endorsed in writing by an independent professional valuer;

(e) any revaluation of the institution's holdings of land and buildings is—

(i) approved by the institution's external auditors; and

(ii) explicitly reported in the institution's audited accounts; and

(f) the fair value gains referred to in section 40(1)(d) are recognized in accordance with applicable accounting standards and any such gains not recognized in the financial statements of the institution are excluded from the part of reserves and retained earnings referred to in that section.

(2) An authorized institution must not include in its Tier 2 capital more than 45% of any fair value gains of any item referred to in section 40(1)(d) arising from any revaluation referred to in that section.

(3) An authorized institution must not, in calculating its Tier 2 capital, set-off losses in respect of land and buildings that are for the institution's own use where the losses are recognized in the institution's profit or loss against unrealized gains that are reflected directly in equity through the statement of changes in equity.

(4) An authorized institution must deduct from its CET1 capital any cumulative losses of the institution arising from the institution's holdings of land and buildings below the depreciated cost value (whether or not any such land and buildings are held for the institution's own use or for investment purposes).

42. Provisions supplementary to section 40(1)(f) and (g)

(L.N. 175 of 2017)

(1) An authorized institution that uses only the STC approach or BSC approach to calculate its credit risk for non-securitization exposures must not include in its Tier 2 capital that amount of its total regulatory reserve for general banking risks and collective provisions that exceeds 1.25% of the institution's total risk-weighted amount for credit risk, being the sum of all the institution's risk-weighted amounts for— *(L.N. 175 of 2017)*

(a) all the institution's non-securitization exposures to credit risk subject to the approach; and

(b) all the institution's securitization exposures to credit risk subject to the SEC-ERBA, SEC-SA or SEC-FBA. *(L.N. 175 of 2017)*

(2) An authorized institution that uses only the IRB approach, or a combination of the STC approach and IRB approach, to calculate its credit risk for non-securitization exposures—

(a) subject to paragraph (b), must apportion its total regulatory reserve for general banking risks and collective provisions between the STC approach, IRB approach, SEC-IRBA, SEC-ERBA, SEC-SA and SEC-FBA on a pro rata basis in accordance with the proportions of the institution's risk-weighted amount for credit risk calculated by using those approaches;

(b) may, with the prior consent of the Monetary Authority, use its own method to apportion its total regulatory reserve for general banking risks and collective provisions between the STC approach, IRB approach, SEC-IRBA, SEC-ERBA, SEC-SA and SEC-FBA; and

(c) must, after it has carried out the apportionment referred to in paragraph (a) or (b)—

(i) comply with subsection (1) in respect of the portion apportioned to the STC approach, SEC-

ERBA, SEC-SA and SEC-FBA as if it were an authorized institution that uses only the STC approach to calculate its credit risk for non-securitization exposures;

(ii) comply with subsection (3) in respect of the portion apportioned to the IRB approach; and

(iii) comply with subsection (4) in respect of the portion apportioned to the SEC-IRBA. *(L.N. 175 of 2017)*

(3) Where an authorized institution uses the IRB approach—

(a) subject to paragraphs (b) and (c), the institution must deduct the amount of the excess of its total EL amount over its total eligible provisions from its CET1 capital in accordance with section 43(1)(i);

(b) the deduction to be made under paragraph (a) must be gross of tax effects (if any); and

(c) if the total EL amount referred to in paragraph (a) is less than the total eligible provisions referred to in that paragraph, the institution may include the amount of the excess of the total eligible provisions over the total EL amount in its Tier 2 capital up to 0.6% of its risk-weighted amount for credit risk calculated by using the IRB approach.

(4) An authorized institution may include that portion of its total regulatory reserve for general banking risks and collective provisions that is apportioned to the SEC-IRBA under subsection (2)(a) or (b) in its Tier 2 capital up to 0.6% of its risk-weighted amount for credit risk calculated by using the SEC-IRBA. *(L.N. 175 of 2017)*

Division 4—Regulatory Deductions

43. Deductions from CET1 capital

(1) An authorized institution must deduct from its CET1 capital— *(L.N. 222 of 2018)*

(a) the amount of any goodwill that is recognized by the institution as an intangible asset of the institution, net of any associated deferred tax liabilities;

(b) the amount of other intangible assets of the institution, net of any associated deferred tax liabilities;

(c) assets of any defined benefit pension fund or plan (except those of such assets to which the institution can demonstrate to the satisfaction of the Monetary Authority that it has unrestricted and unfettered access), net of the amount of obligations under the fund or plan and any associated deferred tax liabilities;

(d) subject to section 44(1), the amount of deferred tax assets, net of deferred tax liabilities (excluding those associated with and already taken into account in the deduction of the amount of goodwill, the amount of other intangible assets and assets of any defined benefit pension fund or plan) of the institution;

(e) the amount of any credit-enhancing interest-only strip, and any gain-on-sale and other increase in the CET1 capital of the institution, arising from a securitization transaction in which the institution is the originating institution; *(L.N. 175 of 2017)*

(f) subject to section 44A, the amount of any securitization exposure of the institution that the Monetary Authority may, by notice in writing given to the institution, require the institution to deduct from its CET1 capital; *(L.N. 175 of 2017)*

(g) the amount of any valuation adjustment made in respect of an exposure of the institution that gives rise to a reduction in the value of the exposure except—

(i) if that exposure is a financial instrument that gives rise to the cash flow hedge reserves that fall within section 38(2)(a);

(ii) such part of that amount that has been taken into account in the calculation of the amount of the institution's retained earnings or other disclosed reserves (or part of the retained earnings or other disclosed reserves) that fall within section 38(1)(c);

(h) the amount of any debit valuation adjustments made by the institution in respect of derivative contracts arising from the institution's own credit risk (which must not be offset by any accounting valuation adjustments arising from the institution's counterparty credit risk);

(i) if the institution uses the IRB approach and the institution's total EL amount referred to in section 42(3)(a) exceeds the institution's total eligible provisions referred to in that section, the amount of the excess of the total EL amount over the total eligible provisions;

(j) any cumulative losses of the institution arising from the institution's holdings of land and buildings below the depreciated cost value referred to in section 41(4);

(k) subject to section 45, the amount of any relevant capital shortfall in respect of a subsidiary of the institution that—

(i) is a securities firm or insurance firm; and

(ii) is not the subject of consolidation under a section 3C requirement;

(l) subject to section 44(2), the amount of any direct holdings, indirect holdings and synthetic holdings by the institution of its own CET1 capital instruments, unless already derecognized under applicable accounting standards, calculated in accordance with Schedule 4E;

(m) subject to section 44(2), the amount of any direct holdings, indirect holdings and synthetic holdings by the institution of CET1 capital instruments issued by any financial sector entity where that entity has a reciprocal cross holding with the institution;

(n) subject to sections 44(2) and 46(1), in respect of any capital investment in a connected company of the institution where that connected company is a commercial entity, that part of the net book value of the investment that exceeds 15% of the capital base of the institution as reported in the institution's capital adequacy ratio return as at the immediately preceding calendar quarter end date; *(L.N. 167 of 2023)*

(o) subject to sections 44(2) and 46(2), the applicable amount of the institution's direct holdings, indirect holdings and synthetic holdings of CET1 capital instruments issued by financial sector entities, calculated in accordance with Schedule 4F, if—

(i) the entities are not the subject of consolidation under a section 3C requirement imposed on the institution;

(ii) the holdings are insignificant LAC investments; and *(L.N. 222 of 2018)*

(iii) the holdings do not otherwise fall within paragraphs (l) and (m);

(p) subject to sections 44(2) and 46(2), the applicable amount of the institution's direct holdings, indirect holdings and synthetic holdings of CET1 capital instruments issued by financial sector entities, calculated in accordance with Schedule 4G, if—

(i) the entities are not the subject of consolidation under a section 3C requirement imposed on the institution;

(ii) the holdings are significant LAC investments; and *(L.N. 222 of 2018)*

(iii) the holdings do not otherwise fall within paragraphs (l) and (m);

(q) subject to sections 44(2) and 46(2)—

(i) (if the institution calculates its capital adequacy ratio on a solo basis under a section 3C requirement) the amount of the institution's direct holdings of CET1 capital instruments issued by financial sector entities that are members of the institution's consolidation group;

(ii) (if the institution calculates its capital adequacy ratio on a solo-consolidated basis under a section 3C requirement) the amount of the institution's direct holdings of CET1 capital instruments issued by financial sector entities, other than any solo-consolidated subsidiaries, that are members of the institution's consolidation group; and

(r) any amount that would otherwise be deducted from the institution's Additional Tier 1 capital under section 47 but cannot be so deducted because the institution does not have sufficient Additional Tier 1 capital to satisfy the deduction.

(2) In this section—

relevant capital shortfall (有關資本短欠), in relation to a subsidiary of an authorized institution, means the amount specified in a notice under section 45(1)(b) given to the institution in respect of that subsidiary.

44. Provisions supplementary to section 43(1)(d), (l), (m), (n), (o), (p) and (q)

(1) For the purposes of determining the net deferred tax assets referred to in section 43(1)(d), deferred tax assets may be netted with deferred tax liabilities only if the deferred tax assets and deferred tax liabilities relate to taxes levied by the same taxation authority and offsetting is permitted by the relevant taxation authority.

(2) For the purposes of paragraphs (l), (m), (n), (o), (p) and (q) of section 43(1), an authorized institution must—

(a) exclude from the holdings referred to in those paragraphs any holdings of capital instruments issued by financial sector entities that are not included within regulatory capital in the relevant financial sectors in which those entities operate;

(b) reduce the amount to be deducted under those paragraphs by any amount of goodwill (related to any holdings of shares falling within those paragraphs) already deducted under section 43(1)(a); and

(c) include in the amount to be deducted under those paragraphs potential future holdings that the institution could be contractually obliged to purchase.

44A. Provisions supplementary to section 43(1)(f)

(1) If an authorized institution is required by a notice given to it under section 43(1)(f) to deduct from its CET1 capital a securitization exposure specified in the notice, the institution

must make the deduction based on the exposure amount of the exposure determined under section 235.

(2) An authorized institution may, for the purposes of subsection (1), deduct from the exposure amount determined under section 235 for a securitization exposure—

(a) the specific provisions or partial write-offs made by the institution for the exposure; and

(b) if applicable, the non-refundable purchase price discounts provided to the institution by the seller of the exposure.

(L.N. 175 of 2017)

45. Provisions supplementary to section 43(1)(k)

(1) Where a subsidiary of an authorized institution that is a securities firm or insurance firm fails to meet the minimum capital requirements applicable to it and fails to remedy the breach within a period as determined or prescribed by the securities regulator or insurance regulator of the securities firm or insurance firm, as the case may be, then—

(a) the institution must, as soon as practicable after it becomes aware of the failure, give notice in writing to the Monetary Authority of particulars of the securities firm or insurance firm, as the case may be, and the details of the failure; and

(b) the Monetary Authority may, by notice in writing given to the institution, and beginning on the date, or the occurrence of the event, specified in the notice, and ending on the date, or the occurrence of the event, specified in the notice, require the institution to deduct from its CET1 capital an amount that, in the opinion of the Monetary Authority, represents the shortfall of the securities firm or insurance firm, as the case may be, in meeting those minimum capital requirements.

(2) The amount to be deducted under section 43(1)(k) by an authorized institution from its CET1 capital—

(a) is in addition to any other deduction the institution is required to make under section 43 from its CET1 capital in respect of the subsidiary concerned of the institution; and

(b) represents the amount by which that subsidiary is deficient in meeting its minimum capital requirements.

(3) An authorized institution must comply with the requirements of a notice given to it under subsection (1)(b).

46. Provisions supplementary to section 43(1)(n), (o), (p) and (q)

(1) An authorized institution must treat as part of the capital investment that is to be deducted under section 43(1)(n) the aggregate amount of any loans, facilities or other credit exposures provided by the institution to any connected company of the institution where the connected company is a commercial entity as if such loans, facilities or other credit exposures were direct capital investment by the institution in the commercial entity, except where the institution demonstrates to the satisfaction of the Monetary Authority that any such loan was made, any such facility was granted, or any such other credit exposure was incurred, in the ordinary course of the institution's business.

(2) An authorized institution must treat as part of the amount of its direct holdings, indirect holdings and synthetic holdings of CET1 capital instruments that are to be deducted under section 43(1)(o), (p) and (q) the aggregate amount of any loans, facilities or other credit exposures provided by the institution to any connected company of the institution where

the connected company is a financial sector entity as if such loans, facilities or other credit exposures were direct holdings, indirect holdings or synthetic holdings of the institution in the financial sector entity, except where the institution demonstrates to the satisfaction of the Monetary Authority that any such loan was made, any such facility was granted, or any such other credit exposure was incurred, in the ordinary course of the institution's business.

47. Deductions from Additional Tier 1 capital

(1) Subject to subsection (2), an authorized institution must deduct from its Additional Tier 1 capital— *(L.N. 222 of 2018)*

(a) the amount of any direct holdings, indirect holdings and synthetic holdings by the institution of its own Additional Tier 1 capital instruments, unless already derecognized under applicable accounting standards, calculated in accordance with Schedule 4E;

(b) the amount of any direct holdings, indirect holdings and synthetic holdings by the institution of Additional Tier 1 capital instruments issued by any financial sector entity where that entity has a reciprocal cross holding with the institution;

(c) the applicable amount of the institution's direct holdings, indirect holdings and synthetic holdings of Additional Tier 1 capital instruments issued by financial sector entities, calculated in accordance with Schedule 4F, if—

(i) the entities are not the subject of consolidation under a section 3C requirement imposed on the institution;

(ii) the holdings are insignificant LAC investments; and *(L.N. 222 of 2018)*

(iii) the holdings do not otherwise fall within paragraphs (a) and (b);

(d) the applicable amount of the institution's direct holdings, indirect holdings and synthetic holdings of Additional Tier 1 capital instruments issued by financial sector entities, calculated in accordance with Schedule 4G, if—

(i) the entities are not the subject of consolidation under a section 3C requirement imposed on the institution;

(ii) the holdings are significant LAC investments; and *(L.N. 222 of 2018)*

(iii) the holdings do not otherwise fall within paragraphs (a) and (b);

(e) (if the institution calculates its capital adequacy ratio on a solo basis under a section 3C requirement) the amount of the institution's direct holdings of Additional Tier 1 capital instruments issued by financial sector entities that are members of the institution's consolidation group;

(f) (if the institution calculates its capital adequacy ratio on a solo-consolidated basis under a section 3C requirement) the amount of the institution's direct holdings of Additional Tier 1 capital instruments issued by financial sector entities, other than any solo-consolidated subsidiaries, that are members of the institution's consolidation group; and

(g) any amount that would otherwise be deducted from the institution's Tier 2 capital under section 48 but cannot be so deducted because the institution does not have sufficient Tier 2 capital to satisfy the deduction.

(2) An authorized institution must—

(a) exclude from the holdings referred to in subsection (1) any holdings of capital instruments issued by financial sector entities that are not included within regulatory capital in the relevant financial sectors in which those entities operate;

(b) reduce the amount to be deducted under subsection (1) by any amount of goodwill (related to any holdings of Additional Tier 1 capital instruments falling within subsection (1)(a), (b), (c), (d), (e) or (f)) already deducted under section 43(1)(a); and

(c) include in the amount to be deducted under subsection (1) potential future holdings that the institution could be contractually obliged to purchase.

48. Deductions from Tier 2 capital

(1) Subject to subsection (2), an authorized institution must deduct from its Tier 2 capital— *(L.N. 222 of 2018)*

(a) the amount of any direct holdings, indirect holdings and synthetic holdings by the institution of its own Tier 2 capital instruments, unless already derecognized under applicable accounting standards, calculated in accordance with Schedule 4E;

(b) the amount of any direct holdings, indirect holdings and synthetic holdings by the institution of Tier 2 capital instruments issued by, or non-capital LAC liabilities of, any financial sector entity where that entity has a reciprocal cross holding with the institution;

(c) the applicable amount of the institution's direct holdings, indirect holdings and synthetic holdings of Tier 2 capital instruments issued by, or non-capital LAC liabilities of, financial sector entities, calculated in accordance with Schedule 4F, if— *(L.N. 222 of 2018)*

(i) the entities are not the subject of consolidation under a section 3C requirement imposed on the institution;

(ii) the holdings are insignificant LAC investments; and

(iii) the holdings do not otherwise fall within paragraph (a) or (b) or section 48A(1)(a) or (b);

(d) the applicable amount of the institution's direct holdings, indirect holdings and synthetic holdings of Tier 2 capital instruments issued by, or non-capital LAC liabilities of, financial sector entities, calculated in accordance with Schedule 4G, if— *(L.N. 222 of 2018)*

(i) the entities are not the subject of consolidation under a section 3C requirement imposed on the institution;

(ii) the holdings are significant LAC investments; and

(iii) the holdings do not otherwise fall within paragraph (a) or (b) or section 48A(1)(a) or (b);

(e) (if the institution calculates its capital adequacy ratio on a solo basis under a section 3C requirement) the amount of the institution's direct holdings of Tier 2 capital instruments issued by financial sector entities that are members of the institution's consolidation group;

(f) (if the institution calculates its capital adequacy ratio on a solo-consolidated basis under a section 3C requirement) the amount of the institution's direct holdings of Tier 2 capital instruments issued by financial sector entities, other than any solo-consolidated subsidiaries, that are members of the institution's consolidation group; and

(g) either of the following—

(i) (if the institution maintains any non-capital LAC debt resources) any amount by which the total amount of the institution's holdings of non-capital LAC liabilities falling within section 48A exceeds the institution's non-capital LAC debt resources;

(ii) (if the institution does not maintain any non-capital LAC debt resources) the total amount of the institution's holdings of non-capital LAC liabilities falling within section 48A. *(L.N. 222 of 2018)*

(2) An authorized institution must—

(a) exclude from the holdings of Tier 2 capital instruments to be deducted under subsection (1) any holdings of capital instruments issued by financial sector entities that are not included within regulatory capital in the relevant financial sectors in which those entities operate; and

(b) include in the amount to be deducted under subsection (1) potential future holdings that the institution could be contractually obliged to purchase.

(3) The amount of an authorized institution's holdings of non-capital LAC liabilities falling within section 48A that do not exceed the institution's non-capital LAC debt resources and that are not deducted from the institution's Tier 2 capital under subsection (1)(g)(i) is to continue to be risk-weighted in accordance with one or more of Parts 4, 5, 6 and 8, as the case requires. *(L.N. 222 of 2018; L.N. 167 of 2023)*

(L.N. 222 of 2018)

48A. Total amount of holdings of non-capital LAC liabilities to be calculated for section 48(1)(g)

(1) For the purposes of section 48(1)(g), an authorized institution must calculate the total amount of the following—

(a) the amount of any direct holdings, indirect holdings and synthetic holdings by the institution of its own non-capital LAC liabilities, unless already derecognized under applicable accounting standards;

(b) the amount of any direct holdings, indirect holdings and synthetic holdings by the institution of non-capital LAC liabilities of financial sector entities that are within the same banking group as the institution but outside the scope of consolidation under a section 3C requirement;

(c) (if the institution calculates its capital adequacy ratio on a solo basis under a section 3C requirement) the amount of the institution's direct holdings of non-capital LAC liabilities of financial sector entities that are members of the institution's consolidation group; and

(d) (if the institution calculates its capital adequacy ratio on a solo-consolidated basis under a section 3C requirement) the amount of the institution's direct holdings of non-capital LAC liabilities of financial sector entities, other than solo-consolidated subsidiaries, that are members of the institution's consolidation group.

(2) In calculating the total amount under subsection (1), the institution must include potential future holdings that the institution could be contractually obliged to purchase.

(L.N. 222 of 2018)

49. *(Repealed L.N. 156 of 2012)*

Part 4

Calculation of Credit Risk for Non-securitization Exposures: STC Approach

Division 1—General

50. Application of Part 4

(1) This Part applies to an authorized institution that is required or permitted by these Rules to use the STC approach to determine the risk-weight or the risk-weighted amount of a non-securitization exposure.

(2) A reference in this Part to an authorized institution is a reference to an authorized institution that is required or permitted by these Rules to use the STC approach to determine the risk-weight or the risk-weighted amount of a non-securitization exposure.

(L.N. 167 of 2023)

51. Interpretation of Part 4

(1) In this Part— *(L.N. 137 of 2011; L.N. 167 of 2023)*

3 months' bank exposure (3個月銀行風險承擔) means an exposure to a bank or qualifying non-bank financial institution with an original contractual period of time for full repayment of not more than 3 months, where—

(a) the exposure is not associated with cross-border movement of goods (including movement of goods between Hong Kong and mainland China or between Hong Kong and Macao); and

(b) the facility to which the exposure relates is not expected or anticipated to be rolled over at the expiration of the contractual period; *(L.N. 167 of 2023)*

6 months' bank exposure (6個月銀行風險承擔) means an exposure to a bank or qualifying non-bank financial institution with an original contractual period of time for full repayment of not more than 6 months, where—

(a) the exposure is associated with cross-border movement of goods (including movement of goods between Hong Kong and mainland China or between Hong Kong and Macao); and

(b) the facility to which the exposure relates is not expected or anticipated to be rolled over at the expiration of the contractual period; *(L.N. 167 of 2023)*

ADC exposure (ADC風險承擔) means land acquisition, development and construction exposure; *(L.N. 167 of 2023)*

attributed risk-weight (歸屬風險權重)—

(a) subject to paragraphs (b), (c), (d) and (e), in relation to a person an exposure to whom would fall within an ECAI ratings based portfolio—

(i) if the person has an ECAI issuer rating—means the risk-weight that would be attributable, in accordance with Subdivision 3 of Division 3, to a senior and unsecured long-term debt obligation of the person based on that ECAI issuer rating and on the assumption that no ECAI issue specific rating has been assigned to any debt obligation of the person;

(ii) if the person does not have an ECAI issuer rating—means the risk-weight that would be attributable, in accordance with that Subdivision, to an unrated exposure to the person and on the assumption that no ECAI issue specific rating has been assigned to any debt obligation of the person;

(b) in relation to a person that is a public sector entity or sovereign foreign public sector entity—means the risk-weight that would be attributable, in accordance with section 57, to an unsecured exposure to the person;

(c) in relation to a relevant international organization or a multilateral development bank to which section 58(1) applies—means a risk-weight of 0%;

(d) in section 59C—has the meaning given by section 59C(5); and

(e) in sections 65C and 65D—means the risk-weight that would be attributable to an unsecured exposure to an obligor under Division 3; *(L.N. 167 of 2023)*

commitment (承諾), in relation to the determination of a CCF applicable to an off-balance sheet exposure, has the meaning given by section 2 of Schedule 6; *(L.N. 167 of 2023)*

commodities finance (商品融資) means short-term lending to finance reserves, inventories or receivables of exchange-traded commodities, where—

(a) the lending will be repaid from the proceeds of the sale of the commodities; and

(b) the borrower has no independent capacity to repay the lending; *(L.N. 167 of 2023)*

comprehensive approach (全面方法), in relation to the use by an authorized institution of recognized collateral which falls within section 80 to reduce the risk-weighted amount of the institution's exposures, means the method of using the recognized collateral set out in Division 7;

corporate (法團) means—

(a) a company; or

(b) a partnership or any other unincorporated body,

that is not a multilateral development bank, unspecified multilateral body, public sector entity, bank or qualifying non-bank financial institution; *(L.N. 167 of 2023)*

credit equivalent amount (信貸等值數額), in relation to an off-balance sheet exposure that is not a default risk exposure, means the credit equivalent amount of the exposure calculated in accordance with section 71(1) or (2), as the case requires; *(L.N. 44 of 2020; L.N. 167 of 2023)*

credit protection covered portion (信用保障涵蓋部分), in relation to an exposure of an authorized institution that is covered by recognized collateral, a recognized guarantee or a recognized credit derivative contract, means the portion of the exposure (which may be all of the exposure) that is covered by—

(a) in the case of recognized collateral—the current market value of the recognized collateral;

(b) in the case of a recognized guarantee or a credit derivative contract recognized under section 99(1) or (2)—the maximum liability of the credit protection provider to the institution under the recognized guarantee or recognized credit derivative contract, as the case may be;

(c) in the case of a credit derivative contract recognized under section 99(3) or (4)—the maximum liability of the credit protection provider to the institution under the recognized credit derivative contract, up to the maximum amount of the contract that may be recognized under that section;

(d) in the case of a credit derivative contract recognized under section 99B(1)—the maximum liability of the credit protection provider or credit protection providers to the institution under the external hedge referred to in that section, up to an amount equal to the amount of the internal risk transfer concerned; or

(e) in the case of a credit derivative contract recognized under section 99B(3)(a) or (b)—the maximum liability of the credit protection provider or credit protection providers to the institution under the external hedge referred to in that section, up to the maximum amount of the internal risk transfer concerned that may be recognized under that section; *(L.N. 167 of 2023)*

credit protection uncovered portion (不受信用保障涵蓋部分), in relation to an exposure of an authorized institution that is covered by recognized collateral, a recognized guarantee or a recognized credit derivative contract, means the portion of the exposure that is not the credit protection covered portion; *(L.N. 167 of 2023)*

debt securities (債務證券) means any securities other than shares, stocks or import or export trade bills;

defaulted exposure (違責風險承擔) means an exposure that—

(a) falls within section 67(2) or (3)(a), as the case requires; or

(b) is treated as a defaulted exposure by an authorized institution under section 67(3)(b); *(L.N. 167 of 2023)*

ECAI ratings based portfolio (ECAI評級基準組合)—

(a) subject to paragraph (b), means—

(i) sovereign exposures;

(ii) public sector entity exposures;

(iii) multilateral development bank exposures;

(iv) unspecified multilateral body exposures;

(v) bank exposures;

(vi) eligible covered bond exposures;

(vii) qualifying non-bank financial institution exposures;

(viii) general corporate exposures; or

(ix) specialized lending; and

(b) excludes exposures referred to in paragraph (a) that are—

(i) real estate exposures;

(ii) equity exposures;

(iii) significant capital investments in commercial entities;

(iv) exposures to capital instruments issued by financial sector entities;

(v) exposures to non-capital LAC liabilities of financial sector entities;

(vi) exposures to subordinated debts issued by banks, qualifying non-bank financial institutions or corporates;

(vii) exposures falling within section 64A, 65K or 65L; or

(viii) defaulted exposures; *(L.N. 167 of 2023)*

equity exposure (股權風險承擔) means an exposure that falls within section 54A; *(L.N. 167 of 2023)*

exposure (風險承擔), in relation to an authorized institution, means a credit exposure (including an asset) of the institution;

exposure amount (風險承擔數額)—

(a) in relation to an on-balance sheet exposure—means the principal amount of the exposure (net of specific provisions, if any);

(b) in relation to an off-balance sheet exposure to a counterparty that is a default risk exposure in respect of one or more derivative contracts or in respect of a netting set that contains both derivative contracts and SFTs—means the outstanding default risk exposure in respect of the counterparty (net of specific provisions, if any);

(c) in relation to an off-balance sheet exposure to a counterparty that is a default risk exposure in respect of one or more SFTs—means the amount of the exposure calculated in accordance with Division 2B of Part 6A (net of specific provisions, if any); or

(d) in relation to any other off-balance sheet exposure, means—

(i) the credit equivalent amount of the exposure calculated in accordance with section 71(1); or

(ii) the credit equivalent amount of the exposure calculated in accordance with section 71(2) and (3) (net of specific provisions, if any); *(L.N. 167 of 2023)*

general bank exposure (一般銀行風險承擔) means an exposure to a bank or qualifying non-bank financial institution that is not a short-term bank exposure; *(L.N. 167 of 2023)*

general corporate exposure (一般法團風險承擔) means an exposure to a corporate that is none of the following—

(a) an eligible covered bond exposure;

(b) a specialized lending;

(c) a regulatory retail exposure;

(d) an exposure falling within section 64A;

(e) a real estate exposure;

(f) an equity exposure;

(g) a significant capital investment in a commercial entity;

(h) an exposure to a capital instrument issued by a financial sector entity;

(i) an exposure to a non-capital LAC liability of a financial sector entity;

(j) an exposure to a subordinated debt;

(k) an exposure falling within section 65K or 65L;

(l) a defaulted exposure; *(L.N. 167 of 2023)*

land acquisition, development and construction exposure (土地購買、開發及建築風險承擔)—

(a) subject to paragraph (b), means an exposure to an individual, a company or a special purpose vehicle financing or refinancing—

(i) land acquisition for development and construction purposes; or

(ii) development and construction of any residential or commercial property; and

(b) excludes an exposure to an individual, a company or a special purpose vehicle financing or refinancing the acquisition of forest or agricultural land, if there is no planning consent or intention to apply for planning consent; *(L.N. 167 of 2023)*

main index (主要指數) means an index by reference to which futures contracts or option contracts are traded on a recognized exchange;

object finance (物品融資) means a method of funding the acquisition of physical assets (other than immovable property) where the repayment of the funds provided by a lender is dependent on the cash flows generated by the assets that have been financed and pledged (or otherwise provided as security) or assigned to the lender; *(L.N. 167 of 2023)*

project finance (項目融資) means a method of financing or refinancing a single project (other than a project of development and construction of residential or commercial property) in which the lender that provides the loan looks primarily to the revenue generated by the project, both as the source of repayment of, and as security for, the loan; *(L.N. 167 of 2023)*

principal amount (本金額)—

(a) in relation to an on-balance sheet exposure of an authorized institution—

(i) if the exposure is measured at fair value, means the value of the exposure determined in accordance with section 4A; or

(ii) if the exposure is not measured at fair value, means the book value (including accrued interest) of the exposure; or *(L.N. 137 of 2011)*

(b) in relation to an off-balance sheet exposure of an authorized institution, means—

(i) subject to subparagraph (ii), in the case of an exposure listed in Schedule 6, the contracted amount of the exposure; *(L.N. 44 of 2020; L.N. 167 of 2023)*

(ii) in the case of an exposure listed in Schedule 6 that arises from an undrawn facility or the undrawn portion of a partially drawn facility, the amount of the undrawn commitment; *(L.N. 175 of 2017; L.N. 44 of 2020; L.N. 167 of 2023)*

(iii) subject to subparagraph (iv), in the case of an exposure in respect of a derivative contract, the notional amount of the contract; *(L.N. 44 of 2020)*

(iv) in the case of an exposure in respect of a derivative contract where the stated notional amount of the contract is leveraged or enhanced by the structure of the contract, the effective notional amount of the contract calculated by taking into account the effect of the leverage or enhancement, as the case requires; *(L.N. 44 of 2020)*

(v) in the case of an exposure to a person arising from the person holding collateral posted by the institution in a manner that is not bankruptcy remote from the person, the fair value of the collateral; *(L.N. 156 of 2012)*

real estate exposure (地產風險承擔) means—

(a) an exposure extended by a lender to a borrower—

(i) that is secured by immovable property; and

(ii) that is required by the facility agreement between the lender and the borrower to be secured on the immovable property referred to in subparagraph (i); or

(b) an ADC exposure; *(L.N. 167 of 2023)*

recognized collateral (認可抵押品) means collateral recognized under section 77;

recognized credit derivative contract (認可信用衍生工具合約) means—

(a) a credit derivative contract recognized under section 99(1), (2) or (5);

(b) a credit derivative contract to the extent that it is recognized under section 99(3) or (4);

(c) an internal risk transfer recognized under section 99B(1); or

(d) an internal risk transfer to the extent that it is recognized under section 99B(3)(a) or (b); *(L.N. 167 of 2023)*

recognized guarantee (認可擔保) means a guarantee recognized under section 98;

regulatory real estate exposure (監管地產風險承擔)—see section 65(1); *(L.N. 167 of 2023)*

regulatory retail exposure (監管零售風險承擔)—see section 64(2); *(L.N. 167 of 2023)*

short-term bank exposure (短期銀行風險承擔) means—

(a) a 3 months' bank exposure; or

(b) a 6 months' bank exposure; *(L.N. 167 of 2023)*

significant capital investment in a commercial entity (對商業實體的重大資本投資) means an authorized institution's holdings of shares in a commercial entity if—

(a) the holdings amount to more than 10% of the ordinary shares issued by the commercial entity; or

(b) the commercial entity is an affiliate of the institution; *(L.N. 167 of 2023)*

simple approach (簡易方法), in relation to the use by an authorized institution of recognized collateral which falls within section 79 to reduce the risk-weighted amount of the institution's exposures, means the method of using the recognized collateral set out in Division 6;

small business (小型企業) means—

(a) subject to paragraph (b), a corporate with annual sales not exceeding $500 million for the most recent financial year; or

(b) a corporate in a consolidated group where the annual sales for the group did not exceed $500 million for the most recent financial year; *(L.N. 167 of 2023)*

sovereign foreign public sector entity (屬官方實體的非本地公營單位)—

(a) subject to paragraph (b), means a foreign public sector entity which is regarded as a sovereign for the purposes of calculating the capital adequacy ratio of a bank by the relevant banking supervisory authority of the jurisdiction in which the entity and the bank are incorporated;

(b) does not include a restricted foreign public sector entity; *(E.R. 3 of 2021; L.N. 167 of 2023)*

specialized lending (專門性借貸) means an exposure of a lender to a corporate that—

(a) arises from object finance, project finance or commodities finance; and

(b) possesses both of the following characteristics, either in legal form or economic substance—

(i) the corporate has few or no other material assets or activities, and therefore the primary source of repayment of the exposure is the income generated by the asset or assets being financed by the lender, rather than the independent capacity of the corporate;

(ii) the terms of the exposure give the lender a substantial degree of control over the asset or assets being financed and the income that the asset or assets generate; *(L.N. 167 of 2023)*

specific provisions (特定準備金) includes partial write-offs; *(L.N. 167 of 2023)*

subordinated debt (後償債項), in relation to an obligor that is a bank, qualifying non-bank financial institution or corporate—

(a) includes a subordinated debt or junior subordinated debt—

(i) that is not an equity exposure to the obligor; and

(ii) that is higher in ranking, or senior, to equity exposures to the obligor in terms of the priority of repayment; but

(b) if the obligor is a financial sector entity, excludes—

(i) a capital instrument issued by the obligor; and

(ii) a non-capital LAC liability of the obligor; *(L.N. 167 of 2023)*

unhedged credit exposure (無對沖信用風險承擔) has the meaning given by section 51A; *(L.N. 167 of 2023)*

unrated exposure (無評級風險承擔) means—

(a) a non-securitization exposure—

(i) that—

(A) falls within an ECAI ratings based portfolio; and

(B) does not have an ECAI issue specific rating assigned to it; and

(ii) the obligor in respect of which has neither of the following—

(A) an ECAI issuer rating;

(B) a long-term ECAI issue specific rating assigned to any other debt obligation issued or undertaken by the obligor; or

(b) a non-securitization exposure—

(i) that—

(A) falls within an ECAI ratings based portfolio; and

(B) does not have an ECAI issue specific rating assigned to it;

(ii) the obligor in respect of which has either or both of the following—

(A) one or more ECAI issuer ratings;

(B) one or more than one debt obligation that has at least one long-term ECAI issue specific rating assigned to it; and

(iii) in respect of which, because of section 4B(1)(b), (c) or (d), 4C(6), 54E or 54F, none of the ratings referred to in subparagraph (ii) can be used for determining the risk-weight attributable to the exposure in accordance with Subdivision 3 of Division 3. *(L.N. 167 of 2023)*

(L.N. 44 of 2020; L.N. 167 of 2023)

(2) *(Repealed L.N. 167 of 2023)*

51A. Meaning of *unhedged credit exposure*

(1) For the purposes of this Part—

unhedged credit exposure (無對沖信用風險承擔) means an exposure falling within section 64 or 65B where—

(a) the obligor in respect of the exposure is—

(i) if the exposure falls within section 64—an individual; and

(ii) if the exposure falls within section 65B—

(A) an individual; or

(B) a property-holding shell company with an individual acting as a guarantor for the exposure;

(b) the exposure is a non-revolving loan—

(i) with a pre-specified schedule of repayments of principal and interest and predefined repayment amounts such that the whole loan amount will be repaid within a fixed repayment period (including a loan with an irregular repayment structure or a loan that allows re-borrowing of the repaid principal with or without extension of the fixed repayment period); or

(ii) that will be repaid within a fixed repayment period with a bullet payment;

(c) the exposure is denominated in a currency that differs from—

(i) the currency of the obligor's source of income; or

(ii) if the obligor is a property-holding shell company and the primary source of repayment is the income of the guarantor—the currency of the guarantor's source of income; and

(d) less than 90% of the relevant amount of the exposure is hedged against the foreign exchange risk resulting from the mismatch in currencies referred to in paragraph (c) through one or both of the following means—

(i) income or income sources of the obligor or guarantor in a currency that matches the currency in which the exposure is denominated;

(ii) derivative contracts or other legal contracts with financial institutions.

(2) An authorized institution must regard an exposure as falling within paragraph (c) of the definition of ***unhedged credit exposure*** in subsection (1) if—

(a) the obligor in respect of the exposure has sources of income that are denominated in more than one currency; or

(b) the repayment of the exposure is dependent on the income of the guarantor of the exposure whose sources of income are denominated in more than one currency.

(3) For the purposes of paragraph (d) of the definition of ***unhedged credit exposure*** in subsection (1)—

relevant amount (有關數額)—

(a) in relation to an exposure falling within paragraph (b)(i) of that definition, means each of the scheduled repayment amounts; and

(b) in relation to an exposure falling within paragraph (b)(ii) of that definition, means the whole outstanding loan amount.

(4) If an authorized institution does not have readily available or sufficient information to determine whether an exposure falls within paragraph (c) of the definition of ***unhedged credit exposure*** in subsection (1), the institution—

(a) may regard the exposure as not falling within that paragraph if the exposure is to a non-revolving loan granted by the institution before the commencement date* of Part 3 of the Banking (Capital) (Amendment) Rules 2023; or

(b) if paragraph (a) does not apply, must regard the exposure as falling within paragraph (c) of that definition if the exposure is denominated in a currency that differs from the currency of the place of residence of the obligor or guarantor.

(L.N. 167 of 2023)

Editorial Note:

* Commencement date: 1 January 2025.

Division 2—Calculation of Credit Risk under STC Approach, Exposures to be Covered in Calculation, and Classification of Exposures

52. Calculation of risk-weighted amount of exposures

(1) Subject to section 53, if an authorized institution is required under these Rules to use only the STC approach to calculate the credit risk for all of its non-securitization exposures, the institution must calculate an amount representing the degree of credit risk to which it is exposed by aggregating—

(a) the risk-weighted amounts of the institution's on-balance sheet exposures; and

(b) the risk-weighted amounts of the institution's off-balance sheet exposures.

(2) Unless otherwise stated in these Rules, if an authorized institution is required or permitted by these Rules to use the STC approach to calculate the credit risk for some of its non-securitization exposures, the institution must calculate the risk-weighted amounts of those exposures in accordance with subsections (3), (4), (5), (6), (7) and (8).

(3) Subject to subsection (5), for the purposes of subsections (1) and (2)—

(a) the risk-weighted amount of each exposure (except CIS exposure and default risk exposure in respect of derivative contracts or SFTs) must be calculated by multiplying the exposure amount of the exposure by the relevant risk-weight attributable to the exposure determined under Division 3;

(b) the risk-weighted amount of each CIS exposure must be calculated in accordance with Division 3A; and

(c) the risk-weighted amount of each default risk exposure in respect of derivative contracts or SFTs is the amount specified in subsection (4).

(4) If an authorized institution—

(a) has an IMM(CCR) approval—

(i) the risk-weighted amount of the default risk exposure in respect of derivative contracts or SFTs covered by the IMM(CCR) approval is the IMM(CCR) risk-weighted amount;

(ii) the risk-weighted amount of the default risk exposure in respect of derivative contracts that are not covered by the IMM(CCR) approval or that fall within section 10B(5) or (7) is the sum of the SA-CCR risk-weighted amounts calculated for the contracts; and

(iii) the risk-weighted amount of the default risk exposure in respect of SFTs that are not covered by the IMM(CCR) approval or that fall within that section is the sum of the SFT risk-weighted amounts calculated for the SFTs;

(b) does not have an IMM(CCR) approval for any of its derivative contracts or SFTs—

(i) the risk-weighted amount of the default risk exposure in respect of derivative contracts is the sum of the SA-CCR risk-weighted amounts calculated for the contracts; and

(ii) the risk-weighted amount of the default risk exposure in respect of SFTs is the sum of the SFT risk-weighted amounts calculated for the SFTs.

(5) An authorized institution may reduce the risk-weighted amount of its exposure by taking into account the effect

of any recognized credit risk mitigation in respect of the exposure in the manner set out in Divisions 5, 6, 7, 8, 9 and 10, unless—

(a) the institution has made disclosures in respect of credit risk for the immediately preceding applicable reporting periods that do not fully comply with the applicable provisions of the Disclosure Rules; or

(b) subsection (6), (7) or (8) applies to the recognized credit risk mitigation concerned.

(6) If an exposure of an authorized institution has an ECAI issue specific rating, the institution must not take into account under subsection (5) the effect of any recognized credit risk mitigation applicable to the exposure that has already been taken into account in that rating.

(7) If an authorized institution has bought credit protection for an exposure and the credit protection is in the form of a single-name credit default swap that falls within section 226J(1), the institution must not take into account under subsection (5) the credit risk mitigating effect of the swap.

(8) If an exposure of an authorized institution is a default risk exposure in respect of derivative contracts or SFTs, the institution must not take into account under subsection (5) the effect of any recognized credit risk mitigation applicable to the exposure that has already been taken into account in the calculation of the amount of the default risk exposure under Part 6A.

(9) In this section—

applicable provisions (適用條文), in relation to an authorized institution that uses the STC approach to calculate the credit risk for all or part of its non-securitization exposures, means the provisions set out in Division 4 of Part 2A of the Disclosure Rules the application of which to the institution has not been exempted by the Monetary Authority under section 3 of those Rules;

applicable reporting period (適用報告期), in relation to an applicable provision, means the reporting period (within the meaning of the Disclosure Rules) referred to in that applicable provision;

Disclosure Rules (《披露規則》) means the Banking (Disclosure) Rules (Cap. 155 sub. leg. M);

SFT risk-weighted amount (SFT風險加權數額), in relation to a default risk exposure in respect of an SFT or portfolio of SFTs, means—

(a) if the amount of the default risk exposure in respect of an SFT is calculated in accordance with section 226MJ—the risk-weighted amount of the default risk exposure calculated in accordance with section 85 or 88, as the case requires; or

(b) if the amount of the default risk exposure in respect of a portfolio of SFTs is calculated in accordance with section 226MK—the risk-weighted amount of the default risk exposure calculated by multiplying the exposure amount of the default risk exposure by the risk-weight attributable to the exposure determined under Division 3.

(L.N. 167 of 2023)

53. On-balance sheet exposures and off-balance sheet exposures to be covered

(1) Subject to subsection (2), if an authorized institution is required under these Rules to use only the STC approach to calculate the credit risk for all of its non-securitization exposures, the institution must, for the purpose of calculating under section 52 an amount representing the degree of

credit risk to which it is exposed, take into account and risk-weight—

(a) all of the institution's on-balance sheet exposures and off-balance sheet exposures booked in its banking book; and

(b) all of the institution's following exposures—

(i) default risk exposures to counterparties in respect of derivative contracts or SFTs booked in its trading book;

(ii) credit exposures to counterparties in respect of transactions (other than repo-style transactions) in securities, foreign exchange or commodities booked in its trading book that remain outstanding after the settlement dates in respect of the transactions;

(iii) credit exposures to counterparties in respect of unsegregated collateral posted by it and held by the counterparties for transactions or contracts booked in its trading book; and

(c) if applicable, all of the institution's market risk exposures that are exempted from section 17 under section 22, except for its total net open position in foreign exchange exposures as derived in accordance with section 296.

(2) Subsection (1) does not apply to—

(a) securitization exposures;

(b) the underlying exposures of eligible traditional securitization transactions (within the meaning of section 229) if the authorized institution opts to apply the treatment under section 230(1) to the underlying exposures;

(c) default fund contributions made to qualifying CCPs and non-qualifying CCPs (within the meaning of section 226V(1));

(d) default risk exposures to qualifying CCPs;

(e) exposures that are risk-weighted as if they were default risk exposures to qualifying CCPs under Division 4 of Part 6A; and

(f) any portion of an exposure (which may be all of the exposure) that is required to be deducted from any of the institution's CET1 capital, Additional Tier 1 capital and Tier 2 capital under Division 4 of Part 3.

(L.N. 167 of 2023)

54. Classification of exposures

(1) An authorized institution must classify its on-balance sheet exposures and off-balance sheet exposures into one only of the following categories and subcategories—

(a) exposures other than CIS exposures—

(i) ECAI ratings based portfolios;

(ii) exposures that are neither ECAI ratings based portfolios nor defaulted exposures;

(iii) defaulted exposures;

(b) CIS exposures.

(2) An authorized institution must—

(a) further classify each of its exposures falling within subsection (1)(a)(i), according to the obligor or the nature of the exposure, into one only of the ECAI ratings based portfolios; and

(b) determine the risk-weight attributable to each of the exposures in accordance with Subdivisions 2 and 3 of Division 3 and, if applicable, Subdivision 9 of that Division.

(3) An authorized institution must—

(a) further classify each of its exposures falling within subsection (1)(a)(ii), according to the obligor or the nature of the exposure, into one only of the following classes—

(i) retail exposures;

(ii) exposures falling within section 64A;

(iii) real estate exposures;

(iv) equity exposures (other than those falling within subparagraph (v) or (vi));

(v) significant capital investments in commercial entities;

(vi) holdings of capital instruments issued by, and non-capital LAC liabilities of, financial sector entities;

(vii) subordinated debts issued by banks, qualifying non-bank financial institutions and corporates;

(viii) cash and gold;

(ix) items in the process of clearing or settlement;

(x) other exposures; and

(b) determine the risk-weight attributable to each of the exposures in accordance with Subdivision 4, 5, 6 or 7 of Division 3, as the case requires, and, if applicable, Subdivision 9 of that Division.

(4) An authorized institution must determine the risk-weight attributable to each of the exposures falling within subsection (1)(a)(iii) in accordance with Subdivision 8 of Division 3 and, if applicable, Subdivision 9 of that Division.

(5) An authorized institution must determine the risk-weight attributable to each of the exposures falling within subsection (1)(b) in accordance with Division 3A.

(6) For the purposes of subsection (2)(a), an authorized institution may treat an entity incorporated outside Hong Kong that is none of the following as a corporate rather than a qualifying non-bank financial institution—

(a) a public sector entity;

(b) a multilateral development bank;

(c) an unspecified multilateral body;

(d) a bank;

(e) an entity that falls within paragraph (a) or (b) of the definition of ***qualifying non-bank financial institution*** in section 2(1).

(L.N. 167 of 2023)

54A. Provisions supplementary to section 54—equity exposures

(1) If an exposure to an instrument issued by an entity (***issuer***) falls within subsection (2), (3), (4) or (5) based on the economic substance of the instrument, an authorized institution must classify the exposure as an equity exposure for the purposes of this Part unless—

(a) the exposure is a CIS exposure;

(b) the exposure is fully deducted from the institution's capital base in accordance with Division 4 of Part 3;

(c) if classification of the exposure is for the purpose of calculating the institution's capital adequacy ratio on a solo-consolidated basis, the issuer is—

(i) a solo-consolidated subsidiary of the institution; and

(ii) the subject of consolidation under a section 3C requirement imposed on the institution; or

(d) if classification of the exposure is for the purpose of calculating the institution's capital adequacy ratio on a consolidated basis, the issuer is the subject of consolidation under a section 3C requirement imposed on the institution.

(2) An instrument falls within this subsection if it represents direct or indirect ownership interests (whether voting or non-voting) in the assets and income of the issuer or another entity.

(3) An instrument falls within this subsection if it meets all of the following requirements—

(a) it is irredeemable in the sense that the return of invested funds can be achieved only by the sale of the investment or sale of the rights to the investment or by the liquidation of the issuer;

(b) it does not embody an obligation on the part of the issuer;

(c) it conveys a residual claim on the assets or income of the issuer.

(4) An instrument falls within this subsection if—

(a) the issuer is not a bank but the instrument would be a Tier 1 capital in accordance with the current Basel Framework if it were issued by a bank; or

(b) it embodies an obligation on the part of the issuer and meets any one or more of the following requirements—

(i) the issuer may indefinitely defer the settlement of the obligation;

(ii) the obligation requires (or permits at the issuer's discretion) settlement by issuance of a fixed number of the issuer's equity shares;

(iii) the obligation requires (or permits at the issuer's discretion) settlement by issuance of a variable number of the issuer's equity shares and, other things being equal, any change in the value of the obligation is attributable to, comparable to, and in the same direction as, the change in the value of a fixed number of the issuer's equity shares;

(iv) the holder of the instrument has the option to require that the obligation be settled in equity shares, unless the authorized institution demonstrates to the satisfaction of the Monetary Authority that—

(A) in the case of a traded instrument—the instrument trades more like the debt of the issuer than equity; or

(B) in the case of a non-traded instrument—the instrument should be treated as a debt position.

(5) An instrument falls within this subsection if it is a debt obligation, a derivative contract or an instrument in any other form, that—

(a) does not fall within subsection (2), (3) or (4); and

(b) is structured with the intent of conveying the economic substance of equity ownership.

(6) To avoid doubt, equity exposures—

(a) include liabilities (such as short positions) falling within subsection (5) from which the return is linked to that of equities unless the liabilities are directly hedged by equity holdings such that the resulted net position in the equities concerned does not involve material risk; and

(b) exclude equity investments that are structured with the intent of conveying the economic substance of debt holdings or securitization exposures.

(7) The Monetary Authority may, by written notice given to an authorized institution, require the institution to treat a debt position of the institution as an equity exposure for the purpose of calculating its credit risk if the Monetary Authority is satisfied that the nature and economic substance of the debt position are such that the debt position should more realistically be characterized as an equity exposure than as a debt position.

(8) An authorized institution must comply with the requirements of a notice given to it under subsection (7).

(L.N. 167 of 2023)

Division 3—Determination of Risk-weights Applicable to Exposures other than CIS Exposures

(L.N. 167 of 2023)

Subdivision 1—Application of Division 3

(L.N. 167 of 2023)

54B. Application of Division 3

This Division applies to the determination of risk-weights applicable to on-balance sheet exposures, and off-balance sheet exposures, that are not CIS exposures.

(L.N. 167 of 2023)

Subdivision 2—Due Diligence Requirements

(L.N. 167 of 2023)

54C. Due diligence requirements

(1) An authorized institution must perform due diligence on its credit exposures (at origination and at least annually thereafter) to ensure that it has an adequate understanding of the risk profile and characteristics of the obligors in respect of the exposures.

(2) If an authorized institution determines the risk-weight of an exposure in accordance with Subdivision 3 by using an ECAI issuer rating or a long-term ECAI issue specific rating (***relevant rating***)—

(a) the institution must, based on the due diligence performed under subsection (1) on the exposure, assess at least annually whether the risk-weight (***rating-based RW***) so determined is appropriate and prudent for the exposure;

(b) if the due diligence referred to in paragraph (a) indicates that the credit risk of the exposure is higher than that implied by the rating-based RW, the institution must allocate to the exposure a risk-weight that is at least the next higher base risk-weight than the base risk-weight applicable to the ECAI ratings based portfolio to which the exposure belongs based on the relevant rating; and

(c) if there is no such next higher base risk-weight, the institution must allocate to the exposure the highest base risk-weight applicable to the ECAI ratings based portfolio to which the exposure belongs.

(3) An authorized institution must not, according to the due diligence performed by it on an exposure, allocate to the exposure a risk-weight that is lower than the exposure's rating-based RW.

(4) Subsection (2) does not apply to—

(a) sovereign exposures; or

(b) public sector entity exposures.

(5) Despite the requirements of this Division, the Monetary Authority may, by written notice given to one or more authorized institutions, require the institution to allocate to an exposure, or exposures belonging to a class of exposure, a risk-weight specified in the notice, if the Monetary Authority considers that—

(a) the exposure or the class has, or could reasonably be construed as potentially having, adverse impacts on the financial soundness of the institution; or

(b) flexibility in the capital treatment of the class is necessary or expedient for supporting the economy or maintaining the stability and effective working of the financial system of Hong Kong.

(6) An authorized institution must comply with the requirements of a notice given to it under subsection (5).

(7) In this section—

base risk-weight (基準風險權重)—

(a) in relation to a multilateral development bank exposure or unspecified multilateral body exposure, means any risk-weight specified in column 3 of Table 2B;

(b) in relation to a bank exposure or qualifying non-bank financial institution exposure, means any risk-weight specified in column 3 of Table 3;

(c) in relation to an eligible covered bond exposure, means any risk-weight specified in column 3 of Table 4B or column 3 of Table 4C; and

(d) in relation to a general corporate exposure or a specialized lending, means any risk-weight specified in column 3 or 4 of Table 5.

(L.N. 167 of 2023)

Subdivision 3—ECAI Ratings Based Portfolios

(L.N. 167 of 2023)

54D. Mapping ECAI rating to credit quality grade

(1) For the purpose of determining the risk-weight attributable to an exposure that falls within one of the ECAI ratings based portfolios and that is not an unrated exposure, an authorized institution must determine the credit quality grade applicable to the exposure in accordance with this section and sections 54E and 54F.

(2) If—

(a) an exposure is a sovereign exposure, a multilateral development bank exposure that is not eligible for a risk-weight of 0%, an unspecified multilateral body exposure, a bank exposure, an eligible covered bond exposure, a qualifying non-bank financial institution exposure (***QNBFI exposure***), a general corporate exposure to a corporate incorporated outside the home jurisdictions of Type B ECAIs or a specialized lending; and

(b) there is a long-term ECAI issue specific rating assigned to the exposure by a Type A ECAI,

an authorized institution must determine the credit quality grade applicable to the exposure by mapping the long-term ECAI issue specific rating of the exposure to a credit quality grade in accordance with the LT ECAI rating mapping table for Type A ECAIs.

(3) If—

(a) an exposure is a bank exposure, a QNBFI exposure, a general corporate exposure to a corporate incorporated outside the home jurisdictions of Type B ECAIs or a specialized lending; and

(b) there is a short-term ECAI issue specific rating assigned to the exposure by a Type A ECAI,

an authorized institution must determine the credit quality grade applicable to the exposure by mapping the short-term ECAI issue specific rating of the exposure to a credit quality grade in accordance with the ST ECAI rating mapping table for Type A ECAIs.

(4) If—

(a) an exposure is a general corporate exposure to a corporate incorporated in the home jurisdiction of a Type B ECAI; and

(b) there is a long-term ECAI issue specific rating or short-term ECAI issue specific rating assigned to the exposure by a Type A ECAI or that Type B ECAI,

an authorized institution must determine the credit quality grade applicable to the exposure by mapping the rating of the exposure to a credit quality grade in accordance with the LT ECAI rating mapping table or the ST ECAI rating mapping table, as the case requires, applicable to the ECAI that assigns the rating.

(5) If—

(a) an exposure is a sovereign exposure, a multilateral development bank exposure that is not eligible for a risk-weight of 0% or an unspecified multilateral body exposure;

(b) there is no long-term ECAI issue specific rating assigned to the exposure by any Type A ECAI; and

(c) a Type A ECAI has assigned an ECAI issuer rating to the obligor in respect of the exposure or a long-term ECAI issue specific rating (***reference rating***) to any other exposure to the obligor,

an authorized institution must determine the credit quality grade applicable to the exposure by mapping the ECAI issuer rating of the obligor or the reference rating, as the case may be, to a credit quality grade in accordance with the LT ECAI rating mapping table for Type A ECAIs.

(6) If—

(a) an exposure is a bank exposure, a QNBFI exposure or a general corporate exposure to a corporate incorporated outside the home jurisdictions of Type B ECAIs;

(b) there is neither a long-term ECAI issue specific rating nor a short-term ECAI issue specific rating assigned to the exposure by any Type A ECAI; and

(c) a Type A ECAI has assigned an ECAI issuer rating to the obligor in respect of the exposure or a long-term ECAI issue specific rating (***reference rating***) to any other exposure to the obligor,

an authorized institution must determine the credit quality grade applicable to the exposure by mapping the ECAI issuer rating of the obligor or the reference rating, as the case may be, to a credit quality grade in accordance with the LT ECAI rating mapping table for Type A ECAIs.

(7) If—

(a) an exposure is a general corporate exposure to a corporate incorporated in the home jurisdiction of a Type B ECAI;

(b) there is neither a long-term ECAI issue specific rating nor a short-term ECAI issue specific rating assigned to the exposure by any ECAI; and

(c) a Type A ECAI or the Type B ECAI referred to in paragraph (a) has assigned an ECAI issuer rating to the corporate or a long-term ECAI issue specific rating (***reference rating***) to any other exposure to the corporate,

an authorized institution must determine the credit quality grade applicable to the exposure by mapping the ECAI issuer rating of the corporate or the reference rating, as the case may be, to a credit quality grade in accordance with the LT ECAI rating mapping table applicable to the ECAI that assigns the rating.

(8) If an exposure is a public sector entity exposure (***PSE exposure***) (including a PSE exposure to a sovereign foreign public sector entity), an authorized institution must—

(a) map the ECAI issuer rating assigned to the sovereign of the jurisdiction in which the public sector entity is incorporated to a credit quality grade in accordance with the LT ECAI rating mapping table for Type A ECAIs; and

(b) regard the credit quality grade so obtained as the credit quality grade applicable to the PSE exposure.

(9) For the purpose of determining whether a multilateral development bank exposure is eligible for a risk-weight of 0%, an authorized institution must determine the credit quality grade applicable to the exposure by mapping the ECAI issuer rating of the multilateral development bank concerned to a credit quality grade in accordance with the LT ECAI rating mapping table for Type A ECAIs.

(L.N. 167 of 2023)

54E. Application of ECAI ratings

(1) This section applies to the use of ECAI ratings by an authorized institution under this Part for determining the risk-weight attributable to an exposure (however described) (***exposure A***) that falls within one of the ECAI ratings based portfolios.

(2) In complying with the requirements of section 54D, the institution must—

(a) if exposure A has only 1 ECAI issue specific rating—use that rating;

(b) if exposure A has 2 ECAI issue specific ratings that would map into different credit quality grades under that section and result in the allocation of different risk-weights to exposure A under the relevant section in relation to exposure A—use the rating that would result in the allocation of the higher of those risk-weights; and

(c) if exposure A has 3 or more ECAI issue specific ratings—refer to the 2 ratings that would, under that section, map into credit quality grades the use of which would result in the allocation of the lowest risk-weights to exposure A under the relevant section in relation to exposure A, and—

(i) if the 2 lowest risk-weights are the same, use any one of the 2 ratings; or

(ii) if the 2 lowest risk-weights are different, use the rating that would result in the allocation of the higher of those 2 risk-weights.

(3) Subject to subsections (5) and (6), if exposure A does not have an ECAI issue specific rating and the obligor in respect of exposure A does not have an ECAI issuer rating but there is a reference exposure, in complying with the requirements

of section 54D the institution must determine the rating to be used as follows—

(a) if the long-term ECAI issue specific rating of the reference exposure is a low quality rating, the institution may use that long-term ECAI issue specific rating if exposure A ranks equally with, or is subordinated to, the reference exposure in respect of payment or repayment;

(b) if the long-term ECAI issue specific rating of the reference exposure is a high quality rating, the institution may use that long-term ECAI issue specific rating if exposure A ranks equally with, or senior to, the reference exposure in respect of payment or repayment.

(4) Subject to subsection (5), if exposure A does not have an ECAI issue specific rating and the obligor in respect of exposure A has an ECAI issuer rating but there is no reference exposure, in complying with the requirements of section 54D the institution must determine the rating to be used as follows—

(a) if the ECAI issuer rating is a low quality rating, the institution may use that ECAI issuer rating if—

(i) that rating is only applicable to unsecured exposures to the obligor as an issuer that are not subordinated to other exposures to that obligor; and

(ii) exposure A ranks equally with, or is subordinated to, the unsecured exposures referred to in subparagraph (i);

(b) subject to paragraph (c), if the ECAI issuer rating is a high quality rating, the institution may use that ECAI issuer rating if—

(i) that rating is only applicable to unsecured exposures to the obligor as an issuer that are not subordinated to other exposures to that obligor; and

(ii) exposure A is not subordinated to other exposures to that obligor;

(c) if the ECAI issuer rating is a high quality rating that only applies to a specific exposure class, the institution may use that ECAI issuer rating if—

(i) exposure A is in that exposure class;

(ii) that rating is only applicable to unsecured exposures to the obligor as an issuer that are not subordinated to other exposures to that obligor in that exposure class; and

(iii) exposure A is not subordinated to other exposures to the obligor in that exposure class.

(5) Subject to subsection (6), if exposure A is of a kind referred to in subsection (3) and the reference exposure has more than one long-term ECAI issue specific rating, or is of a kind referred to in subsection (4) and the obligor in respect of exposure A has more than one ECAI issuer rating, in complying with the requirements of section 54D, the institution must determine the rating to be used as follows—

(a) the institution must apply subsection (3) to each long-term ECAI issue specific rating or subsection (4) to each ECAI issuer rating, as the case requires;

(b) if it is determined under paragraph (a) that only 1 long-term ECAI issue specific rating or ECAI issuer rating can be used—the institution must use that rating;

(c) if it is determined under paragraph (a) that 2 long-term ECAI issue specific ratings or 2 ECAI issuer ratings can be used and the use of the 2 ratings would result in the allocation of different risk-weights to exposure A under the relevant section in relation to exposure A—the institution must use the rating that would result in the allocation of the higher of the 2 different risk-weights;

(d) if it is determined under paragraph (a) that 3 or more ECAI issue specific ratings or 3 or more ECAI issuer ratings can be used and the use of those ratings would result in the allocation of different risk-weights to exposure A under the relevant section in relation to exposure A—the institution must refer to the 2 ratings that would result in the allocation of the lowest risk-weights to exposure A and—

(i) if the 2 lowest risk-weights are the same, use any one of the 2 ratings; or

(ii) if the 2 lowest risk-weights are different, use the rating that would result in the allocation of the higher of those 2 risk-weights.

(6) If exposure A is of a kind referred to in subsection (3) and there is more than one reference exposure, the institution must—

(a) apply subsection (3) or (5), as the case requires, to each reference exposure, to determine the long-term ECAI issue specific rating to be used for the purposes of paragraph (b); and

(b) apply subsection (2), as if the long-term ECAI issue specific ratings determined under paragraph (a) were those of exposure A, to determine the long-term ECAI issue specific rating to be used for the purpose of complying with the requirements of section 54D.

(7) If—

(a) exposure A does not have an ECAI issue specific rating;

(b) the obligor in respect of exposure A has—

(i) at least one reference exposure that has one or more long-term ECAI issue specific ratings; and

(ii) one or more ECAI issuer ratings; and

(c) the use, in accordance with section 54D and the relevant section in relation to exposure A, of the ratings below would result in the allocation of 2 different risk-weights to exposure A—

(i) the long-term ECAI issue specific rating that would be determined under subsection (3), (5) or (6), as the case requires, as if the obligor did not have any ECAI issuer rating; and

(ii) the ECAI issuer rating that would be determined under subsection (4) or (5), as the case requires, as if there were no reference exposure,

the institution may, in complying with the requirements of that section, use the rating that would result in the allocation of the lower of the 2 different risk-weights to exposure A.

(8) In determining the ECAI rating to be used under subsection (3), (4), (5), (6) or (7)—

(a) subject to paragraph (b), the institution—

(i) must use ECAI ratings applicable to foreign currency, if available, to the extent that exposure A is denominated in foreign currency;

(ii) must use ECAI ratings applicable to local currency, if available, to the extent that exposure A is denominated in local currency; and

(iii) may use ECAI issuer ratings applicable to foreign currency, if available, to the extent that—

(A) exposure A is denominated in local currency; and

(B) no ECAI rating applicable to local currency is available;

(b) if exposure A is denominated in a currency different from the local currency of the obligor in respect of exposure A, the institution may use the obligor's ECAI rating applicable to the obligor's local currency, if available, for the purpose of—

(i) risk-weighting exposure A where exposure A arises from the institution's participation in an exposure created by a multilateral development bank; or

(ii) risk-weighting the credit protection covered portion of exposure A where exposure A is guaranteed by a multilateral development bank against the risk of the obligor not being able to repay exposure A to the institution because of exchange controls of the jurisdiction in which the obligor is located.

(9) In this section—

high quality rating (高質素評級), in relation to exposure A, means an ECAI issuer rating assigned to the obligor in respect of exposure A, or a long-term ECAI issue specific rating assigned to a reference exposure to the obligor in respect of exposure A, that, if being used to determine a risk-weight attributable to exposure A in accordance with section 54D and the relevant section in relation to exposure A, would result in the allocation of a risk-weight to exposure A that would be lower than the risk-weight that would be allocated to an unrated exposure to the obligor;

low quality rating (低質素評級), in relation to exposure A, means an ECAI issuer rating assigned to the obligor in respect of exposure A, or a long-term ECAI issue specific rating assigned to a reference exposure to the obligor in respect of exposure A, that, if being used to determine a risk-weight attributable to exposure A in accordance with section 54D and the relevant section in relation to exposure A, would result in the allocation of a risk-weight to exposure A that would be equal to or higher than the risk-weight that would be allocated to an unrated exposure to the obligor;

reference exposure (參照風險承擔), in relation to the obligor in respect of exposure A, means an exposure (other than exposure A) to the obligor that has one or more long-term ECAI issue specific ratings assigned to it;

relevant section (有關條文), in relation to an exposure that belongs to one of the ECAI ratings based portfolios, means the section in this Subdivision that is applicable to the ECAI ratings based portfolio to which the exposure belongs, but excludes sections 59A and 61(3) and (4).

(L.N. 167 of 2023)

54F. Further restrictions on use of ECAI ratings

(1) For the purposes of this Part—

(a) an authorized institution may use an ECAI rating to determine the risk-weight attributable to its exposure only if the rating takes into account and reflects the entire amount of the exposure with regard to all payments owed to the institution;

(b) subject to subsection (2), an authorized institution must not use an ECAI rating assigned to a bank or bank exposure that incorporates assumptions of implicit government support unless the bank is a public bank owned by the government concerned; and

(c) subject to subsection (2), any ECAI issuer rating assigned to a bank (other than a public bank owned by a government), and any ECAI issue specific rating assigned to an exposure to such a bank, that incorporates assumptions of implicit government support must be ignored when—

(i) determining under section 54E which ECAI rating may be used for the purposes of section 54D; and

(ii) determining whether an exposure to such a bank is an unrated exposure for the purposes of this Part.

(2) Despite subsection (1)(b) and (c), an authorized institution may continue to use ECAI ratings that incorporate assumptions of implicit government support for a period of up to 5 years after the commencement date* of this section for the purpose of determining the risk-weights attributable to bank exposures.

(3) In this section—

implicit government support (隱性政府支持), in relation to banks incorporated in a jurisdiction, means the notion that the government of that jurisdiction would act to prevent bank creditors from incurring losses in the event of a bank default or bank distress.

(L.N. 167 of 2023)

Editorial Note:

* Commencement date: 1 January 2025.

55. Sovereign exposures

(1) Subject to section 56, an authorized institution must allocate a risk-weight to a sovereign exposure that has been assigned a credit quality grade under section 54D(2) or (5) in accordance with Table 2.

Table 2

Risk-weights for Sovereign Exposures

Column 1	Column 2	Column 3
Item	Credit quality grade	Risk-weight
1.	1, 2	0%
2.	3	20%
3.	4	50%
4.	5, 6	100%
5.	7	150%

(2) Subject to section 56, an authorized institution must allocate a risk-weight of 100% to a sovereign exposure that is an unrated exposure.

(L.N. 167 of 2023)

56. Exceptions to section 55

(1) If a sovereign exposure is a domestic currency exposure to the Government (including an exposure to the Exchange Fund), an authorized institution may allocate a risk-weight of 0% to the exposure.

(2) If—

(a) a sovereign exposure is a domestic currency exposure to a sovereign (other than the Government or a restricted sovereign); and

(b) the relevant banking supervisory authority for the jurisdiction of the sovereign would permit banks incorporated in that jurisdiction to allocate a risk-weight to the exposure that is lower than the risk-weight that would be allocated under section 55 to the exposure,

an authorized institution may allocate the lower risk-weight to the exposure.

(3) If a sovereign exposure is an exposure to a relevant international organization, an authorized institution may allocate a risk-weight of 0% to the exposure.

(L.N. 167 of 2023)

57. Public sector entity exposures

(1) Subject to subsection (3), an authorized institution must allocate a risk-weight to a public sector entity exposure (***PSE exposure***) that has been assigned a credit quality grade under section 54D(8) in accordance with Table 2A.

Table 2A

Risk-weights for PSE Exposures

Column 1	Column 2	Column 3
Item	Credit quality grade	Risk-weight
1.	1, 2	20%
2.	3	50%
3.	4, 5, 6	100%
4.	7	150%

(2) If the sovereign of the jurisdiction in which the public sector entity is incorporated does not have an ECAI issuer rating, an authorized institution must allocate a risk-weight of 100% to the exposure.

(3) If a PSE exposure is an exposure to a sovereign foreign public sector entity, section 55, with all necessary modifications, applies to the exposure as if the entity were a sovereign, using the credit quality grade assigned to the PSE exposure under section 54D(8).

(L.N. 167 of 2023)

58. Multilateral development bank exposures and unspecified multilateral body exposures

(1) An authorized institution may allocate a risk-weight of 0% to a multilateral development bank exposure (***MDB exposure***) if the multilateral development bank concerned is assigned a credit quality grade of 1 or 2 under section 54D(9).

(2) If subsection (1) is not applicable to an MDB exposure, an authorized institution must treat the multilateral development bank as if it were an unspecified multilateral body and—

(a) if the MDB exposure is not an unrated exposure—

(i) determine the credit quality grade applicable to the exposure in accordance with section 54D(2) or (5), as the case requires; and

(ii) determine the risk-weight attributable to the exposure in accordance with subsection (3), based on the credit quality grade so determined; and

(b) if the MDB exposure is an unrated exposure—determine the risk-weight attributable to the exposure in accordance with subsection (4).

(3) Subject to section 54C, an authorized institution must allocate a risk-weight to an unspecified multilateral body exposure that has been assigned a credit quality grade under section 54D(2) or (5) in accordance with Table 2B.

Table 2B

Risk-weights for Unspecified Multilateral Body Exposures

Column 1	Column 2	Column 3
Item	Credit quality grade	Risk-weight
1.	1, 2	20%
2.	3	30%
3.	4	50%
4.	5, 6	100%
5.	7	150%

(4) An authorized institution must allocate a risk-weight of 50% to an unspecified multilateral body exposure that is an unrated exposure.

(L.N. 167 of 2023)

59. Bank exposures

(1) This section applies to a bank exposure that is neither of the following exposures—

(a) an unrated exposure to a bank;

(b) an eligible covered bond exposure.

(2) Subject to sections 54C and 59A, if the exposure has been assigned a credit quality grade under section 54D(2) or (6), an authorized institution must allocate a risk-weight to the exposure in accordance with Table 3.

Table 3

Risk-weights for Bank Exposures with Credit Quality Grades Obtained by Mapping to LT ECAI Rating Mapping Table for Type A ECAIs

Column 1	Column 2	Column 3	Column 4
Item	Credit quality grade	Risk-weight for general bank exposures	Risk-weight for short-term bank exposures (other than exposures that have a short-term ECAI issue specific rating)
1.	1, 2	20%	20%
2.	3	30%	20%
3.	4	50%	20%
4.	5, 6	100%	50%
5.	7	150%	150%

(3) If the exposure has been assigned a credit quality grade under section 54D(3), an authorized institution must allocate a risk-weight to the exposure in accordance with Table 4.

Table 4

Risk-weights for Bank Exposures with Credit Quality Grades Obtained by Mapping to ST ECAI Rating Mapping Table for Type A ECAIs

Column 1	Column 2	Column 3
Item	Credit quality grade	Risk-weight for general bank exposures and short-term bank exposures
1.	1	20%
2.	2	50%

Column 1	Column 2	Column 3
Item	Credit quality grade	Risk-weight for general bank exposures and short-term bank exposures
3.	3	100%
4.	4	150%

(L.N. 167 of 2023)

59A. Provisions supplementary to section 59

(1) Despite section 59(2), an authorized institution must allocate a risk-weight of 150% to a general bank exposure or a 3 months' bank exposure to a bank—

(a) if—

(i) section 54D(6) applies to the exposure; and

(ii) there is a reference exposure to the same bank; and

(b) if sections 54D(3) and 59(3) applied to the reference exposure, it would be allocated a risk-weight of 150% in accordance with those sections.

(2) The risk-weight allocated under section 59(2) to a bank exposure that is not a 6 months' bank exposure and has an original maturity of 1 year or less (***subject exposure***) must not be lower than 100%—

(a) if—

(i) section 54D(6) applies to the subject exposure; and

(ii) there are one or more reference exposures to the same bank but none of the reference exposures falls within subsection (1)(b); and

(b) if sections 54D(3) and 59(3) applied to the reference exposures, one or more of the reference exposures would be allocated a risk-weight of 50% or 100% in accordance with those sections.

(3) If—

(a) a bank exposure (***subject exposure***) to which section 54D(6) applies is a 3 months' bank exposure; and

(b) there are one or more reference exposures to the same bank but none of the reference exposures falls within subsection (1)(b) or (2)(b),

the subject exposure must be allocated a risk-weight in accordance with subsection (4).

(4) If subsection (3) applies, the subject exposure must be allocated a risk-weight that is the higher of—

(a) the risk-weight that would be allocated to the reference exposures in accordance with sections 54D(3) and 59(3) if those sections applied to the reference exposures; and

(b) the risk-weight that would be allocated to the subject exposure in accordance with sections 54D(6) and 59(2) if those sections applied to the subject exposure as if there were no reference exposures.

(5) For the purposes of subsection (4), if the 2 risk-weights referred to in subsection (4)(a) and (b) are the same, any one of those risk-weights may be allocated to the subject exposure.

(6) In this section—

reference exposure (參照風險承擔), in relation to a bank exposure to which section 54D(6) applies, means another exposure to the same bank that has a short-term ECAI issue specific rating, regardless of who is holding that other exposure.

(L.N. 167 of 2023)

59B. Bank exposures—standardized credit risk assessment

approach—assignment of credit assessment grade

(1) This section applies to an unrated exposure to a bank other than an eligible covered bond exposure.

(2) An authorized institution must assign a credit assessment grade to the exposure in accordance with subsections (3), (4) and (5).

(3) The institution must not assign a credit assessment grade of A to the exposure unless the institution assesses that the bank—

(a) has adequate capacity to meet its financial commitments (including repayments of principal and interest) in a timely manner, for the projected life of the assets or exposures concerned and irrespective of the economic cycles and business conditions; and

(b) meets or exceeds the published minimum regulatory requirements (including buffers) established by the relevant supervisor.

(4) The institution may assign a credit assessment grade of B to the exposure if the institution assesses that—

(a) the bank falls within either or both of subparagraphs (i) and (ii)—

(i) the bank—

(A) does not fall within subsection (3)(a); and

(B) is subject to substantial credit risk, such as repayment capacities that are dependent on stable or favourable economic or business conditions;

(ii) the bank does not fall within subsection (3)(b), including because of the absence of a buffer requirement in the published minimum regulatory requirements applicable to the bank; and

(b) the bank meets or exceeds the published minimum regulatory requirements (excluding buffers) established by the relevant supervisor.

(5) The institution must assign a credit assessment grade of C to the exposure if—

(a) the institution assesses that—

(i) the bank—

(A) does not fall within subsection (3)(a) or (4)(a)(i)(B); and

(B) has material default risks and limited margins of safety; and

(ii) adverse business, financial or economic conditions are very likely to lead, or have led, to an inability of the bank to meet its financial commitments;

(b) the institution assesses that—

(i) the bank fails to meet the published minimum regulatory requirements (excluding buffers) established by the relevant supervisor; or

(ii) the minimum quantitative regulatory requirements imposed by the relevant supervisor are not publicly disclosed or otherwise made available by the bank to the institution; or

(c) the external auditor of the bank has issued an adverse audit opinion or has expressed substantial doubt about the bank's ability to continue as a going concern in the bank's financial statements or audited reports issued within the previous 12 months.

(6) Despite subsections (2), (3), (4) and (5), an authorized institution must assign a credit assessment grade of C to an unrated exposure to a bank if the institution chooses not to

conduct an assessment to determine whether the bank would be eligible for a credit assessment grade of A or B.

(7) In this section—

home jurisdiction (原屬司法管轄區), in relation to a bank, means the jurisdiction in which the bank is incorporated;

published minimum regulatory requirements (已公布最低監管規定)—

(a) in relation to an internationally active bank, means the minimum quantitative regulatory requirements imposed by the relevant supervisor on the bank that are—

(i) consistent with the Basel Framework; and

(ii) publicly disclosed or otherwise made known by the bank to its creditors or counterparties;

(b) in relation to a bank that is not an internationally active bank, means the minimum quantitative regulatory requirements imposed by the relevant supervisor on the bank—

(i) that include at least a minimum regulatory capital requirement; and

(ii) that are publicly disclosed or otherwise made known by the bank to its creditors or counterparties; and

(c) do not include—

(i) liquidity standards; or

(ii) bank-specific minimum regulatory requirements—

(A) that may be imposed through supervisory actions taken by the relevant supervisor; and

(B) that are not made public;

relevant supervisor (有關監管者), in relation to a bank, means—

(a) the Monetary Authority if the bank is an authorized institution incorporated in Hong Kong; or

(b) in any other case, the relevant banking supervisory authority in the bank's home jurisdiction.

(L.N. 167 of 2023)

59C. Bank exposures—standardized credit risk assessment approach—allocation of risk-weight

(1) Subject to subsection (2), an authorized institution must allocate a risk-weight to an unrated exposure to a bank in accordance with Table 4A based on the credit assessment grade assigned by the institution to the unrated exposure under section 59B(2).

Table 4A

Risk-weights for Unrated Exposures to Banks

Column 1	Column 2	Column 3	Column 4
Item	Credit assessment grade	Risk-weight for general bank exposures	Risk-weight for short-term bank exposures
1.	A	40%	20%
2.	B	75%	50%
3.	C	150%	150%

(2) An authorized institution may allocate a risk-weight of 30% to an unrated exposure to a bank if—

(a) the institution assigns a credit assessment grade of A to the bank under section 59B(2); and

(b) the bank has—

(i) a CET1 capital ratio, calculated in the manner specified by the relevant supervisor of the bank, that meets or exceeds 14%; and

(ii) a leverage ratio, calculated in the manner specified by the relevant supervisor of the bank, that meets or exceeds 5%.

(3) Subject to subsection (4), an unrated exposure to a bank must not be allocated under subsection (1) or (2) a risk-weight that is lower than the attributed risk-weight of the sovereign of the bank's home jurisdiction if—

(a) the unrated exposure is not denominated in the local currency of the home jurisdiction; or

(b) the unrated exposure—

(i) is booked in a branch of the bank in a jurisdiction other than its home jurisdiction (***host jurisdiction***); and

(ii) is not denominated in the local currency of the host jurisdiction.

(4) Subsection (3) does not apply to an unrated exposure to a bank that is a trade-related contingency.

(5) In this section—

attributed risk-weight (歸屬風險權重), in relation to a sovereign—

(a) if the sovereign has an ECAI issuer rating or a long-term ECAI issue specific rating assigned to a debt obligation of the sovereign—means the risk-weight that would be attributable, in accordance with sections 54D and 55(1), to a senior and unsecured exposure (other than a domestic currency exposure) to the sovereign based on that rating; or

(b) in any other case—means the risk-weight that would be attributable, in accordance with section 55(2), to an unrated exposure (other than a domestic currency exposure) to the sovereign;

home jurisdiction (原屬司法管轄區) has the meaning given by section 59B(7);

relevant supervisor (有關監管者) has the meaning given by section 59B(7).

(L.N. 167 of 2023)

59D. Eligible covered bond exposures

(1) Subject to section 54C, an authorized institution must allocate a risk-weight to an eligible covered bond exposure that has been assigned a credit quality grade under section 54D(2) in accordance with Table 4B.

Table 4B

Risk-weights for Eligible Covered Bonds with Long-term ECAI Issue Specific Ratings

Column 1	Column 2	Column 3
Item	Credit quality grade	Risk-weight
1.	1, 2	10%
2.	3, 4	20%
3.	5, 6	50%
4.	7	100%

(2) Subject to section 54C, if no credit quality grade can be assigned to an eligible covered bond exposure under section 54D(2), an authorized institution must—

(a) determine the attributed risk-weight of the issuer of the eligible covered bond; and

(b) allocate a risk-weight to the eligible covered bond exposure in accordance with Table 4C based on the attributed risk-weight of the issuer determined under paragraph (a).

Table 4C

Risk-weights for Eligible Covered Bonds without Long-term ECAI Issue Specific Ratings

Column 1	Column 2	Column 3
Item	Attributed risk-weight of issuer	Risk-weight for eligible covered bond exposures
1.	20%	10%
2.	30%	15%
3.	40%	20%
4.	50%	25%
5.	75%	35%
6.	100%	50%
7.	150%	100%

(3) For the purposes of subsection (2), if the issuer of an eligible covered bond is a financial institution other than a bank, an authorized institution may determine the attributed risk-weight of the issuer in a manner as if the issuer were a bank.

(4) The Monetary Authority must develop implementing technical standards to specify the conditions a covered bond must meet

in order to be recognized as an eligible covered bond for the purposes of this section, including—

(a) the types and qualities of claims included in the underlying assets of the covered bond;

(b) the size of the underlying assets assigned to the covered bond relative to the size of the outstanding amount of the covered bond; and

(c) information that must be made available to investors on a regular basis.

(L.N. 167 of 2023)

60. Exposures to qualifying non-bank financial institutions

(1) This section applies to a qualifying non-bank financial institution exposure that is neither an eligible covered bond exposure nor an exposure that falls within section 64A.

(2) If the exposure has been assigned a credit quality grade under section 54D(2), (3) or (6), sections 59 and 59A apply to the exposure as they apply to a bank exposure that is not an unrated exposure.

(3) Subject to subsection (4), if the exposure is an unrated exposure, sections 59B and 59C apply to the exposure as they apply to a bank exposure that is an unrated exposure, as if a reference in section 59B to published minimum regulatory requirements were a reference to the minimum quantitative regulatory requirements—

(a) that are—

(i) imposed on the qualifying non-bank financial institution concerned by the regulatory authority in the jurisdiction in which it is incorporated; and

(ii) publicly disclosed or otherwise made known by the qualifying non-bank financial institution to its creditors or counterparties; and

(b) that do not include—

(i) liquidity standards; or

(ii) institution-specific minimum regulatory requirements—

(A) that may be imposed through supervisory actions taken by the regulatory authority; and

(B) that are not made public.

(4) If—

(a) the exposure is an unrated exposure; and

(b) the obligor in respect of the exposure is a qualifying non-bank financial institution within the meaning of paragraph (a) or (b) of the definition of ***qualifying non-bank financial institution*** in section 2(1),

an authorized institution must allocate to the unrated exposure a risk-weight of 75% if the exposure is a general bank exposure or a risk-weight of 50% if the exposure is a short-term bank exposure.

(L.N. 167 of 2023)

61. General corporate exposures

(1) Subject to subsections (3) and (4) and section 54C, an authorized institution must allocate a risk-weight to a general corporate exposure that has been assigned a credit quality grade under section 54D(2), (3), (4), (6) or (7) in accordance with Table 5.

Table 5

Risk-weights for General Corporate Exposures

Column 1	Column 2	Column 3	Column 4	Column 5	Column 6
Item	Credit quality grade	Risk-weight for credit quality grade obtained by mapping to LT ECAI rating mapping table for Type A ECAIs	Risk-weight for credit quality grade obtained by mapping to LT ECAI rating mapping table for Type B ECAIs	Risk-weight for credit quality grade obtained by mapping to ST ECAI rating mapping table for Type A ECAIs	Risk-weight for credit quality grade obtained by mapping to ST ECAI rating mapping table for Type B ECAIs
1.	1	20%	20%	20%	20%
2.	2	20%	30%	50%	30%
3.	3	50%	50%	100%	50%
4.	4	75%	75%	150%	100%
5.	5	100%	100%	Not applicable	150%
6.	6, 7	150%	150%	Not applicable	Not applicable

(2) Subject to subsections (3) and (4), if a general corporate exposure is an unrated exposure—

(a) subject to paragraph (b), an authorized institution must allocate a risk-weight of 100% to the general corporate exposure; or

(b) an authorized institution may allocate a risk-weight of 85% to the general corporate exposure if the corporate concerned is a small business.

(3) An authorized institution must allocate a risk-weight of 150% to a general corporate exposure—

(a) if—

(i) the exposure is an exposure to which section 54D(6) or (7) applies or an unrated exposure; and

(ii) there is a reference exposure to the same corporate; and

(b) if subsection (1) and section 54D(3) or (4) applied to the reference exposure, it would be allocated a risk-weight of 150% in accordance with those provisions.

(4) The risk-weight allocated to a general corporate exposure with an original maturity of 1 year or less under subsection (1) or (2), as the case requires, must not be lower than 100%—

(a) if—

(i) the exposure is an exposure to which section 54D(6) or (7) applies or an unrated exposure; and

(ii) there are one or more reference exposures to the same corporate but none of the reference exposures falls within subsection (3)(b); and

(b) if subsection (1) and section 54D(3) or (4) applied to the reference exposures, one or more of the reference exposures would be allocated a risk-weight of 50% or 100% in accordance with those provisions.

(5) In this section—

reference exposure (參照風險承擔), in relation to a general corporate exposure that does not have an ECAI issue specific rating, means another general corporate exposure to the same corporate that has a short-term ECAI issue specific rating, regardless of who is holding that other general corporate exposure.

(L.N. 167 of 2023)

61A. *(Repealed L.N. 167 of 2023)*

62. Specialized lending

(1) Subject to section 54C, an authorized institution must allocate a risk-weight to a specialized lending that has been assigned a credit quality grade under section 54D(2) or (3) in accordance with Table 5.

(2) An authorized institution must allocate to a specialized lending that does not have an ECAI issue specific rating a risk-weight of—

(a) if the lending arises from an object finance—100%;

(b) if the lending arises from a commodities finance—100%;

(c) if the lending arises from a project finance (whether high quality or not)—130% during the preoperational phase;

(d) if the lending arises from a high quality project finance—80% during the operational phase; or

(e) if the lending arises from a project finance, other than a high quality project finance—100% during the operational phase.

(3) For the purposes of subsection (2), a specialized lending arising from a high quality project finance is an exposure to a project finance entity where—

(a) the entity is able to meet its financial commitments in a timely manner and its ability to do so is assessed to be robust against adverse changes in the economic cycle and business conditions;

(b) the entity is restricted from acting to the detriment of the creditors (for example, by not being able to issue additional debt without the consent of existing creditors);

(c) the entity has sufficient reserve funds or other financial arrangements to cover the contingency funding and working capital requirements of the project;

(d) the revenues are availability-based or subject to a rate-of-return regulation or take-or-pay contract;

(e) the entity's revenue depends on one main counterparty, which is a central government, public sector entity or a corporate, that has an attributed risk-weight of 80% or lower;

(f) the contractual provisions governing the exposure provide for a high degree of protection for creditors in case of a default of the entity;

(g) the main counterparty, or other counterparties that similarly comply with the eligibility criteria set out in paragraph (e) for the main counterparty, will protect the creditors from the losses resulting from a termination of the project;

(h) all assets and contracts necessary to operate the project have been pledged (or otherwise provided as security) to the creditors to the extent permitted by applicable law; and

(i) creditors may assume control of the entity in case of a default of the entity.

(4) For the purposes of subsection (3)(d), the revenues are availability-based if—

(a) once construction is completed, the project finance entity is entitled to payments from its contractual counterparties (***availability payments***), as long as contract conditions are fulfilled;

(b) the availability payments are sized to cover operating and maintenance costs, debt service costs and equity returns as the project finance entity operates the project; and

(c) the availability payments are not subject to swings in demand, such as traffic levels, and are adjusted typically only for lack of performance or lack of availability of the asset to the public of the jurisdiction in which the asset is located.

(5) In this section—

operational phase (營運階段), in relation to a project finance, means the phase in which the entity that was specifically created to finance the project has—

(a) a positive net cash flow that is sufficient to cover any remaining contractual obligation; and

(b) declining long-term debt;

preoperational phase (營運前階段), in relation to a project finance, means the phase before the operational phase.

(L.N. 167 of 2023)

63. *(Repealed L.N. 167 of 2023)*

63A. *(Repealed L.N. 167 of 2023)*

Subdivision 4—Retail Exposures and IPO Financing

(L.N. 167 of 2023)

64. Retail exposures

(1) Subject to subsection (7), an authorized institution must allocate—

(a) a risk-weight of 75% to a regulatory retail exposure to an obligor if—

(i) the exposure arises from a credit facility other than a revolving credit facility or the obligor is not a transactor in respect of the exposure; and

(ii) the obligor is not a transactor in respect of any other exposure;

(b) to a regulatory retail exposure to an obligor—

(i) a risk-weight of 45% if the obligor is a transactor in respect of the exposure; or

(ii) a risk-weight of 75% if—

(A) the exposure arises from a credit facility other than a revolving credit facility or the obligor is not a transactor in respect of the exposure; and

(B) the institution has another exposure to the obligor that falls within subparagraph (i); and

(c) a risk-weight of 100% to an exposure (other than a real estate exposure, an exposure that falls within section 64A or a defaulted exposure) to an individual, if the exposure is not a regulatory retail exposure (***other retail exposure***).

(2) For the purposes of subsection (1), an exposure of an authorized institution to a single obligor, or to a particular obligor in a group of obligors that is considered by the institution as a group of obligors for risk management purposes (including, but not limited to, those grouped under the Banking (Exposure Limits) Rules (Cap. 155 sub. leg. S)), is a regulatory retail exposure if—

(a) that single obligor, or that particular obligor in the group of obligors, is an individual or a small business;

(b) the exposure is none of the following—

(i) a real estate exposure;

(ii) a default risk exposure in respect of derivative contracts entered into with the obligor;

(iii) an exposure that falls within section 64A;

(iv) a defaulted exposure;

(v) a holding of securities issued by the obligor, whether listed or not;

(vi) an exposure that falls within Subdivision 6 or section 65K or 65L;

(c) the exposure arises from a transaction, whether drawn down or not, that takes any of the following forms—

(i) a revolving credit facility or a line of credit to an individual (such as a credit card or an overdraft);

(ii) a term loan or a lease to an individual (such as an auto loan or other instalment loan);

(iii) a revolving credit facility, a line of credit, a term loan, a lease or a commitment (within the meaning of section 2 of Schedule 6) to a small business;

(d) the maximum aggregate exposure of the institution to that single obligor, or to that group of obligors, does not exceed $10 million; and

(e) no aggregate exposure of the institution to that single obligor, or to that group of obligors, exceeds 0.2% of the institution’s overall regulatory retail portfolio.

(3) For the purposes of subsection (2)(d) and (e), aggregate exposure—

(a) includes all forms of exposures (other than real estate exposures secured by residential properties) to an individual or a small business (***in-scope exposures***); and

(b) must be calculated by aggregating the exposure amounts of the in-scope exposures without taking into account any recognized credit risk mitigation.

(4) For the purposes of subsection (2)(e), an authorized institution must—

(a) identify the full set of exposures to individuals and small businesses;

(b) from the full set of exposures identified under paragraph (a), identify the subset of exposures that meet all the criteria specified in subsection (2)(a), (b), (c) and (d); and

(c) regard the subset of exposures identified under paragraph (b) as the institution's overall regulatory retail portfolio.

(5) Subsection (6) applies if—

(a) an authorized institution has any branch or subsidiary in a jurisdiction outside Hong Kong (***relevant jurisdiction***);

(b) the branch or subsidiary has exposures to individuals or small businesses (***relevant exposures***) in the relevant jurisdiction; and

(c) transfer of any information on the relevant exposures necessary for complying with subsection (6) outside the relevant jurisdiction is not prohibited by law.

(6) The institution must include in the aggregate exposure referred to in subsection (3) and the full set of exposures identified under subsection (4)(a)—

(a) for the purpose of calculating its capital adequacy ratio on a solo basis—the relevant exposures of its overseas branches; and

(b) for the purpose of calculating its capital adequacy ratio on a solo-consolidated basis or consolidated basis—the relevant exposures of its overseas branches and overseas subsidiaries subject to the consolidation.

(7) If a regulatory retail exposure or other retail exposure is an unhedged credit exposure, an authorized institution must apply a multiplier of 1.5 to the risk-weight applicable to the exposure determined under subsection (1), subject to a cap of 150%.

(L.N. 167 of 2023)

64A. Exposures arising from IPO financing

(1) This section applies to a credit facility granted by an authorized institution to a qualifying non-bank financial institution, a corporate or an individual (***borrower***) if— *(L.N. 167 of 2023)*

(a) the facility is granted by the institution solely for the purpose of financing the borrower's subscription of securities to be listed on The Stock Exchange of Hong Kong Limited through an IPO;

(b) the settlement process of the IPO is conducted on the Fast Interface for New Issuance operated by Hong Kong Securities Clearing Company Limited; and

(c) the money advanced by the institution under the facility is still legally owned and held by, and under the control of, the institution until the settlement of the payment for the securities successfully subscribed.

(2) The institution may allocate a risk-weight of 0% to its exposure arising from the facility during the period between the time the commitment to extend the facility is made by the institution and the time—

(a) payment for the securities successfully subscribed is made by the institution to the receiving bank of the issuer of the securities; or

(b) if the IPO is cancelled before the payment referred to in paragraph (a) is made, the outstanding loan amount under the facility is fully repaid.

(L.N. 167 of 2023)

Subdivision 5—Real Estate Exposures

(L.N. 167 of 2023)

65. What are regulatory real estate exposures

(1) Subject to subsection (3), a real estate exposure (other than an ADC exposure) of an authorized institution to an obligor is a regulatory real estate exposure if all of the following criteria are met in respect of the exposure—

(a) the exposure is secured by an immovable property that falls within subsection (2)(a), (b) or (c) (***mortgaged property***);

(b) any claim on the mortgaged property is legally enforceable in all relevant jurisdictions;

(c) the collateral agreement and the legal process underpinning any claim on the mortgaged property provide for the institution to realize the value of the mortgaged property within a reasonable time frame;

(d) the exposure is secured by a first legal charge on the mortgaged property or, if the mortgaged property falls within subsection (2)(c), the exposure will be secured by a first legal charge on the residential property after it is fully completed;

(e) the exposure is granted for one or more of the following purposes—

(i) financing the acquisition of the mortgaged property;

(ii) refinancing the acquisition of the mortgaged property;

(iii) cashing out the equity in the mortgaged property;

(f) the institution's underwriting policies with respect to the granting of real estate exposures are adequate and prudent and include—

(i) assessment of the ability of the obligor to repay; and

(ii) if the repayment of the exposure depends materially on the cash flows generated by the mortgaged property—assessment of relevant metrics (such as occupancy rate);

(g) the mortgaged property is valued in a manner consistent with the relevant guidance issued by the Monetary Authority and the value of the mortgaged property does not depend materially on the performance of the obligor;

(h) all the information (including information on the ability of the obligor to repay and on the valuation of the mortgaged property) required at loan origination and for monitoring purposes is properly documented.

(2) Immovable property falls within this subsection if the property is—

(a) a fully-completed immovable property;

(b) forest or agricultural land; or

(c) a residential property under construction or land on which a residential property will be constructed where—

(i) the real estate exposure secured by which is granted to an individual or a property-holding shell company owned by an individual who is the guarantor of the exposure; and

(ii) either of the following conditions is met—

(A) the residential property is constructed, or to be constructed, under a subsidized home ownership scheme launched by the Government or a domestic public sector entity;

(B) the institution is able to demonstrate, with the support of written and reasoned legal advice, that the sovereign of the jurisdiction (including Hong Kong) in which the property or land is located or any public sector entity of that jurisdiction has the legal power and ability to ensure that the property under construction or to be constructed will be finished.

(3) An authorized institution may classify a real estate exposure secured by a residential property as a regulatory real estate exposure despite the criteria set out in subsection (1) if—

(a) the exposure was originated before the commencement date* of Part 3 of the Banking (Capital) (Amendment) Rules 2023;

(b) the exposure was eligible for a risk-weight of 35% under subsection (1) as in force immediately before that date; and

(c) there has been no material change to the loan terms and conditions since that date.

(4) For the purposes of sections 65B, 65C and 65D—

(a) subject to paragraphs (b), (c) and (d), a real estate exposure depends materially on the cash flows generated by the mortgaged property if both the servicing of the exposure and the prospects for recovery in the event of default depend materially on the cash flows generated by the mortgaged property, rather than on the income, revenue and net worth of the obligor generated from other sources;

(b) an authorized institution may treat a regulatory real estate exposure as an exposure that does not depend materially on the cash flows generated by the mortgaged property (***non-IPRE exposure***) if the mortgaged property is a residential property that is—

(i) the primary residence of the obligor in respect of the exposure; or

(ii) if the obligor in respect of the exposure is a property-holding shell company owned by an individual who is the guarantor of the exposure—that individual's primary residence;

(c) an authorized institution may treat a regulatory real estate exposure that does not fall within paragraph (b) as a non-IPRE exposure if the mortgaged property is a residential property and both of the following conditions are met—

(i) the obligor in respect of the exposure is an individual or a property-holding shell company owned by an individual who is the guarantor of the exposure;

(ii) the total number of residential properties (including the mortgaged property but excluding any residential property that falls within paragraph (b)(i) or (ii)) pledged (or otherwise provided as security) to the institution by the individual and any property-holding shell company owned by the individual is 2 or fewer; and

(d) for any real estate exposure that was originated before the commencement date of Part 3 of the Banking (Capital) (Amendment) Rules 2023, an authorized institution may, if information necessary for assessment is not sufficient or readily available, treat the exposure as a non-IPRE exposure.

(L.N. 167 of 2023)

Editorial Note:

* Commencement date: 1 January 2025.

65A. Loan-to-value ratio

(1) The loan-to-value ratio (***LTV ratio***) of a regulatory real estate exposure (***subject exposure***) secured by one or more immovable properties (***subject security***) must be calculated as a ratio of the amount specified in paragraph (a) to the amount specified in paragraph (b)—

(a) the sum of—

(i) the principal amount of any outstanding drawn portion of the subject exposure (including accrued interest); and

(ii) the amount of any undrawn committed portion of the subject exposure;

(b) the value at origination of the subject security, with the exceptions set out in subsections (6) and (7).

(2) If a pool of regulatory real estate exposures (collectively referred to as ***subject exposure***) is secured by one or more immovable properties (***subject security***), the LTV ratio of the subject exposure must be calculated as a ratio of the

amount specified in paragraph (a) to the amount specified in paragraph (b)—

(a) the sum of—

(i) the principal amount of any outstanding drawn portion of each of the regulatory real estate exposures in the pool (including accrued interest); and

(ii) the amount of any undrawn committed portion of each of the regulatory real estate exposures in the pool;

(b) the value at origination of the subject security, with the exceptions set out in subsections (6) and (7).

(3) If—

(a) a pool of real estate exposures is secured by one or more immovable properties (***subject security***); and

(b) the pool consists of both regulatory real estate exposures and real estate exposures that are neither regulatory real estate exposures nor ADC exposures,

the LTV ratio applicable to the regulatory real estate exposures in the pool (***subject exposures***) must be calculated in accordance with subsection (2) where the reference to regulatory real estate exposures in subsection (2)(a) is taken to be a reference to all of the exposures in the pool referred to in paragraph (a).

(4) The numerator of the LTV ratio calculated under subsection (1), (2) or (3)—

(a) must not be reduced by any specific provisions; and

(b) must not take into account the effect of any recognized credit risk mitigation (including mortgage insurance) except for cash on deposit with the authorized institution—

(i) that is unconditionally and irrevocably pledged (or otherwise provided as security) by the obligor in respect of the subject exposure under a netting or offsetting agreement for the sole purpose of redemption of the subject exposure; and

(ii) for which the security arrangement meets all of the following requirements—

(A) the institution has a well-founded legal basis for concluding that the netting or offsetting agreement with the obligor is enforceable in each relevant jurisdiction regardless of whether the obligor is insolvent or bankrupt;

(B) the institution is able at any time to determine those assets and liabilities with the obligor that are subject to the netting or offsetting agreement;

(C) the institution monitors and controls the roll-off risks that may arise when short-term liabilities that have been netted against longer term exposures are no longer available;

(D) the institution monitors and controls its exposures to the obligor on a net basis.

(5) If a regulatory real estate exposure of an authorized institution secured by one or more immovable properties (***subject security***) was originated before the commencement date* of this section and the subject security was revalued at least once before that date, the institution may treat the value at the last revaluation conducted before that date as the value at origination of the subject security.

(6) In calculating the LTV ratio of a subject exposure under subsection (1), (2) or (3), an authorized institution must use

a value lower than the value at origination of the subject security if—

(a) downward adjustment of the value of the subject security is warranted by the prevailing local property market situations;

(b) the Monetary Authority, by written notice given to the institution, requires the institution to revise the value of the subject security downwards; or

(c) an extraordinary, idiosyncratic event occurs and results in a permanent reduction of the value of the subject security.

(7) If—

(a) an authorized institution incurs a new real estate exposure secured by a subject security that is also the security for at least one existing real estate exposure of the institution and an updated valuation of the security is obtained as part of the new loan application process in relation to the new real estate exposure, the institution may use the updated valuation in calculating the LTV ratio of the pool of regulatory real estate exposures secured by the subject security under subsection (2) or (3);

(b) the value of a subject security has been adjusted downwards under subsection (6)(a), an authorized institution may make a subsequent upward adjustment to the value of the subject security and, except in cases where the resultant adjusted value is higher than the value at origination of the subject security, use the resultant adjusted value in the LTV ratio calculation under subsection (1), (2) or (3);

(c) the value of a subject security has been adjusted downwards under subsection (6)(b), an authorized institution may, with the prior consent of the Monetary Authority, make a subsequent upward adjustment to the value of the subject security and use the resultant adjusted value in the LTV ratio calculation under subsection (1), (2) or (3); and

(d) modifications are made to an immovable property included in a subject security that unequivocally increase the value of the property and there is an updated valuation that confirms the increase in value, an authorized institution may take into account that increase in the LTV ratio calculation under subsection (1), (2) or (3).

(8) In this section—

value at origination (批出承擔時價值)—

(a) in relation to a regulatory real estate exposure of an authorized institution secured by one or more immovable properties, means the valuation of the property or properties obtained by the institution at the time of origination of the exposure; and

(b) in relation to a pool of real estate exposures of an authorized institution originated at the same time and secured by one or more immovable properties, means the valuation of the property or properties obtained by the institution at the time of origination of the pool.

(L.N. 167 of 2023)

Editorial Note:

* Commencement date: 1 January 2025.

65B. Risk-weights of regulatory residential real estate exposures

(1) This section applies to a regulatory real estate exposure of an authorized institution that is secured by a residential property,

including such a regulatory real estate exposure to a member of its staff (whether solely or jointly with another person).

(2) Subject to subsection (4) and section 65E, if the exposure is an exposure that does not depend materially on cash flows generated by the residential property securing the exposure (***non-IPRE exposure***), the institution must allocate a risk-weight to the exposure in accordance with Table 6 based on the LTV ratio of the exposure calculated under section 65A.

Table 6

Risk-weights for Regulatory Residential Real Estate Exposures that are Non-IPRE Exposures

Column 1	Column 2	Column 3
Item	LTV ratio	Risk-weight
1.	Not more than 50%	20%
2.	More than 50% but not more than 60%	25%
3.	More than 60% but not more than 80%	30%
4.	More than 80% but not more than 90%	40%
5.	More than 90% but not more than 100%	50%
6.	More than 100%	70%

(3) Subject to subsection (4) and section 65E, if the exposure is not a non-IPRE exposure, the institution must allocate a risk-weight to the exposure in accordance with Table 7 based on the LTV ratio of the exposure calculated under section 65A.

Table 7

Risk-weights for Regulatory Residential Real Estate Exposures that are not Non-IPRE Exposures

Column 1	Column 2	Column 3
Item	LTV ratio	Risk-weight
1.	Not more than 50%	30%
2.	More than 50% but not more than 60%	35%
3.	More than 60% but not more than 80%	45%
4.	More than 80% but not more than 90%	60%
5.	More than 90% but not more than 100%	75%
6.	More than 100%	105%

(4) If the exposure is an unhedged credit exposure, the institution must apply a multiplier of 1.5 to the risk-weight applicable to the exposure determined under subsection (2) or (3), as the case requires, subject to a cap of 150%.

(L.N. 167 of 2023)

65C. Risk-weights of regulatory commercial real estate exposures

(1) This section applies to a regulatory real estate exposure of an authorized institution to an obligor that is secured by a property other than residential property.

(2) If the exposure is an exposure that does not depend materially on cash flows generated by the property securing the exposure

(***non-IPRE exposure***), the institution must allocate a risk-weight to the exposure in accordance with Table 8 based on the LTV ratio of the exposure calculated under section 65A.

Table 8

Risk-weights for Regulatory Commercial Real Estate Exposures that are Non-IPRE Exposures

Column 1	Column 2	Column 3
Item	LTV ratio	Risk-weight
1.	Not more than 60%	Min (60%, attributed risk-weight of the obligor)
2.	More than 60%	Attributed risk-weight of the obligor

(3) If the exposure is not a non-IPRE exposure, the institution must allocate a risk-weight to the exposure in accordance with Table 9 based on the LTV ratio of the exposure calculated under section 65A.

Table 9

Risk-weights for Regulatory Commercial Real Estate Exposures that are not Non-IPRE Exposures

Column 1	Column 2	Column 3
Item	LTV ratio	Risk-weight
1.	Not more than 60%	70%
2.	More than 60% but not more than 80%	90%
3.	More than 80%	110%

(L.N. 167 of 2023)

65D. Risk-weights of other real estate exposures

(1) This section applies to a real estate exposure of an authorized institution that is neither a regulatory real estate exposure nor an ADC exposure.

(2) Subject to section 65E, if the exposure does not depend materially on the cash flows generated by the property securing the exposure, the institution must allocate to the exposure—

(a) a risk-weight of 75% if the obligor in respect of the exposure is an individual;

(b) a risk-weight of 85% if the obligor in respect of the exposure is a small business; and

(c) in any other case, the attributed risk-weight of the obligor.

(3) Despite subsection (2)(b), the institution may allocate a risk-weight of 100% to the exposure if the obligor in respect of the exposure is a corporate and the institution has not verified whether the corporate is a small business.

(4) Subject to section 65E, if the exposure depends materially on the cash flows generated by the property securing the exposure, the institution must allocate a risk-weight of 150% to the exposure.

(L.N. 167 of 2023)

65E. Risk-weights of real estate exposures secured by residential property outside Hong Kong

If—

(a) a real estate exposure (other than an ADC exposure) of an authorized institution is secured by a residential property outside Hong Kong; and

(b) the relevant supervisory authority of the jurisdiction in which the residential property is situated has implemented capital adequacy standards that were formulated in accordance with the Basel Framework,

the institution may allocate a risk-weight to the exposure provided for under the capital adequacy standards (but excluding any approach that is based on internal models) applicable to banks incorporated in that jurisdiction.

(L.N. 167 of 2023)

65F. ADC exposures

(1) Subject to subsections (2) and (3), an authorized institution must allocate a risk-weight of 150% to an ADC exposure.

(2) An ADC exposure in respect of residential property situated in Hong Kong may be allocated a risk-weight of 100% if both of the following criteria are met—

(a) prudential underwriting standards with respect to the granting of ADC exposures meet the criteria specified in section 65(1) where applicable;

(b) the obligor in respect of the ADC exposure has substantial equity at risk, where the equity at risk is determined as an appropriate amount of obligor-contributed equity to the property's appraised as-completed value.

(3) If—

(a) an authorized institution has an ADC exposure in respect of one or more residential properties situated in a jurisdiction outside Hong Kong (***subject ADC exposure***); and

(b) the relevant banking supervisory authority of the jurisdiction—

(i) has implemented the standardized approach for credit risk under the current Basel Framework; and

(ii) would, under the standardized approach for credit risk set out in the capital adequacy standards of the jurisdiction, permit banks incorporated in the jurisdiction to allocate a risk-weight that is lower than 150% to certain ADC exposures in respect of residential properties situated in the jurisdiction,

the institution may allocate the same lower risk-weight to the subject ADC exposure if the conditions for the lower risk-weight specified in the capital adequacy standards of the jurisdiction are met in respect of the subject ADC exposure.

(L.N. 167 of 2023)

Subdivision 6—Equity Exposures, Capital Instruments other than Equity Exposures, Non-capital LAC Liabilities, etc.

(Subdivision 6 added L.N. 167 of 2023)

65G. Equity exposures

(1) Subject to sections 65H and 65I, an authorized institution must allocate—

(a) a risk-weight of 400% to a speculative unlisted equity exposure; and

(b) a risk-weight of 250% to an equity exposure that is not a speculative unlisted equity exposure.

(2) In this section—

speculative unlisted equity exposure (投機性非上市股權風險承擔) means an equity investment in an unlisted company that is—

(a) invested for short-term resale purposes; or

(b) considered venture capital or similar investment that is—

(i) subject to price volatility; and

(ii) acquired in anticipation of significant future capital gains.

65H. Significant capital investments in commercial entities

If the net book value of an authorized institution's significant capital investment in a commercial entity exceeds 15% of the institution's capital base as at the immediately preceding calendar quarter end date as reported in its capital adequacy ratio return, the institution must—

(a) subject to section 43(1)(n), allocate a risk-weight of 1 250% to the amount of the net book value of the investment that exceeds that 15%; and

(b) allocate a risk-weight determined in accordance with section 65G(1)(a) or (b), as the case requires, to the amount of the net book value of the investment that does not exceed that 15%.

65I. Holdings of capital instruments issued by, and non-capital LAC liabilities of, financial sector entities

(1) If an authorized institution has an insignificant LAC investment that is a direct holding, indirect holding or synthetic holding of a capital instrument issued by, or a non-capital LAC liability of, a financial sector entity, any amount of the insignificant LAC investment that is not deducted from the institution's capital base under sections 43(1)(o), 47(1)(c) and 48(1)(c) must be allocated—

(a) a risk-weight determined in accordance with section 65G(1)(a) or (b), as the case requires, if the insignificant LAC investment is an equity exposure; or

(b) a risk-weight of 150% if the insignificant LAC investment is not an equity exposure.

(2) If an authorized institution has a significant LAC investment that is a direct holding, indirect holding or synthetic holding of a capital instrument issued by, or a non-capital LAC liability of, a financial sector entity, any amount of the significant LAC investment that is not deducted from the institution's capital base under sections 43(1)(p), 47(1)(d) and 48(1)(d) must be allocated—

(a) a risk-weight of 250% if the significant LAC investment is in a CET1 capital instrument; or

(b) in any other case—

(i) a risk-weight determined in accordance with section 65G(1)(a) or (b), as the case requires, if the significant LAC investment is an equity exposure; or

(ii) a risk-weight of 150% if the significant LAC investment is not an equity exposure.

(3) If an authorized institution maintains any non-capital LAC debt resources and has holdings of non-capital LAC liabilities that fall within section 48A, the institution must allocate a risk-weight of 150% to any amount of the holdings that is

not deducted from the institution's capital base under section 48(1)(g)(i).

65J. Exposures to subordinated debts

An authorized institution must allocate a risk-weight of 150% to an exposure to a subordinated debt issued by a bank, qualifying non-bank financial institution or corporate.

Subdivision 7—Exposures not falling within Subdivision 3, 4, 5 or 6

(L.N. 167 of 2023)

65K. Cash and gold

(1) An authorized institution must allocate a risk-weight of 0% to the following—

(a) notes and coins owned by the institution that are the lawful currency of a jurisdiction and are held by the institution or in transit;

(b) the institution's holding of certificates of indebtedness issued by the Government for the issue of legal tender notes;

(c) gold bullion held by the institution, or gold bullion held on an allocated basis for the institution by another person, that is backed by gold bullion liabilities.

(2) Gold bullion held on an unallocated basis for an authorized institution by another person that is backed by gold bullion liabilities must be risk-weighted as a claim on that person.

(3) Gold bullion held by an authorized institution, or gold bullion held for the institution by another person, that is not backed by gold bullion liabilities must be allocated a risk-weight of 100%.

(L.N. 167 of 2023)

65L. Items in the process of clearing or settlement

(1) An authorized institution must allocate a risk-weight of 0% to the following—

(a) an unsettled clearing item of the institution that is being processed through any interbank clearing system in Hong Kong;

(b) any receivable from a transaction of the institution in securities, foreign exchange or commodities that is not yet due for settlement.

(2) An authorized institution must allocate a risk-weight of 20% to a cheque, draft or other item drawn on another bank—

(a) that is payable to the account of the institution immediately on presentation; and

(b) that is in the process of collection.

(3) In the case of transactions in securities, foreign exchange and commodities that are entered into by an authorized institution on a delivery-versus-payment basis, if any of those transactions is outstanding after the settlement date in respect of the transaction concerned, the institution must allocate to the positive current exposure incurred by the institution under the transaction a risk-weight of—

(a) 0% if the transaction is outstanding up to and including the 4th business day after the settlement date;

(b) 100% if the transaction remains outstanding from 5 to 15 business days (both days inclusive) after the settlement date;

(c) 625% if the transaction remains outstanding from 16 to 30 business days (both days inclusive) after the settlement date;

(d) 937.5% if the transaction remains outstanding from 31 to 45 business days (both days inclusive) after the settlement date; and

(e) 1 250% if the transaction remains outstanding for 46 or more business days after the settlement date.

(4) In the case of transactions in securities, foreign exchange and commodities that are entered into by an authorized institution on a basis other than a delivery-versus-payment basis, if any of those transactions is outstanding after the settlement date in respect of the transaction concerned, the institution must—

(a) if the transaction remains outstanding up to and including the 4^{th} business day after the settlement date, risk-weight the following items as exposures to the counterparty to the transaction—

(i) the amount of payment made, or the current market value of the thing delivered, by the institution under the transaction; and

(ii) any positive current exposure incurred by the institution under the transaction;

(b) if the transaction remains outstanding for 5 or more business days after the settlement date, allocate a risk-weight of 1 250% to—

(i) the amount of payment made, or the current market value of the thing delivered, by the institution under the transaction; and

(ii) any positive current exposure incurred by the institution under the transaction.

(5) Unless otherwise stated in Part 6A, subsections (1)(b), (3) and (4) do not apply to repo-style transactions.

(L.N. 167 of 2023)

66. Other exposures that are not defaulted exposures

(1) If an exposure is not a defaulted exposure and none of the sections in Subdivisions 3, 4, 5 and 6 or section 65K or 65L applies to the exposure, an authorized institution must allocate a risk-weight of 100% to the exposure.

(2) If, in respect of an exposure of an authorized institution, the institution has difficulty in allocating any accrued interest under the exposure to the obligors of the institution, the institution may, with the prior consent of the Monetary Authority, treat the accrued interest as an exposure to which subsection (1) applies.

(L.N. 167 of 2023)

Subdivision 8—Defaulted Exposures

(L.N. 167 of 2023)

67. Defaulted exposures

(1) Despite Subdivisions 3, 4, 5 and 7 and section 65J, an authorized institution must—

(a) allocate a risk-weight of 100% to a defaulted exposure that is a residential real estate exposure (other than an ADC exposure) where repayments do not depend materially on the cash flows generated by the residential property securing the exposure; and

(b) in any other case, allocate a risk-weight of 150% to a defaulted exposure.

(2) An exposure of an authorized institution to an obligor is a defaulted exposure if—

(a) the exposure is past due for more than 90 days; or

(b) the obligor is a defaulted borrower.

(3) Despite subsection (2)—

(a) a retail exposure (being a regulatory retail exposure or an exposure to an individual that is neither a real estate exposure nor a regulatory retail exposure) of an authorized institution is a defaulted exposure if—

(i) the exposure is past due for more than 90 days;

(ii) the exposure is put on non-accrued status;

(iii) a write-off or specific provision is made for the exposure as a result of a significant perceived decline in the credit quality of the exposure; or

(iv) a distressed restructuring of the exposure is agreed by the institution; and

(b) if—

(i) the institution or any member of the consolidation group of the institution has other outstanding retail exposures to the obligor in respect of a defaulted exposure; and

(ii) those other outstanding retail exposures do not fall within paragraph (a)(i), (ii), (iii) or (iv),

the institution may choose whether to treat those other outstanding retail exposures as defaulted exposures for the purposes of this Part.

(4) For the purposes of subsection (2)(b), an obligor is a defaulted borrower in relation to an authorized institution if any one or more of the following events have occurred in respect of the obligor—

(a) any material credit obligation is past due for more than 90 days;

(b) any material credit obligation is put on non-accrued status;

(c) a write-off or specific provision is made as a result of a significant perceived decline in credit quality subsequent to the institution taking on any credit exposure to the obligor;

(d) any credit obligation is sold at a material credit-related economic loss;

(e) a distressed restructuring of any credit obligation is agreed by the institution;

(f) a filing for the obligor's bankruptcy or a similar order has been made in respect of any of the obligor's credit obligations to the institution or any member of the consolidation group of the institution;

(g) the obligor has sought, or has been placed in, bankruptcy or similar protection where this would avoid or delay repayment of any of the credit obligations to the institution or any member of the consolidation group of the institution;

(h) any other situation where the institution considers that the obligor is unlikely to pay in full its credit obligations to the institution, without recourse to actions by the institution such as realization of available collateral.

(5) For the purposes of subsections (2)(a), (3)(a)(i) and (4)(a)—

(a) if an authorized institution has provided an overdraft facility to an obligor and advised the obligor of the credit limit set for the facility, the facility becomes past due once—

(i) the obligor has breached the credit limit; or

(ii) the institution has advised the obligor of a new credit limit that is smaller than the current outstanding balance of the facility;

(b) if an authorized institution has not provided any overdraft facility to an obligor, an overdraft by the obligor becomes past due on the same day that the overdraft occurs.

(6) To avoid doubt, failure of a counterparty to settle a transaction on the settlement date referred to in section 65L(3) or (4) is not in itself regarded as a default for the purposes of this Part.

(7) In this section—

distressed restructuring (不利的重組) means a restructuring that may result in a diminished financial obligation caused by material forgiveness, or postponement, of principal, interest or, if relevant, fees;

non-accrued status (非累算狀況), in relation to an exposure of an authorized institution to an obligor, includes situations where accrued interest on the exposure is no longer recognized by the institution as income or, if recognized, an equivalent amount of provisions is made by the institution in respect of the exposure.

(L.N. 167 of 2023)

Subdivision 9—Miscellaneous Provisions

(L.N. 167 of 2023)

68. Exposures to credit-linked notes

(1) Subject to subsections (3), (4) and (5), if a credit-linked note issued by an issuer has an ECAI issue specific rating, an authorized institution must—

(a) subject to section 54E(2), determine the credit quality grade applicable to the note by mapping the ECAI issue specific rating of the note to a credit quality grade in accordance with the LT ECAI rating mapping table for

Type A ECAIs or the LT ECAI rating mapping table for Type B ECAIs, as the case requires;

(b) determine the risk-weight that would be attributable to the note as an exposure to the issuer under Subdivision 3 based on the credit quality grade determined under paragraph (a);

(c) determine the risk-weight that would be attributable to the reference obligations of the note—

(i) under that Subdivision based on the credit quality grade determined under paragraph (a) if the reference obligations would fall within one of the ECAI ratings based portfolios; or

(ii) under Subdivision 4, 5, 6, 7 or 8, as applicable, if the reference obligations would not fall within any ECAI ratings based portfolio; and

(d) allocate to an exposure to the note the higher of the 2 risk-weights determined under paragraphs (b) and (c).

(2) Subject to subsections (3), (4) and (5), if a credit-linked note issued by an issuer does not have an ECAI issue specific rating, an authorized institution must allocate a risk-weight to an exposure to the note that is the higher of—

(a) the risk-weight that would be attributable to the note as an exposure to the issuer under Subdivision 3, 4 or 7, as applicable; and

(b) the risk-weight that would be attributable to the reference obligations of the note under Subdivision 3, 4, 5, 6, 7 or 8, as applicable.

(3) If a credit-linked note (whether having an ECAI issue specific rating or not)—

(a) is a first-to-default note, second-to-default note or n^{th}-to-default note; or

(b) provides credit protection proportionately to a basket of reference obligations,

an authorized institution must determine the risk-weight attributable to an exposure to the note as the risk-weight attributable to the pool of reference obligations of the note determined in accordance with section 68B(1), (2), (3) or (4), as the case requires, as if the exposure to the note were a direct exposure to the credit default swap embedded in the note.

(4) If an exposure to a credit-linked note is a defaulted exposure, an authorized institution must determine the risk-weight applicable to the exposure in accordance with Subdivision 8.

(5) This section does not apply to an exposure to a credit-linked note, or any part of such an exposure, to which any provision in Subdivision 6 applies.

(L.N. 167 of 2023)

68A. Determination of risk-weight applicable to certain types of off-balance sheet exposures

(1) If an off-balance sheet exposure of an authorized institution (***subject exposure***) is an asset sale with recourse, a sale and repurchase agreement (other than a repo-style transaction) or a forward asset purchase, where the institution is exposed to the credit risk of the assets sold or to be purchased, the risk-weight applicable to the subject exposure is the risk-weight applicable to those assets.

(2) If a subject exposure is partly paid-up shares and securities, the risk-weight applicable to the subject exposure is the risk-weight applicable to the relevant shares or securities.

(3) If a subject exposure is a direct credit substitute arising from the selling of credit protection in the form of total return swap or credit default swap in the authorized institution's banking

book, subject to section 68B, the risk-weight applicable to the subject exposure is the risk-weight applicable to the reference obligation specified in the swap.

(4) If a subject exposure is a default risk exposure in respect of a single-name credit default swap that falls within section 226J(1) and the amount of the default risk exposure is determined in accordance with section 226J(3), the risk-weight applicable to the subject exposure is the attributed risk-weight of the counterparty in respect of the swap without taking into account any recognized credit risk mitigation afforded to the swap.

(5) If a subject exposure is a commitment to extend a loan secured by a fully completed immovable property and the exposure, but for the fact that it does not satisfy any one or more of section 65(1)(b), (c) or (d), would have been a regulatory real estate exposure, the authorized institution may allocate a risk-weight in accordance with section 65B or 65C, as the case requires, to the exposure, if the institution has no reason to believe that any of section 65(1)(b), (c) or (d) will not be satisfied immediately after the loan that is the subject of the commitment is drawn down.

(L.N. 167 of 2023)

68B. Further provisions in relation to direct credit substitutes

(1) If a subject exposure referred to in section 68A(3) arises from a first-to-default credit derivative contract—

(a) subject to paragraph (b), the risk-weight applicable to the subject exposure is the sum of the risk-weights applicable to the reference obligations in the basket of reference obligations specified in the contract; and

(b) the risk-weight applicable to the subject exposure is subject to a cap of 1 250%.

(2) If a subject exposure referred to in section 68A(3) arises from a second-to-default credit derivative contract—

(a) subject to paragraph (b), the risk-weight applicable to the subject exposure is the sum of the risk-weights applicable to the reference obligations in the basket of reference obligations specified in the contract but excluding the lowest of those risk-weights; and

(b) the risk-weight applicable to the subject exposure is subject to a cap of 1 250%.

(3) If a subject exposure referred to in section 68A(3) arises from any other n^{th}-to-default credit derivative contract, subsection (2), with all necessary modifications, applies to that contract as it applies to a second-to-default credit derivative contract, so that the reference to “lowest” in subsection (2)(a) means—

(a) “lowest and second lowest” in the case of a third-to-default credit derivative contract; and

(b) “lowest, second lowest and third lowest” in the case of a fourth-to-default credit derivative contract,

and likewise for other n^{th}-to-default credit derivative contracts.

(4) If a subject exposure referred to in section 68A(3) arises from a credit derivative contract that provides credit protection proportionately in respect of the reference obligations in the basket of reference obligations specified in the contract, the risk-weight applicable to the subject exposure is calculated in accordance with Formula 1B.

Formula 1B

Calculation of Risk-weight of Off-balance Sheet Exposure Arising from Credit Derivative Contract under Section 68B(4)

$$RW_a = \sum_i (a_i \cdot RW_i)$$

where—

(a) RW_a is the weighted average risk-weight of a basket of reference obligations;

(b) a_i is the proportion of credit protection allocated to reference obligation i; and

(c) RW_i is the risk-weight of reference obligation i.

(L.N. 167 of 2023)

68C. Exposures in respect of assets underlying SFTs

(1) This section applies to an authorized institution's exposure to the asset underlying a specified SFT.

(2) Subject to subsection (3), if a specified SFT is booked in the institution's banking book, the institution must—

(a) treat the securities sold or lent, or the securities provided as collateral, under the specified SFT as an on-balance sheet exposure of the institution as if the institution had never entered into the specified SFT; and

(b) allocate to the exposure the risk-weight attributable to the securities.

(3) If the securities referred to in subsection (2)(a) are securitization issues, the risk-weight attributable to the securities must be determined in accordance with Part 7.

(4) To avoid doubt, if a specified SFT is booked in an authorized institution's trading book, an exposure of the institution to the asset underlying the specified SFT is an exposure subject to the requirements of Part 8 instead of this Part.

(5) In this section—

specified SFT (指明SFT), in relation to an authorized institution, means—

(a) a repo-style transaction that falls within paragraph (a) or (b) of the definition of ***repo-style transaction*** in section 2(1); or

(b) a repo-style transaction that falls within paragraph (d) of that definition under which the collateral provided by the institution is in the form of securities.

(L.N. 167 of 2023)

Division 3A—CIS Exposures

(L.N. 167 of 2023)

69. Interpretation of Division 3A

In this Division—

indirect CIS exposure (間接CIS風險承擔) means an indirect CIS exposure within the meaning of section 226ZH;

Level 1 CIS (1級CIS) means a Level 1 CIS within the meaning of section 226ZH;

Level 2 CIS (2級CIS) means a Level 2 CIS within the meaning of section 226ZH;

Level n+1 CIS (n+1級CIS) means a Level n+1 CIS within the meaning of section 226ZH.

(L.N. 167 of 2023)

70. Treatment of CIS exposure held by authorized institution

(1) If no amount of an authorized institution's CIS exposure to a Level 1 CIS constitutes a deductible holding, the institution

must calculate the risk-weighted amount of the exposure in accordance with Part 6B.

(2) If any amount of an authorized institution's CIS exposure to a Level 1 CIS constitutes one or more deductible holdings, the institution must—

(a) classify the amounts of the CIS exposure that constitute deductible holdings into one portion (***portion A***);

(b) classify the amount of the CIS exposure that does not constitute deductible holdings into another portion (***portion B***);

(c) apply the treatment set out in section 70A to each of the amounts of the CIS exposure in portion A; and

(d) calculate the risk-weighted amount of portion B (if any) in accordance with Part 6B.

(L.N. 167 of 2023)

70AA. *(Repealed L.N. 167 of 2023)*

70AAB. *(Repealed L.N. 167 of 2023)*

70AAC. *(Repealed L.N. 167 of 2023)*

70AAD. *(Repealed L.N. 167 of 2023)*

70A. Treatment of CIS exposure constituting deductible holding

(1) This section applies in relation to an authorized institution's CIS exposure to a Level 1 CIS, or any part of the exposure, that constitutes a deductible holding.

(2) The institution must—

(a) determine, in accordance with Division 4 of Part 3, the amount of the deductible holding that is required to be deducted from its capital base;

(b) if the deductible holding falls within section 43(1)(o) or (p), 47(1)(c) or 48(1)(c) or (g)(i)—determine the amount of the deductible holding that is required to be risk-weighted in accordance with section 48(3), section 5 of Schedule 4F or section 1(7) of Schedule 4G, as the case requires;

(c) deduct any amount determined under paragraph (a) from its capital base; and

(d) calculate the risk-weighted amount of any amount determined under paragraph (b) by multiplying that amount by the applicable risk-weight determined in accordance with subsection (3).

(3) The institution must—

(a) allocate a risk-weight, determined in accordance with section 65G(1)(a) or (b), as the case requires, to any amount of deductible holding determined under subsection (2)(b), if the deductible holding is an insignificant LAC investment that is an equity exposure;

(b) allocate a risk-weight of 150% to any amount of deductible holding determined under subsection (2)(b), if the deductible holding is—

(i) an insignificant LAC investment that is not an equity exposure; or

(ii) a holding of non-capital LAC liabilities falling within section 48A; and

(c) allocate a risk-weight of 250% to any amount of deductible holding determined under subsection (2)(b), if the deductible holding is a significant LAC investment in a CET1 capital instrument.

(4) To avoid doubt, this section also applies to cases where a CIS exposure to a Level 1 CIS, or any part of the exposure,

constitutes a deductible holding because regulatory deductible items are held by—

(a) a Level 2 CIS to which the Level 1 CIS has a CIS exposure; or

(b) a Level n+1 CIS (where n is an integer equal to or greater than 2) to which the Level 1 CIS has an indirect CIS exposure.

(L.N. 167 of 2023)

70B. Determination of risk-weights applicable to certain types of off-balance sheet CIS exposures

(1) This section applies to a CIS exposure that is an off-balance sheet exposure.

(2) If the CIS exposure is an asset sale with recourse, a sale and repurchase agreement (other than a repo-style transaction) or a forward asset purchase, where the seller or buyer of the assets underlying the transaction is exposed to the credit risk of the assets sold or to be purchased, the risk-weight applicable to the CIS exposure is the risk-weight applicable to those assets.

(3) If the CIS exposure is partly paid-up shares and securities, the risk-weight applicable to the CIS exposure is the risk-weight applicable to the relevant shares or securities.

(L.N. 167 of 2023)

Division 4—Calculation of Exposure Amounts of Off-balance Sheet Exposures

(L.N. 167 of 2023)

71. Calculation of exposure amounts of off-balance sheet exposures

(L.N. 167 of 2023)

(1) An authorized institution must calculate the credit equivalent amount of an off-balance sheet exposure (other than an exposure to which subsection (2) or (5) applies) by—

(a) determining the CCF applicable to the exposure in accordance with Schedule 6 and, if applicable, subsection (1A); and

(b) multiplying the principal amount of the exposure, after deducting any specific provisions applicable to the exposure, by the CCF determined under paragraph (a). *(L.N. 167 of 2023)*

(1A) If an off-balance sheet exposure (***exposure A***) is a commitment the drawdown of which would give rise to another off-balance sheet exposure (***exposure B***), the CCF applicable to exposure A is the lower of—

(a) the CCF applicable to the commitment determined in accordance with Schedule 6; and

(b) the CCF applicable to exposure B determined in accordance with Schedule 6. *(L.N. 167 of 2023)*

(2) If—

(a) an authorized institution has posted unsegregated collateral to a counterparty for a transaction or contract booked in its banking book or trading book; and

(b) either—

(i) the collateral is not posted for a derivative contract or SFT; or

(ii) the collateral is posted for a derivative contract or SFT but is not included in the calculation of default risk exposures under Division 1A, 2 or 2B of Part 6A,

the institution must calculate the credit equivalent amount of its off-balance sheet exposure to the counterparty in respect of the collateral as the product of the principal amount (without deduction of any specific provisions) of the collateral and a factor of (1 + H). *(L.N. 44 of 2020)*

(3) For the purposes of subsection (2), H is the standard supervisory haircut applicable to the collateral, subject to adjustment set out in section 92. *(L.N. 44 of 2020)*

(4) *(Repealed L.N. 167 of 2023)*

(5) An authorized institution must calculate its default risk exposure in respect of derivative contracts or SFTs by using the approach or methods set out in Division 1A, 2 or 2B of Part 6A, as the case requires. *(L.N. 44 of 2020)*

72-73. *(Repealed L.N. 167 of 2023)*

74. *(Repealed L.N. 54 of 2022)*

75-76. *(Repealed L.N. 167 of 2023)*

76A. *(Repealed L.N. 167 of 2023)*

Division 5—Use of Recognized Collateral in Credit Risk Mitigation: General

77. Recognized collateral

(1) Collateral is recognized for the purpose of calculating the risk-weighted amount of an exposure (***collateralized exposure***) of an authorized institution if—

(a) for an institution that uses the simple approach in its treatment of recognized collateral—all the criteria specified in subsections (2) and (3) are met; or

(b) for an institution that uses the comprehensive approach in its treatment of recognized collateral—all the criteria specified in subsections (2) and (4) are met.

(2) The criteria specified in this subsection are—

(a) all documentation creating the collateral and providing for the obligations of the parties with respect to each other in respect of the collateral is binding on all parties and legally enforceable in all relevant jurisdictions;

(b) the legal mechanism by which the collateral is pledged (or otherwise provided as security) ensures that the authorized institution has the right to realize, or to take legal possession of, the collateral in a timely manner in the event of a default by, or the insolvency or bankruptcy of, or any other event specified in the relevant legal documentation applicable to any of—

(i) the obligor in respect of the collateralized exposure; or

(ii) the custodian, if any, holding the collateral;

(c) the authorized institution has clear and adequate procedures for the timely realization of collateral in respect of an event referred to in paragraph (b);

(d) the authorized institution has taken all steps to fulfil requirements under the law applicable to the institution's interest in the collateral that are necessary to obtain and maintain an enforceable security interest, whether by registration or otherwise, or to exercise a right to set-off in relation to the title transfer of the collateral;

(e) if the collateral is to be held by a custodian, the authorized institution has taken reasonable steps to ensure that the custodian segregates the collateral from the custodian's assets;

(f) if the collateral is provided under a margin agreement for derivative contracts or SFTs, the authorized institution—

(i) has devoted sufficient resources to enable the orderly operation of the agreement; and

(ii) has collateral management policies in place to control, monitor and report—

(A) risks (including liquidity risk and concentration risk) associated with the agreement;

(B) reuse of collateral; and

(C) the rights ceded by the institution in respect of collateral posted; and

(g) the credit quality of the obligor in respect of the collateralized exposure does not have material positive correlation with—

(i) the current market value of the collateral; and

(ii) the residual risks (including legal, operational, liquidity and market risks) arising from the use of the collateral for the purpose of mitigating the credit risk of the collateralized exposure.

(3) The criteria specified in this subsection are—

(a) the collateral falls within any one of the items listed in section 79(1);

(b) the collateral is pledged (or otherwise provided as security) for not less than the life of the collateralized exposure; and

(c) the collateral—

(i) subject to subparagraph (ii), is revalued not less than every 6 months from the date on which the collateral is taken in respect of the collateralized exposure; and

(ii) if the collateralized exposure is a defaulted exposure, is revalued not less than every 3 months from the date on which the collateralized exposure is classified as a defaulted exposure.

(4) The criteria specified in this subsection are—

(a) the collateral falls within any one of the items listed in section 80(1);

(b) the authorized institution has in place a written internal policy and systems and procedures—

(i) adequate to enable the institution to manage collateral provided to it in respect of any exposure; and

(ii) to revalue collateral as necessary and take account of the minimum holding periods for collateral in the calculation of the risk-weighted amounts of its collateralized exposures.”.

(L.N. 167 of 2023)

78. Approaches to use of recognized collateral

(1) Subject to subsection (2), an authorized institution may use the simple approach or the comprehensive approach in its treatment of recognized collateral for the purpose of calculating the risk-weighted amounts of its exposures that are not default risk exposures (***non-default risk exposures***). *(L.N. 44 of 2020)*

(1A) Subject to subsection (2), an authorized institution may use the simple approach or the comprehensive approach to take into account the credit risk mitigation effect of recognized collateral for the purpose of calculating the risk-weighted amount of a default risk exposure only if either of the following is complied with in respect of the exposure—

(a) the exposure is in respect of an SFT calculated in accordance with section 226MJ;

(b) the exposure is in respect of one or more than one derivative contract entered into by the institution with a counterparty and the conditions specified in subsection (1B) are met. *(L.N. 44 of 2020)*

(1B) The conditions are—

(a) the institution entered into the contract or contracts with the counterparty under a general banking facility consisting of 2 or more credit lines, and, for at least one of those credit lines, if drawn (whether in full or not), the drawn portion that will result from such drawdown is, at the time of the drawdown, a non-default risk exposure;

(b) the credit lines are secured by the same recognized collateral;

(c) no amount of the recognized collateral is designated solely for offsetting losses on default risk exposures incurred by the institution under the general banking facility; and

(d) the recognized collateral is not included in the calculation of the default risk exposure under Division 1A or 2 of Part 6A. *(L.N. 44 of 2020)*

(1C) If the same recognized collateral is available to cover both default risk exposures and non-default risk exposures, an authorized institution may, under the simple approach or comprehensive approach, take into account the credit risk mitigation effect of the recognized collateral for the purpose of calculating the risk-weighted amount of the non-default risk exposures only to the extent of the current market value, or the part of such value, of the collateral that is not included in the calculation of the default risk exposures under Division 1A or 2 of Part 6A. *(L.N. 44 of 2020)*

(2) An authorized institution must—

(a) for exposures that are not defaulted exposures, use only the simple approach or only the comprehensive approach to the treatment of recognized collateral; and

(b) for defaulted exposures, use only the simple approach to the treatment of recognized collateral. *(L.N. 167 of 2023)*

79. Collateral which may be recognized under simple approach

(L.N. 167 of 2023)

(1) Subject to subsections (2) and (3), only collateral of the following description may be recognized in relation to an authorized institution that uses the simple approach in its treatment of recognized collateral—

(a) cash on deposit with the institution or held at a third-party bank;

(b) certificates of deposit issued by the institution;

(c) instruments issued by the institution that are comparable to instruments referred to in paragraph (b);

(d) gold bullion;

(e) debt securities issued by a sovereign that have a long-term ECAI issue specific rating that, if mapped to a credit quality grade in accordance with the LT ECAI rating mapping table for Type A ECAIs, would result in the debt securities being assigned a credit quality grade of 1, 2, 3, 4 or 5;

(f) debt securities (other than restricted debt securities) issued by a sovereign foreign public sector entity that have a long-term ECAI issue specific rating that, if mapped to a credit quality grade in accordance with the LT ECAI rating mapping table for Type A ECAIs, would result in the debt securities being assigned a credit quality grade of 1, 2, 3, 4 or 5;

(g) debt securities issued by a multilateral development bank that would be allocated a risk-weight of 0% under section 58;

(h) debt securities issued by an entity (other than an entity falling within paragraph (e), (f) or (g)) that have a long-term ECAI issue specific rating where that rating—

(i) is issued by a Type A ECAI; and

(ii) if mapped to a credit quality grade in accordance with the LT ECAI rating mapping table for Type A ECAIs, would result in the debt securities being assigned a credit quality grade of 1, 2, 3 or 4;

(i) debt securities issued by a corporate incorporated in the home jurisdiction of a Type B ECAI that have a long-term ECAI issue specific rating where that rating—

(i) is issued by that Type B ECAI; and

(ii) if mapped to a credit quality grade in accordance with the LT ECAI rating mapping table for Type B ECAIs, would result in the debt securities being assigned a credit quality grade of 1, 2, 3 or 4;

(j) debt securities issued by an entity (other than an entity falling within paragraph (g)) that have a short-term ECAI issue specific rating where that rating—

(i) is issued by a Type A ECAI; and

(ii) if mapped to a credit quality grade in accordance with the ST ECAI rating mapping table for Type

A ECAIs, would result in the debt securities being assigned a credit quality grade of 1, 2 or 3;

(k) debt securities issued by a corporate incorporated in the home jurisdiction of a Type B ECAI that have a short-term ECAI issue specific rating where that rating—

(i) is issued by that Type B ECAI; and

(ii) if mapped to a credit quality grade in accordance with the ST ECAI rating mapping table for Type B ECAIs, would result in the debt securities being assigned a credit quality grade of 1, 2, 3 or 4;

(l) debt securities issued by a bank that do not have an ECAI issue specific rating where—

(i) the debt securities are not subordinated to any other debt obligations of the bank;

(ii) the debt securities are listed on a recognized exchange and the institution is of the reasonable opinion that, having regard to current market conditions, there is sufficient liquidity in the market for the debt securities to enable the institution to dispose of the debt securities at an open market price;

(iii) other debt securities issued by the bank that rank equally with the first-mentioned debt securities—

(A) have a long-term ECAI issue specific rating that, if mapped to a credit quality grade in accordance with the LT ECAI rating mapping table for Type A ECAIs, would result in those other debt securities being assigned a credit quality grade of 1, 2, 3 or 4; or

(B) have a short-term ECAI issue specific rating that, if mapped to a credit quality grade in accordance with the ST ECAI rating mapping table for Type A ECAIs, would result in those other debt securities being assigned a credit quality grade of 1, 2 or 3; and

(iv) the institution is not aware, and has no reason to be aware, of information suggesting that it is justifiable for the debt securities to have an ECAI issue specific rating that would be mapped to a credit quality grade of 5, 6 or 7 in accordance with the LT ECAI rating mapping table for Type A ECAIs or a credit quality grade of 4 in accordance with the ST ECAI rating mapping table for Type A ECAIs;

(m) equities (including convertible bonds) that are included in any main indices;

(n) units or shares in a collective investment scheme where—

(i) the price of the units or shares in that scheme is quoted publicly on a daily basis; and

(ii) that scheme is restricted by its investment guidelines or objects to investing in those items listed in this subsection except in paragraph (o); or

(o) securities that are—

(i) eligible for inclusion in the trading book; and

(ii) received by the institution under a repo-style transaction booked in the institution's trading book. *(L.N. 167 of 2023)*

(2) A reference to debt securities in subsection (1) does not include debt securities that are re-securitization exposures. *(L.N. 167 of 2023)*

(3) If a debt security issued by a sovereign has neither a long-term ECAI issue specific rating nor short-term ECAI issue specific rating, an authorized institution may, for the purposes of this section, regard the ECAI issuer rating of the sovereign, if any, as the long-term ECAI issue specific rating of the debt security. *(L.N. 44 of 2020)*

80. Collateral that may be recognized under comprehensive approach

(1) Subject to subsection (2), only collateral of the following description may be recognized in relation to an authorized institution that uses the comprehensive approach in its treatment of recognized collateral—

(a) collateral falling within any paragraph of section 79(1);

(b) equities (including convertible bonds) that are not included in a main index but are listed on a recognized exchange; or

(c) units or shares in a collective investment scheme where—

(i) the price of the units or shares in that scheme is quoted publicly on a daily basis; and

(ii) that scheme is restricted by its investment guidelines or objects to investing in the equities referred to in paragraph (b) and those items listed in section 79(1) (except in section 79(1)(o)).

(2) Collateral referred to in subsection (1) does not include debt securities that are re-securitization exposures.

(L.N. 167 of 2023)

Division 6—Use of Recognized Collateral in Credit Risk Mitigation: Simple Approach

81. Calculation of risk-weighted amount of exposures taking into account credit risk mitigating effect of recognized collateral under simple approach

If an authorized institution uses the simple approach in its treatment of recognized collateral, the institution must calculate the risk-weighted amounts of its on-balance sheet exposures and off-balance sheet exposures to which the collateral relates in accordance with this Division.

(L.N. 167 of 2023)

82. Determination of risk-weight to be allocated to recognized collateral under simple approach

(1) Subject to subsections (2), (3), (4) and (5), if an authorized institution uses the simple approach in its treatment of recognized collateral, the institution—

(a) subject to paragraph (b), must determine the risk-weight to be allocated to the collateral in accordance with Division 3, section 226ZJ or Part 7, as the case requires, as if the collateral were an on-balance sheet exposure; and

(b) must not allocate a risk-weight of less than 20% to the collateral.

(2) For recognized collateral—

(a) that falls within section 79(1)(a), (b) or (c);

(b) that is held at a third-party bank in a non-custodial arrangement; and

(c) that is unconditionally and irrevocably pledged (or otherwise provided as security) or assigned to an authorized institution, the institution must treat the credit protection covered portion of the exposure to which the collateral relates as an exposure to the third-party bank and allocate a risk-weight to the credit protection covered portion in accordance with sections 59 and 59A, or sections 59B and 59C, as the case requires.

(3) An authorized institution may allocate—

(a) a risk-weight of 0% to recognized collateral provided under a repo-style transaction entered into with a counterparty if all the criteria specified in subsection (4) are met; or

(b) a risk-weight of 10% to recognized collateral provided under a repo-style transaction entered into with a counterparty if all the criteria specified in subsection (4) (other than subsection (4)(a)) are met.

(4) The criteria specified in this subsection are—

(a) the counterparty is—

(i) a sovereign;

(ii) a public sector entity;

(iii) a multilateral development bank, where exposures to which would be allocated a risk-weight of 0% under section 58;

(iv) a bank or securities firm;

(v) a qualifying non-bank financial institution (other than a securities firm) that has an attributed risk-weight of not more than 20%;

(vi) a corporate (other than a securities firm)—

(A) that is an investment company, insurance firm, finance company or other similar financial institution; and

(B) that has an attributed risk-weight of not more than 20%; or

(vii) a qualifying CCP;

(b) the exposure to which the collateral relates and the collateral are—

(i) cash; or

(ii) debt securities issued by a sovereign, or a sovereign foreign public sector entity, that would be allocated a risk-weight of 0% under this Part;

(c) the exposure and the collateral have no currency mismatch;

(d) either—

(i) the exposure is only an overnight exposure; or

(ii) the exposure and the collateral are subject to daily mark-to-market, and, if the mark-to-market value of any excess collateral (***margin***) is below the value required under the terms of the transaction, the counterparty is required to bring the margin up to the required value on the same day (***remargin***);

(e) the authorized institution reasonably expects, if the counterparty fails to remargin, the time between the day on which the exposure is marked-to-market for the last time before the counterparty's failure to remargin and the day on which the institution realizes the collateral for its benefit to be no more than 4 business days;

(f) the transaction is settled by means of a settlement system customarily used for repo-style transactions;

(g) the transaction is documented using standard market documentation for repo-style transactions involving securities of the same type as those that are the subject matter of the transaction; and

(h) the documentation setting out the transaction provides that—

(i) the authorized institution may terminate the transaction immediately if—

(A) the counterparty commits an event of default under the transaction; or

(B) an event of default occurs in respect of the counterparty; and

(ii) the authorized institution has, immediately on any such default, an unfettered and legally enforceable right to seize and realize the collateral for its benefit, whether or not the counterparty is insolvent or bankrupt.

(5) An authorized institution may allocate a risk-weight of 0% to recognized collateral provided in respect of an exposure other than a default risk exposure where—

(a) the collateral and the exposure have no currency mismatch; and

(b) the collateral is either—

(i) cash; or

(ii) debt securities—

(A) that are issued by a sovereign, or a sovereign foreign public sector entity, and would be allocated a risk-weight of 0% under this Part; and

(B) the current market value of which has been discounted by 20%.

(6) In this section—

cash (現金)—

(a) in relation to an exposure, means money paid by an authorized institution to a counterparty under a repo-style transaction; or

(b) in relation to collateral, means recognized collateral that falls within section 79(1)(a), (b) or (c), other than collateral held at a third-party bank in a non-custodial arrangement.

(L.N. 167 of 2023)

83. Calculation of risk-weighted amount of on-balance sheet exposures

An authorized institution shall calculate the risk-weighted amount of each of its on-balance sheet exposures by—

(a) dividing the exposure amount of the exposure into— *(L.N. 167 of 2023)*

(i) the credit protection covered portion; and

(ii) the credit protection uncovered portion;

(b) multiplying the credit protection covered portion by the risk-weight attributable to the recognized collateral and multiplying the credit protection uncovered portion by the risk-weight attributable to the exposure; and

(c) adding together the 2 products derived from the application of paragraph (b).

84. Calculation of risk-weighted amount of off-balance sheet exposures other than default risk exposures

(L.N. 137 of 2011; L.N. 44 of 2020)

An authorized institution shall calculate the risk-weighted amount of each of its off-balance sheet exposures which is not a default risk exposure by— *(L.N. 137 of 2011; L.N. 44 of 2020)*

(a) dividing the principal amount of the exposure, net of specific provisions, into—

(i) the credit protection covered portion; and

(ii) the credit protection uncovered portion;

(b) multiplying the credit protection covered portion and the credit protection uncovered portion by the CCF applicable to the off-balance sheet exposure to produce 2 credit equivalent amounts;

(c) multiplying the credit equivalent amount of the credit protection covered portion by the risk-weight attributable to the recognized collateral and multiplying the credit equivalent amount of the credit protection uncovered portion by the risk-weight attributable to the exposure; and

(d) adding together the 2 products derived from the application of paragraph (c).

85. Calculation of risk-weighted amount of default risk exposures

(L.N. 137 of 2011; L.N. 44 of 2020)

(1) An authorized institution must calculate the risk-weighted amount of its default risk exposure that is an exposure mentioned in section 78(1A)(a) or (b) by— *(L.N. 137 of 2011; L.N. 44 of 2020)*

(a) dividing the exposure amount of the exposure into—

(i) the credit protection covered portion; and

(ii) the credit protection uncovered portion; *(L.N. 167 of 2023)*

(b) multiplying the credit protection covered portion by the risk-weight attributable to the recognized collateral and multiplying the credit protection uncovered portion by the risk-weight attributable to the exposure; and *(L.N. 156 of 2012)*

(c) adding together the 2 products derived from the application of paragraph (b). *(L.N. 156 of 2012)*

(d) *(Repealed L.N. 156 of 2012)*

(2) *(Repealed L.N. 44 of 2020)*

Division 7—Use of Recognized Collateral in Credit Risk Mitigation: Comprehensive Approach

86. Calculation of risk-weighted amount of exposures taking into account credit risk mitigating effect of recognized collateral under comprehensive approach

If an authorized institution uses the comprehensive approach in its treatment of recognized collateral, the institution must calculate the risk-weighted amounts of its on-balance sheet exposures and off-balance sheet exposures to which the collateral relates by—

(a) calculating the net credit exposure to the obligor of each of the exposures in accordance with section 87, 88 or 89, with the applicable haircuts determined in accordance with sections 90, 91 and 92; and

(b) multiplying the net credit exposure so obtained by the risk-weight attributable to the exposure.

(L.N. 167 of 2023)

87. Calculation of net credit exposure of on-balance sheet exposures

An authorized institution shall calculate its net credit exposure to an obligor in respect of an on-balance sheet exposure by the use of Formula 2.

Formula 2

Calculation of Net Credit Exposure to Obligor under On-balance Sheet Exposure

$$E^* = \max\ \{0, [E \times (1 + H_e) - C \times (1 - H_c - H_{fx})]\}$$

where—

E^*	=	net credit exposure;
E	=	exposure amount of on-balance sheet exposure;
H_e	=	haircut applicable to the authorized institution's exposure to the obligor pursuant to the standard supervisory haircuts subject to adjustment as set out in section 92;
C	=	current market value of the recognized collateral before adjustment required by the comprehensive approach to the treatment of recognized collateral;
H_c	=	haircut applicable to the recognized collateral pursuant to the standard supervisory haircuts subject to adjustment as set out in section 92; and
H_{fx}	=	haircut applicable in consequence of a currency mismatch, if any, pursuant to the standard supervisory haircuts subject to adjustment as set out in section 92.

(L.N. 44 of 2020; L.N. 167 of 2023)

88. Calculation of net credit exposure of off-balance sheet exposures other than default risk exposures in respect of derivative contracts

(L.N. 156 of 2012; L.N. 44 of 2020)

(1) An authorized institution shall calculate its net credit exposure to an obligor in respect of an off-balance sheet exposure (other than a default risk exposure in respect of derivative contracts) by the use of Formula 3. *(L.N. 44 of 2020; L.N. 167 of 2023)*

Formula 3

Calculation of Net Credit Exposure to Obligor under Off-balance Sheet Exposure other than Default Risk Exposure in Respect of Derivative Contracts

(L.N. 44 of 2020)

$$E^* = \max\{0, [E \times (1 + H_e) - C \times (1 - H_c - H_{fx})]\} \times CCF$$

where—

E* = net credit exposure;

E = either of the following— *(L.N. 44 of 2020)*

(a) if the off-balance sheet exposure is a default risk exposure mentioned in section 78(1A)(a)—the amount of the default risk exposure calculated in accordance with section 226MJ;

(b) in any other case—principal amount of the off-balance sheet exposure, net of specific provisions (if any);

H_e = either of the following— *(L.N. 44 of 2020)*

(a) unless paragraph (b) applies—haircut applicable to the authorized institution’s exposure to the obligor pursuant to the standard supervisory haircuts subject to adjustment as set out in section 92;

(b) if the off-balance sheet exposure is a default risk exposure mentioned in section 78(1A)(a)—haircut applicable to the securities provided by the institution to the obligor under the SFT concerned pursuant to the standard supervisory haircuts subject to adjustment as set out in section 92;

C = current market value of the recognized collateral before adjustment required by the comprehensive approach to the treatment of recognized collateral;

H_c = haircut applicable to the recognized collateral pursuant to the standard supervisory haircuts subject to adjustment as set out in section 92;

H_{fx} = haircut applicable in consequence of a currency mismatch, if any, pursuant to the standard supervisory haircuts subject to adjustment as set out in section 92; and

CCF = either of the following— *(L.N. 44 of 2020)*

(a) if the off-balance sheet exposure is a default risk exposure mentioned in section 78(1A)(a)—100%;

(b) in any other case—CCF applicable to the off-balance sheet exposure.

(L.N. 156 of 2012; L.N. 44 of 2020; L.N. 167 of 2023)

(2) If an off-balance sheet exposure is a default risk exposure mentioned in section 78(1A)(a), the net credit exposure in respect of the exposure calculated by using Formula 3 may be further reduced by the amount of any specific provisions made by the authorized institution. *(L.N. 167 of 2023)*

89. Calculation of net credit exposure of default risk exposures in respect of derivative contracts

(L.N. 156 of 2012; L.N. 44 of 2020)

An authorized institution must calculate the net credit exposure of its default risk exposure that is an exposure mentioned in section 78(1A)(b) by the use of Formula 4. *(L.N. 44 of 2020)*

Formula 4

Calculation of Net Credit Exposure to Counterparty under Derivative Contracts

(L.N. 44 of 2020)

$$E^* = \max \{0, [E - C \times (1 - H_c - H_{fx})]\}$$

where—

E^* = net credit exposure;

E = exposure amount of the default risk exposure in respect of the derivative contracts concerned;

C = current market value of the recognized collateral before adjustment required by the comprehensive approach to the treatment of recognized collateral;

H_c = haircut applicable to the recognized collateral pursuant to the standard supervisory haircuts subject to adjustment as set out in section 92; and

H_{fx} = haircut applicable in consequence of a currency mismatch, if any, pursuant to the standard supervisory haircuts subject to adjustment as set out in section 92.

(L.N. 156 of 2012; L.N. 44 of 2020; L.N. 167 of 2023)

90. Haircut applicable to a basket of recognized collateral

If a basket of recognized collateral is provided to an authorized institution in respect of an exposure of the institution and the recognized collateral is made up of assets that are subject to haircuts of different values, the institution must calculate the haircut applicable to the basket of recognized collateral by the use of Formula 5.

Formula 5

Calculation of Haircut where Recognized Collateral is made up of Assets with Different Haircuts

$$H_a = \sum_i (a_i \times H_i)$$

where—

(a) H_a is the haircut applicable to the basket of recognized collateral;

(b) a_i is the weight of asset i in relation to the aggregate value of all assets in the basket; and

(c) H_i is the haircut applicable to asset i under the standard supervisory haircuts subject to adjustment as set out in section 92.

(L.N. 167 of 2023)

91. Minimum holding periods

(1AA) For the purposes of section 87, 88, 89, 90, 94, 100 or 103 and subject to subsection (4), an authorized institution must, in order to determine the haircuts applicable to an exposure and the recognized collateral provided in respect of the exposure, set the minimum holding period of the transaction giving rise to the exposure as—

(a) if the exposure is not a default risk exposure or is a default risk exposure mentioned in section 78(1A)(a)—the minimum holding period determined in accordance with subsections (1), (2) and (3); or

(b) if the exposure is a default risk exposure mentioned in section 78(1A)(b)—the minimum holding period or the margin period of risk of the transaction determined in accordance with Part 6A. *(L.N. 44 of 2020)*

(1) Where in respect of an exposure of an authorized institution, there is— *(L.N. 156 of 2012)*

(a) a daily revaluation of the exposure and the recognized collateral provided in respect of the exposure; or

(b) a requirement that the obligor in respect of the exposure has to bring the value of the recognized collateral provided in respect of the exposure up to a value required under the terms of the transaction giving rise to the exposure based on the daily mark-to-market value of the exposure and the collateral (referred to in this Division as ***daily remargining***),

the institution must determine the minimum holding period of the transaction giving rise to the exposure in accordance with Table 12 based on the type of transaction to which the transaction belongs.

Table 12

Minimum Holding Periods

(L.N. 44 of 2020)

Type of transaction	Minimum holding period	Condition
Repo-style transactions	5 business days	Daily remargining
Other capital market transactions	10 business days	Daily remargining
Secured lending transactions	20 business days	Daily revaluation

(L.N. 44 of 2020)

(2) Where the exposure referred to in subsection (1) arises from a netting set that falls within any of the descriptions in section 226M(2), (3) or (7), the minimum holding period of the netting set must be equal to the longer margin period of risk that would apply to the netting set under section 226M(2), (3) or (7), as the case requires. *(L.N. 156 of 2012; L.N. 175 of 2017)*

(3) If—

(a) an exposure is not subject to daily remargining; or

(b) an exposure and the recognized collateral provided in respect of the exposure are not subject to daily revaluation,

the minimum holding period of the transaction giving rise to the exposure must be calculated by using Formula 5A.

Formula 5A

Calculation of Minimum Holding Period for Circumstances Set Out in Paragraphs (a) and (b)

$$\text{Minimum holding period} = N_R + (T_M - 1)$$

where—

N_R = actual number of days between each remargining or each revaluation; and

T_M = minimum holding period determined in accordance with subsections (1) and (2) for the transaction as if there were daily remargining or daily revaluation.

(L.N. 44 of 2020)

(4) When calculating the credit equivalent amount of an off-balance sheet exposure to a counterparty arising from unsegregated collateral posted to the counterparty for mitigating the credit risk of a contract or transaction in accordance with section 71(2), an authorized institution must, for the purpose of determining the haircut applicable to the collateral—

(a) determine the minimum holding period or the margin period of risk of the contract or transaction in accordance with subsections (1), (2) and (3) or Part 6A, as the case requires; and

(b) take the minimum holding period or the margin period of risk determined under paragraph (a) to be the minimum holding period of the collateral. *(L.N. 44 of 2020)*

(L.N. 44 of 2020)

92. Adjustment of standard supervisory haircuts in certain circumstances

(1) Where an authorized institution is required under these Rules to use a haircut to take into account the volatility of the value of an exposure, collateral or exchange rate, if— *(L.N. 167 of 2023)*

(a) the minimum holding period or the margin period of risk of the transaction giving rise to the exposure determined in accordance with section 91(1), (2) and (3) or Part 6A is not 10 business days; or

(b) the minimum holding period of the collateral determined in accordance with section 91(4) is not 10 business days,

the institution must determine the value of the haircut by adjusting the standard supervisory haircut concerned in accordance with section 3 of Schedule 7.

(2) Despite subsection (1) and the standard supervisory haircuts specified in Schedule 7, an authorized institution may, in calculating the risk-weighted amount of a default risk exposure in respect of a repo-style transaction under section 88, apply a haircut of 0% to both the exposure and the recognized collateral received under the repo-style transaction if the repo-style transaction satisfies all the criteria set out in section 82(4). *(L.N. 167 of 2023)*

(L.N. 44 of 2020)

93. *(Repealed L.N. 167 of 2023)*

Division 8—Use of Recognized Netting in Credit Risk Mitigation

94. On-balance sheet netting

(1) Where amounts owed by an obligor to an authorized institution in respect of on-balance sheet exposures (other than CIS exposures) of the institution are subject to recognized netting, the institution— *(L.N. 54 of 2022)*

(a) may take into account the effect of the recognized netting in calculating its exposure to the obligor; and

(b) if a net credit exposure for the institution is the result of so taking into account the effect of the recognized netting, shall use the net credit exposure in calculating the risk-weighted amount of the exposure.

(2) An authorized institution shall calculate its net credit exposure, if any, referred to in subsection (1)(b) by the use of Formula 7.

Formula 7

Calculation of Net Credit Exposure under Recognized Netting

$$\text{Net credit exposure} = \max [0, \text{exposures} - \text{liabilities} \times (1 - H_{fx})]$$

where—

exposures	=	the amounts subject to recognized netting, net of specific provisions, owed by the obligor to the authorized institution;
liabilities	=	the amounts subject to recognized netting owed by the authorized institution to the obligor; and
H_{fx}	=	haircut applicable in consequence of a currency mismatch, if any, between the currencies in which the exposures and liabilities are denominated pursuant to the standard supervisory haircuts applicable to currency mismatch set out in Schedule 7 subject to adjustment as set out in section 92.

(3) An authorized institution must calculate the risk-weighted amount of its net credit exposure to an obligor as the product of the net credit exposure and the risk-weight attributable, in accordance with Division 3, to the exposure. *(L.N. 167 of 2023)*

94A. *(Repealed L.N. 44 of 2020)*

95-97. *(Repealed L.N. 44 of 2020)*

Division 9—Use of Recognized Guarantees and Recognized

Credit Derivative Contracts in Credit Risk Mitigation

98. Recognized guarantees

A guarantee given to an authorized institution is recognized for the purposes of calculating the risk-weighted amount of a specific exposure or a specific pool of exposures of the institution (***guaranteed exposure***) if— *(L.N. 167 of 2023)*

(a) the guarantee is given by an eligible credit protection provider described in section 99A (***guarantor***); *(L.N. 167 of 2023)*

(b) the guarantee gives the institution a direct claim against the guarantor; *(L.N. 167 of 2023)*

(c) the credit protection provided by the guarantee relates specifically to the guaranteed exposure; *(L.N. 167 of 2023)*

(ca) the credit quality of the obligor in respect of the guaranteed exposure does not have material positive correlation with—

(i) the credit quality of the guarantor; and

(ii) the residual risks (including legal, operational, liquidity and market risks) arising from the use of the guarantee for the purpose of mitigating the credit risk of the guaranteed exposure; *(L.N. 167 of 2023)*

(d) the undertaking of the guarantor to make payment in specified circumstances relating to the guaranteed exposure is clearly documented so that the extent of the credit protection provided by the guarantee is clearly defined;

(e) there is no clause in the guarantee, the satisfaction of which is outside the direct control of the institution, which would allow the guarantor to cancel the guarantee unilaterally or which would increase the effective cost of the credit protection provided by the guarantee as a result of the deteriorating credit quality of the guaranteed exposure except for a clause permitting termination in the event of a failure by the institution to pay sums due from it under the terms of the guarantee;

(f) there is no clause in the guarantee, the satisfaction of which is outside the direct control of the institution, which could operate to prevent the guarantor from being obliged to pay out promptly in the event that the obligor in respect of the guaranteed exposure defaults in making any payments due to the institution in respect of the guaranteed exposure;

(g) the jurisdiction in which the guarantor is located and from which the guarantor may be obliged to make payment has no existing exchange controls in place or, if there are existing exchange controls in place, approval has been obtained for the funds to be remitted freely in the event that the guarantor is called on under the terms of the guarantee to make payment to the institution; *(L.N. 167 of 2023)*

(h) the guarantor has no recourse to the institution for any losses suffered as a result of the guarantor being obliged to make any payment to the institution pursuant to the guarantee;

(i) the institution has the right to receive payment from the guarantor without having to take legal action in order to pursue the obligor in respect of the guaranteed exposure for payment; and

(j) the guarantee is binding on all parties and legally enforceable in all relevant jurisdictions.

99. Recognized credit derivative contracts

(1) Subject to subsections (2), (3), (4) and (5), a credit derivative contract (***subject contract***) entered into by an authorized institution as a protection buyer may be recognized for the purpose of calculating the risk-weighted amount of an exposure of the institution (***protected exposure***) if—

(a) the subject contract is a credit default swap or total return swap (other than a restricted credit derivative contract);

(b) the protection seller of the subject contract is an eligible credit protection provider described in section 99A;

(c) the economic benefit derived by the institution would make good the economic loss suffered by the institution in consequence of the default of the obligor in respect of the protected exposure in a manner substantially similar to that of a recognized guarantee;

(d) the subject contract gives the institution a direct claim against the protection seller;

(e) the credit protection provided by the subject contract relates to a specific exposure or a specific pool of exposures;

(f) the credit quality of the reference entity of the subject contract does not have material positive correlation with—

(i) the credit quality of the protection seller; and

(ii) the residual risks (including legal, operational, liquidity and market risks) arising from the use of the subject contract for the purpose of mitigating the credit risk of the protected exposure;

(g) the undertaking of the protection seller under the subject contract to make payment in specified circumstances is clearly documented so that the extent of the credit protection provided by the subject contract is clearly defined;

(h) there is no clause in the subject contract, the satisfaction of which is outside the direct control of the institution, that would—

(i) allow the protection seller to cancel the subject contract unilaterally; or

(ii) increase the effective cost of the credit protection offered by the subject contract as a result of the deteriorating credit quality of the reference entity or any of the specified obligations of the subject contract,

except for a clause permitting termination in the event of a failure by the institution to pay sums due from it under the terms of the subject contract;

(i) there is no clause in the subject contract, the satisfaction of which is outside the direct control of the institution, that could operate to prevent the protection seller from being obliged to pay out promptly in the event that the reference entity defaults in making any payments due;

(j) the jurisdiction in which the protection seller is located and from which the protection seller may be obliged to make payment has no existing exchange controls in place or, if there are existing exchange controls in place, approval has been obtained for the funds to be remitted freely in the event that the protection seller is called on under the terms of the subject contract to make payment to the institution;

(k) the protection seller has no recourse to the institution for any losses suffered as a result of the protection seller being obliged to make any payment to the institution under the subject contract;

(l) the subject contract obliges the protection seller to make payment to the institution in the following credit events—

(i) any failure by the reference entity to pay amounts due under the terms of any of the specified obligations (subject to any grace period in the subject contract that is of substantially similar duration to any grace period provided for in the terms of the specified obligations);

(ii) the bankruptcy or insolvency of the reference entity, or the reference entity's failure or inability to pay its debts as they fall due, or the reference entity's written admission of the reference entity's inability generally to pay its debts as they fall due, or any event with respect to the reference entity that has an analogous effect to any of the foregoing events; or

(iii) restructuring of any of the specified obligations, involving forgiveness or postponement of payment of any principal or interest or fees, that results in the holder of the specified obligation restructured making specific provision or other similar debit to its profit and loss account;

(m) in any case where any of the specified obligations provides a grace period within which the reference entity may make good a default in payment, the subject contract is not capable of terminating prior to the expiry of the grace period;

(n) in any case where the subject contract provides for settlement in cash, it provides an adequate mechanism for valuation of loss and specifies a reasonable period within which that valuation is to be arrived at following a credit event;

(o) in any case where the specified obligations do not include or are different from the protected exposure—

(i) each of the specified obligations ranks for payment or repayment equally with, or junior to, the protected exposure; and

(ii) the obligor in respect of the protected exposure is the same person as the reference entity of the subject contract and legally enforceable cross default or cross acceleration clauses are included in the terms of both the protected exposure and the specified obligations;

(p) in any case where, under the terms of the subject contract, it is a condition of settlement that the institution transfers the protected exposure to the protection seller, the terms of the protected exposure provide that any consent which may be required from the obligor in respect of the protected exposure must not be unreasonably withheld;

(q) the subject contract specifies clearly the identity of the person who is empowered to determine whether a credit event has occurred, that person is not solely the protection seller and the institution is, under the terms of the subject contract, entitled to inform the protection seller of the occurrence of a credit event; and

(r) the subject contract is binding on all parties and legally enforceable in all relevant jurisdictions.

(2) If all the criteria set out in subsection (1) are met in respect of the subject contract except that the credit events specified in the subject contract do not include the credit event described in subsection (1)(l)(iii), the subject contract may be recognized for the purpose of calculating the risk-weighted amount of the protected exposure if all of the following conditions are met—

(a) the protected exposure is an exposure to a corporate;

(b) unanimous consent of all creditors in respect of the protected exposure is required to amend the maturity, principal, coupon, currency or seniority status of the protected exposure;

(c) the legal domicile in which the protected exposure is governed has well-established legislation on insolvency, bankruptcy or liquidation that—

(i) allows for a corporate to reorganize or restructure; and

(ii) provides for an orderly settlement of creditor claims.

(3) If—

(a) all the criteria set out in subsection (1) are met in respect of the subject contract except that the credit events specified in the subject contract do not include the credit event described in subsection (1)(l)(iii);

(b) any one or more of the conditions set out in subsection (2) are not met in respect of the subject contract; and

(c) the maximum liability of the protection seller to the authorized institution under the subject contract is more than the amount of the protected exposure,

the amount of the subject contract that may be recognized for the purpose of calculating the risk-weighted amount of the protected exposure must not be more than 60% of the amount of the protected exposure.

(4) If—

(a) all the criteria set out in subsection (1) are met in respect of the subject contract except that the credit events specified in the subject contract do not include the credit event described in subsection (1)(l)(iii);

(b) any one or more of the conditions set out in subsection (2) are not met in respect of the subject contract; and

(c) the maximum liability of the protection seller to the authorized institution under the subject contract is equal to or less than the amount of the protected exposure,

the amount of the subject contract that may be recognized for the purpose of calculating the risk-weighted amount of the protected exposure must not be more than 60% of the maximum liability of the protection seller to the institution under the subject contract.

(5) If the subject contract is a credit derivative contract embedded in a cash funded credit-linked note issued by the authorized institution, the subject contract is recognized for the purpose of calculating the risk-weighted amount of the protected exposure if all the criteria set out in subsection (1), excluding the criterion set out in subsection (1)(b), are met.

(6) In this section—

restricted credit derivative contract (受限制信用衍生工具合約), in relation to an authorized institution, means—

(a) a total return swap where—

(i) the institution is the protection buyer under the swap; and

(ii) the institution records the net payments received by it under the swap as net income but does not record, through deductions in fair value in the accounts of the institution or by an addition to reserves or provisions, the extent to which the value of the protected exposure has deteriorated; or

(b) a first-to-default credit derivative contract, a second-to-default credit derivative contract or any other n^{th}-to-default credit derivative contract;

specified obligation (指明義務), in relation to a credit derivative contract entered into by an authorized institution as a protection buyer in respect of an exposure of the institution—

(a) means an obligation of a specified reference entity specified in the credit derivative contract that is—

(i) a reference obligation; or

(ii) an obligation used for the purpose of determining whether a credit event has occurred; and

(b) may or may not include the exposure of the institution.

(L.N. 167 of 2023)

99A. Eligible credit protection providers

(1) For the purposes of sections 98 and 99, an entity that provides credit protection is an eligible credit protection provider if the conditions set out in subsection (2)(a) and (b) are met.

(2) The conditions are—

(a) the entity is—

(i) a sovereign;

(ii) a public sector entity;

(iii) a multilateral development bank;

(iv) an unspecified multilateral body;

(v) a bank;

(vi) a qualifying CCP;

(vii) a prudentially regulated financial institution; or

(viii) an entity not listed in subparagraphs (i) to (vii) that has an ECAI issuer rating; and

(b) the attributed risk-weight of the entity is lower than the risk-weight that would be allocated to the exposure in respect of which the credit protection is provided.

(3) In this section—

prudentially regulated financial institution (受審慎監管的金融機構) means—

(a) a qualifying non-bank financial institution other than a qualifying CCP;

(b) an entity (other than a bank, qualifying non-bank financial institution or qualifying CCP) that is—

(i) authorized by a regulator under the law of a jurisdiction to carry on financial activities in that jurisdiction; and

(ii) subject to supervisory standards imposed by the regulator that are substantially consistent with international norms; or

(c) an entity that is a member of a group of companies (comprised of the ultimate holding company and all of its subsidiaries) where any major entity in the group is a bank or falls within paragraph (a) or (b).

(L.N. 167 of 2023)

99B. Recognized internal risk transfer to trading book

(1) Subject to subsection (3), an internal risk transfer used by an authorized institution to transfer the credit risk of one or more credit exposures (***protected credit exposure***) booked

in the institution's banking book to its trading book may be recognized for the purpose of calculating the risk-weighted amount of the protected credit exposure under this Part if there is an external hedge that meets all the conditions specified in subsection (2)(a) or (b).

(2) The conditions are—

(a) the external hedge in respect of the protected credit exposure—

(i) is in the form of a credit derivative contract entered into by the institution with a third party and booked in the institution's trading book;

(ii) exactly matches the internal risk transfer; and

(iii) meets the requirements set out in section 99(1)(a), (b), (c), (l), (m), (n), (o), (p), (q) and (r); or

(b) all of the following apply—

(i) the external hedge in respect of the protected credit exposure is made up of multiple credit derivative contracts entered into by the institution with one or more third parties (***aggregate external hedge***) and booked in the institution's trading book;

(ii) each of those credit derivative contracts meets the requirements set out in section 99(1)(a), (b), (c), (l), (m), (n), (o), (p), (q) and (r);

(iii) the aggregate external hedge exactly matches the internal risk transfer;

(iv) the internal risk transfer exactly matches the aggregate external hedge.

(3) For the purposes of subsection (1), if the external hedge meets the conditions specified in subsection (2)(a) or (b) except that the credit events specified in the external hedge do not include the credit event described in section 99(1)(l)(iii)—

(a) in cases where the amount of the internal risk transfer is more than the amount of the protected credit exposure—the amount of the internal risk transfer that may be recognized for the purpose of calculating the risk-weighted amount of the protected credit exposure must not be more than 60% of the amount of the protected credit exposure; or

(b) in cases where the amount of the internal risk transfer is equal to or less than the amount of the protected credit exposure—only up to 60% of the amount of the internal risk transfer may be recognized for the purpose of calculating the risk-weighted amount of the protected credit exposure.

(4) In this section—

internal risk transfer (內部風險轉移) means an internal written record of a transfer of credit risk from an authorized institution's banking book to its trading book.

(L.N. 167 of 2023)

100. Capital treatment of recognized guarantees and recognized credit derivative contracts

(1) If an exposure is covered by a recognized guarantee or recognized credit derivative contract (***protected exposure***)—

(a) in the case of a recognized guarantee or a recognized credit derivative contract recognized under section 99—an authorized institution must calculate the risk-weighted amount of the protected exposure in accordance with subsection (2); and

(b) in the case of a recognized credit derivative contract in the form of an internal risk transfer recognized under section 99B—

(i) an authorized institution is not required to calculate a risk-weighted amount under this Part for the credit protection covered portion of the protected exposure if capital charges are held by the institution for the trading book leg of the internal risk transfer and the corresponding external hedge in accordance with the requirements of Part 8; and

(ii) if there is any credit protection uncovered portion, the institution must calculate the risk-weighted amount of the unprotected amount of the protected exposure in accordance with subsection (2).

(2) If the credit protection covered portion and the credit protection uncovered portion of a protected exposure rank equally—

(a) sections 83, 84 and 85, with all necessary modifications, apply to the authorized institution in relation to the calculation of the risk-weighted amount of the protected exposure; and

(b) the authorized institution must—

(i) subject to subsections (5), (6) and (7), allocate to the protected amount of the protected exposure the risk-weight determined in accordance with Division 3 by regarding the protected amount as an exposure of the institution to the credit protection provider; and

(ii) allocate to the unprotected amount of the protected exposure the risk-weight attributable to the protected exposure under that Division.

(3) For the purposes of subsection (2)—

(a) if section 83 or 85 applies to the authorized institution—

(i) subject to subsection (4), the protected amount of the protected exposure is the credit protection covered portion of the protected exposure; and

(ii) the unprotected amount of the protected exposure is the credit protection uncovered portion of the protected exposure; and

(b) if section 84 applies to the authorized institution—

(i) subject to subsection (4), the protected amount of the protected exposure is the product of the credit protection covered portion of the protected exposure and the CCF applicable to the protected exposure; and

(ii) the unprotected amount of the protected exposure is the product of the credit protection uncovered portion of the protected exposure and the CCF applicable to the protected exposure.

(4) If, in respect of a protected exposure, there is a currency mismatch, an authorized institution, in determining the credit protection covered portion for the purposes of subsection (1)(b) or the protected amount for the purposes of subsection (2), must adjust the amount of the credit protection covered portion of the protected exposure by the use of Formula 11.

Formula 11

Calculation of Amount of Credit Protection Covered Portion if there is a Currency Mismatch

$$G_a = G \times (1 - H_{fx})$$

where—

(a) G_a is the credit protection covered portion adjusted for a currency mismatch;

(b) G is the credit protection covered portion before adjustment for a currency mismatch; and

(c) H_{fx} is the haircut applicable in consequence of a currency mismatch in accordance with the standard supervisory haircuts subject to adjustment as set out in section 92.

(5) If—

(a) section 56(1) or (2) applies to domestic currency exposures to a sovereign; and

(b) a protected exposure—

(i) is funded in the local currency of that sovereign; and

(ii) is the subject of a recognized guarantee by that sovereign denominated in the local currency,

an authorized institution may allocate the lower risk-weight provided for by section 56(1) or (2), as the case requires, to the protected amount of the protected exposure.

(6) If the credit protection covered portion of a protected exposure is such a credit protection covered portion because of a recognized guarantee (***original guarantee***) and is the subject of a counter-guarantee given by a sovereign, an authorized institution may, in respect of the credit protection covered portion, treat the counter-guarantee as if it were the original guarantee if—

(a) the counter-guarantee covers all credit risk elements of the protected exposure to the extent that it relates to the credit protection covered portion;

(b) the counter-guarantee is given in such terms that it can be called if—

(i) for any reason the obligor in respect of the protected exposure fails to make payments due in respect of the protected exposure; and

(ii) the original guarantee could be called;

(c) the counter-guarantee meets all of the requirements for guarantees set out in section 98 (except that the counter-guarantee need not meet the requirements set out in section 98(b) and (c)); and

(d) the institution reasonably considers, and demonstrates to the satisfaction of the Monetary Authority, that—

(i) the cover of the counter-guarantee is adequate and effective; and

(ii) there is no evidence to suggest that the coverage of the counter-guarantee is less effective than that of a direct and explicit guarantee by the sovereign that gives the counter-guarantee.

(7) If a recognized credit derivative contract is cleared by a qualifying CCP, an authorized institution may allocate to the protected amount of the protected exposure to which the contract relates—

(a) a risk-weight of 2% if—

(i) the institution is a clearing member of the qualifying CCP;

(ii) the institution is a direct client of a clearing member of the qualifying CCP and all of the conditions set out in section 226ZA(6) are met; or

(iii) the institution is an indirect client within a multi-level client structure associated with the qualifying CCP and all of the conditions set out in section

226ZA(6), with all necessary modifications, are met for arrangements among the CCP, clearing member, all clients at levels higher than the institution within the multi-level client structure, and the institution; or

(b) a risk-weight of 4% if—

(i) the institution is a direct client of a clearing member of the qualifying CCP and all of the conditions set out in section 226ZA(6) (excluding the condition set out in section 226ZA(6)(a)(iii)) are met; or

(ii) the institution is an indirect client within a multi-level client structure associated with the qualifying CCP and all of the conditions set out in section 226ZA(6) (excluding the condition set out in section 226ZA(6)(a)(iii)), with all necessary modifications, are met for arrangements among the CCP, clearing member, all clients at levels higher than the institution within the multi-level client structure, and the institution.

(L.N. 167 of 2023)

101. Provisions supplementary to section 100

(1) Subject to subsection (9) and section 99(2), (3) and (4), if the credit protection in respect of an authorized institution's exposure consists of a recognized credit derivative contract which is a credit default swap or total return swap— *(L.N. 167 of 2023)*

(a) if upon the happening of a credit event the protection seller is obliged to pay the amount specified in the contract to the institution in exchange for delivery by the institution of the deliverable obligation specified in the contract, the institution may treat the exposure as being fully covered;

(b) if upon the happening of a credit event the protection seller is obliged to pay the amount specified in the contract to the institution less the market value of the reference obligation specified in the contract, calculated by specified calculation agents at some specified point in time after the credit event has occurred, the institution may treat the exposure as being fully covered; and

(c) if upon the happening of a credit event the protection seller is obliged to pay a fixed amount to the institution, the institution may only treat that amount of the exposure which is equivalent to the fixed amount as being fully covered.

(2)-(6) *(Repealed L.N. 167 of 2023)*

(6A) *(Repealed L.N. 167 of 2023)*

(7) If an authorized institution has obtained tranched credit protection for its exposure, it must—

(a) decompose the exposure into a protected sub-tranche and an unprotected sub-tranche; and

(b) determine the risk-weighted amount of the exposure in accordance with Part 7. *(L.N. 175 of 2017)*

(8) Subject to subsection (9), if the credit protection in respect of an authorized institution's exposure takes the form of an issue of credit-linked notes by the institution, the institution— *(L.N. 167 of 2023)*

(a) may only treat that amount of the exposure which is equivalent to the cash funding received from the notes as being fully covered; and

(b) must treat the credit protection covered portion of the exposure as an exposure collateralized by cash deposit. *(L.N. 156 of 2012; L.N. 167 of 2023)*

(c) *(Repealed L.N. 167 of 2023)*

(9) If the credit protection in respect of an authorized institution's exposure consists of a recognized credit derivative contract (including such a contract embedded in credit-linked notes issued by the institution) that provides that, on the happening of a credit event, the protection seller is not obliged to make a payment in respect of any loss or to absorb any loss if the loss is below a specified amount (***materiality threshold***), the institution must, in calculating its capital adequacy ratio, allocate a risk-weight of 1 250% to the portion of the exposure that is below the materiality threshold. *(L.N. 167 of 2023)*

Division 10—Multiple Recognized Credit Risk Mitigation and Maturity Mismatches

102. Multiple recognized credit risk mitigation

(1) Where in respect of a single exposure of an authorized institution to an obligor, 2 or more forms of recognized credit risk mitigation have been used by the institution, the institution shall calculate the risk-weighted amount of the exposure in accordance with this Part by dividing the exposure into the portions which respectively represent the proportions of the exposure covered by each of the forms of recognized credit risk mitigation so used. *(L.N. 167 of 2023)*

(2) Where in respect of a single exposure of an authorized institution to an obligor, there is an overlap of coverage between 2 or more forms of recognized credit risk mitigation used by the institution, the institution may select, in respect of the portion of the exposure covered by the overlap, the

recognized credit risk mitigation which result in the lowest risk-weighted amount of that portion of the exposure covered by the overlap.

(3) Where an authorized institution has an exposure to an obligor in respect of which credit protection has been provided by a single credit protection provider in circumstances where the relevant credit protection has different maturities, the institution shall calculate the risk-weighted amount of the exposure in accordance with this Part by dividing the exposure into different portions reflecting the maturity of the credit protection respectively attributable to the different portions. *(L.N. 167 of 2023)*

(4) Where an authorized institution has an exposure to an obligor in the form of a general banking facility consisting of 2 or more credit lines—

(a) the institution may, in calculating its risk-weighted amount in respect of the credit lines, allocate any credit protection taken in respect of the exposure amongst the individual exposures under each of the credit lines; and

(b) if the institution exercises its discretion under paragraph (a), the institution shall aggregate the risk-weighted amounts of the individual exposures under each of the credit lines to determine the total risk-weighted amount of the exposure in respect of the general banking facility.

103. Maturity mismatches

(1) Where the credit protection provided in respect of an exposure of an authorized institution (other than the netting of SFTs and derivative contracts) has a residual maturity which is shorter than the residual maturity of the exposure (referred to in this section as ***maturity mismatch***), the institution shall adjust the value of the credit protection by the use of Formula 12. *(L.N. 44 of 2020)*

Formula 12

Adjustment of Calculation of Value of Credit Protection where there is Maturity Mismatch

$$P_a = P \times (t - 0.25) / (T - 0.25)$$

where—

P_a = value of credit protection adjusted for maturity mismatch;

P = value of credit protection adjusted by standard supervisory haircuts (subject to adjustment as set out in section 92) for volatility of value of collateral and currency mismatch (if applicable); *(L.N. 44 of 2020)*

t = Min (T, residual maturity of credit protection) expressed in years; and

T = Min (5, residual maturity of the exposure) expressed in years.

(2) Where there is a maturity mismatch, the institution, in calculating its risk-weighted amount of the exposure—

(a) shall take into account the credit protection only if the credit protection has an original maturity of not less than one year;

(b) shall not take into account the credit protection once it has a residual maturity of not more than 3 months; and

(c) shall not take into account the credit protection if the credit protection is in the form of recognized collateral and the risk-weighted amount of the exposure is calculated by using the simple approach to the treatment of recognized collateral.

(3) For the purposes of calculating the respective maturities of an exposure of an authorized institution and any credit protection covering the exposure—

(a) the institution shall, at any time before the obligor in respect of the exposure to which the credit protection relates performs the obligor's obligations, take the effective maturity of the exposure to be the longest possible remaining time after taking into account any applicable grace period provided for in the terms of the exposure;

(b) if the terms of the credit protection provide for an option which may reduce the term of that credit protection, the institution shall take into account the option and the earliest possible date upon which it may be exercised;

(c) if the terms of the credit protection provide that the credit protection provider may terminate the credit protection before its maturity, the institution shall take the maturity of the credit protection to be the first date upon which the credit protection provider may so terminate the credit protection; and

(d) if the terms of the credit protection permit the institution to terminate the credit protection before its maturity and there is a positive incentive for the institution to exercise its discretion so to do, the institution shall take the maturity of the credit protection to be the time left to run before the earliest date upon which the institution may exercise the discretion.

(4) For the purposes of this section, the original maturity and residual maturity of credit protection which is recognized collateral falling within section 79(1)(a), (d), (m) or (n) or 80(1)(b) or (c) shall be taken to be the period for which it will continue to fulfil the requirements of section 77 applicable to the credit protection. *(L.N. 156 of 2012)*

(L.N. 167 of 2023)

Part 5

Calculation of Credit Risk for Non-securitization Exposures: BSC Approach

Division 1—General

104. Application of Part 5

(1) This Part applies to an authorized institution which uses the BSC approach to calculate its credit risk for non-securitization exposures.

(2) A reference to an authorized institution in this Part is a reference to an authorized institution which uses the BSC approach to calculate its credit risk for non-securitization exposures. *(L.N. 167 of 2023)*

105. Interpretation of Part 5

In this Part— *(L.N. 167 of 2023)*

ADC exposure (ADC風險承擔) has the meaning given by section 51(1); *(L.N. 167 of 2023)*

attributed risk-weight (歸屬風險權重)—

(a) in relation to a person (however described), subject to paragraph (b), means the risk-weight that would be attributable, in accordance with Subdivision 2 or 5 of Division 3, to an unsecured exposure to the person as an obligor on the following assumptions—

(i) that the unsecured exposure is a loan granted to the person;

(ii) that the residual maturity of the loan is not less than one year;

(iii) that the loan is not a domestic currency exposure;

(b) in sections 132, 133 and 134—

(i) in relation to the credit protection provider of a credit protection afforded to an exposure (other than a real estate exposure), means the risk-weight that would be attributable, in accordance with Division 3, to the exposure as if the credit protection provider were the obligor in respect of the exposure; and

(ii) in relation to the credit protection provider of a credit protection afforded to a real estate exposure, means the risk-weight that would be attributable, in accordance with that Division, to a senior and unsecured exposure to the credit protection provider; *(L.N. 167 of 2023)*

commitment (承諾), in relation to the determination of a CCF applicable to an off-balance sheet exposure, has the meaning given by section 2 of Schedule 6; *(L.N. 167 of 2023)*

corporate (法團) means—

(a) a company; or

(b) a partnership or any other unincorporated body,

that is not a multilateral development bank, unspecified multilateral body, public sector entity or bank; *(L.N. 167 of 2023)*

credit equivalent amount (信貸等值數額), in relation to an off-balance sheet exposure that is not a default risk exposure, means the credit equivalent amount of the exposure calculated in accordance with section 118(1) or (2), as the case requires; *(L.N. 44 of 2020; L.N. 167 of 2023)*

credit protection covered portion (信用保障涵蓋部分), in relation to an exposure of an authorized institution that is covered by recognized collateral, a recognized guarantee or a recognized credit derivative contract, means the portion of the exposure (which may be all of the exposure) that is covered by—

(a) in the case of recognized collateral—the current market value of the recognized collateral;

(b) in the case of a recognized guarantee or a credit derivative contract recognized under section 133(1) or (2)—the maximum liability of the credit protection provider to the institution under the recognized guarantee or recognized credit derivative contract, as the case may be; or

(c) in the case of a credit derivative contract recognized under section 133(3) or (4)—the maximum liability of the credit protection provider to the institution under the recognized credit derivative contract, up to the maximum amount of the contract that may be recognized under that section; *(L.N. 167 of 2023)*

credit protection uncovered portion (不受信用保障涵蓋部分), in relation to an exposure of an authorized institution that is covered by recognized collateral, a recognized guarantee or a recognized credit derivative contract, means the portion of the exposure that is not the credit protection covered portion; *(L.N. 167 of 2023)*

debt securities (債務證券) means any securities other than shares, stocks or import or export trade bills;

equity exposure (股權風險承擔) means an exposure that falls within section 54A; *(L.N. 167 of 2023)*

exposure (風險承擔), in relation to an authorized institution, means a credit exposure (including an asset) of the institution;

exposure amount (風險承擔數額)—

(a) in relation to an on-balance sheet exposure—means the principal amount of the exposure (net of specific provisions, if any);

(b) in relation to an off-balance sheet exposure to a counterparty that is a default risk exposure in respect of one or more derivative contracts or in respect of a netting set that contains both derivative contracts and SFTs—means the outstanding default risk exposure in respect of the counterparty (net of specific provisions, if any);

(c) in relation to an off-balance sheet exposure to a counterparty that is a default risk exposure in respect of one or more SFTs—means the amount of the exposure calculated in accordance with Division 2B of Part 6A (net of specific provisions, if any); or

(d) in relation to any other off-balance sheet exposure, means—

(i) the credit equivalent amount of the exposure calculated in accordance with section 118(1); or

(ii) the credit equivalent amount of the exposure calculated in accordance with section 118(2); *(L.N. 167 of 2023)*

principal amount (本金額)—

(a) in relation to an on-balance sheet exposure of an authorized institution—

(i) if the exposure is measured at fair value, means the value of the exposure determined in accordance with section 4A; or

(ii) if the exposure is not measured at fair value, means the book value (including accrued interest) of the exposure; or *(L.N. 137 of 2011)*

(b) in relation to an off-balance sheet exposure of an authorized institution, means—

(i) subject to subparagraph (ii), in the case of an exposure listed in Schedule 6, the contracted amount of the exposure; *(L.N. 44 of 2020; L.N. 167 of 2023)*

(ii) in the case of an exposure listed in Schedule 6 that arises from an undrawn facility or the undrawn portion of a partially drawn facility, the amount of the undrawn commitment; *(L.N. 175 of 2017; L.N. 44 of 2020; L.N. 167 of 2023)*

(iii) subject to subparagraph (iv), in the case of an exposure in respect of a derivative contract, the notional amount of the contract; *(L.N. 44 of 2020)*

(iv) in the case of an exposure in respect of a derivative contract where the stated notional amount of the contract is leveraged or enhanced by the structure of the contract, the effective notional amount of the contract calculated by taking into account the effect of the leverage or enhancement, as the case requires; *(L.N. 44 of 2020)*

(v) in the case of an exposure to a person arising from the person holding collateral posted by the institution in a manner that is not bankruptcy remote from the person, the fair value of the collateral; *(L.N. 156 of 2012)*

real estate exposure (地產風險承擔) has the meaning given by section 51(1); *(L.N. 167 of 2023)*

recognized collateral (認可抵押品) means collateral recognized under section 124;

recognized credit derivative contract (認可信用衍生工具合約) means—

(a) a credit derivative contract recognized under section 133(1), (2) or (5); or

(b) a credit derivative contract to the extent that it is recognized under section 133(3) or (4); *(L.N. 167 of 2023)*

recognized guarantee (認可擔保) means a guarantee recognized under section 132;

regulatory residential real estate exposure (監管住宅地產風險承擔)—see section 115(1); *(L.N. 167 of 2023)*

specific provisions (特定準備金) has the meaning given by section 51(1); *(L.N. 167 of 2023)*

subordinated debt (後償債項), in relation to an obligor that is a bank or corporate—

(a) includes a subordinated debt or junior subordinated debt—

(i) that is not an equity exposure to the obligor; and

(ii) that is higher in ranking, or senior, to equity exposures to the obligor in terms of the priority of repayment; but

(b) if the obligor is a financial sector entity, excludes—

(i) a capital instrument issued by the obligor; and

(ii) a non-capital LAC liability of the obligor; *(L.N. 167 of 2023)*

Tier 2 country (第2級國家) means any country which is not a Tier 1 country.

(L.N. 44 of 2020; L.N. 167 of 2023)

Division 2—Calculation of Credit Risk under BSC Approach, Exposures to be Covered in Calculation, and Classification of Exposures

106. Calculation of risk-weighted amount of exposures

(1) Subject to section 107, an authorized institution must calculate an amount representing the degree of credit risk to which it is exposed by aggregating—

(a) the risk-weighted amounts of the institution's on-balance sheet exposures; and

(b) the risk-weighted amounts of the institution's off-balance sheet exposures.

(2) Subject to subsection (4), for the purposes of subsection (1)—

(a) the risk-weighted amount of each exposure (except CIS exposure and default risk exposure in respect of derivative contracts or SFTs) must be calculated by multiplying the exposure amount of the exposure by the relevant risk-weight attributable to the exposure determined under Division 3;

(b) the risk-weighted amount of each CIS exposure must be calculated in accordance with Division 3A; and

(c) the risk-weighted amount of each default risk exposure in respect of derivative contracts or SFTs is the amount specified in subsection (3).

(3) If an authorized institution—

(a) has an IMM(CCR) approval—

(i) the risk-weighted amount of the default risk exposure in respect of derivative contracts or SFTs covered by the IMM(CCR) approval is the IMM(CCR) risk-weighted amount;

(ii) the risk-weighted amount of the default risk exposure in respect of derivative contracts that are not covered by the IMM(CCR) approval or that fall within section 10B(5) or (7) is the sum of the

SA-CCR risk-weighted amounts calculated for the contracts; and

(iii) the risk-weighted amount of the default risk exposure in respect of SFTs that are not covered by the IMM(CCR) approval or that fall within that section is the sum of the SFT risk-weighted amounts calculated for the SFTs;

(b) does not have an IMM(CCR) approval for any of its derivative contracts or SFTs—

(i) the risk-weighted amount of the default risk exposure in respect of derivative contracts is—

(A) if the institution uses the current exposure method to calculate default risk exposures in respect of derivative contracts—the sum of the CEM risk-weighted amounts calculated for the contracts; or

(B) if the institution uses the SA-CCR approach to calculate default risk exposures in respect of derivative contracts—the sum of the SA-CCR risk-weighted amounts calculated for the contracts; and

(ii) the risk-weighted amount of the default risk exposure in respect of SFTs is the sum of the SFT risk-weighted amounts calculated for the SFTs.

(4) An authorized institution may reduce the risk-weighted amount of its exposure by taking into account the effect of any recognized credit risk mitigation in respect of the exposure in the manner set out in Divisions 5, 6, 7 and 8, unless—

(a) the institution has made disclosures in respect of credit risk for the immediately preceding applicable reporting periods that do not fully comply with the applicable provisions of the Disclosure Rules; or

(b) subsection (5) or (6) applies to the recognized credit risk mitigation concerned.

(5) If an authorized institution has bought credit protection for an exposure and the credit protection is in the form of a single-name credit default swap that falls within section 226J(1), the institution must not take into account under subsection (4) the credit risk mitigating effect of the swap.

(6) If an exposure of an authorized institution is a default risk exposure in respect of derivative contracts or SFTs, the institution must not take into account under subsection (4) the effect of any recognized credit risk mitigation applicable to the exposure that has already been taken into account in the calculation of the amount of the default risk exposure under Part 6A.

(7) In this section—

applicable provisions (適用條文), in relation to an authorized institution that uses the BSC approach to calculate the credit risk for all of its non-securitization exposures, means the provisions set out in Division 4 of Part 2A of the Disclosure Rules the application of which to the institution has not been exempted by the Monetary Authority under section 3 of those Rules;

applicable reporting period (適用報告期), in relation to an applicable provision, means the reporting period (within the meaning of the Disclosure Rules) referred to in that applicable provision;

CEM risk-weighted amount (CEM風險加權數額) means the risk-weighted amount of the default risk exposure in respect of a derivative contract calculated as the product of—

(a) the exposure amount of the default risk exposure calculated by using the current exposure method; and

(b) the risk-weight applicable to the default risk exposure determined under this Part;

Disclosure Rules (《披露規則》) means the Banking (Disclosure) Rules (Cap. 155 sub. leg. M);

SFT risk-weighted amount (SFT風險加權數額) means the risk-weighted amount of the default risk exposure in respect of an SFT calculated in accordance with section 129.

(L.N. 167 of 2023)

107. On-balance sheet exposures and off-balance sheet exposures to be covered

(1) Subject to subsection (2), if an authorized institution is required under these Rules to use only the BSC approach to calculate the credit risk for all of its non-securitization exposures, the institution must, for the purpose of calculating under section 106 an amount representing the degree of credit risk to which it is exposed, take into account and risk-weight—

(a) all of the institution's on-balance sheet exposures and off-balance sheet exposures booked in its banking book;

(b) all of the institution's following exposures—

(i) default risk exposures to counterparties in respect of derivative contracts or SFTs booked in its trading book;

(ii) credit exposures to counterparties in respect of transactions (other than repo-style transactions) in securities, foreign exchange or commodities booked in its trading book that remain outstanding after the settlement dates in respect of the transactions;

(iii) credit exposures to counterparties in respect of unsegregated collateral posted by it and held by the counterparties for transactions or contracts booked in its trading book; and

(c) if applicable, all of the institution's market risk exposures that are exempted from section 17 under section 22, except for its total net open position in foreign exchange exposures as derived in accordance with section 296.

(2) Subsection (1) does not apply to—

(a) securitization exposures;

(b) the underlying exposures of eligible traditional securitization transactions (within the meaning of section 229) if the authorized institution opts to apply the treatment under section 230(1) to the underlying exposures;

(c) default fund contributions made to qualifying CCPs and non-qualifying CCPs (within the meaning of section 226V(1));

(d) default risk exposures to qualifying CCPs;

(e) exposures that are risk-weighted as if they were default risk exposures to qualifying CCPs under Division 4 of Part 6A; and

(f) any portion of an exposure (which may be all of the exposure) that is required to be deducted from any of the institution's CET1 capital, Additional Tier 1 capital and Tier 2 capital under Division 4 of Part 3.

(L.N. 167 of 2023)

108. Classification of exposures

(1) An authorized institution must classify its on-balance sheet exposures and off-balance sheet exposures into one only of the following categories—

(a) exposures that are not CIS exposures;

(b) CIS exposures.

(2) An authorized institution must—

(a) further classify each of the exposures falling within subsection (1)(a), according to the obligor or the nature of the exposure, into one only of the following subcategories—

(i) exposures that do not fall within subparagraph (ii), (iii), (iv), (v), (vi) or (vii)—

(A) sovereign exposures;

(B) public sector entity exposures;

(C) multilateral development bank exposures;

(D) unspecified multilateral body exposures;

(E) bank exposures (other than eligible covered bond exposures);

(F) eligible covered bond exposures;

(G) exposures falling within section 113A;

(H) real estate exposures;

(ii) equity exposures (other than those falling within subparagraph (iii) or (iv));

(iii) significant capital investments in commercial entities within the meaning of section 115F(2);

(iv) holdings of capital instruments issued by, and non-capital LAC liabilities of, financial sector entities;

(v) subordinated debts issued by banks and corporates;

(vi) cash and gold;

(vii) items in the process of clearing or settlement; and

(b) classify each of the exposures falling within subsection (1)(a) that does not fall within paragraph (a) as other exposures.

(3) An authorized institution must—

(a) determine the risk-weight attributable to each of the exposures falling within subsection (1)(a) in accordance with Division 3; and

(b) determine the risk-weight attributable to each of the exposures falling within subsection (1)(b) in accordance with Division 3A.

(L.N. 167 of 2023)

Division 3—Determination of Risk-weights Applicable to Exposures other than CIS Exposures

(L.N. 54 of 2022; L.N. 167 of 2023)

Subdivision 1—Application of Division 3

(L.N. 54 of 2022; L.N. 167 of 2023)

108A. Application of Division 3

This Division applies to the determination of risk-weights applicable to on-balance sheet exposures, and off-balance sheet exposures, that are not CIS exposures.

(L.N. 167 of 2023)

Subdivision 2—Exposures not falling within Subdivision 3, 4 or 5

(L.N. 167 of 2023)

109. Sovereign exposures

(1) An authorized institution must allocate a risk-weight to a sovereign exposure in accordance with this section.

(2) An authorized institution must allocate a risk-weight of 0% to the following exposures—

(a) an exposure to a sovereign of a Tier 1 country that arises from a loan granted to the sovereign;

(b) an exposure to a sovereign of a Tier 2 country that—

(i) arises from a loan granted to the sovereign; and

(ii) is a domestic currency exposure;

(c) an exposure to a sovereign that is a relevant international organization.

(3) An authorized institution must allocate a risk-weight of 10% to the following exposures—

(a) an exposure to a sovereign of a Tier 1 country that arises from—

(i) fixed rate debt securities with a residual maturity of less than one year that are issued by the sovereign; or

(ii) floating rate debt securities of any maturity that are issued by the sovereign;

(b) an exposure to a sovereign of a Tier 2 country that—

(i) arises from—

(A) fixed rate debt securities with a residual maturity of less than one year that are issued by the sovereign; or

(B) floating rate debt securities of any maturity that are issued by the sovereign; and

(ii) is a domestic currency exposure.

(4) An authorized institution must allocate a risk-weight of 20% to the following exposures—

(a) an exposure to a sovereign of a Tier 1 country that arises from fixed rate debt securities with a residual maturity of not less than one year that are issued by the sovereign;

(b) an exposure to a sovereign of a Tier 2 country that—

(i) arises from fixed rate debt securities with a residual maturity of not less than one year that are issued by the sovereign; and

(ii) is a domestic currency exposure.

(5) An authorized institution must allocate a risk-weight of 100% to an exposure to a sovereign of a Tier 2 country that does not fall within subsection (2)(b), (3)(b) or (4)(b).

(6) To avoid doubt, for the purposes of this section, an exposure to the Government includes an exposure to the Exchange Fund.

(L.N. 167 of 2023)

110. Public sector entity exposures

An authorized institution must allocate a risk-weight of—

(a) 20% to an exposure to a public sector entity of a Tier 1 country; and

(b) 100% to an exposure to a public sector entity of a Tier 2 country.

(L.N. 167 of 2023)

111. Multilateral development bank exposures

An authorized institution must allocate a risk-weight of 0% to an exposure to a multilateral development bank.

(L.N. 167 of 2023)

112. Unspecified multilateral body exposures

An authorized institution must allocate a risk-weight of 50% to an exposure to an unspecified multilateral body.

(L.N. 167 of 2023)

113. Bank exposures

(1) An authorized institution must allocate a risk-weight of—

(a) 20% to—

(i) an exposure to a bank that falls within paragraph (a) of the definition of ***bank*** in section 2(1);

(ii) an exposure to a bank that falls within paragraph (b) of that definition and that is incorporated in a Tier 1 country; and

(iii) an exposure, with a residual maturity of less than one year, to a bank that falls within paragraph (b) of that definition and that is incorporated in a Tier 2 country; and

(b) 100% to an exposure, with a residual maturity of not less than one year, to a bank that falls within paragraph (b) of that definition and that is incorporated in a Tier 2 country.

(2) This section does not apply to an exposure to a bank that is an eligible covered bond exposure.

(L.N. 167 of 2023)

113A. Exposures arising from IPO financing

(1) This section applies to a credit facility granted by an authorized institution to a corporate or an individual

(***borrower***) if—

(a) the facility is granted by the institution solely for the purpose of financing the borrower's subscription of securities to be listed on The Stock Exchange of Hong Kong Limited through an IPO;

(b) the settlement process of the IPO is conducted on the Fast Interface for New Issuance operated by Hong Kong Securities Clearing Company Limited; and

(c) the money advanced by the institution under the facility is still legally owned and held by, and under the control of, the institution until the settlement of the payment for the securities successfully subscribed.

(2) The institution may allocate a risk-weight of 0% to its exposure arising from the facility during the period between the time the commitment to extend the facility is made by the institution and the time—

(a) payment for the securities successfully subscribed is made by the institution to the receiving bank of the issuer of the securities; or

(b) if the IPO is cancelled before the payment referred to in paragraph (a) is made, the outstanding loan amount under the facility is fully repaid.

(3) *(Repealed L.N. 167 of 2023)*

(L.N. 167 of 2023)

113B. Eligible covered bond exposures

(1) An authorized institution must—

(a) determine the attributed risk-weight of the issuer of an eligible covered bond; and

(b) allocate a risk-weight to an exposure to that eligible covered bond in accordance with Table 13 based on the attributed risk-weight of the issuer determined under paragraph (a).

Table 13

Risk-weights for Eligible Covered Bonds

Column 1	Column 2	Column 3
Item	Attributed risk-weight of issuer	Risk-weight for eligible covered bond exposures
1.	20%	10%
2.	100%	50%

(2) For the purposes of subsection (1), if the issuer of an eligible covered bond is a financial institution other than a bank, an authorized institution may determine the attributed risk-weight of the issuer in a manner as if the issuer were a bank.

(L.N. 167 of 2023)

114. Cash and gold

(1) An authorized institution must allocate a risk-weight of 0% to the following—

(a) notes and coins owned by the institution that are the lawful currency of a jurisdiction and are held by the institution or in transit;

(b) the institution’s holding of certificates of indebtedness issued by the Government for the issue of legal tender notes;

(c) gold bullion held by the institution, or gold bullion held on an allocated basis for the institution by another person, that is backed by gold bullion liabilities.

(2) Gold bullion held on an unallocated basis for an authorized institution by another person that is backed by gold bullion liabilities must be allocated the attributed risk-weight of that person.

(3) Gold bullion held by an authorized institution, or gold bullion held for the institution by another person, that is not backed by gold bullion liabilities must be allocated a risk-weight of 100%.

(L.N. 167 of 2023)

114A. Items in the process of clearing or settlement

(1) An authorized institution must allocate a risk-weight of 0% to the following—

(a) an unsettled clearing item of the institution that is being processed through any interbank clearing system in Hong Kong;

(b) any receivable from a transaction of the institution in securities, foreign exchange or commodities that is not yet due for settlement.

(2) An authorized institution must allocate a risk-weight of 20% to a cheque, draft or other item drawn on another bank—

(a) that is payable to the account of the institution immediately on presentation; and

(b) that is in the process of collection.

(3) In the case of transactions in securities, foreign exchange and commodities that are entered into by an authorized institution on a delivery-versus-payment basis, if any of those transactions is outstanding after the settlement date in respect

of the transaction concerned, the institution must allocate to the positive current exposure incurred by the institution under the transaction a risk-weight of—

(a) 0% if the transaction is outstanding up to and including the 4th business day after the settlement date;

(b) 100% if the transaction remains outstanding from 5 to 15 business days (both days inclusive) after the settlement date;

(c) 625% if the transaction remains outstanding from 16 to 30 business days (both days inclusive) after the settlement date;

(d) 937.5% if the transaction remains outstanding from 31 to 45 business days (both days inclusive) after the settlement date; and

(e) 1 250% if the transaction remains outstanding for 46 or more business days after the settlement date.

(4) In the case of transactions in securities, foreign exchange and commodities that are entered into by an authorized institution on a basis other than a delivery-versus-payment basis, if any of those transactions is outstanding after the settlement date in respect of the transaction concerned, the institution must—

(a) if the transaction remains outstanding up to and including the 4th business day after the settlement date, risk-weight the following items as loans to the counterparty to the transaction—

(i) the amount of payment made, or the current market value of the thing delivered, by the institution under the transaction; and

(ii) any positive current exposure incurred by the institution under the transaction;

(b) if the transaction remains outstanding for 5 or more business days after the settlement date, allocate a risk-weight of 1 250% to—

(i) the amount of payment made, or the current market value of the thing delivered, by the institution under the transaction; and

(ii) any positive current exposure incurred by the institution under the transaction.

(5) Unless otherwise stated in Part 6A, subsections (1)(b), (3) and (4) do not apply to repo-style transactions.

(L.N. 167 of 2023)

Subdivision 3—Real Estate Exposures

(L.N. 167 of 2023)

115. What are regulatory residential real estate exposures

(1) Subject to subsection (3), a real estate exposure (other than an ADC exposure) of an authorized institution to an obligor is a regulatory residential real estate exposure if all of the following criteria are met in respect of the exposure—

(a) the exposure is secured by a residential property that falls within subsection (2)(a) or (b) (***mortgaged property***);

(b) any claim on the mortgaged property is legally enforceable in all relevant jurisdictions;

(c) the collateral agreement and the legal process underpinning any claim on the mortgaged property provide for the institution to realize the value of the mortgaged property within a reasonable time frame;

(d) the exposure is secured by a first legal charge on the mortgaged property or, if the mortgaged property falls within subsection (2)(b), the exposure will be secured by a first legal charge on the residential property after it is fully completed;

(e) the exposure is granted for one or more of the following purposes—

(i) financing the acquisition of the mortgaged property;

(ii) refinancing the acquisition of the mortgaged property;

(iii) cashing out the equity in the mortgaged property;

(f) the institution's underwriting policies with respect to the granting of real estate exposures are adequate and prudent and include—

(i) assessment of the ability of the obligor to repay; and

(ii) if the repayment of the exposure depends materially on the cash flows generated by the mortgaged property—assessment of relevant metrics (such as occupancy rate);

(g) the mortgaged property is valued in a manner consistent with the relevant guidance issued by the Monetary Authority and the value of the mortgaged property does not depend materially on the performance of the obligor;

(h) all the information (including information on the ability of the obligor to repay and on the valuation of the mortgaged property) required at loan origination and for monitoring purposes is properly documented.

(2) Residential property falls within this subsection if the property is—

(a) a fully-completed residential property; or

(b) a residential property under construction or land on which a residential property will be constructed where—

(i) the real estate exposure secured by which is granted to an individual or a property-holding shell company owned by an individual who is the guarantor of the exposure; and

(ii) either of the following conditions is met—

(A) the residential property is constructed, or to be constructed, under a subsidized home ownership scheme launched by the Government or a domestic public sector entity;

(B) the institution is able to demonstrate, with the support of written and reasoned legal advice, that the sovereign of the jurisdiction (including Hong Kong) in which the property or land is located or any public sector entity of that jurisdiction has the legal power and ability to ensure that the property under construction or to be constructed will be finished.

(3) An authorized institution may classify a real estate exposure secured by a residential property as a regulatory residential real estate exposure despite the criteria set out in subsection (1) if—

(a) the exposure was originated before the commencement date* of Part 3 of the Banking (Capital) (Amendment) Rules 2023;

(b) the exposure was eligible for a risk-weight of 50% under subsection (1) as in force immediately before that date; and

(c) there has been no material change to the loan terms and conditions since that date.

(L.N. 167 of 2023)

Editorial Note:

* Commencement date: 1 January 2025.

115A. Loan-to-value ratio

(1) The loan-to-value ratio (***LTV ratio***) of a regulatory residential real estate exposure (***subject exposure***) secured by one or more residential properties (***subject security***) must be calculated as a ratio of the amount specified in paragraph (a) to the amount specified in paragraph (b)—

(a) the sum of—

(i) the principal amount of any outstanding drawn portion of the subject exposure (including accrued interest); and

(ii) the amount of any undrawn committed portion of the subject exposure;

(b) the value at origination of the subject security, with the exceptions set out in subsections (6) and (7).

(2) If a pool of regulatory residential real estate exposures (collectively referred to as ***subject exposure***) is secured by one or more residential properties (***subject security***), the LTV ratio of the subject exposure must be calculated as a ratio of the amount specified in paragraph (a) to the amount specified in paragraph (b)—

(a) the sum of—

(i) the principal amount of any outstanding drawn portion of each of the regulatory residential real estate exposures in the pool (including accrued interest); and

(ii) the amount of any undrawn committed portion of each of the regulatory residential real estate exposures in the pool;

(b) the value at origination of the subject security, with the exceptions set out in subsections (6) and (7).

(3) If—

(a) a pool of real estate exposures is secured by one or more residential properties (***subject security***); and

(b) the pool consists of both regulatory residential real estate exposures and real estate exposures that are neither regulatory residential real estate exposures nor ADC exposures,

the LTV ratio applicable to the regulatory residential real estate exposures in the pool (***subject exposures***) must be calculated in accordance with subsection (2) where the reference to regulatory residential real estate exposures in subsection (2)(a) is taken to be a reference to all of the exposures in the pool referred to in paragraph (a).

(4) The numerator of the LTV ratio calculated under subsection (1), (2) or (3)—

(a) must not be reduced by any specific provisions; and

(b) must not take into account the effect of any recognized credit risk mitigation (including mortgage insurance) except for cash on deposit with the authorized institution—

(i) that is unconditionally and irrevocably pledged (or otherwise provided as security) by the obligor in respect of the subject exposure under a netting or offsetting agreement for the sole purpose of redemption of the subject exposure; and

(ii) for which the security arrangement meets all of the following requirements—

(A) the institution has a well-founded legal basis for concluding that the netting or offsetting agreement with the obligor is enforceable in each relevant jurisdiction regardless of whether the obligor is insolvent or bankrupt;

(B) the institution is able at any time to determine those assets and liabilities with the obligor that are subject to the netting or offsetting agreement;

(C) the institution monitors and controls the roll-off risks that may arise when short-term liabilities that have been netted against longer term exposures are no longer available;

(D) the institution monitors and controls its exposures to the obligor on a net basis.

(5) If a regulatory residential real estate exposure of an authorized institution secured by one or more residential properties (***subject security***) was originated before the commencement date* of this section and the subject security was revalued at least once before that date, the institution may treat the value at the last revaluation conducted before that date as the value at origination of the subject security.

(6) In calculating the LTV ratio of a subject exposure under subsection (1), (2) or (3), an authorized institution must use a value lower than the value at origination of the subject security if—

(a) downward adjustment of the value of the subject security is warranted by the prevailing local property market situations;

(b) the Monetary Authority, by written notice given to the institution, requires the institution to revise the value of the subject security downwards; or

(c) an extraordinary, idiosyncratic event occurs and results in a permanent reduction of the value of the subject security.

(7) If—

(a) an authorized institution incurs a new residential real estate exposure secured by a subject security that is also the security for at least one existing residential real estate exposure of the institution and an updated valuation of the security is obtained as part of the new loan application process in relation to the new residential real estate exposure, the institution may use the updated valuation in calculating the LTV ratio of the pool of regulatory residential real estate exposures secured by the subject security under subsection (2) or (3);

(b) the value of a subject security has been adjusted downwards under subsection (6)(a), an authorized institution may make a subsequent upward adjustment to the value of the subject security and, except in cases where the resultant adjusted value is higher than the value at origination of the subject security, use the resultant adjusted value in the LTV ratio calculation under subsection (1), (2) or (3);

(c) the value of a subject security has been adjusted downwards under subsection (6)(b), an authorized institution may, with the prior consent of the Monetary Authority, make a subsequent upward adjustment to the value of the subject security and use the resultant adjusted value in the LTV ratio calculation under subsection (1), (2) or (3); and

(d) modifications are made to a residential property included in a subject security that unequivocally increase the value of the property and there is an updated valuation that confirms the increase in value, an authorized institution may take into account that increase in the LTV ratio calculation under subsection (1), (2) or (3).

(8) In this section—

value at origination (批出承擔時價值)—

(a) in relation to a regulatory residential real estate exposure of an authorized institution secured by one or more residential properties, means the valuation of the property or properties obtained by the institution at the time of origination of the exposure; and

(b) in relation to a pool of residential real estate exposures of an authorized institution originated at the same time and secured by one or more residential properties, means the valuation of the property or properties obtained by the institution at the time of origination of the pool.

(L.N. 167 of 2023)

Editorial Note:

* Commencement date: 1 January 2025.

115B. Risk-weights of regulatory residential real estate exposures

(1) This section applies to a regulatory residential real estate exposure of an authorized institution, including a regulatory residential real estate exposure to a member of its staff (whether solely or jointly with another person).

(2) Subject to section 115C, if the exposure is an exposure that does not depend materially on cash flows generated by the residential property securing the exposure (***non-IPRE exposure***), the institution must allocate a risk-weight to the exposure in accordance with Table 13A based on the LTV ratio of the exposure calculated under section 115A.

Table 13A

Risk-weights for Regulatory Residential Real Estate Exposures that are Non-IPRE Exposures

Column 1	Column 2	Column 3
Item	LTV ratio	Risk-weight
1.	Not more than 70%	40%
2.	More than 70% but not more than 90%	50%
3.	More than 90%	100%

(3) Subject to section 115C, if the exposure is not a non-IPRE exposure, the institution must allocate a risk-weight to the exposure in accordance with Table 13B based on the LTV ratio of the exposure calculated under section 115A.

Table 13B

Risk-weights for Regulatory Residential Real Estate Exposures that are not Non-IPRE Exposures

Column 1	Column 2	Column 3
Item	LTV ratio	Risk-weight
1.	Not more than 70%	50%
2.	More than 70% but not more than 90%	70%
3.	More than 90%	120%

(4) For the purposes of subsections (2) and (3)—

(a) subject to paragraphs (b) and (c), the exposure is not a non-IPRE exposure if both the servicing of the exposure and the prospects for recovery in the event of default depend materially on the cash flows generated by the residential property securing the exposure, rather than on the income, revenue and net worth of the obligor in respect of the exposure generated from other sources;

(b) the institution may treat the exposure as a non-IPRE exposure if the property is—

(i) the primary residence of the obligor in respect of the exposure; or

(ii) if the obligor in respect of the exposure is a property-holding shell company owned by an individual who is the guarantor of the exposure—that individual's primary residence; and

(c) if the exposure was originated before the commencement date* of Part 3 of the Banking (Capital) (Amendment) Rules 2023, the institution may, if information necessary for assessment is not sufficient or readily available, treat the exposure as a non-IPRE exposure.

(L.N. 167 of 2023)

Editorial Note:

* Commencement date: 1 January 2025.

115C. Risk-weights of real estate exposures secured by residential property outside Hong Kong

If—

(a) a real estate exposure (other than an ADC exposure) of an authorized institution is secured by a residential property outside Hong Kong; and

(b) the relevant supervisory authority of the jurisdiction in which the residential property is situated has implemented capital adequacy standards that were formulated in accordance with the Basel Framework,

the institution may allocate a risk-weight to the exposure provided for under the capital adequacy standards (but excluding any approach that is based on internal models) applicable to banks incorporated in that jurisdiction.

(L.N. 167 of 2023)

115D. Risk-weights of other real estate exposures

An authorized institution must allocate a risk-weight of 150% to—

(a) an ADC exposure; and

(b) any other real estate exposure that is neither a regulatory residential real estate exposure nor a real estate exposure to which section 115C applies.

(L.N. 167 of 2023)

Subdivision 4—Equity Exposures and Subordinated Debts

(Subdivision 4 added L.N. 167 of 2023)

115E. Equity exposures

(1) Subject to sections 115F and 115G, an authorized institution

must allocate—

(a) a risk-weight of 400% to a speculative unlisted equity exposure; and

(b) a risk-weight of 250% to an equity exposure that is not a speculative unlisted equity exposure.

(2) In this section—

speculative unlisted equity exposure (投機性非上市股權風險承擔) means an equity investment in an unlisted company that is—

(a) invested for short-term resale purposes; or

(b) considered venture capital or similar investment that is—

(i) subject to price volatility; and

(ii) acquired in anticipation of significant future capital gains.

115F. Significant capital investments in commercial entities

(1) If the net book value of an authorized institution's significant capital investment in a commercial entity exceeds 15% of the institution's capital base as at the immediately preceding calendar quarter end date as reported in its capital adequacy ratio return, the institution must—

(a) subject to section 43(1)(n), allocate a risk-weight of 1 250% to the amount of the net book value of the investment that exceeds that 15%; and

(b) allocate a risk-weight determined in accordance with section 115E(1)(a) or (b), as the case requires, to the amount of the net book value of the investment that does not exceed that 15%.

(2) In this section—

significant capital investment in a commercial entity (對商業實體的重大資本投資) means an authorized institution's holdings of shares in a commercial entity if—

(a) the holdings amount to more than 10% of the ordinary shares issued by the commercial entity; or

(b) the commercial entity is an affiliate of the institution.

115G. Holdings of capital instruments issued by, and non-capital LAC liabilities of, financial sector entities

(1) If an authorized institution has an insignificant LAC investment that is a direct holding, indirect holding or synthetic holding of a capital instrument issued by, or a non-capital LAC liability of, a financial sector entity, any amount of the insignificant LAC investment that is not deducted from the institution's capital base under sections 43(1)(o), 47(1)(c) and 48(1)(c) must be allocated—

(a) a risk-weight determined in accordance with section 115E(1)(a) or (b), as the case requires, if the insignificant LAC investment is an equity exposure; or

(b) a risk-weight of 150% if the insignificant LAC investment is not an equity exposure.

(2) If an authorized institution has a significant LAC investment that is a direct holding, indirect holding or synthetic holding of a capital instrument issued by, or a non-capital LAC liability of, a financial sector entity, any amount of the significant LAC investment that is not deducted from the institution's capital base under sections 43(1)(p), 47(1)(d) and 48(1)(d) must be allocated—

(a) a risk-weight of 250% if the significant LAC investment is in a CET1 capital instrument; or

(b) in any other case—

(i) a risk-weight determined in accordance with section 115E(1)(a) or (b), as the case requires, if the significant LAC investment is an equity exposure; or

(ii) a risk-weight of 150% if the significant LAC investment is not an equity exposure.

(3) If an authorized institution maintains any non-capital LAC debt resources and has holdings of non-capital LAC liabilities that fall within section 48A, the institution must allocate a risk-weight of 150% to any amount of the holdings that is not deducted from the institution's capital base under section 48(1)(g)(i).

115H. Exposures to subordinated debts

An authorized institution must allocate a risk-weight of 150% to an exposure to a subordinated debt issued by a bank or corporate.

Subdivision 5—Other Exposures

(L.N. 167 of 2023)

116. Other exposures

(1) Subject to subsection (2), if none of the sections in Subdivisions 2, 3 and 4 applies to an exposure, an authorized institution must allocate a risk-weight of 100% to the exposure.

(2) The Monetary Authority may, by written notice given to an authorized institution, direct the institution to allocate to an exposure, or an exposure belonging to a class of exposures, to which this section applies, a risk-weight specified in the notice, being a risk-weight greater than 100%.

(3) An authorized institution must comply with a notice given to it under subsection (2).

(4) If, in respect of an exposure of an authorized institution, the institution has difficulty in allocating any accrued interest under the exposure to the obligors of the institution, the institution may, with the prior consent of the Monetary Authority, treat the accrued interest as an exposure to which this section applies.

(L.N. 167 of 2023)

Subdivision 6—Provisions Supplementary to Subdivisions 2, 3, 4 and 5

(L.N. 167 of 2023)

117. Exposures to credit-linked notes

(1) Subject to subsections (2) and (3), an authorized institution must allocate a risk-weight to an exposure to a credit-linked note that is the higher of the following—

(a) the risk-weight that would be attributable to the note as an exposure to the issuer of the note under Subdivision 2 or 5, as applicable;

(b) the risk-weight that would be attributable to the reference obligations of the note under Subdivision 2, 3, 4 or 5, as applicable.

(2) Subject to subsection (3), if a credit-linked note—

(a) is a first-to-default note, second-to-default note or n^{th}-to-default note; or

(b) provides credit protection proportionately to a basket of reference obligations,

an authorized institution must determine the risk-weight attributable to an exposure to the note as the risk-weight attributable to the pool of reference obligations of the note determined in accordance with section 117B(1), (2), (3) or

(4), as the case requires, as if the exposure to the note were a direct exposure to the credit default swap embedded in the note.

(3) This section does not apply to an exposure to a credit-linked note, or any part of such an exposure, to which any provision in Subdivision 4 applies.

(L.N. 167 of 2023)

117A. Determination of risk-weight applicable to certain types of off-balance sheet exposures

(1) If an off-balance sheet exposure of an authorized institution (***subject exposure***) is an asset sale with recourse, a sale and repurchase agreement (other than a repo-style transaction) or a forward asset purchase, where the institution is exposed to the credit risk of the assets sold or to be purchased, the risk-weight applicable to the subject exposure is the risk-weight applicable to those assets.

(2) If a subject exposure is partly paid-up shares and securities, the risk-weight applicable to the subject exposure is the risk-weight applicable to the relevant shares or securities.

(3) If a subject exposure is a direct credit substitute arising from the selling of credit protection in the form of total return swap or credit default swap in the authorized institution's banking book, subject to section 117B, the risk-weight applicable to the subject exposure is the risk-weight applicable to the reference obligation specified in the swap.

(4) If a subject exposure is a default risk exposure in respect of a single-name credit default swap that falls within section 226J(1) and the amount of the default risk exposure is determined in accordance with section 226J(3), the risk-weight applicable to the subject exposure is the attributed risk-weight of the counterparty in respect of the swap without

taking into account any recognized credit risk mitigation afforded to the swap.

(5) If a subject exposure is a commitment to extend a loan secured by a fully completed residential property and the exposure, but for the fact that it does not satisfy any one or more of section 115(1)(b), (c) or (d), would have been a regulatory residential real estate exposure, the authorized institution may allocate a risk-weight in accordance with section 115B to the exposure, if the institution has no reason to believe that any of section 115(1)(b), (c) or (d) will not be satisfied immediately after the loan that is the subject of the commitment is drawn down.

(L.N. 167 of 2023)

117AB. *(Repealed L.N. 167 of 2023)*

117AC. *(Repealed L.N. 167 of 2023)*

117AD. *(Repealed L.N. 167 of 2023)*

117AE. *(Repealed L.N. 167 of 2023)*

117B. Further provisions in relation to direct credit substitutes

(1) If a subject exposure referred to in section 117A(3) arises from a first-to-default credit derivative contract—

(a) subject to paragraph (b), the risk-weight applicable to the subject exposure is the sum of the risk-weights applicable to the reference obligations in the basket of reference obligations specified in the contract; and

(b) the risk-weight applicable to the subject exposure is subject to a cap of 1 250%.

(2) If a subject exposure referred to in section 117A(3) arises from a second-to-default credit derivative contract—

(a) subject to paragraph (b), the risk-weight applicable to the subject exposure is the sum of the risk-weights applicable to the reference obligations in the basket of reference obligations specified in the contract but excluding the lowest of those risk-weights; and

(b) the risk-weight applicable to the subject exposure is subject to a cap of 1 250%.

(3) If a subject exposure referred to in section 117A(3) arises from any other n^{th}-to-default credit derivative contract, subsection (2), with all necessary modifications, applies to that contract as it applies to a second-to-default credit derivative contract, so that the reference to "lowest" in subsection (2)(a) means—

(a) "lowest and second lowest" in the case of a third-to-default credit derivative contract; and

(b) "lowest, second lowest and third lowest" in the case of a fourth-to-default credit derivative contract,

and likewise for other n^{th}-to-default credit derivative contracts.

(4) If a subject exposure referred to in section 117A(3) arises from a credit derivative contract that provides credit protection proportionately in respect of the reference obligations in the basket of reference obligations specified in the contract, the risk-weight applicable to the subject exposure is calculated in accordance with Formula 13.

Formula 13

Calculation of Risk-weight of Off-balance Sheet Exposure Arising from Credit Derivative Contract under

$$RW_a = \sum_i (a_i \cdot RW_i)$$

where—

(a) RW_a is the weighted average risk-weight of a basket of reference obligations;

(b) a_i is the proportion of credit protection allocated to reference obligation i; and

(c) RW_i is the risk-weight of reference obligation i.

(L.N. 167 of 2023)

117C. Exposures in respect of assets underlying SFTs

(1) This section applies to an authorized institution's exposure to the asset underlying a specified SFT.

(2) Subject to subsection (3), if a specified SFT is booked in the institution's banking book, the institution must—

(a) treat the securities sold or lent, or the securities provided as collateral, under the specified SFT as an on-balance sheet exposure of the institution as if the institution had never entered into the specified SFT; and

(b) allocate to the exposure the risk-weight attributable to the securities.

(3) If the securities referred to in subsection (2)(a) are securitization issues, the risk-weight attributable to the securities must be determined in accordance with Part 7.

(4) To avoid doubt, if a specified SFT is booked in an authorized institution's trading book, an exposure of the institution to the asset underlying the specified SFT is an exposure subject to the requirements of Part 8 instead of this Part.

(5) In this section—

specified SFT (指明SFT), in relation to an authorized institution, means—

(a) a repo-style transaction that falls within paragraph (a) or (b) of the definition of ***repo-style transaction*** in section 2(1); or

(b) a repo-style transaction that falls within paragraph (d) of that definition under which the collateral provided by the institution is in the form of securities.

(L.N. 167 of 2023)

Division 3A—CIS Exposures

(Division 3A added L.N. 167 of 2023)

117D. Interpretation of Division 3A

In this Division—

indirect CIS exposure (間接CIS風險承擔) means an indirect CIS exposure within the meaning of section 226ZH;

Level 1 CIS (1級CIS) means a Level 1 CIS within the meaning of section 226ZH;

Level 2 CIS (2級CIS) means a Level 2 CIS within the meaning of section 226ZH;

Level n+1 CIS (n+1級CIS) means a Level n+1 CIS within the meaning of section 226ZH.

117E. Treatment of CIS exposure held by authorized institution

(1) If no amount of an authorized institution's CIS exposure to a Level 1 CIS constitutes a deductible holding, the institution must calculate the risk-weighted amount of the exposure in accordance with Part 6B.

(2) If any amount of an authorized institution's CIS exposure to a Level 1 CIS constitutes one or more deductible holdings, the institution must—

(a) classify the amounts of the CIS exposure that constitute deductible holdings into one portion (***portion A***);

(b) classify the amount of the CIS exposure that does not constitute deductible holdings into another portion (***portion B***);

(c) apply the treatment set out in section 117F to each of the amounts of the CIS exposure in portion A; and

(d) calculate the risk-weighted amount of portion B (if any) in accordance with Part 6B.

117F. Treatment of CIS exposure constituting deductible holding

(1) This section applies in relation to an authorized institution's CIS exposure to a Level 1 CIS, or any part of the exposure, that constitutes a deductible holding.

(2) The institution must—

(a) determine, in accordance with Division 4 of Part 3, the amount of the deductible holding that is required to be deducted from its capital base;

(b) if the deductible holding falls within section 43(1)(o) or (p), 47(1)(c) or 48(1)(c) or (g)(i)—determine the amount of the deductible holding that is required to be risk-weighted in accordance with section 48(3), section 5 of Schedule 4F or section 1(7) of Schedule 4G, as the case requires;

(c) deduct any amount determined under paragraph (a) from its capital base; and

(d) calculate the risk-weighted amount of any amount determined under paragraph (b) by multiplying that amount by the applicable risk-weight determined in accordance with subsection (3).

(3) The institution must—

(a) allocate a risk-weight, determined in accordance with section 115E(1)(a) or (b), as the case requires, to any amount of deductible holding determined under subsection (2)(b), if the deductible holding is an insignificant LAC investment that is an equity exposure;

(b) allocate a risk-weight of 150% to any amount of deductible holding determined under subsection (2)(b), if the deductible holding is—

(i) an insignificant LAC investment that is not an equity exposure; or

(ii) a holding of non-capital LAC liabilities falling within section 48A; and

(c) allocate a risk-weight of 250% to any amount of deductible holding determined under subsection (2)(b), if the deductible holding is a significant LAC investment in a CET1 capital instrument.

(4) To avoid doubt, this section also applies to cases where a CIS exposure to a Level 1 CIS, or any part of the exposure, constitutes a deductible holding because regulatory deductible items are held by—

(a) a Level 2 CIS to which the Level 1 CIS has a CIS exposure; or

(b) a Level n+1 CIS (where n is an integer equal to or greater than 2) to which the Level 1 CIS has an indirect CIS exposure.

117G. Determination of risk-weights applicable to certain types of off-balance sheet CIS exposures

(1) This section applies to a CIS exposure that is an off-balance sheet exposure.

(2) If the CIS exposure is an asset sale with recourse, a sale and repurchase agreement (other than a repo-style transaction) or a forward asset purchase, where the seller or buyer of the assets underlying the transaction is exposed to the credit risk of the assets sold or to be purchased, the risk-weight applicable to the CIS exposure is the risk-weight applicable to those assets.

(3) If the CIS exposure is partly paid-up shares and securities, the risk-weight applicable to the CIS exposure is the risk-weight applicable to the relevant shares or securities.

Division 4—Calculation of Exposure Amounts of Off-balance Sheet Exposures

(L.N. 167 of 2023)

118. Calculation of exposure amounts of off-balance sheet exposures

(L.N. 167 of 2023)

(1) An authorized institution must calculate the credit equivalent amount of an off-balance sheet exposure (other than an exposure to which subsection (2) or (3) applies) by—

(a) determining the CCF applicable to the exposure in accordance with Schedule 6 and, if applicable, subsection (1A); and

(b) multiplying the principal amount of the exposure, after deducting any specific provisions applicable to the exposure, by the CCF determined under paragraph (a). *(L.N. 167 of 2023)*

(1A) If an off-balance sheet exposure (***exposure A***) is a commitment the drawdown of which would give rise to another off-balance sheet exposure (***exposure B***), the CCF applicable to exposure A is the lower of—

(a) the CCF applicable to the commitment determined in accordance with Schedule 6; and

(b) the CCF applicable to exposure B determined in accordance with Schedule 6. *(L.N. 167 of 2023)*

(2) If—

(a) an authorized institution has posted unsegregated collateral to a counterparty for a transaction or contract booked in its banking book or trading book; and

(b) either—

(i) the collateral is not posted for a derivative contract or SFT; or

(ii) the collateral is posted for a derivative contract or SFT but is not included in the calculation of default risk exposure under Division 1A, 2, 2A or 2B of Part 6A,

the institution must treat the principal amount of the collateral, net of specific provisions, as the credit equivalent amount of its off-balance sheet exposure to the counterparty in respect of the collateral. *(L.N. 44 of 2020)*

(3) An authorized institution must calculate its default risk exposure in respect of derivative contracts or SFTs by using the approach or methods set out in Division 1A, 2, 2A or 2B of Part 6A, as the case requires. *(L.N. 44 of 2020)*

119-120. *(Repealed L.N. 167 of 2023)*

121. *(Repealed L.N. 54 of 2022)*

122-123. *(Repealed L.N. 167 of 2023)*

123A. *(Repealed L.N. 167 of 2023)*

Division 5—Use of Recognized Collateral in Credit Risk Mitigation

124. Recognized collateral

Collateral is recognized for the purposes of calculating the risk-weighted amount of an exposure of an authorized institution where—

(a) all documentation creating the collateral and providing for the obligations of the parties with respect to each other in respect of the collateral is binding on all parties and legally enforceable in all relevant jurisdictions;

(b) the legal mechanism by which the collateral is pledged (or otherwise provided as security) ensures that the institution has the right to realize, or to take legal possession of, the collateral in a timely manner in the event of a default by, or the insolvency or bankruptcy of, or any other event specified in the relevant legal documentation applicable to any of— *(L.N. 167 of 2023)*

(i) the obligor in respect of the exposure; or

(ii) the custodian, if any, holding the collateral;

(c) the institution has clear and adequate procedures for the timely realization of collateral in respect of an event referred to in paragraph (b);

(d) the institution has taken all steps to fulfil requirements under the law applicable to the institution’s interest in the collateral which are necessary to obtain and maintain an enforceable security interest, whether by registration or otherwise, or to exercise a right to set-off in relation to the title transfer of the collateral; *(L.N. 167 of 2023)*

(e) if the collateral is to be held by a custodian, the institution has taken reasonable steps to ensure that the custodian segregates the collateral from the custodian's assets;

(ea) if the collateral is provided under a margin agreement for derivative contracts or SFTs, the institution— *(L.N. 44 of 2020)*

(i) has devoted sufficient resources to enable the orderly operation of the agreement; and

(ii) has collateral management policies in place to control, monitor and report—

(A) risks (including liquidity risk and concentration risk) associated with the agreement;

(B) reuse of collateral; and

(C) the rights ceded by the institution in respect of collateral posted; *(L.N. 156 of 2012)*

(f) the credit quality of the obligor in respect of the exposure does not have material positive correlation with—

(i) the current market value of the collateral; and

(ii) the residual risks (including legal, operational, liquidity and market risks) arising from the use of the collateral for the purpose of mitigating the credit risk of the exposure; *(L.N. 167 of 2023)*

(g) the collateral—

(i) is pledged (or otherwise provided as security) for not less than the life of the exposure; and *(L.N. 167 of 2023)*

(ii) is revalued not less than every 6 months from the date upon which the collateral is taken in respect of the exposure; and

(h) the collateral falls within any one of the paragraphs of section 125(1). *(L.N. 156 of 2012; L.N. 167 of 2023)*

125. Collateral which may be recognized for purposes of section 124(h)

(1) Subject to subsection (2), for the purposes of section 124(h), only collateral of the following description may be recognized in relation to an authorized institution— *(L.N. 156 of 2012)*

(a) cash on deposit with the institution or held at a third-party bank;

(b) certificates of deposit issued by the institution;

(c) instruments issued by the institution which are comparable to instruments referred to in paragraph (b);

(ca) gold bullion; *(L.N. 167 of 2023)*

(d) debt securities issued or guaranteed by a sovereign of a Tier 1 country;

(e) debt securities issued or guaranteed by a relevant international organization;

(f) debt securities issued by a public sector entity of a Tier 1 country; *(L.N. 167 of 2023)*

(g) debt securities issued by a multilateral development bank; *(L.N. 167 of 2023)*

(h) debt securities issued by an unspecified multilateral body; *(L.N. 167 of 2023)*

(i) debt securities (other than eligible covered bonds) issued by—

(i) a bank falling within paragraph (a) of the definition of ***bank*** in section 2(1); or

(ii) a bank falling within paragraph (b) of that definition that is incorporated in a Tier 1 country; or *(L.N. 167 of 2023)*

(j) eligible covered bonds. *(L.N. 167 of 2023)*

(2) A reference to debt securities in subsection (1) does not include debt securities that are re-securitization exposures. *(L.N. 167 of 2023)*

126. Calculation of risk-weighted amount of exposures taking into account credit risk mitigating effect of recognized collateral

(L.N. 167 of 2023)

(1) An authorized institution may take into account the credit risk mitigating effect of recognized collateral in the calculation of the risk-weighted amounts of its exposures that are not default risk exposures (***non-default risk exposures***) only in accordance with section 127 or 128, as the case requires. *(L.N. 44 of 2020; L.N. 167 of 2023)*

(1A) An authorized institution may take into account the credit risk mitigating effect of recognized collateral in the calculation of the risk-weighted amount of a default risk exposure in accordance with section 129 only if any of the following is complied with in respect of the exposure— *(L.N. 167 of 2023)*

(a) the exposure is in respect of a derivative contract calculated by using the current exposure method;

(b) the exposure is in respect of an SFT calculated in accordance with section 226MJ; or

(c) the following—

(i) the exposure is in respect of one or more than one derivative contract entered into by the institution with a counterparty;

(ii) the exposure is calculated by using the SA-CCR approach or the IMM(CCR) approach; and

(iii) the conditions specified in subsection (1B) are met. *(L.N. 44 of 2020)*

(1B) The conditions are—

(a) the institution entered into the contract or contracts with the counterparty under a general banking facility consisting of 2 or more credit lines, and, for at least one of those credit lines, if drawn (whether in full or not), the drawn portion that will result from such drawdown is, at the time of the drawdown, a non-default risk exposure;

(b) the credit lines are secured by the same recognized collateral;

(c) no amount of the recognized collateral is designated solely for offsetting losses on default risk exposures incurred by the institution under the general banking facility; and

(d) the recognized collateral is not included in the calculation of the default risk exposure under Division 1A or 2 of Part 6A. *(L.N. 44 of 2020)*

(1C) If the same recognized collateral is available to cover both default risk exposures and non-default risk exposures, an authorized institution may, under section 127 or 128, take into account the credit risk mitigating effect of the recognized collateral for the purpose of calculating the risk-weighted amount of the non-default risk exposures only to the extent of the current market value, or the part of such value, of the collateral that is not included in the calculation of the default risk exposures under Division 1A or 2 of Part 6A. *(L.N. 44 of 2020; L.N. 167 of 2023)*

(1D) However, the calculation in accordance with section 127, 128 or 129 is subject to subsections (2), (3) and (4). *(L.N. 44 of 2020)*

(2) Where the recognized collateral consists of collateral—

(a) which falls within section 125(1)(a), (b) or (c); *(L.N. 156 of 2012)*

(b) which is held at a third-party bank in a non-custodial arrangement; and

(c) which is unconditionally and irrevocably pledged or assigned to an authorized institution,

the institution shall allocate to the credit protection covered portion of the exposure the attributed risk-weight of the third-party bank.

(3) An authorized institution must, if the exposure and the recognized collateral have currency mismatch, reduce the value of the collateral by 8%. *(L.N. 44 of 2020; L.N. 167 of 2023)*

(4) An authorized institution must—

(a) if the recognized collateral is not a securitization issue, determine the risk-weight to be allocated to the collateral in accordance with Subdivision 2 of Division 3 as if the collateral were an on-balance sheet exposure; and *(L.N. 167 of 2023)*

(b) if the recognized collateral is a securitization issue, determine the risk-weight to be allocated to the collateral in accordance with Part 7 as if the collateral were an on-balance sheet exposure. *(L.N. 156 of 2012; L.N. 175 of 2017)*

127. Calculation of risk-weighted amount of on-balance sheet exposures

An authorized institution shall calculate the risk-weighted amount of each of its on-balance sheet exposures by—

(a) dividing the exposure amount of the exposure into— *(L.N. 167 of 2023)*

(i) the credit protection covered portion; and

(ii) the credit protection uncovered portion;

(b) multiplying the credit protection covered portion by the risk-weight attributable to the recognized collateral and multiplying the credit protection uncovered portion by the risk-weight attributable to the exposure; and

(c) adding together the 2 products derived from the application of paragraph (b).

128. Calculation of risk-weighted amount of off-balance sheet exposures other than default risk exposures

(L.N. 137 of 2011; L.N. 44 of 2020)

An authorized institution shall calculate the risk-weighted amount of each of its off-balance sheet exposures which is not a default risk exposure by— *(L.N. 137 of 2011; L.N. 44 of 2020)*

(a) dividing the principal amount of the exposure, net of specific provisions, into—

(i) the credit protection covered portion; and

(ii) the credit protection uncovered portion;

(b) multiplying the credit protection covered portion and the credit protection uncovered portion by the CCF applicable to the off-balance sheet exposure to produce 2 credit equivalent amounts;

(c) multiplying the credit equivalent amount of the credit protection covered portion by the risk-weight attributable to the recognized collateral and multiplying the credit equivalent amount of the credit protection uncovered portion by the risk-weight attributable to the exposure; and

(d) adding together the 2 products derived from the application of paragraph (c).

129. Calculation of risk-weighted amount of default risk exposures

(L.N. 137 of 2011; L.N. 44 of 2020)

(1) An authorized institution must calculate the risk-weighted amount of its default risk exposure that is an exposure mentioned in section 126(1A)(a), (b) or (c) by— *(L.N. 137 of 2011; L.N. 44 of 2020)*

(a) dividing the exposure amount of the exposure into— *(L.N. 44 of 2020; L.N. 167 of 2023)*

(i) the credit protection covered portion; and

(ii) the credit protection uncovered portion; *(L.N. 156 of 2012)*

(b) multiplying the credit protection covered portion by the risk-weight attributable to the recognized collateral and multiplying the credit protection uncovered portion by the risk-weight attributable to the exposure; and *(L.N. 156 of 2012)*

(c) adding together the 2 products derived from the application of paragraph (b). *(L.N. 156 of 2012)*

(d) *(Repealed L.N. 156 of 2012)*

(2) *(Repealed L.N. 44 of 2020)*

Division 6—Use of Recognized Netting in Credit Risk

Mitigation

130. On-balance sheet netting

(1) Where amounts owed by an obligor to an authorized institution in respect of on-balance sheet exposures (other than CIS exposures) of the institution are subject to recognized netting, the institution— *(L.N. 54 of 2022)*

(a) may take into account the effect of the recognized netting in calculating its exposure to the obligor; and

(b) if a net credit exposure for the institution is the result of so taking into account the effect of the recognized netting, shall use the net credit exposure in calculating the risk-weighted amount of the exposure.

(2) An authorized institution shall calculate its net credit exposure, if any, referred to in subsection (1)(b) by the use of Formula 14.

Formula 14

Calculation of Net Credit Exposure under Recognized Netting

(L.N. 137 of 2011)

$$\text{Net credit exposure} = \max\left[0, \text{exposures} - \text{liabilities} \times (1 - H_{fx})\right]$$

where—

exposures = the amounts subject to recognized netting, net of specific provisions, owed by the obligor to the authorized institution;

liabilities = the amounts subject to recognized netting owed by the authorized institution to the obligor; and

H_{fx} = the 8% haircut to be applicable in consequence of a currency mismatch, if any, between the currencies in which the exposures and liabilities are denominated.

(3) Where an authorized institution has a net credit exposure to an obligor after taking into account recognized netting, the institution shall calculate the risk-weighted amount of the net credit exposure by multiplying the net credit exposure by the attributed risk-weight of the obligor.

130A. *(Repealed L.N. 44 of 2020)*

131. *(Repealed L.N. 44 of 2020)*

Division 7—Use of Recognized Guarantees and Recognized Credit Derivative Contracts in Credit Risk Mitigation

132. Recognized guarantees

A guarantee given to an authorized institution is recognized for the purposes of calculating the risk-weighted amount of a specific exposure or a specific pool of exposures of the institution (***guaranteed exposure***) if— *(L.N. 167 of 2023)*

(a) the guarantee is given by—

(i) a sovereign;

(ii) a public sector entity of a Tier 1 country;

(iii) a multilateral development bank;

(iv) an unspecified multilateral body;

(v) a bank; or

(vi) a qualifying CCP,

in each case having an attributed risk-weight lower than the risk-weight that would be allocated to the guaranteed exposure; *(L.N. 167 of 2023)*

(b) the guarantee gives the institution a direct claim against the guarantor;

(c) the credit protection provided by the guarantee relates specifically to the guaranteed exposure; *(L.N. 167 of 2023)*

(ca) the credit quality of the obligor in respect of the guaranteed exposure does not have material positive correlation with—

(i) the credit quality of the guarantor; and

(ii) the residual risks (including legal, operational, liquidity and market risks) arising from the use of the guarantee for the purpose of mitigating the credit risk of the guaranteed exposure; *(L.N. 167 of 2023)*

(d) the undertaking of the guarantor to make payment in specified circumstances relating to the guaranteed exposure is clearly documented so that the extent of the credit protection provided by the guarantee is clearly defined;

(e) there is no clause in the guarantee, the satisfaction of which is outside the direct control of the institution, which would allow the guarantor to cancel the guarantee unilaterally or which would increase the effective cost of the credit protection provided by the guarantee as a result of the deteriorating credit quality of the guaranteed exposure except for a clause permitting termination in the event of a failure by the institution to pay sums due from it under the terms of the guarantee;

(f) there is no clause in the guarantee, the satisfaction of which is outside the direct control of the institution, which could operate to prevent the guarantor from being obliged to pay out promptly in the event that the obligor in respect of the guaranteed exposure defaults in making any payments due to the institution in respect of the guaranteed exposure;

(g) the jurisdiction in which the guarantor is located and from which the guarantor may be obliged to make payment has no existing exchange controls in place or, if there are existing exchange controls in place, approval has been obtained for the funds to be remitted freely in the event that the guarantor is called on under the terms of the guarantee to make payment to the institution; *(L.N. 167 of 2023)*

(h) the guarantor has no recourse to the institution for any losses suffered as a result of the guarantor being obliged to make any payment to the institution pursuant to the guarantee;

(i) the institution has the right to receive payment from the guarantor without having to take legal action in order to pursue the obligor in respect of the guaranteed exposure for payment; and

(j) the guarantee is binding on all parties and legally enforceable in all relevant jurisdictions.

133. Recognized credit derivative contracts

(1) Subject to subsections (2), (3), (4) and (5), a credit derivative contract (***subject contract***) entered into by an authorized institution as a protection buyer may be recognized for

the purpose of calculating the risk-weighted amount of an exposure of the institution (***protected exposure***) if—

(a) the subject contract is a credit default swap or total return swap (other than a restricted credit derivative contract);

(b) the protection seller of the subject contract is—

(i) a sovereign;

(ii) a public sector entity of a Tier 1 country;

(iii) a multilateral development bank;

(iv) an unspecified multilateral body;

(v) a bank; or

(vi) a qualifying CCP,

in each case having an attributed risk-weight lower than the risk-weight that would be allocated to the protected exposure;

(c) the economic benefit derived by the institution would make good the economic loss suffered by the institution in consequence of the default of the obligor in respect of the protected exposure in a manner substantially similar to that of a recognized guarantee;

(d) the subject contract gives the institution a direct claim against the protection seller;

(e) the credit protection provided by the subject contract relates to a specific exposure or a specific pool of exposures;

(f) the credit quality of the reference entity of the subject contract does not have material positive correlation with—

(i) the credit quality of the protection seller; and

(ii) the residual risks (including legal, operational, liquidity and market risks) arising from the use of the subject contract for the purpose of mitigating the credit risk of the protected exposure;

(g) the undertaking of the protection seller under the subject contract to make payment in specified circumstances is clearly documented so that the extent of the credit protection provided by the subject contract is clearly defined;

(h) there is no clause in the subject contract, the satisfaction of which is outside the direct control of the institution, that would—

(i) allow the protection seller to cancel the subject contract unilaterally; or

(ii) increase the effective cost of the credit protection offered by the subject contract as a result of the deteriorating credit quality of the reference entity or any of the specified obligations of the subject contract,

except for a clause permitting termination in the event of a failure by the institution to pay sums due from it under the terms of the subject contract;

(i) there is no clause in the subject contract, the satisfaction of which is outside the direct control of the institution, that could operate to prevent the protection seller from being obliged to pay out promptly in the event that the reference entity defaults in making any payments due;

(j) the jurisdiction in which the protection seller is located and from which the protection seller may be obliged to make payment has no existing exchange controls in place or, if there are existing exchange controls in place, approval has been obtained for the funds to be remitted freely in the event that the protection seller is called on under the terms of the subject contract to make payment to the institution;

(k) the protection seller has no recourse to the institution for any losses suffered as a result of the protection seller being obliged to make any payment to the institution under the subject contract;

(l) the subject contract obliges the protection seller to make payment to the institution in the following credit events—

(i) any failure by the reference entity to pay amounts due under the terms of any of the specified obligations (subject to any grace period in the subject contract that is of substantially similar duration to any grace period provided for in the terms of the specified obligations);

(ii) the bankruptcy or insolvency of the reference entity, or the reference entity's failure or inability to pay its debts as they fall due, or the reference entity's written admission of the reference entity's inability generally to pay its debts as they fall due, or any event with respect to the reference entity that has an analogous effect to any of the foregoing events; or

(iii) restructuring of any of the specified obligations, involving forgiveness or postponement of payment of any principal or interest or fees, that results in the holder of the specified obligation restructured making specific provision or other similar debit to its profit and loss account;

(m) in any case where any of the specified obligations provides a grace period within which the reference entity may make good a default in payment, the subject contract is not capable of terminating prior to the expiry of the grace period;

(n) in any case where the subject contract provides for settlement in cash, it provides an adequate mechanism for valuation of loss and specifies a reasonable period within which that valuation is to be arrived at following a credit event;

(o) in any case where the specified obligations do not include or are different from the protected exposure—

(i) each of the specified obligations ranks for payment or repayment equally with, or junior to, the protected exposure; and

(ii) the obligor in respect of the protected exposure is the same person as the reference entity of the subject contract and legally enforceable cross default or cross acceleration clauses are included in the terms of both the protected exposure and the specified obligations;

(p) in any case where, under the terms of the subject contract, it is a condition of settlement that the institution transfers the protected exposure to the protection seller, the terms of the protected exposure provide that any consent which may be required from the obligor in respect of the protected exposure must not be unreasonably withheld;

(q) the subject contract specifies clearly the identity of the person who is empowered to determine whether a credit event has occurred, that person is not solely the protection seller and the institution is, under the terms of the subject contract, entitled to inform the protection seller of the occurrence of a credit event; and

(r) the subject contract is binding on all parties and legally enforceable in all relevant jurisdictions.

(2) If all the criteria set out in subsection (1) are met in respect of the subject contract except that the credit events specified in the subject contract do not include the credit event described in subsection (1)(l)(iii), the subject contract may be recognized for the purpose of calculating the risk-weighted amount of the protected exposure if all of the following conditions are met—

(a) the protected exposure is an exposure to a corporate;

(b) unanimous consent of all creditors in respect of the protected exposure is required to amend the maturity, principal, coupon, currency or seniority status of the protected exposure;

(c) the legal domicile in which the protected exposure is governed has well-established legislation on insolvency, bankruptcy or liquidation that—

(i) allows for a corporate to reorganize or restructure; and

(ii) provides for an orderly settlement of creditor claims.

(3) If—

(a) all the criteria set out in subsection (1) are met in respect of the subject contract except that the credit events specified in the subject contract do not include the credit event described in subsection (1)(l)(iii);

(b) any one or more of the conditions set out in subsection (2) are not met in respect of the subject contract; and

(c) the maximum liability of the protection seller to the authorized institution under the subject contract is more than the amount of the protected exposure, the amount of the subject contract that may be recognized for the purpose of calculating the risk-weighted amount of the protected exposure must not be more than 60% of the amount of the protected exposure.

(4) If—

(a) all the criteria set out in subsection (1) are met in respect of the subject contract except that the credit events specified in the subject contract do not include the credit event described in subsection (1)(l)(iii);

(b) any one or more of the conditions set out in subsection (2) are not met in respect of the subject contract; and

(c) the maximum liability of the protection seller to the authorized institution under the subject contract is equal to or less than the amount of the protected exposure,

the amount of the subject contract that may be recognized for the purpose of calculating the risk-weighted amount of the protected exposure must not be more than 60% of the maximum liability of the protection seller to the institution under the subject contract.

(5) If the subject contract is a credit derivative contract embedded in a cash funded credit-linked note issued by the authorized institution, the subject contract is recognized for the purpose of calculating the risk-weighted amount of the protected exposure if all the criteria set out in subsection (1), excluding the criterion set out in subsection (1)(b), are met.

(6) In this section—

restricted credit derivative contract (受限制信用衍生工具合約), in relation to an authorized institution, means—

(a) a total return swap where—

(i) the institution is the protection buyer under the swap; and

(ii) the institution records the net payments received by it under the swap as net income but does not record, through deductions in fair value in the accounts of the institution or by an addition to reserves or provisions, the extent to which the value of the protected exposure has deteriorated; or

(b) a first-to-default credit derivative contract, a second-to-default credit derivative contract or any other n^{th}-to-default credit derivative contract;

specified obligation (指明義務), in relation to a credit derivative contract entered into by an authorized institution as a protection buyer in respect of an exposure of the institution—

(a) means an obligation of a specified reference entity specified in the credit derivative contract that is—

(i) a reference obligation; or

(ii) an obligation used for the purpose of determining whether a credit event has occurred; and

(b) may or may not include the exposure of the institution.

(L.N. 167 of 2023)

134. Capital treatment of recognized guarantees and recognized credit derivative contracts

(1) If an exposure is covered by a recognized guarantee or recognized credit derivative contract (***protected exposure***), an authorized institution must calculate the risk-weighted amount of the protected exposure in accordance with subsection (2).

(2) If the credit protection covered portion and the credit protection uncovered portion of a protected exposure rank equally—

(a) sections 127, 128 and 129, with all necessary modifications, apply to the authorized institution in relation to the calculation of the risk-weighted amount of the protected exposure; and

(b) the authorized institution must—

(i) subject to subsections (5) and (6), allocate to the protected amount of the protected exposure the attributed risk-weight of the credit protection provider; and

(ii) allocate to the unprotected amount of the protected exposure the risk-weight attributable to the protected exposure under Division 3.

(3) For the purposes of subsection (2)—

(a) if section 127 or 129 applies to the authorized institution—

(i) subject to subsection (4), the protected amount of the protected exposure is the credit protection covered portion of the protected exposure; and

(ii) the unprotected amount of the protected exposure is the credit protection uncovered portion of the protected exposure; and

(b) if section 128 applies to the authorized institution—

(i) subject to subsection (4), the protected amount of the protected exposure is the product of the credit protection covered portion of the protected exposure and the CCF applicable to the protected exposure; and

(ii) the unprotected amount of the protected exposure is the product of the credit protection uncovered portion of the protected exposure and the CCF applicable to the protected exposure.

(4) If, in respect of a protected exposure, there is a currency mismatch, an authorized institution, in determining the

protected amount for the purposes of subsection (2), must reduce the amount of the credit protection covered portion of the protected exposure by 8%.

(5) If the credit protection covered portion of a protected exposure is such a credit protection covered portion because of a recognized guarantee (***original guarantee***) and is the subject of a counter-guarantee given by a sovereign, an authorized institution may, in respect of the credit protection covered portion, treat the counter-guarantee as if it were the original guarantee if—

(a) the counter-guarantee covers all credit risk elements of the protected exposure to the extent that it relates to the credit protection covered portion;

(b) the counter-guarantee is given in such terms that it can be called if—

(i) for any reason the obligor in respect of the protected exposure fails to make payments due in respect of the protected exposure; and

(ii) the original guarantee could be called;

(c) the counter-guarantee meets all of the requirements for guarantees set out in section 132 (except that the counter-guarantee need not meet the requirements set out in section 132(b) and (c)); and

(d) the institution reasonably considers, and demonstrates to the satisfaction of the Monetary Authority, that—

(i) the cover of the counter-guarantee is adequate and effective; and

(ii) there is no evidence to suggest that the coverage of the counter-guarantee is less effective than that of a direct and explicit guarantee by the sovereign that gives the counter-guarantee.

(6) If a recognized credit derivative contract is cleared by a qualifying CCP, an authorized institution may allocate to the protected amount of the protected exposure to which the contract relates—

(a) a risk-weight of 2% if—

(i) the institution is a clearing member of the qualifying CCP;

(ii) the institution is a direct client of a clearing member of the qualifying CCP and all of the conditions set out in section 226ZA(6) are met; or

(iii) the institution is an indirect client within a multi-level client structure associated with the qualifying CCP and all of the conditions set out in section 226ZA(6), with all necessary modifications, are met for arrangements among the CCP, clearing member, all clients at levels higher than the institution within the multi-level client structure, and the institution; or

(b) a risk-weight of 4% if—

(i) the institution is a direct client of a clearing member of the qualifying CCP and all of the conditions set out in section 226ZA(6) (excluding the condition set out in section 226ZA(6)(a)(iii)) are met; or

(ii) the institution is an indirect client within a multi-level client structure associated with the qualifying CCP and all of the conditions set out in section 226ZA(6) (excluding the condition set out in section 226ZA(6)(a)(iii)), with all necessary modifications, are met for arrangements among the CCP, clearing member, all clients at levels higher than the institution within the multi-level client structure, and the institution.

(L.N. 167 of 2023)

135. Provisions supplementary to section 134

(1) Subject to subsection (9) and section 133(2), (3) and (4), if the credit protection in respect of an authorized institution's exposure consists of a recognized credit derivative contract which is a credit default swap or total return swap— *(L.N. 167 of 2023)*

(a) if upon the happening of a credit event the protection seller is obliged to pay the amount specified in the contract to the institution in exchange for delivery by the institution of the deliverable obligation specified in the contract, the institution may treat the exposure as being fully covered;

(b) if upon the happening of a credit event the protection seller is obliged to pay the amount specified in the contract to the institution less the market value of the reference obligation specified in the contract, calculated by specified calculation agents at some specified point in time after the credit event has occurred, the institution may treat the exposure as being fully covered; and

(c) if upon the happening of a credit event the protection seller is obliged to pay a fixed amount to the institution, the institution may only treat that amount of the exposure which is equivalent to the fixed amount as being fully covered.

(2)-(6) *(Repealed L.N. 167 of 2023)*

(6A) *(Repealed L.N. 167 of 2023)*

(7) If an authorized institution has obtained tranched credit protection for its exposure, it must—

(a) decompose the exposure into a protected sub-tranche and an unprotected sub-tranche; and

(b) determine the risk-weighted amount of the exposure in accordance with Part 7. *(L.N. 175 of 2017)*

(8) Subject to subsection (9), if the credit protection in respect of an authorized institution's exposure takes the form of an issue of credit-linked notes by the institution, the institution— *(L.N. 167 of 2023)*

(a) may only treat that amount of the exposure which is equivalent to the cash funding received from the notes as being fully covered; and

(b) must treat the credit protection covered portion of the exposure as an exposure collateralized by cash deposit. *(L.N. 156 of 2012; L.N. 167 of 2023)*

(c) *(Repealed L.N. 167 of 2023)*

(9) If the credit protection in respect of an authorized institution's exposure consists of a recognized credit derivative contract (including such a contract embedded in credit-linked notes issued by the institution) that provides that, on the happening of a credit event, the protection seller is not obliged to make a payment in respect of any loss or to absorb any loss if the loss is below a specified amount (***materiality threshold***), the institution must, in calculating its capital adequacy ratio, allocate a risk-weight of 1 250% to the portion of the exposure that is below the materiality threshold. *(L.N. 167 of 2023)*

Division 8—Multiple Recognized Credit Risk Mitigation and Maturity Mismatches

136. Multiple recognized credit risk mitigation

(1) Where in respect of a single exposure of an authorized

institution to an obligor, 2 or more forms of recognized credit risk mitigation have been used by the institution, the institution shall calculate the risk-weighted amount of the exposure in accordance with this Part by dividing the exposure into the portions which respectively represent the proportions of the exposure covered by each of the forms of recognized credit risk mitigation so used. *(L.N. 167 of 2023)*

(2) Where in respect of a single exposure of an authorized institution to an obligor, there is an overlap of coverage between 2 or more forms of recognized credit risk mitigation used by the institution, the institution may select, in respect of the portion of the exposure covered by the overlap, the recognized credit risk mitigation which result in the lowest risk-weighted amount of that portion of the exposure covered by the overlap.

(3) Where an authorized institution has an exposure to an obligor in the form of a general banking facility consisting of 2 or more credit lines—

(a) the institution may, in calculating its risk-weighted amount in respect of the credit lines, allocate any credit protection taken in respect of the exposure amongst the individual exposures under each of the credit lines; and

(b) if the institution exercises its discretion under paragraph (a), the institution shall aggregate the risk-weighted amounts of the individual exposures under each of the credit lines to determine the total risk-weighted amount of the exposure in respect of the general banking facility.

137. Maturity mismatches

(1) Where the credit protection provided in respect of an exposure of an authorized institution (other than the netting of derivative contracts) has a residual maturity which is shorter than the residual maturity of the exposure, the institution

shall not take into account the credit risk mitigation effect of that credit protection for the purposes of this Part. *(L.N. 44 of 2020)*

(2) For the purposes of calculating the respective maturities of an exposure of an authorized institution and any credit protection covering the exposure—

(a) the institution shall, at any time before the obligor in respect of the exposure to which the credit protection relates performs the obligor's obligations, take the effective maturity of the exposure to be the longest possible remaining time after taking into account any applicable grace period provided for in the terms of the exposure;

(b) if the terms of the credit protection provide for an option which may reduce the term of that credit protection, the institution shall take into account the option and the earliest possible date upon which it may be exercised;

(c) if the terms of the credit protection provide that the credit protection provider may terminate the credit protection before its maturity, the institution shall take the maturity of the credit protection to be the first date upon which the credit protection provider may so terminate the credit protection; and

(d) if the terms of the credit protection permit the institution to terminate the credit protection before its maturity and there is a positive incentive for the institution to exercise its discretion so to do, the institution shall take the maturity of the credit protection to be the time left to run before the earliest date upon which the institution may exercise the discretion.

(3) For the purposes of this section, the residual maturity of credit protection which is recognized collateral falling within section 125(1)(a) or (ca) shall be taken to be the period for which it will continue to fulfil the requirements of section 124 applicable to the credit protection. *(L.N. 156 of 2012)*

(L.N. 167 of 2023)

Part 6

Calculation of Credit Risk for Non-securitization Exposures: IRB Approach

Division 1—General

138. Application of Part 6

(1) This Part applies to an authorized institution which uses the IRB approach to calculate its credit risk for non-securitization exposures.

(2) A reference to an authorized institution in this Part is a reference to an authorized institution which uses the IRB approach to calculate its credit risk for non-securitization exposures. *(L.N. 167 of 2023)*

139. Interpretation of Part 6

(1) In this Part— *(L.N. 167 of 2023)*

advanced IRB approach (高級IRB計算法) means an approach under which an authorized institution calculates its credit risk for corporate or sovereign exposures by— *(L.N. 167 of 2023)*

(a) providing its own estimates of the PD, LGD and EAD of those exposures; and

(b) measuring the M of those exposures,

in accordance with Divisions 4, 5, 9, 10 and 11;

cash items (現金項目), in relation to an authorized institution, means all or any of the following—

(a) notes and coins owned by the institution that are the lawful currency of a jurisdiction and are held by the institution or in transit; *(L.N. 167 of 2023)*

(b) the institution's holdings of certificates of indebtedness issued by the Government for the issue of legal tender notes;

(c) gold bullion held by the institution, or gold bullion held on an allocated basis for the institution by another person, which is backed by gold bullion liabilities;

(d) gold bullion held by the institution, or gold bullion held for the institution by another person, which is not backed by gold bullion liabilities;

(e) cheques, drafts and other items drawn on other banks—

(i) which are payable to the account of the institution immediately upon presentation; and

(ii) which are in the process of collection;

(f) unsettled clearing items of the institution which are being processed through any interbank clearing system in Hong Kong;

(g) receivables from transactions in securities, foreign exchange, and commodities which are not yet due for settlement; *(L.N. 167 of 2023)*

(h) positive current exposure incurred by the institution under transactions in securities, foreign exchange, and commodities— *(L.N. 167 of 2023)*

(i) which are entered into on a delivery-versus-payment basis; and

(ii) which are outstanding after the settlement date for the transaction; *(L.N. 137 of 2011)*

(i) the amounts of payment made or the current market value of the thing delivered, and the positive current exposure incurred, by the institution under transactions in securities, foreign exchange, and commodities— *(L.N. 167 of 2023)*

(i) which are entered into on a basis other than a delivery-versus-payment basis; and *(L.N. 156 of 2012)*

(ii) which are outstanding up to and including the fourth business day after the settlement date for the transaction,

where the sum of the amounts of payment made (or the current market value of the thing delivered) and the positive current exposure incurred is less than $10 million in respect of each such transaction;

(j) the amounts of payment made or the current market value of the thing delivered, and the positive current exposure incurred, by the institution in respect of transactions in securities, or transactions in foreign exchange or commodities, that— *(L.N. 167 of 2023)*

(i) are entered into on a basis other than a delivery-versus-payment basis; and

(ii) have remained unsettled after the contractual date of payment or delivery to the institution for 5 or more business days; *(L.N. 156 of 2012)*

CIS calculation approach (CIS計算方法), in relation to a CIS exposure, means any one or more of the following approaches, as determined under Part 6B, to be used for calculating the risk-weighted amount of the CIS exposure—

(a) the look-through approach;

(b) the third-party approach;

(c) the mandate-based approach;

(d) the fall-back approach; *(L.N. 54 of 2022)*

corporate (法團) has the meaning given by section 51(1); *(L.N. 167 of 2023)*

credit equivalent amount (信貸等值數額), in relation to an off-balance sheet exposure of an authorized institution that is not a default risk exposure, means the value obtained by multiplying the principal amount of the exposure by the applicable CCF; *(L.N. 156 of 2012; L.N. 44 of 2020)*

credit risk components (信用風險組成部分) means the estimates of PD, LGD, EAD, EL and M which constitute inputs into the IRB risk-weight functions to determine the risk-weight to be allocated to—

(a) corporate, sovereign, bank or retail exposures; *(L.N. 167 of 2023)*

(b) *(Repealed L.N. 167 of 2023)*

dilution risk (攤薄風險), in relation to a receivable purchased by an authorized institution, means the possibility that the amount of the receivable is reduced through cash or non-cash credits to the obligor in respect of the receivable;

double default (雙重違責), in relation to an authorized institution's exposure to which a recognized guarantee or recognized credit derivative contract relates, means the default of both the obligor and the credit protection provider in respect of the exposure;

EAD means exposure at default;

EL means expected loss;

EL amount (EL額) means expected loss amount;

eligible provisions (合資格準備金), in relation to an authorized institution, means the sum of—

(a) the institution's specific provisions, partial write-offs, regulatory reserve for general banking risks and collective provisions attributed to non-securitization exposures that are subject to the IRB approach; and

(b) any discounts falling within section 163(3) or 164(5) on exposures referred to in paragraph (a) that are in default; *(L.N. 156 of 2012; L.N. 167 of 2023)*

equity exposure (股權風險承擔) means an exposure that falls within section 54A; *(L.N. 167 of 2023)*

expected long run loss rate (預期長期損失率), in relation to a pool of retail exposures of an authorized institution, means a loss rate calculated based on the realized losses over the total outstanding amount of exposures which fall within the pool of retail exposures, measured over a period of time which is not less than the period required under section 178(1)(g);

expected loss (預期損失), in relation to an exposure of an authorized institution, means the estimated loss likely to be incurred by the institution on the exposure arising from the potential default of the obligor or dilution risk in respect of the exposure over a one-year period, expressed as a ratio, relative to the EAD of the exposure;

expected loss amount (預期損失額), in relation to an exposure of an authorized institution, means—

(a) subject to paragraph (b), the expected loss amount of the exposure calculated by multiplying the EL of the exposure by the EAD of the exposure;

(b) if the exposure is an off-balance sheet exposure arising from a netting set that consists of one or more than one derivative contract, the expected loss amount of the exposure calculated by multiplying the EL of the exposure by the outstanding default risk exposure of the netting set; *(L.N. 156 of 2012; L.N. 44 of 2020)*

exposure (風險承擔), in relation to an authorized institution, means a credit exposure (including an asset) of the institution;

exposure at default (違責風險承擔), in relation to an exposure of an authorized institution, means the expected amount (being, in the case of an off-balance sheet exposure, the credit equivalent amount, default risk exposure or outstanding default risk exposure, as the case may be) of the exposure upon the default of the obligor in respect of the exposure, which is measured without deduction of specific provisions and partial write-offs; *(L.N. 156 of 2012)*

facility grade (融通等級), in relation to an authorized institution, means a rating of loss severity in the event of default within the facility rating scale of the institution's rating system, as measured by LGD, to which exposures are assigned on the basis of a specified and distinct set of internal rating criteria;

facility type (融通類型), in relation to an authorized institution, means a type of exposures with identical or similar transaction characteristics;

fall-back approach (備選方法) has the meaning given by section 226ZG; *(L.N. 54 of 2022)*

financial institution (金融機構) means an entity that—

(a) is a financial sector entity; or

(b) is engaged predominantly in any one or more of the following activities, whether by itself or through any of its subsidiaries—

(i) lending;

(ii) factoring;

(iii) provisions of credit enhancement;

(iv) securitization;

(v) proprietary trading;

(vi) any other financial services activity specified in Part 11 of Schedule 1; *(L.N. 167 of 2023)*

financial institution treated as corporate (視為法團的金融機構) means a financial institution (other than a bank) that is not a qualifying non-bank financial institution; *(L.N. 167 of 2023)*

foundation IRB approach (基礎IRB計算法) means an approach under which an authorized institution calculates its credit risk for corporate, sovereign or bank exposures by—

(a) providing its own estimates of the PD of those exposures; and

(b) subject to section 167(1)(c), using supervisory estimates for the other credit risk components of those exposures, *(L.N. 167 of 2023)*

in accordance with Divisions 4, 5, 9, 10 and 11;

fully secured exposure (具全數保證風險承擔), for the purpose of taking into account the credit risk mitigating effect of recognized collateral under the advanced IRB approach and retail IRB approach, means an exposure that is secured by recognized collateral the value of which (after the application of haircut in accordance with the standard supervisory haircuts subject to adjustment as set out in section 92) is equal to or more than the value of the exposure (after the application of haircut in accordance with the standard supervisory haircuts subject to adjustment as set out in section 92); *(L.N. 167 of 2023)*

HVCRE exposure (高波動性商業地產風險承擔) means an authorized institution's specialized lending that falls within high-volatility commercial real estate under section 143(1)(e); *(L.N. 212 of 2015)*

IRB class (IRB類別) means a class of non-securitization exposures specified in Table 16 (including the IRB subclasses which fall within that class);

IRB subclass (IRB子類別) means a subclass of non-securitization exposures specified in Table 16;

LGD means loss given default;

look-through approach (透視計算法) has the meaning given by section 226ZG; *(L.N. 54 of 2022)*

loss given default (違責損失率), in relation to an exposure of an authorized institution, means the loss likely to be incurred by the institution upon the default of the obligor in respect of the exposure, expressed as a ratio, relative to the EAD of the exposure;

M means maturity;

mandate-based approach (授權基準計算法) has the meaning given by section 226ZG; *(L.N. 54 of 2022)*

maturity (到期期限)—

(a) in relation to a corporate, sovereign or bank exposure of an authorized institution which uses the foundation IRB approach or advanced IRB approach, means the effective maturity of the exposure as determined or calculated in accordance with section 167 or 168, as the case requires; *(L.N. 137 of 2011; L.N. 167 of 2023)*

(b) *(Repealed L.N. 167 of 2023)*

obligor grade (承擔義務人等級), in relation to an authorized institution, means a rating within the obligor rating scale of the institution's rating system representing an assessment of the risk of default to which exposures to obligors are assigned on the basis of a specified and distinct set of internal rating criteria and from which estimates of PD are derived;

partially secured exposure (具部分保證風險承擔), for the purpose of taking into account the credit risk mitigating effect of recognized collateral under the advanced IRB approach and retail IRB approach, means an exposure that is secured by recognized collateral but is not a fully secured exposure; *(L.N. 167 of 2023)*

PD means probability of default;

pool (組別) means a category of exposures which have—

(a) similar obligor and transaction characteristics; and

(b) identical estimates of PD, LGD and EAD;

principal amount (本金額)—

(a) in relation to an on-balance sheet exposure of an authorized institution—

(i) if the exposure is measured at fair value, means the value of the exposure determined in accordance with section 4A; or

(ii) if the exposure is not measured at fair value, means the book value (including accrued interest) of the exposure; or *(L.N. 137 of 2011)*

(b) in relation to an off-balance sheet exposure of an authorized institution, means—

(i)-(ii) *(Repealed L.N. 44 of 2020)*

(iii) subject to subparagraph (iv), in the case of an exposure listed in Table 20 or to which section 166 or 182 applies, the contracted amount of the exposure; *(L.N. 44 of 2020)*

(iv) in the case of an exposure listed in Table 20 or to which section 166 or 182 applies that arises from an undrawn facility or the undrawn portion of a partially drawn facility, the amount of the undrawn commitment; *(L.N. 175 of 2017; L.N. 44 of 2020)*

(v) in the case of an exposure to a person arising from the person holding collateral posted by the institution in a manner that is not bankruptcy remote from the person, the fair value of the collateral; *(L.N. 156 of 2012)*

probability of default (違責或然率), in relation to an exposure of an authorized institution, means the probability of default of the obligor in respect of the exposure over a one-year period;

rating system (評級系統) means all the methods, models, processes, controls, and data collection and information technology systems, used by an authorized institution which enable the assessment of credit risk, the assignment of internal credit risk ratings, and the quantification of default and loss estimates, by the institution;

re-ageing (重新確定帳齡) means a process by which an exposure of an authorized institution previously classified as a past due exposure, the terms of which have not been changed, is subsequently classified as performing by reason of the subsequent good performance of the obligor in respect of the exposure, notwithstanding that all outstanding arrears in respect of the exposure have not been repaid;

recognized collateral (認可抵押品)—

(a) in relation to an authorized institution which uses the foundation IRB approach to calculate its credit risk for corporate, sovereign or bank exposures, means—

(i) recognized financial collateral; or

(ii) recognized IRB collateral; or *(L.N. 137 of 2011)*

(b) in relation to an authorized institution which uses the advanced IRB approach to calculate its credit risk for corporate or sovereign exposures or the retail IRB approach to calculate its credit risk for retail exposures, means any collateral— *(L.N. 167 of 2023)*

(i) which is recognized by the institution for credit risk mitigation in accordance with its policies and procedures; and

(ii) which satisfy the requirements under section 77(2); *(L.N. 156 of 2012; L.N. 167 of 2023)*

recognized credit derivative contract (認可信用衍生工具合約)—

(a) if an authorized institution uses the substitution framework to take into account the credit risk mitigating effect of credit derivative contracts for its corporate, sovereign, bank or retail exposures—means a credit derivative contract that falls within section 211 or 212, as the case requires; or

(b) in any other case—means an internal risk transfer recognized under section 213(1) or an internal risk transfer to the extent that it is recognized under section 213(2)(a); *(L.N. 167 of 2023)*

recognized financial collateral (認可財務抵押品)—

(a) subject to paragraph (b), means any collateral that—

(i) falls within the description in section 80(1)(a), (b) or (c); and

(ii) meets the criteria specified in section 77(2); and

(b) does not include any collateral in the form of—

(i) real property; or

(ii) debt securities that are re-securitization exposures; *(L.N. 167 of 2023)*

recognized guarantee (認可擔保)—

(a) in relation to an authorized institution which uses the substitution framework to take into account the credit risk mitigating effect of guarantees for its corporate, sovereign, bank or retail exposures, means a guarantee that falls within section 211 or 212, as the case requires; *(L.N. 137 of 2011; L.N. 167 of 2023)*

(b) *(Repealed L.N. 167 of 2023)*

recognized IRB collateral (認可IRB抵押品) means any collateral in the form of—

(a) financial receivables which fall within section 205;

(b) commercial real estate or residential real estate which falls within section 206 or 208, as the case requires; or

(c) physical assets (except commercial real estate or residential real estate) which fall within section 207 or 208, as the case requires;

residential mortgage loan (住宅按揭貸款), in relation to an authorized institution, means a credit facility provided by the institution to a borrower—

(a) that is secured on residential property or residential properties; and

(b) that is required by the facility agreement between the institution and the borrower to be secured on the residential property or residential properties referred to in paragraph (a); *(L.N. 167 of 2023)*

residual value risk (剩餘價值風險), in relation to a leasing arrangement entered into by an authorized institution, means the institution's exposure to potential loss due to the fair value of the leased asset declining below the residual value estimated for the leased asset at the time of inception of the lease;

retail IRB approach (零售IRB計算法) means an approach under which an authorized institution calculates its credit risk for retail exposures in accordance with Divisions 4, 6, 9, 10 and 11;

risk-weight function (風險權重函數) means a formula used by an authorized institution to determine the risk-weight to be allocated to—

(a) a corporate, sovereign, bank or retail exposure of the institution; *(L.N. 167 of 2023)*

(b) *(Repealed L.N. 167 of 2023)*

SFT risk-weighted amount (SFT風險加權數額), in relation to SFTs, means the sum of the default risk risk-weighted amounts for all counterparties to the SFTs where the default risk risk-weighted amount for each of the counterparties is calculated as the sum of the risk-weighted amounts of the default risk exposures across all the SFTs with the counterparty calculated in accordance with section 202; *(L.N. 156 of 2012; L.N. 44 of 2020)*

specialized lending (專門性借貸) means an exposure of a lender to a corporate that—

(a) falls within section 143(1); and

(b) possesses both of the following characteristics, either in legal form or economic substance—

(i) the corporate has few or no other material assets or activities, and therefore the primary source of repayment of the exposure is the income generated by the asset or assets being financed by the lender, rather than the independent capacity of the corporate;

(ii) the terms of the exposure give the lender a substantial degree of control over the asset or assets being financed and the income that the asset or assets generate; *(L.N. 167 of 2023)*

specific risk-weight approach (特定風險權重計算法) means an approach under which an authorized institution calculates its credit risk in accordance with Division 8 for non-securitization exposures which do not fall within the IRB class of corporate, sovereign, bank, retail or CIS exposures; *(L.N. 167 of 2023)*

substitution framework (替代框架), in relation to an exposure of an authorized institution, means the method set out in sections 215, 216 and 217 for taking into account the credit risk mitigating effect of a recognized guarantee or recognized credit derivative contract;

supervisory estimate (監管性估計), in relation to an exposure of an authorized institution, means—

(a) the risk-weight specified in this Part in respect of the exposure; or

(b) the value specified in this Part of a credit risk component to be input into a risk-weight function to calculate the risk-weight to be allocated to the exposure under the use of the IRB approach;

supervisory slotting criteria approach (監管分類準則計算法) means an approach under which an authorized institution calculates its credit risk for specialized lending in accordance with section 158(2);

third-party approach (第三方計算法) has the meaning given by section 226ZG; *(L.N. 54 of 2022)*

total EL amount (EL總額), in relation to an authorized institution, means the sum of the institution's EL amounts attributed to corporate, sovereign, bank and retail exposures of the institution that are subject to the IRB approach; *(L.N. 167 of 2023)*

total eligible provisions (合資格準備金總額), in relation to an authorized institution, means the sum of the institution's eligible provisions attributed to corporate, sovereign, bank and retail exposures of the institution that are subject to the IRB approach. *(L.N. 167 of 2023)*

(L.N. 167 of 2023)

(2) For the purposes of an authorized institution calculating, in respect of an exposure of the institution, the EL or PD over a one-year period pursuant to these Rules, it shall be sufficient if the institution calculates its credit risk using the latest estimates of the EL or PD, as the case may be, made or generated at any time within the past 12 months if the institution has not received information which causes, or which could reasonably be expected to cause, the institution to consider there may have been a material variation in the EL or PD of the exposure, as the case may be (in which case the institution shall not use those estimates in such calculation).

(3) *(Repealed L.N. 167 of 2023)*

Division 2—Calculation of Credit Risk under IRB Approach, Exposures to be Covered in Calculation, and Classification of Exposures

140. Calculation of risk-weighted amount of exposures

(1) Subject to subsection (2) and section 141, an authorized institution must calculate the risk-weighted amount of the institution's exposure to credit risk by aggregating the figures derived from the application of subsections (1A), (1B), (1BA) and (1C). *(L.N. 156 of 2012; L.N. 54 of 2022)*

(1A) Subject to subsections (1B), (1BA) and (1C), the authorized institution must multiply the EAD of the exposure by the exposure's relevant risk-weight. *(L.N. 156 of 2012; L.N. 54 of 2022)*

(1B) For a CIS exposure constituting a deductible holding that is not deducted from the capital base of an authorized institution under Division 4 of Part 3, the institution must calculate the risk-weighted amount of the exposure in accordance with section 183. *(L.N. 167 of 2023)*

(1BA) For a CIS exposure not constituting a deductible holding, the authorized institution must calculate the risk-weighted amount of the exposure in accordance with Part 6B. *(L.N. 54 of 2022; L.N. 167 of 2023)*

(1C) For a counterparty credit risk exposure in respect of derivative contracts or SFTs— *(L.N. 44 of 2020)*

(a) the authorized institution must, if it has an IMM(CCR) approval for its transactions or contracts, calculate the risk-weighted amount of the counterparty credit risk exposure as the sum of— *(L.N. 167 of 2023)*

(i) the IMM(CCR) risk-weighted amount of the transactions or contracts concerned that are covered by the IMM(CCR) approval; and

(ii) the sum of the SA-CCR risk-weighted amount or SFT risk-weighted amount of the transactions or contracts concerned that are not covered by the IMM(CCR) approval or that fall within section 10B(5) or (7); and

(iii) *(Repealed L.N. 167 of 2023)*

(b) *(Repealed L.N. 167 of 2023)*

(c) the authorized institution must, if it does not have an IMM(CCR) approval for any of its transactions or contracts, calculate the risk-weighted amount of the counterparty credit risk exposure as the sum of—

(i) the sum of the SA-CCR risk-weighted amount; and

(ii) the SFT risk-weighted amount. *(L.N. 156 of 2012; L.N. 44 of 2020; L.N. 167 of 2023)*

(iii) *(Repealed L.N. 167 of 2023)*

(1D) For the purposes of subsection (1C), the authorized institution may, in the case of a default risk exposure in respect of long settlement transactions, determine the exposure's relevant risk-weight using the STC approach on a permanent basis. *(L.N. 156 of 2012)*

(1E) *(Repealed L.N. 167 of 2023)*

(2) An authorized institution may reduce the risk-weighted amount of an exposure by taking into account the effect of any recognized credit risk mitigation in respect of the exposure in accordance with Division 10.

140A. Calculation of exposure at default

(1) Subject to subsection (2), an authorized institution must estimate the EAD of exposures under this Part in accordance with section 163, 164, 165, 166, 179, 180, 181, 182, 183, 195, 196, 197, 201 or 202, or Part 6A, as appropriate. *(L.N. 156 of 2012; L.N. 44 of 2020)*

(2) For the purposes of subsection (1), for estimating the EAD of on-balance sheet exposures that are measured at fair value—

(a) in respect of sections 163 and 164, a reference to current drawn amount is a reference to the value determined in accordance with section 4A; and

(b) in respect of section 183, an authorized institution must determine the EAD of a CIS exposure constituting deductible holding as the value of the deductible holding determined in accordance with section 4A. *(L.N. 167 of 2023)*

(L.N. 137 of 2011)

141. Exposures to be covered

(1) Subject to subsection (2) and section 12, if the Monetary Authority grants an approval to an authorized institution to use the IRB approach for one or more IRB adoption classes to calculate its credit risk for non-securitization exposures, the institution must, for the purpose of calculating under section

140 an amount representing the degree of credit risk to which it is exposed, take into account and risk-weight—

(a) all of the institution's exposures booked in its banking book within the IRB adoption class for which the approval is granted; and

(b) all of the institution's following exposures within the IRB adoption class for which the approval is granted—

(i) default risk exposures to counterparties in respect of derivative contracts or SFTs booked in its trading book;

(ii) credit exposures to counterparties in respect of transactions (other than repo-style transactions) in securities, foreign exchange or commodities booked in its trading book that remain outstanding after the settlement dates in respect of the transactions;

(iii) credit exposures to counterparties in respect of unsegregated collateral posted by it and held by the counterparties for transactions or contracts booked in its trading book.

(2) Subsection (1) does not apply to—

(a) securitization exposures;

(b) the underlying exposures of eligible traditional securitization transactions (within the meaning of section 229) if the authorized institution opts to apply the treatment under section 230(1) to the underlying exposures;

(c) equity exposures;

(d) default fund contributions made to qualifying CCPs and non-qualifying CCPs (within the meaning of section 226V(1));

(e) default risk exposures to qualifying CCPs;

(f) exposures that are risk-weighted as if they were default risk exposures to qualifying CCPs under Division 4 of Part 6A; and

(g) any portion of an exposure (which may be all of the exposure) that is required to be deducted from any of the institution's CET1 capital, Additional Tier 1 capital and Tier 2 capital under Division 4 of Part 3.

(3) To avoid doubt, if an authorized institution uses a combination of the STC approach and the IRB approach to calculate its credit risk for non-securitization exposures (***exposures***), section 53 applies to the institution with respect to its exposures subject to the STC approach even though it does not use the STC approach to calculate the credit risk for all of its exposures.

(L.N. 167 of 2023)

142. Classification of exposures

(1) Subject to subsections (2) and (3), an authorized institution shall, in accordance with sections 143, 144 and 146— *(L.N. 167 of 2023)*

(a) classify each of its exposures which fall within section 141 into one only of the 6 IRB classes specified in column 2 of Table 16; and

(b) then, classify the exposures into one only of the 26 IRB subclasses specified in column 3 of Table 16. *(L.N. 212 of 2015; L.N. 54 of 2022; L.N. 167 of 2023)*

Table 16

Classes and Subclasses of Exposures under IRB Approach

Item	IRB class	IRB subclass
1.	Corporate exposures	(a) Specialized lending (project finance) *(L.N. 167 of 2023)* (b) Specialized lending (object finance) *(L.N. 167 of 2023)* (c) Specialized lending (commodities finance) *(L.N. 167 of 2023)* (d) Specialized lending (income-producing real estate) *(L.N. 167 of 2023)* (da) Specialized lending (high-volatility commercial real estate) *(L.N. 212 of 2015)* (e) Small-and-medium sized corporates (ea) Large corporates *(L.N. 167 of 2023)* (eb) Financial institutions treated as corporates *(L.N. 167 of 2023)* (f) Other corporates
2.	Sovereign exposures	(a) Sovereigns (b) Sovereign foreign public sector entities (c) Multilateral development banks
3.	Bank exposures	(a) Banks (excluding covered bonds) *(L.N. 167 of 2023)*

Item	IRB class	IRB subclass
		(b) Qualifying non-bank financial institutions *(L.N. 167 of 2023)*
		(c) Public sector entities (excluding sovereign foreign public sector entities)
		(d) Unspecified multilateral bodies *(L.N. 167 of 2023)*
		(e) Covered bonds *(L.N. 167 of 2023)*
4.	Retail exposures	(a) Small business retail exposures
		(b) Residential mortgages to individuals
		(c) Residential mortgages to property-holding shell companies
		(d) Qualifying revolving retail exposures (transactor) *(L.N. 167 of 2023)*
		(da) Qualifying revolving retail exposures (revolver) *(L.N. 167 of 2023)*
		(e) Other retail exposures to individuals
5.	CIS exposures *(L.N. 167 of 2023)*	CIS exposures *(L.N. 167 of 2023)*
6.	Other exposures	(a) Cash items
		(b) Other items

(2) For the purposes of complying with subsection (1), an authorized institution shall demonstrate to the satisfaction of the Monetary Authority that its methodology for classifying, in accordance with that subsection, exposures referred to in that subsection is reliable and consistent over time.

(3) Where an exposure of an authorized institution which has been classified under subsection (1) would, if section 143(3) or (3A) or 144(2), (4)(c) or (4A)(a) were to apply to it at any time subsequently, be reclassified under that subsection, the institution shall so reclassify the exposure unless— *(L.N. 167 of 2023)*

(a) in the case of an exposure denominated in a currency other than Hong Kong dollars, the exposure's falling within, or failure to remain within, the value threshold or exposure limit specified in that section arises solely as a result of short-term exchange rate fluctuations; or

(b) the outstanding balance of the exposure falls within the value threshold or exposure limit specified in that section primarily because of—

(i) repayments made by the obligor in respect of the exposure; or

(ii) write-offs made by the institution in respect of the outstanding balance of the exposure.

143. Corporate exposures

(1) Subject to subsection (4A), for the purposes of section 142(1) as read with Table 16— *(L.N. 212 of 2015)*

(a) an authorized institution's specialized lending shall fall within project finance if the institution looks primarily to the revenue generated by a single project funded by the lending, both as the source of repayment of, and as security for, the lending;

(b) an authorized institution’s specialized lending shall fall within object finance if the lending funds the acquisition of physical assets and the repayment of the lending is dependent on the cash flows generated by the assets which have been financed and pledged (or otherwise provided as security) or assigned to the institution;

(c) an authorized institution’s specialized lending shall fall within commodities finance if the lending is structured short-term lending to finance reserves, inventories, or receivables of exchange-traded commodities, and— *(L.N. 167 of 2023)*

(i) the repayment of the lending will be from the proceeds of the sale of the commodities; and

(ii) the obligor in respect of the exposure has no independent capacity to repay the lending;

(d) an authorized institution’s specialized lending shall fall within income-producing real estate if the lending funds the acquisition of real estate and the prospects for repayment and recovery of the lending depend primarily on the cash flows generated by the real estate acquired; *(L.N. 212 of 2015)*

(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 higher loss rate volatility compared to other types of specialized lending, and falls within any of the following descriptions—

(i) a commercial real estate exposure secured by any commercial real estate situated 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 situated 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 land acquisition, development or construction 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 of the exposure and the obligor in respect of the exposure does not have substantial equity at risk in the commercial real estate. *(L.N. 212 of 2015; L.N. 167 of 2023)*

(2) Where an authorized institution is not able to estimate the credit risk components as required in this Part for corporate exposures in respect of the institution's specialized lending, the institution shall use the supervisory slotting criteria approach to calculate the risk-weighted amount of such specialized lending in accordance with section 158(2).

(3) Subject to subsections (4), (4A), (4B) and (4C), for the purposes of section 142(1) as read with Table 16, an authorized institution may only classify an exposure to a corporate as a corporate exposure which falls within the IRB subclass of small-and-medium sized corporates if— *(L.N. 212 of 2015; L.N. 167 of 2023)*

(a) subject to paragraph (b), the corporate concerned has a reported total annual sales, in its latest annual financial statements, of less than $500 million; or *(L.N. 167 of 2023)*

(b) in any case where the corporate concerned is a member of a group of companies, the group of companies has a consolidated reported total annual sales, in the group's latest consolidated annual financial statements, of less than $500 million. *(L.N. 167 of 2023)*

(c) *(Repealed L.N. 167 of 2023)*

(3A) Subject to subsections (3B), (4A), (4B) and (4C), for the purposes of section 142(1) as read with Table 16, an authorized institution may only classify an exposure to a corporate as a corporate exposure that falls within the IRB subclass of large corporates if—

(a) subject to paragraph (b), the corporate concerned has a reported total annual revenue, in its audited annual financial statements, of more than $5 billion; or

(b) in any case where the corporate concerned is a member of a group of companies, the group of companies has a consolidated reported total annual revenue, in the group's audited consolidated annual financial statements, of more than $5 billion. *(L.N. 167 of 2023)*

(3B) The reported total annual revenue referred to in subsection (3A) must be either an average amount of the annual revenue of the corporate or the group concerned in the past 3 years or the latest amount of the annual revenue updated every 3 years by an authorized institution. *(L.N. 167 of 2023)*

(3C) Subject to subsections (4A) and (4B), for the purposes of section 142(1) as read with Table 16, an authorized institution may only classify an exposure to a corporate as a corporate exposure that falls within the IRB subclass of financial institutions treated as corporates if the corporate is a financial institution treated as corporate. *(L.N. 167 of 2023)*

(4) Where an authorized institution demonstrates to the satisfaction of the Monetary Authority, in respect of a

corporate to which the institution has an exposure, that the corporate's scale of business is not accurately reflected in the corporate's total annual sales, the institution may, with the prior consent of the Monetary Authority, substitute the corporate's total assets for total annual sales in determining whether the exposure falls within subsection (3) in respect of that corporate. *(L.N. 167 of 2023)*

(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);

(b) be classified as exposures that fall within the IRB subclass of small-and-medium sized corporates under subsection (3); *(L.N. 212 of 2015; L.N. 167 of 2023)*

(c) be classified as exposures that fall within the IRB subclass of large corporates under subsection (3A); or *(L.N. 167 of 2023)*

(d) be classified as exposures that fall within the IRB subclass of financial institutions treated as corporates under subsection (3C). *(L.N. 167 of 2023)*

(4B) 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)(a), (b), (c) or (d) as exposures that fall within the IRB subclass of specialized lending (project finance), specialized lending (object finance), specialized lending (commodities finance) or specialized lending (income-producing real estate) respectively, whether or not the exposures may be classified as exposures that fall within—

(a) the IRB subclass of small-and-medium sized corporates under subsection (3);

(b) the IRB subclass of large corporates under subsection (3A); or

(c) the IRB subclass of financial institutions treated as corporates under subsection (3C). *(L.N. 167 of 2023)*

(4C) 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 (3C) as exposures that fall within the IRB subclass of financial institutions treated as corporates, whether or not the exposures may be classified as exposures that fall within—

(a) the IRB subclass of small-and-medium sized corporates under subsection (3); or

(b) the IRB subclass of large corporates under subsection (3A). *(L.N. 167 of 2023)*

(5) For the purposes of section 142(1) as read with Table 16, an authorized institution shall classify all of its exposures to corporates which do not fall within—

(a) the IRB subclass of specialized lending under subsection (1); *(L.N. 167 of 2023)*

(b) the IRB subclass of small-and-medium sized corporates pursuant to subsection (3);

(ba) the IRB subclass of large corporates under subsection (3A); *(L.N. 167 of 2023)*

(bb) the IRB subclass of financial institutions treated as corporates under subsection (3C); *(L.N. 167 of 2023)*

(c) the IRB subclass of small business retail exposures pursuant to section 144(2); or

(d) the IRB subclass of residential mortgages to property-holding shell companies pursuant to section 144(3)(b),

as exposures which fall within the IRB subclass of other corporates.

(6) The Monetary Authority may categorize any type of commercial real estate situated 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. *(L.N. 212 of 2015)*

(7) For the purposes of subsection (1)(e)(iii)(B), there is uncertainty of repayment 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. *(L.N. 212 of 2015)*

144. Retail exposures

(1) For the purposes of section 142(1) as read with Table 16, an authorized institution may only classify an exposure as a retail exposure which falls within the IRB subclass of small business retail exposures, residential mortgages to individuals, residential mortgages to property-holding shell companies, qualifying revolving retail exposures (transactor), qualifying revolving retail exposures (revolver), or other retail exposures to individuals, as the case may be, if the exposure is included

in a pool of exposures managed by the institution on a pooled or portfolio basis. *(L.N. 167 of 2023)*

(2) Subject to subsection (1), for the purposes of section 142(1) as read with Table 16, an authorized institution may only classify an exposure to a corporate as a retail exposure which falls within the IRB subclass of small business retail exposures if the total exposure of the institution or its consolidation group to—

(a) subject to paragraph (b), the corporate;

(b) if applicable—

(i) a group of companies of which the corporate is a member; or

(ii) the corporate and other persons (including individuals) which are consolidated by the institution with the corporate for risk management purposes,

is less than $10 million.

(3) Subject to subsection (1), for the purposes of section 142(1) as read with Table 16—

(a) an authorized institution shall classify a residential mortgage loan to one or more than one individual as a retail exposure which falls within the IRB subclass of residential mortgages to individuals where the property securing the residential mortgage loan concerned is used, or intended for use, as the residence of the borrower or as the residence of a tenant, or a licensee, of the borrower;

(b) an authorized institution shall classify a residential mortgage loan to a property-holding shell company as a retail exposure which falls within the IRB subclass of residential mortgages to property-holding shell companies where—

(i) the property securing the residential mortgage loan concerned is used, or intended for use, as the residence of one or more than one director or shareholder of the property-holding shell company or as the residence of a tenant, or a licensee, of the property-holding shell company;

(ii) all of the borrowed-monies obligations of the property-holding shell company arising under the residential mortgage loan concerned are the subject of a personal guarantee—

(A) which is entered into by one or more than one director or shareholder of the property-holding shell company (referred to in this paragraph as ***guarantor***); and

(B) which fully and effectively covers those obligations;

(iii) the institution, having due regard to the guarantor's financial obligations (including, in particular, all the guarantor's borrowed-monies obligations and obligations of suretyship), is satisfied that the guarantor is able to perform all the guarantor's obligations under the guarantee; and

(iv) the residential mortgage loan concerned made available to the property-holding shell company has been assessed by reference to substantially similar credit underwriting standards (including loan purpose, and loan-to-value and debt-service ratios) as would normally be applied by the institution to an individual.

(4) Subject to subsection (1), for the purposes of section 142(1) as read with Table 16, an authorized institution shall classify an exposure as a retail exposure which falls within the IRB subclass of qualifying revolving retail exposures (transactor) if— *(L.N. 167 of 2023)*

(a) the exposure is revolving, unsecured, and unconditionally cancellable (both contractually and in practice) by the institution;

(b) the exposure is to one or more than one individual and not explicitly for business purposes;

(c) the exposure is not more than $1 million;

(d) the exposure belongs to a pool of exposures which have exhibited, in comparison with other IRB subclasses of retail exposures, low loss rate volatility, relative to the institution's average level of loss rates for retail exposures, especially within the pools to which low estimates of PD are attributed;

(e) data on loss rates for qualifying revolving retail exposures are retained by the institution in order to allow analysis of the volatility of loss rates; *(L.N. 167 of 2023)*

(f) treatment of the exposure as falling within the IRB subclass of qualifying revolving retail exposures (transactor) is consistent with the underlying risk characteristics of the exposure; and *(L.N. 167 of 2023)*

(g) the exposure is to an obligor who is a transactor. *(L.N. 167 of 2023)*

(4A) Subject to subsection (1), for the purposes of section 142(1) as read with Table 16, an authorized institution must classify an exposure as a retail exposure that falls within the IRB subclass of qualifying revolving retail exposures (revolver) if—

(a) the requirements set out in subsection (4)(a), (b), (c), (d) and (e) are satisfied;

(b) treatment of the exposure as falling within the IRB subclass of qualifying revolving retail exposures (revolver) is consistent with the underlying risk characteristics of the exposure; and

(c) the exposure does not fall within the IRB subclass of qualifying revolving retail exposures (transactor). *(L.N. 167 of 2023)*

(5) Subject to subsections (1) and (6), for the purposes of section 142(1) as read with Table 16, an authorized institution shall classify all of its exposures to individuals which do not fall within—

(a) the IRB subclass of residential mortgages to individuals;

(b) the IRB subclass of qualifying revolving retail exposures (transactor); or *(L.N. 167 of 2023)*

(c) the IRB subclass of qualifying revolving retail exposures (revolver), *(L.N. 167 of 2023)*

as exposures which fall within the IRB subclass of other retail exposures to individuals.

(6) An authorized institution shall treat any of its exposures to individuals which are not managed by the institution on a pooled or portfolio basis in accordance with subsection (1) as corporate exposures.

145. *(Repealed L.N. 167 of 2023)*

146. Other exposures

(1) Subject to subsection (2), for the purposes of section 142(1) as read with Table 16, an authorized institution shall classify under the IRB class of other exposures any of the institution’s

exposures which do not fall within the IRB class of corporate, sovereign, bank, retail or CIS exposures. *(L.N. 137 of 2011; L.N. 167 of 2023)*

(2) For the purposes of section 142(1) as read with Table 16, an authorized institution must classify under the IRB subclass of other items—

(a) any of the institution's other exposures that do not fall within the IRB subclass of cash items. *(L.N. 156 of 2012)*

(b) *(Repealed L.N. 156 of 2012)*

Division 3—IRB Calculation Approaches

147. IRB calculation approaches

(1) Subject to subsections (2), (3) and (3B), an authorized institution shall, for the purposes of calculating the risk-weighted amount of its exposures, select IRB calculation approaches from the range of IRB calculation approaches set out in Table 17 available for each of the 6 IRB classes. *(L.N. 167 of 2023)*

Table 17

IRB Calculation Approaches

Item	IRB class	IRB calculation approach
1.	Corporate exposures	(a) Foundation IRB approach
		(b) Advanced IRB approach
		(c) Supervisory slotting criteria approach

Item	IRB class	IRB calculation approach
2.	Sovereign exposures	(a) Foundation IRB approach (b) Advanced IRB approach
3.	Bank exposures	Foundation IRB approach *(L.N. 167 of 2023)*
4.	Retail exposures	Retail IRB approach
5.	CIS exposures *(L.N. 167 of 2023)*	CIS calculation approach *(L.N. 167 of 2023)*
6.	Other exposures	Specific risk-weight approach

(2) An authorized institution shall not select an IRB calculation approach set out in Table 17 unless the institution satisfies the requirements specified in this Part applicable to or in relation to that IRB calculation approach.

(3) Subject to subsection (3A), if, under these Rules, an authorized institution may use more than one IRB calculation approach set out in Table 17 to calculate its credit risk for exposures which fall within an IRB class, the institution shall not, except with the prior consent of the Monetary Authority— *(L.N. 167 of 2023)*

(a) use more than one such IRB calculation approach to calculate its credit risk for exposures which fall within that IRB class; or

(b) discontinue using one such IRB calculation approach, and commence using another such IRB calculation approach, to calculate its credit risk for exposures which fall within that IRB class.

(3A) If an authorized institution used the advanced IRB approach before the commencement date* of Part 3 of the Banking (Capital) (Amendment) Rules 2023 for—

(a) exposures to corporates that satisfy the requirements set out in section 143(3A)(a) or (b);

(b) exposures to corporates that are financial institutions treated as corporates; or

(c) bank exposures,

the institution is not required to obtain the prior consent of the Monetary Authority under subsection (3) to commence using the foundation IRB approach to calculate its credit risk for those exposures on and after that date. *(L.N. 167 of 2023)*

(3B) An authorized institution must not use the advanced IRB approach to calculate its credit risk for exposures to corporates that satisfy the requirements set out in section 143(3A)(a) or (b) and corporates that are financial institutions treated as corporates. *(L.N. 167 of 2023)*

(3C) Despite section 8(4)(a), if an authorized institution used the IRB approach before the commencement date of Part 3 of the Banking (Capital) (Amendment) Rules 2023 to calculate its credit risk for equity exposures (within the meaning of the pre-amended Part 6), the institution must use the STC approach on and after that date to calculate its credit risk for equity exposures. *(L.N. 167 of 2023)*

(4) An authorized institution shall—

(a) subject to paragraphs (b) and (c), only use more than one rating system for exposures which fall within an IRB class if the institution demonstrates to the satisfaction of the Monetary Authority that the rating systems concerned are necessary having regard to the characteristics and complexity of those exposures;

(b) only assign an exposure to a rating system referred to in paragraph (a) if that rating system accurately reflects the level of credit risk of the exposure; and

(c) document the reason for assigning an exposure to a particular rating system.

(5) In this section—

pre-amended Part 6 (原有的第6部) means Part 6 of these Rules as in force immediately before the commencement date of Part 3 of the Banking (Capital) (Amendment) Rules 2023. *(L.N. 167 of 2023)*

Editorial Note:

* Commencement date: 1 January 2025.

Division 4—Risk-weighting Framework under IRB Approach

148. General requirements for estimation of probability of default, loss given default and exposure at default

An authorized institution shall, for the purposes of making estimates of PD and, where relevant, LGD and EAD (collectively referred to in this Division as ***estimates***)—

(a) conduct periodic assessments of its risk quantification process and update the process as necessary to ensure that new data and analytical techniques and evolving industry practices are incorporated into the process;

(b) update the institution's estimates produced by the institution's risk quantification process not less than once in every 12 months;

(c) base the institution's estimates on historical experience and empirical evidence and not only on subjective or judgmental considerations, take into account all relevant data and information available and use appropriate methods;

(d) demonstrate to the satisfaction of the Monetary Authority that the data the institution uses in its estimates (whether internal data or external data, or both)—

(i) are representative of its long run default experience and long run loss experience (covering a period which captures a reasonable mix of high-default and low-default years of at least one economic cycle); and

(ii) are based on economic or market conditions which are relevant to current and foreseeable economic or market conditions;

(e) ensure that adjustments to the estimates, based on data which fall within paragraph (d)—

(i) are only made or approved by officers of the institution with the necessary experience and expertise to make or approve such adjustments and who have been authorized by the institution to make or approve such adjustments; and

(ii) form part of the institution's risk quantification process and are based on the exercise in good faith of judgment by officers who fall within subparagraph (i) and are not biased towards reducing the institution's regulatory capital for credit risk; and

(f) demonstrate to the satisfaction of the Monetary Authority that the institution has—

(i) a set of procedures to evaluate the appropriateness of the method or data used in making the estimates; and

(ii) a mechanism for increasing the estimates when the evaluation referred to in subparagraph (i) indicates that the estimates fail to satisfy the institution's internal standards on the accuracy of estimates used by the institution.

149. Default of obligor

(1) Subject to subsection (4), for the purposes of this Part, a default of the obligor in respect of an exposure of an authorized institution has occurred if— *(L.N. 137 of 2011)*

(a) the institution considers that the obligor is unlikely to pay in full the obligor's credit obligations to the institution (or to any member of the consolidation group of the institution) without recourse by the institution to realizing any collateral held by the institution or taking any other action in respect of the exposure; or

(b) subject to subsections (2), (3) and (8), the obligor is past due for more than 90 days in respect of the payment of any material portion of all of the obligor's outstanding credit obligations to the institution (or to any member of the consolidation group of the institution).

(1A) For the purposes of subsection (1)(a), an authorized institution may regard an obligor as being unlikely to pay in full its credit obligations to the institution if one or more of the following events have occurred in respect of the obligor—

(a) any material credit obligation is put on non-accrued status;

(b) a write-off or specific provision is made as a result of a significant perceived decline in credit quality subsequent to the institution taking on any credit exposure to the obligor;

(c) any credit obligation is sold at a material credit-related economic loss;

(d) a distressed restructuring of any credit obligation is agreed by the institution;

(e) a filing for the obligor's bankruptcy or a similar order has been made in respect of any of the obligor's credit obligations to the institution or any member of the consolidation group of the institution;

(f) the obligor has sought, or has been placed in, bankruptcy or similar protection where this would avoid or delay repayment of any of the credit obligations to the institution or any member of the consolidation group of the institution. *(L.N. 167 of 2023)*

(2) Where the obligor in respect of a retail exposure is past due for more than 90 days in respect of any payment owing by the obligor in respect of that exposure—

(a) subject to paragraph (b), an authorized institution—

(i) must treat the exposure as being in default; and

(ii) may treat all other outstanding credit obligations of the obligor to the institution (or to any member of the consolidation group of the institution) as being in default; *(L.N. 137 of 2011; L.N. 156 of 2012)*

(b) the institution shall disregard paragraph (a) if the obligor is also past due for more than 90 days in respect of any payment owing by the obligor in respect of any other exposure which is not a retail exposure.

(3) For the purposes of subsections (1)(b) and (2), an overdraft provided by an authorized institution to an obligor (being a borrower under the overdraft) is past due if—

(a) the obligor has breached a maximum limit which was set by the institution, and the institution has advised the obligor of the maximum limit;

(b) the institution has advised the obligor of a maximum limit which is less than the current outstanding balance of the overdraft; or

(c) the overdraft is not authorized by the institution.

(4) Subject to subsection (5), where an authorized institution intends to use, for a particular IRB class or IRB subclass of the institution, the default criteria (not being the prescribed default criteria) set by the relevant banking supervisory authority of the institution's parent bank, the institution shall not use those default criteria except with the prior consent of the Monetary Authority.

(5) The Monetary Authority shall not give an authorized institution the consent referred to in subsection (4) to use the default criteria referred to in that subsection in respect of a particular IRB class or IRB subclass of the institution unless the institution demonstrates to the satisfaction of the Monetary Authority that the differences between those default criteria and the prescribed default criteria will not materially affect the accuracy of the estimates generated by the institution's rating system.

(5A) Subject to subsections (5B), (5C) and (5D), an authorized institution must treat its exposures to all individual obligors in a connected group as being in default if—

(a) a default of an obligor (***defaulting obligor***) in the connected group has occurred; and

(b) the defaulting obligor has been rated substantially on the basis of the economic or financial interdependence between the members in the connected group in accordance with the institution's policy and practices referred to in section 154(d). *(L.N. 156 of 2012)*

(5B) Subsection (5A) does not apply in respect of the authorized institution's exposures to all obligors in the connected group if—

(a) the default referred to in paragraph (a) of that subsection (***relevant default***) is a default to which subsection (2)(a) applies by virtue of—

(i) the fact that the relevant default is a retail exposure in respect of which the defaulting obligor is past due for more than 90 days in respect of any payment owing by the obligor to the institution in respect of that exposure; and

(ii) the fact that the defaulting obligor is not also past due for more than 90 days in respect of any payment owing by the obligor to the institution in respect of any other exposure that is not a retail exposure; and

(b) the institution has not, following the occurrence of the relevant default, exercised its discretion under subsection (2)(a)(ii) to treat all other outstanding credit obligations of the defaulting obligor to the institution (or to any member of the consolidation group of the institution) as being in default. *(L.N. 156 of 2012)*

(5C) The authorized institution may disregard subsection (5A) in respect of the institution's exposures to any obligor in the connected group if that obligor has not been rated on the basis referred to in paragraph (b) of that subsection. *(L.N. 156 of 2012)*

(5D) The authorized institution may disregard subsection (5A) in respect of the institution's exposures to any obligor in the connected group if the institution demonstrates to the satisfaction of the Monetary Authority that disregarding that subsection in respect of those exposures—

(a) is neither imprudent nor unreasonable; and

(b) will not materially prejudice the calculation of the institution's regulatory capital for credit risk. *(L.N. 156 of 2012)*

(6) Subject to subsection (7), an authorized institution shall—

(a) keep a record of defaults in exposures of the institution using the prescribed default criteria;

(b) use the prescribed default criteria to generate the estimates from the institution's rating system; and

(c) only use internal data (to the extent that such data had come into existence before 1 January 2007) or external data which are inconsistent with the prescribed default criteria if the institution demonstrates to the satisfaction of the Monetary Authority that it has made adjustments to the data such that the data are consistent with the prescribed default criteria. *(L.N. 128 of 2014)*

(7) Subsection (6) applies to and in relation to an authorized institution which uses the default criteria referred to in subsection (4) as it applies to and in relation to an authorized institution which uses the prescribed default criteria.

(8) An authorized institution shall not engage in the practice of re-ageing for the purposes of subsection (1).

(9) In this section—

distressed restructuring (不利的重組) has the meaning given by section 67(7); *(L.N. 167 of 2023)*

non-accrued status (非累算狀況) has the meaning given by section 67(7); *(L.N. 167 of 2023)*

prescribed default criteria (訂明違責準則) means the criteria specified in subsection (1);

rated (受評級), in relation to an obligor of an authorized institution, means that the institution's corporate, sovereign or bank exposures to the obligor have been assigned to obligor grades by using the IRB approach. *(L.N. 137 of 2011)*

Division 5—Specific Requirements for Corporate, Sovereign and Bank Exposures

150. Rating dimensions

(1) Subject to subsection (4), an authorized institution shall ensure that its rating system for corporate, sovereign and bank exposures has 2 distinct and separate rating scales, comprising—

(a) obligor grades which reflect, exclusively, the risk of default of obligors; and

(b) facility grades which reflect—

(i) transaction-specific factors affecting loss severity in the case of default of obligors; and

(ii) where relevant, the characteristics of obligors to the extent that the characteristics are predictive of LGD.

(2) An authorized institution which uses the foundation IRB approach shall be regarded as complying with subsection (1)(b) if its rating system for corporate, sovereign and bank exposures has a rating scale which reflects the EL of exposures assigned to each grade.

(3) An authorized institution shall, in respect of its corporate, sovereign and bank exposures—

(a) rank and assign each exposure to the obligor grades and facility grades in accordance with its rating criteria and based on all relevant information available regarding the creditworthiness of the obligor or loss severity of the exposure; and

(b) assign the same obligor grade to separate exposures to the same obligor unless the institution demonstrates to the satisfaction of the Monetary Authority that the risk of default of the obligor in respect of such exposures is different.

(4) An authorized institution may use a rating system for its specialized lending under supervisory slotting criteria approach which reflects EL by incorporating considerations about the creditworthiness of obligors and loss severity in respect of such lending.

151. Rating structure

(1) An authorized institution shall ensure that its process for assigning corporate, sovereign and bank exposures to its obligor grades or facility grades results in a consistent, logical and cogent differentiation of credit risk inherent in those exposures—

(a) with no excessive concentrations on particular obligor grades or facility grades;

(b) with the level of perceived and measured credit risk increasing as credit quality declines from one grade to the next; and

(c) allowing for reasonably accurate, consistent and verifiable estimation of credit risk components for each exposure.

(2) Subject to subsection (3), an authorized institution shall ensure that its rating system for corporate, sovereign and bank exposures has—

(a) not less than 7 obligor grades for exposures to obligors who are not in default; and

(b) not less than one obligor grade for exposures to obligors who are in default.

(3) Where an authorized institution uses the supervisory slotting criteria approach for its specialized lending, the institution shall ensure that its rating system has—

(a) not less than 4 obligor grades for specialized lending to obligors who are not in default; and

(b) not less than one obligor grade for specialized lending to obligors who are in default.

152. Rating criteria

An authorized institution shall ensure that—

(a) its rating definitions in respect of obligor grades and facility grades; and

(b) its rating processes and criteria for assigning exposures to such grades,

are specific, logical, sufficiently detailed and consistently applied and result in a clear differentiation of credit risk inherent in the exposures.

153. Rating assignment horizon

An authorized institution shall—

(a) use a time horizon of more than one year for the purposes of assigning its exposures to obligor grades;

(b) subject to paragraph (c), ensure that the obligor grade to which an exposure is assigned accurately represents the institution's assessment of the willingness and ability of an obligor in respect of the exposure to perform the obligor's contractual obligations, after taking into account any potentially adverse economic conditions over an economic cycle within the industry or geographic region relevant to the obligor; *(L.N. 267 of 2006; L.N. 156 of 2012)*

(c) act prudently in assessing information relating to the willingness and ability of an obligor in respect of an exposure to perform the obligor's contractual obligations; and *(L.N. 156 of 2012)*

(d) when estimating the PD for an obligor that is highly leveraged or whose assets are predominantly traded assets, ensure such estimate reflects the performance of the obligor's assets based on volatilities calibrated to data from periods of significant financial stress. *(L.N. 156 of 2012)*

154. Rating coverage

An authorized institution shall—

(a) in the case of each exposure which falls within the IRB classes of corporate, sovereign and bank exposures, assign the exposure to an obligor grade or facility grade as part of the institution's process for giving credit approvals; *(L.N. 137 of 2011)*

(b) in the case of each obligor to whom the institution has a corporate, sovereign or bank exposure, assign the exposure to the obligor grade which accurately reflects the level of credit risk of the obligor in respect of the exposure; *(L.N. 137 of 2011)*

(c) subject to paragraphs (d) and (e), rate on an individual basis each legal entity to which the institution is exposed; *(L.N. 156 of 2012)*

(d) for the purposes of paragraph (c), demonstrate, to the satisfaction of the Monetary Authority, that its policy and practices regarding the assignment of exposures to obligor grades in respect of individual obligors in a connected group—

(i) are prudent and reasonable;

(ii) set out, at the least—

(A) the circumstances under which the institution may or may not assign the same obligor grade in respect of exposures to separate obligors in a connected group; and

(B) the definition of a connected group for the purposes of rating assignment; and

(iii) are applied in a consistent manner; and *(L.N. 137 of 2011; L.N. 156 of 2012)*

(e) set out in policies and put into operation a process for the identification of specific wrong-way risk for each legal entity to which the institution is exposed. *(L.N. 156 of 2012)*

155. Integrity of rating process

An authorized institution shall ensure that—

(a) the institution has in place policies and procedures to ensure that the rating process for corporate, sovereign and bank exposures is independent of the institution's staff and management responsible for originating such exposures;

(b) the assignment of exposures to obligor grades and facility grades is reviewed and updated not less than once in every 12 months and exposures to obligors which are more likely to default are subject to more frequent review and updating;

(c) whenever the institution becomes aware of any new material information on an exposure (including in relation to the obligor in respect of that exposure), a review is conducted, within a reasonable period after the institution becomes so aware, of whether the exposure should be assigned to a different obligor grade or facility grade, as the case may be;

(d) the institution has in place an effective process to obtain and update relevant information on the financial conditions and on other credit risk characteristics of the obligors in respect of the institution's exposures which affect assigned estimates of PD, LGD and EAD; and

(e) the institution has in place an effective process for—

(i) identifying, documenting, reviewing and updating the circumstances in which it is appropriate for officers of the institution to override the inputs to, or the outputs of, the institution's rating system; *(L.N. 137 of 2011)*

(ii) ensuring that such circumstances are prudent; *(L.N. 137 of 2011)*

(iii) ensuring that all permissible overrides are approved by officers of the institution having delegated credit authority and are applied in a consistent manner; and *(L.N. 137 of 2011)*

(iv) monitoring the nature and performance of such overrides following approval. *(L.N. 137 of 2011)*

156. Calculation of risk-weighted amount of corporate, sovereign and bank exposures

(1) An authorized institution shall, for the purposes of calculating the risk-weighted amount of the institution's corporate, sovereign and bank exposures—

(a) subject to section 167(1)(c), if the institution uses the foundation IRB approach, provide its own estimate of the PD of each of its obligor grades and use supervisory estimates for the other credit risk components for inclusion into the risk-weight function to be used in that calculation; *(L.N. 167 of 2023)*

(b) if the institution uses the advanced IRB approach, provide its own estimate of the PD, LGD and EAD of each of its obligor grades and facility grades, as the case may be, and calculate the M of its exposures for inclusion into the risk-weight function to be used in that calculation; and

(c) if the institution uses the supervisory slotting criteria approach to calculate the risk-weighted amount of its specialized lending, use the relevant supervisory estimate for the risk-weight to be allocated to the specialized lending.

(2) Subject to subsection (5A) and section 158(2), an authorized institution shall use Formula 16 to calculate the risk-weighted amount of the institution's corporate, sovereign and bank exposures which are not in default. *(L.N. 156 of 2012; L.N. 167 of 2023)*

Formula 16

Risk-weight Function for Corporate, Sovereign and Bank Exposures

Correlation (R)	=	0.12 × (1 – EXP (–50 × PD)) / (1 – EXP (–50)) + 0.24 × [1 – (1 – EXP (–50 × PD)) / (1 – EXP (–50))]
Maturity adjustment (b)	=	(0.11852 – 0.05478 × 1n (PD))^2

Capital charge factor (K)	=	[LGD× N[(1 – R)^–0.5 × G(PD) + (R / (1 – R))^0.5 × G(0.999)] – PD × LGD] × (1 – 1.5 × b)^– 1 × (1 + (M – 2.5) × b)
Risk-weight (RW)	=	K × 12.5
Risk-weighted amount	=	RW × EAD

where—

(a) PD and LGD are expressed in decimals, EAD is expressed in Hong Kong dollars and M is expressed in years;

(b) EXP denotes exponential;

(c) 1n denotes the natural logarithm;

(d) N(x) denotes the cumulative distribution function for a standard normal random variable; and

(e) G(z) denotes the inverse cumulative distribution function for a standard normal random variable.

(3) An authorized institution shall apply a zero capital charge factor (K) to a sovereign exposure of the institution if the calculation required under this section in respect of the exposure results in a negative capital charge factor (K) for the exposure.

(4) Subject to section 158(2), an authorized institution shall use the same risk-weight function set out in Formula 16 to calculate the risk-weighted amount of the institution’s corporate, sovereign and bank exposures which are in default except that the capital charge factor (K) for a defaulted corporate, sovereign or bank exposure shall be equal to the greater of—

(a) zero; or

(b) the figure resulting from the subtraction of the institution's best estimate of the EL of the exposure from the LGD of the exposure.

(5) *(Repealed L.N. 167 of 2023)*

(5A) Where an exposure falls within section 140(1D), an authorized institution may calculate the risk-weighted amount of the exposure by multiplying the EAD of the exposure by the relevant risk-weight attributable to that exposure determined under Part 4. *(L.N. 156 of 2012)*

(6)-(10) *(Repealed L.N. 167 of 2023)*

157. Provisions supplementary to section 156(2)—firm-size adjustments for small-and-medium sized corporates

(L.N. 167 of 2023)

(1) If a corporate exposure of an authorized institution falls within the IRB subclass of small-and-medium sized corporates, the institution must make an adjustment to take into account the size of the corporate concerned (***firm-size adjustment***) to the calculation of the correlation (R) in the risk-weight function specified in Formula 16 by substituting the following correlation formula for that in Formula 16—

Correlation (R) = 0.12 × (1 – EXP (–50 × PD)) / (1 – EXP (–50)) + 0.24 ×[1 – (1 – EXP (–50 × PD)) / (1 – EXP (–50))] – 0.04 ×(1 – (S – 50) / 450). *(L.N. 167 of 2023)*

(2) In the correlation formula set out in subsection (1), S is expressed in terms of a million as— *(L.N. 267 of 2006; L.N. 167 of 2023)*

(a) subject to paragraph (b), the total annual sales of the corporate; or

(b) in any case where the corporate concerned is a member of a group of companies, the consolidated total annual sales of the group of companies of which the corporate is a member,

(c) *(Repealed L.N. 167 of 2023)*

of not less than \$50 million to not more than \$500 million.

(3) Where any total annual sales referred to in subsection (2) is less than \$50 million, the authorized institution concerned shall, for the purposes of that subsection, treat the total annual sales as if it were \$50 million.

(4) Where an authorized institution demonstrates to the satisfaction of the Monetary Authority that the total annual sales of a corporate does not accurately reflect the corporate's scale of business, then, for the purposes of this section, the institution may, with the prior consent of the Monetary Authority, substitute the corporate's total assets for the total annual sales in calculating the firm-size adjustment.

(5) If an authorized institution's specialized lending or its exposure that falls within the IRB subclass of financial institutions treated as corporates would have been 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), (4B) and (4C)—

(a) the institution may make a firm-size adjustment referred to in subsection (1) to the calculation of the correlation (R) in the risk-weight function specified in Formula 16 in respect of the exposure; and

(b) subsections (2), (3) and (4) apply accordingly. *(L.N. 167 of 2023)*

(L.N. 167 of 2023)

157A. Provisions supplementary to section 156(2)—asset value

correlation multiplier for exposures to certain financial institutions

(L.N. 167 of 2023)

(1) Subsection (2) applies to an obligor that is—

(a) a large regulated financial institution; or

(b) a financial institution that is not supervised by a financial regulator.

(2) Where a corporate, sovereign or bank exposure of an authorized institution is to an obligor to which this subsection applies, the institution must multiply the correlation (R) in the risk-weight function specified in Formula 16 by 1.25. *(L.N. 167 of 2023)*

(3) In this section—

financial regulator (金融監管者) means a regulatory authority that imposes supervisory standards (including supervisory standards relating to capital and liquidity) that are substantially consistent with international standards;

large regulated financial institution (大型受監管金融機構) means a financial institution that is supervised by a financial regulator and that—

(a) has total assets of not less than $780 billion as determined by reference to the institution's most recent audited consolidated financial statements or (if the institution does not have any subsidiary) the institution's most recent audited financial statements; or

(b) is a member of a group of companies (comprised of the ultimate holding company and all of its subsidiaries) that has total assets of not less than $780 billion as determined by reference to the group's most recent audited consolidated financial statements.

(L.N. 156 of 2012; L.N. 167 of 2023)

158. Provisions supplementary to section 156—risk-weights for specialized lending

(1) Subject to subsections (1A), (1B) and (1C), where an authorized institution is able to comply with— *(L.N. 212 of 2015)*

(a) section 159 in relation to the estimation of PD under the foundation IRB approach of any of its specialized lending; or

(b) sections 159, 161, 164 and 168 in relation to the estimation of PD, LGD and EAD and the calculation of M under the advanced IRB approach of any of its specialized lending,

the institution shall use the risk-weight function specified in Formula 16 (if applicable, adjusted in accordance with section 157(5) in respect of specialized lending that falls within that section 157(5) or section 157A in respect of exposures to obligors that fall within any of the descriptions in section 157A(1)(a) and (b)) to derive the risk-weighted amount of such specialized lending. *(L.N. 167 of 2023)*

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

(a) the value of 0.24 in the correlation (R) in the risk-weight function specified in Formula 16 is to be replaced by a value of 0.3;

(b) if section 157(5) is applicable, the value of 0.24 in the correlation (R) in section 157(1) is to be replaced by a value of 0.3; and

(c) if section 157A is applicable, a reference to Formula 16 in that section is a reference to the Formula as adjusted under paragraph (a) or (b). *(L.N. 212 of 2015; L.N. 167 of 2023)*

(1B) An authorized institution that falls within subsection (1)(b) in respect of any of its HVCRE exposures must not use the advanced IRB approach to derive the risk-weighted amount of any of such exposures if both of the following circumstances (***triggering circumstances***) occur—

(a) the institution has material income-producing real estate exposures;

(b) the institution does not use the advanced IRB approach to derive the risk-weighted amount of all of its exposures falling within the IRB subclass of specialized lending (income-producing real estate). *(L.N. 212 of 2015; L.N. 167 of 2023)*

(1C) Despite subsection (1B), if an authorized institution started to use the advanced IRB approach to derive the risk-weighted amount of any of its HVCRE exposures at a time when it did not have any material income-producing real estate exposure, even if both of the triggering circumstances subsequently occur in respect of it, it may continue to so use the advanced IRB approach until the expiry of 6 months after the date on which it becomes aware of the occurrence of the circumstances. *(L.N. 212 of 2015)*

(2) Where an authorized institution does not fall within subsection (1) in respect of any of its specialized lending, the institution shall—

(a) use the supervisory slotting criteria approach to derive the risk-weighted amount of such specialized lending;

(b) assign any internal grade to such specialized lending based on the institution’s criteria, systems and processes;

(c) map the internal grades assigned to specialized lending referred to in paragraph (b) to one of the 5 supervisory rating grades of “strong”, “good”, “satisfactory”, “weak” and “default” set out in Table 18 or 18A, whichever is applicable, by reference to— *(L.N. 212 of 2015)*

(i) the criteria specified in paragraphs CRE33.13 to CRE33.16 in Chapter CRE33 of the consolidated Basel Framework launched by the Basel Committee as amended or supplemented from time to time; or *(L.N. 167 of 2023)*

(ii) the credit quality grades specified in a table made by the Monetary Authority under section 4B(2); *(L.N. 167 of 2023)*

(d) subject to subsections (3) and (4), apply the risk-weight specified in Table 18 or 18A, whichever is applicable, for the relevant supervisory rating grade in calculating the risk-weighted amount of such specialized lending.

Table 18

Supervisory Rating Grades for Determination of Risk-weights for Specialized Lending other than HVCRE Exposures

(L.N. 212 of 2015)

	Strong	Good	Satisfactory	Weak	Default
Credit quality grade	1	2	3	4	Not applicable
Risk-weight	70%	90%	115%	250%	0%

Table 18A

Supervisory Rating Grades for Determination of Risk-weights for HVCRE Exposures

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

(L.N. 212 of 2015)

(3) An authorized institution may allocate a risk-weight of 50% to its specialized lending (other than HVCRE exposures and specified ADC exposures) which falls into the supervisory rating grade of "strong" in Table 18, and a risk-weight of 70% to its specialized lending (other than HVCRE exposures and specified ADC exposures) which falls into the supervisory rating grade of "good" in Table 18, if— *(L.N. 212 of 2015; L.N. 167 of 2023)*

(a) the specialized lending 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 specialized lending 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).

(4) An authorized institution may allocate 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— *(L.N. 167 of 2023)*

(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). *(L.N. 212 of 2015)*

(5) For the purposes of this section, an authorized institution has material income-producing real estate exposures if the average aggregate EAD of its exposures falling within the IRB subclass of specialized lending (income-producing real estate) over the past 12 months exceeds 5% of the institution's capital base as determined under Part 3. *(L.N. 212 of 2015; L.N. 167 of 2023)*

(6) In this section—

specified ADC exposure (指明ADC風險承擔) means a specialized lending—

(a) that finances the land acquisition, development or construction phase of commercial real estate (excluding commercial real estate of a type referred to in section 143(1)(e)(i) or (ii)) that exhibits higher loss rate volatility compared to other types of specialized lending; and

(b) in respect of which there is uncertainty of repayment within the meaning of section 143(7) but the obligor in respect of which has substantial equity at risk in the commercial real estate. *(L.N. 212 of 2015)*

(L.N. 156 of 2012; L.N. 212 of 2015; L.N. 167 of 2023)

159. Probability of default

(1) An authorized institution which uses the foundation IRB approach or advanced IRB approach shall estimate the PD of each of its obligor grades such that—

(a) subject to paragraphs (ab), (b) (ba) and (c), the estimate of the PD is a long run average of one-year default rates for obligors in respect of exposures which fall within the obligor grade to which the estimate relates; *(L.N. 167 of 2023)*

(ab) the long run average PD referred to in paragraph (a) must be an observed historical average PD that is a simple average based on the number of obligors in respect of the corporate, sovereign and bank exposures; *(L.N. 167 of 2023)*

(b) subject to paragraph (ba), in the case of a corporate or bank exposure of the institution that is not in default, the estimate of the PD is not less than 0.05%; *(L.N. 167 of 2023)*

(ba) paragraph (b) does not apply to the portion of such an exposure of the institution that is covered by a recognized guarantee issued by a sovereign; *(L.N. 167 of 2023)*

(c) in the case of a corporate, sovereign or bank exposure of the institution which is in default, the estimate of the PD is 100%; and

(d) the estimate of the PD is based on not less than one source of data—

(i) which is relevant to the institution's corporate, sovereign or bank exposures;

(ii) which covers a period of not less than 5 years; and *(L.N. 167 of 2023)*

(iii) which includes a representative mix of good and bad years of the economic cycle relevant for the institution's corporate, sovereign or bank exposures. *(L.N. 167 of 2023)*

(2) For the purposes of subsection (1)—

(a) an authorized institution shall use information, sources of data and techniques which take into account the institution's long run default experience and long run loss experience as referred to in section 148(d)(i); and

(b) if an authorized institution uses a primary technique for the estimation of PD and other techniques as a point of comparison and potential adjustment, the institution shall act prudently in—

(i) comparing the results of the primary technique and other techniques; and

(ii) making adjustments for the respective limitations of the primary technique and other techniques.

160. Loss given default under foundation IRB approach

(1) An authorized institution which uses the foundation IRB approach shall—

(a) subject to paragraphs (c) and (d), use a supervisory estimate of 45% for the LGD of its senior exposures that are financial institution treated as corporate, sovereign or bank exposures that are— *(L.N. 156 of 2012; L.N. 167 of 2023)*

(i) unsecured; or

(ii) secured by collateral which is not recognized collateral; *(L.N. 156 of 2012)*

(ab) subject to paragraphs (c) and (d), use a supervisory estimate of 40% for the LGD of its senior exposures that are corporate exposures (other than financial institution treated as corporate exposures) that are—

(i) unsecured; or

(ii) secured by collateral which is not recognized collateral; *(L.N. 167 of 2023)*

(b) subject to paragraphs (c) and (d), use a supervisory estimate of 75% for the LGD of its subordinated exposures which are corporate, sovereign or bank exposures; *(L.N. 156 of 2012)*

(ba) subject to paragraphs (c) and (d), use the supervisory estimate of the LGD specified in paragraph (a), (ab) or (b), as the case requires, for its default risk exposures; *(L.N. 167 of 2023)*

(c) use a supervisory estimate of 100% for the LGD of the institution's default risk exposures in respect of single-name credit default swaps if—

(i) the swaps fall within section 226J(1); and

(ii) those exposures are determined in accordance with section 226J(3); and *(L.N. 156 of 2012)*

(d) for transactions that fall within section 226J(4), use a supervisory estimate of 100% for the LGD of the institution's default risk exposures in respect of the transactions if—

(i) the institution calculates its market risk capital charge by using the STM approach or the IMA; and *(L.N. 167 of 2023)*

(ii) the determination of the default risk exposures under that section has used existing calculations for SA-DRC (as defined by section 281) or default risk charge (as defined by section 281), as the case requires, that already contain an LGD assumption. *(L.N. 167 of 2023)*

(2) Subject to subsections (1)(ba) and (3), an authorized institution which uses the foundation IRB approach may, for the purposes of calculating the risk-weighted amount of a senior exposure of the institution which falls within any of its IRB classes of corporate, sovereign and bank exposures, take into account the credit risk mitigating effect of any— *(L.N. 167 of 2023)*

(a) recognized financial collateral; or

(b) recognized IRB collateral.

(3) For the purposes of subsection (2), an authorized institution must—

(a) subject to paragraph (d), use Formula 18 to determine the effective LGD (LGD*) applicable to an exposure covered by a recognized collateral for inclusion into the risk-weight function specified in Formula 16;

(b) continue to calculate EAD without taking into account the presence of any collateral and, to avoid doubt, the terms unsecured portion of the exposure (E_U) and the secured portion of the exposure (E_S) are only used to calculate LGD* for the purposes of Formula 18;

(c) for the purposes of Formula 18—

(i) use sections 90, 91 and 92(1) to determine H_E and H_{fx};

(ii) use sections 90, 91 and 92(1) to determine H_C if the recognized collateral is a recognized financial collateral and use 40% as H_C if the recognized collateral is a recognized IRB collateral;

(iii) to avoid doubt, apply a haircut of 0% to applicable repo-style transactions that are treated as collateralized loans to the counterparty in accordance with section 92(2); and

(iv) adjust the value of the recognized collateral in accordance with section 103, with all necessary modifications, if the recognized collateral in respect of an exposure of the institution has a residual maturity that is shorter than the residual maturity of the exposure; and

(d) if the institution has obtained more than one recognized collateral in respect of the exposure—

(i) use Formula 19 to determine the effective LGD (LGD*) applicable to an exposure covered by the recognized collaterals for inclusion into the risk-weight function specified in Formula 16;

(ii) continue to calculate EAD without taking into account the presence of any collateral and, to avoid doubt, the terms unsecured portion of the exposure (E_U) and the secured portion of the exposure (E_S) are only used to calculate LGD* for the purposes of Formula 19; and

(iii) for the purposes of Formula 19—

(A) use sections 90, 91 and 92(1) to determine H_E and $H_{fx,i}$;

(B) use sections 90, 91 and 92(1) to determine $H_{C,i}$ if the recognized collateral is a recognized financial collateral and use 40% as $H_{C,i}$ if the recognized collateral is a recognized IRB collateral;

(C) to avoid doubt, apply a haircut of 0% to applicable repo-style transactions that are treated as collateralized loans to the counterparty in accordance with section 92(2); and

(D) adjust the value of the recognized collateral in accordance with section 103, with all necessary modifications, if the recognized collateral in respect of an exposure of the institution has a residual maturity that is shorter than the residual maturity of the exposure.

Formula 18

Determination of Effective LGD of Exposure Secured by Recognized Collateral

$$\mathrm{LGD}^* = \mathrm{LGD}_U \times \frac{E_U}{E \times (1 + H_E)} + \mathrm{LGD}_S \times \frac{E_S}{E \times (1 + H_E)}$$

where—

(a) LGD* is the effective LGD;

(b) LGD_U is the supervisory estimate of the LGD specified in subsection (1)(a), (ab), (c) or (d), as the case requires, for the unsecured portion of the exposure;

(c) E_U is $E \times (1 + H_E) - E_S$;

(d) E is the EAD of the exposure;

(e) H_E is the haircut applicable to the authorized institution's exposure to the obligor under the standard supervisory haircuts subject to adjustment as set out in section 92(1);

(f) LGD_S is—

(i) 0% if the recognized collateral is a recognized financial collateral; or

(ii) the applicable value of LGD_S specified in Table 18B in respect of the type of recognized IRB collateral concerned, if the recognized collateral is a recognized IRB collateral;

(g) E_S is min $[C \times (1 - H_C - H_{fx}), E \times (1 + H_E)]$;

(h) C is the current market value of the recognized collateral before adjustment required by the comprehensive approach to the treatment of recognized collateral;

(i) H_C is—

(i) the haircut applicable to the recognized financial collateral under the standard supervisory haircuts, if the recognized collateral is a recognized financial collateral; or

(ii) 40% if the recognized collateral is a recognized IRB collateral; and

(j) H_{fx} is the haircut applicable in consequence of a currency mismatch, if any, under the standard supervisory haircuts subject to adjustment as set out in section 92(1).

Table 18B

LGD_S Applicable to Recognized IRB Collateral

Column 1	Column 2	Column 3
Item	Recognized IRB collateral	LGD_S
1.	Recognized financial receivables	20%
2.	Recognized commercial real estate and recognized residential real estate	20%
3.	Other recognized IRB collateral	25%

Formula 19

Determination of Effective LGD of Exposure Secured by more than One Recognized Collateral

$$LGD^* = LGD_U \times \frac{E_U}{E \times (1 + H_E)} + \sum_i LGD_{S,i} \times \frac{E_{S,i}}{E \times (1 + H_E)}$$

where—

(a) LGD* is the effective LGD;

(b) LGD_U is the supervisory estimate of the LGD specified in subsection (1)(a), (ab), (c) or (d), as the case requires, for the unsecured portion of the exposure;

(c) E_U is max $[0, E \times (1 + H_E) - \sum_i E_{S,i}]$;

(d) E is the EAD of the exposure;

(e) H_E is the haircut applicable to the authorized institution's exposure to the obligor under the standard supervisory haircuts subject to adjustment as set out in section 92(1);

(f) $LGD_{S,i}$, for each recognized collateral i is—

(i) 0% if the recognized collateral is a recognized financial collateral; or

(ii) the applicable value of LGD_S specified in Table 18B in respect of the type of recognized IRB collateral concerned, if the recognized collateral is a recognized IRB collateral;

(g) $E_{S,i}$ is $C_i \times (1 - H_{C,I} - H_{fx,i})$, where the total $E_{S,i}$ across all collaterals, $\sum_i E_{S,i}$, is subject to a maximum value of $E \times (1 + H_E)$;

(h) C_i is the current market value of each recognized collateral i before adjustment required by the comprehensive approach to the treatment of recognized collateral;

(i) $H_{C,i}$, for each recognized collateral i, is—

(i) the haircut applicable to the recognized financial collateral under the standard supervisory haircuts, if the recognized collateral is a recognized financial collateral; or

(ii) 40% if the recognized collateral is a recognized IRB collateral; and

(j) $H_{fx,i}$, for each recognized collateral i, is the haircut applicable in consequence of a currency mismatch, if any, under the standard supervisory haircuts subject to adjustment as set out in section 92(1).

(L.N. 167 of 2023)

(4) *(Repealed L.N. 167 of 2023)*

(5) In this section—

financial institution treated as corporate exposures (視為法團的金融機構風險承擔) means exposures to financial institutions treated as corporates; *(L.N. 167 of 2023)*

senior exposure (優先風險承擔), in relation to an authorized institution, means an exposure of the institution to an obligor which is not a subordinated exposure;

subordinated exposure (後償風險承擔), in relation to an authorized institution, means an exposure of the institution to an obligor which—

(a) is lower in ranking, or junior, to other claims against the obligor in terms of the priority of repayment; or

(b) will be repaid only after all the senior claims against the obligor have been repaid.

161. Loss given default under advanced IRB approach

(1) Subject to subsections (2) and (3), an authorized institution which uses the advanced IRB approach shall estimate the LGD of each of its facility types such that— *(L.N. 156 of 2012)*

(a) subject to paragraph (b), the estimate of the LGD reflects the effect on the severity of the loss suffered in respect of an exposure which falls within a facility type of economic downturn conditions where credit losses are expected to be substantially higher than average;

(b) the estimate of the LGD is not less than the long run default-weighted average loss rate given default calculated as the average loss rate of all observed defaults within the data source used by the institution for the estimation of the LGD of a facility type;

(ba) subject to paragraph (be) and subsection (1B), the estimate of the LGD of a corporate exposure that is unsecured or secured by a collateral that is not a recognized collateral is not less than 25%; *(L.N. 167 of 2023)*

(bb) subject to paragraph (be), the estimate of the LGD of a corporate exposure that is a fully secured exposure secured by—

(i) financial receivables; or

(ii) commercial real estate or residential real estate,

is not less than 10%; *(L.N. 167 of 2023)* (bc) subject to paragraph (be), the estimate of the LGD of a corporate exposure that is a fully secured exposure secured by physical collateral (other than commercial real estate and residential real estate) is not less than 15%; *(L.N. 167 of 2023)*

(bd) subject to paragraph (be) and subsections (1A) and (1B), the estimate of the LGD of a corporate exposure that is a partially secured exposure or is secured by more than one recognized collateral is not less than the effective LGD floor calculated by the use of Formula 19A; *(L.N. 167 of 2023)*

(be) paragraphs (ba), (bb), (bc) and (bd) do not apply to the portion of a corporate exposure of the institution that is covered by a recognized guarantee issued by a sovereign; *(L.N. 167 of 2023)*

(c) the estimate of the LGD of a facility type—

(i) is based on historical recovery rates of exposures which fall within the facility type; and

(ii) is not solely based on the estimated market value of collateral in any case where the institution holds collateral in respect of an exposure which falls within the facility type;

(d) the estimate of the LGD of a facility type reflects the possibility that the institution will have to incur unexpected losses during the debt recovery period applicable to an exposure which falls within the facility type;

(e) the estimate of the LGD of a facility type is based on not less than one source of data—

(i) which is relevant to the exposures which fall within the facility type;

(ii) which covers a period of not less than 7 years; and

(iii) which covers at least one economic cycle;

(f) if the process of estimating the LGD of a facility type involves data mapping in respect of the institution's exposures which fall within the facility type to the factors in reference data sets used by ECAIs—

(i) the mapping process is based on a comparison of available common elements in the ECAIs' reference data and the institution's exposures; and

(ii) in any case where the institution combines multiple sets of reference data used by ECAIs, the institution has in place a policy—

(A) setting out the manner in which the combination is effected; and

(B) ensuring that the institution avoids biases or inconsistencies in the mapping process.

Formula 19A

Determination of Effective LGD Floor for Partially Secured Exposure or Exposure Secured by more than One Recognized Collateral

$$LGD^{\#} = 25\% \times \frac{E_U}{E \times (1 + H_E)} + \sum_i LGD_{S\,floor,i} \times \frac{E_{S,i}}{E \times (1 + H_E)}$$

where—

(a) $LGD^{\#}$ is the effective LGD floor;

(b) E_U is max $[0, E \times (1 + H_E) - \sum_i E_{S,i}]$;

(c) E is the EAD of the exposure;

(d) H_E is the haircut applicable to the authorized institution's exposure to the obligor under the standard supervisory haircuts subject to adjustment as set out in section 92(1);

(e) $LGD_{S\ floor,i}$, for each recognized collateral i, is the applicable value of LGD floor specified in Table 19A in respect of the type of recognized collateral concerned;

(f) $E_{S,i}$ is $C_i \times (1 - H_{C,i} - H_{fx,i})$, subject to a minimum value of 0 and the total $E_{S,i}$ across all collaterals, $\sum_i E_{S,i}$, is subject to a maximum value of $E \times (1 + H_E)$;

(g) C_i is the current market value of each recognized collateral i before adjustment required by the comprehensive approach to the treatment of recognized collateral;

(h) $H_{C,i}$, for each recognized collateral i, is—

(i) the haircut applicable to the recognized collateral under the standard supervisory haircuts, if the recognized collateral is of the type of financial collateral; or

(ii) 40% if the recognized collateral is of the types of financial receivables, commercial real estate, residential real estate or physical collateral (other than commercial real estate and residential real estate); and

(i) $H_{fx,i}$, for each recognized collateral i, is the haircut applicable in consequence of a currency mismatch, if any, under the standard supervisory haircuts subject to adjustment as set out in section 92(1).

Table 19A

LGD Floors by Type of Recognized Collateral

Column 1	Column 2	Column 3
Item	Recognized collateral	LGD floor
1.	Financial collateral	0%
2.	Financial receivables	10%
3.	Commercial real estate or residential real estate	10%
4.	Physical collateral (other than commercial real estate and residential real estate)	15%

(L.N. 167 of 2023)

(1A) For the purposes of Formula 19A, an authorized institution must—

(a) use sections 90, 91 and 92(1) to determine H_E and $H_{fx,i}$;

(b) use sections 90, 91 and 92(1) to determine $H_{C,i}$ if the recognized collateral is a financial collateral and use 40% as $H_{C,i}$ if the recognized collateral is not a financial collateral;

(c) to avoid doubt, apply a haircut of 0% to applicable repo-style transactions that are treated as collateralized loans to the counterparty in accordance with section 92(2); and

(d) adjust the value of the recognized collateral in accordance with section 103, with all necessary modifications, if the recognized collateral in respect of an exposure of the institution has a residual maturity that is shorter than the residual maturity of the exposure. *(L.N. 167 of 2023)*

(1B) If an authorized institution is unable to estimate an LGD for an exposure that is secured by one or more recognized financial collaterals or recognized IRB collaterals as a result of lack of sufficient data to model the effect of the recognized collateral on recoveries, the institution may determine the LGD of the exposure in accordance with section 160(3) under Formula 18 or 19, as the case requires, with the value of LGD_U being replaced by the higher of—

(a) the LGD estimated by the institution for unsecured exposure without taking into account the presence of any collateral; or

(b) 25%. *(L.N. 167 of 2023)*

(2) An authorized institution shall— *(L.N. 156 of 2012)*

(a) have in place an effective and well-documented process for assessing the effects, if any, of economic downturn conditions on debt recovery rates in respect of different facility types and for producing estimates of LGD which reflect those conditions;

(b) take into account all major factors relevant to measuring loss, including the time value of money, the risk premium, and any direct and indirect costs associated with collection in respect of exposures which fall within the facility type;

(c) take into account the extent of any positive correlation between the credit risk of an obligor to whom the institution has an exposure which falls within a facility type and that of any collateral provided in respect of that exposure or that of the provider of such collateral and address the effect of such correlation, if any, in a prudent manner; and

(d) address any currency mismatch and maturity mismatch in a prudent manner.

(3) An authorized institution that uses the advanced IRB approach must comply with section 160(1)(c) or (d), as the case requires, in estimating the LGD of a facility type that comprises default risk exposures in respect of—

(a) single-name credit default swaps that fall within the description in section 160(1)(c)(i) and (ii); or

(b) transactions that fall within the description in section 160(1)(d)(i) and (ii),

as if the institution were an authorized institution that uses the foundation IRB approach. *(L.N. 156 of 2012)*

162. *(Repealed L.N. 167 of 2023)*

163. Exposure at default under foundation IRB approach—on-balance sheet exposures and off-balance sheet exposures other than default risk exposures

(L.N. 44 of 2020)

(1) An authorized institution which uses the foundation IRB approach shall, in relation to an on-balance sheet exposure of the institution—

(a) use the current drawn amount of the exposure, after taking into account the credit risk mitigating effect of any recognized netting as specified in section 209, as an estimate of the EAD of the exposure such that the EAD of the exposure is not less than the sum of—

(i) the amount by which the institution's CET1 capital would be reduced if the exposure were fully written-off; and *(L.N. 156 of 2012)*

(ii) any specific provisions and partial write-offs in respect of the exposure; and

(b) not take into account any discount in respect of the exposure in calculating the risk-weighted amount of the exposure.

(2) Subject to subsection (2AA), an authorized institution that uses the foundation IRB approach shall, for the purposes of estimating the EAD of an off-balance sheet exposure (other than default risk exposure) of the institution specified in column 2 of Table 20, calculate the credit equivalent amount of the exposure by multiplying the principal amount of the exposure by the CCF specified in column 3 of that Table opposite the type of off-balance sheet exposure. *(L.N. 44 of 2020; L.N. 167 of 2023)*

Table 20

Determination of CCF for Off-balance Sheet Exposures other than Default Risk Exposures

(L.N. 44 of 2020)

Item	Off-balance sheet exposures	CCF
1.	Direct credit substitutes	100%

Item	Off-balance sheet exposures	CCF
2.	Transaction-related contingencies	50%
3.	Trade-related contingencies	20%
4.	Asset sales with recourse	100%
4A.	Sale and repurchase agreements (excluding those that are repo-style transactions) *(L.N. 167 of 2023)*	100%
5.	Forward asset purchases	100%
6.	Partly paid-up securities (being an off-balance sheet exposure to the credit risk of the securities purchased from an issuer where only a part of the issue price or nominal face value of the securities has been paid by the institution and the institution will be required to pay the unpaid amount in the future) *(L.N. 175 of 2017)*	100%
7.	Forward forward deposits placed	100%
8.	Note issuance and revolving underwriting facilities *(L.N. 167 of 2023)*	50%

Item	Off-balance sheet exposures	CCF
9.	Subject to subsection (2AA), commitments that do not fall within any of items 1, 2, 3, 4, 4A, 5, 6, 7 and 8—	
	(a) subject to paragraph (c), that may be cancelled at any time unconditionally by an authorized institution without prior notice or that provide for automatic cancellation due to a deterioration in the creditworthiness of the person to whom the commitment has been made;	10%
	(b) subject to paragraph (c), that do not fall within paragraph (a); and	40%
	(c) the drawdown of which will give rise to an off-balance sheet exposure falling within any of items 1, 2, 3, 4, 4A, 5, 6, 7 and 8 or any item specified in section 166 *(L.N. 167 of 2023)*	the lower of— (i) the CCF applicable to the commitment determined under paragraph (a) or (b), as the case requires; and

Item	Off-balance sheet exposures	CCF
		(ii) the CCF applicable to the off-balance sheet exposure arising from the drawdown of the commitment concerned

(2AA) An authorized institution may allocate a CCF of 0% to a commitment that falls within the IRB class of corporate exposures if the commitment satisfies all of the following conditions—

(a) the credit quality of the obligor is closely monitored by the institution on an ongoing basis;

(b) the institution receives no fees or commissions to establish or maintain the commitment;

(c) the obligor is required to apply to the institution for initial and each subsequent drawdown;

(d) the institution has full authority, regardless of the fulfilment by the obligor of the conditions set out in the facility documentation, over the execution of each drawdown;

(e) the institution's decision on the execution of each drawdown is only made after assessing the creditworthiness of the obligor immediately prior to drawdown. *(L.N. 167 of 2023)*

(2A) Where an authorized institution that uses the foundation IRB approach has an off-balance sheet exposure to a counterparty arising from unsegregated collateral posted to the counterparty, if—

(a) the collateral is posted for a transaction or contract booked in the institution's banking book or trading book; and

(b) either—

(i) the transaction or contract is not a derivative contract or SFT; or

(ii) the transaction or contract is a derivative contract or SFT but the collateral is not included in the calculation of default risk exposures under Division 1A, 2 or 2B of Part 6A,

the institution must estimate the EAD of the off-balance sheet exposure as the product of the principal amount of the collateral and a factor of (1 + H). *(L.N. 44 of 2020)*

(2B) For the purposes of subsection (2A), H is the standard supervisory haircut applicable to the collateral, subject to adjustment set out in section 3 of Schedule 7 with the minimum holding period applicable to the collateral determined in the same way as set out in section 91(4). *(L.N. 44 of 2020)*

(3) In this section— *(L.N. 167 of 2023)*

commitment (承諾), in relation to the determination of a CCF applicable to an off-balance sheet exposure, has the meaning given by section 2 of Schedule 6; *(L.N. 167 of 2023)*

discount (折讓), in relation to an on-balance sheet exposure of an authorized institution, means the amount by which the institution's estimate of the EAD of the exposure exceeds the sum referred to in subsection (1)(a).

164. Exposure at default under advanced IRB approach—on-balance sheet exposures and off-balance sheet exposures other than default risk exposures

(L.N. 44 of 2020)

(1) Subject to subsection (4B), an authorized institution that uses the advanced IRB approach must, in relation to an on-balance sheet exposure of the institution— *(L.N. 167 of 2023)*

(a) estimate the EAD of the exposure such that the estimate is not less than—

(i) the current drawn amount of the exposure, after taking into account the credit risk mitigating effect of any recognized netting as specified in section 209;

(ii) the sum of—

(A) the amount by which the institution's CET1 capital would be reduced if the exposure were fully written-off; and *(L.N. 156 of 2012)*

(B) any specific provisions and partial write-offs in respect of the exposure; and

(b) not take into account any discount in respect of the exposure in calculating the risk-weighted amount of the exposure.

(2) Subject to subsection (4B) and section 163(2AA), an authorized institution that uses the advanced IRB approach must— *(L.N. 167 of 2023)*

(a) estimate the EAD of an off-balance sheet exposure of the institution specified in column 2 of Table 20 in accordance with subsections (3), (3A) and (4); and *(L.N. 167 of 2023)*

(b) estimate the EAD of an off-balance sheet exposure of the institution to a counterparty arising from unsegregated collateral posted to the counterparty in accordance with subsections (4) and (4A) if—

(i) the collateral is posted for a transaction or contract booked in the institution's banking book or trading book; and

(ii) either—

(A) the transaction or contract is not a derivative contract or SFT; or

(B) the transaction or contract is a derivative contract or SFT but the collateral is not included in the calculation of default risk exposures under Division 1A, 2 or 2B of Part 6A. *(L.N. 44 of 2020)*

(3) Subject to subsection (4), an authorized institution must—

(a) if the exposure is an off-balance sheet exposure specified in subsection (3A)—use its own estimate of CCF to calculate the EAD of the exposure; and

(b) in any other case—determine the EAD of the exposure in accordance with section 163(2) as if it were using the foundation IRB approach. *(L.N. 167 of 2023)*

(3A) For the purposes of subsection (3)(a), the exposure specified is an off-balance sheet exposure that—

(a) is revolving in nature; and

(b) is not subject to a CCF of 100% in Table 20. *(L.N. 167 of 2023)*

(4) An authorized institution shall estimate the EAD of an off-balance sheet exposure of the institution such that—

(a) in the case of a facility, the estimate of the EAD of the facility reflects the possibility of additional drawings by the obligor in respect of that facility up to and after the time a default event is triggered in respect of the facility;

(b) subject to paragraphs (c) and (ca), the estimate of the EAD is a prudent estimate of the long run default-weighted average EAD of exposures which fall within a facility type with allowance made for the likely margin of error and for any identified positive correlation between the frequency of defaults in respect of exposures which fall within the facility type and any increase in the estimate of the EAD of those exposures; *(L.N. 167 of 2023)*

(c) in the case of a facility type for which the estimate of the EAD is volatile over an economic cycle, the institution uses an estimate of the EAD of the facility type which is appropriate for an economic downturn if that estimate is more prudent than the long run default-weighted average EAD of exposures which fall within the facility type;

(ca) if the estimate of the EAD is based on alternative measures of central tendency or only on the economic downturn data, the institution must ensure that the estimate does not fall below a conservative estimate of the long run default-weighted average EAD of exposures that fall within a facility type; *(L.N. 167 of 2023)*

(d) the estimate of the EAD to be used for each facility type is based on procedures established by the institution which provide a clear and unambiguous delineation of each facility type to which the estimate relates;

(e) the estimate of the EAD to be used for each facility type—

(i) is based on all relevant data and information available to the institution in respect of exposures which fall within the facility type; and

(ii) is derived from criteria which are material drivers for the estimation of the EAD of exposures which fall within the facility type;

(f) the estimate of the EAD of a facility type is based on not less than one source of data—

(i) which is relevant to exposures which fall within the facility type;

(ii) which covers a period of not less than 7 years; and

(iii) which covers at least one economic cycle.

(4A) The EAD for an authorized institution's off-balance sheet exposure estimated under subsection (2)(b) must not be lower than the principal amount of the collateral concerned. *(L.N. 44 of 2020)*

(4B) Subject to subsection (4C), the EAD applicable to a corporate exposure for inclusion into the risk-weight function specified in Formula 16 must not be less than the sum of—

(a) the EAD of the on-balance sheet exposure; and

(b) 50% of the EAD of the off-balance sheet exposure determined in accordance with section 163(2). *(L.N. 167 of 2023)*

(4C) Subsection (4B) does not apply to the portion of a corporate exposure of an authorized institution that is covered by a recognized guarantee issued by a sovereign. *(L.N. 167 of 2023)*

(5) In subsection (1)(b)—

discount (折讓), in relation to an on-balance sheet exposure of an authorized institution, means the amount by which the institution's estimate of the EAD of the exposure exceeds the sum referred to in subsection (1)(a)(ii).

164A. *(Repealed L.N. 44 of 2020)*

165. Exposure at default under foundation IRB approach or advanced IRB approach—default risk exposures in respect of derivative contracts

An authorized institution that uses the foundation IRB approach or the advanced IRB approach must determine the outstanding default risk exposure in respect of derivative contracts booked in the banking book or trading book of the institution based on the default risk exposure calculated for the contracts by using the SA-CCR approach or the IMM(CCR) approach, as the case requires.

(L.N. 44 of 2020)

166. Exposure at default under foundation IRB approach or advanced IRB approach—off-balance sheet exposures not covered by sections 163, 164, 165 and 202

(1) This section applies to an off-balance sheet exposure that is not any of the following—

(a) an off-balance sheet exposure specified in column 2 of Table 20;

(b) an off-balance sheet exposure the EAD of which is estimated in accordance with section 163(2A) or 164(2)(b);

(c) a default risk exposure mentioned in section 165 or 202.

(2) An authorized institution that uses the foundation IRB approach or the advanced IRB approach must, in estimating the EAD of its off-balance sheet exposure, calculate the credit equivalent amount of the exposure—

(a) by applying—

(i) if a CCF applicable to the exposure is specified in Part 2 of Schedule 1—that CCF; or

(ii) if no such CCF is specified—a CCF of 100%; and

(b) in accordance with section 163 or 164, as the case requires, with all necessary modifications.

(L.N. 44 of 2020)

167. Maturity under foundation IRB approach

(1) An authorized institution which uses the foundation IRB approach— *(L.N. 167 of 2023)*

(a) subject to paragraphs (b) and (c), shall use 2.5 years for the M of a corporate, sovereign or bank exposure of the institution for inclusion into the risk-weight function specified in Formula 16;

(b) subject to paragraph (c), shall use 6 months for the M of a corporate, sovereign or bank exposure of the institution in the case of such an exposure in respect of a repo-style transaction;

(c) subject to subsection (2), may calculate the M of all of its corporate, sovereign and bank exposures in accordance with section 168. *(L.N. 167 of 2023)*

(2) An authorized institution that uses the foundation IRB approach must give written notice to the Monetary Authority within 7 days after commencing to calculate the M of all of its corporate, sovereign and bank exposures in accordance with section 168 as if that section were applicable to those exposures. *(L.N. 167 of 2023)*

168. Maturity under advanced IRB approach

(1) An authorized institution which uses the advanced IRB approach shall calculate the M of a corporate or sovereign exposure of the institution as follows— *(L.N. 44 of 2020; L.N. 167 of 2023)*

(a) subject to subsections (2) and (3), the M of the exposure is the greater of—

(i) one year; or

(ii) the remaining effective maturity, in years, of the exposure as calculated in accordance with paragraph (b), (ba), (bb), (bc) or (c), as the case requires; *(L.N. 156 of 2012; L.N. 167 of 2023)*

(b) subject to paragraphs (ba), (bb), (bc) and (c), if the exposure is subject to a predetermined cash flow schedule, the M of the exposure is calculated by the use of Formula 20; *(L.N. 156 of 2012; L.N. 167 of 2023)*

(ba) if the exposure is a default risk exposure in respect of a netting set calculated using the IMM(CCR) approach and the original maturity of the longest-dated contract contained in the netting set is greater than one year, the M of the exposure is calculated by the use of Formula 20A instead of Formula 20; *(L.N. 156 of 2012)*

(bb) subject to paragraph (c)—

(i) if the exposure is a default risk exposure in respect of a netting set calculated using the IMM(CCR) approach and all the transactions in the netting set have an original maturity of not more than one year—

(A) the effective maturity of each transaction in the netting set is calculated by the use of Formula 20; and

(B) the effective maturity of the netting set is calculated as the weighted average effective maturity of the transactions (using the notional amount of each transaction for weighting the maturity of the transactions within the netting set); and

(ii) if the netting set referred to in subparagraph (i) contains only one transaction, Formula 20 is used to calculate the M of the exposure; *(L.N. 156 of 2012)*

(bc) if the exposure is an exposure to which a revolving facility relates, the M of the exposure is calculated using the maximum contractual termination date of the facility, instead of using the repayment date of the facility currently drawn; *(L.N. 167 of 2023)*

(c) if it is not practicable for the institution to comply with paragraph (b) or (bb) in respect of the exposure, the institution shall use a more prudent measure of M which is not less than the maximum remaining time, in years, that the obligor is permitted to take to fully perform the contractual obligations (including principal payments, interest payments and fees) of the obligor under the terms of the agreement governing the exposure; *(L.N. 156 of 2012)*

(d) subject to paragraphs (ba) and (bb), if the exposure is a default risk exposure resulting from the netting of nettable derivative contracts, the M of the exposure is the greater of the following—

(i) the weighted average maturity of the contracts (using the notional amount of each contract for weighting the maturity of the contracts);

(ii) 1 year. *(L.N. 44 of 2020)*

Formula 20

Calculation of Maturity for Corporate and Sovereign Exposures Subject to Predetermined Cash Flow Schedule

(L.N. 167 of 2023)

$$M = \sum_t t \times CF_t / \sum_t CF_t$$

where—

(a) CF_t denotes the cash flows (including principal payments, interest payments and fees) contractually payable by the obligor in period t; and

(b) t is expressed in years (that is, where a payment is due to be received in 18 months, t = 1.5).

Formula 20A

Formula to be Used Instead of Formula 20 where Section 168(1)(ba) is Applicable

$$M = \frac{\sum_{k=1}^{t_k \le 1\,year} \text{Effective EE}_k \times \Delta t_k \times df_k + \sum_{t_k > 1\,year}^{maturity} EE_k \times \Delta t_k \times df_k}{\sum_{k=1}^{t_k \le 1\,year} \text{Effective EE}_k \times \Delta t_k \times df_k}$$

where—

(a) df_k is the risk-free discount factor for future time period t_k;

(b) Effective EE_k = effective EE at time t_k calculated in accordance with section 226G;

(c) *maturity* = the time when the transaction that has the longest residual maturity in the netting set matures; and

(d) $\Delta t_k = t_k - t_{k-1}$, which is the time interval between t_k and t_{k-1} when EE is calculated at dates that are not equally spaced over time.

(L.N. 156 of 2012; L.N. 51 of 2013)

(2) An authorized institution shall use 5 years as the M of any exposure referred to in subsection (1) which would, but for this subsection, have an M of greater than 5 years.

(3) Where an authorized institution has an exposure that falls within paragraph (a) or (b) of the definition of ***relevant short-term exposure*** in subsection (5)— *(L.N. 156 of 2012)*

(a) subsection (1)(a) shall not apply to the exposure; and

(b) the M of the exposure shall be the greater of—

(i) one day; or

(ii) the remaining effective maturity, in years, of the exposure as calculated in accordance with subsection (1)(b) or (c), as the case requires.

(4) Where an exposure of an authorized institution falls within paragraph (ab) of the definition of ***relevant short-term exposure*** in subsection (5)—

(a) subject to paragraphs (b) and (c), the institution must calculate the M of the exposure in accordance with subsection (1)(d) except that the M need not be equal to or greater than one year;

(b) subject to paragraph (c), if the exposure is a default risk exposure calculated using the IMM(CCR) approach, the institution must calculate the M in accordance with subsection (1)(bb) except that the M need not be equal to or greater than one year; and

(c) in determining the M, the institution must apply a minimum level of M equal to—

(i) 10 days for a netting set that contains derivative contracts or margin lending transactions; *(L.N. 44 of 2020)*

(ii) 5 days for a netting set that contains repo-style transactions; and

(iii) 10 days for a netting set that contains transactions or contracts that fall within both subparagraphs (i) and (ii). *(L.N. 156 of 2012)*

(5) In this section—

relevant short-term exposure (有關短期風險承擔), in relation to an authorized institution—

(a) means an exposure in respect of a derivative contract or margin lending transaction that is fully or almost fully collateralized, or in respect of a repo-style transaction with an original maturity of less than one year, where the documentation for the contract or transaction contains clauses— *(L.N. 156 of 2012; L.N. 44 of 2020)*

(i) requiring daily revaluation or re-margining; and

(ii) allowing for the prompt realization or set-off of the collateral in the event of default or failure to revalue or re-margin, as the case may be;

(ab) means an exposure in respect of a netting set in which all the contracts or transactions fall within the description in paragraph (a); *(L.N. 156 of 2012; L.N. 44 of 2020)*

(b) means an exposure with an original maturity of less than one year which is not part of the institution's ongoing financing of the obligor in respect of the exposure (there being no intent or legal obligation to roll over the exposure concerned in the future), and includes—

(i) an import or export letter of credit, or a similar exposure, which can be accounted for at its actual remaining maturity;

(ii) a securities purchase, securities sale, cash settlement by wire transfer, foreign exchange settlement, or any other exposure arising from an unsettled transaction that is entered into on a basis other than a delivery-versus-payment basis, if the exposure does not continue for 5 business days or more after the settlement date; and *(L.N. 156 of 2012)*

(iii) any other short-term exposure in respect of which the institution demonstrates to the satisfaction of the Monetary Authority that the institution has no intent or legal obligation to roll over the exposure and will not in practice roll over the exposure.

169. *(Repealed L.N. 167 of 2023)*

Division 6—Specific Requirements for Retail Exposures

170. Rating dimensions

(1) An authorized institution shall—

(a) ensure that its rating system for retail exposures—

(i) reflects the risk of default of the obligors and transaction-specific factors affecting loss severity in the case of default of obligors in respect of retail exposures; and

(ii) captures the risk characteristics of the obligors, the risk characteristics of the transactions and the frequency and duration of the delinquency of retail exposures;

(b) assign each of its retail exposures to not more than one pool of retail exposures in accordance with its rating criteria and based on all relevant information available regarding the risk characteristics of the obligor in respect of the exposure, the risk characteristics of the transaction to which the exposure relates and the frequency and duration of the delinquency (if any) of the exposure; and

(c) estimate the PD, LGD and EAD of each pool of retail exposures.

(2) For the avoidance of doubt, it is hereby declared that different pools of retail exposures of an authorized institution may have the same estimates of PD, LGD and EAD.

171. Rating structure

An authorized institution shall ensure that its process for assigning its retail exposures to various pools of retail exposures results in the grouping of exposures which provides for a consistent, logical and cogent differentiation of credit risk inherent in those retail exposures—

(a) with no excessive concentrations on particular pools of retail exposures; and

(b) allowing for reasonably accurate, consistent and verifiable estimation of credit risk components for each pool of retail exposures.

172. Rating criteria

An authorized institution shall ensure that—

(a) its rating definitions in respect of the pools of retail exposures; and

(b) its rating processes and criteria for assigning exposures to such pools, are specific, logical, sufficiently detailed and consistently applied and result in a clear differentiation of credit risk inherent in the exposures.

173. Rating assignment horizon

An authorized institution shall—

(a) use a time horizon of more than one year for the purposes of assigning its retail exposures to its pools of retail exposures;

(b) subject to paragraph (c), ensure that its assignment of a retail exposure to a pool of retail exposures of the institution accurately represents the institution's assessment of the willingness and ability of an obligor in respect of the exposure to perform the obligor's contractual obligations, after taking into account any potentially adverse economic conditions over an economic cycle within the industry or geographic region relevant to the obligor; and *(L.N. 267 of 2006)*

(c) act prudently in assessing information relating to the willingness and ability of an obligor in respect of a retail exposure to perform the obligor's contractual obligations.

174. Rating coverage

An authorized institution shall, in the case of each exposure which falls within the IRB class of retail exposures, assign the exposure to a pool of retail exposures as part of the institution's process for giving credit approvals.

175. Integrity of rating process

An authorized institution shall ensure that—

(a) the institution has in place policies and procedures to ensure that the rating process for retail exposures is independent of the institution's staff and management responsible for originating such exposures;

(b) a review is conducted, not less than once in every 12 months, of—

(i) the risk characteristics and delinquency status of each pool of retail exposures; and

(ii) the status of an obligor under an exposure which falls within a pool of retail exposures to ensure that the exposure is assigned to the pool that accurately reflects the credit risk of the exposure; and

(c) the institution has in place an effective process for—

(i) identifying, documenting, reviewing and updating the circumstances in which it is appropriate for officers of the institution to override the inputs to, or the outputs of, the institution's rating system; *(L.N. 137 of 2011)*

(ii) ensuring that such circumstances are prudent; *(L.N. 137 of 2011)*

(iii) ensuring that all permissible overrides are approved by officers of the institution having delegated credit authority and are applied in a consistent manner; and *(L.N. 137 of 2011)*

(iv) monitoring the nature and performance of such overrides following approval. *(L.N. 137 of 2011)*

176. Calculation of risk-weighted amount of retail exposures

(1) An authorized institution shall, for the purposes of calculating the risk-weighted amount of the institution's retail exposures,

provide its own estimates of the PD, LGD and EAD of each pool of retail exposures.

(2) An authorized institution shall use Formula 21 to calculate the risk-weighted amount of the institution's retail exposures which—

(a) fall within the IRB subclass of residential mortgages to individuals or residential mortgages to property-holding shell companies; and

(b) are not in default.

Formula 21

Risk-weight Function for Residential Mortgages

Correlation (R)	=	0.15
Capital charge factor (K)	=	LGD × N[(1 – R)^–0.5 × G(PD) + (R / (1 – R))^0.5 × G(0.999)] – PD × LGD
Risk-weight (RW)	=	K × 12.5
Risk-weighted amount	=	RW × EAD

where—

(a) PD and LGD are expressed in decimals and EAD is expressed in Hong Kong dollars;

(b) N(x) denotes the cumulative distribution function for a standard normal random variable; and

(c) G(z) denotes the inverse cumulative distribution function for a standard normal random variable.

(3) An authorized institution shall use Formula 22 to calculate the risk-weighted amount of the institution's retail exposures which—

(a) fall within the IRB subclass of qualifying revolving retail exposures (transactor) or qualifying revolving retail exposures (revolver); and *(L.N. 167 of 2023)*

(b) are not in default.

Formula 22

Risk-weight Function for Qualifying Revolving Retail Exposures (Transactor and Revolver)

(L.N. 167 of 2023)

Correlation (R)	=	0.04
Capital charge factor (K)	=	LGD × N[(1 – R)^–0.5 × G(PD) + (R / (1 – R))^0.5 × G(0.999)] – PD × LGD
Risk-weight (RW)	=	K × 12.5
Risk-weighted amount	=	RW × EAD

where—

(a) PD and LGD are expressed in decimals and EAD is expressed in Hong Kong dollars;

(b) N(x) denotes the cumulative distribution function for a standard normal random variable; and

(c) $G(z)$ denotes the inverse cumulative distribution function for a standard normal random variable.

(4) An authorized institution shall use Formula 23 to calculate the risk-weighted amount of the institution's retail exposures which—

(a) fall within the IRB subclass of small business retail exposures or other retail exposures to individuals; and

(b) are not in default.

Formula 23

Risk-weight Function for Small Business Retail Exposures or other Retail Exposures to Individuals

Correlation (R)	=	0.03 × (1 – EXP (–35 × PD)) / (1 – EXP (–35)) + 0.16 × [1 – (1 – EXP (–35 × PD)) / (1 – EXP (–35))]
Capital charge factor (K)	=	LGD × N[(1 – R)^–0.5 × G(PD) + (R / (1 – R))^0.5 × G(0.999)] – PD × LGD
Risk-weight (RW)	=	K × 12.5
Risk-weighted amount	=	RW × EAD

where—

(a) PD and LGD are expressed in decimals and EAD is expressed in Hong Kong dollars;

(b) EXP denotes exponential;

(c) N(x) denotes the cumulative distribution function for a standard normal random variable; and

(d) G(z) denotes the inverse cumulative distribution function for a standard normal random variable.

(5) An authorized institution shall use the risk-weight function set out in subsection (2), (3) or (4) as applicable to the IRB subclass within which a retail exposure falls to calculate the risk-weighted amount of any such retail exposure which is in default except that the capital charge factor (K) for a defaulted retail exposure shall be equal to the greater of—

(a) zero; or

(b) the figure resulting from the subtraction of the institution's best estimate of the EL of the exposure from the LGD of the exposure.

177. Probability of default

(1) An authorized institution which uses the retail IRB approach shall estimate the PD of each pool of retail exposures of the institution such that—

(a) subject to paragraphs (ab), (b), (ba), (bb) and (c), the estimate of the PD is a long run average of one-year default rates for obligors in respect of retail exposures which fall within the pool to which the estimate relates; *(L.N. 167 of 2023)*

(ab) the estimate of the PD must be based on an observed historical average of one-year default rates; *(L.N. 167 of 2023)*

(b) subject to paragraph (bb), the estimate of the PD of a retail exposure that falls within the IRB subclass of qualifying revolving retail exposures (revolver) and is not in default is not less than 0.1%; *(L.N. 167 of 2023)*

(ba) subject to paragraph (bb), the estimate of the PD of a retail exposure that falls within the IRB subclass of small business retail exposures, residential mortgages to individuals, residential mortgages to property-holding shell companies, qualifying revolving retail exposures (transactor) or other retail exposures to individuals and is not in default is not less than 0.05%; *(L.N. 167 of 2023)*

(bb) paragraphs (b) and (ba) do not apply to the portion of a retail exposure of the institution that is covered by a recognized guarantee issued by a sovereign; *(L.N. 167 of 2023)*

(c) the estimate of the PD to be assigned to a pool of retail exposures of the institution which are in default is 100%;

(d) *(Repealed L.N. 167 of 2023)*

(e) the estimate of the PD of a pool of retail exposures of the institution is based on not less than one source of data—

(i) which is relevant to the institution's retail exposures;

(ii) which covers a period of not less than 5 years; and *(L.N. 167 of 2023)*

(iii) which includes a representative mix of good and bad years of the economic cycle relevant for the institution's retail exposures. *(L.N. 167 of 2023)*

(2) For the purposes of subsection (1), an authorized institution shall—

(a) use internal data as the primary source of information for estimating the risk characteristics for each of its pools of retail exposures;

(b) only use external data or models for any estimate of the PD if the institution demonstrates to the satisfaction of the Monetary Authority that there is a strong correlation—

(i) between the institution's process of assigning exposures to a pool of retail exposures and the classification process used by the external data source; and

(ii) between the institution's credit risk profile and the composition of the external data; and

(c) use all relevant data sources as points of comparison for internal data referred to in paragraph (a), or external data or models referred to in paragraph (b), used by the institution.

(3) For the purposes of subsection (1)(a), an authorized institution may, based on its estimate of the expected long run loss rate for a pool of retail exposures, use its long run default-weighted average loss rate given default as calculated in section 178(1)(b) to infer its estimate of the PD of the pool of retail exposures.

(4)-(5) *(Repealed L.N. 167 of 2023)*

178. Loss given default

(1) An authorized institution which uses the retail IRB approach shall estimate the LGD of each pool of retail exposures of the institution such that—

(a) subject to paragraph (b), the estimate of the LGD of the pool reflects the effect on the severity of the loss suffered in respect of the retail exposures which fall within the pool of economic downturn conditions where credit losses are expected to be substantially higher than average;

(b) subject to subsection (3), the estimate of the LGD of the pool is not less than the long run default-weighted average loss rate given default calculated as the average loss rate of all observed defaults within the data source used by the institution for the estimation of the LGD of that pool;

(c) subject to paragraph (d), the estimate of the LGD of a retail exposure that falls within the IRB subclass of residential mortgages to individuals or residential mortgages to property-holding shell companies is not less than 10%; *(L.N. 137 of 2011)*

(ca) subject to paragraph (d), the estimate of the LGD of a retail exposure that falls within the IRB subclass of qualifying revolving retail exposures (transactor) or qualifying revolving retail exposures (revolver) is not less than 50%; *(L.N. 167 of 2023)*

(cb) subject to paragraph (d), the estimate of the LGD of a retail exposure that—

(i) is unsecured or secured by a collateral that is not a recognized collateral; and

(ii) falls within the IRB subclass of small business retail exposures or other retail exposures to individuals,

is not less than 30%; *(L.N. 167 of 2023)*

(cc) subject to paragraph (d), the estimate of the LGD of a retail exposure that—

(i) is a fully secured exposure secured by a recognized collateral of the types of—

(A) financial receivables; or

(B) commercial real estate or residential real estate; and

(ii) falls within the IRB subclass of small business retail exposures or other retail exposures to individuals,

is not less than 10%; *(L.N. 167 of 2023)*

(cd) subject to paragraph (d), the estimate of the LGD of a retail exposure that—

(i) is a fully secured exposure secured by a recognized collateral of the type of physical collateral (other than commercial real estate and residential real estate); and

(ii) falls within the IRB subclass of small business retail exposures or other retail exposures to individuals,

is not less than 15%; *(L.N. 167 of 2023)*

(ce) subject to paragraph (d), the estimate of the LGD of a retail exposure that—

(i) is a partially secured exposure or is secured by more than one recognized collateral; and

(ii) falls within the IRB subclass of small business retail exposures or other retail exposures to individuals,

is not less than the effective LGD floor calculated by the use of Formula 19A, with the value of 25% in that formula being replaced by a value of 30%; *(L.N. 167 of 2023)*

(d) paragraphs (c), (ca), (cb), (cc), (cd) and (ce) do not apply to the portion of a retail exposure of the institution that is covered by a recognized guarantee issued by a sovereign; *(L.N. 167 of 2023)*

(e) the estimate of the LGD of a pool of retail exposures of the institution—

(i) is based on historical recovery rates of exposures which fall within the pool; and

(ii) is not solely based on the estimated market value of collateral in any case where the institution holds collateral in respect of an exposure which falls within the pool;

(f) the estimate of the LGD of a pool of retail exposures of the institution reflects the possibility that the institution will have to incur unexpected losses during the debt recovery period applicable to an exposure which falls within the pool;

(g) the estimate of the LGD of a pool of retail exposures of the institution is based on not less than one source of data—

(i) which is relevant to the exposures which fall within the pool;

(ii) which covers a period of not less than 5 years; and *(L.N. 167 of 2023)*

(iii) which covers at least one economic cycle; and

(h) if the process of estimating the LGD of a pool of retail exposures of the institution involves data mapping in respect of the institution's exposures which fall within the pool to the factors in reference data sets used by ECAIs—

(i) the mapping process is based on a comparison of available common elements in the ECAIs' reference data and the pool; and

(ii) in any case where the institution combines multiple sets of reference data used by ECAIs, the institution has in place a policy—

(A) setting out the manner in which the combination is effected; and

(B) ensuring that the institution avoids biases or inconsistencies in the mapping process.

(2) For the purposes of subsection (1), an authorized institution shall—

(a) have in place an effective and well-documented process for assessing the effect, if any, of economic downturn conditions on debt recovery rates in respect of different pools of retail exposures and for producing estimates of LGD which reflect those conditions;

(b) take into account all major factors relevant to measuring loss, including the time value of money, the risk premium, and any direct and indirect costs associated with collection in respect of retail exposures which fall within a pool;

(c) take into account the extent of any positive correlation between the credit risk of an obligor to whom the institution has an exposure which falls within a pool of retail exposures and that of any collateral provided in respect of that exposure or that of the provider of such collateral and address the effect of such correlation, if any, in a prudent manner; and

(d) address any currency mismatch and maturity mismatch in a prudent manner.

(3) For the purposes of subsection (1)(b), an authorized institution may, based on its estimate of the expected long run loss rate for a pool of retail exposures, use its estimate of the PD as referred to in section 177 to infer its long run default-

weighted average loss rate given default for the pool of retail exposures.

179. Exposure at default—on-balance sheet exposures

Section 164(1), (4B) and (4C), with all necessary modifications, applies to an authorized institution which uses the retail IRB approach in respect of the estimation by the institution of the EAD of each pool of its on-balance sheet retail exposures as it applies to the institution's estimation of the EAD of its on-balance sheet corporate and sovereign exposures.

(L.N. 167 of 2023)

180. Exposure at default—off-balance sheet exposures other than default risk exposures

(L.N. 44 of 2020)

(1) Section 164(2), (3), (3A), (4)(a), (b), (c), (ca), (d) and (e), (4A), (4B) and (4C), with all necessary modifications, applies to an authorized institution that uses the retail IRB approach in respect of the estimation by the institution of the EAD of each pool of its off-balance sheet retail exposures as it applies to the institution's estimation of the EAD of its off-balance sheet corporate and sovereign exposures. *(L.N. 167 of 2023)*

(2) *(Repealed L.N. 167 of 2023)*

(3) An authorized institution shall estimate the EAD of its off-balance sheet exposures specified in Table 20 for each pool of retail exposures such that—

(a) in the case of the estimate of the EAD of a retail facility with an uncertain future drawdown—

(i) the institution takes into account—

(A) the institution's overall drawdown and repayment history with regard to its retail exposures which fall within the same facility type as the retail facility concerned; or

(B) the institution's expectation based on the history of additional drawings by the obligors in respect of facilities which fall within such facility type up to and after the time a default event has been triggered in respect of such a facility;

(ii) if the CCF used by the institution for the calculation of the credit equivalent amount of the retail facility does not reflect the expectation of additional drawings on the retail facility extended up to and after the time a default event has been triggered, the institution reflects in its estimate of the LGD of the retail exposures the likelihood of such additional drawings; and

(b) the estimate of the EAD of off-balance sheet exposures which fall within a pool of retail exposures is based on not less than one source of data—

(i) which is relevant to such retail exposures; and

(ii) which covers a period of not less than 5 years. *(L.N. 167 of 2023)*

180A. *(Repealed L.N. 44 of 2020)*

181. Exposure at default—default risk exposures in respect of derivative contracts

(L.N. 44 of 2020)

Section 165, with all necessary modifications, applies to an authorized institution which uses the retail IRB approach in respect of the estimation by the institution of the EAD of its retail exposures that are default risk exposures in respect of derivative contracts as it applies to the institution's estimation of the EAD of its corporate, sovereign and bank exposures that are default risk exposures in respect of derivative contracts.

(L.N. 44 of 2020)

182. Exposure at default—off-balance sheet exposures not covered by sections 180, 181 and 202

(1) This section applies to an off-balance sheet exposure that is not any of the following—

(a) an off-balance sheet exposure specified in column 2 of Table 20;

(b) a default risk exposure mentioned in section 181 or 202.

(2) An authorized institution that uses the retail IRB approach must, in estimating the EAD of its off-balance sheet exposure, calculate the credit equivalent amount of the exposure—

(a) by applying—

(i) if a CCF applicable to the exposure is specified in Part 2 of Schedule 1—that CCF; or

(ii) if no such CCF is specified—a CCF of 100%; and

(b) in accordance with section 180, with all necessary modifications.

(L.N. 44 of 2020)

Division 7—Specific Requirements for CIS Exposures Constituting Deductible Holdings

(Division 7 replaced L.N. 167 of 2023)

183. CIS exposure constituting deductible holding

(1) This section applies in relation to an authorized institution's CIS exposure to a Level 1 CIS, or any part of the exposure,

that constitutes a deductible holding if the deductible holding is not deducted from the institution's capital base under Division 4 of Part 3.

(2) The authorized institution must calculate the risk-weighted amount of the deductible holding—

(a) if the deductible holding is a significant LAC investment in a CET1 capital instrument issued by a financial sector entity—by multiplying that portion of the EAD of the deductible holding that is not subject to deduction from the institution's CET1 capital under section 43(1)(p) by a risk-weight of 250%; or

(b) if the deductible holding is an insignificant LAC investment, or a holding of non-capital LAC liabilities that falls within section 48A, that is not subject to deduction from the institution's capital base—

(i) if the deductible holding is an equity exposure—by determining the risk-weighted amount in accordance with section 65G(1)(a) or (b); or

(ii) in any other case—by regarding that portion of the EAD of the deductible holding as if it were directly held by the institution and multiplying the corresponding risk-weight determined in accordance with this Part.

(3) To avoid doubt, this section also applies to cases where a CIS exposure to a Level 1 CIS, or any part of the exposure, constitutes a deductible holding because regulatory deductible items are held by—

(a) a Level 2 CIS to which the Level 1 CIS has a CIS exposure; or

(b) a Level n+1 CIS (where n is an integer equal to or greater than 2) to which the Level 1 CIS has an indirect CIS exposure.

(4) In this section—

indirect CIS exposure (間接CIS風險承擔) means an indirect CIS exposure within the meaning of section 226ZH;

Level 1 CIS (1級CIS) means a Level 1 CIS within the meaning of section 226ZH;

Level 2 CIS (2級CIS) means a Level 2 CIS within the meaning of section 226ZH;

Level n+1 CIS (n+1級CIS) means a Level n+1 CIS within the meaning of section 226ZH.

184-194. *(Repealed L.N. 167 of 2023)*

Division 8—Specific Requirements for Other Exposures

195. Cash items

(1) An authorized institution which uses the specific risk-weight approach shall calculate the risk-weighted amount of its cash items by multiplying the EAD of each item by the relevant risk-weight set out in Table 21.

Table 21

Risk-weights for Cash Items

Item	Cash items	Risk-weight
1.	Cash items which fall within paragraphs (a), (b), (c), (f) and (g) of the definition of ***cash items*** in section 139(1)	0%

Item	Cash items	Risk-weight
2.	Cash items which fall within paragraphs (d) and (i) of the definition of ***cash items*** in section 139(1)	100%
3.	Cash items which fall within paragraph (e) of the definition of ***cash items*** in section 139(1)	20%
4.	Cash items falling within paragraph (h) of the definition of ***cash items*** in section 139(1) which are outstanding—	
	(a) up to and including the fourth business day after the settlement date;	0%
	(b) including the fifth business day and up to and including the fifteenth business day after the settlement date;	100%
	(c) including the sixteenth business day and up to and including the thirtieth business day after the settlement date;	625%
	(d) including the thirty-first business day and up to and including the forty-fifth business day after the settlement date; and	937.5%
	(e) including and after the forty-sixth business day after the settlement date	1,250%

Item	Cash items	Risk-weight
5.	Cash items that fall within paragraph (j) of the definition of ***cash items*** in section 139(1) *(L.N. 156 of 2012)*	1,250%

(1A) Unless otherwise stated in Part 6A, cash items falling within paragraphs (g), (h), (i) and (j) of the definition of ***cash items*** in section 139(1) do not apply to repo-style transactions. *(L.N. 167 of 2023)*

(2) For the purposes of subsection (1), the EAD of a cash item is the principal amount of the cash item. *(L.N. 167 of 2023)*

196. Other items

(1) Subject to subsection (2), an authorized institution which uses the specific risk-weight approach shall calculate the risk-weighted amount of its exposures which fall within the IRB subclass of other items by multiplying the EAD of each exposure by a risk-weight of 100%.

(2) The Monetary Authority may, by notice in writing given to an authorized institution, require the institution to calculate the risk-weighted amount of an exposure (or a portfolio of exposures) to which this section applies, by multiplying the EAD of the exposure (or the portfolio of exposures) by a risk-weight of more than 100% as specified in the notice.

(3) An authorized institution shall comply with the requirements of a notice given to it under subsection (2).

(4) For the purposes of subsections (1) and (2), the EAD of an exposure which falls within the IRB subclass of other items is the principal amount of the exposure. *(L.N. 167 of 2023)*

Division 9—Specific Requirements for Certain Portfolios of Exposures

197. Purchased receivables

An authorized institution shall—

(a) classify its purchased receivables as corporate exposures or retail exposures in accordance with the nature of the receivables; and

(b) subject to section 199(1), calculate the risk-weighted amount for both default risk and dilution risk in respect of its purchased receivables in accordance with sections 198, 199 and 200.

198. Calculation of risk-weighted amount for default risk in respect of purchased receivables

(1) An authorized institution shall calculate the risk-weighted amount for default risk in respect of its purchased receivables—

(a) subject to paragraph (c) and subsection (2), in the case of a portfolio of purchased receivables which falls within one of the IRB subclasses of corporate exposures only, by using in accordance with Division 5 the risk-weight function which is applicable to the IRB subclass within which the portfolio of purchased receivables falls;

(b) subject to paragraph (c) and subsection (3), in the case of a portfolio of purchased receivables which falls within one of the IRB subclasses of retail exposures only, by using in accordance with Division 6 the risk-weight function which is applicable to the IRB subclass within which the portfolio of purchased receivables falls;

(c) subject to subsection (2) or (3), in the case of a portfolio of purchased receivables containing a mixture of exposures in respect of which the institution cannot separate the exposures into different IRB subclasses of corporate exposures or retail exposures, by using in accordance with Division 5 or 6, as the case requires, the risk-weight function which will result in the highest risk-weighted amount of the exposures in the portfolio of purchased receivables.

(2) For the purposes of subsection (1)(a), an authorized institution which purchases corporate receivables shall make its estimates of the PD and LGD (or, if applicable, EL) of each of the purchased receivables constituting the portfolio of purchased corporate receivables of the institution (referred to in this Division as ***bottom-up approach***) on the assumption that there is no recourse to, or other support from, the seller of the corporate receivables or any third-party guarantor.

(3) For the purposes of subsection (1)(b), an authorized institution which purchases retail receivables shall—

(a) make its estimates of the PD and LGD (or, if applicable, EL) of the portfolio of purchased retail receivables (referred to in this Division as ***top-down approach***) on the assumption that there is no recourse to, or other support from, the seller of the retail receivables or any third-party guarantor; and

(b) comply with section 200.

199. Calculation of risk-weighted amount for dilution risk in respect of purchased receivables

(1) An authorized institution shall calculate the risk-weighted amount for dilution risk in respect of its purchased receivables in accordance with subsection (2) unless the institution demonstrates to the satisfaction of the Monetary Authority that the dilution risk it faces in respect of its purchased receivables is immaterial.

(2) For the purposes of calculating the risk-weighted amount for dilution risk in respect of its purchased receivables, an authorized institution shall—

(a) if the bottom-up approach is used, estimate the EL for dilution risk for each of its purchased receivables (expressed as a percentage of the EAD of the relevant purchased receivable);

(b) if the top-down approach is used—

(i) estimate the EL for dilution risk for a portfolio of its purchased receivables (expressed as a percentage of the total EAD of all receivables in the relevant portfolio of purchased receivables); and

(ii) comply with section 200;

(c) make the estimate of EL referred to in paragraph (a) or (b) on the assumption that there is no recourse to, or other support from, the seller of the receivables or any third-party guarantor.

(3) An authorized institution shall, for the purposes of calculating the risk-weighted amount for dilution risk in respect of its purchased receivables, use the corporate risk-weight function set out in Formula 16 with—

(a) PD set as equal to the institution's estimate of EL for dilution risk;

(b) LGD set at 100%; and

(c) subject to subsection (4), M determined in accordance with—

(i) in the case of purchased corporate receivables—

(A) section 167 if the institution uses the foundation IRB approach;

(B) section 168 if the institution uses the advanced IRB approach;

(ii) in the case of purchased retail receivables, section 168.

(4) An authorized institution may set M at one year for the purposes of subsection (3)(c) if the institution demonstrates to the satisfaction of the Monetary Authority that the institution's dilution risk in respect of its purchased receivables is monitored and managed by the institution with a view to the risk being resolved within one year after the purchase.

200. Requirements for authorized institution using top-down approach to estimate probability of default, etc. of purchased receivables for default risk or dilution risk

An authorized institution which uses the top-down approach to estimate the PD and LGD (or, if applicable, EL) of its purchased receivables for default risk or dilution risk shall—

(a) subject to paragraph (b), group its purchased receivables into portfolios so that accurate and consistent estimates of the PD and LGD (or, if applicable, EL) for default risk and estimates of the EL for dilution risk can be determined;

(b) make the grouping required under paragraph (a) so as to reflect the seller's credit underwriting practices in respect of the receivables and the heterogeneity of the seller's customers;

(c) comply with Division 6 in respect of the methods and data used for estimating the PD and LGD (or, if applicable, EL); and

(d) in the case of default risk, have in place policies, systems and procedures to ensure compliance with paragraphs CRE36.115 to CRE36.121 in Chapter

CRE36 of the consolidated Basel Framework launched by the Basel Committee as amended or supplemented from time to time. *(L.N. 167 of 2023)*

(L.N. 212 of 2015)

201. Leasing arrangements

(1) Where an authorized institution has an exposure arising from a leasing arrangement which does not expose the institution to residual value risk, the institution—

(a) shall treat the exposure as an exposure secured by collateral of the same type as the subject matter of the lease; and

(b) if the collateral referred to in paragraph (a) is recognized collateral in accordance with section 208, may take into account the credit risk mitigating effect of the collateral in calculating the risk-weighted amount of the exposure.

(2) Where an authorized institution has an exposure arising from a leasing arrangement which exposes the institution to residual value risk, the institution shall—

(a) calculate the risk-weighted amount for default risk by using the risk-weight function applicable to the IRB subclass within which an exposure to the lessee falls, with the EAD set as equal to the discounted lease payment stream, and the PD and LGD as those which the institution assigns to the exposure; and

(b) calculate the risk-weighted amount for residual value risk by multiplying the residual value of the leased asset by 100%.

202. Securities financing transactions

(1) Where an authorized institution does not have an IMM(CCR) approval for SFTs, the institution must calculate the risk-

weighted amount of its default risk exposures in respect of SFTs (whether booked in its banking book or trading book) in accordance with subsection (6) and Division 2B of Part 6A, and calculate the risk-weighted amount of its exposures to the assets underlying the SFTs in accordance with subsections (4) and (5) and section 68C. *(L.N. 44 of 2020)*

(2) Subject to subsections (3), (4), (5) and (6), an authorized institution that has an IMM(CCR) approval for SFTs must apply section 68C and Division 2 of Part 6A to all its SFTs. *(L.N. 44 of 2020)*

(3) Where—

(a) an authorized institution has an IMM(CCR) approval for SFTs but the approval does not include SFTs that are long settlement transactions; or

(b) an authorized institution is permitted under section 10B(5), or has chosen under section 10B(7), to use the methods set out in Division 2B of Part 6A for certain SFTs, *(L.N. 44 of 2020)*

the institution must calculate the risk-weighted amount of its default risk exposures in respect of SFTs (whether booked in its banking book or trading book) that are not, by virtue of the circumstance described in paragraph (a) or (b), subject to the IMM(CCR) approach, in accordance with subsection (6) and Division 2B of Part 6A, and calculate the risk-weighted amount of its exposures to the assets underlying the SFTs in accordance with subsections (4) and (5) and section 68C. *(L.N. 44 of 2020)*

(4) Where an authorized institution applies section 68C to an SFT booked in its banking book, the institution must determine the risk-weight to be allocated to its exposure under the SFT in accordance with— *(L.N. 167 of 2023)*

(a) the risk-weight function for corporate, sovereign and bank exposures;

(b) the risk-weight function for retail exposures; or *(L.N. 54 of 2022)*

(c) *(Repealed L.N. 167 of 2023)*

(d) Part 6B for CIS exposures that do not constitute a deductible holding, *(L.N. 54 of 2022)*

as the case may be, according to the nature of the asset underlying the SFT, and, where applicable, the IRB class within which the issuer of the asset falls.

(5) To avoid doubt, if a specified SFT (as defined by section 68C(5)) is booked in an authorized institution's trading book, an exposure of the institution to the asset underlying the specified SFT is an exposure subject to the requirements of Part 8 instead of this Part. *(L.N. 167 of 2023)*

(6) Where an authorized institution applies Division 2 or 2B of Part 6A, as the case requires, to an SFT, the institution must determine the risk-weight to be allocated to its exposure under the SFT in accordance with— *(L.N. 44 of 2020)*

(a) the risk-weight function for corporate, sovereign and bank exposures; or

(b) the risk-weight function for retail exposures,

as the case may be, according to the IRB class within which an exposure to the counterparty to the SFT falls and, where applicable, in accordance with the treatment of credit risk mitigation set out in Division 10.

(L.N. 156 of 2012; L.N. 167 of 2023)

202A. Credit-linked notes

(1) Subject to subsection (2), an authorized institution that has an exposure in respect of a credit-linked note held by the

institution must allocate a risk-weight, as determined by the applicable risk-weight function, to the exposure that is the greater of—

(a) the risk-weight attributable to the reference obligation or basket of reference obligations of the note, as the case may be, as if the institution had a direct exposure to the reference obligation or the basket of reference obligations; and

(b) the risk-weight attributable to the note.

(2) An authorized institution is not required to provide regulatory capital for its exposure in respect of a credit-linked note held by the institution in excess of the institution's maximum liability under the note.

(L.N. 137 of 2011)

202B. Capital treatment of IPO financing

An authorized institution may apply section 64A, with all necessary modifications, to determine the risk-weight for the purpose of calculating the risk-weighted amount of the exposures arising from IPO financing in respect of the institution's corporate, bank and retail exposures.

(L.N. 167 of 2023)

202C. Capital instruments issued by, and non-capital LAC liabilities of, financial sector entities

(1) If an authorized institution has an insignificant LAC investment that is a direct holding, indirect holding or synthetic holding of a capital instrument issued by, or a non-capital LAC liability of, a financial sector entity that does not fall within section 54A, the institution must determine the risk-weight of any amount of the insignificant LAC investment that is not deducted from the institution's capital

base under sections 43(1)(o), 47(1)(c) and 48(1)(c) in accordance with this Part.

(2) If an authorized institution has a significant LAC investment that is a direct holding, indirect holding or synthetic holding of a capital instrument issued by, or a non-capital LAC liability of, a financial sector entity that does not fall within section 54A, the institution must determine the risk-weight of any amount of the significant LAC investment that is not deducted from the institution's capital base under sections 43(1)(p), 47(1)(d) and 48(1)(d) in accordance with this Part.

(3) If an authorized institution has holdings of non-capital LAC liabilities that fall within section 48A and do not fall within section 54A, the institution must determine the risk-weight of any amount of the holdings that is not deducted from the institution's capital base in accordance with this Part.

(L.N. 167 of 2023)

Division 10—Credit Risk Mitigation

203. Credit risk mitigation—general

(1) Subject to subsections (1A) and (1B), an authorized institution may take into account the effect of recognized credit risk mitigation in calculating the risk-weighted amount of its exposures, including— *(L.N. 156 of 2012)*

(a) recognized collateral;

(b) recognized netting; and

(c) recognized guarantees and recognized credit derivative contracts.

(1A) An authorized institution must not take into account the effect of recognized credit risk mitigation in accordance with this Division in calculating the risk-weighted amount of its exposures to the extent that the credit risk mitigating effect concerned has already been taken into account in the institution's calculation of the risk-weighted amount of its exposures in accordance with these Rules other than this Division. *(L.N. 156 of 2012; L.N. 51 of 2013)*

(1B) Where an authorized institution has bought credit protection for an exposure and the credit protection is in the form of a single-name credit default swap that falls within section 226J(1), the institution must not take into account the credit risk mitigating effect of the swap when calculating the risk-weighted amount of the exposure. *(L.N. 156 of 2012)*

(2) The risk-weighted amount of an exposure of an authorized institution in respect of which recognized credit risk mitigation has been taken into account by the institution shall not be higher than that of an identical exposure in respect of which recognized credit risk mitigation has not been so taken into account.

204. Recognized collateral

(1) For the purposes of section 203(1)(a), an authorized institution shall only take into account the credit risk mitigating effect of recognized collateral through its determination of the LGD of a corporate, sovereign, bank or retail exposure of the institution that is not a default risk exposure (***non-default risk exposure***) against which recognized collateral is held in accordance with— *(L.N. 44 of 2020)*

(a) section 160 if the exposure is a corporate, sovereign or bank exposure for which the institution uses the foundation IRB approach;

(b) section 161 if the exposure is a corporate or sovereign exposure for which the institution uses the advanced IRB approach; *(L.N. 167 of 2023)*

(c) section 178 if the exposure is a retail exposure for which the institution uses the retail IRB approach.

(2) For the purposes of section 203(1)(a), an authorized institution may take into account the credit risk mitigating effect of recognized collateral in accordance with this Division in the calculation of the risk-weighted amount of a default risk exposure only if either of the following is complied with in respect of the exposure—

(a) the exposure is in respect of an SFT that is not nettable calculated in accordance with section 226MJ;

(b) the exposure is in respect of one or more than one derivative contract entered into by the institution with a counterparty and the conditions specified in subsection (3) are met. *(L.N. 44 of 2020)*

(3) The conditions are—

(a) the institution entered into the contract or contracts with the counterparty under a general banking facility consisting of 2 or more credit lines, and, for at least one of those credit lines, if drawn (whether in full or not), the drawn portion that will result from such drawdown is, at the time of the drawdown, a non-default risk exposure;

(b) the credit lines are secured by the same recognized collateral;

(c) no amount of the recognized collateral is designated solely for offsetting losses on default risk exposures incurred by the institution under the general banking facility; and

(d) the recognized collateral is not included in the calculation of the default risk exposure under Division 1A or 2 of Part 6A. *(L.N. 44 of 2020)*

(4) If the same recognized collateral is available to cover both default risk exposures and non-default risk exposures, an authorized institution may take into account the credit risk mitigating effect of the recognized collateral for the purpose of calculating the risk-weighted amount of the non-default risk exposures—

(a) only to the extent of the current market value, or the part of such value, of the collateral that is not included in the calculation of the default risk exposures under Division 1A or 2 of Part 6A; and

(b) in accordance with other applicable provisions in this Division relating to recognized collateral. *(L.N. 44 of 2020)*

205. Recognized financial receivables

(1) A financial receivable constitutes a recognized financial receivable taken as collateral for a corporate, sovereign or bank exposure of an authorized institution only if it is a claim on the obligor in respect of the receivable (referred to in this section as ***receivable obligor***) with an original maturity of not more than one year and—

(a) the claim on the receivable obligor is legally enforceable in all relevant jurisdictions and the legal requirements for establishing the claim have been fulfilled; *(L.N. 167 of 2023)*

(b) there is in place a framework which allows the institution to have the claim on the receivable obligor as a perfected first priority claim;

(c) the institution has taken all steps to fulfil requirements under the law applicable to the institution's interest in the claim which are necessary to obtain and maintain an enforceable security interest, whether by registration or otherwise, or to exercise a right to set-off in relation to the receivable (referred to in this section as ***receivable collateral***);

(d) the agreement and the legal process underpinning the claim allow the institution to realize the value of the receivable collateral in a timely manner;

(e) the institution has in place clearly documented procedures to ensure that any legal conditions required for declaring the default of the obligor in respect of the exposure covered by the receivable collateral (referred to in this section as ***direct obligor***) and for timely collection of the receivable collateral are observed;

(f) in the event of the financial distress or default of the direct obligor, the institution has the legal authority to sell or assign the receivable collateral to other parties without the consent of the receivable obligor;

(g) subject to paragraph (h), the institution has in place an effective process for assessing, monitoring and controlling the credit risk of the receivable collateral;

(h) if the institution relies on the direct obligor to review the credit risk of the receivable obligor, the institution has reviewed the quality of the direct obligor's credit management policies;

(i) in the case of receivable collateral which consists of a pool of receivables, the loan-to-value ratio between the amount of the exposure covered by the pool of receivables constituting the receivable collateral and the value of the pool of receivables reflects the anticipated cost of collection of the receivables and the level of concentration on a particular receivable obligor within the pool of receivables;

(j) in the case of receivable collateral which consists of a pool of receivables, the institution ensures that—

(i) subject to subparagraph (ii), the pool of receivables constituting the receivable collateral is diversified and the positive correlation between the creditworthiness of the direct obligor and the receivable obligors is not unduly high;

(ii) if the positive correlation between the creditworthiness of the direct obligor and the receivable obligors is unduly high, the attendant risk is taken into account in the setting of loan-to-value ratio in respect of the pool of receivables constituting the receivable collateral; and

(k) the institution has—

(i) a clearly documented process for collecting payments from the receivable obligors in the event of the financial distress or default of the direct obligor; and

(ii) the resources which are required in the documented process referred to in subparagraph (i) for collecting payments from the receivable obligors.

(2) For the avoidance of doubt, it is hereby declared that financial receivables derived from the following do not fall within subsection (1)— *(L.N. 128 of 2014)*

(a) securitization transactions;

(b) sub-participations;

(c) credit derivative contracts; and

(d) any affiliates of the direct obligor of an authorized institution. *(L.N. 128 of 2014)*

(3) For the purposes of subsection (2)—

affiliate (附屬成員), in relation to a direct obligor of an authorized institution, means—

(a) a subsidiary of the direct obligor;

(b) a person that belongs to the same group of companies as the direct obligor; or

(c) an employee of the direct obligor. *(L.N. 128 of 2014)*

206. Recognized commercial real estate and recognized residential real estate

Commercial real estate or residential real estate constitutes recognized commercial real estate or recognized residential real estate respectively for a corporate, sovereign or bank exposure of an authorized institution only if—

(a) the institution's credit risk to the obligor in respect of the exposure is not materially dependent on the performance of the underlying property or project constituting the collateral (referred to in this section as ***property collateral***) but on the capacity of the obligor to repay the exposure from other sources;

(b) the value of the property collateral is not materially dependent on the performance of the obligor in respect of the exposure;

(c) the institution has—

(i) a first lien on, or a first charge over, the property collateral; or

(ii) first and subsequent liens on, or first and subsequent charges over, the property collateral if all of such liens or charges are held by the institution;

(d) the institution has in place clearly documented procedures to ensure that there is no prior claim, or claim of equal ranking, by another party on the property collateral;

(e) the institution's claim on the property collateral is legally enforceable in all relevant jurisdictions and the legal requirements for establishing the claim have been fulfilled; *(L.N. 167 of 2023)*

(f) the institution has taken all steps to fulfil requirements under the law applicable to the institution's claim on the property collateral which are necessary to obtain and maintain an enforceable security interest, whether by registration or otherwise, or to exercise a right to set-off in relation to the property collateral;

(g) the agreement and the legal process underpinning the institution's interest in the property collateral allow the institution to realize the value of the property collateral in a timely manner;

(h) the institution has in place clearly documented procedures to ensure that any legal conditions required for declaring the default of the obligor in respect of the exposure covered by the property collateral and for timely collection of the property collateral are observed;

(i) the property collateral is valued at not more than its fair value;

(j) the value of the property collateral is monitored frequently and reviewed not less than once in every 12 months;

(k) the institution has in place clearly documented policies specifying the types of commercial real estate and residential real estate which the institution accepts as collateral for its corporate, sovereign or bank exposures and the lending criteria associated with such collateral; and

(l) the institution ensures that the property collateral is adequately insured against damage or deterioration.

207. Other recognized IRB collateral

Physical collateral (other than commercial real estate and residential real estate) constitutes other recognized IRB collateral for a corporate, sovereign or bank exposure of an authorized institution only if—

(a) a liquid market exists for the disposal of the physical collateral in an expeditious and economically efficient manner;

(ab) the institution reassesses the condition referred to in paragraph (a) periodically and when there is information indicating material changes in the market; *(L.N. 167 of 2023)*

(b) well-established market prices are publicly available for the physical collateral;

(ba) the institution demonstrates that the amount it receives when the collateral is realized does not deviate significantly from the market price; *(L.N. 167 of 2023)*

(c) the institution has a first lien on, or a first charge over, the physical collateral;

(d) the institution has in place clearly documented procedures to ensure that there is no prior claim, or claim of equal ranking, by another party on the physical collateral;

(e) the institution's claim on the physical collateral is legally enforceable in all relevant jurisdictions and the legal requirements for establishing the claim have been fulfilled; *(L.N. 167 of 2023)*

(f) the institution has taken all steps to fulfil requirements under the law applicable to the institution's claim on the physical collateral which are necessary to obtain and maintain an enforceable security interest, whether by registration or otherwise, or to exercise a right to set-off in relation to the physical collateral;

(g) the agreement and the legal process underpinning the institution's interest in the physical collateral allow the institution to realize the value of the physical collateral in a timely manner;

(h) the institution has in place clearly documented procedures to ensure that any legal conditions required for declaring the default of the obligor in respect of the exposure covered by the physical collateral and for timely collection of the physical collateral are observed;

(i) subject to paragraph (j), the loan agreement and all other documentation underpinning the institution's interest in the physical collateral include detailed descriptions of the collateral and the right to examine and revalue the collateral whenever the institution considers necessary; *(L.N. 167 of 2023)*

(j) the institution performs periodic revaluation and, where practicable, periodic inspection of the physical collateral;

(k) the institution has in place clearly documented policies specifying the types of physical collateral which the institution accepts as collateral for its corporate, sovereign or bank exposures and the lending criteria associated with such collateral; and

(l) the institution ensures that the physical collateral is adequately insured against damage or deterioration.

208. Leased assets may be recognized as collateral

A leased asset of an authorized institution constitutes recognized collateral only if—

(a) the lease concerned does not expose the institution to residual value risk;

(b) the leased asset satisfies the requirements set out in—

(i) section 206 if it is commercial real estate or residential real estate;

(ii) section 207 if it is a physical asset;

(c) the institution has in place effective and clearly documented policies and procedures for managing the risk associated with the leased asset with respect to the location of the asset, the use to which it is put, its age and its planned obsolescence;

(d) there is in place a legal framework which establishes the institution's legal ownership of the leased asset and its ability to exercise its rights as the owner in a timely manner; and

(e) the difference between the rate of depreciation of the leased asset and the rate of amortization of the lease payments is not material to the extent that it will overstate the credit risk mitigating effect of the asset.

209. Recognized netting

(1) Subject to subsection (3B), for the purposes of section 203(1)(b), where an authorized institution is entitled pursuant to a valid bilateral netting agreement or valid cross-product netting agreement to net amounts owed by the institution to a counterparty against amounts owed by the counterparty to the institution, the institution shall only take into account the credit risk mitigating effect of recognized netting through the calculation of the EAD of its exposure to the counterparty. *(L.N. 156 of 2012; L.N. 175 of 2017; L.N. 44 of 2020)*

(2) An authorized institution must—

(a) in calculating the EAD of its exposure to the counterparty in respect of the institution's on-balance sheet corporate, sovereign, bank, retail or other exposures—subject to subsection (4), apply sections 94 and 103, with all necessary modifications, to take into account the credit risk mitigating effect of recognized netting; and

(b) in calculating the EAD of its exposure to the counterparty in respect of derivative contracts—take into account the credit risk mitigating effect of recognized netting in accordance with Division 1A or 2 of Part 6A, as the case requires. *(L.N. 44 of 2020)*

(3) Subject to subsection (3B), an authorized institution may only take into account the credit risk mitigating effect of recognized netting in respect of SFTs by— *(L.N. 167 of 2023)*

(a) in relation to a corporate, sovereign or bank exposure of an authorized institution that uses the foundation IRB approach—taking the default risk exposure (that is, E*) calculated in accordance with section 226MK or 226ML, as the case requires, as the EAD for inclusion into the risk-weight function specified in Formula 16; or

(b) in relation to a corporate or sovereign exposure of an authorized institution that uses the advanced IRB approach or a retail exposure of an authorized institution that uses the retail IRB approach— *(L.N. 167 of 2023)*

(i) taking the default risk exposure (that is, E*) calculated in accordance with section 226MK or 226ML, as the case requires, as the EAD for inclusion into the risk-weight function specified in Formula 16, 21, 22 or 23, as the case requires; and

(ii) applying its estimate of LGD to the default risk exposure (that is, E*) to the counterparty. *(L.N. 44 of 2020; L.N. 167 of 2023)*

(3A) *(Repealed L.N. 44 of 2020)*

(3B) Where an authorized institution uses the IMM(CCR) approach to calculate the EAD of a netting set that contains SFTs, the institution must take into account the effect of any recognized netting in respect of repo-style transactions in the manner set out in Division 2 of Part 6A instead of in the manner set out in subsections (1) and (3) except for transactions for which the institution is permitted under section 10B(5), or has chosen under section 10B(7), to use the methods set out in Division 2B of Part 6A. *(L.N. 156 of 2012; L.N. 44 of 2020)*

(4) For the purposes of subsection (2)—

(a) *(Repealed L.N. 44 of 2020)*

(b) the references in section 94 to "net credit exposure" shall be calculated without deduction of any specific provisions or partial write-offs in respect of the exposure. *(L.N. 44 of 2020)*

210. Recognized guarantees and recognized credit derivative contracts

(1) For the purposes of section 203(1)(c), subject to subsection (2), an authorized institution shall only take into account the credit risk mitigating effect of a recognized guarantee or recognized credit derivative contract in accordance with sections 211, 212, 213, 214, 215, 216, 217 and 219.

(2) An authorized institution shall—

(a) have in place clearly documented criteria, methods and processes, which comply with sections 214, 215, 216, 217 and 219, for taking into account the credit risk mitigating effect of recognized guarantees and recognized credit derivative contracts; and

(b) take into account such effects consistently— *(L.N. 167 of 2023)*

(i) both for a given type of recognized guarantee or recognized credit derivative contract; and

(ii) over time.

(L.N. 167 of 2023)

211. Recognized guarantees and recognized credit derivative contracts under substitution framework for corporate, sovereign and bank exposures under foundation IRB approach

(L.N. 167 of 2023)

(1) Subject to subsection (2), a guarantee which falls within section 98 constitutes a recognized guarantee under the substitution framework, and a credit derivative contract which falls within section 99 constitutes a recognized credit derivative contract under the substitution framework, in relation to—

(a) a corporate, sovereign or bank exposure of an authorized institution for which the institution uses the foundation IRB approach. *(L.N. 167 of 2023)*

(b) *(L.N. 167 of 2023)*

(2) For the purposes of subsection (1), the references in sections 98(a) and 99(1)(b) to section 99A are taken to be references to subsections (3), (4) and (5). *(L.N. 167 of 2023)*

(3) An entity that provides credit protection to an exposure is an eligible credit protection provider if both of the conditions set out in subsection (4) are met. *(L.N. 167 of 2023)*

(4) The conditions are—

(a) the entity is—

(i) a sovereign;

(ii) a public sector entity;

(iii) a multilateral development bank;

(iv) an unspecified multilateral body;

(v) a bank;

(vi) a qualifying CCP;

(vii) a prudentially regulated financial institution;

(viii) an entity not listed in subparagraphs (i) to (vii) that has an ECAI issuer rating; or

(ix) a corporate to which an authorized institution has an exposure that is assessed under the institution's rating system and assigned to an obligor grade with an estimate of PD; and

(b) the attributed risk-weight of the entity is lower than the risk-weight that would be allocated to the exposure in respect of which the credit protection is provided. *(L.N. 167 of 2023)*

(5) In this section—

prudentially regulated financial institution (受審慎監管的金融機構) has the meaning given by section 99A(3). *(L.N. 167 of 2023)*

212. Recognized guarantees and recognized credit derivative contracts under substitution framework for corporate and sovereign exposures under advanced IRB approach and for retail exposures under retail IRB approach

(L.N. 167 of 2023)

(1) A guarantee or credit derivative contract, in relation to— *(L.N. 167 of 2023)*

(a) a corporate or sovereign exposure of an authorized institution for which the institution uses the advanced IRB approach; or *(L.N. 167 of 2023)*

(b) a retail exposure of an authorized institution for which the institution uses the retail IRB approach,

constitutes a recognized guarantee under the substitution framework, or a recognized credit derivative contract under the substitution framework, as the case may be, only if—

(c) the guarantee or credit derivative contract is evidenced in writing, non-cancellable on the part of the credit protection provider, in force until the exposure to which the guarantee or credit derivative contract relates (referred to in this section as ***underlying exposure***) is satisfied in full and legally enforceable against the credit protection provider in a jurisdiction where the credit protection provider has assets to attach under the enforcement of a judgment; *(L.N. 167 of 2023)*

(ca) the guarantee or credit derivative contract is unconditional, and there is no clause in the contract outside the direct control of the institution that prevents the credit protection provider from being obliged to pay out in a timely manner in the event that the original counterparty fails to make the payment due; *(L.N. 167 of 2023)*

(cb) the credit derivative contract under which the protection buyer obtains credit protection for a basket of exposures is a first-to-default credit derivative contract; *(L.N. 167 of 2023)*

(d) the institution has in place clearly documented criteria for the types of credit protection providers which it will recognize for credit risk mitigation purposes under the substitution framework; and

(e) the criteria used by the institution in recognizing a credit derivative contract under the substitution framework require that the specified obligation under the credit derivative contract on which the credit protection of that contract is based cannot be different from the underlying exposure unless the conditions specified in section 99(1)(o) are satisfied. *(L.N. 167 of 2023)*

(2) A guarantee or credit derivative contract that only covers the remaining loss after an authorized institution has first pursued the obligor for payment and has completed the workout process may constitute a recognized guarantee or a recognized credit derivative contract, as the case may be, under the substitution framework if the conditions set out in subsection (1)(c), (ca), (cb), (d) and (e), as the case requires, are met. *(L.N. 167 of 2023)*

213. Recognized internal risk transfer to trading book

(1) Subject to subsection (3), an internal risk transfer used by an authorized institution to transfer the credit risk of one or more credit exposures (***protected credit exposure***) booked in the institution's banking book to its trading book may be recognized for the purpose of calculating the risk-weighted amount of the protected credit exposure under this Part if there is an external hedge that meets all the conditions set out in subsection (2)(a) or (b).

(2) The conditions are—

(a) the external hedge in respect of the protected credit exposure—

(i) is in the form of a credit derivative contract entered into by the institution with a third party and booked in the institution's trading book;

(ii) exactly matches the internal risk transfer; and

(iii) meets the requirements set out in section 99(1)(a), (b), (c), (l), (m), (n), (o), (p), (q) and (r); or

(b) all of the following apply—

(i) the external hedge in respect of the protected credit exposure is made up of multiple credit derivative contracts entered into by the institution with one or more third parties (***aggregate external hedge***) and booked in the institution's trading book;

(ii) each of those credit derivative contracts meets the requirements set out in section 99(1)(a), (b), (c), (l), (m), (n), (o), (p), (q) and (r);

(iii) the aggregate external hedge exactly matches the internal risk transfer;

(iv) the internal risk transfer exactly matches the aggregate external hedge.

(3) For the purposes of subsection (1), if the external hedge meets the conditions specified in subsection (2)(a) or (b) except that the credit events specified in the external hedge do not include the credit event described in section 99(1)(l)(iii)—

(a) in cases where the amount of the internal risk transfer is more than the amount of the protected credit exposure—the amount of the internal risk transfer that may be recognized for the purpose of calculating the risk-weighted amount of the protected credit exposure must not be more than 60% of the amount of the protected credit exposure; or

(b) in cases where the amount of the internal risk transfer is equal to or less than the amount of the protected credit exposure—only up to 60% of the amount of the internal risk transfer may be recognized for the purpose of calculating the risk-weighted amount of the protected credit exposure.

(4) In this section—

internal risk transfer (內部風險轉移) has the meaning given by section 99B(4).

(L.N. 167 of 2023)

214. Capital treatment of recognized guarantees and recognized credit derivative contracts

(1) Subject to subsection (2) and section 219, an authorized institution which takes into account the credit risk mitigating effect of a recognized guarantee or recognized credit derivative contract (other than an internal risk transfer recognized under section 213) in calculating the risk-weighted amount of an exposure (***protected exposure***) of the institution shall do so using the substitution framework. *(L.N. 167 of 2023)*

(2) Subject to section 219, an authorized institution that takes into account the credit risk mitigating effect of an internal risk transfer recognized under section 213—

(a) is not required to calculate a risk-weighted amount under this Part for the covered portion of the protected exposure if capital charges are held by the institution for the trading book leg of the internal risk transfer and the corresponding external hedge in accordance with the requirements of Part 8; and

(b) if there is any uncovered portion, must calculate the risk-weighted amount of the unprotected amount of the protected exposure in the same manner as for any other direct exposure to the obligor. *(L.N. 167 of 2023)*

(3) *(Repealed L.N. 167 of 2023)*

215. Provisions supplementary to section 214(1)—substitution framework (general)

An authorized institution which uses the substitution framework in respect of a corporate, sovereign, bank or retail exposure of the institution (referred to in this section as ***underlying exposure***)—*(L.N. 167 of 2023)*

(a) shall not reflect the effect of double default when taking into account the credit risk mitigating effect of a recognized guarantee or recognized credit derivative contract in calculating the risk-weighted amount of the underlying exposure; and

(b) shall, subject to sections 216(3B) and 217(5), to the extent that the credit risk mitigating effect of a recognized guarantee or recognized credit derivative contract is taken into account by the institution in calculating the risk-weighted amount of the underlying exposure, ensure that the risk-weight of the underlying exposure concerned, as adjusted after taking into account the credit risk mitigating effect of the recognized guarantee or recognized credit derivative contract, is not less than that of a comparable direct exposure to the credit protection provider. *(L.N. 51 of 2013)*

216. Provisions supplementary to section 214(1)—substitution framework for corporate, sovereign and bank exposures under foundation IRB approach

(L.N. 167 of 2023)

(1) In relation to a corporate, sovereign or bank exposure for which an authorized institution uses the foundation IRB approach (***underlying exposure***), the institution must take into account the credit risk mitigating effect of a recognized guarantee or recognized credit derivative contract in respect of the underlying exposure in accordance with subsections (2), (3), (3AA), (3A), (3B), (4), (5), (6) and (7). *(L.N. 167 of 2023)*

(2) An authorized institution shall divide the EAD of an underlying exposure into the portion covered by the recognized guarantee or recognized credit derivative contract (referred to in this section as ***covered portion***) and the portion not covered by the recognized guarantee or recognized credit derivative contract (referred to in this section as ***uncovered portion***) such that—

(a) if the covered portion and uncovered portion of the underlying exposure are of equal seniority in terms of ranking for payment to the institution—

(i) in the case where the institution uses the IRB approach to calculate its credit risk for exposures to the guarantor or counterparty, as the case may be—the covered portion of the underlying exposure receives the treatment set out in subsections (3), (3A) and (3B) and the uncovered portion of the underlying exposure receives the treatment set out in subsection (4); or

(ii) in the case where the institution uses the STC approach to calculate its credit risk for exposures to the guarantor or counterparty, as the case may be—the covered portion of the underlying exposure receives the treatment set out in subsections (3AA), (3A) and (3B) and the uncovered portion of the underlying exposure receives the treatment set out in subsection (4); *(L.N. 167 of 2023)*

(b) if the institution has obtained tranched credit protection for its exposure, it must—

(i) decompose the exposure into a protected sub-tranche and an unprotected sub-tranche; and

(ii) determine the risk-weighted amount of the exposure in accordance with Part 7. *(L.N. 175 of 2017)*

(3) Subject to subsection (3B), an authorized institution shall, in the case of a covered portion of an underlying exposure— *(L.N. 51 of 2013)*

(a) derive a risk-weight by using the risk-weight function applicable to the IRB subclass within which the exposure to the credit protection provider falls, and the PD of the obligor grade to which the exposure to the credit protection provider is assigned; *(L.N. 167 of 2023)*

(b) *(Repealed L.N. 167 of 2023)*

(c) replace, at the institution's discretion, the estimate of the LGD of the underlying exposure with the estimate of the LGD of the recognized guarantee or recognized credit derivative contract after taking into account the seniority in terms of ranking for payment, and any recognized collateral provided by the credit protection provider to the institution in respect of the recognized guarantee or recognized credit derivative contract.

(3AA) Subject to subsection (3B), an authorized institution may allocate to the covered portion of an underlying exposure a relevant risk-weight attributable to that portion of the underlying exposure under Part 4, if the guarantee or contract falls within section 98 or 99, as the case requires. *(L.N. 167 of 2023)*

(3A) If the covered portion of an authorized institution's underlying exposure is a covered portion because of a recognized guarantee (***original guarantee***) and is the subject of a counter-guarantee given by a sovereign, the institution may, in respect of the covered portion, treat the counter-guarantee as if it were the original guarantee if—

(a) the counter-guarantee covers all credit risk elements of the underlying exposure to the extent that it relates to the covered portion;

(b) the counter-guarantee is given in such terms that it can be called if—

(i) for any reason the obligor in respect of the underlying exposure to which the original guarantee relates fails to make payments due in respect of the underlying exposure; and

(ii) the original guarantee could be called;

(c) the counter-guarantee meets all of the requirements for guarantees set out in section 98 (except that the counter-guarantee need not meet the requirements set out in section 98(b) and (c)); and

(d) the institution reasonably considers, and demonstrates to the satisfaction of the Monetary Authority, that—

(i) the cover of the counter-guarantee is adequate and effective; and

(ii) there is no evidence to suggest that the coverage of the counter-guarantee is less effective than that of a direct and explicit guarantee by the sovereign that gives the counter-guarantee. *(L.N. 167 of 2023)*

(3B) Where an authorized institution's underlying exposure is covered by a recognized credit derivative contract cleared by a qualifying CCP, the institution may allocate to the covered portion of the underlying exposure— *(L.N. 167 of 2023)*

(a) a risk-weight of 2% if—

(i) the institution is a clearing member of the qualifying CCP;

(ii) the institution is a direct client of a clearing member of the qualifying CCP, and all the conditions set out in section 226ZA(6) are met; or

(iii) the institution is an indirect client within a multi-level client structure associated with the qualifying CCP, and all the conditions set out in section 226ZA(6), with all necessary modifications, are met for arrangements among the CCP, clearing member, all clients at levels higher than the institution within the multi-level client structure, and the institution; or *(L.N. 44 of 2020; L.N. 167 of 2023)*

(b) a risk-weight of 4% if—

(i) the institution is a direct client of a clearing member of the qualifying CCP and all of the conditions set out in section 226ZA(6) (excluding the condition set out in section 226ZA(6)(a)(iii)) are met; or

(ii) the institution is an indirect client within a multi-level client structure associated with the qualifying CCP and all of the conditions set out in section 226ZA(6) (excluding the condition set out in section 226ZA(6)(a)(iii)), with all necessary modifications, are met for arrangements among the CCP, clearing member, all clients at levels higher than the institution within the multi-level client structure, and the institution. *(L.N. 167 of 2023)*

(c) *(Repealed L.N. 167 of 2023)*

(4) In the case of an uncovered portion of an underlying exposure, an authorized institution must allocate a risk-weight calculated in the same manner as for any other direct

exposure to the obligor in respect of the underlying exposure. *(L.N. 167 of 2023)*

(5) Where there is a currency mismatch between an underlying exposure of an authorized institution and a recognized guarantee or recognized credit derivative contract covering the underlying exposure, the institution shall adjust the amount of the covered portion, with all necessary modifications, in accordance with section 100(4). *(L.N. 167 of 2023)*

(6) Where there is a maturity mismatch between an underlying exposure of an authorized institution and a recognized guarantee or recognized credit derivative contract covering the underlying exposure and the residual maturity of the recognized guarantee or recognized credit derivative contract is shorter than the residual maturity of the underlying exposure, the institution shall adjust the value of the credit protection, with all necessary modifications, in accordance with section 103.

(7) If the credit protection for an authorized institution's underlying exposure consists of a recognized credit derivative contract that provides that, on the happening of a credit event, the protection seller is not obliged to make a payment in respect of any loss or absorb any loss if the loss is below a specified amount (***materiality threshold***), the institution must, in calculating its capital adequacy ratio, allocate a risk-weight of 1 250% to the portion of the underlying exposure that is below the materiality threshold. *(L.N. 167 of 2023)*

217. Provisions supplementary to section 214(1)—substitution framework for corporate and sovereign exposures under advanced IRB approach and for retail exposures under retail IRB approach

(L.N. 167 of 2023)

(1) Subject to subsections (1A), (1B), (2) and (5), in relation to—

(a) a corporate or sovereign exposure for which an authorized institution uses the advanced IRB approach; or

(b) a retail exposure for which an authorized institution uses the retail IRB approach,

(***underlying exposure***), the institution must take into account the credit risk mitigating effect of a recognized guarantee or recognized credit derivative contract in respect of the underlying exposure by adjusting the institution's estimate of the PD or LGD of the underlying exposure. *(L.N. 167 of 2023)*

(1A) If—

(a) a recognized guarantee is provided to an authorized institution or a recognized credit derivative contract is entered into by the institution; and

(b) the institution uses the foundation IRB approach or STC approach to calculate its credit risk for exposures to the guarantor or counterparty, as the case may be,

the institution must divide the EAD of an underlying exposure into the portion covered by the recognized guarantee or recognized credit derivative contract (***covered portion***) and the portion not covered by the recognized guarantee or recognized credit derivative contract (***uncovered portion***) in accordance with subsection (1B). *(L.N. 167 of 2023)*

(1B) The institution must divide the EAD of an underlying exposure into a covered portion and an uncovered portion under subsection (1A) so that—

(a) in the case where the institution uses the foundation IRB approach to calculate its credit risk for exposures to the guarantor or counterparty, as the case may be—the covered portion of the underlying exposure receives the treatment set out in subsections (3A), (4) and (5) and the uncovered portion of the underlying exposure receives the treatment set out in subsection (6); and

(b) in the case where the institution uses the STC approach to calculate its credit risk for exposures to the guarantor or counterparty, as the case may be—the covered portion of the underlying exposure receives the treatment set out in subsections (3B), (4) and (5) and the uncovered portion of the underlying exposure receives the treatment set out in subsection (6). *(L.N. 167 of 2023)*

(2) Subject to subsections (3) and (4), an authorized institution shall ensure that its criteria and processes for making adjustments pursuant to subsection (1) to its estimates of the PD or LGD— *(L.N. 156 of 2012)*

(a) subject to paragraphs (b), (c) and (d), satisfy the requirements set out in this Part applicable to the institution for assigning exposures to obligor grades and facility grades; *(L.N. 156 of 2012)*

(b) reflect the willingness and ability of the credit protection provider to perform its contractual obligations under the guarantee or credit derivative contract;

(c) address the likely timing of any payments under the guarantee or credit derivative contract and the degree to which the ability of the credit protection provider to perform its contractual obligations under the guarantee or credit derivative contract is positively correlated with the ability of the obligor in respect of the underlying exposure to repay; and

(d) take into account the extent to which residual risk to the obligor in respect of the underlying exposure remains (including any currency mismatch and maturity mismatch between the recognized guarantee or recognized credit derivative contract and the underlying exposure).

(3) An authorized institution may only make an adjustment to the estimate of PD pursuant to subsection (1) in accordance with section 216.

(3A) Subject to subsection (5), an authorized institution may allocate to the covered portion of an underlying exposure a relevant risk-weight attributable to that portion of the underlying exposure determined using the foundation IRB approach. *(L.N. 167 of 2023)*

(3B) Subject to subsection (5), an authorized institution may allocate to the covered portion of an underlying exposure a relevant risk-weight attributable to that portion of the underlying exposure determined under Part 4, if the guarantee or contract falls within section 98 or 99, as the case requires. *(L.N. 167 of 2023)*

(4) If the covered portion of an authorized institution's underlying exposure is a covered portion because of a recognized guarantee (***original guarantee***) and is the subject of a counter-guarantee given by a sovereign, the institution may, in respect of the covered portion, treat the counter-guarantee as if it were the original guarantee if—

(a) the counter-guarantee covers all credit risk elements of the underlying exposure to the extent that it relates to the covered portion;

(b) the counter-guarantee is given in such terms that it can be called if—

(i) for any reason the obligor in respect of the underlying exposure to which the original guarantee relates fails to make payments due in respect of the underlying exposure; and

(ii) the original guarantee could be called;

(c) the counter-guarantee meets all of the requirements for guarantees set out in section 98 (except that the counter-guarantee need not meet the requirements set out in section 98(b) and (c)); and

(d) the institution reasonably considers, and demonstrates to the satisfaction of the Monetary Authority, that—

(i) the cover of the counter-guarantee is adequate and effective; and

(ii) there is no evidence to suggest that the coverage of the counter-guarantee is less effective than that of a direct and explicit guarantee by the sovereign that gives the counter-guarantee. *(L.N. 167 of 2023)*

(5) Where an authorized institution's underlying exposure is covered by a recognized credit derivative contract cleared by a qualifying CCP, the institution may allocate to the covered portion of the underlying exposure— *(L.N. 167 of 2023)*

(a) a risk-weight of 2% if—

(i) the institution is a clearing member of the qualifying CCP;

(ii) the institution is a direct client of a clearing member of the qualifying CCP, and all the conditions set out in section 226ZA(6) are met; or

(iii) the institution is an indirect client within a multi-level client structure associated with the qualifying CCP, and all the conditions set out in section 226ZA(6), with all necessary modifications, are met for arrangements among the CCP, clearing member, all clients at levels higher than the institution within the multi-level client structure, and the institution; or *(L.N. 44 of 2020; L.N. 167 of 2023)*

(b) a risk-weight of 4% if—

(i) the institution is a direct client of a clearing member of the qualifying CCP and all of the conditions set out in section 226ZA(6) (excluding the condition set out in section 226ZA(6)(a)(iii)) are met; or

(ii) the institution is an indirect client within a multi-level client structure associated with the qualifying CCP and all of the conditions set out in section 226ZA(6) (excluding the condition set out in section 226ZA(6)(a)(iii)), with all necessary modifications, are met for arrangements among the CCP, clearing member, all clients at levels higher than the institution within the multi-level client structure, and the institution. *(L.N. 167 of 2023)*

(c) *(Repealed L.N. 167 of 2023)*

(6) In the case of an uncovered portion of an underlying exposure, an authorized institution must allocate a risk-weight calculated in the same manner as for any other direct exposure to the obligor in respect of the underlying exposure. *(L.N. 167 of 2023)*

218. *(Repealed L.N. 167 of 2023)*

219. Capital treatment of recognized guarantees and recognized credit derivative contracts in respect of purchased receivables

(1) Subject to subsections (2), (3) and (4), an authorized institution may take into account the credit risk mitigating effect of a recognized guarantee or recognized credit derivative contract for its exposures in respect of purchased receivables— *(L.N. 167 of 2023)*

(a) in accordance with sections 210, 211, 212, 213, 214, 215, 216 and 217; and *(L.N. 167 of 2023)*

(b) without regard to whether the guarantee or contract covers default risk or dilution risk, or both.

(2) Where—

(a) an authorized institution is the beneficiary of a recognized guarantee or has entered into a recognized credit derivative contract as protection buyer in respect of its exposure in respect of purchased receivables; and

(b) the guarantee or contract covers both default risk and dilution risk in respect of a purchased receivable or a portfolio of purchased receivables,

the institution shall, for the purposes of calculating the risk-weighted amount of its exposure in respect of the purchased receivable or the portfolio of purchased receivables, as the case may be, substitute the risk-weight of the exposure to the credit protection provider for the sum of the risk-weights for default risk and dilution risk which would otherwise be allocated to the exposure in respect of the purchased receivable or the purchased receivables in the portfolio, as the case may be, in accordance with sections 197, 198, 199 and 200.

(3) Where a recognized guarantee or recognized credit derivative contract covers only default risk or dilution risk, but not both, in respect of a purchased receivable or a portfolio of purchased receivables of an authorized institution, the institution shall, for the purposes of calculating the risk-weighted amount of its exposure for default risk and dilution risk in respect of the purchased receivable or the portfolio of purchased receivables, as the case may be— *(L.N. 167 of 2023)*

(a) substitute the risk-weight of the exposure to the credit protection provider for the risk-weight which would otherwise be allocated for default risk or dilution risk covered by the guarantee or contract in respect of the purchased receivable or the purchased receivables in the portfolio, as the case may be;

(b) calculate the risk-weighted amount of the institution's exposure for the other risk component (being default risk or dilution risk not covered by the guarantee or contract) in respect of the purchased receivable or the purchased receivables in the portfolio, as the case may be, in accordance with sections 197, 198, 199 and 200; and

(c) aggregate the risk-weighted amount calculated under paragraph (a) with the risk-weighted amount calculated under paragraph (b).

(4) Where a recognized guarantee or recognized credit derivative contract covers only a portion of default risk or dilution risk in respect of a purchased receivable or a portfolio of purchased receivables of an authorized institution, the institution shall, for the purposes of calculating the risk-weighted amount of its exposure for default risk and dilution risk in respect of the purchased receivable or the portfolio of purchased receivables, as the case may be—

(a) divide the exposure into a covered portion and an uncovered portion for default risk and dilution risk in accordance with section 216(2);

(b) calculate the risk-weighted amount of the uncovered portion of the exposure in respect of default risk and dilution risk in accordance with sections 197, 198, 199 and 200;

(c) calculate the risk-weighted amount of the covered portion of the exposure in respect of default risk and dilution risk in accordance with subsection (2); and

(d) aggregate the risk-weighted amount calculated under paragraph (b) with the risk-weighted amount calculated under paragraph (c).

(5)-(6) *(Repealed L.N. 167 of 2023)*

Division 11—Treatment of Expected Losses and Eligible Provisions

220. Calculation of expected losses and eligible provisions for corporate, sovereign, bank and retail exposures

(1) An authorized institution—

(a) shall compare the institution's total EL amount and the institution's total eligible provisions, as calculated in accordance with subsections (2), (3), (4) and (5) and section 221;

(b) if the total EL amount exceeds the total eligible provisions, shall deduct the difference from the institution's CET1 capital in accordance with section 43(1)(i); and

(c) if the total EL amount is less than the total eligible provisions, may, in accordance with section 42(3)(c), include the difference in its Tier 2 capital up to a maximum of 0.6% of the institution's risk-weighted amount for credit risk calculated by using the IRB approach. *(L.N. 156 of 2012)*

(2) Subject to subsections (3), (4) and (5), an authorized institution—

(a) shall calculate the EL as the PD multiplied by the LGD of each of its corporate, sovereign, bank and retail exposures which are not in default;

(b) subject to paragraph (c), shall determine and use its best estimate of the EL for each of its corporate, sovereign, bank and retail exposures which are in default based on current economic circumstances and the exposure's default status;

(c) may, if it uses the foundation IRB approach and has the prior consent of the Monetary Authority to do so, use the supervisory estimate for the LGD as the EL for its corporate, sovereign and bank exposures which are in default.

(3) Subject to subsection (4), where an authorized institution uses the supervisory slotting criteria approach for its specialized lending, the institution shall determine the EL amount of the specialized lending by multiplying the risk-weighted amount of the specialized lending by 8%.

(4) Subject to subsection (5), an authorized institution shall, for the purposes of subsection (3), determine the risk-weight to be used in the calculation of the risk-weighted amount of the specialized lending (being the EAD multiplied by the risk-weight) in accordance with Table 22 or 22A, whichever is applicable, by reference to the relevant supervisory rating grade to which the exposure has been mapped. *(L.N. 212 of 2015)*

Table 22

Risk-weights for Determination of EL Amount of Specialized Lending other than HVCRE Exposures

(L.N. 212 of 2015)

Strong	Good	Satisfactory	Weak	Default
5%	10%	35%	100%	625%

Table 22A

Risk-weights for Determination of EL Amount of HVCRE Exposures

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

(L.N. 212 of 2015)

(5) Where an authorized institution allocates preferential risk-weights to its specialized lending which falls within the "strong" and "good" grades in accordance with section 158(3), then, in the calculation of the risk-weighted amount of the specialized lending, the institution may allocate preferential risk-weights of 0% and 5% to the specialized lending which falls within the "strong" and "good" grades respectively in calculating the EL amount. *(L.N. 167 of 2023)*

(L.N. 137 of 2011)

221. Determination of eligible provisions for calculation of total eligible provisions

Where an authorized institution which uses the IRB approach also uses the STC approach to calculate its credit risk for a portion of its corporate, sovereign, bank or retail exposures, the institution shall exclude from the calculation of total eligible provisions those regulatory reserve for general banking risks and collective provisions which are attributable to that portion of its exposures subject to the STC approach in accordance with section 42(2).

(L.N. 156 of 2012; L.N. 175 of 2017)

222. EL amount—CIS exposures

(L.N. 54 of 2022; L.N. 167 of 2023)

(1) *(Repealed L.N. 167 of 2023)*

(2) An authorized institution must take the EL amount of its CIS exposures to be zero, regardless of the approach used in calculating the risk-weighted amounts of the CIS exposures. *(L.N. 54 of 2022)*

223. *(Repealed L.N. 167 of 2023)*

Division 12—*(Repealed L.N. 167 of 2023)*

224. *(Repealed L.N. 167 of 2023)*

Division 13—*(Repealed L.N. 167 of 2023)*

225-226. *(Repealed L.N. 167 of 2023)*

Part 6A

Calculation of Counterparty Credit Risk

(Part 6A added L.N. 156 of 2012)

Division 1—General

226A. Interpretation of Part 6A

In this Part—

commodity-related derivative contract (商品關聯衍生工具合約) means a derivative contract the value of which is determined by reference to the value of, or any fluctuation in the value of, one or more commodities (within the meaning of paragraph (a) of the definition of ***commodity*** in section 2(1)); *(L.N. 167 of 2023)*

credit protection covered portion (信用保障涵蓋部分) has the meaning given by section 51(1);

cross-product net amount (跨產品淨額), in relation to any bilateral master agreements or transactions covered by a valid cross-product netting agreement, means a net sum of—

(a) the positive and negative close-out values of the individual bilateral master agreements; and

(b) the positive and negative mark-to-market values of the individual transactions;

current exposure (現行風險承擔), in relation to the use of the IMM(CCR) approach and a netting set with a counterparty, means the larger of—

(a) zero; or

(b) the market value of the transaction or transactions within the netting set that would be lost upon the default of the counterparty (but assuming no recovery on the value of that transaction or those transactions in bankruptcy);

effective EE (有效EE) means effective expected exposure;

effective expected exposure (有效預期風險承擔), in relation to a netting set, means the amount calculated in accordance with section 226G;

initial margin (開倉保證金) has the meaning given by section 226V(1); *(L.N. 44 of 2020)*

margin agreement (保證金協議) means a contractual agreement or provisions to an agreement under which one counterparty must supply collateral to a second counterparty when an exposure of that second counterparty to the first counterparty exceeds a specified level;

margin period of risk (保證金風險期間) means, in the event of counterparty default, the period from the last exchange of collateral covering a netting set until the netting set can be closed out and the resulting market risk is re-hedged;

margin threshold (保證金門檻), in relation to a margin agreement, means the maximum amount of unsecured exposure above which one of the parties to the agreement has the right to call for collateral;

minimum transfer amount (最低轉移額), in relation to a margin agreement, means an amount below which no transfer of collateral is made;

payment transaction (付款交易) means a transaction that executes a payment or fund transfer;

recognized credit derivative contract (認可信用衍生工具合約) has the meaning given by section 51(1), 105, 139(1) or 227(1), as the case requires; *(L.N. 175 of 2017)*

specific wrong-way risk (特定錯向風險) means the risk that arises when the exposure to a counterparty is positively correlated with the probability of default of the counterparty due to the nature of the transactions with the counterparty;

spot transaction (即期交易) means a single outright transaction involving the delivery of a security, commodity, foreign currency or any other financial instrument against cash within a period that is regarded as an immediate delivery under the market standard for that particular security, commodity, currency or financial instrument at the current market price on the date of the transaction; *(L.N. 44 of 2020)*

underlying exposure (基礎風險承擔), in relation to a derivative contract, means the underlying asset, index, financial instrument, rate or thing as designated in the derivative contract; *(L.N. 44 of 2020)*

variation margin (變動保證金), in relation to a margin agreement between 2 counterparties, means the collateral posted by one counterparty to the other counterparty, or exchanged between the 2 counterparties, on a regular basis based on the price movement or change in value of one or more transactions subject to the agreement. *(L.N. 44 of 2020)*

(L.N. 167 of 2023)

226B. Valid cross-product netting agreement

(1) In this Part, a reference to a valid cross-product netting agreement is to be construed, in relation to an authorized institution's transactions with a counterparty that are covered by an IMM(CCR) approval, as an agreement (***netting arrangement***) in respect of which the conditions set out in subsection (2) are met.

(2) The conditions are—

(a) the netting arrangement—

(i) is in writing;

(ii) is bilateral between the institution and the counterparty;

(iii) permits netting across transactions of different product categories;

(iv) creates a single legal obligation for all individual bilateral master agreements and individual transactions covered by the netting arrangement; and

(v) provides, in effect, that the institution would have a single claim or obligation to receive or pay only the cross-product net amount, in the event that the counterparty to the netting arrangement, or a counterparty to whom the netting arrangement has been validly assigned, fails to comply with any obligation under any of the bilateral master agreements or transactions due to default, insolvency, bankruptcy, or similar circumstance;

(b) the institution has been given independent, written and reasoned legal advice that concludes with a high degree of certainty that, in the event of a challenge in a court of law or before an administrative authority, including a challenge resulting from default, insolvency, bankruptcy, or similar circumstance, the relevant court or administrative authority would find the institution's exposure to be the cross-product net amount under—

(i) the law of the jurisdiction in which the counterparty is incorporated or the equivalent location in the case of non-corporate entities, and if a branch of the counterparty is involved, then also under the law of the jurisdiction in which the branch is located;

(ii) the law that governs the individual bilateral master agreements and individual transactions covered by the netting arrangement; and

(iii) the law that governs the netting arrangement;

(c) the legal advice referred to in paragraph (b) addresses the validity and enforceability of the netting arrangement under its terms and the impact of the netting arrangement on the material provisions of any individual bilateral master agreement covered by the netting arrangement;

(d) the legal advice referred to in paragraph (b)—

(i) is generally recognized by the legal community in Hong Kong; or

(ii) is a memorandum of law that addresses all relevant issues in a reasoned manner;

(e) the institution establishes and maintains procedures to verify that any transaction that is covered by the netting arrangement and to be included in a netting set is covered by legal advice described in paragraphs (b), (c) and (d);

(f) the institution establishes and maintains procedures to monitor developments in any law relevant to the netting arrangement in order to ensure that the netting arrangement continues to satisfy the conditions set out in this subsection applicable to it;

(g) the netting arrangement is not subject to a provision that permits the non-defaulting counterparty to make only limited payment, or no payment at all, to the defaulter or the estate of the defaulter, regardless of whether the defaulter is a net creditor under the netting arrangement;

(h) each bilateral master agreement covered by the netting arrangement falls within the definition of ***valid bilateral netting agreement*** in section 2(1) and the credit risk mitigation for each transaction covered by the netting arrangement meets the applicable requirements for the recognition of credit risk mitigation set out in Part 4, 5 or 6, as the case may be;

(i) the institution maintains in its files documentation adequate to support the nettings under the netting arrangement;

(j) the institution measures and manages its aggregate credit exposure to the counterparty to the netting arrangement on a net basis; and

(k) the institution aggregates credit exposures to the counterparty to the netting arrangement to arrive at a single legal exposure across transactions covered by the netting arrangement and that aggregation is factored into credit limits and internal capital processes.

(3) For the purposes of subsection (2)—

(a) repo-style transactions;

(b) margin lending transactions; and

(c) derivative contracts,

are to be treated as different product categories.

Division 1A—SA-CCR Approach

(Division 1A added L.N. 44 of 2020)

Subdivision 1—Interpretation and Application

226BA. Interpretation of Division 1A

In this Division—

asset class (資產類別) means a class of derivative contracts referred to in section 226BL(1);

basis transaction (基準差交易) means a derivative contract under which both legs of the contract are denominated in the same currency and the cash flows of the 2 legs depend on different risk factors from the same asset class;

hedging set (對沖組合) means a hedging set of derivative contracts classified under section 226BM, 226BN, 226BO, 226BP or 226BQ;

independent collateral (獨立抵押品), in relation to derivative contracts in a netting set entered into between 2 counterparties—

(a) means the collateral posted by one counterparty (***first counterparty***) to the other counterparty—

(i) that may be seized on the default of the first counterparty to offset losses on the netting set; and

(ii) the amount of which the first counterparty is required to post (which could be expressed as a fixed percentage of the notional amounts of the contracts) does not change in response to the changes in the market value of the contracts it secures; and

(b) includes initial margin and independent amount;

margined contract (保證金合約) means a derivative contract of an authorized institution covered by a variation margin agreement, but excludes a derivative contract that is structured so that any outstanding exposure under the contract is settled daily;

unmargined contract (無保證金合約) means a derivative contract of an authorized institution that—

(a) is not covered by a variation margin agreement; or

(b) is structured so that any outstanding exposure under the contract is settled daily;

variation margin agreement (變動保證金協議) means a margin agreement entered into by an authorized institution with a counterparty under which the counterparty has an obligation to post variation margin to the institution;

volatility transaction (波動性交易) means a derivative contract the payment under which is determined by reference to a measure of the volatility (historical or implied) of a risk factor and the measure is explicitly specified in the contract.

226BB. Application of Division 1A

This Division applies to an authorized institution that uses the SA-CCR approach to calculate default risk exposures in respect of derivative contracts.

Subdivision 2—Main Formula: Default Risk Exposure as Function of Replacement Cost and Potential Future Exposure

226BC. Calculation of default risk exposure under SA-CCR approach of single netting set containing unmargined contracts only

(1) This section applies to a netting set that contains unmargined contracts only.

(2) Subject to sections 226BH and 226BI, an authorized institution must use Formula 23AA to calculate the default risk exposure in respect of the netting set.

Formula 23AA

$$\text{Default risk exposure} = \alpha \times (\text{RC} + \text{PFE})$$

where—

(a) $\alpha = 1.4$;

(b) RC is the replacement cost of the netting set calculated in accordance with subsection (3); and

(c) PFE is the potential future exposure of the netting set calculated in accordance with section 226BR(1).

(3) Subject to subsection (4), the replacement cost of the netting set is calculated by using Formula 23AB.

Formula 23AB

$$RC = \max(V - C\ ;\ 0)$$

where—

(a) RC is the replacement cost of the netting set;

(b) V is the current mark-to-market value of the netting set; and

(c) C is the haircut value of net collateral held for the netting set, which is equal to the net amount of independent collateral for the netting set calculated in accordance with section 226BJ(3).

(4) If the netting set is subject to a margin agreement entered into by an authorized institution with a counterparty under which only the institution has an obligation to post variation margin, C in Formula 23AB is calculated by subtracting the value specified in paragraph (b) from the amount specified in paragraph (a)—

(a) the net amount of independent collateral for the netting set calculated in accordance with section 226BJ(3);

(b) the haircut value of variation margin posted by the institution under the margin agreement calculated in accordance with section 226BJ(4).

226BD. Calculation of default risk exposure under SA-CCR approach of single netting set covered by single variation margin agreement

(1) This section applies to a netting set—

(a) that is covered by a single variation margin agreement; and

(b) that contains margined contracts only.

(2) Subject to sections 226BH and 226BI, an authorized institution must use Formula 23AC to calculate the default risk exposure in respect of the netting set.

Formula 23AC

$$\text{Default risk exposure} = \alpha \times (\text{RC} + \text{PFE})$$

where—

(a) $\alpha = 1.4$;

(b) RC is the replacement cost of the netting set calculated in accordance with subsection (3); and

(c) PFE is the potential future exposure of the netting set calculated in accordance with section 226BR(1).

(3) The replacement cost of the netting set is calculated by using Formula 23AD.

Formula 23AD

$$RC = \max (V - C\ ;\ TH + MTA - NICA\ ;\ 0)$$

where—

(a) RC is the replacement cost of the netting set;

(b) V is the current mark-to-market value of the netting set;

(c) NICA is the net amount of independent collateral for the netting set calculated in accordance with section 226BJ(3);

(d) C is the haircut value of net collateral held for the netting set, which is calculated as the sum of the net amount of non-independent collateral calculated in accordance with section 226BJ(1) and the NICA;

(e) TH is the margin threshold specified in the variation margin agreement concerned; and

(f) MTA is the minimum transfer amount specified in the variation margin agreement concerned.

226BE. Calculation of default risk exposure under SA-CCR approach of multiple netting sets covered by single variation margin agreement

(1) This section applies to netting sets—

(a) that are covered by a single variation margin agreement; and

(b) that contain margined contracts only.

(2) Subject to sections 226BH and 226BI, an authorized institution must use Formula 23AE to calculate the default risk exposure in respect of the netting sets.

Formula 23AE

$$\text{Default risk exposure} = \alpha \times (\text{RC} + \text{PFE})$$

where—

(a) $\alpha = 1.4$;

(b) RC is the replacement cost of the netting sets calculated in accordance with subsection (3); and

(c) PFE is the potential future exposure of the netting sets calculated in accordance with section 226BS.

(3) The replacement cost of the netting sets is calculated by using Formula 23AF.

Formula 23AF

$$RC_{MA} = \max\left\{\sum_{NS \in MA} \max\{V_{NS} ; 0\} - \max\{C_{MA} ; 0\} ; 0\right\} + X$$

$$X = \max\left\{\sum_{NS \in MA} \min\{V_{NS} ; 0\} - \min\{C_{MA} ; 0\} ; 0\right\}$$

where—

(a) RC_{MA} is the replacement cost of all netting sets subject to variation margin agreement MA;

(b) V_{NS} is the current mark-to-market value of netting set NS;

(c) C_{MA} is the haircut value of net collateral held under variation margin agreement MA, which is calculated as the sum of the net amount of non-independent collateral calculated in accordance with section 226BJ(1) and the net amount of independent collateral calculated in accordance with section 226BJ(3); and

(d) $NS \in MA$ means netting set NS is covered by variation margin agreement MA.

226BF. Calculation of default risk exposure under SA-CCR approach of single netting set covered by multiple variation margin agreements

(1) This section applies to a netting set—

(a) that is covered by more than one variation margin agreement; and

(b) that contains margined contracts only.

(2) Subject to sections 226BH and 226BI, an authorized institution must use Formula 23AG to calculate the default risk exposure in respect of the netting set.

Formula 23AG

$$\text{Default risk exposure} = \alpha \times (\text{RC} + \text{PFE})$$

where—

(a) $\alpha = 1.4$;

(b) RC is the replacement cost of the netting set calculated in accordance with subsection (3); and

(c) PFE is the potential future exposure of the netting set calculated in accordance with section 226BR(2).

(3) The replacement cost of the netting set is calculated by using Formula 23AH.

Formula 23AH

$$\text{RC} = \max\,(\text{V} - \text{C}\ ;\ \text{TH} + \text{MTA} - \text{NICA}\ ;\ 0)$$

where—

(a) RC is the replacement cost of the netting set;

(b) V is the current mark-to-market value of the netting set;

(c) NICA is the net amount of independent collateral for the netting set calculated in accordance with section 226BJ(3);

(d) C is the haircut value of net collateral held for the netting set, which is calculated as the sum of the net amount of non-independent collateral calculated in accordance with section 226BJ(2) and the NICA;

(e) TH is the sum of the margin thresholds across all the variation margin agreements covering the margined contracts in the netting set; and

(f) MTA is the sum of the minimum transfer amounts across all the variation margin agreements covering the margined contracts in the netting set.

226BG. Calculation of default risk exposure under SA-CCR approach of single netting set containing both margined contracts and unmargined contracts

(1) This section applies to a netting set that contains both margined contracts (which may be covered by one or more than one variation margin agreement) and unmargined contracts.

(2) Subject to sections 226BH and 226BI, an authorized institution must use Formula 23AI to calculate the default risk exposure in respect of the netting set.

Formula 23AI

$$\text{Default risk exposure} = \alpha \times (\text{RC} + \text{PFE})$$

where—

(a) $\alpha = 1.4$;

(b) RC is the replacement cost of the netting set calculated in accordance with subsection (3); and

(c) PFE is the potential future exposure of the netting set calculated in accordance with section 226BR(2).

(3) Subject to subsection (4), the replacement cost of the netting set is calculated by using Formula 23AJ.

Formula 23AJ

$$RC = \max(V - C\ ;\ TH + MTA - NICA\ ;\ 0)$$

where—

(a) RC is the replacement cost of the netting set;

(b) V is the current mark-to-market value of all the margined contracts and unmargined contracts in the netting set;

(c) NICA is the net amount of independent collateral for the netting set calculated in accordance with section 226BJ(3);

(d) C is the haircut value of net collateral held for all the margined contracts and unmargined contracts in the netting set, which is calculated as the sum of the net amount of non-independent collateral calculated in accordance with section 226BJ(1) or (2) and the NICA;

(e) TH is—

(i) if the margined contracts in the netting set are covered by a single variation margin agreement—the margin threshold specified in that agreement; or

(ii) if the margined contracts in the netting set are covered by more than one variation margin agreement—the sum of the margin thresholds across all the variation margin agreements covering the margined contracts; and

(f) MTA is—

(i) if the margined contracts in netting set are covered by a single variation margin agreement—the minimum transfer amount specified in that agreement; or

(ii) if the margined contracts in the netting set are covered by more than one variation margin agreement—the sum of the minimum transfer amounts across all the variation margin agreements covering the margined contracts.

(4) If some of the contracts in the netting set are subject to a margin agreement entered into by an authorized institution with a counterparty under which only the institution has an

obligation to post variation margin, C in Formula 23AJ is calculated by subtracting the value specified in paragraph (b) from the sum specified in paragraph (a)—

(a) the sum of the net amount of non-independent collateral calculated in accordance with section 226BJ(1) or (2) and the NICA calculated in accordance with section 226BJ(3);

(b) the haircut value of variation margin posted by the institution under the margin agreement calculated in accordance with section 226BJ(4).

226BH. Determination of default risk exposure in certain circumstances

(1) Subject to subsections (2), (3), (4) and (5), the amount of default risk exposure of a netting set that contains margined contracts (whether exclusively or not) calculated under section 226BD, 226BF or 226BG is capped at the amount that would have been calculated under section 226BC if the margined contracts in the netting set were unmargined contracts.

(2) If—

(a) a sold option of an authorized institution is not subject to any recognized netting;

(b) the premium for the option has been fully paid upfront by the counterparty concerned; and

(c) the option is not subject to any margin agreement,

the amount of default risk exposure to the counterparty in respect of the option may be set to zero.

(3) If a sold option of an authorized institution meets the criteria in subsection (2)(b) and (c) but is a transaction within a netting set that falls within paragraph (a)(i) of the definition of ***netting set*** in section 2(1), the amount of default risk

exposure to the counterparty concerned in respect of the option may be set to zero only if—

(a) the netting set contains sold options only; or

(b) the sold option is removed from the netting set such that the default risk exposure in respect of the netting set is calculated without taking into account the sold option.

(4) If—

(a) an authorized institution is the protection seller in respect of a credit-related derivative contract with periodic premium payments and the contract is not subject to any recognized netting;

(b) the contract is not a sold option; and

(c) the contract is not subject to any margin agreement,

the amount of default risk exposure to the protection buyer in respect of the contract calculated under section 226BC is capped at the amount of the unpaid premium under the contract.

(5) If an authorized institution is the protection seller in respect of a credit-related derivative contract with periodic premium payments and the contract is a transaction within a netting set that falls within paragraph (a)(i) of the definition of ***netting set*** in section 2(1), the institution may apply the cap referred to in subsection (4) to the default risk exposure to the protection buyer in respect of the contract only if the institution—

(a) removes the contract from the netting net; and

(b) calculates the amount of the default risk exposure in accordance with section 226BC as if the contract were not subject to recognized netting and not subject to any margin agreement.

226BI. Treatments for certain credit derivative contracts

An authorized institution may treat the default risk exposure in respect of a credit derivative contract as zero if—

(a) both of the following conditions are met—

(i) the contract is a credit default swap in which the institution is the protection seller;

(ii) a regulatory capital is held in respect of the risk-weighted amount calculated in accordance with Part 4, 5, 6 or 7, as the case requires, for the institution's exposure to the credit risk of the reference obligation underlying the swap; or

(b) both of the following conditions are met—

(i) the institution is the protection buyer in the contract;

(ii) the credit risk mitigation effect of the contract has been recognized and taken into account under Divisions 9 and 10 of Part 4, Divisions 7 and 8 of Part 5, Division 10 of Part 6, or Division 5 of Part 7, for the purpose of calculating the risk-weighted amount of the exposure to which credit protection is provided by the contract.

226BJ. Calculation of haircut value of net collateral held

(1) In calculating the haircut value of net collateral held by an authorized institution for section 226BD(3), 226BE(3) or 226BG(3), the net amount of non-independent collateral referred to in that section must be calculated by using Formula 23AK.

Formula 23AK

$$C_{non\text{-}IC} = C_{received} \cdot [1 - H] - C_{posted} \cdot [1 + H]$$

where—

(a) $C_{non\text{-}IC}$ is the net amount of non-independent collateral held (if the resulting amount is positive) or posted (if the resulting amount is negative) under the variation margin agreement concerned;

(b) $C_{received}$ is the current market value of collateral (including variation margin but excluding independent collateral) received by the institution under the variation margin agreement concerned;

(c) C_{posted} is the current market value of collateral (including variation margin but excluding independent collateral) posted by the institution under the variation margin agreement concerned; and

(d) H is the standard supervisory haircut applicable to the collateral concerned, subject to adjustment set out in section 3 of Schedule 7 based on the margin period of risk appropriate for the derivative contracts concerned determined in accordance with section 226BZE(2), (3), (4), (5) and (6).

(2) In calculating the haircut value of net collateral held by an authorized institution for section 226BF(3) or 226BG(3), the net amount of non-independent collateral referred to in that section must be calculated as the sum of the net amount of non-independent collateral held or posted under each of the

variation margin agreements concerned calculated by using Formula 23AK.

(3) In calculating the haircut value of net collateral held by an authorized institution for section 226BC(3), 226BD(3), 226BE(3), 226BF(3) or 226BG(3), the net amount of independent collateral must be calculated by using Formula 23AL.

Formula 23AL

$$NICA = ICA_{received} \cdot [1 - H] - ICA_{posted} \cdot [1 + H]$$

where—

(a) NICA is the net amount of independent collateral held (if the resulting amount is positive) or posted (if the resulting amount is negative);

(b) $ICA_{received}$ is the current market value of independent collateral posted by the counterparty concerned to the institution (regardless of whether the collateral is segregated in a bankruptcy remote account or not);

(c) ICA_{posted} is the current market value of independent collateral posted by the institution to the same counterparty, where the collateral is unsegregated collateral; and

(d) H is the standard supervisory haircut applicable to the collateral concerned, subject to adjustment set out in section 3 of Schedule 7 based on—

(i) if the collateral is received or posted for unmargined contracts—the lower of—

(A) the minimum holding period calculated by using Formula 5A in section 91 with N_R in that formula being construed to mean the period from the current date to the maturity date of the contract in the netting set concerned that has the longest residual maturity; or

(B) a minimum holding period of 250 days; or

(ii) if the collateral is received or posted for margined contracts—the margin period of risk appropriate for the derivative contracts concerned determined in accordance with section 226BZE(2), (3), (4), (5) and (6).

(4) The haircut value of variation margin posted by an authorized institution referred to in sections 226BC(4) and 226BG(4) is calculated as the product of—

(a) the current market value of the variation margin posted by the authorized institution concerned; and

(b) a factor of (1 + H), where H has the same meaning as given by subsection (3) for collateral received or posted for unmargined contracts.

(5) Collateral posted to an authorized institution by a counterparty may be included in the calculation under subsection (1), (2) or (3) only if—

(a) the collateral—

(i) falls within the description in section 79(1) (excluding section 79(1)(o)) or 80(1)(b) or (c); and

(ii) meets the criteria specified in section 77(2); and *(L.N. 167 of 2023)*

(b) the collateral is not a re-securitization exposure.

(6) An authorized institution must include all collateral posted by it (except independent collateral that is not unsegregated collateral) to a counterparty in the calculation under subsection (1), (2), (3) or (4), regardless of whether the collateral meets the conditions set out in subsection (5)(a) and (b).

(7) If collateral that meets the descriptions in subsection (5) is received by an authorized institution outside a netting set but is available to offset losses on default risk exposures, the institution must, for the purposes of this section, treat the collateral in the following way—

(a) subject to paragraph (b)—

(i) if the collateral is available to offset losses on 1 netting set only, the collateral must be treated as an independent collateral received for that netting set; or

(ii) if the collateral is available to offset losses on more than one netting set, the collateral must be treated as if it were an independent collateral received under a single variation margin agreement that applies to multiple netting sets;

(b) if the collateral is available to offset not only losses on default risk exposures but also losses on exposures that are not default risk exposures, only that portion of the collateral designated solely for offsetting losses on default risk exposures can be treated as an independent collateral under paragraph (a)(i) or (ii).

226BK. Authorized institution to hold regulatory capital for credit risk or market risk of posted collateral

To avoid doubt, an authorized institution must, for collateral posted by it for a derivative contract (whether the collateral is included in the calculations under section 226BJ or not), hold regulatory capital for the credit risk or market risk, whichever is applicable, of the collateral itself calculated under Part 4, 5, 6, 7 or 8, as the case requires—

(a) as if it had not been posted as collateral; and

(b) if the collateral is held by another person, as if the collateral were held by the institution.

Subdivision 3—Classification of Derivative Contracts into Asset Classes and Further Classification into Hedging Sets

226BL. Classification of derivative contracts into asset classes

(1) Subject to subsections (2), (3) and (4), an authorized institution must classify each of the derivative contracts in a netting set into one of the following 5 asset classes—

(a) interest rate contracts;

(b) exchange rate contracts;

(c) credit-related derivative contracts;

(d) equity-related derivative contracts;

(e) commodity-related derivative contracts.

(2) In classifying a derivative contract, an authorized institution must—

(a) first determine the primary risk factor of the contract taking into account the sensitivities and volatility of the underlying exposure of the contract; and

(b) then—

(i) if the primary risk factor of the contract so determined is inflation—classify the contract into the asset class of interest rate contracts; or

(ii) in any other case—classify the contract into an asset class based on the contract's primary risk factor.

(3) The Monetary Authority may, by written notice given to an authorized institution, require the institution to classify a derivative contract of the institution into more than one asset class if the Monetary Authority considers that classifying the contract into only 1 asset class would significantly underestimate the default risk exposure in respect of the contract.

(4) An authorized institution given a notice under subsection (3) must, unless otherwise specified by the Monetary Authority in the notice—

(a) include the full position of the contract in each of the asset classes into which the contract is classified and determine the sign of each relevant risk factor in an appropriate way; and

(b) determine, for each asset class, the supervisory delta adjustment applicable to the contract in respect of the position included in the asset class in accordance with section 226BZB.

(5) An authorized institution must comply with the requirements of a notice given to it under subsection (3).

226BM. Further classification of derivative contracts in asset class of interest rate contracts

(1) All derivative contracts in a netting set that fall within the asset class of interest rate contracts must be further classified

into different hedging sets as follows—

(a) non-inflation derivative contracts that are basis transactions referencing the same pair of risk factors must be grouped together to form a hedging set;

(b) inflation derivative contracts that are basis transactions referencing the same pair of risk factors must be grouped together to form a hedging set;

(c) non-inflation derivative contracts that are volatility transactions referencing interest rates of the same currency must be grouped together to form a hedging set;

(d) inflation derivative contracts that are volatility transactions referencing measures of inflation for the same currency must be grouped together to form a hedging set;

(e) non-inflation derivative contracts (other than basis transactions or volatility transactions) referencing interest rates of the same currency must be grouped together to form a hedging set; and

(f) inflation derivative contracts (other than basis transactions or volatility transactions) referencing measures of inflation for the same currency must be grouped together to form a hedging set.

(2) A derivative contract classified into a hedging set under subsection (1) must be further allocated into a maturity bucket in accordance with Table 23AA.

Table 23AA

Column 1	Column 2
End date (E) applicable to a derivative contract	Maturity bucket (MB_k)
< 1 year	k = 1
≧1 year and ≦5 years	k = 2
> 5 years	k = 3

(3) For the purposes of subsection (2), the value of E applicable to a derivative contract is determined in the same way as the value of E in Formula 23AZ in section 226BZC(2).

(4) In this section—

non-inflation derivative contract (非通脹衍生工具合約) means a derivative contract in the asset class of interest rate contracts that is not an inflation derivative contract.

226BN. Further classification of derivative contracts in asset class of exchange rate contracts

All derivative contracts in a netting set that fall within the asset class of exchange rate contracts must be further classified into different hedging sets as follows—

(a) volatility transactions referencing the same currency pair, or the same currency index, must be grouped together to form a hedging set; and

(b) contracts (other than volatility transactions) referencing the same currency pair, or the same currency index, must be grouped together to form a hedging set.

226BO. Further classification of derivative contracts in asset class of credit-related derivative contracts

(1) All derivative contracts in a netting set that fall within the asset class of credit-related derivative contracts must be further classified into different hedging sets as follows—

(a) basis transactions referencing the same pair of risk factors must be grouped together to form a hedging set;

(b) volatility transactions must be grouped together to form a hedging set; and

(c) all other contracts must be grouped together to form a hedging set.

(2) Derivative contracts classified into a hedging set under subsection (1) must be further classified into different subsets by grouping contracts within the hedging set that reference the same entity together to form a subset.

(3) For the purposes of subsection (2), a credit index is regarded as an entity and each separate credit index referenced by the derivative contracts must be treated as a separate entity.

226BP. Further classification of derivative contracts in asset class of equity-related derivative contracts

(1) All derivative contracts in a netting set that fall within the asset class of equity-related derivative contracts must be further classified into different hedging sets as follows—

(a) basis transactions referencing the same pair of risk factors must be grouped together to form a hedging set;

(b) volatility transactions must be grouped together to form a hedging set; and

(c) all other contracts must be grouped together to form a hedging set.

(2) Derivative contracts classified into a hedging set under subsection (1) must be further classified into different subsets by grouping contracts within the hedging set that reference the same entity together to form a subset.

(3) For the purposes of subsection (2), an equity index is regarded as an entity and each separate equity index referenced by the derivative contracts must be treated as a separate entity.

226BQ. Further classification of derivative contracts in asset class of commodity-related derivative contracts

(1) All derivative contracts in a netting set that fall within the asset class of commodity-related derivative contracts must be further classified into different hedging sets as follows—

(a) basis transactions referencing the same pair of risk factors must be grouped together to form a hedging set;

(b) volatility transactions must be assigned into one of the following hedging sets based on the underlying commodities of the transactions—

(i) energy;

(ii) metals;

(iii) agricultural products;

(iv) other commodities; and

(c) all other contracts must be assigned into one of the following hedging sets based on the underlying commodities of the contracts—

(i) energy;

(ii) metals;

(iii) agricultural products;

(iv) other commodities.

(2) Subject to subsection (3), derivative contracts classified into a hedging set under subsection (1) must be further classified into different subsets based on the type of underlying commodity into which the underlying exposures of the contracts fall.

(3) For the purpose of further classifying contracts in the hedging set of energy (mentioned in subsection (1)(b)(i) or (c)(i)) into different subsets under subsection (2), there must be at least the following 2 subsets—

(a) electricity;

(b) oil and gas.

(4) If the Monetary Authority considers that an authorized institution is significantly exposed to the basis risk resulting from different products within a hedging set or subset, the Monetary Authority may, by written notice given to the institution, require the institution to use more refined definitions of commodity types to define the subsets in the hedging set.

(5) An authorized institution must comply with the requirement of a notice given to it under subsection (4).

Subdivision 4—Calculation of Potential Future Exposure

226BR. Calculation of potential future exposure of netting set

(1) The potential future exposure of a netting set mentioned in section 226BC or 226BD is calculated by using Formula 23AM.

Formula 23AM

$$\text{PFE} = \text{multiplier} \cdot \sum_{a} \text{AddOn}^{(a)}$$

where—

(a) PFE is the potential future exposure of the netting set;

(b) multiplier is the amount calculated in accordance with subsection (3); and

(c) $AddOn^{(a)}$ is the add-on for derivative contracts in the netting set that fall within asset class a calculated in accordance with section 226BT.

(2) The potential future exposure of a netting set mentioned in section 226BF or 226BG is calculated by using Formula 23AM but $AddOn^{(a)}$ must be computed by—

(a) dividing the netting set into sub-netting sets such that—

(i) all margined contracts with the same margin period of risk are grouped together to form a sub-netting set; and

(ii) all unmargined contracts, if any, are grouped together to form a sub-netting set;

(b) calculating the add-on for derivative contracts in each of the sub-netting sets that fall within asset class a in accordance with section 226BT as if each of the sub-netting sets were a netting set; and

(c) aggregating all the add-ons obtained under paragraph (b).

(3) The multiplier in Formula 23AM is calculated by using Formula 23AN.

Formula 23AN

$$\text{multiplier} = \min\{1; \text{Floor} + (1 - \text{Floor}) \cdot A\}$$

$$A = \exp\left(\frac{V - C}{2 \cdot (1 - \text{Floor}) \cdot \sum_a \text{AddOn}^{(a)}}\right)$$

where—

(a) V and C have the same meaning as in Formula 23AB, 23AD, 23AH or 23AJ, as the case requires;

(b) Floor is 5%;

(c) exp (...) is the exponential function; and

(d) $\text{AddOn}^{(a)}$ has the same meaning as in Formula 23AM or subsection (2), as the case requires.

226BS. Calculation of potential future exposure of netting sets covered by same variation margin agreement

The potential future exposure of netting sets mentioned in section 226BE is calculated by using Formula 23AO.

Formula 23AO

$$PFE_{MA} = \sum_{NS \in MA} PFE_{NS}^{(\text{unmargined})}$$

where—

(a) PFE_{MA} is the potential future exposure of all netting sets subject to variation margin agreement MA;

(b) $PFE_{NS}^{(unmargined)}$ is the potential future exposure of netting set NS calculated in accordance with section 226BR(1) in a way as if netting set NS were not subject to any variation margin agreement; and

(c) $NS \in MA$ means netting set NS is covered by variation margin agreement MA.

Subdivision 5—Calculation of Add-on

226BT. Calculation of add-on for derivative contracts in same asset class

(1) The add-on for derivative contracts in a netting set that fall within the same asset class is calculated in accordance with subsection (2) or (3), as the case requires.

(2) If the asset class concerned is interest rate contracts, exchange rate contracts or commodity-related derivative contracts, the add-on must be calculated by using Formula 23AP.

Formula 23AP

$$AddOn^{(a)} = \sum_{j} AddOn_{j}^{(a)}$$

where—

(a) $AddOn^{(a)}$ is the add-on for derivative contracts in the netting set that fall within asset class a; and

(b) $\mathrm{AddOn}_j^{(a)}$ is the add-on for derivative contracts in the netting set that fall within hedging set j in asset class a, calculated in accordance with section 226BU, 226BV or 226BY, as the case requires.

(3) Subject to subsection (4), if the asset class concerned is credit-related derivative contracts or equity-related derivative contracts, the add-on must be calculated by using Formula 23AQ.

Formula 23AQ

$$\mathrm{AddOn}^{(a)} = \left[\left(\sum_k \rho_k \cdot \mathrm{AddOn}(\mathrm{Entity}_k)\right)^2 + I^{(a)}\right]^{0.5}$$

$$I^{(a)} = \sum_k \left(1 - (\rho_k)^2\right) \cdot \left(\mathrm{AddOn}(\mathrm{Entity}_k)\right)^2$$

where—

(a) $\mathrm{AddOn}^{(a)}$ is the add-on for derivative contracts in the netting set that fall within asset class a;

(b) $\mathrm{AddOn}(\mathrm{Entity}_k)$ is the add-on for a subset of the derivative contracts that reference entity k calculated in accordance with section 226BW or 226BX, as the case requires; and

(c) ρ_k is the correlation factor applicable to entity k, which is—

(i) 50% if entity k is a single entity; or

(ii) 80% if entity k is an index.

(4) If the contracts falling within the asset class of credit-related derivative contracts or equity-related derivative contracts form more than one hedging set, an authorized institution must calculate a separate add-on for each of the hedging sets in accordance with subsection (3) as if a reference to netting set in that subsection were a reference to hedging set.

226BU. Calculation of add-on for hedging sets in asset class of interest rate contracts

(1) An authorized institution must calculate the add-on for a hedging set in the asset class of interest rate contracts by using Formula 23AR.

Formula 23AR

$$\mathrm{AddOn}_j^{(IR)} = \mathrm{SF}_j^{(IR)} \cdot \text{Effective Notional}_j^{(IR)}$$

where—

(a) $\mathrm{AddOn}_j^{(IR)}$ is the add-on for hedging set j in the asset class of interest rate contracts;

(b) $SF_j^{(IR)}$ is the supervisory factor for hedging set j, which is, subject to adjustments set out in section 226BZ—

(i) 0.5% if hedging set j comprises interest rate contracts; or

(ii) 0.5% if hedging set j comprises inflation derivative contracts; and

(c) $\text{Effective Notional}_j^{(IR)}$ is the effective notional amount for hedging set j calculated in accordance with subsection (2).

(2) An authorized institution may use either Formula 23AS or Formula 23AT to calculate $\text{Effective Notional}_j^{(IR)}$ in Formula 23AR.

Formula 23AS

$$\text{Effective Notional}_j^{(IR)} = \left[\left(D^{(MB1)}\right)^2 + \left(D^{(MB2)}\right)^2 + \left(D^{(MB3)}\right)^2 + A\right]^{0.5}$$

$$A = 1.4 \cdot D^{(MB1)} \cdot D^{(MB2)} + 1.4 \cdot D^{(MB2)} \cdot D^{(MB3)}$$

$$+ 0.6 \cdot D^{(MB1)} \cdot D^{(MB3)}$$

Formula 23AT

$$\text{Effective Notional}_j^{(IR)} = \left|D^{(MB1)}\right| + \left|D^{(MB2)}\right| + \left|D^{(MB3)}\right|$$

where—

$D^{(MB1)}$, $D^{(MB2)}$ and $D^{(MB3)}$ are the effective notional amounts calculated in accordance with section 226BZA(2) respectively for maturity buckets 1, 2 and 3 (as allocated in accordance with section 226BM(2)) in hedging set j.

226BV. Calculation of add-on for hedging sets in asset class of exchange rate contracts

An authorized institution must calculate the add-on for a hedging set in the asset class of exchange rate contracts by using Formula 23AU.

Formula 23AU

$$\text{AddOn}_j^{(FX)} = SF^{(FX)} \cdot \left|\text{Effective Notional}_j^{(FX)}\right|$$

where—

(a) $\text{AddOn}_j^{(FX)}$ is the add-on for hedging set j in the asset class of exchange rate contracts;

(b) $SF^{(FX)}$ is the supervisory factor for the asset class of exchange rate contracts, which is equal to 4%, subject to adjustments set out in section 226BZ; and

(c) $\text{Effective Notional}_j^{(FX)}$ is the effective notional amount for hedging set j calculated in accordance with section 226BZA(3).

226BW. Calculation of add-on for subsets in asset class of credit-related derivative contracts

(1) An authorized institution must calculate the add-on for derivative contracts in a subset (as classified in accordance with section 226BO(2)) in the asset class of credit-related derivative contracts by using Formula 23AV.

Formula 23AV

$$\text{AddOn}\left(\text{Entity}_k\right) = \text{SF}_k^{(\text{Credit})} \cdot \text{Effective Notional}_k^{(\text{Credit})}$$

where—

(a) $\text{AddOn}\left(\text{Entity}_k\right)$ is the add-on for a subset comprising contracts that reference entity k;

(b) $\text{SF}_k^{(\text{Credit})}$ is the supervisory factor for entity k determined in accordance with subsection (2) or (3), subject to adjustments set out in section 226BZ; and

(c) $\text{Effective Notional}_k^{(\text{Credit})}$ is the effective notional amount for contracts in the subset calculated in accordance with section 226BZA(4).

(2) For a contract referencing entity k (including a contract whose underlying exposure is a credit instrument issued by entity k or a credit-related derivative contract referencing entity k)—

(a) subject to paragraph (b), if entity k is a single entity, an authorized institution must—

(i) determine the credit quality grade applicable to the ECAI issuer rating of entity k or the long-term ECAI issue specific rating of the credit instrument, as the case may be, by mapping the rating to a credit quality grade in accordance with the LT ECAI rating mapping table for Type A ECAIs; and

(ii) determine the supervisory factor applicable to entity k by mapping the resultant credit quality grade to the corresponding supervisory factor in accordance with Table 23AB;

Table 23AB

Column 1	Column 2	Column 3
Item	Credit quality grade	Supervisory factor (%)
1.	1, 2	0.38
2.	3	0.42
3.	4	0.54
4.	5	1.06
5.	6	1.6
6.	7	6.0

(L.N. 167 of 2023)

(b) if entity k referred to in paragraph (a) is a corporate incorporated in the home jurisdiction of a Type B ECAI, an authorized institution may— *(L.N. 167 of 2023)*

(i) choose to determine the supervisory factor applicable to entity k by mapping the ECAI issuer rating of entity k or the long-term ECAI issue specific rating of the credit instrument, as the case may be, assigned by that Type B ECAI to a credit quality grade in accordance with the LT ECAI rating mapping table for Type B ECAIs; and

(ii) determine the supervisory factor applicable to entity k by mapping the resultant credit quality grade to the corresponding supervisory factor in accordance with Table 23AC;

Table 23AC

Column 1	Column 2	Column 3
Item	Credit quality grade	Supervisory factor (%)
1.	1	0.38
2.	2	0.42
3.	3	0.54
4.	4	1.06
5.	5	1.6
6.	6, 7	6.0

(L.N. 167 of 2023)

(c) if neither ECAI issuer rating nor long-term ECAI issue specific rating is available for determination of the supervisory factor for entity k in accordance with paragraph (a) or (b), the supervisory factor applicable to entity k is 1.06%. *(L.N. 167 of 2023)*

(3) For a contract referencing entity k (including a contract whose underlying exposure is a credit-related derivative contract referencing entity k), if entity k is an index, an authorized institution must—

(a) determine whether the index is an investment grade index or a non-investment grade index; and

(b) determine the supervisory factor applicable to entity k based on the type of index in accordance with Table 23AD.

Table 23AD

Column 1	Column 2
Type of index	Supervisory factor (%)
Investment grade index	0.38
Non-investment grade index	1.06

(4) For the purposes of subsection (3) and Table 23AD—

(a) an index is an investment grade index where the minimum credit rating specified by the index service provider concerned for the purpose of determining whether an entity is eligible for being included in the index—

(i) if mapped to a credit quality grade in accordance with the LT ECAI rating mapping table for Type A ECAIs—would be mapped to a credit quality grade of 1, 2, 3 or 4; or

(ii) if mapped to a credit quality grade in accordance with the LT ECAI rating mapping table for Type B ECAIs—would be mapped to a credit quality grade of 1, 2 or 3; and *(L.N. 167 of 2023)*

(b) a non-investment grade index is an index that is not an investment grade index.

(5) In complying with subsection (2)(a) or (b) in relation to entity k, an authorized institution must, if there is more than one

ECAI issuer rating or more than one long-term ECAI issue specific rating the use of which would result in the allocation by the institution of different supervisory factors to entity k, determine the ECAI rating to be used in the same way as that set out in section 54E(2). *(L.N. 167 of 2023)*

226BX. Calculation of add-on for subsets in asset class of equity-related derivative contracts

An authorized institution must calculate an add-on for derivative contracts in a subset (as classified in accordance with section 226BP(2)) in the asset class of equity-related derivative contracts by using Formula 23AW.

Formula 23AW

$$\mathrm{AddOn}\left(\mathrm{Entity}_k\right) = \mathrm{SF}_k^{(\mathrm{Equity})} \cdot \mathrm{Effective\ Notional}_k^{(\mathrm{Equity})}$$

where—

(a) $\mathrm{AddOn}\left(\mathrm{Entity}_k\right)$ is the add-on for a subset comprising contracts that reference entity k;

(b) $\mathrm{SF}_k^{(\mathrm{Equity})}$ is the supervisory factor for entity k which is, subject to adjustments set out in section 226BZ—

(i) 32% if entity k is a single entity; or

(ii) 20% if entity k is an index; and

(c) $\mathrm{Effective\ Notional}_k^{(\mathrm{Equity})}$ is the effective notional amount for contracts in the subset calculated in accordance with section 226BZA(4).

226BY. Calculation of add-on for hedging sets in asset class of commodity-related derivative contracts

An authorized institution must calculate the add-on for a hedging set in the asset class of commodity-related derivative contracts by using Formula 23AX.

Formula 23AX

$$\mathrm{AddOn}_j^{(\mathrm{Com})} = \left[\left(\rho^{(\mathrm{Com})} \cdot \sum_k \mathrm{AddOn}\left(\mathrm{Type}_k^j\right)\right)^2 + \mathrm{I}_j^{(\mathrm{Com})}\right]^{0.5}$$

$$\mathrm{I}_j^{(\mathrm{Com})} = \left(1 - \left(\rho^{(\mathrm{Com})}\right)^2\right) \cdot \sum_k \left(\mathrm{AddOn}\left(\mathrm{Type}_k^j\right)\right)^2$$

$$\mathrm{AddOn}\left(\mathrm{Type}_k^j\right) = \mathrm{SF}_k^{(\mathrm{Com})} \cdot \text{Effective Notional}_k^{(\mathrm{Com})}$$

where—

(a) $\mathrm{AddOn}_j^{(\mathrm{Com})}$ is the add-on for hedging set j in the asset class of commodity-related derivative contracts;

(b) $\rho^{(\mathrm{Com})}$ is 40%;

(c) $SF_k^{(Com)}$ is the supervisory factor for subset k (as classified in accordance with section 226BQ(2)) in hedging set j which is, subject to adjustments set out in section 226BZ—

(i) 40% if the type of the underlying commodity based on which the contracts are classified into the subset is electricity; or

(ii) 18% in any other case; and

(d) $\text{Effective Notional}_k^{(Com)}$ is the effective notional amount for contracts that fall within subset k in hedging set j calculated in accordance with section 226BZA(4).

226BZ. Treatments of supervisory factor for basis transactions and volatility transactions

The supervisory factor applicable to an asset class, a hedging set, a subset or an entity, when used in calculating the add-on for a hedging set in an asset class or for a subset in a hedging set, must be adjusted by multiplying the supervisory factor by—

(a) if the hedging set consists of basis transactions—one-half; or

(b) if the hedging set consists of volatility transactions—5.

Subdivision 6—Calculation of Effective Notional Amount

226BZA. Calculation of effective notional amount for hedging sets etc.

(1) The effective notional amount for each derivative contract is calculated by using Formula 23AY.

Formula 23AY

$$\text{Effective Notional} = \delta \cdot d \cdot MF^{(type)}$$

where—

(a) Effective Notional is the effective notional amount for a derivative contract;

(b) δ is the supervisory delta adjustment applicable to the contract determined in accordance with section 226BZB;

(c) d is the adjusted notional of the contract determined in accordance with section 226BZC; and

(d) $MF^{(type)}$ is the maturity factor for the contract determined in accordance with section 226BZD or 226BZE, as the case requires.

(2) The effective notional amount for a maturity bucket (as allocated in accordance with section 226BM(2)) in a hedging set in the asset class of interest rate contracts is the sum of the effective notional amounts calculated under subsection (1) for all the derivative contracts in the maturity bucket.

(3) The effective notional amount for a hedging set in the asset class of exchange rate contracts is the sum of the effective notional amounts calculated under subsection (1) for all the derivative contracts in the hedging set.

(4) The effective notional amount for a subset (as classified in accordance with section 226BO(2), 226BP(2) or 226BQ(2)) in the asset class of credit-related derivative contracts, equity-related derivative contracts or commodity-related derivative contracts is the sum of the effective notional amounts

calculated under subsection (1) for all the derivative contracts in the subset.

(5) For the purposes of subsection (1), an authorized institution may approximate or replicate the payoff of a complex and non-linear derivative contract with a combination of simple derivative contracts if—

(a) this is necessary in order to be able to calculate the effective notional amount of the complex and non-linear derivative contract by using Formula 23AY; and

(b) the way in which the approximation or replication is made is unlikely to affect the prudence of the default risk exposure calculated under this Division for the netting set to which the complex and non-linear derivative contract belongs. *(L.N. 54 of 2022)*

226BZB. Supervisory delta adjustment applicable to derivative contracts

(1) The supervisory delta adjustment (δ) applicable to a derivative contract that is not an option and does not provide tranched credit protection is determined in accordance with Table 23AE based on the type of derivative contract within which the contract falls.

Table 23AE

Column 1	Column 2
Type of derivative contract	δ
A derivative contract whose market value increases when the value of the contract's primary risk factor increases	+1

Column 1	Column 2
Type of derivative contract	δ
A derivative contract whose market value decreases when the value of the contract's primary risk factor increases	–1

(2) The supervisory delta adjustment (δ) applicable to a derivative contract that is an option is determined in accordance with Table 23AF based on the type of derivative contract within which the contract falls.

Table 23AF

Column 1	Column 2
Type of derivative contract	δ
Bought call option	+ N(+d)
Sold call option	– N(+d)
Bought put option	– N(–d)
Sold put option	+ N(–d)

(3) In Table 23AF—

(a) N(...) represents the cumulative distribution function for a standard normal random variable; and

(b) $$d = \frac{\ln\left(\frac{(P+\lambda)}{(K+\lambda)}\right) + 0.5 \cdot \sigma^2 \cdot T}{\sigma \cdot \sqrt{T}}$$

where—

(i) subject to subsection (4), P is the price of the underlying exposure of the option concerned (where appropriate, the forward value (rather than the spot price) of the underlying exposure is to be used to account for the risk-free rate as well as the possible cash flows generated from the underlying exposure prior to the option expiry);

(ii) K is the strike price of the option;

(iii) if the option falls within the asset class of interest rate contracts, λ is the presumed lowest possible extent to which the interest rates of the currency concerned can become negative, in any other case, λ is equal to zero;

(iv) σ is the supervisory volatility determined in accordance with Table 23AG based on the asset class (or subclass, where applicable) to which the option belongs; and

Table 23AG

Column 1	Column 2	Column 3
Asset class	Subclass	σ (%)
Interest rate contracts	-	50
Exchange rate contracts	-	15
Credit-related derivative contracts	Single-name	100
	Index	80

Column 1	Column 2	Column 3
Asset class	Subclass	σ (%)
Equity-related derivative contracts	Single-name	120
	Index	75
Commodity-related derivative contracts	Electricity	150
	Commodities other than electricity	70

(v) T is the time period (measured in years) from the current date to the latest contractual or allowable exercise date of the option.

(4) For the purposes of subsection (3)(b), if the payoff of an option is determined by reference to the average price of the underlying exposure over a pre-specified period, P is the current value of the average price.

(5) The supervisory delta adjustment (δ) applicable to a derivative contract that provides tranched credit protection is determined in accordance with Table 23AH based on the type of credit protection.

Table 23AH

Column 1	Column 2
Type of credit protection	δ
Purchased tranched credit protection	$+\dfrac{15}{(1+14\cdot A)\cdot(1+14\cdot D)}$
Sold tranched credit protection	$-\dfrac{15}{(1+14\cdot A)\cdot(1+14\cdot D)}$

where—

(a) A—

(i) in the case of a tranche of a securitization transaction—is the attachment point of the tranche;

(ii) in the case of a credit-related derivative contract referencing a basket of m reference entities where the n^{th} default in the basket will trigger payment under the contract—is equal to (n – 1) divided by m;

(b) D—

(i) in the case of a tranche of a securitization transaction—is the detachment point of the tranche;

(ii) in the case of a credit-related derivative contract referencing a basket of m reference entities where the n^{th} default in the basket will trigger payment under the contract—is equal to n divided by m.

226BZC. Calculation of adjusted notional of derivative contracts

(1) Subject to subsection (5)—

(a) the adjusted notional of a derivative contract falling within the asset class of interest rate contracts or credit-related derivative contracts is the product of—

(i) the notional amount of the contract (converted to Hong Kong dollars at the current market spot exchange rate if it is not denominated in Hong Kong dollars); and

(ii) the supervisory duration of the contract calculated by using Formula 23AZ;

(b) the adjusted notional of a derivative contract falling within the asset class of exchange rate contracts is—

(i) the notional amount of the foreign currency leg of the contract, converted to Hong Kong dollars at the current market spot exchange rate; or

(ii) if both legs of the contract are denominated in currencies other than Hong Kong dollars—the notional amount of the leg that, after having been converted to Hong Kong dollars at the current market spot exchange rate, has the larger value; and

(c) the adjusted notional of a derivative contract falling within the asset class of equity-related derivative contracts or commodity-related derivative contracts is—

(i) subject to subparagraph (iv), if the underlying exposure of the contract is an equity or a commodity—the product of the current market price of 1 unit of the equity or commodity and the number of units referenced by the contract; *(L.N. 167 of 2023)*

(ii) subject to subparagraph (iv), if the underlying exposure of the contract is an index (including an index on volatility)—the product of the current level of the index and the value of each index point designated in the contract; *(L.N. 167 of 2023)*

(iii) if the contract is a volatility transaction—the product of the current value of the volatility measure specified in the contract and the contractual notional amount of the contract; or *(L.N. 167 of 2023)*

(iv) if the notional amount of the contract is a fixed amount that is expressly stated in the contract—that stated notional amount. *(L.N. 167 of 2023)*

(2) The supervisory duration of a derivative contract falling within the asset class of interest rate contracts or credit-related derivative contracts is calculated by using Formula 23AZ.

Formula 23AZ

$$SD = \frac{\exp(-0.05 \cdot S) - \exp(-0.05 \cdot E)}{0.05}$$

where—

(a) SD is the supervisory duration of the contract, subject to a floor of 10 business days;

(b) subject to subsections (3) and (4), S is—

(i) subject to paragraph (ii), the time period (measured in years) from the current date to the start date of the time period referenced by the contract; or

(ii) if the start date has passed—zero; and

(c) subject to subsections (3) and (4), E is the time period (measured in years) from the current date to the end date of the time period referenced by the contract.

(3) Subsection (4) applies if a derivative contract (***principal contract***) referred to in subsection (2)(b) or (c)—

(a) falls within the asset class of interest rate contracts and references the value of another interest rate contract, interest rate instrument, inflation derivative contract or inflation-linked instrument; or

(b) falls within the asset class of credit-related derivative contracts and references the value of another credit-related derivative contract or credit instrument.

(4) In determining the values of S and E in Formula 23AZ—

(a) subject to paragraph (c), if the principal contract references another derivative contract—references to the principal contract in paragraphs (b) and (c) of that formula is construed to mean the contract underlying the principal contract;

(b) subject to paragraph (c), if the principal contract references an instrument that is not a derivative contract—references to the principal contract in paragraphs (b) and (c) of that formula is construed to mean the instrument underlying the principal contract; or

(c) if the principal contract is an option on an interest rate swap and the option can be exercised on any one of a number of fixed and pre-determined exercise dates—

(i) S is the time period (measured in years) from the current date to the earliest allowed exercise date of the option; and

(ii) E is the time period (measured in years) from the current date to the end date of the time period referenced by the interest rate swap.

(5) If the notional amount of a derivative contract is not stated clearly or is not fixed until maturity, the notional amount to be used in the calculation of the adjusted notional of the derivative contract is—

(a) if the stated notional amount of the contract is a formula with market values as inputs—the amount calculated by entering the current market values into that formula;

(b) if the contract is structured so that its notional amount is variable over time—the time-weighted average notional amount over the remaining time to maturity of the contract;

(c) if the contract is leveraged by multiplying the rates referenced by the contract by a factor—the notional amount of the contract as if it were unleveraged which is calculated by multiplying the stated notional amount of the contract by the factor; or

(d) if the contract has multiple exchanges of principal—the product of the remaining number of exchanges of principal to be made under the contract and the stated notional amount of the contract.

226BZD. Maturity factor for unmargined contracts

(1) The maturity factor for an unmargined contract is calculated by using Formula 23AZA.

Formula 23AZA

$$MF_i^{(unmargined)} = \sqrt{\frac{\min\{M_i;\ 1\text{ year}\}}{1\text{ year}}}$$

where—

(a) $MF_i^{(unmargined)}$ is the maturity factor for unmargined contract i; and

(b) M_i is the remaining time to maturity of unmargined contract i (measured in years) from the current date, or, where applicable, the value as determined in accordance with subsection (2), (3) or (4), subject to a floor of 10 business days.

(2) If—

(a) the underlying exposure of an unmargined contract is another derivative contract (***underlying contract***); and

(b) the unmargined contract may be exercised or settled by physical delivery of the underlying contract,

the M_i of the unmargined contract for the purposes of Formula 23AZA is the time period from the current date to the final settlement date of the underlying contract.

(3) If—

(a) an unmargined contract is a derivative contract structured to settle the outstanding exposures under the contract on specified dates; and

(b) the terms of the contract are reset so that the fair value of the contract is zero on the specified dates,

the M_i of the derivative contract for the purposes of Formula 23AZA is the time period from the current date until the next reset date.

(4) If a derivative contract falls within paragraph (b) of the definition of ***unmargined contract*** in section 226BA, the M_i of the derivative contract for the purposes of Formula 23AZA is 10 business days.

226BZE. Maturity factor for margined contracts

(1) The maturity factor for a margined contract is calculated by using Formula 23AZB.

Formula 23AZB

$$MF_i^{(margined)} = \frac{3}{2}\sqrt{\frac{MPOR_i}{1\ year}}$$

where—

(a) $MF_i^{(margined)}$ is the maturity factor for margined contract i; and

(b) $MPOR_i$ is the margin period of risk appropriate for the variation margin agreement covering margined contract i, subject to the requirements set out in subsections (2), (3), (4), (5) and (6).

(2) Subject to subsections (3), (4) and (6) and unless otherwise required by Division 4, the margin period of risk applicable to a margined contract subject to daily remargining and daily mark-to-market must not be less than the following supervisory floor—

(a) 5 business days if the contract is a CCP-related transaction or an offsetting transaction in respect of a qualifying CCP entered into by an authorized institution—

(i) as a clearing member with its direct client; or

(ii) with a lower level client within a multi-level client structure associated with the qualifying CCP; or

(b) 10 business days in any other case.

(3) If a margined contract subject to daily remargining and daily mark-to-market is in a netting set referred to in section

226M(2), the margin period of risk applicable to the contract must not be less than the supervisory floor specified in that section.

(4) If a margined contract subject to daily remargining and daily mark-to-market is in a netting set referred to in section 226M(3), the margin period of risk applicable to the contract must not be less than the supervisory floor specified in that section.

(5) If the remargining frequency of a margined contract is not daily, the margin period of risk applicable to the contract must not be less than the supervisory floor calculated by using Formula 23E in section 226M(6) with F in that formula construed to mean the supervisory floor that would be applicable to the contract, if it were subject to daily remargining, determined in accordance with—

(a) subsection (2);

(b) section 226M(2) under subsection (3); or

(c) section 226M(3) under subsection (4).

(6) If a margined contract is—

(a) one referred to in subsection (2), (3), (4) or (5); and

(b) in a netting set over which there has been more than 2 margin call disputes during the previous 2 quarters and the disputes have lasted longer than the margin period of risk applicable to the contract under that subsection,

the margin period of risk applicable to the contract for the subsequent 2 quarters must be at least double the supervisory floor that would be applicable to the contract, if there were no margin call dispute, under that subsection.

Division 2—IMM(CCR) Approach

226C. Application of Division 2

(1) This Division applies to an authorized institution that has an IMM(CCR) approval for calculating the default risk exposures in respect of contracts or transactions falling within any one or more of the categories referred to in section 10B(1)(a), (b) and (c).

(2) Unless otherwise expressly permitted by, and in accordance with, another provision of these Rules, an authorized institution must calculate its default risk exposures in respect of all the transactions (however described) that are covered by its IMM(CCR) approval in accordance with this Division.

226D. Calculation of IMM(CCR) risk-weighted amount at portfolio level under IMM(CCR) approach

(1) An authorized institution must, for each of its counterparties—

(a) calculate the sum of its default risk exposures (and outstanding default risk exposures in the case of netting sets that contain derivative contracts) in respect of all the netting sets with the counterparty based on effective EPEs that are estimated using current market data, and multiply the sum so calculated by the risk-weight applicable to the counterparty to obtain the risk-weighted amount of the sum (***risk-weighted amount A***); and

(b) subject to subsection (3), calculate the sum of its default risk exposures (and outstanding default risk exposures in the case of netting sets that contain derivative contracts) in respect of all the netting sets with the counterparty based on effective EPEs that are estimated using a stress calibration as set out in section 3(f) of Schedule 2A, and multiply the sum so calculated by the risk-weight applicable to the counterparty to obtain the risk-weighted amount of the sum (***risk-weighted amount B***). *(L.N. 44 of 2020)*

(2) An authorized institution must, after completing the calculations required under subsection (1)—

(a) aggregate all of its counterparties' risk-weighted amount A;

(b) aggregate all of its counterparties' risk-weighted amount B; and

(c) determine the IMM(CCR) risk-weighted amount as the greater of the 2 aggregates.

(3) The calibration referred to in subsection (1)(b) must be a single consistent stress calibration for the whole portfolio of counterparties concerned.

(4) For the purposes of subsection (1), an authorized institution that uses the STC approach or BSC approach to calculate its credit risk for non-securitization exposures must risk-weight its default risk exposures and, if applicable, outstanding default risk exposures net of specific provisions.

226E. Calculation of default risk exposure at netting set level under IMM(CCR) approach

(1) Subject to subsection (2) and sections 226I and 226J(3) and (4), an authorized institution must use Formula 23A to calculate the default risk exposure of a netting set.

Formula 23A

Calculation of Default Risk Exposure at Netting Set Level under IMM(CCR) Approach

$$\text{Default risk exposure} = \alpha \times \text{effective EPE}$$

where—

$\alpha = 1.4.$

(2) Subject to subsection (3), the Monetary Authority may, by notice in writing given to an authorized institution, require the institution to use a higher α in Formula 23A based on the risk profile of the institution's counterparty credit risk exposures.

(3) Factors that the Monetary Authority may take into account for the purposes of deciding whether or not to give a notice under subsection (2) to an authorized institution include—

(a) the granularity of the institution's counterparties;

(b) the level of exposures to general wrong-way risk (being the risk that arises when the probability of default of counterparties is positively correlated with general market risk factors);

(c) the correlation of market values across the institution's counterparties; and

(d) other institution-specific characteristics of the institution's counterparty credit risk exposures.

(4) An authorized institution must comply with the requirements of a notice given to it under subsection (2).

226F. Calculation of effective EPE

Subject to section 226K, an authorized institution must use Formula 23B to calculate the effective EPE of a netting set.

Formula 23B

Calculation of Effective EPE of Netting Set

$$\text{Effective EPE} = \sum_{k=1}^{\min(1\text{ year, maturity})} \text{effective EE}_{t_k} \times \Delta t_k$$

where—

effective EE_{tk} = effective EE at time t_k calculated in accordance with section 226G;

maturity = the time when the transaction that has the longest residual maturity in the netting set matures; and

Δt_k = $t_k - t_{k-1}$, which is the time interval between t_k and t_{k-1} when EE is calculated at dates that are not equally spaced over time.

226G. Calculation of effective EE

(1) An authorized institution must use Formula 23C to calculate the effective EE at time t_k in respect of a netting set.

Formula 23C

Calculation of Effective EE at Time t_k in Respect of Netting Set

$$\text{Effective EE}_{t_k} = \max\left(\text{effective EE}_{t_{k-1}}, \text{EE}_{t_k}\right)$$

where—

EE_{tk} = EE at time t_k calculated in accordance with section 226H.

(2) In using Formula 23C—

(a) the current date is denoted as t_0; and

(b) effective EE_{t0} equals current exposure.

226H. Calculation of EE

(1) An authorized institution must calculate the EE of a netting set at any particular future date (being a date before the transaction that has the longest residual maturity in the netting set matures) as the average of the distribution of exposures at that particular future date.

(2) An authorized institution must estimate the distribution of exposures at any particular future date by—

(a) estimating the probability distribution of the net market values of the transactions within the netting set at that future date, given the realized market value of those transactions up to the present time; and

(b) setting all negative net market values obtained in the estimation referred to in paragraph (a) to zero.

(3) Subject to subsection (4), an authorized institution may, when estimating the probability distribution referred to in subsection (2)(a), include any collateral that—

(a) falls within the description in section 80(1)(a), (b) or (c); and

(b) meets the criteria specified in section 77(2),

except collateral in the form of debt securities that are re-securitization exposures. *(L.N. 167 of 2023)*

(4) Subsection (3) does not apply in the case of an authorized institution that has an IMM(CCR) approval that prohibits the institution from using that subsection.

226I. Treatments for certain credit derivative contracts

An authorized institution may treat the default risk exposure in respect of a credit derivative contract as zero if— *(L.N. 44 of 2020)*

(a) the contract is a credit default swap in which the institution is the protection seller and regulatory capital is held in respect of the risk-weighted amount calculated in accordance with Part 4, 5, 6 or 7, as the case may be, for the institution's exposure to the credit risk of the reference obligation underlying the swap; or *(L.N. 44 of 2020)*

(b) the institution is the protection buyer in the contract and the credit risk mitigation effect of the contract has been recognized and taken into account in accordance with Divisions 9 and 10 of Part 4, Divisions 7 and 8 of Part 5, Division 10 of Part 6, or Division 5 of Part 7, for the purposes of the calculation of the risk-weighted amount of the exposure to which credit protection is provided by the contract.

(L.N. 175 of 2017)

226J. Treatments for transactions with specific wrong-way risk

(1) Where in respect of an authorized institution's transaction with a counterparty there is—

(a) a legal connection between the counterparty and the issuer of the assets underlying the transaction (or, where the transaction is a credit-related derivative contract, the reference entity specified in that contract); and *(L.N. 44 of 2020)*

(b) specific wrong-way risk,

the institution must treat the transaction as a separate netting set from its other netting sets with the counterparty.

(2) For the purposes of subsection (1), a legal connection is considered to exist if the counterparty and the issuer (or the reference entity in the case of a credit-related derivative contract)— *(L.N. 44 of 2020)*

(a) would constitute a single risk because one of them, directly or indirectly, has control over the other; or

(b) would be regarded as constituting a single risk because they are so interconnected that, if one of them were to experience financial problems, in particular funding or repayment difficulties, the other would be likely to encounter funding or repayment difficulties.

(3) An authorized institution must, if a single-name credit default swap falls within subsection (1), set the default risk exposure to the counterparty in respect of that swap as equal to the full expected loss in the remaining fair value of the reference obligations specified in that swap (being the amount determined after recognizing any market value that has already been lost and any expected recoveries, assuming the reference entity concerned is in liquidation).

(4) An authorized institution must, if—

(a) a transaction is referenced to a single issuer;

(b) the transaction is not a single-name credit default swap; and

(c) the transaction falls within subsection (1),

set the default risk exposure to the counterparty in respect of that transaction as equal to the value of the transaction estimated under the assumption of a jump-to-default of the asset underlying the transaction.

226K. Treatments for margin agreements

(1) An authorized institution must, for a netting set that is subject to a margin agreement, determine the effective EPE in respect of the netting set by—

(a) using the effective EE calculated from Formula 23C without taking into account the margin agreement; or *(L.N. 44 of 2020)*

(b) *(Repealed L.N. 44 of 2020)*

(c) subject to subsections (2) and (3), if the internal model used by the institution captures the effects of margin agreements when estimating EE, using the EE generated by the model directly in Formula 23C.

(2) Subsection (1)(c) does not apply in the case of an authorized institution that has an IMM(CCR) approval that prohibits the institution from using that subsection.

(3) An authorized institution must not, for the purposes of subsection (1)(c), recognize, in its default risk exposure calculations for derivative contracts and SFTs, the effect of collateral that is not cash of the same currency as the default risk exposure unless— *(L.N. 44 of 2020)*

(a) the institution models collateral jointly with the exposure in the calculations; or

(b) if the institution is not able to meet the requirement in paragraph (a), it applies standard supervisory haircuts (subject to adjustment set out in section 3 of Schedule 7) to the collateral. *(L.N. 44 of 2020)*

(4) An authorized institution must not capture the effect of a reduction of default risk exposure due to any clauses of a collateral agreement that require receipt of collateral when the credit quality of the counterparty concerned deteriorates.

(5) An authorized institution must, if it has posted unsegregated collateral to a counterparty under a margin agreement for a netting set, take into account its exposure to the counterparty arising from the unsegregated collateral (***relevant exposure***) in the calculation of effective EPE under section 226F. *(L.N. 44 of 2020)*

(6) For the purposes of subsection (5), if an authorized institution determines the effective EPE of the netting set in accordance with subsection (1)(a), the amount of its relevant exposure must be calculated in accordance with the requirements under section 71(2), 118(2), 163(2A) or 164(2)(b), as the case requires, instead of by using the internal model. *(L.N. 44 of 2020)*

(7) To avoid doubt, an authorized institution must, for collateral posted by it for a netting set (whether the collateral is taken into account in the determination of the effective EPE of the netting set or not), hold regulatory capital for the credit risk or market risk, whichever is applicable, of the collateral itself calculated under Part 4, 5, 6, 7 or 8, as the case requires—

(a) as if it had not been posted as collateral; and

(b) if the collateral is held by another person, as if the collateral were held by the institution. *(L.N. 44 of 2020)*

226L. *(Repealed L.N. 44 of 2020)*

226M. Margin period of risk

(1) Subject to subsections (2), (3) and (7) and unless otherwise required by Division 4, if a netting set of an authorized institution is subject to a margin agreement and the transactions in the netting set are subject to daily remargining and daily mark-to-market, the supervisory floor of the margin period of risk used for calculating the default risk exposure in respect of the netting set is—

(a) 5 business days if the netting set consists of repo-style transactions only;

(b) 5 business days if the netting set is not a netting set referred to in paragraph (a) and only consists of CCP-related transactions or offsetting transactions in respect of a qualifying CCP entered into by the institution—

(i) as a clearing member with its direct client; or

(ii) with a lower level client within a multi-level client structure associated with the qualifying CCP; or

(c) 10 business days in any other case. *(L.N. 44 of 2020)*

(2) Unless otherwise required by Division 4, an authorized institution must, if a netting set contains more than 5 000 transactions at any point in time during a quarter, impose a supervisory floor of 20 business days on the margin period of risk for that netting set for the following quarter.

(3) An authorized institution must, if a netting set contains at least one transaction—

(a) that involves illiquid collateral; or

(b) that is a derivative contract that cannot be easily replaced,

impose a supervisory floor of 20 business days on the margin period of risk for that netting set.

(4) For the purposes of subsection (3)—

(a) an authorized institution must determine whether or not collateral is illiquid collateral and whether or not a derivative contract is one that cannot be easily replaced— *(L.N. 44 of 2020)*

(i) on the assumption of stressed market conditions; and

(ii) taking into consideration whether, for the collateral or contract concerned, there are continuously active markets where a counterparty would, within 2 or fewer business days, obtain multiple price quotations that would not move the market or represent a price reflecting a market discount (in the case of collateral) or premium (in the case of a derivative contract);

(b) a transaction cannot be easily replaced if—

(i) the transaction is not marked-to-market daily; or

(ii) the fair value of the transaction, or the fair value of the asset underlying the transaction, is determined by models using inputs that are not observable in the market; and

(c) an authorized institution must consider whether the transactions undertaken by it or the assets it holds as collateral are concentrated in a particular counterparty, and if that counterparty exited the market precipitously, whether the institution would be able to replace those transactions.

(5) *(Repealed L.N. 175 of 2017)*

(6) An authorized institution must, for a netting set that is not subject to daily remargining, set the margin period of risk at not less than the margin period of risk calculated by using Formula 23E.

Formula 23E

Calculation of Margin Period of Risk for Netting Set Not Subject to Daily Remargining

$$\text{Margin period of risk} = F + N - 1$$

where—

F = the supervisory floor specified in subsection (1), (2) or (3), as the case requires, that would be applicable to the netting set if the netting set were subject to daily remargining; and

N = the actual number of days between each remargining of the netting set.

(7) If—

(a) a netting set is one referred to in subsection (1), (2), (3) or (6); and

(b) there have been more than 2 margin call disputes over the netting set during the previous 2 quarters and the disputes have lasted longer than the margin period of risk applicable to that netting set under that subsection,

an authorized institution must use a margin period of risk that is at least double the margin period of risk applicable to that netting set under that subsection for the subsequent 2 quarters. *(L.N. 175 of 2017)*

(L.N. 44 of 2020)

Division 2A—Current Exposure Method

(Division 2A added L.N. 44 of 2020)

226MA. Application of Division 2A

This Division applies to an authorized institution that uses the current exposure method to calculate the default risk exposure in respect of derivative contracts.

226MB. Calculation of default risk exposure

(1) Subject to subsections (2) and (3) and section 226MC, an authorized institution must use Formula 23EA to calculate the default risk exposure in respect of a derivative contract.

Formula 23EA

$$\text{Default risk exposure} = \alpha \times (\text{RC} + \text{PFE})$$

where—

(a) $\alpha = 1.4$;

(b) RC is the current exposure of the contract (if any collateral posted by the institution for the contract is unsegregated collateral, the current exposure of the contract must include the current market value of the collateral); and

(c) PFE is the potential future exposure of the contract calculated in accordance with section 226MD.

(2) If the premium for a sold option of an authorized institution has been fully paid upfront by the counterparty concerned, the amount of default risk exposure to the counterparty in respect of the option may be set to zero.

(3) If an authorized institution is the protection seller in respect of a credit-related derivative contract with periodic premium payments and the contract is not a sold option, the amount of default risk exposure to the protection buyer of the contract calculated under this section is capped at the amount of the unpaid premium under the contract.

226MC. Treatments for certain credit derivative contracts

An authorized institution may treat the default risk exposure in respect of a credit derivative contract as zero if—

(a) both of the following conditions are met—

(i) the contract is a credit default swap in which the institution is the protection seller;

(ii) a regulatory capital is held in respect of the risk-weighted amount calculated in accordance with Part 5 or 7 for the institution's exposure to the credit risk of the reference obligation underlying the swap; or

(b) both of the following conditions are met—

(i) the institution is the protection buyer in the contract;

(ii) the credit risk mitigation effect of the contract has been recognized and taken into account under Divisions 7 and 8 of Part 5 or Division 5 of Part 7, for the purpose of calculating the risk-weighted amount of the exposure to which credit protection is provided by the contract.

226MD. Calculation of potential future exposure of derivative contract

(1) The potential future exposure of a derivative contract is calculated by multiplying the notional amount of the derivative contract by the credit conversion factor applicable to the contract determined in accordance with Table 23AI based on the type of derivative contract within which the contract falls.

Table 23AI

Column 1	Column 2	Column 3
Item	Type of derivative contract	Credit conversion factor
1.	Interest rate contract—	
	(a) with a residual maturity of not more than 1 year;	0.5%
	(b) with a residual maturity of more than 1 year but not more than 5 years;	2%
	(c) with a residual maturity of more than 5 years	4%
2.	Credit-related derivative contract that references a single entity, or a single-name credit instrument, having category 1 credit quality grade—	
	(a) with a residual maturity of not more than 1 year;	0.5%
	(b) with a residual maturity of more than 1 year but not more than 5 years;	2.5%
	(c) with a residual maturity of more than 5 years	4.5%
3.	Credit-related derivative contract that references an investment grade index—	
	(a) with a residual maturity of not more than 1 year;	0.5%

Column 1	Column 2	Column 3
Item	Type of derivative contract	Credit conversion factor
	(b) with a residual maturity of more than 1 year but not more than 5 years;	2.5%
	(c) with a residual maturity of more than 5 years	4.5%
4.	Credit-related derivative contract that references a single entity, or a single-name credit instrument, having category 2 credit quality grade—	
	(a) with a residual maturity of not more than 1 year;	1.5%
	(b) with a residual maturity of more than 1 year but not more than 5 years;	7%
	(c) with a residual maturity of more than 5 years	12.5%
5.	Credit-related derivative contract that references a single entity that does not have any ECAI issuer rating or a single-name credit instrument that does not have any long-term ECAI issue specific rating—	
	(a) with a residual maturity of not more than 1 year;	1.5%

Column 1	Column 2	Column 3
Item	Type of derivative contract	Credit conversion factor
	(b) with a residual maturity of more than 1 year but not more than 5 years;	7%
	(c) with a residual maturity of more than 5 years	12.5%
6.	Credit-related derivative contract that references a non-investment grade index—	
	(a) with a residual maturity of not more than 1 year;	1.5%
	(b) with a residual maturity of more than 1 year but not more than 5 years;	7%
	(c) with a residual maturity of more than 5 years	12.5%
7.	Credit-related derivative contract that references a single entity, or a single-name credit instrument, having category 3 credit quality grade—	
	(a) with a residual maturity of not more than 1 year;	6%
	(b) with a residual maturity of more than 1 year but not more than 5 years;	26.5%

Column 1	Column 2	Column 3
Item	Type of derivative contract	Credit conversion factor
	(c) with a residual maturity of more than 5 years	47%
8.	Exchange rate contract	4%
9.	Equity-related derivative contract that references a single name	32%
10.	Equity-related derivative contract that references an index	20%
11.	Commodity-related derivative contract the underlying commodity of which is precious metal (including gold)	18%
12.	Commodity-related derivative contract the underlying commodity of which is electricity	40%
13.	Commodity-related derivative contract (other than those referred to in items 11 and 12)	18%

Column 1	Column 2	Column 3
Item	Type of derivative contract	Credit conversion factor
14.	Any other derivative contract not specified in items 1 to 13	the applicable CCF specified in Part 2 of Schedule 1 or, if no such CCF is specified, 40%

(2) For the purposes of subsection (1)—

(a) if the derivative contract is a contract to which section 226ME is applicable, the notional amount must be determined in accordance with that section; and

(b) the type of derivative contract within which a contract falls must be determined based on the contract's primary risk factor.

(3) For the purposes of items 3 and 6 in Table 23AI—

(a) an index is an investment grade index where the minimum credit rating specified by the index service provider concerned for the purpose of determining whether an entity is eligible for being included in the index—

(i) if mapped to a credit quality grade in accordance with the LT ECAI rating mapping table for Type A

ECAIs—would be mapped to a credit quality grade of 1, 2, 3 or 4; or

(ii) if mapped to a credit quality grade in accordance with the LT ECAI rating mapping table for Type B ECAIs—would be mapped to a credit quality grade of 1, 2 or 3; and *(L.N. 167 of 2023)*

(b) a non-investment grade index is an index that is not an investment grade index.

(4) For the purposes of items 2, 4 and 7 in Table 23AI, an authorized institution must determine whether a single entity or a single-name credit instrument has a category 1, 2 or 3 credit quality grade by mapping the ECAI issuer rating of the entity, or the long-term ECAI issue specific rating of the credit instrument, to a credit quality grade in accordance with— *(L.N. 167 of 2023)*

(a) unless paragraph (b) applies—the LT ECAI rating mapping table for Type A ECAIs; or *(L.N. 167 of 2023)*

(b) if the entity is a corporate incorporated in the home jurisdiction of a Type B ECAI (***relevant Type B ECAI***) or the credit instrument is issued by such a corporate—

(i) the LT ECAI rating mapping table for Type A ECAIs in cases where the rating is issued by a Type A ECAI; or

(ii) the LT ECAI rating mapping table for Type B ECAIs in cases where the rating is issued by the relevant Type B ECAI. *(L.N. 167 of 2023)*

(5) For the purposes of items 2, 4 and 7 in Table 23AI—

(a) a single entity, or a single-name credit instrument, has a category 1 credit quality grade if the ECAI rating concerned is mapped to—

(i) a credit quality grade of 1, 2, 3 or 4 under subsection (4)(a) or (b)(i); or

(ii) a credit quality grade of 1, 2 or 3 under subsection (4)(b)(ii); *(L.N. 167 of 2023)*

(b) a single entity, or a single-name credit instrument, has a category 2 credit quality grade if the ECAI rating concerned is mapped to—

(i) a credit quality grade of 5 or 6 under subsection (4)(a) or (b)(i); or

(ii) a credit quality grade of 4 or 5 under subsection (4)(b)(ii); or *(L.N. 167 of 2023)*

(c) a single entity, or a single-name credit instrument, has a category 3 credit quality grade if the ECAI rating concerned is mapped to—

(i) a credit quality grade of 7 under subsection (4)(a) or (b)(i); or

(ii) a credit quality grade of 6 or 7 under subsection (4)(b)(ii). *(L.N. 167 of 2023)*

(6) Subject to subsection (7)(a), for the purposes of Table 23AI—

(a) the residual maturity of an interest rate contract that references the value of another interest rate contract (***underlying contract***) or interest rate instrument is the time period from the current date to the maturity date of the underlying contract or instrument; and

(b) the residual maturity of a credit-related derivative contract that references the value of another credit-related derivative contract (***underlying contract***) or credit instrument is the time period from the current date to the maturity date of the underlying contract or instrument.

(7) If a derivative contract is structured to settle the outstanding exposures under the contract on specified dates and the terms of the contract are reset so that the fair value of the contract is zero on the specified dates, an authorized institution—

(a) must treat the residual maturity of the contract as the time period from the current date until the next reset date; and

(b) if the contract is an interest rate contract and its remaining time to final maturity is more than 1 year—must not apply a credit conversion factor of less than 2% to the contract.

226ME. Notional amount of certain types of derivative contracts

(1) Subject to subsections (2) and (3)—

(a) the notional amount of an exchange rate contract is—

(i) the notional amount of the foreign currency leg of the contract, converted to Hong Kong dollars at the current market spot exchange rate; or

(ii) if both legs of the contract are denominated in currencies other than Hong Kong dollars—the notional amount of the leg that, after having been converted to Hong Kong dollars at the current market spot exchange rate, has the larger value; and

(b) the notional amount of an equity-related derivative contract or a commodity-related derivative contract is—

(i) if the underlying exposure of the contract is an equity or a commodity—the product of the current market price of 1 unit of the equity or commodity and the number of units referenced by the contract;

(ii) if the underlying exposure of the contract is an index (including an index on volatility)—the product of the current level of the index and the value of each index point designated in the contract; or

(iii) if the contract is a volatility transaction—the product of the current value of the volatility measure specified in the contract and the contractual notional amount of the contract.

(2) For a derivative contract that has multiple exchanges of principal, the notional amount of the contract is the product of the remaining number of exchanges of principal to be made under the contract and the stated notional amount of the contract.

(3) If the stated notional amount of a derivative contract is leveraged or enhanced by the structure of the contract, the notional amount of the contract is the effective notional amount of the contract calculated by taking into account the effect of the leverage or enhancement, as the case requires.

226MF. Authorized institution to hold regulatory capital for credit risk or market risk of posted collateral

To avoid doubt, an authorized institution must, for collateral posted by it for derivative contracts (whether the collateral is included in the calculation under section 226MB or not), hold regulatory capital for the credit risk or market risk, whichever is applicable, of the collateral itself calculated under Part 5, 7 or 8, as the case requires—

(a) as if it had not been posted as collateral; and

(b) if the collateral is held by another person—as if the collateral were held by the institution.

Division 2B—Calculation of Default Risk Exposure in Respect of SFTs

(Division 2B added L.N. 44 of 2020)

226MG. Interpretation for Division 2B

In this Division—

principal amount (本金額)—

(a) if the asset concerned is measured at fair value—means the value of the asset determined in accordance with section 4A;

(b) if the asset concerned is not measured at fair value—means the book value of the asset.

226MH. Application of Division 2B

This Division applies to the following authorized institutions—

(a) an authorized institution that does not have an IMM(CCR) approval for SFTs;

(b) an authorized institution that has an IMM(CCR) approval for certain types of SFTs only; and

(c) an authorized institution that is permitted under section 10B(5), or has chosen under section 10B(7), to use the methods prescribed in this Division for certain SFTs.

226MI. Calculation of default risk exposures in respect of SFTs: general

(1) An authorized institution that uses the IRB approach to calculate its credit risk for non-securitization exposures to counterparties in respect of its SFTs must, for any of those SFTs (whether booked in its banking book or trading book) that are not subject to the IMM(CCR) approach, calculate the

amount of the default risk exposure in respect of the SFTs in accordance with sections 226MJ, 226MK and 226ML.

(2) An authorized institution that uses the STC approach to calculate its credit risk for non-securitization exposures to counterparties in respect of its SFTs must, for any of those SFTs (whether booked in its banking book or trading book) that are not subject to the IMM(CCR) approach—

(a) calculate the amount of the default risk exposure in respect of the SFTs in accordance with sections 226MJ and 226MK if the institution uses the comprehensive approach in its treatment of recognized collateral for any exposures that are not defaulted exposures; or

(b) calculate the amount of the default risk exposure in respect of the SFTs in accordance with section 226MJ if the institution uses the simple approach in its treatment of recognized collateral for any exposures that are not defaulted exposures.

(3) An authorized institution that uses the BSC approach to calculate its credit risk for non-securitization exposures—

(a) must, for its SFTs (whether booked in its banking book or trading book) that are not subject to the IMM(CCR) approach, calculate the amount of the default risk exposure in respect of the SFTs in accordance with section 226MJ; and

(b) must not take into account the effect of any recognized netting in such calculation.

(4) If, immediately before the commencement date* of Part 3 of the Banking (Capital) (Amendment) Rules 2023, an authorized institution that uses the STC approach or BSC approach to calculate its credit risk for non-securitization exposures had an approval granted under section 226ML(3) as in force immediately before that date to use a VaR model

as an alternative to the use of Formula 23EB as in force immediately before that date for the purpose of calculating the amount of the default risk exposure in respect of nettable repo-style transactions, the approval is revoked on that date.

(5) In this section—

defaulted exposure (違責風險承擔) has the meaning given by section 51(1).

(L.N. 167 of 2023)

Editorial Note:

* Commencement date: 1 January 2025.

226MJ. Calculation of default risk exposure in respect of SFTs that are not nettable

(L.N. 167 of 2023)

(1) An authorized institution must calculate the amount of the default risk exposure in respect of each of the following SFTs in accordance with this section—

(a) an SFT that is not nettable;

(b) a nettable SFT for which—

(i) the institution is not permitted to use the comprehensive approach to take into account the effect of recognized netting because the institution falls within section 226MI(2)(b) or (3); or

(ii) the institution has chosen not to take into account the effect of recognized netting in the calculation of the amount of the default risk exposure in respect of the SFT. *(L.N. 167 of 2023)*

(2) An authorized institution must treat all securities and money provided by it to a counterparty under an SFT as if they were a loan to the counterparty secured on the money and securities

that are provided to, or to the order of, the institution under the SFT.

(3) Accordingly, the authorized institution must take the principal amount of the securities and the money provided by it as the amount of the default risk exposure in respect of the SFT.

226MK. Calculation of default risk exposure in respect of nettable SFTs

(L.N. 167 of 2023)

(1) Subject to section 226ML, an authorized institution must calculate the amount of the default risk exposure in respect of its nettable SFTs that do not fall within section 226MJ(1)(b) in accordance with this section.

(2) An authorized institution must not take into account the effect of recognized netting covering the institution's SFTs in the calculation of the amount of the default risk exposure in respect of the SFTs other than under this section.

(3) An authorized institution must calculate the amount of the default risk exposure in respect of nettable SFTs in a netting set entered into by the institution with a counterparty by using Formula 23EB.

Formula 23EB

Calculation of Amount of Default Risk Exposure in respect of Nettable SFTs in Netting Set

$$E^* = \max\left\{0;\ \sum_i E_i - \sum_j C_j + 0.4 \cdot A_{Net} + 0.6 \cdot \frac{A_{Gross}}{\sqrt{N}} + \sum_{fx}(E_{fx} \cdot H_{fx})\right\}$$

$$A_{Net} = \left|\sum_s E_s H_s\right|$$

$$A_{Gross} = \sum_s E_s |H_s|$$

where—

(a) E^* is the amount of the default risk exposure after taking into account recognized netting;

(b) E_i is the current market value of cash i or security i lent or sold to the counterparty under the SFTs or otherwise posted to the counterparty under the valid bilateral netting agreement entered into with the counterparty;

(c) C_j is the current market value of cash j or security j borrowed or purchased from the counterparty under the SFTs or otherwise held by the institution under the valid bilateral netting agreement;

(d) E_s is the absolute value of the net current market value of security s in the netting set;

(e) H_s is the standard supervisory haircut appropriate to E_s (subject to subsection (4) and adjustment set out in section 3 of Schedule 7), which has—

(i) a positive sign if the security is lent, sold or posted by the institution; or

(ii) a negative sign if the security is borrowed, purchased or held by the institution;

(f) N is the number of groups of the same securities contained in the netting set, but those groups whose E_s is less than one-tenth of the largest E_s in the netting set are not counted;

(g) E_{fx} is the absolute value of the net position in each currency fx different from the settlement currency; and

(h) H_{fx} is the standard supervisory haircut applicable in consequence of a mismatch, if any, between currency fx and the settlement currency (subject to subsection (4) and adjustment set out in section 3 of Schedule 7).

(L.N. 167 of 2023)

(4) For the purposes of subsection (3)—

(a) in determining the values of H_s and H_{fx} in Formula 23EB, the minimum holding period applicable to the SFTs is determined in the same way as that set out in section 91(1), (2) and (3);

(b) if an authorized institution's nettable SFTs in a netting set entered into with a counterparty contain one or more than one repo-style transaction that meets all of the criteria specified in section 82(4) (***qualifying transaction***), the institution may set H_s in Formula 23EB appropriate to E_s at zero, where E_s in such case must be construed as the absolute value of the net current market value of security s underlying the qualifying transaction; and

(c) paragraph (b) does not apply to an authorized institution's nettable SFTs in a netting set if—

(i) the institution uses the IRB approach to calculate the credit risk for its non-securitization exposures to the counterparty concerned; and

(ii) at least one of the nettable SFTs in the netting set is a repo-style transaction that is not a qualifying transaction. *(L.N. 167 of 2023)*

(5) An authorized institution—

(a) subject to paragraph (b), must net its nettable SFTs booked in its banking book separately from netting its nettable SFTs booked in its trading book and vice versa;

(b) may net SFTs booked in its banking book with SFTs booked in its trading book in respect of the same counterparty if—

(i) all those SFTs are marked-to-market daily; and

(ii) all the securities received by the institution under all those SFTs are recognized collateral (within the meaning of section 51(1)) falling within section 79(1) (excluding section 79(1)(o)) or 80(1)(b) or (c). *(L.N. 167 of 2023)*

(L.N. 167 of 2023)

226ML. Use of value-at-risk model instead of section 226MJ and Formula 23EB

(1) An authorized institution may use an internal model based on VaR (***VaR model***) as an alternative to the use of section

226MJ and Formula 23EB for the purpose of calculating the amount of its default risk exposure to a counterparty in respect of single SFTs or nettable SFTs if—

(a) the authorized institution uses the IRB approach to calculate the risk-weighted amounts of the SFTs;

(b) the authorized institution is either—

(i) granted an approval under section 18(2)(a) by the Monetary Authority to use the IMA to calculate its market risk capital charge in respect of any one or more trading desks; or

(ii) granted an approval under subsection (4)(a) by the Monetary Authority; and

(c) all the requirements in subsection (2) are met.

(2) The requirements are that—

(a) the VaR model approved under subsection (1)(b)(i) or (ii), as the case may be, captures risk sufficient to—

(i) fulfil the back-testing requirements under section 322G(1); and

(ii) be assigned to the green zone in the profit and loss attribution test under section 322G(2);

(b) none of the collateral posted or received by the institution in respect of the SFTs is a securitization exposure; and

(c) the collateral is revalued on a daily basis.

(3) An authorized institution that does not have the approval referred to in subsection (1)(b)(i) may apply to the Monetary Authority for an approval to use a VaR model as an alternative to—

(a) the use of section 226MJ for the purpose of calculating the amount of default risk exposure to a counterparty in respect of single SFTs; and

(b) the use of Formula 23EB for the purpose of calculating the amount of default risk exposure to a counterparty in respect of nettable SFTs.

(4) Subject to subsection (5), the Monetary Authority must—

(a) determine the application made by an authorized institution under subsection (3) by granting or refusing to grant the approval; and

(b) give a written notice of the decision to the authorized institution.

(5) The Monetary Authority must refuse to grant the approval under subsection (4)(a) unless the authorized institution satisfies the Monetary Authority that the institution and the VaR model in respect of which the approval is sought satisfy the requirements specified in Schedule 3 with the following exceptions and modifications—

(a) instead of an expected shortfall at a 97.5% confidence level, the model must calculate the VaR at a 99%, one-tailed confidence level;

(b) the model does not need to satisfy the requirements specified in section 2 of that Schedule in relation to default risk charge; and

(c) instead of the minimum liquidity horizon of 10 days specified in Table A in section 1(1) of that Schedule, the model assumes—

(i) a minimum holding period of 5 business days for margined repo-style transactions;

(ii) a minimum holding period of 10 business days for SFTs other than margined repo-style transactions; and

(iii) a longer minimum holding period than the one specified in subparagraph (i) or (ii) when this is appropriate given the liquidity of the market instruments concerned.

(6) An authorized institution must not, without the prior written consent of the Monetary Authority, make any significant change to the VaR model that is the subject of the approval granted to the institution under subsection (4)(a).

(7) An authorized institution that is permitted under subsection (1) to use the VaR model must calculate the amount of default risk exposure in respect of SFTs by using Formula 23EC.

Formula 23EC

$$E^{*} = \max\left\{0, \left[\left(\sum (E) - \sum (C)\right) + \text{VaR output}\right]\right\}$$

where—

(a) E* is the amount of default risk exposure;

(b) E is the current market value of all money and securities provided by the institution under the SFTs;

(c) C is the current market value of all money and securities received by the institution under the SFTs; and

(d) VaR output is the VaR number generated by the VaR model in respect of the previous business day.

(8) If the authorized institution mentioned in subsection (7) has an approval referred to in subsection (1)(b)(i), the VaR output in Formula 23EC must be calculated—

(a) at a 99%, one-tailed confidence level; and

(b) based on—

(i) a minimum holding period of 5 business days for margined repo-style transactions;

(ii) a minimum holding period of 10 business days for SFTs other than margined repo-style transactions; and

(iii) a longer minimum holding period than the one specified in subparagraph (i) or (ii) when this is appropriate given the liquidity of the market instruments concerned.

(L.N. 167 of 2023)

226MM. Supplementary provisions to sections 226MK and 226ML

For the purposes of sections 226MK and 226ML, securities received by an authorized institution under SFTs may be included in the calculation under either of those sections only if—

(a) for SFTs booked in the institution’s banking book—the securities are recognized collateral (within the meaning of section 51(1)) falling within section 79(1) (excluding section 79(1)(o)) or 80(1)(b) or (c); and

(b) for SFTs booked in the institution’s trading book—the securities are eligible for being included in the trading book and the securities are provided to the institution under arrangements that meet all the criteria specified in section 77(2) and (4)(b).

(L.N. 167 of 2023)

Division 3—*(Repealed L.N. 167 of 2023)*

226N. *(Repealed L.N. 167 of 2023)*

226O. *(Repealed L.N. 167 of 2023)*

226P. *(Repealed L.N. 167 of 2023)*

226Q. *(Repealed L.N. 167 of 2023)*

226R. *(Repealed L.N. 167 of 2023)*

226S. *(Repealed L.N. 167 of 2023)*

226T. *(Repealed L.N. 167 of 2023)*

Division 4—Exposures to CCPs

226U. Application of Division 4

(1) This Division applies to any authorized institution, regardless of the approach adopted by the institution for calculating its credit risk for non-securitization exposures.

(2) To avoid doubt, exposures of an authorized institution— *(L.N. 44 of 2020)*

(a) to—

(i) CCPs;

(ii) clearing members;

(iii) direct clients; or

(iv) higher level clients or lower level clients within multi-level client structures; and

(b) arising from delayed or failed settlement of—

(i) cash transactions in securities (other than repo-style transactions), foreign exchange or commodities; or

(ii) cash-settled derivative contracts,

are not subject to the requirements of this Division but are subject to the capital treatments set out in one or more of Parts 4, 5 and 6, as the case requires, for transactions settled on a delivery-versus-payment basis or a basis other than the delivery-versus-payment basis. *(L.N. 44 of 2020; L.N. 167 of 2023)*

226V. Interpretation of Division 4

(1) In this Division—

Basel CCR Rules (《巴塞爾CCR規則》) means the rules set out in chapters CRE50, CRE51, CRE52, CRE53, CRE54 and CRE55 of the current Basel Framework; *(L.N. 44 of 2020; L.N. 167 of 2023)*

Committee on Payments and Market Infrastructures (支付及市場基礎設施委員會) means the international standard setter, whose secretariat is hosted by the Bank for International Settlements in Basel, Switzerland, that promotes, monitors and makes recommendations about the safety and efficiency of payment, clearing, settlement and related arrangements, with a view to supporting financial stability and the wider economy; *(L.N. 44 of 2020)*

initial margin (開倉保證金)—

(a) means the collateral posted—

(i) to a CCP by—

(A) a clearing member of the CCP;

(B) a direct client of a clearing member of the CCP; or

(C) an indirect client within a multi-level client structure associated with the CCP; and

(ii) to mitigate the potential future exposure of the CCP to the clearing member arising from the possible future change in the value of the transactions of any one or more of the parties referred to in subparagraph (i)(A), (B) and (C);

(b) if the collateral referred to in paragraph (a) exceeds the minimum amount that the clearing member, direct client or indirect client is required to post and the CCP or clearing member may, where appropriate, prevent the clearing member, direct client or indirect client from withdrawing the excess amount posted—includes the excess amount; and

(c) does not include—

(i) any default fund contributions made by the clearing member; and

(ii) any collateral posted by the clearing member, direct client or indirect client that can be used by the CCP to mutualize losses among clearing members; *(L.N. 44 of 2020)*

International Organization of Securities Commissions (證券委員會國際組織) means the international association of securities regulators, whose general secretariat is based in Madrid, Spain, that sets international standards for securities markets and promotes information exchange and cooperation among its members;

non-qualifying CCP (不合資格CCP) means a CCP that is not a qualifying CCP;

qualifying CCP (合資格CCP) means—

(a) a CCP—

(i) that has been granted a licence by a regulator or overseer to operate as a CCP (including a licence granted by way of confirming an exemption) and is permitted by the regulator or overseer to operate as such with respect to products offered by the CCP;

(ii) that is based and prudentially supervised in a jurisdiction where the regulator or overseer has established, and publicly indicated that it applies to the CCP on a continuous basis, domestic rules and regulations that are consistent with the principles in the document entitled “Principles for financial market infrastructures” published by the Committee on Payments and Market Infrastructures and the Technical Committee of the International Organization of Securities Commissions, as in force from time to time;

(iii) that calculates and makes available, or makes available sufficient information for other relevant parties to calculate, the parameters specified in paragraphs 54.28 to 54.36 of the Basel CCR Rules in accordance with the methodology and requirements set out in those paragraphs, so that the CCP’s clearing members are able to calculate the regulatory capital for their default fund contribution made to the CCP, and update the calculation at least quarterly and whenever there are material changes to the number of, or the level of exposure in respect of, cleared transactions or material changes to the financial resources of the CCP; and

(iv) that provides sufficient information in the manner specified in paragraphs 54.37, 54.38 and 54.39 of the Basel CCR Rules to its regulator or overseer, clearing members and the relevant banking supervisory authorities of the clearing members to enable them to review the calculations of the parameters referred to in subparagraph (iii) or the capital charge calculations performed by the clearing members; or

(b) a CCP regarded as a qualifying CCP under section 1 of Schedule 16. *(L.N. 44 of 2020)*

(L.N. 44 of 2020)

(2) For the purposes of this Division—

(a) an authorized institution's default risk exposure to a CCP includes—

(i) any initial margin that is held by the CCP and posted by the institution; and

(ii) if the institution is a clearing member of the CCP, any variation margin that is held by the CCP and payable by the CCP to the institution; and *(L.N. 51 of 2013)*

(b) in determining whether any netting done pursuant to an arrangement with a CCP is recognized netting— *(L.N. 44 of 2020)*

(i) any reference to agreement in the definition of ***valid bilateral netting agreement*** in section 2(1); or

(ii) any reference to bilateral master agreement in section 226B(2), is to be construed as an enforceable arrangement employed by a CCP that provides legally enforceable rights of set-off. *(L.N. 44 of 2020)*

226W. Calculation of credit risk exposures

(1) Subject to subsections (3), (6), (7) and (8), an authorized institution must calculate its default risk exposure to a CCP, a clearing member, a direct client, or a higher level client or lower level client within a multi-level client structure in respect of derivative contracts and SFTs using the same methodology as it would be required to use if the transactions or contracts— *(L.N. 44 of 2020)*

(a) were not cleared by CCPs; or

(b) were not CCP-related transactions or offsetting transactions.

(2) *(Repealed L.N. 44 of 2020)*

(3) An authorized institution may treat the default risk exposure to a CCP, in respect of payment transactions or spot transactions, as zero if the CCP's default risk exposures to all clearing members are fully collateralized on a daily basis.

(4) *(Repealed L.N. 44 of 2020)*

(5) In subsection (6)—

20-business day supervisory floor (20個營業日的監管下限), in relation to the calculation of the default risk exposure of a large netting set, means the higher supervisory floor of 20 business days required under—

(a) section 91(2) (as applied by section 226MK and insofar as it relates to section 226M(2));

(b) section 226BZE(3); or *(L.N. 167 of 2023)*

(c) section 226M(2); *(L.N. 167 of 2023)*

(d) *(Repealed L.N. 167 of 2023)*

large netting set (大型淨額計算組合) means a netting set that falls within the description in section 226M(2). *(L.N. 44 of 2020)*

(6) The 20-business day supervisory floor does not apply to an authorized institution using the SA-CCR approach, the IMM(CCR) approach or the method set out in section 226MK in its calculation of the default risk exposure of a large netting set with a qualifying CCP if the netting set— *(L.N. 167 of 2023)*

(a) does not contain illiquid collateral or transactions that cannot be easily replaced; and

(b) does not contain any disputed transactions. *(L.N. 44 of 2020)*

(7) For the purpose of calculating the default risk exposures to CCPs arising from clearing of derivative contracts under section 226X or 226ZD, a minimum margin period of risk of 10 business days must be used. *(L.N. 44 of 2020)*

(8) If a CCP retains the variation margin posted by an authorized institution against a transaction and the variation margin is not protected against the insolvency of the CCP, the minimum margin period of risk or the minimum holding period, as the case requires, used in calculating the institution's default risk exposure in respect of the transaction is the lesser of—

(a) 1 year; or

(b) the remaining time to maturity of the transaction, subject to a floor of 10 business days. *(L.N. 44 of 2020)*

226X. Exposures of clearing members to qualifying CCPs

(1) An authorized institution that is a clearing member of a qualifying CCP must calculate the risk-weighted amount of

its—

(a) default risk exposure to the qualifying CCP in respect of derivative contracts or SFTs entered into with the qualifying CCP for the institution's own purposes; and

(b) default risk exposure to the qualifying CCP that arises when the institution provides clearing services to its direct clients and is obliged to reimburse the clients for any loss suffered by them due to changes in the value of their transactions in the event that the qualifying CCP defaults, *(L.N. 44 of 2020)*

by allocating a risk-weight of 2% to the exposures.

(2) For the purposes of subsection (1), an authorized institution may calculate the risk-weighted amount taking into account any credit risk mitigation techniques (including recognized netting and margining) that are recognized under these Rules in the same manner as permitted for the calculation of the risk-weighted amount of its default risk exposures in respect of bilateral transactions.

(2A) For the purposes of subsections (1) and (2), if an authorized institution uses the IRB approach to calculate its credit risk for certain non-securitization exposures, the institution must, in calculating the risk-weighted amounts of its default risk exposures to qualifying CCPs, take into account any credit risk mitigating effect in the calculation in accordance with Part 4. *(L.N. 167 of 2023)*

(3) An authorized institution must not under subsections (2) and (2A) take into account the effect of any credit risk mitigation techniques applicable to a default risk exposure of the institution in respect of the contracts or transactions concerned if that effect has already been taken into account in the calculation of the default risk exposure. *(L.N. 51 of 2013)*

(4) An authorized institution that is a clearing member of a qualifying CCP must use Formula 23K to calculate the regulatory capital for its default fund contribution (K_{AI}) made to the qualifying CCP.

Formula 23K

$$K_{AI} = \max\left(K_{CCP} \cdot \left(\frac{DF_{AI}^{funded}}{DF_{CCP} + DF_{CM}^{funded}}\right); 8\% \cdot 2\% \cdot DF_{AI}^{funded}\right)$$

where—

(a) K_{CCP} is the hypothetical capital requirement of the qualifying CCP calculated in accordance with the methodology and requirements set out in paragraphs 54.28 to 54.35 of the Basel CCR Rules for its default risk exposures to all of its clearing members and their direct clients and, subject to section 226Y(6A) and unless otherwise specified by the Monetary Authority under subsection (5), the risk-weight allocated to the default risk exposures for the purpose of the calculation is 20%; *(L.N. 167 of 2023)*

(b) DF_{AI}^{funded} is the funded default fund contribution made by the institution;

(c) DF_{CCP} is the qualifying CCP's funded own resources, including capital and retained earnings, which are contributed to the default waterfall, where these resources are junior to, or rank equally with, clearing members' funded default fund contributions; and

(d) DF_{CM}^{funded} is the total funded default fund contributions made by the clearing members of the qualifying CCP.

(L.N. 44 of 2020)

(5) The Monetary Authority may, by written notice to all authorized institutions, specify a risk-weight that is higher than 20%, or equal to 20% (if the risk-weight currently in use is higher than 20%), for the purpose of the calculation of K_{CCP} under paragraph 54.29 of the Basel CCR Rules if the Monetary Authority considers that the risk-weight specified is warranted by the overall credit quality of the clearing members of the qualifying CCP concerned. *(L.N. 44 of 2020)*

(6) The effective date of the risk-weight specified under subsection (5) is to be a date not less than 2 months from the date on which the authorized institutions were notified. *(L.N. 44 of 2020)*

(7) An authorized institution that is a clearing member of the qualifying CCP concerned must ensure that the risk-weight specified under subsection (5) and its effective date are communicated promptly to the person responsible for the calculation of the K_{CCP}. *(L.N. 44 of 2020)*

(8) Subsections (4), (5), (6) and (7) apply subject to section 2 of Schedule 16. *(L.N. 44 of 2020)*

(9) An authorized institution may allocate a risk-weight of 0% to its funded default fund contribution made to the qualifying CCP, to the extent of the amount for covering settlement-risk-only products. *(L.N. 44 of 2020; L.N. 167 of 2023)*

(10) Subsection (11) applies if the sum of—

(a) an authorized institution's risk-weighted amount of its default risk exposure to a qualifying CCP; and

(b) the risk-weighted amount of its default fund contribution made to the qualifying CCP,

is higher than the total risk-weighted amount (***latter amount***) that would be calculated for those same exposures if the qualifying CCP were a non-qualifying CCP. *(L.N. 44 of 2020)*

(11) The latter amount must be used in the institution's capital adequacy ratio calculations. *(L.N. 44 of 2020)*

(E.R. 1 of 2015)

226Y. Provisions supplementary to section 226X(4)

(1)-(2) *(Repealed L.N. 44 of 2020)*

(3) An authorized institution must recalculate K_{AI} by using Formula 23K— *(L.N. 44 of 2020)*

(a) at least on a quarterly basis; and

(b) whenever there are material changes to—

(i) the number of transactions of the institution cleared by the qualifying CCP or the number of transactions cleared by the qualifying CCP;

(ii) the exposure of the institution or qualifying CCP in respect of transactions cleared by the qualifying CCP; or

(iii) the financial resources of the qualifying CCP.

(4)-(5) *(Repealed L.N. 44 of 2020)*

(6) An authorized institution must calculate the risk-weighted amount of its exposure to the qualifying CCP in respect of its default fund contribution as the product of K_{AI} and 12.5.

(6A) If a qualifying CCP (***first QCCP***) has a link to another qualifying CCP (***second QCCP***) such that an authorized institution, as a clearing member of the first QCCP, is able to centrally clear transactions carried out with the second

QCCP's clearing members or their clearing clients without the need of the institution to become the second QCCP's clearing member or its clearing client, for the purposes of section 226X(4)—

(a) the second QCCP may be treated as if it were a clearing member of the first QCCP;

(b) in calculating the K_{CCP} of the first QCCP referred to in paragraph (a) of Formula 23K, a risk-weight of 2%, instead of the risk-weight of 20% required under that paragraph or the risk-weight specified by the Monetary Authority under section 226X(5), may be allocated to the first QCCP's default risk exposure to the second QCCP calculated in accordance with paragraphs 54.28 to 54.35 of the Basel CCR Rules; and

(c) for any asset posted to the first QCCP by the institution for the purposes of the link that could be used by that QCCP as both initial margin and contribution to the mutualized loss sharing arrangement in relation to the link, the institution must treat the asset as a default fund contribution. *(L.N. 167 of 2023)*

(7) This section applies subject to section 2 of Schedule 16. *(L.N. 44 of 2020)*

226Z. Exposures of clearing members to direct clients

(L.N. 44 of 2020)

(1) An authorized institution that is a clearing member of a CCP must calculate—

(a) the risk-weighted amount of its default risk exposure and risk-weighted amount for CVA risk in respect of its direct clients arising from CCP-related transactions or offsetting transactions; and

(b) the risk-weighted amount of its default risk exposures and risk-weighted amount for CVA risk arising from guarantees of direct clients' performance,

in accordance with one or more of Parts 4, 5 and 6, as the case requires, and Part 8A.

(2) Where an authorized institution—

(a) is a clearing member of a CCP; and

(b) has entered into a transaction, being the CCP-related transaction or offsetting transaction for a derivative contract traded on an exchange, with its direct client under a bilateral agreement between the institution and the client,

the institution must calculate the risk-weighted amount of its default risk exposure and risk-weighted amount for CVA risk in respect of the direct client arising from the derivative contract as if the derivative contract were an OTC derivative transaction.

(2A) For the purposes of subsections (1) and (2), if—

(a) an authorized institution has collected collateral from its direct client for a transaction cleared by a CCP and passed on the collateral to the CCP to secure that transaction; and

(b) the collateral is not a form of recognized credit risk mitigation in respect of the institution's default risk exposure to the direct client arising from the transaction because the institution does not have a first lien (or any similar right or security interest) on the collateral,

the institution may take into account the credit risk mitigation effect of the collateral passed on to the CCP in calculating the risk-weighted amount of the institution's default risk exposure to the direct client arising from the transaction as if the collateral were a form of recognized credit risk mitigation. *(L.N. 51 of 2013)*

(3) If, in calculating a default risk exposure to a direct client, an authorized institution has applied—

(a) a shorter margin period of risk determined in accordance with section 226BZE(2)(a) or 226M(1)(b); or

(b) a margin period of risk determined in accordance with section 226BZE(5) or (6), or section 226M(6) or (7), based on the shorter margin period of risk referred to in paragraph (a),

the reduced default risk exposure resulted from the use of a shorter margin period of risk under paragraph (a) or (b) must also be used in the calculation of the risk-weighted amount for CVA risk in respect of the direct client. *(L.N. 44 of 2020)*

(4) *(Repealed L.N. 44 of 2020)*

(L.N. 44 of 2020; L.N. 167 of 2023)

226ZA. Exposures of direct clients to clearing members

(L.N. 44 of 2020)

(1) Where an authorized institution—

(a) is a direct client of a clearing member of a CCP; and

(b) enters into a CCP-related transaction or an offsetting transaction (***relevant transaction***) with the clearing member that acts as a financial intermediary between the institution and the CCP,

the institution must, subject to subsections (3) and (4), calculate the risk-weighted amount of its default risk exposure and risk-weighted amount for CVA risk in respect of the clearing member arising from the relevant transaction in accordance with Part 4, 5 or 6, as the case requires, and Part 8A. *(L.N. 167 of 2023)*

(2) Where an authorized institution—

(a) is a direct client of a clearing member of a CCP; and

(b) has entered into a transaction, being the CCP-related transaction or offsetting transaction for a derivative contract traded on an exchange, with the clearing member under a bilateral agreement between the institution and the clearing member,

the institution must calculate the risk-weighted amount of its default risk exposure and risk-weighted amount for CVA risk in respect of the clearing member arising from the derivative contract as if the derivative contract were an OTC derivative transaction. *(L.N. 167 of 2023)*

(3) An authorized institution may, if the CCP is a qualifying CCP and all the conditions set out in subsection (6) are met, calculate the risk-weighted amount of its default risk exposure to the clearing member arising from the relevant transaction in accordance with sections 226W(6) and 226X(1), (2), (2A) and (3) as if its default risk exposure were to the CCP.

(4) An authorized institution may, if the CCP is a qualifying CCP and all the conditions set out in subsection (6) (excluding the condition set out in subsection (6)(a)(iii)) are met, calculate the risk-weighted amount of its default risk exposure to the clearing member arising from the relevant transaction in accordance with sections 226W(6) and 226X(1), (2), (2A) and (3) as if its default risk exposure were to the CCP except that the applicable risk-weight must be 4% instead of 2%.

(5) *(Repealed L.N. 44 of 2020)*

(6) The conditions that must be met for the relevant transaction of an authorized institution to receive the treatment referred to in subsections (3) and (4) are— *(L.N. 44 of 2020)*

(a) the offsetting transaction with the CCP for the relevant transaction is identified by the CCP as a clearing client transaction and the collateral for supporting the offsetting transaction is held by the CCP or the clearing member, or both, as applicable, under arrangements that prevent any losses to the institution due to— *(L.N. 44 of 2020)*

(i) the default or insolvency of the clearing member;

(ii) the default or insolvency of the clearing member's other direct clients; and

(iii) the joint default or joint insolvency of the clearing member and any of its other direct clients;

(b) the institution—

(i) has conducted a sufficient legal review and has a well-founded basis to conclude that, in the event of a challenge in a court of law or before an administrative authority, the relevant court or administrative authority would find that the arrangements referred to in paragraph (a) would be legal, valid, binding and enforceable under the relevant laws of the relevant jurisdictions; and

(ii) undertakes such further review as necessary to ensure continuing enforceability of the arrangements referred to in paragraph (a); and *(L.N. 44 of 2020)*

(c) relevant laws, regulations, rules, contractual or administrative arrangements provide that the offsetting transaction between the CCP and the clearing member is highly likely to continue to be indirectly transacted through the CCP, or by the CCP, if the clearing member defaults or becomes insolvent, and in such circumstances, the institution's positions and collateral with the CCP will be transferred at market value unless the institution requests to close out the positions at market value.

(L.N. 44 of 2020)

226ZB. Exposures of direct clients to CCPs

(L.N. 44 of 2020)

(1) Subject to subsections (2) and (3), where an authorized institution is a direct client of a clearing member of a CCP, if the institution enters into a transaction (***relevant transaction***) with the CCP and the performance of the institution under the relevant transaction is guaranteed by the clearing member, the institution must calculate the risk-weighted amount of its default risk exposure and risk-weighted amount for CVA risk in respect of the clearing member arising from the relevant transaction in accordance with Part 4, 5 or 6, as the case requires, and Part 8A. *(L.N. 167 of 2023)*

(2) The authorized institution may, if the CCP is a qualifying CCP and all the conditions set out in section 226ZA(6) are met, calculate the risk-weighted amount of its default risk exposure to the CCP arising from the relevant transaction in accordance with sections 226W(6) and 226X(1), (2), (2A) and (3).

(3) The authorized institution may, if the CCP is a qualifying CCP and all the conditions set out in section 226ZA(6) (excluding the condition set out in section 226ZA(6)(a)(iii)) are met, calculate the risk-weighted amount of its default risk exposure to the CCP arising from the relevant transaction in accordance with sections 226W(6) and 226X(1), (2), (2A) and (3) except that the applicable risk-weight must be 4% instead of 2%.

(4) *(Repealed L.N. 44 of 2020)*

(5) In determining whether the condition set out in section 226ZA(6)(a) is met for the purposes of subsections (2) and (3), that section is to have effect as if the words "the offsetting transaction with the CCP for the relevant transaction is identified by the CCP as a clearing client transaction and the collateral for supporting the offsetting transaction" were substituted the words "the collateral for supporting the relevant transaction". *(L.N. 175 of 2017)*

(L.N. 44 of 2020)

226ZBA. Exposure of authorized institution to higher level client or lower level client within multi-level client structure

(1) Subject to subsection (5), if an authorized institution within a multi-level client structure enters into an offsetting transaction or a CCP-related transaction with a higher level client or lower level client (***relevant client***) within the structure (***relevant transaction***), the institution must calculate the risk-weighted amount of its default risk exposure and risk-weighted amount for CVA risk in respect of the relevant client arising from the relevant transaction in accordance with Part 4, 5 or 6, as the case requires, and Part 8A. *(L.N. 167 of 2023)*

(2) If the relevant transaction referred to in subsection (1) is entered into between the institution and the relevant client under a bilateral agreement for a derivative contract traded on an exchange, the institution must calculate the risk-weighted amount of its default risk exposure and risk-weighted amount for CVA risk in respect of the relevant client arising from the derivative contract as if the derivative contract were an OTC derivative transaction. *(L.N. 167 of 2023)*

(3) In calculating the default risk exposure to the relevant client referred to in subsection (1) or (2) where such client is a lower level client, if the CCP concerned is a qualifying CCP, section 226Z(3) applies to the institution's netting set with the

lower level client as it applies to a clearing member's netting set with the clearing member's direct client.

(4) For the purposes of subsections (1) and (2), section 226Z(2A) applies to the collateral collected by the institution from a lower level client within the multi-level client structure that has been passed on to the CCP concerned to secure a transaction cleared by the CCP as if the collateral were collected by an authorized institution as a clearing member from the clearing member's direct client that has been passed on to a CCP.

(5) For a relevant transaction referred to in subsection (1) entered into by an authorized institution with a higher level client, the institution may calculate the risk-weighted amount of its default risk exposure to the higher level client arising from the relevant transaction—

(a) if all the conditions set out in section 226ZA(6), with all necessary modifications, are met for arrangements among the CCP, clearing member, all clients at levels higher than the institution within the multi-level client structure, and the institution—in accordance with sections 226W(6) and 226X(1), (2), (2A) and (3) as if its default risk exposure were to the CCP; or

(b) if all the conditions set out in section 226ZA(6) (excluding the condition set out in section 226ZA(6)(a)(iii)), with all necessary modifications, are met for arrangements among the CCP, clearing member, all clients at levels higher than the institution within the multi-level client structure, and the institution—in accordance with sections 226W(6) and 226X(1), (2), (2A) and (3) as if its default risk exposure were to the CCP except that the applicable risk-weight must be 4% instead of 2%.

(L.N. 44 of 2020)

226ZC. CCP ceases to be qualifying CCP

(1) Where a CCP ceases to be a qualifying CCP—

(a) subject to subsection (2), an authorized institution may, for a period of not more than 3 months commencing on the cessation, continue to calculate its default risk exposure in respect of transactions cleared by the CCP as if the CCP were a qualifying CCP; and

(b) an institution may, at any time before the expiration of the period referred to in paragraph (a), and must, on and after the expiration of that period, calculate its default risk exposures in respect of transactions cleared by the CCP on the basis that the CCP is a non-qualifying CCP unless the CCP again becomes a qualifying CCP.

(2) The Monetary Authority may, by notice in writing given to an authorized institution, require the institution to calculate its default risk exposure to a CCP that has ceased to be a qualifying CCP in accordance with the requirements applicable to a non-qualifying CCP, beginning on the date, or the occurrence of the event, specified in the notice.

(3) An authorized institution must comply with the requirements of a notice given to it under subsection (2).

(4) Subsections (1) and (2) apply to the calculation of regulatory capital for default fund contribution to a CCP as they apply to the calculation of default risk exposures in respect of transactions cleared by the CCP.

226ZD. Exposures of clearing members to non-qualifying CCPs

(1) An authorized institution that is a clearing member of a non-qualifying CCP must calculate, in accordance with Part 4, the risk-weighted amount of—

(a) its default risk exposure to the CCP in respect of derivative contracts or SFTs entered into with the CCP; and

(b) its default risk exposure to the CCP arising from guarantees provided by the institution to its direct clients for any loss due to changes in the value of the clients' transactions in the event that the CCP defaults. *(L.N. 44 of 2020)*

(1A) To avoid doubt, for the purposes of subsection (1), if there is recognized credit risk mitigation not included in the calculation of the default risk exposure to the non-qualifying CCP, the recognized credit risk mitigation may be taken into account in the calculation of the risk-weighted amount of the exposure only if this is conducted in accordance with Part 4. *(L.N. 44 of 2020)*

(2) Subject to subsections (3) and (5), an authorized institution must allocate a risk-weight of 1,250% to its default fund contribution to a non-qualifying CCP and, for that purpose, the institution's default fund contribution must include the funded and unfunded contributions that the institution is liable to pay if the non-qualifying CCP requires the institution to do so. *(L.N. 44 of 2020)*

(3) If the default fund contribution of an authorized institution to a non-qualifying CCP consists of a binding commitment in respect of an unfunded default fund contribution to the CCP and the amount of the commitment is unlimited, the institution must determine the amount of the commitment to which a 1,250% risk-weight is to apply based on its own estimation, unless the Monetary Authority, by notice in writing given to the institution, requires the institution to—

(a) use the amount specified by the Monetary Authority in the notice as the amount of the commitment to which a 1,250% risk-weight is to apply; or

(b) use the method specified by the Monetary Authority in the notice to estimate the amount of the commitment to which a 1,250% risk-weight is to apply.

(4) An authorized institution must comply with the requirements of a notice given to it under subsection (3).

(5) An authorized institution may allocate a risk-weight of 0% to its funded default fund contribution made to a non-qualifying CCP, to the extent of the amount for covering settlement-risk only products. *(L.N. 44 of 2020; L.N. 167 of 2023)*

226ZE. Treatment of posted collateral

(1) Subject to subsections (2), (3) and (4), if—

(a) an authorized institution has posted collateral to—

(i) a CCP;

(ii) a CCP's clearing member; or

(iii) a higher level client within a multi-level client structure; and

(b) the collateral is unsegregated collateral,

the institution must, in respect of the collateral, calculate the risk-weighted amount of its credit exposure to the person holding the collateral in accordance with Part 4, 5 or 6, as the case requires. *(L.N. 44 of 2020)*

(2) Where the person referred to in subsection (1) is a CCP, the institution must determine the risk-weight applicable to the CCP in accordance with Part 4, 5 or 6, as the case requires, if the CCP is a qualifying CCP and in accordance with Part 4 if the CCP is a non-qualifying CCP.

(3) Where an authorized institution is a clearing member of a CCP and has posted collateral for transactions with the CCP, the institution is not, in respect of the collateral, required to

hold regulatory capital for its credit exposure to the person holding the collateral if the collateral—

(a) is held by a custodian; and

(b) is bankruptcy remote from the CCP.

(4) Where an authorized institution is a direct client of a clearing member of a CCP, or is an indirect client within a multi-level client structure associated with a CCP, and has posted collateral for transactions cleared by the CCP, the institution is not, in respect of the collateral, required to hold regulatory capital for its credit exposure to the person holding the collateral if the collateral— *(L.N. 44 of 2020)*

(a) is held by a custodian; and

(b) is bankruptcy remote from the CCP, the clearing member concerned, the clearing member's direct clients, and, if clearing of the transactions by the CCP involves a multi-level client structure, clients within the structure at levels higher than the institution and those clients' clearing clients (whether within the structure or not). *(L.N. 44 of 2020)*

(5)-(6) *(Repealed L.N. 44 of 2020)*

(6A) Subsections (1) and (2) do not apply to collateral posted by an authorized institution that is—

(a) included as part of a default risk exposure to a CCP under section 226V(2)(a); or

(b) included in the calculation of the default risk exposure to a CCP, clearing member or higher level client under Division 1A, 2, 2A or 2B. *(L.N. 44 of 2020)*

(7) To avoid doubt—

(a) any unsegregated collateral posted by an authorized institution to a CCP, clearing member or higher level client (***concerned party***) must be risk-weighted in accordance with section 226X, 226ZA, 226ZB, 226ZBA or 226ZD, as the case requires, if the unsegregated collateral is—

(i) posted in respect of one or more than one CCP-related transaction or offsetting transaction or in respect of a transaction entered into by the institution as a direct client with a CCP; and

(ii) included as part of the institution's default risk exposure to the concerned party by virtue of Division 1A, 2, 2A or 2B or section 226V(2)(a); and *(L.N. 44 of 2020)*

(b) an authorized institution that has posted an asset as collateral must hold regulatory capital for the credit risk or market risk, whichever is applicable, of the asset itself calculated in accordance with Part 4, 5, 6, 7 or 8, as the case requires, as if it had not been posted as collateral and, if the collateral is held by another person, as if the collateral were held by the institution.

(8) In this section—

custodian (保管人) means a trustee, agent, pledgee, secured creditor or any other person that holds property (***property holder***) in a way—

(a) that does not give the property holder a beneficial interest in the property; and

(b) that will not result in the property being subject to legally-enforceable claims by the property holder's creditors, or to a court-ordered stay of the return of the property, if the property holder becomes insolvent or bankrupt.

Part 6B

Calculation of Risk-weighted Amounts of CIS Exposures

(Part 6B added L.N. 54 of 2022)

Division 1—Preliminary

226ZF. Application of Part 6B

This Part applies to the calculation of the risk-weighted amounts of an authorized institution's CIS exposures booked in its banking book, or any parts of such exposures, that do not constitute deductible holdings.

226ZG. Interpretation of Part 6B

In this Part—

BSC AI means an authorized institution that uses the BSC approach to calculate its credit risk for all its non-securitization exposures;

credit equivalent amount (信貸等值數額), in relation to the calculation of the risk-weighted amount of an off-balance sheet exposure that is a CIS exposure by an authorized institution—

(a) if the institution is an STC AI or an exempted IRB AI—has the meaning given by section 51(1);

(b) if the institution is a BSC AI—has the meaning given by section 105; or

(c) if the institution is an IRB AI—has the meaning given by section 139(1);

exempted IRB AI (豁免IRB AI) means an authorized institution that uses the IRB approach to calculate its credit risk for some of its non-securitization exposures but uses the STC approach to calculate the risk-weighted amounts of its CIS exposures; *(L.N. 167 of 2023)*

fall-back approach (備選方法) means the approach of determining, in accordance with section 226ZS, the risk-weight applicable to a CIS exposure to, or any of the underlying exposures of, the collective investment scheme concerned;

IRB AI means an authorized institution that uses the IRB approach to calculate the risk-weighted amounts of its CIS exposures;

look-through approach (透視計算法) means the approach of calculating, in accordance with section 226ZO, the risk-weighted amount of the underlying exposures of the collective investment scheme concerned;

LTA conditions (LTA條件)—see section 226ZM;

mandate-based approach (授權基準計算法) means the approach of calculating, in accordance with sections 226ZQ and 226ZR, the risk-weighted amount of the underlying exposures of the collective investment scheme concerned;

principal amount (本金額), in relation to the calculation of the risk-weighted amount of an on-balance sheet exposure that is a CIS exposure by an authorized institution—

(a) if the institution is an STC AI or an exempted IRB AI—means the principal amount within the meaning of paragraph (a) of the definition of ***principal amount*** in section 51(1);

(b) if the institution is a BSC AI—means the principal amount within the meaning of paragraph (a) of the definition of ***principal amount*** in section 105; or

(c) if the institution is an IRB AI—means the principal amount within the meaning of paragraph (a) of the definition of ***principal amount*** in section 139(1);

STC AI means an authorized institution that uses the STC approach to calculate its credit risk for all its non-securitization exposures;

third-party approach (第三方計算法) means the approach of using the risk-weighted amount of all underlying exposures of a collective investment scheme calculated by a third party in calculating, in accordance with section 226ZP, the input to be used in calculating the risk-weighted amount of a CIS exposure to the scheme;

TPA conditions (TPA條件)—see section 226ZN.

(L.N. 167 of 2023)

226ZH. Interpretation: levels of collective investment scheme etc.

(1) An authorized institution or a collective investment scheme holds a CIS exposure to a collective investment scheme if the CIS exposure is held directly by the institution or the first-mentioned collective investment scheme (as the case requires).

(2) If an authorized institution holds a CIS exposure to a collective investment scheme, that collective investment scheme is a Level 1 CIS in relation to the institution.

(3) If a Level 1 CIS in relation to an authorized institution holds a CIS exposure to another collective investment scheme—

(a) that another collective investment scheme is a Level 2 CIS in relation to the institution;

(b) any collective investment scheme to which the Level 2 CIS holds a CIS exposure is a Level n+1 CIS (where n = 2) in relation to the institution;

(c) the Level 1 CIS has an indirect CIS exposure to the Level n+1 CIS through (n–1) interposed collective investment scheme (***interposed CIS***); and

(d) the Level 2 CIS is that interposed CIS.

(4) A Level 1 CIS in relation to an authorized institution holds an indirect CIS exposure to a Level n+1 CIS (where n is an integer ≥ 3) in relation to the institution if—

(a) there are (n–1) interposed CISs between the Level 1 CIS and the Level n+1 CIS;

(b) a CIS exposure to the $(n–1)^{th}$ interposed CIS (***Level n CIS***) is held directly by the $(n–2)^{th}$ interposed CIS and likewise for other interposed CISs (if any); and

(c) the Level n CIS holds a CIS exposure to the Level n+1 CIS.

(5) A reference in a provision in Division 2, 3 or 4 to a CIS exposure to a collective investment scheme is—

(a) unless paragraph (b) applies, a reference to an authorized institution's CIS exposure to a Level 1 CIS; or

(b) when it is necessary to apply the provision to calculate the risk-weighted amount of a CIS exposure to a Level n+1 CIS held directly by a Level n CIS (where n is an integer ≥ 1) in order to calculate the risk-weighted amount of an authorized institution's CIS exposure to a Level 1 CIS—a reference to the Level n CIS's CIS exposure to the Level n+1 CIS.

(6) A reference in a provision in Division 2, 3 or 4 to an underlying exposure or underlying exposures of a collective investment scheme is—

(a) unless paragraph (b) applies, a reference to an underlying exposure or underlying exposures of a Level 1 CIS; or

(b) when it is necessary to apply the provision to calculate the risk-weighted amount of the underlying exposures of a Level n+1 CIS (where n is an integer $\geq$ 1) in order to calculate the risk-weighted amount of the underlying exposures of a Level 1 CIS—a reference to an underlying exposure or underlying exposures of the Level n+1 CIS.

Division 2—Calculation of Risk-weighted Amounts of CIS Exposures to Collective Investment Schemes

226ZI. Calculation of risk-weighted amount of CIS exposure

(1) An authorized institution must calculate the risk-weighted amount of a CIS exposure (***$RWA_{CIS\ exposure}$***) to a collective investment scheme by using Formula 23L.

Formula 23L

Calculation of Risk-weighted Amount of CIS Exposure to Collective Investment Scheme

$$RWA_{CIS\ exposure} = \text{Effective RW} * P_{CIS\ exposure}$$

where—

(a) Effective RW is the effective risk-weight applicable to the CIS exposure determined in accordance with section 226ZJ; and

(b) subject to subsections (2) and (3), $P_{CIS\ exposure}$ is—

(i) if the CIS exposure is an on-balance sheet exposure—the principal amount of the CIS exposure; or

(ii) if the CIS exposure is an off-balance sheet exposure—the credit equivalent amount of the CIS exposure.

(2) If the maximum financial leverage of the scheme is taken, under paragraph (b)(ii) of Formula 23M, as the Leverage in that Formula, $P_{\text{CIS exposure}}$ of the CIS exposure to the scheme may be adjusted by regarding the total equity implied by the maximum financial leverage as the actual total equity of the scheme.

(3) If—

(a) the CIS exposure to the scheme (***first scheme***) is held by the authorized institution or another collective investment scheme (***second scheme***);

(b) the CIS exposure is in the form of units or shares in the first scheme; and

(c) the institution uses the look-through approach, the third-party approach or a combination of approaches that contains the look-through approach to calculate the risk-weighted amount of the underlying exposures of the first scheme,

the institution may set $P_{\text{CIS exposure}}$ in Formula 23L equal to the product of the total equity of the first scheme and the percentage of units or shares in the first scheme held by the institution or the second scheme, as the case may be.

(4) To avoid doubt, if any part of an authorized institution's CIS exposure to a Level 1 CIS constitutes one or more than one deductible holding of the institution, the institution is only required to calculate a risk-weighted amount in accordance

with this Division for that part of the CIS exposure that does not constitute any deductible holding of the institution.

226ZJ. Calculation of effective risk-weight applicable to CIS exposure for purposes of section 226ZI

(1) If, under Division 3 or 6, an authorized institution chooses to, or is required to, allocate a risk-weight to a CIS exposure to a collective investment scheme by using the fall-back approach and not in combination with any other approach (as applicable under section 226ZS(1)), the effective risk-weight applicable to the CIS exposure is 1,250%.

(2) If subsection (1) is not applicable, the effective risk-weight applicable to the CIS exposure (***effective RW***) must be calculated by using Formula 23M.

Formula 23M

Calculation of Effective Risk-weight Applicable to CIS Exposure

$$\text{Effective RW} = \min \{1{,}250\%; \text{Avg RW}_{\text{CIS}} * \text{Leverage}\}$$

where—

(a) Avg RW_{CIS} is the amount calculated by dividing the amount specified in subparagraph (i) by the amount specified in subparagraph (ii)—

(i) the aggregate risk-weighted amount of the underlying exposures of the scheme calculated by using (as applicable under Division 3 or 6)—

(A) the look-through approach;

(B) the third-party approach;

(C) the mandate-based approach; or

(D) any combination of the look-through approach, the mandate-based approach and the fall-back approach;

(ii) the total assets of the scheme; and

(b) Leverage is—

(i) if the risk-weighted amounts of all or part of the underlying exposures of the scheme are determined by using the look-through approach or the risk-weighted amounts of all of the underlying exposures of the scheme are determined by using the third-party approach—the ratio of the total assets of the scheme to its total equity; or

(ii) if subparagraph (i) is not applicable and the risk-weighted amounts of all or part of the underlying exposures of the scheme are determined by using the mandate-based approach—the maximum financial leverage permitted by the scheme's mandate or by the legislation or regulations governing the scheme, as the case may be.

Division 3—Determination of Approaches to be Used

226ZK. Approaches to be used in calculating risk-weighted amounts of CIS exposures etc.

(1) An authorized institution must use the look-through approach to calculate the risk-weighted amount of all underlying

exposures of a Level 1 CIS if the LTA conditions are met in respect of the Level 1 CIS.

(2) If the LTA conditions are not met in respect of the Level 1 CIS, the institution may choose to use the third-party approach for the purpose of calculating the risk-weighted amount of a CIS exposure to the Level 1 CIS if the TPA conditions are met in respect of the Level 1 CIS.

(3) If the LTA conditions are not met in respect of the Level 1 CIS, and the institution chooses not to use the third-party approach or the use of the third-party approach is infeasible, the institution must—

(a) use the mandate-based approach to calculate the risk-weighted amount of all underlying exposures of the Level 1 CIS; or

(b) subject to subsection (5), use any combination of the look-through approach, the mandate-based approach and the fall-back approach to calculate the risk-weighted amount of all underlying exposures of the Level 1 CIS.

(4) If—

(a) the LTA conditions are not met in respect of the Level 1 CIS;

(b) the institution chooses not to use the third-party approach or the use of the third-party approach is infeasible; and

(c) neither using the mandate-based approach under subsection (3)(a) nor using the combination mentioned in subsection (3)(b) is feasible,

the institution must allocate a risk-weight under the fall-back approach to its CIS exposure to the Level 1 CIS to calculate the risk-weighted amount of the CIS exposure.

(5) The institution may use the look-through approach under subsection (3)(b) for any part of the underlying exposures of the Level 1 CIS only if the LTA conditions are met in respect of the Level 1 CIS and section 226ZM applies for this purpose as if a reference to all of the underlying exposures of a collective investment scheme in that section were a reference to that part of the underlying exposures of the Level 1 CIS.

(6) If different approaches are used under subsection (3)(b), the requirements applicable to any approach concerned under this Part must be met in respect of the part of the underlying exposures for which the approach is used.

226ZL. Approaches to be used in calculating risk-weighted amounts of CIS exposures to Level 1 CIS: BSC AI

Despite section 226ZK, a BSC AI may, for the purpose of calculating the risk-weighted amount of its CIS exposure to a Level 1 CIS, allocate a risk-weight under the fall-back approach (as applicable under section 226ZS(1)) to its CIS exposure to the Level 1 CIS.

226ZM. LTA conditions

(1) For the calculation of the risk-weighted amount of the underlying exposures of a collective investment scheme by an authorized institution, the LTA conditions are met in respect of the scheme if both of the following requirements are satisfied—

(a) there is sufficient and frequent information available to the institution regarding all the underlying exposures of the scheme;

(b) the information and all underlying exposures are verified by an independent third party, such as a depository, a custodian bank or a management company.

(2) The requirement in subsection (1)(a) is satisfied if—

(a) the frequency of financial reporting of the scheme is the same as, or more frequent than, that of the authorized institution's financial reporting; and

(b) the granularity of the financial information provided in the scheme's financial report is sufficient for determining the risk-weighted amount of all its underlying exposures in accordance with the look-through approach.

(3) For the purposes of subsection (2), a financial report of the scheme need not be an audited report.

226ZN. TPA conditions

(1) For the use by an authorized institution of the risk-weighted amount of the underlying exposures of a collective investment scheme calculated by a third party, the TPA conditions are met in respect of the scheme if—

(a) a risk-weighted amount of all the underlying exposures of the scheme calculated by the third party (***third-party output***) is available to the institution;

(b) the third party recalculates and updates the third-party output at a frequency that is the same as, or more frequent than, that of the institution's financial reporting;

(c) the third party is the depository or the management company (however described) of the scheme;

(d) the third party calculates the third-party output in a way described in subsection (2); and

(e) an external auditor has confirmed the correctness of the calculations that generate the third-party output.

(2) The condition in subsection (1)(d) is met if the third party calculates the third-party output— *(L.N. 167 of 2023)*

(a) by using the look-through approach in the same way as an STC AI that holds a CIS exposure to the scheme directly would be required to do under section 226ZO as if sections 65H, 65I, 70A, 226ZT and 226ZX did not exist; or

(b) in accordance with the capital standards issued by the Basel Committee that are in force at the time of the calculation and that correspond to—

(i) this Part (other than sections 226ZT and 226ZX);

(ii) Part 4 (other than sections 65H, 65I, 70A); and

(iii) Parts 6A and 7, in so far as they relate to an STC AI.

(3) *(Repealed L.N. 167 of 2023)*

(L.N. 167 of 2023)

Division 4—Determination of Risk-weight under Different Approaches

226ZO. Look-through approach: calculation of risk-weighted amount of underlying exposures

(1) An authorized institution using the look-through approach to calculate the risk-weighted amount of an underlying exposure of a collective investment scheme must comply with this section.

(2) If an underlying exposure of a collective investment scheme is a CIS exposure to another collective investment scheme, the institution must calculate the risk-weighted amount of the underlying exposure in accordance with—

(a) if that another collective investment scheme is a Level 2 CIS in relation to the institution—sections 226ZU and 226ZX; or

(b) if that another collective investment scheme is a Level n+1 CIS (where n is an integer ≥ 2) in relation to the institution—sections 226ZV, 226ZW and 226ZX.

(3) If an underlying exposure of a collective investment scheme is a capital investment in a commercial entity, the institution must calculate the risk-weighted amount of the underlying exposure—

(a) if the institution is an STC AI or an exempted IRB AI—in accordance with those provisions of Part 4 that would be applicable to the capital investment if the capital investment were held directly by the institution and sections 43(1)(n), 46(1) and 65H did not exist;

(b) if the institution is a BSC AI—in accordance with those provisions of Part 5 that would be applicable to the capital investment if the capital investment were held directly by the institution and sections 43(1)(n), 46(1) and 115F did not exist; or

(c) if the institution is an IRB AI—in accordance with those provisions of Part 4 or 6, as the case requires, that would be applicable to the capital investment if the capital investment were held directly by the institution and sections 43(1)(n), 46(1) and 65H did not exist. *(L.N. 167 of 2023)*

(4) Subject to subsection (5), if an underlying exposure of a collective investment scheme is an exposure to CVA risk in respect of derivative contracts or SFTs entered into by the scheme, the institution must, instead of using the methods set out in Part 8A— *(L.N. 167 of 2023)*

(a) for derivative contracts, and SFTs the default risk exposures of which are not required to be calculated in accordance with section 226MJ—calculate the risk-weighted amount of the underlying exposure as the product of the following, as if the contracts or SFTs were entered into by the institution—

(i) the amount of the default risk exposure of the derivative contracts or SFTs;

(ii) 0.5; and

(iii) the risk-weight applicable to the default risk exposure; or

(b) for SFTs the default risk exposures of which are required to be calculated in accordance with section 226MJ—calculate the risk-weighted amount of the underlying exposure as the product of the following, as if the SFTs were entered into by the institution—

(i) the sum of the risk-weighted amounts of the default risk exposures of the SFTs calculated in accordance with—

(A) if the institution is an STC AI or an exempted IRB AI—section 85 or 86, as the case requires;

(B) if the institution is a BSC AI—section 129; or

(C) if the institution is an IRB AI—section 202; and

(ii) 0.5. *(L.N. 167 of 2023)*

(5) An authorized institution may, in calculating the risk-weighted amount of an underlying exposure of a collective investment scheme under subsection (4)—

(a) exclude the default risk exposures of derivative contracts and SFTs of the scheme that are entered into with qualifying CCPs; and

(b) if no information obtained by the institution for the purpose of using the look-through approach suggests that the scheme's CVA risk arising from SFTs is material—exclude the default risk exposures of SFTs of the scheme that are not entered into with qualifying CCPs.

(6) If an underlying exposure of a collective investment scheme does not fall within subsection (2), (3) or (4), the institution must calculate the risk-weighted amount of the underlying exposure, as if it were held directly by the institution—

(a) if the institution is an STC AI or an exempted IRB AI—in accordance with Part 4 or 7, or Division 4 of Part 6A, as the case requires;

(b) if the institution is a BSC AI—in accordance with Part 5 or 7, or Division 4 of Part 6A, as the case requires; or

(c) if the institution is an IRB AI—in accordance with Part 6 or 7, or Division 4 of Part 6A, as the case requires.

(7) If, in calculating the risk-weighted amount of an underlying exposure under subsection (2), (3), (4) or (6), it is infeasible for an IRB AI to use the IRB calculation approaches set out in Table 17 or the SEC-IRBA under Part 7, as the case requires, or the IRB AI is not granted an approval to use the IRB approach, to determine the risk-weighted amount of the underlying exposure, the IRB AI must determine the risk-weighted amount of the underlying exposure by— *(L.N. 167 of 2023)*

(a) *(Repealed L.N. 167 of 2023)*

(b) if the exposure is a securitization exposure—using the SEC-ERBA, SEC-SA or SEC-FBA under Part 7, as the case requires; or

(c) if the exposure does not fall within paragraph (b)—applying Part 4. *(L.N. 167 of 2023)*

(8) If an IRB AI is granted an exemption under section 12(2)(a), in relation to an exposure that is an underlying exposure mentioned in subsection (3), (4)(b) or (6) and the underlying exposure is not a securitization exposure, the IRB AI must apply subsection (3)(a), (4)(b)(i)(A) and (ii) or (6)(a) instead of subsection (3)(c), (4)(b)(i)(C) and (ii) or (6)(c), as the case requires, to determine the risk-weighted amount of the underlying exposure.

226ZP. Use of risk-weighted amount obtained by using third-party approach

An authorized institution using the third-party approach for the purpose of calculating the risk-weighted amount of a CIS exposure to a collective investment scheme—

(a) must multiply the risk-weighted amount of all underlying exposures of the scheme calculated by the third party concerned by 1.2; and

(b) must use the product calculated under paragraph (a) as the aggregate risk-weighted amount of the underlying exposures of the scheme for the purposes of Formula 23M.

226ZQ. Mandate-based approach: general requirements

(1) An authorized institution using the mandate-based approach to calculate the risk-weighted amounts of the underlying exposures of a collective investment scheme must comply with this section.

(2) The institution must use the information contained in any one or more of the following documents to calculate the risk-weighted amounts of the underlying exposures of a collective investment scheme—

(a) the mandate of the scheme;

(b) other disclosures of the scheme;

(c) the legislation or regulations governing the scheme.

(3) The institution must calculate the risk-weighted amounts of the underlying exposures of the scheme based on the assumptions specified in subsections (4), (5), (6) and (7).

(4) The scheme invests in underlying exposures falling within paragraph (ab)(i) of the definition of ***underlying exposures*** in section 2(1) in the following order—

(a) first invests in assets that would attract the highest risk-weight under—

(i) if the institution is an STC AI, an IRB AI or an exempted IRB AI—this Part and Parts 4 and 7; or

(ii) if the institution is a BSC AI—this Part and Parts 5 and 7,

(iii) *(Repealed L.N. 167 of 2023)*

to the maximum extent allowed under the mandate of the scheme (or, if applicable, under the relevant legislation or regulations governing the scheme); and *(L.N. 167 of 2023)*

(b) then invests in other assets in descending order of risk-weight, to the maximum extent allowed under the mandate of the scheme (or, if applicable, under the relevant legislation or regulations governing the scheme).

(5) The credit equivalent amount of the scheme's underlying exposures falling within paragraph (ab)(ii) of the definition of ***underlying exposures*** in section 2(1) arising from derivative contracts entered into by the scheme is equal to—

(a) unless paragraph (b) applies, the notional amount of the scheme's position in the underlying exposures (as defined by section 226A) of the derivative contracts; or

(b) either—

(i) if the underlying exposures of the derivative contracts are unknown—the full notional amount of the derivative contracts; or

(ii) if the notional amount of the derivative contracts is unknown—the maximum notional amount of derivative contracts allowed under the mandate of the scheme (or, if applicable, under the relevant legislation or regulations governing the scheme).

(6) The amount of the scheme's underlying exposures falling within paragraph (ab)(iii) of the definition of ***underlying exposures*** in section 2(1) arising from derivative contracts is the default risk exposure calculated for the derivative contracts by using—

(a) if the institution is an STC AI, an exempted IRB AI or an IRB AI—the SA-CCR approach; or

(b) if the institution is a BSC AI—the SA-CCR approach or current exposure method.

(7) The credit equivalent amount of any other underlying exposures of the scheme is equal to—

(a) unless paragraph (b) applies, the contracted amount of the underlying exposures; or

(b) if the contracted amount is unknown—the maximum contracted amount allowed under the mandate of the scheme (or, if applicable, under the relevant legislation or regulations governing the scheme).

(8) For the purpose of using the SA-CCR approach under subsection (6)(a) or (b)—

(a) if the replacement cost of a netting set is unknown—

(i) the sum of the notional amounts of the derivative contracts in the netting set must be regarded as the replacement cost of the netting set; and

(ii) the value of the multiplier in Formula 23AM must be set at 1; and

(b) if the potential future exposure of a netting set is unknown—the product of the sum of the notional amounts of the derivative contracts in the netting set and 15% must be regarded as the potential future exposure of the netting set.

(9) For the purpose of using the current exposure method under subsection (6)(b)—

(a) if the replacement cost of a derivative contract is unknown—the notional amount of the contract must be regarded as the replacement cost of the contract; and

(b) if the credit conversion factor applicable to a derivative contract is unknown—47% must be regarded as the credit conversion factor applicable to the contract.

226ZR. Mandate-based approach: calculation of risk-weighted amounts of underlying exposures

(1) In addition to section 226ZQ, an authorized institution using the mandate-based approach to calculate the risk-weighted amounts of the underlying exposures of a collective investment scheme must comply with this section.

(2) If an underlying exposure of a collective investment scheme is a CIS exposure to another collective investment scheme, the institution must calculate the risk-weighted amount of the underlying exposure in accordance with—

(a) if that another collective investment scheme is a Level 2 CIS in relation to the institution—sections 226ZU and 226ZX; or

(b) if that another collective investment scheme is a Level n+1 CIS (where n is an integer ≥ 2) in relation to the institution—sections 226ZV, 226ZW and 226ZX.

(3) If an underlying exposure of a collective investment scheme is a capital investment in a commercial entity, the institution must calculate the risk-weighted amount of the underlying exposure—

(a) if the institution is an STC AI, an IRB AI or an exempted IRB AI—in accordance with those provisions of Part 4 that would be applicable to the capital investment if the capital investment were held directly by the institution and sections 43(1)(n), 46(1) and 65H did not exist; or *(L.N. 167 of 2023)*

(b) if the institution is a BSC AI—in accordance with those provisions of Part 5 that would be applicable to the capital investment if the capital investment were held directly by the institution and sections 43(1)(n), 46(1) and 115F did not exist. *(L.N. 167 of 2023)*

(c) *(Repealed L.N. 167 of 2023)*

(4) Subject to subsection (5), if an underlying exposure of a collective investment scheme is an exposure to CVA risk in respect of derivative contracts or SFTs entered into by the scheme, the institution must, instead of using the methods set out in Part 8A— *(L.N. 167 of 2023)*

(a) for derivative contracts, and SFTs the default risk exposures of which are not required to be calculated in accordance with section 226MJ—calculate the risk-weighted amount of the underlying exposure as the product of the following, as if the contracts or SFTs were entered into by the institution—

(i) the amount of the default risk exposure of the derivative contracts or SFTs;

(ii) 0.5; and

(iii) the risk-weight applicable to the default risk exposure; or

(b) for SFTs the default risk exposures of which are required to be calculated in accordance with section 226MJ—calculate the risk-weighted amount of the underlying exposure as the product of the following, as if the SFTs were entered into by the institution—

(i) the sum of the risk-weighted amounts of the default risk exposures of the SFTs calculated in accordance with—

(A) if the institution is an STC AI, an IRB AI or an exempted IRB AI—section 85 or 86, as the case requires; or

(B) if the institution is a BSC AI—section 129; and

(C) *(Repealed L.N. 167 of 2023)*

(ii) 0.5. *(L.N. 167 of 2023)*

(5) An authorized institution may, in calculating the risk-weighted amount of an underlying exposure of a collective investment scheme under subsection (4)—

(a) exclude the default risk exposures of derivative contracts and SFTs of the scheme that are entered into with qualifying CCPs; and

(b) if no information obtained by the institution for the purpose of using the mandate-based approach suggests that the scheme's CVA risk arising from SFTs is material—exclude the default risk exposures of SFTs of the scheme that are not entered into with qualifying CCPs.

(6) If an underlying exposure of a collective investment scheme does not fall within subsection (2), (3) or (4), the institution must calculate the risk-weighted amount of the underlying exposure, as if it were held directly by the institution—

(a) if the institution is an STC AI or an exempted IRB AI—in accordance with Part 4 or 7, or Division 4 of Part 6A, as the case requires;

(b) if the institution is a BSC AI—in accordance with Part 5 or 7, or Division 4 of Part 6A, as the case requires; or

(c) if the institution is an IRB AI, by—

(i) *(Repealed L.N. 167 of 2023)*

(ii) using the SEC-ERBA, SEC-SA or SEC-FBA under Part 7, as the case requires—if the exposure is a securitization exposure; or

(iii) applying Part 4 or Division 4 of Part 6A, as the case requires—if the exposure does not fall within subparagraph (ii). *(L.N. 167 of 2023)*

(7) If, due to the lack of sufficient information available to the institution, more than one risk-weight is applicable to an underlying exposure, the institution must allocate to the underlying exposure the highest of those applicable risk-weights.

226ZS. Fall-back approach

(1) If an authorized institution uses only the fall-back approach (and not in combination with one or more than one other approach) for the purpose of calculating the risk-weighted amount of a CIS exposure to a collective investment scheme, the institution must allocate a risk-weight of 1,250% to the exposure.

(2) If an authorized institution uses the fall-back approach in combination with one or more than one other approach for the purpose of calculating the risk-weighted amount of the underlying exposures of a collective investment scheme, any underlying exposure of the scheme that is subject to the fall-back approach must be allocated a risk-weight of 1,250%.

Division 5—Regulatory Deductible Items Held by Level 1 CIS

226ZT. Certain regulatory deductible items held by Level 1 CIS may be excluded from underlying exposures

(1) This section applies to an authorized institution's CIS exposure to a Level 1 CIS if—

(a) any part of the CIS exposure constitutes one or more than one deductible holding of the institution;

(b) some or all of the regulatory deductible items concerned are held directly by the Level 1 CIS; and

(c) the deductible holding is—

(i) fully deducted from the capital base of the institution under Division 4 of Part 3;

(ii) partially deducted from the capital base of the institution under Division 4 of Part 3 and partially risk-weighted under section 70A(3), 117F(3) or 183; or

(iii) fully risk-weighted under section 70A(3), 117F(3) or 183. *(L.N. 167 of 2023)*

(2) The institution may exclude any regulatory deductible items that are held by the Level 1 CIS and associated with the holding falling within subsection (1)(c) from its underlying exposures when calculating the aggregate risk-weighted

amount of the underlying exposures of the Level 1 CIS mentioned in paragraph (a)(i) of Formula 23M.

Division 6—CIS Exposures Held by Collective Investment Schemes

226ZU. Calculation of risk-weighted amounts of CIS exposures held by Level 1 CIS

(1) This section applies to the calculation of the risk-weighted amount of a Level 1 CIS's CIS exposure to a Level 2 CIS.

(2) The risk-weight allocated to the CIS exposure to a Level 2 CIS must be determined, or the risk-weighted amount of the underlying exposures of the Level 2 CIS must be calculated, by using the approach or approaches determined in accordance with Division 3 as if the Level 2 CIS were a Level 1 CIS.

(3) The risk-weighted amount of the CIS exposure must be calculated in accordance with Division 2 by using the risk-weight or risk-weighted amount referred to in subsection (2) determined or calculated in accordance with Division 4.

(4) If there is any regulatory deductible item held by the Level 2 CIS, the application of Divisions 2 and 4 under subsection (3) is subject to modification by section 226ZX.

226ZV. Calculation of risk-weighted amounts of CIS exposures held by Level 2 CIS onwards

(1) Subsections (2) and (3) apply to the calculation of the risk-weighted amount of an underlying exposure of a Level n CIS that is a CIS exposure to a Level n+1 CIS (where n is an integer not less than 2) if, under section 226ZU, an authorized institution—

(a) does not use the third-party approach to obtain the risk-weighted amount of the underlying exposures of the Level 2 CIS that is interposed between the Level 1 CIS and the Level n+1 CIS; and

(b) does not allocate a risk-weight of 1,250% to the CIS exposure of the Level 1 CIS to the Level 2 CIS under the fall-back approach in accordance with section 226ZS(1).

(2) Subject to subsection (3), the institution must calculate the risk-weighted amount of the CIS exposure to the Level n+1 CIS held by the Level n CIS by using the fall-back approach—

(a) unless paragraph (b) applies, in accordance with sections 226ZI, 226ZJ(1) and 226ZS(1); or

(b) if there is any regulatory deductible item held by the Level n+1 CIS—in accordance with sections 226ZI, 226ZJ(1) and 226ZS(1) as modified by section 226ZX.

(3) If it is determined under section 226ZW that the look-through approach can be used to calculate the risk-weighted amount of the underlying exposures of the Level n+1 CIS, the institution may calculate the risk-weighted amount of the CIS exposure to the Level n+1 CIS held by the Level n CIS by using the look-through approach—

(a) unless paragraph (b) applies, in accordance with sections 226ZI, 226ZJ(2) and 226ZO; or

(b) if there is any regulatory deductible item held by the Level n+1 CIS—in accordance with sections 226ZI, 226ZJ(2) and 226ZO as modified by section 226ZX.

226ZW. Calculation of risk-weighted amounts of CIS exposures held by Level 2 CIS onwards: conditions for using look-through approach

For the purpose of calculating the risk-weighted amount of a CIS exposure to a Level n+1 CIS (***Level n+1 CIS exposure***) held by a Level n CIS (where n is an integer not less than 2), an authorized institution may calculate the risk-weighted amount of the underlying exposures of the Level n+1 CIS by using the look-through approach only if—

(a) either—

(i) in cases where n = 2—

(A) the risk-weighted amount of all or part of the underlying exposures of the Level n CIS is also calculated by using the look-through approach; and

(B) the Level n+1 CIS exposure is one of those underlying exposures that are subject to the look-through approach; or

(ii) in cases where n is an integer > 2, the risk-weighted amount of all of the underlying exposures of the Level n CIS is also calculated by using the look-through approach; and

(b) the LTA conditions are met in respect of the Level n+1 CIS.

226ZX. Calculation of risk-weighted amounts of CIS exposures held by Level 1 CIS onwards: certain regulatory deductible items may be excluded

(1) This section applies to a Level n+1 CIS (where n is an integer ≥ 1) to which a Level 1 CIS holds a CIS exposure or an indirect CIS exposure if—

(a) any part of an authorized institution's CIS exposure to the Level 1 CIS constitutes one or more than one deductible holding of the institution;

(b) some or all of the regulatory deductible items concerned are held directly by the Level n+1 CIS; and

(c) the deductible holding is—

(i) fully deducted from the capital base of the institution under Division 4 of Part 3;

(ii) partially deducted from the capital base of the institution under Division 4 of Part 3 and partially risk-weighted under section 70A(3), 117F(3) or 183; or

(iii) fully risk-weighted under section 70A(3), 117F(3) or 183. *(L.N. 167 of 2023)*

(2) For the purpose of calculating the risk-weighted amount of that part of the institution's CIS exposure to the Level 1 CIS that does not constitute any deductible holding, the institution may exclude any regulatory deductible items that are held by the Level n+1 CIS and associated with the holding falling within subsection (1)(c) from its underlying exposures when calculating the aggregate risk-weighted amount of the underlying exposures of the Level n+1 CIS mentioned in paragraph (a)(i) of Formula 23M.

Part 7

Calculation of Credit Risk for Securitization Exposures

Division 1—General

227. Interpretation of Part 7

(1) In this Part— *(L.N. 167 of 2023)*

ABCP programme (ABCP計劃) means an asset-backed commercial paper programme;

AP, in relation to a tranche in a securitization transaction, means the value of the attachment point of the tranche determined in accordance with section 247; *(L.N. 175 of 2017)*

asset-backed commercial paper programme (有資產支持的商業票據計劃) means a programme under which—

(a) an SPE in a securitization transaction issues debt securities with an original maturity of not more than one year; and

(b) the payments in respect of those debt securities are secured by a pool of underlying exposures acquired from third parties and held by, or to the order of, that SPE;

clean-up call (結清權)—

(a) in relation to a traditional securitization transaction, means an option which permits the originator in the transaction to repurchase the outstanding securitization issues of the transaction once the amount of the outstanding securitization issues, or of the underlying exposures that have not been repaid, has fallen below a level specified in the documentation for the transaction; or *(L.N. 137 of 2011)*

(b) in relation to a synthetic securitization transaction, means an option which permits the person purchasing credit protection under the documentation for the transaction to extinguish the credit protection once the amount of the reference pool of underlying exposures has fallen below a level specified in the documentation; *(L.N. 44 of 2020)*

credit enhancement (信用提升), in relation to a securitization exposure under a securitization transaction, means a contractual arrangement whereby a person—

(a) retains or assumes credit risk in respect of the exposure; and

(b) provides, in substance, some degree of credit protection to one or more than one other party to the transaction;

DP, in relation to a tranche in a securitization transaction, means the value of the detachment point of the tranche determined in accordance with section 247; *(L.N. 175 of 2017)*

early amortization provision (提早攤銷規定), in relation to a securitization transaction in which the underlying exposures are revolving in nature, means a mechanism which, once triggered, allows investors in the securitization issues to be paid out prior to the originally stated maturity of the securitization issues held by the investors;

eligible securitization transaction (合資格證券化交易)—see section 229; *(L.N. 175 of 2017)*

eligible synthetic securitization transaction (合資格合成證券化交易)—see section 229; *(L.N. 175 of 2017)*

eligible traditional securitization transaction (合資格傳統證券化交易)—see section 229; *(L.N. 175 of 2017)*

exposure amount (風險承擔數額)—

(a) in relation to a securitization exposure—means the amount determined in accordance with section 235;

(b) in relation to an underlying exposure of a securitization transaction (including an exposure, collateral or asset regarded as an underlying exposure of the transaction for the purposes of this Part) that is a securitization exposure—means the amount determined in accordance with section 235;

(c) in relation to an underlying exposure of a securitization transaction (including an exposure regarded as an underlying exposure of the transaction for the purposes of this Part) that is an exposure to the counterparty credit risk of a counterparty in respect of a derivative contract (other than a credit derivative contract)—means the current exposure of the derivative contract; or *(L.N. 167 of 2023)*

(d) in relation to an underlying exposure of a securitization transaction (including an exposure, collateral or asset regarded as an underlying exposure of the transaction for the purposes of this Part) that is not an underlying exposure mentioned in paragraph (b) or (c)—

(i) in the case where the risk-weight of the underlying exposure is required under this Part to be determined in accordance with Part 4—

(A) if the underlying exposure is an on-balance sheet exposure—means the principal amount of the underlying exposure determined in accordance with Part 4; and

(B) if the underlying exposure is an off-balance sheet exposure—means the credit equivalent amount of the underlying exposure determined in accordance with Part 4; and

(ii) in the case where the risk-weight of the underlying exposure is required under this Part to be determined in accordance with Part 6—means the EAD of the underlying exposure determined in accordance with Part 6; *(L.N. 175 of 2017)*

first loss tranche (首先損失份額), in relation to a securitization transaction, means the tranche (including, where the underlying exposures in the transaction are purchased receivables, the tranche in the form of a refundable purchase price discount) which will be exposed first to any credit loss associated with the underlying exposures in the transaction up to a specified or ascertainable level; *(L.N. 175 of 2017)*

gain-on-sale (出售收益), in relation to a securitization transaction, means any increase in the CET1 capital of the originating institution resulting from the sale of underlying exposures in the transaction; *(L.N. 156 of 2012)*

implicit support (隱性支持), in relation to a securitization transaction—

(a) means any direct or indirect support that an authorized institution provides (or has provided) to investors in the transaction in excess of its predetermined contractual obligations, with a view to reducing potential or actual losses that they may suffer; and

(b) includes any clean-up call the exercise of which is found to provide credit enhancement to the transaction; *(L.N. 175 of 2017)*

inferred rating (推斷評級), in relation to a securitization exposure that does not have an ECAI issue specific rating (***principal exposure***), means the credit assessment rating—

(a) attributed to the principal exposure by making reference to another securitization exposure that has an ECAI issue specific rating; and

(b) the use of which to risk-weight the principal exposure under the SEC-ERBA is allowed under section 268; *(L.N. 175 of 2017)*

investing institution (投資機構), in relation to a securitization transaction, means an authorized institution which is an investor in the transaction;

investor (投資者), in relation to a securitization transaction, means any person, other than the originator in the transaction, who assumes securitization exposures by—

(a) purchasing securitization issues;

(b) providing credit protection to other parties to the transaction; or

(c) providing liquidity facilities in respect of the transaction;

liquidity facility (流動資金融通), in relation to an authorized institution, means a contractual agreement pursuant to which the institution provides funding in respect of a securitization transaction to ensure the timeliness of cash flows to investors in the securitization issues in the transaction; *(L.N. 175 of 2017)*

long-term inferred rating (長期推斷評級), in relation to a securitization exposure of an authorized institution, means an inferred rating which is a long-term credit assessment rating attributed to the exposure by the institution;

maturity mismatch (到期期限錯配), in relation to a credit protection in the form of recognized collateral, recognized guarantee or recognized credit derivative contract afforded to an authorized institution against one or more than one exposure—

(a) if there is only one exposure covered by the credit protection—means that the residual maturity of the credit protection determined in the manner set out in section 103(3) and (4) is shorter than the residual maturity of the exposure determined in the manner set out in section 103(3); or

(b) if there is more than one exposure with different residual maturities covered by the credit protection—means that the residual maturity of the credit protection determined in the manner set out in section 103(3) and (4) is shorter than the longest residual maturity of any of the exposures determined in the manner set out in section 103(3); *(L.N. 175 of 2017)*

non-eligible securitization transaction (非合資格證券化交易)—see section 229; *(L.N. 175 of 2017)*

non-eligible synthetic securitization transaction (非合資格合成證券化交易)—see section 229; *(L.N. 175 of 2017)*

non-eligible traditional securitization transaction (非合資格傳統證券化交易)—see section 229; *(L.N. 175 of 2017)*

non-senior tranche (非高級份額)—see section 228; *(L.N. 175 of 2017)*

originating institution (發起機構), in relation to a securitization transaction, means an authorized institution which is the originator in the transaction;

originator (發起人), in relation to a securitization transaction, means a person who—

(a) directly or indirectly originates the underlying exposures in the transaction; or

(b) serves as a sponsor of an ABCP programme or a programme with similar features;

Part 4 credit risk mitigation (第4部減低信用風險措施), in relation to the calculation of the risk-weighted amount of an underlying exposure of a securitization transaction in accordance with Part 4, means—

(a) recognized netting;

(b) recognized collateral as defined by section 51(1);

(c) recognized credit derivative contract as defined by section 51(1); or

(d) recognized guarantee as defined by section 51(1); *(L.N. 175 of 2017)*

Part 6 credit risk mitigation (第6部減低信用風險措施), in relation to the calculation of the risk-weighted amount of an underlying exposure of a securitization transaction in accordance with Part 6, means—

(a) recognized netting;

(b) recognized collateral as defined by section 139(1);

(c) recognized credit derivative contract as defined by section 139(1); or

(d) recognized guarantee as defined by section 139(1); *(L.N. 175 of 2017)*

Part 7 credit risk mitigation (第7部減低信用風險措施), in relation to the calculation of the risk-weighted amount of a securitization exposure to a securitization transaction in accordance with this Part, means—

(a) recognized collateral as defined by this section;

(b) recognized credit derivative contract as defined by this section; or

(c) recognized guarantee as defined by this section; *(L.N. 175 of 2017)*

principal amount (本金額)—

(a) in relation to an on-balance sheet securitization exposure of an authorized institution—

(i) if the exposure is measured at fair value—means the value of the exposure determined in accordance with section 4A; and

(ii) if the exposure is not measured at fair value—means the book value of the exposure; or *(L.N. 175 of 2017)*

(b) in relation to an off-balance sheet securitization exposure (other than default risk exposure) of an authorized institution, means an amount which is— *(L.N. 44 of 2020)*

(i) subject to subparagraph (ii), the contracted amount of the exposure;

(ii) in the case of such an exposure which is the undrawn portion of a partially drawn facility, the amount of the undrawn commitment;

rated (獲評級), in relation to a securitization exposure, means that the exposure has—

(a) an ECAI issue specific rating issued by an ECAI nominated by the authorized institution concerned for the purposes of this Part in accordance with section 4C; or *(L.N. 175 of 2017; L.N. 167 of 2023)*

(b) if paragraph (a) does not apply, an inferred rating or an internal credit rating; *(L.N. 222 of 2018)*

recognized collateral (認可抵押品) means collateral referred to in section 243(2)(a) or (b); *(L.N. 175 of 2017)*

recognized credit derivative contract (認可信用衍生工具合約) means a contract referred to in section 243(2)(d); *(L.N. 175 of 2017)*

recognized guarantee (認可擔保) means a guarantee referred to in section 243(2)(c); *(L.N. 175 of 2017)*

refundable purchase price discount (可退款的買入價折扣), in relation to the sale of receivables by a seller to a buyer, means the portion of the discount on the purchase price that—

(a) is provided by the seller to the buyer for the purpose of providing protection to the buyer against default risk or dilution risk, or both, associated with the receivables; and

(b) may be refunded to the seller based on the performance of the receivables; *(L.N. 175 of 2017)*

re-securitization exposure (再證券化類別風險承擔)—

(a) means a securitization exposure that is an exposure to a re-securitization transaction; but

(b) does not include a securitization exposure of an authorized institution or another person resulting from retranching another securitization exposure where the institution has verified that the cash flows to and from the institution or the person could be replicated, in all circumstances and conditions, by an exposure to a securitization transaction of which the underlying exposures contain no securitization exposures; *(L.N. 175 of 2017)*

re-securitization transaction (再證券化交易) means a securitization transaction in respect of which not less than one of the underlying exposures of the transaction is a securitization exposure; *(L.N. 137 of 2011)*

revolving (循環), in relation to an underlying exposure of an authorized institution in a securitization transaction, means that the borrower's outstanding balance of the exposure is permitted to fluctuate based on the borrower's decision to borrow and repay, up to a limit established by the institution;

securitization issues (證券化票據), in relation to a securitization transaction, means the securities issued by the issuer in the transaction;

securitization transaction (證券化交易), means a transaction involving the tranching of credit risk associated with a pool of underlying exposures and in respect of which—

(a) there are not less than 2 different tranches;

(b) payments to investors or other parties to the transaction depend on the performance of the underlying exposures; and

(c) the subordination of tranches determines the distribution of losses during the life of the transaction;

senior tranche (高級份額)—see section 228; *(L.N. 175 of 2017)*

servicer cash advance facility (服務者現金墊支融通), in relation to an authorized institution which provides credit administration services in respect of the underlying exposures in a securitization transaction, means a contractual agreement pursuant to which the institution advances cash in respect of the transaction to ensure an uninterrupted flow of payments to investors in the securitization issues in the transaction; *(L.N. 175 of 2017)*

short-term inferred rating (短期推斷評級), in relation to a securitization exposure of an authorized institution, means an inferred rating which is a short-term credit assessment rating attributed to the exposure by the institution;

SPE means a special purpose entity;

special purpose entity (特定目的實體) means a company, trust or other entity—

(a) which is created for the sole purpose of acquiring and holding the underlying exposures in a traditional securitization transaction or assuming credit risk in respect of the underlying exposures in a synthetic securitization transaction, as the case may be, and engaging in activities related or incidental to the issuance of securitization issues in the transaction; and

(b) which is insulated from the effects of default, insolvency or bankruptcy of the originator in the transaction; *(L.N. 128 of 2014)*

sponsor (保薦人), in relation to an ABCP programme or a programme with similar features, means a person who establishes the programme and manages, or participates in the management of, the programme by performing one or more of the following activities—

(a) approving the sellers to participate in the programme;

(b) approving the pool of underlying exposures to be purchased under the programme;

(c) administering the programme, including arranging for the placement into the market of securities issued under the programme; or

(d) providing any credit enhancement or liquidity facility in respect of the programme;

synthetic securitization transaction (合成證券化交易) means a securitization transaction where the credit risk of a reference pool of underlying exposures is transferred, in whole or in part, through the use of credit protection afforded to the underlying exposures; *(L.N. 222 of 2018)*

traditional securitization transaction (傳統證券化交易) means a securitization transaction where—

(a) a pool of underlying exposures is sold by the originator in the transaction to an SPE; and

(b) the cash flows from the pool of underlying exposures are used to service payments to investors or other parties to the transaction;

tranche (份額) means a contractually established segment (referred to in this definition as ***relevant segment***) of the credit risk associated with a pool of underlying exposures in a securitization transaction where—

(a) a position in the relevant segment entails a risk of credit loss greater than, or less than, that of a position of the same amount in each other contractually established segment; and

(b) no account is taken of credit protection provided by third parties directly to the holders of positions in the relevant segment or in other contractually established segments;

underlying exposures (組成項目)—

(a) in relation to a securitization transaction that is not a re-securitization transaction, means one or more than one on-balance sheet or off-balance sheet non-securitization exposure in respect of which credit risk is transferred to one or more than one person by the originator in the transaction; or

(b) in relation to a re-securitization transaction—

(i) either—

(A) means one or more than one on-balance sheet or off-balance sheet securitization exposure being re-securitized through the transaction; or

(B) means one or more than one on-balance sheet or off-balance sheet securitization exposure being re-securitized through the transaction and one or more than one on-balance sheet or off-balance sheet non-securitization exposure being securitized through the transaction; and

(ii) does not include the underlying exposures in respect of the original securitization transaction that gave rise to the securitization exposure referred to in subparagraph (i)(A) or (B); *(L.N. 137 of 2011)*

unrated (無評級), in relation to a securitization exposure, means that the exposure is not a rated exposure. *(L.N. 175 of 2017)*

(L.N. 137 of 2011; L.N. 175 of 2017)

(2) For the avoidance of doubt, it is hereby declared that no reference in this Part to a securitization transaction shall be construed as excluding a reference to a securitization transaction which has more than one originator or more than one SPE.

(3) Unless otherwise expressly stated, a reference in this Part to a securitization exposure of an authorized institution (howsoever expressed) means a securitization exposure booked in the institution's banking book. *(L.N. 137 of 2011)*

227A. Meaning of *ECAI issue specific rating*

(1) An ECAI issue specific rating, in relation to a securitization transaction, means a short-term credit assessment rating or long-term credit assessment rating that—

(a) is assigned by a Type A ECAI to— *(L.N. 167 of 2023)*

(i) a specific securitization exposure to the transaction;

(ii) a specific class of securitization exposures to the transaction; or

(iii) the transaction if it is a securities issuing programme (including an ABCP programme) that issues securitization issues; and

(b) is for the time being neither withdrawn nor suspended by that ECAI.

(2) If—

(a) an ECAI issue specific rating is assigned by a Type A ECAI to an ABCP programme or any other type of securities issuing programme that issues securitization issues (***programme rating***); and *(L.N. 167 of 2023)*

(b) according to the rating definitions, rating criteria or other similar documentation of the ECAI, the programme rating only refers to the creditworthiness of the programme with respect to a specific class of securitization issues issued under the programme,

the programme rating may be treated under these Rules as if it were an ECAI issue specific rating assigned to that specific class of securitization issues.

(L.N. 222 of 2018)

228. Meaning of *senior tranche*, etc.

(1) For the purposes of this Part, a senior tranche is a tranche in, or a securitization exposure to, a securitization transaction that is effectively backed or secured by a first legal claim on the entire amount of the underlying exposures of the transaction.

(2) However, if a tranche or securitization exposure that is a senior tranche under subsection (1) (***original senior tranche***) is retranched or partially hedged, the new senior part formed as a result, instead of the original senior tranche, is the senior tranche.

(3) Fees or other similar payments due under a securitization transaction that could be regarded as falling within subsection (1) or (2) in a technical sense is not a senior tranche.

(4) A reference in this Part to a non-senior tranche is a reference to a tranche or securitization exposure that is not a senior tranche.

(5) A reference in this Part to a securitization exposure in a senior or non-senior tranche is not construed as excluding a securitization exposure that is the only securitization exposure in a senior or non-senior tranche. Therefore the securitization exposure itself is also regarded as a senior or non-senior tranche.

(L.N. 175 of 2017)

229. Meaning of *eligible securitization transactions*, etc.

(1) For the purposes of this Part—

(a) a traditional securitization transaction is an eligible traditional securitization transaction if all of the following criteria are met—

(i) all the requirements set out in Schedule 9 that are applicable to, or in relation to, the transaction or its originating institution are satisfied; *(L.N. 222 of 2018)*

(ii) the transaction is not one specified in subsection (2); and

(b) a synthetic securitization transaction is an eligible synthetic securitization transaction if all of the following criteria are met—

(i) all the requirements set out in Schedule 10 that are applicable to, or in relation to, the transaction or its originating institution are satisfied;

(ii) the transaction is not one specified in subsection (2).

(2) The transaction is a transaction that—

(a) at least one underlying exposure of which is revolving in nature (***revolving underlying exposure***); and

(b) contains an early amortization provision, or a provision of similar nature, that, if triggered, would—

(i) subordinate the institution's senior or equally ranked interest in the revolving underlying exposures to the interests of other parties to the transaction;

(ii) subordinate the institution's subordinated interest to an even greater degree relative to the interests of other parties to the transaction; or

(iii) in other ways increase the institution's exposure to losses associated with the revolving underlying exposures.

(3) For the purposes of this Part—

(a) a reference to a non-eligible traditional securitization transaction is a reference to a traditional securitization transaction that is not an eligible traditional securitization transaction;

(b) a reference to a non-eligible synthetic securitization transaction is a reference to a synthetic securitization transaction that is not an eligible synthetic securitization transaction;

(c) a reference to an eligible securitization transaction is a reference to an eligible traditional securitization transaction or an eligible synthetic securitization transaction; and

(d) a reference to a non-eligible securitization transaction is a reference to a securitization transaction that is not an eligible securitization transaction.

(L.N. 175 of 2017)

Division 2—Recognition of Credit Risk Transfer under Securitization Transaction

(Division 2 replaced L.N. 175 of 2017)

230. Treatment of underlying exposures of eligible securitization transactions: general

(1) Subject to subsections (3), (4) and (5), an originating institution of an eligible traditional securitization transaction may exclude the underlying exposures of the transaction from the calculation of the risk-weighted amount for credit risk. *(L.N. 167 of 2023)*

(2) Subject to subsections (2A), (3), (4) and (5), an originating institution of an eligible synthetic securitization transaction may— *(L.N. 44 of 2020)*

(a) calculate the risk-weighted amount of the underlying exposures of the transaction in accordance with one or more of Parts 4, 5 and 6 and this Part, as the case requires, as if the underlying exposures were not securitized; and

(b) subject to section 231, in calculating the risk-weighted amount under paragraph (a), take into account the effect of the credit risk mitigation used for transferring the credit risk of the underlying exposures to the other parties to the transaction in accordance with— *(L.N. 44 of 2020)*

(i) if the credit risk mitigation is in the form of tranched credit protection and the underlying exposures are non-securitization exposures—this Part as if the institution's credit exposure to the underlying exposures were a securitization exposure;

(ii) if the credit risk mitigation is not in the form of tranched credit protection and the underlying exposures are non-securitization exposures—

(A) Divisions 5, 6, 7, 9 and 10 of Part 4 (for any part of the calculation mentioned in paragraph (a) (which may be the whole calculation) that is made in accordance with Part 4);

(B) Divisions 5, 7 and 8 of Part 5 (if the calculation mentioned in paragraph (a) is made in accordance with Part 5); or

(C) Division 10 of Part 6 (for any part of the calculation mentioned in paragraph (a) (which may be the whole calculation) that is made in accordance with Part 6); or

(iii) if the underlying exposures are securitization exposures—Division 5. *(L.N. 167 of 2023)*

(2A) If the credit risk mitigation used in an eligible synthetic securitization transaction for transferring the credit risk of the underlying exposures to other parties to the transaction is a recognized guarantee or a recognized credit derivative contract provided by an SPE in respect of which all the requirements set out in section 2(a) of Schedule 10 are satisfied—

(a) the treatment set out in subsection (2) is not applicable to the underlying exposures of the transaction; and

(b) subject to subsections (2B), (3), (4) and (5) and section 231, the originating institution may only—

(i) if the credit risk mitigation is not in the form of tranched credit protection—calculate the risk-weighted amount of the underlying exposures of the transaction in accordance with subsection (2)(a) and take into account the effect of the credit risk mitigation in the calculation in accordance with Divisions 9 and 10 of Part 4 regardless of whether the calculation is made in accordance with Part 4;

(ii) if the credit risk mitigation is in the form of tranched credit protection—

(A) decompose the underlying exposures of the transaction into a protected sub-tranche and an unprotected sub-tranche;

(B) calculate the risk-weighted amount of the protected sub-tranche in accordance with this Part as if it were a securitization exposure and take into account the effect of the credit risk mitigation in the calculation in accordance with Divisions 9 and 10 of Part 4 instead of Division 5 of this Part; and

(C) calculate the risk-weighted amount of the unprotected sub-tranche by using the SEC-IRBA, SEC-ERBA, SEC-SA or SEC-FBA, as the case requires, and in accordance with sections 240, 241 and 249, as if the unprotected sub-tranche were a securitization exposure. *(L.N. 44 of 2020)*

(2B) For the purposes of subsection (2A)(b)(i) and (ii)(B)—

(a) the risk-weight applicable to the credit protection covered portion (within the meaning of section 51(1)) or the protected sub-tranche, as the case requires, is the weighted-average risk-weight of the SPE's assets determined under Part 4; and

(b) the amount of the credit protection covered portion or the protected sub-tranche, as the case requires, must not be larger than the current market value of the SPE's assets adjusted downwards by standard supervisory haircuts for volatility of the value of the assets and any currency mismatch subject to adjustment set out in section 92. *(L.N. 44 of 2020)*

(3) The originating institution of the transaction must give notice to the Monetary Authority of its intention to apply the treatment under subsection (1), (2) or (2A) to the underlying exposures of the transaction for the purpose of calculating its capital adequacy ratio when— *(L.N. 44 of 2020)*

(a) the institution applies the treatment for the first time; or

(b) if the transaction ceases to become an eligible securitization transaction after the institution has applied the treatment—the institution reapplies the treatment.

(4) The notice must—

(a) be given at least one month before the treatment is applied; and

(b) be accompanied by—

(i) the information on the particulars of the credit risk to the underlying exposures retained by the institution; and

(ii) a written confirmation that the transaction is an eligible securitization transaction, provided by a person who has sufficient seniority and authority and is independent of the persons (whether inside or outside the institution) responsible for originating the transaction or the underlying exposures.

(5) However, the Monetary Authority may, by notice in writing, require an originating institution not to apply, or to discontinue the application of, the treatment under subsection (1), (2) or (2A) to the underlying exposures of the transaction if the Monetary Authority is of the view that— *(L.N. 44 of 2020)*

(a) the confirmation under subsection (4)(b)(ii) is not based on an adequate assessment of the degree of credit risk transfer against the criteria set out in section 229(1)(a) or (b); or

(b) the transaction contains features that render the criteria inadequate to determine whether significant credit risk transfer is achieved.

(5A) The originating institution of a securitization transaction must comply with the requirement of a notice given to it under subsection (5). *(L.N. 222 of 2018)*

(6) To avoid doubt, an originating institution that applies the treatment under subsection (1), (2) or (2A) to the underlying exposures of a securitization transaction must— *(L.N. 44 of 2020)*

(a) calculate in accordance with this Part the risk-weighted amounts of the securitization exposures to the transaction retained, held or purchased by the institution; and

(b) include the amounts in the calculation of the institution's capital adequacy ratio.

230A. *(Repealed L.N. 175 of 2017)*

231. Treatment of underlying exposures of eligible synthetic

securitization transactions in case of maturity mismatch or call option

(1) This section applies if—

(a) an originating institution of an eligible synthetic securitization transaction intends to take into account, under section 230(2)(b) or (2A)(b), the effect of the credit risk mitigation used for transferring the credit risk of the underlying exposures of the transaction;

(b) where the credit risk mitigation is in the form of tranched credit protection—the risk-weight assigned to the unprotected sub-tranche concerned under this Part is below 1,250%; and

(c) either—

(i) there is a maturity mismatch between the underlying exposures of the transaction and the credit protection through which the credit risk is transferred under the transaction; or

(ii) the transaction incorporates a call option (other than a clean-up call) which is capable, when exercised, of terminating the transaction and the credit protection on a specified date.

(2) The institution may take into account the effect of the credit protection in its calculation of the risk-weighted amount of the underlying exposures if—

(a) the credit protection has an original maturity of not less than 1 year and a residual maturity of more than 3 months; and

(b) the institution takes into account the effect of the maturity mismatch or the call option by adjusting the value of the credit protection by using Formula 12, with the residual maturity of the underlying exposures determined as the longest residual maturity of any of the underlying exposures of the transaction.

(2A) In applying subsection (2)(b) for the purposes of section 230(2A)(b), P in Formula 12 must be construed to mean the amount of the credit protection covered portion or the protected sub-tranche, as the case requires, referred to in section 230(2B)(b). *(L.N. 44 of 2020)*

(3) To avoid doubt, for credit risk mitigation referred to in section 230(2)(b)(ii) or (2A)(b), the institution must apply the treatment under subsection (2) instead of the treatments for maturity mismatch under Parts 4, 5 and 6.

(L.N. 44 of 2020)

232. Treatment of expected losses and provisions in respect of underlying exposures

(1) This section applies to an authorized institution if—

(a) it is the originating institution of an eligible securitization transaction;

(b) it applies the treatments under section 230(1), (2) or (2A) to the underlying exposures of the transaction; *(L.N. 44 of 2020)*

(c) the underlying exposures are still held on the balance sheet of the institution; and

(d) the institution would use the IRB approach to calculate the credit risk for the underlying exposures if they were not securitized.

(2) The institution—

(a) must not, in determining the institution's total eligible provisions for the purposes of sections 42(3)(c) and 43(1)(i), include any specific provisions, partial write-offs, regulatory reserve for general banking risks and collective provisions made for, or any non-refundable purchase price discounts on, the underlying exposures; and

(b) must not, in determining the institution's total EL amount for the purposes of those sections, include the EL amount estimated for the underlying exposures.

232A. *(Repealed L.N. 175 of 2017)*

233. Treatment of underlying exposures of non-eligible securitization transactions

(1) An originating institution of a non-eligible traditional securitization transaction—

(a) must calculate the risk-weighted amount of the underlying exposures of the transaction in accordance with one or more of Parts 4, 5 and 6 and this Part, as the case requires, as if the underlying exposures were not securitized; and

(b) must not, in its capital base determined in accordance with Part 3, include any gain-on-sale or any other increase in its CET1 capital arising from the transaction.

(2) An originating institution of a non-eligible synthetic securitization transaction—

(a) must calculate the risk-weighted amount of the underlying exposures of the transaction in accordance with one or more of Parts 4, 5 and 6 and this Part, as the case requires, as if the credit risk of the underlying exposures were not transferred to the other parties to the transaction; and

(b) must not, in the calculation under paragraph (a), take into account the effect of the credit risk mitigation used for transferring the credit risk of the underlying exposures to the other parties to the transaction.

(3) An originating institution of a non-eligible securitization transaction that has—

(a) calculated the risk-weighted amount of the underlying exposures of the transaction in accordance with subsection (1) or (2); and

(b) included the amount in the calculation of its capital adequacy ratio,

is not required to calculate risk-weighted amounts for any securitization exposures it may have to the transaction.

(L.N. 167 of 2023)

234. Measures for authorized institution providing implicit support

(1) If an authorized institution provides implicit support to a securitization transaction, it—

(a) must, in calculating its capital adequacy ratio, include the risk-weighted amounts calculated for all the underlying exposures of the transaction under these Rules as if the underlying exposures were not securitized;

(b) must not, in its capital base determined in accordance with Part 3, include any gain-on-sale or any other increase in its CET1 capital arising from the transaction;

(c) must notify the Monetary Authority, within 1 month from the date on which the support is provided, of the particulars of the following matters—

(i) the support provided; and

(ii) the impact of the support on the institution's capital adequacy ratio; and

(d) must disclose publicly the particulars mentioned in paragraph (c)(i) and (ii).

(2) If an authorized institution provides or has provided implicit support to more than one securitization transaction (whether at the same time or not), the Monetary Authority may, by notice in writing given to the institution—

(a) require the institution not to apply the treatment under section 230(1), (2) and (2A) to other securitization transactions for the period, or until the occurrence of the event, specified in the notice; or *(L.N. 44 of 2020)*

(b) advise the institution that the Monetary Authority is considering exercising the power under section 97F of the Ordinance to vary any capital requirement rule applicable to the institution, including by increasing all or any of its CET1 capital ratio, Tier 1 capital ratio and Total capital ratio.

(3) The originating institution of a securitization transaction must comply with the requirement of a notice given to it under subsection (2)(a).

(4) To avoid doubt, subsection (2)(b) does not operate to limit the circumstances in respect of which the Monetary Authority may exercise the power under section 97F of the Ordinance in relation to an authorized institution to which that subsection applies.

Division 3—General Requirements for Risk-weighting Securitization Exposures

(Division 3 replaced L.N. 175 of 2017)

235. Determination of exposure amount of securitization exposure

(1) An authorized institution must determine the exposure amount of an on-balance sheet securitization exposure as—

(a) if the exposure arises from a funded credit protection provided by the institution—the amount determined under subsection (4) or (5)(b); or

(b) in any other case—the principal amount of the exposure (net of purchase price discounts if applicable).

(2) An authorized institution must determine the exposure amount of an off-balance sheet securitization exposure as—

(a) if the exposure is a default risk exposure—the amount calculated by using the same approach or method the institution is required under section 10A to use to calculate its default risk exposure;

(b) if the exposure arises from an unfunded credit protection provided by the institution—the amount determined under subsection (4) or (5)(b); or

(c) in any other case, the amount calculated by multiplying the principal amount of the exposure by—

(i) if the exposure arises from the undrawn portion of a qualified servicer cash advance facility provided by the institution—a factor that is the same as the CCF under the STC approach applicable to a commitment (within the meaning of section 2 of Schedule 6) that may be cancelled at any time unconditionally by the institution; or *(L.N. 167 of 2023)*

(ii) in any other case—a factor of 100%.

(3) For the purposes of subsection (2)(c), a servicer cash advance facility is a qualified servicer cash advance facility if—

(a) the facility documentation clearly identifies and limits the circumstances under which the facility may be drawn;

(b) the authorized institution providing the facility is entitled to full reimbursement of cash advanced under the facility, and the entitlement—

(i) ranks senior to payment or repayment of other claims on cash flows from the underlying exposures of the securitization transaction concerned; and *(L.N. 222 of 2018)*

(ii) is not subject to any deferral or waiver by the institution;

(c) drawings under the facility are limited to the amount assessed by the institution as likely to be repaid fully from the cash flows generated by the underlying exposures or through realization of the underlying exposures or any credit enhancement available in the transaction;

(d) the facility is not able to be drawn so as to provide credit support to cover losses already incurred in respect of the pool of underlying exposures prior to the drawing;

(e) there are no regular or continuous drawings under the facility to indicate that the facility is either—

(i) used to provide permanent or regular funding to investors in the securitization issues; or

(ii) structured such that drawdown is certain; and

(f) the facility is unconditionally cancellable by the institution without prior notice to the person to whom the facility is provided.

(4) If an authorized institution provides full or proportional credit protection to a securitization exposure, it must determine the exposure amount of its securitization exposure arising from the credit protection as the amount of the portion of the

securitization exposure on which it has provided the credit protection.

(5) If an authorized institution provides tranched credit protection to a securitization exposure or non-securitization exposure, it must—

(a) decompose the exposure into a protected sub-tranche and an unprotected sub-tranche; and

(b) determine the exposure amount of its securitization exposure arising from the credit protection as the amount of the protected sub-tranche.

236. Calculation of risk-weighted amount of securitization exposure

(1) Subject to subsections (2) and (3) and Division 5, an authorized institution must calculate the risk-weighted amount of a securitization exposure by multiplying the exposure amount of the exposure determined in accordance with section 235 by the risk-weight of the exposure determined in accordance with Division 4, 7, 8, 9 or 10.

(2) For the purposes of subsection (1), if the institution—

(a) provides full or proportional credit protection to a securitization exposure, the institution must calculate the risk-weighted amount of the credit protection as if it directly held the portion of the exposure on which it has provided the credit protection;

(b) provides tranched credit protection to a securitization exposure, the institution must calculate the risk-weighted amount of the credit protection as if it had direct exposure to the sub-tranche of the securitization exposure on which it has provided the credit protection;

(c) provides tranched credit protection to, or obtains tranched credit protection for, a non-securitization exposure, the institution must calculate the risk-weighted amounts of the protected sub-tranche and the unprotected sub-tranche as if they were tranches of a securitization transaction of which the underlying exposure is the non-securitization exposure.

(3) For the purposes of subsection (1), the exposure amount of a securitization exposure determined in accordance with section 235—

(a) may be reduced by any specific provisions or write-offs made for the securitization exposure; and

(b) if the securitization exposure is subject to a risk-weight of 1,250% and the institution is the originating institution of the securitization transaction concerned, may be further reduced by—

(i) the amount of any specific provisions made by the institution for the underlying exposures of the transaction; and

(ii) if the underlying exposures of the transaction consist of purchased receivables—the amount of any non-refundable purchase price discounts on the receivables provided to the institution by the seller.

(4) To avoid doubt—

(a) collective provisions made in respect of the underlying exposures of a securitization transaction must not be included in any calculation under this Part; and

(b) if only the drawn portion of a revolving facility has been securitized—

(i) only that portion is subject to the requirements under this Part; and

(ii) the risk-weighted amount of the undrawn portion of the facility must be calculated in accordance with Part 4, 5 or 6, as the case requires.

236A. *(Repealed L.N. 175 of 2017)*

237. Treatment of refundable purchase price discount provided, and first-loss protection obtained, by authorized institution for purchased receivables

(1) If an authorized institution has, as a seller of receivables, provided a refundable purchase price discount to the buyer of the receivables, the institution must calculate the risk-weighted amount of the discount in accordance with this Part as if it were a first-loss tranche of a securitization transaction.

(2) If an authorized institution is a buyer of receivables and the seller of the receivables has provided a refundable purchase price discount to the institution in respect of the receivables, the institution may—

(a) treat the discount as a first-loss protection; and

(b) calculate the risk-weighted amount of its credit exposure to the receivables in accordance with this Part as if the credit exposure were a securitization exposure.

(3) If any recognized collateral or recognized guarantee obtained by an authorized institution for its purchased receivables provides first-loss protection to the default risk or dilution risk, or both, in respect of the receivables, the institution may take into account the first-loss protection in the calculation of the risk-weighted amount of its credit exposure to the receivables in accordance with this Part as if the credit exposure were a securitization exposure.

238. Treatment of derivative contract for mitigating market risk in securitization transaction

The risk-weight of a securitization exposure to a securitization transaction arising from a derivative contract used for mitigating market risk in the transaction must be inferred from—

(a) a securitization exposure (***reference exposure***) to the transaction that ranks equally in respect of payment or repayment with the derivative contract; or

(b) if such a reference exposure does not exist—the next tranche in the transaction that is subordinated to the derivative contract.

239. Treatment of overlapping securitization exposures

(1) This section applies if—

(a) an authorized institution has more than one securitization exposure to the same securitization transaction; and

(b) the institution is able to verify that fulfilling its obligations with respect to a securitization exposure (***exposure A***) will preclude all or part of the institution's losses on another securitization exposure (***exposure B***) under all circumstances.

(2) The institution may, after determining the amount with which exposure A overlaps exposure B (***overlapping portion***), apply the treatments set out in subsection (3) instead of calculating the risk-weighted amount of each of the securitization exposures based on the full exposure amount of each of the securitization exposures.

(3) The treatments are—

(a) if both exposures are booked in the institution's banking book—

(i) calculating the risk-weighted amount of the overlapping portion in accordance with this Part by attributing it to exposure A; and

(ii) calculating the risk-weighted amount of the portion of each of the exposures that is not the overlapping portion in accordance with this Part; and

(b) if one of the exposures is booked in the institution's banking book (***banking book exposure***) and the other is booked in the trading book (***trading book exposure***)—

(i) if the institution is able to determine whether attributing the overlapping portion to the banking book exposure or to the trading book exposure will result in a higher regulatory capital for the overlapping portion—

(A) calculating the regulatory capital for the overlapping portion by attributing it to the exposure that will result in a higher regulatory capital for the overlapping portion; and

(B) calculating the regulatory capital for the portion of each of the exposures that is not the overlapping portion in accordance with this Part or Part 8, as the case requires; or

(ii) if the institution is unable to so determine—calculating the regulatory capital for the exposures in accordance with both this Part and Part 8 as if there were no overlapping portion.

(4) To avoid doubt, subsection (3)(b) does not operate to exclude the following amounts from the calculation of market risk capital charge under Part 8— *(L.N. 167 of 2023)*

(a) the regulatory capital calculated under subsection (3)(b)(i)(A) for the overlapping portion that has been attributed to the trading book exposure of the institution; and

(b) the regulatory capital calculated under subsection (3)(b)(i)(B) for that portion of the trading book exposure of the institution that is not the overlapping portion.

(5) In this section—

regulatory capital (監管資本), in relation to a securitization exposure booked in the trading book or an overlapping portion that has been attributed to the exposure, means—

(a) the SBM capital charge, RRAO and SA-DRC in relation to securitization exposures calculated by using the STM approach; or

(b) the market risk capital charge for specific risk in relation to securitization exposures calculated by using the SSTM approach. *(L.N. 167 of 2023)*

Division 4—Floors and Caps on Capital Requirements for Securitization Exposures

(Division 4 replaced L.N. 175 of 2017)

240. Floors on risk-weights determined by using SEC-IRBA, SEC-ERBA or SEC-SA

(1) Subject to subsections (3) and (4), if the risk-weight of a securitization exposure (other than a re-securitization exposure) determined by using the SEC-IRBA, SEC-ERBA or SEC-SA, as the case requires, is lower than 15%, a risk-weight of 15% must be assigned to the exposure.

(2) Subject to subsection (4), if the risk-weight of a re-securitization exposure determined by using the SEC-SA is lower than 100%, a risk-weight of 100% must be assigned to the exposure.

(3) The risk-weight determined for a rated securitization exposure by using the SEC-ERBA (after applying subsection (1) if

applicable) must not be lower than the risk-weight determined by using the SEC-ERBA (after applying that subsection if applicable) for a senior tranche in the same securitization transaction with the same rating and maturity.

(4) If—

(a) the risk-weight of an unrated securitization exposure in a non-senior tranche of a securitization transaction is determined by using the SEC-SA; and

(b) the next more senior tranche or securitization exposure in the same securitization transaction is rated,

the risk-weight determined by using the SEC-SA (after applying subsection (1) if applicable) for the unrated securitization exposure is subject to a floor which is equal to the risk-weight determined by using the SEC-ERBA (after applying that subsection if applicable) for the rated tranche or securitization exposure.

241. Caps on risk-weights for exposures in senior tranches determined by using SEC-IRBA, SEC-ERBA or SEC-SA

(1) An authorized institution may apply the treatment set out in subsection (2) to a securitization exposure in a senior tranche (***senior exposure***) of a securitization transaction only if—

(a) it has the information on the composition of the underlying exposures of the transaction at all times so that it is able to determine the risk-weights of the underlying exposures in accordance with these Rules; and

(b) the senior exposure is not a re-securitization exposure.

(2) If the risk-weight of the senior exposure determined by using the SEC-IRBA, SEC-ERBA or SEC-SA (after applying section 240 if applicable) is higher than the weighted average risk-weight of the underlying exposures (***risk-weight cap***)

calculated in accordance with subsection (3), (4), (5) or (6) (using the exposure amounts of the underlying exposures for weighting the risk-weights), the institution may allocate to the senior exposure a risk-weight equal to the risk-weight cap (regardless of whether the risk-weight cap is lower than 15% or not). *(L.N. 167 of 2023)*

(3) If the senior exposure is backed by an IRB pool, the risk-weight cap is calculated by using the following risk-weights—

(a) the risk-weights of the underlying exposures in the IRB pool determined under Part 6; and *(L.N. 167 of 2023)*

(b) the risk-weight applicable to the expected loss (within the meaning of section 139(1)) of the underlying exposures in the IRB pool derived by multiplying the expected loss by 12.5.

(4) If the senior exposure is backed by an SA pool, the risk-weight cap is calculated by using the risk-weights of the underlying exposures in the SA pool determined under Part 4.

(5) If the senior exposure is backed by a mixed pool and the institution is required under section 15 to use the SEC-IRBA to determine the risk-weight of the senior exposure, the risk-weight cap is calculated by using the following risk-weights—

(a) for the portion of the underlying exposures in the mixed pool for which the institution is able to calculate a K_{IRB} in accordance with section 254(1)—the risk-weights of the underlying exposures calculated under subsection (3); and

(b) for the portion of the underlying exposures in the mixed pool for which the institution is unable to calculate a K_{IRB} in accordance with section 254(1)—the risk-weights of the underlying exposures determined under Part 4.

(6) If—

(a) the senior exposure is backed by a mixed pool; and

(b) the institution is required under section 15 to use the SEC-ERBA or SEC-SA to determine the risk-weight of the senior exposure,

the risk-weight cap is calculated by using the risk-weights of the underlying exposures (including those that would be subject to the IRB approach if they were not securitized or if they were held by the institution) in the mixed pool determined under Part 4.

242. Maximum capital charge for all securitization exposures to securitization transaction

(1) The maximum capital charge calculated in accordance with this section does not apply to—

(a) securitization exposures held by an investing institution; and

(b) re-securitization exposures.

(2) If the total capital charge calculated by an originating institution of a securitization transaction under the SEC-IRBA, SEC-ERBA or SEC-SA (after applying sections 240 and 241, if applicable) for all its securitization exposures to the transaction is higher than the maximum capital charge calculated for the transaction under subsection (3), the institution may use the maximum capital charge so calculated as the total capital charge for the exposures in the calculation of its capital adequacy ratio.

(3) The maximum capital charge for a securitization transaction to which an originating institution has securitization exposures is calculated as the product of—

(a) the capital charge factor (K_p) for the pool of underlying exposures of the transaction determined under subsection (4), (5) or (6);

(b) the largest proportion of interest that the institution holds in one or more than one tranche of the transaction (P) determined under subsection (7); and

(c) the total exposure amount of the underlying exposures.

(4) If the securitization exposures are backed by an IRB pool and the risk-weights for the exposures are determined by using the SEC-IRBA, K_p is the K_{IRB} calculated for the pool in accordance with section 254(1).

(5) If the securitization exposures are backed by an SA pool and the risk-weights for the exposures are determined by using the SEC-ERBA or SEC-SA, K_p is the K_{SA} calculated for the pool in accordance with section 275.

(6) If the securitization exposures are backed by a mixed pool and the risk-weights for the exposures are determined by using the SEC-IRBA, SEC-ERBA or SEC-SA, K_p is the weighted average of the following 2 ratios (using the exposure amounts of the underlying exposures as the weights)— *(E.R. 1 of 2018)*

(a) the K_{IRB} calculated in accordance with section 254(1) for the portion of the pool for which the institution is able to calculate the K_{IRB}; and

(b) the K_{SA} calculated in accordance with section 275 for the portion of the pool for which the institution is unable to calculate the K_{IRB} in accordance with section 254(1).

(7) An originating institution must determine P (expressed as a percentage) as follows—

(a) if the institution has at least one securitization exposure in a single tranche of a securitization transaction—P is equal to the total nominal amount of its securitization exposures in the tranche divided by the nominal amount of the tranche; or

(b) if the institution has securitization exposures in different tranches of a securitization transaction—the institution must calculate a P for each tranche in accordance with paragraph (a) and take the one with the largest value as the P for the purpose of calculating the maximum capital charge under subsection (3).

(8) Despite the application of the maximum capital charge calculated under this section by an originating institution of a securitization transaction to its securitization exposures to the transaction, the entire amount of any gain-on-sale and other increase in the CET1 capital, and the entire amount of any credit-enhancing interest-only strips, arising from the transaction are subject to the deduction required under section 43.

Division 5—Use of Credit Risk Mitigation for Securitization Exposures

(Division 5 replaced L.N. 175 of 2017)

243. Credit risk mitigation recognized for purpose of calculating the risk-weighted amounts of securitization exposures

(1) An authorized institution may only take into account the credit risk mitigations specified in subsection (2) in calculating the risk-weighted amount of its securitization exposure.

(2) The credit risk mitigations are—

(a) if the risk-weight of the securitization exposure is determined by using the SEC-IRBA—collateral, including collateral pledged by SPEs, that is recognized financial collateral or recognized IRB collateral as defined by section 139(1);

(b) if the risk-weight of the securitization exposure is determined by using the SEC-ERBA, SEC-SA or SEC-FBA—collateral, including collateral pledged by SPEs, that is recognized collateral as defined by section 51(1);

(c) a guarantee provided by a person (other than an SPE) falling within section 99A(2)(a)(i), (ii), (iii), (iv), (v), (vi) or (vii), or an entity (other than an SPE) specified in subsection (3), that meets the requirements set out in section 98(b), (c), (ca), (d), (e), (f), (g), (h), (i) and (j); and *(L.N. 167 of 2023)*

(d) a credit derivative contract provided by a person (other than an SPE) falling within section 99A(2)(a)(i), (ii), (iii), (iv), (v), (vi) or (vii), or an entity (other than an SPE) specified in subsection (3), that meets the requirements set out in section 99(1)(a) and (c) to (r) and, if applicable, section 99(2), (3) or (4). *(L.N. 167 of 2023)*

(3) The entity is one that does not fall within any of section 99A(2)(a)(i), (ii), (iii), (iv), (v), (vi) and (vii) and—

(a) if it is not a corporate incorporated in the home jurisdiction of any of the Type B ECAIs—

(i) has an ECAI issuer rating that, if mapped to a credit quality grade in accordance with the LT ECAI rating mapping table for Type A ECAIs, would result in the entity being assigned a credit quality grade of 1, 2, 3 or 4; and

(ii) had an ECAI issuer rating at the time the credit protection was given that, if mapped to a credit quality grade in accordance with the LT ECAI rating mapping table for Type A ECAIs, would result in the entity being assigned a credit quality grade of 1, 2 or 3; or

(b) if it is a corporate incorporated in the home jurisdiction of a Type B ECAI (***relevant Type B ECAI***)—

(i) has an ECAI issuer rating assigned by a Type A ECAI or the relevant Type B ECAI that, if mapped to a credit quality grade in accordance with the LT ECAI rating mapping table for Type A ECAIs or the LT ECAI rating mapping table for Type B ECAIs, as the case requires, would result in the corporate being assigned a credit quality grade of 1, 2, 3 or 4; and

(ii) had an ECAI issuer rating assigned by a Type A ECAI or the relevant Type B ECAI at the time the credit protection was given that, if mapped to a credit quality grade in accordance with the LT ECAI rating mapping table for Type A ECAIs or the LT ECAI rating mapping table for Type B ECAIs, as the case requires, would result in the corporate being assigned a credit quality grade of 1, 2 or 3. *(L.N. 167 of 2023)*

244. Treatment of Part 7 credit risk mitigation—full or proportional credit protection

(1) This section applies if—

(a) an authorized institution obtains a Part 7 credit risk mitigation for its securitization exposure; and

(b) the credit risk mitigation provides full or proportional credit protection against the exposure.

(2) The institution may take into account the credit risk mitigation effect of the credit protection in calculating the risk-weighted

amount of the exposure only if the effect is taken into account in accordance with subsection (3), (4), (5) or (6).

(3) Subject to subsection (7), if—

(a) the institution uses the IRB approach to calculate its credit risk for all or part of its non-securitization exposures; and *(L.N. 167 of 2023)*

(b) the risk-weight of the securitization exposure is determined by using the SEC-IRBA,

the credit risk mitigation effect of the credit protection must be taken into account by applying the treatments under the foundation IRB approach set out in Division 10 of Part 6.

(4) If—

(a) the institution uses the IRB approach to calculate its credit risk for all or part of its non-securitization exposures; and *(L.N. 167 of 2023)*

(b) the risk-weight of the securitization exposure is determined by using the SEC-ERBA, SEC-SA or SEC-FBA,

the credit risk mitigation effect of the credit protection must be taken into account by applying the treatments set out in Divisions 7, 9 and 10 of Part 4.

(5) If the institution uses the STC approach to calculate its credit risk for all of its non-securitization exposures, the credit risk mitigation effect of the credit protection must be taken into account by using the same approaches that it uses for recognized credit risk mitigation obtained for non-securitization exposures under Part 4. *(L.N. 167 of 2023)*

(6) If the institution uses the BSC approach to calculate its credit risk for non-securitization exposures, the credit risk mitigation effect of the credit protection must be taken into account—

(a) for recognized collateral—by using the simple approach (within the meaning of section 51(1));

(b) in any other case—in accordance with Part 4.

(7) In applying the treatment under subsection (3) in respect of any recognized collateral, the institution must, instead of taking into account the credit risk mitigating effect of the collateral through the determination of the LGD of the securitization exposure, take into account the effect by applying one of the 2 formulas set out in section 160(3) for calculating the unsecured portion of an exposure (E_U), as applicable, with the following modifications—

(a) the component E of that formula is to be taken to be a reference to the exposure amount of the securitization exposure determined in accordance with section 235 (after the adjustments set out in section 236(3) if applicable); and

(b) the E_U calculated for the securitization exposure under that formula is to be taken as the exposure amount of the securitization exposure for the purposes of section 236(1). *(L.N. 167 of 2023)*

245. Treatment of Part 7 credit risk mitigation—tranched credit protection

(1) This section applies if—

(a) an authorized institution obtains a Part 7 credit risk mitigation for its securitization exposure; and

(b) the credit risk mitigation provides tranched credit protection against the exposure.

(2) The institution must—

(a) decompose the exposure into a protected sub-tranche and an unprotected sub-tranche; and

(b) determine the risk-weighted amount of each sub-tranche in accordance with subsection (3).

(3) The institution must—

(a) determine the risk-weighted amount of the protected sub-tranche by taking into account the credit risk mitigation effect of the tranched credit protection in accordance with section 244; and

(b) determine the risk-weighted amount of the unprotected sub-tranche by using the SEC-IRBA, SEC-ERBA, SEC-SA or SEC-FBA, as the case requires, and in accordance with sections 240, 241 and 249.

246. Treatment of maturity mismatch between securitization exposures and credit protection

For the purposes of sections 244 and 245, if there is a maturity mismatch between the credit protection and the securitization exposure, section 231(2) applies to the exposure and the credit protection as it applies to—

(a) the underlying exposures of a synthetic securitization transaction; and

(b) the credit protection through which the credit risk of the underlying exposures is transferred under the transaction.

Division 6—Determination of Certain Inputs Used in Risk-weighting Approach

(Division 6 replaced L.N. 175 of 2017)

247. Value of attachment point and value of detachment point of tranche in securitization transaction

(1) Subject to subsection (3), the value of the attachment point

(***AP***) of a tranche in a securitization transaction (***relevant tranche***) is the greater of the following—

(a) the ratio (expressed in decimals) of the amount specified in subparagraph (i) to the amount specified in subparagraph (ii)—

(i) the total outstanding amount of all the underlying exposures of the transaction minus the total outstanding amount of the relevant tranche and all other tranches in the transaction that are senior to, or rank equally with, the relevant tranche;

(ii) the total outstanding amount of all the underlying exposures of the transaction;

(b) zero.

(2) Subject to subsection (3), the value of the detachment point (***DP***) of a relevant tranche is the greater of the following—

(a) the ratio (expressed in decimals) of the amount specified in subparagraph (i) to the amount specified in subparagraph (ii)—

(i) the total outstanding amount of all the underlying exposures of the transaction minus the total outstanding amount of all tranches in the transaction that are senior to the relevant tranche;

(ii) the total outstanding amount of all the underlying exposures of the transaction;

(b) zero.

(3) In determining the AP or DP of a tranche in a securitization transaction—

(a) over-collateralization and the loss-absorbing part of funded reserve accounts that provide credit enhancement must be included as tranches of the transaction;

(b) the assets forming the loss-absorbing part of the funded reserve accounts must be included as underlying exposures of the transaction; and

(c) any unfunded reserve accounts (including those to be funded by future receipts from underlying exposures) and any facilities, derivative contracts or assets that do not provide credit enhancement must not be included in the calculations of the AP and DP.

(4) For the purposes of subsection (3), an authorized institution must take into account the economic substance of the securitization transaction so as to determine conservatively whether there are anything falling within the items that must or must not be included under subsection (3)(a), (b) or (c) in light of the structure of the transaction.

248. Tranche maturity of tranche in securitization transaction

(1) Subject to subsections (2), (3), (4) and (5), an authorized institution must calculate the tranche maturity of a tranche in a securitization transaction by using Formula 24 or 25.

Formula 24

Tranche Maturity Based on Contractual Cash Flows

$$M_T = \sum_t t \cdot CF_t \Big/ \sum_t CF_t$$

where—

(a) M_T is the tranche maturity of the tranche; and

(b) CF_t is the cash flows (including principal, interest payments and fees) contractually payable under the tranche by the issuer in the securitization transaction in period t.

Formula 25

Tranche Maturity Based on Final Legal Maturity

$$M_T = 1 + (M_L - 1) \cdot 80\%$$

where—

(a) M_T is the tranche maturity of the tranche; and

(b) M_L is the final legal maturity of the tranche.

(2) An authorized institution must use Formula 25 to calculate the tranche maturity of a tranche in a securitization transaction if—

(a) the contractual payments under the tranche—

(i) are not unconditional; or

(ii) depend on the actual performance of the underlying exposures of the transaction; or

(b) the dates on which the contractual payments under the tranche will be paid are unknown or uncertain.

(3) However, if the securitization exposure to the transaction is an off-balance sheet exposure or the securitization exposure arises from an instrument where the risk of the securitization exposure is not limited to the losses realized until the maturity of the instrument, the tranche maturity of the securitization

exposure is the maximum period of time (which may be longer than the contractual maturity of the exposure) the institution is exposed to the potential losses from the pool of underlying exposures of the transaction.

(4) If the exposure mentioned in subsection (3) arises from a commitment provided by the institution to the transaction, the tranche maturity of the exposure must be calculated as the sum of—

(a) the contractual maturity of the commitment; and

(b) either of the following—

(i) for underlying exposures in the pool that are not revolving in nature—the longest maturity of the underlying exposures in the pool to which the institution would be exposed after a draw of the commitment has occurred;

(ii) for underlying exposures in the pool that are revolving in nature—the longest contractually possible remaining maturity of assets that might be added to the pool in future during the revolving period of the securitization transaction.

(5) If—

(a) a securitization exposure of an authorized institution arises from—

(i) a credit protection provided by the institution to a securitization exposure or securitization transaction; or

(ii) a tranched credit protection provided by the institution to a non-securitization exposure; and

(b) the institution is only exposed to losses that occur up to the maturity of the credit protection, the institution may use the contractual maturity of the credit protection as the tranche maturity of the exposure and does not need to comply with subsections (3) and (4).

(6) The tranche maturity is measured in years and subject to a floor of 1 year and a cap of 5 years.

249. Supplementary provisions to sections 236 and 245 in relation to tranched credit protection

(1) This section applies to an authorized institution that uses the SEC-IRBA, SEC-ERBA or SEC-SA to determine the risk-weight of the protected sub-tranche or unprotected sub-tranche of a securitization exposure to a securitization transaction (***original exposure***) covered by tranched credit protection obtained or provided by the institution.

(2) If the institution uses the SEC-IRBA or SEC-SA to determine the risk-weights of the sub-tranches, it must—

(a) calculate the AP and DP separately for each sub-tranche as if the sub-tranche were directly issued as a separate tranche under the transaction at its inception; and

(b) calculate the K_{IRB} in accordance with section 254 (in the case of the SEC-IRBA) or the K_{SA} in accordance with section 275 (in the case of the SEC-SA), based on the entire pool of the underlying exposures of the transaction for the purpose of determining the risk-weights of the sub-tranches.

(3) If the institution uses the SEC-ERBA to determine the risk-weights of the sub-tranches, it must—

(a) allocate the risk-weight of the original exposure determined by using the SEC-ERBA to the sub-tranche that has the highest priority of repayment among the sub-tranches; and *(L.N. 167 of 2023)*

(b) for a sub-tranche of lower priority of repayment—

(i) determine the risk-weight of the sub-tranche by using the SEC-ERBA by—

(A) regarding the ECAI issue specific rating, the inferred rating or the internal credit rating of a tranche in the same securitization transaction that is subordinated to the tranche within which the original exposure falls as if the rating were that of the sub-tranche; and *(L.N. 222 of 2018)*

(B) using the tranche thickness for the sub-tranche calculated by subtracting AP of the sub-tranche from the DP of the sub-tranche, where the AP and the DP are calculated separately for the sub-tranche as if the sub-tranche were directly issued as a separate tranche under the transaction at its inception; or

(ii) if there is no rated subordinated tranche available for applying the treatment set out in subparagraph (i), determine the risk-weight of the sub-tranche as the greater of—

(A) the risk-weight of the sub-tranche determined by using the SEC-SA, based on the AP and DP calculated separately for the sub-tranche as if the sub-tranche were directly issued as a separate tranche under the transaction at its inception; and

(B) the risk-weight of the original exposure determined by using the SEC-ERBA without taking into account any credit protection afforded to the original exposure.

(4) For the purposes of subsections (2) and (3), a sub-tranche of lower priority of repayment must be treated as a non-senior tranche regardless of whether the original exposure, prior to any credit protection, is an exposure in a senior tranche or not.

Division 7—Risk-weighting Requirements under SEC-IRBA

(Division 7 added L.N. 175 of 2017)

250. Application of Division 7

This Division applies to an authorized institution that is required to use the SEC-IRBA to determine the risk-weight of a securitization exposure to a securitization transaction under section 15.

251. Determination of risk-weights of securitization exposures

(1) Subject to subsection (5), an authorized institution must determine the risk-weight of a securitization exposure in a tranche of a securitization transaction (***relevant tranche***) in accordance with subsection (2), (3) or (4).

(2) If the DP of the relevant tranche is less than or equal to the K_{IRB} calculated in accordance with section 254 for the pool of underlying exposures of the transaction (***relevant*** $\boldsymbol{K_{IRB}}$ ***value***), the institution must allocate a risk-weight of 1,250% to the exposure. *(L.N. 167 of 2023)*

(3) If—

(a) the AP of the relevant tranche is less than the relevant K_{IRB} value; and

(b) the DP of the relevant tranche is greater than the relevant K_{IRB} value,

the institution must determine the risk-weight (expressed in decimals) of the exposure by using Formula 26.

Formula 26

Risk-weight Formula when DP > K_{IRB} > AP

$$RW = \left[\left(\frac{K_{IRB} - AP}{DP - AP}\right) \cdot 12.5\right] +$$

$$\left[\left(\frac{DP - K_{IRB}}{DP - AP}\right) \cdot 12.5 \cdot K_{SSFA(K_{IRB})}\right]$$

where—

(a) RW is the risk-weight of the exposure;

(b) K_{IRB} is the relevant K_{IRB} value; and

(c) $K_{SSFA(KIRB)}$ is the capital charge per unit of securitization exposure calculated in accordance with section 253 for the relevant tranche.

(4) If the AP of the relevant tranche is greater than or equal to the relevant K_{IRB} value, the institution must determine the risk-weight (expressed in decimals) of the exposure by using Formula 27.

Formula 27

Risk-weight Formula when AP ≥ K_{IRB}

$$RW = K_{SSFA(K_{IRB})} \cdot 12.5$$

where—

(a) RW is the risk-weight of the exposure; and

(b) $K_{SSFA(KIRB)}$ is the capital charge per unit of securitization exposure calculated in accordance with section 253 for the relevant tranche.

(5) If the underlying exposures of the transaction consist of purchased receivables, the dilution risk in respect of the receivables must be taken into account in accordance with section 252 in the determination of the risk-weight of the securitization exposure unless the institution has assessed prudently that the dilution risk faced by it in respect of the receivables is immaterial.

251A. *(Repealed L.N. 175 of 2017)*

252. Treatment of dilution risk of underlying exposures for purposes of section 251

(1) For the purposes of section 251, if the underlying exposures of a securitization transaction consist of purchased receivables—

(a) a separate K_{IRB} must be calculated for the dilution risk (***$K_{IRB(dilution)}$***) of the receivables in accordance with section 254(1) and Divisions 9 and 10 of Part 6; and

(b) a separate K_{IRB} must be calculated for the default risk (***$K_{IRB(default)}$***) of the receivables in accordance with section 254(1) and Divisions 9 and 10 of Part 6.

(2) If the default risk and dilution risk of the purchased receivables are treated in an aggregate manner within the transaction such that losses from both risks are covered by the same credit enhancement or credit protection, the authorized institution concerned must calculate the K_{IRB} of the purchased

receivables covering both risks by adding together the 2 figures obtained under subsection (1).

(3) If the credit enhancement or credit protection within the transaction is only available to cover losses from either the default risk or the dilution risk of the purchased receivables but not both, the authorized institution concerned must, for the purposes of determining the AP, DP and tranche maturity of the tranche in respect of each of the 2 risks and whether a $K_{IRB(dilution)}$ or $K_{IRB(default)}$ or both is to be used in calculating the risk-weight of a securitization exposure to the transaction—

(a) ascertain how the losses arising from default risk and dilution risk would be allocated to the tranche within which the securitization exposure falls; and

(b) make conservative assumptions about the extent to which the securitization exposure would benefit from the credit enhancement or credit protection.

253. Capital charge per unit of securitization exposure under SEC-IRBA

An authorized institution must calculate the capital charge per unit of securitization exposure for a tranche of a securitization transaction (***relevant tranche***) by using Formula 27A.

Formula 27A

Capital Charge per Unit of Securitization Exposure under SEC-IRBA

$$K_{SSFA(K_{IRB})} = \frac{e^{a \cdot u} - e^{a \cdot l}}{a(u - l)}$$

where—

(a) $K_{SSFA(KIRB)}$ is the capital charge per unit of securitization exposure for the relevant tranche;

(b) $a = -(1 / (p \cdot K_{IRB}))$, where p is the p-parameter for the relevant tranche calculated in accordance with section 260;

(c) $u = DP - K_{IRB}$;

(d) $l = \max(AP - K_{IRB}; 0)$;

(e) e is a constant that is the base of the natural logarithm; and

(f) K_{IRB} is the K_{IRB} calculated in accordance with section 254 (and section 252 if applicable) for the pool of underlying exposures of the transaction.

254. Calculation of K_{IRB} for underlying exposures

(1) If the pool of underlying exposures of a securitization transaction (including assets or exposures that are treated as the underlying exposures of the transaction under section 256 or 257) is an IRB pool, the K_{IRB} (expressed in decimals) of the pool is the ratio of the amount specified in paragraph (a) to the amount specified in paragraph (b)—

(a) the IRB capital charge calculated for the underlying exposures in the pool in accordance with section 255;

(b) the total exposure amount of the underlying exposures in the pool.

(2) If the pool of underlying exposures of a securitization transaction (including assets or exposures that are treated as the underlying exposures of the transaction under section 256 or 257) is a mixed pool, the K_{IRB} of the pool must be calculated by using Formula 27B.

Formula 27B

Calculation of K_{IRB} of Mixed Pool

$$K_{IRB} = d \cdot K_{IRB}^{(subpool\ 1)} + (1 - d) \cdot K_{SA}^{(subpool\ 2)}$$

where—

(a) d is the percentage of the total exposure amount of the underlying exposures in the pool for which the authorized institution concerned is able to calculate a K_{IRB} in accordance with subsection (1) over the total exposure amount of all the underlying exposures in the pool;

(b) $K_{IRB}^{(subpool\ 1)}$ is the K_{IRB} calculated in accordance with subsection (1) for those underlying exposures in the pool for which the institution is able to so calculate a K_{IRB}; and

(c) $K_{SA}^{(subpool\ 2)}$ is the K_{SA} calculated in accordance with section 275 for those underlying exposures in the pool for which the institution is unable to calculate a K_{IRB} in accordance with subsection (1).

255. Calculation of IRB capital charge for underlying exposures in IRB pool

(1) Subject to subsection (2) and sections 256, 257, 258 and 259, the IRB capital charge for the underlying exposures (including defaulted underlying exposures) in an IRB pool is calculated as the sum of—

(a) the product of—

(i) the risk-weighted amount of the underlying exposures calculated in accordance with Part 6 (as if the underlying exposures were held directly by the authorized institution concerned if they are not held by the institution); and *(L.N. 167 of 2023)*

(ii) 0.08; and

(b) the EL amount of the underlying exposures calculated in accordance with Part 6.

(2) For the purposes of subsection (1), an authorized institution may take into account the credit risk mitigation effect of any Part 6 credit risk mitigation afforded to individual underlying exposures, or to the entire pool of the underlying exposures, in the manner set out in Part 6.

256. Specific requirements applicable to calculation of K_{IRB}—SPE's exposure

(1) If a securitization transaction involves an SPE, all exposures incurred by the SPE (***SPE's exposure***) in respect of the transaction (including assets in which the SPE may have invested a reserve account or cash collateral account, and claims on counterparties resulting from derivative contracts entered into by the SPE with the counterparties) must be treated as underlying exposures of the transaction in calculating the K_{IRB} in accordance with section 254(1).

(2) However, the authorized institution concerned is not required to comply with subsection (1) in respect of an SPE's exposure if the institution has assessed prudently that the risk of the exposure—

(a) is immaterial; or

(b) does not have any adverse effect on the securitization exposure concerned.

(3) If the SPE's exposure arises from a derivative contract other than a credit derivative contract, in calculating the IRB capital charge for the underlying exposures in the pool concerned in accordance with section 255, the risk-weighted amount of the SPE's exposure is the product of—

(a) the current exposure of the derivative contract; and

(b) the risk-weight of the counterparty concerned determined in accordance with Part 6.

257. Specific requirements applicable to calculation of K_{IRB}—collateral for funded synthetic securitization transaction

(1) This section applies to the calculation of the K_{IRB} in accordance with section 254(1) for a pool of underlying exposures of a funded synthetic securitization transaction if—

(a) assets are held under the transaction as collateral for the repayment of the securitization exposure concerned; and

(b) the default risk of the collateral is subject to tranched loss allocation.

(2) The authorized institution concerned must—

(a) treat the collateral as an underlying exposure of the transaction; and

(b) include the risk-weighted amount of the collateral (calculated as the product of the exposure amount of the collateral and its risk-weight determined in accordance with Part 6 or this Part) in the calculation of the IRB capital charge for the underlying exposures in the pool under section 255.

(3) However, the institution is not required to comply with subsection (2) if it has assessed prudently that the exposure amount of the collateral or the default risk of the collateral is immaterial.

258. Further provisions to sections 256 and 257

(1) A derivative contract or collateral that has been included in the calculation of the IRB capital charge for the underlying exposures in a pool under section 256(3) or 257(2) must not be included in the calculation of the total exposure amount of the underlying exposures in the pool under section 254(1)(b).

(2) The K_{IRB} of the pool of underlying exposures (including those exposures referred to in section 256(1) or 257(2)) must be calculated by using the exposure amounts of those underlying exposures without deducting—

(a) any specific provisions or partial write-offs made for such exposures; or

(b) any non-refundable purchase price discounts on such exposures.

259. Treatment of default risk of underlying exposures in calculation of K_{IRB}

(1) Subject to subsection (4), an authorized institution may calculate the risk-weighted amount for default risk in respect of underlying exposures (regardless of whether they are purchased receivables or not) for the purposes of section 255(1)(a)(i) by using the top-down approach referred to in section 198(3) in accordance with the provisions in Divisions 9 and 10 of Part 6 that are applicable to the approach if—

(a) the underlying exposures fall or would fall within the IRB class of retail exposures under the IRB approach;

(b) the institution is unable to use internal data as the primary source of information for estimating the risk characteristics for the underlying exposures under section 177(2)(a); and

(c) all other requirements under Part 6 (except section 177(2)(b)) and Schedule 2 applicable to the IRB class of retail exposures are met by the institution in respect of the underlying exposures.

(2) If the institution uses the top-down approach under subsection (1)—

(a) references to “purchased receivables”, “retail receivables” or “receivables” in the provisions in Divisions 9 and 10 of Part 6 that are applicable to the top-down approach are to be construed as references to the underlying exposures; and

(b) the institution may use external data to estimate the PD and LGD of the underlying exposures provided that the institution has verified in a prudent manner that—

(i) there is a strong link between the institution’s process of grouping the underlying exposures into portfolios under section 200(a) and the classification process used by the external data source; and

(ii) there is a strong link between the credit risk profile of the underlying exposures and the composition of the external data.

(3) For the purposes of subsection (1)(c)—

(a) the institution is regarded as having met the requirement of section 200(d) if it meets the requirement through a party to the securitization transaction concerned acting for and in the interest of the investors in the transaction in accordance with the terms of the related securitization documents; and

(b) in the paragraphs referred to in section 200(d)— *(L.N. 167 of 2023)*

(i) references to “a bank purchasing receivables” or “the bank” are to be construed as references to the institution, except in paragraph CRE36.118(1) where the references are to be construed as references to the securitization transaction concerned; and *(L.N. 167 of 2023)*

(ii) references to “purchased receivables”, “receivables” or “receivable” are to be construed as references to the underlying exposures concerned.

(4) If the Monetary Authority considers that—

(a) any of the requirements referred to in subsection (1)(c) is not met in respect of any of the underlying exposures; or

(b) the institution uses external data to estimate the PD and LGD but has not verified in a prudent manner the matter mentioned in subsection (2)(b)(i) or (ii),

the Monetary Authority may give a notice in writing specified in subsection (5) to the institution.

(5) The notice may—

(a) require the institution not to use the top-down approach to calculate the risk-weighted amount for default risk in respect of the underlying exposures; and

(b) require the institution to use the SEC-ERBA, SEC-SA or SEC-FBA to determine the risk-weight of a securitization exposure backed by the underlying exposures.

(6) An authorized institution must comply with the requirements of a notice given to it under subsection (4).

260. Calculation of p-parameter

(1) The p-parameter for a tranche in a securitization transaction

is calculated by using Formula 27C.

Formula 27C

p-parameter under SEC-IRBA

$$p = \max\left[0.3; \left(A + \left(\frac{B}{N}\right) + C \cdot K_{IRB} + D \cdot LGD_{SEC} + E \cdot M_T\right)\right]$$

where—

(a) p is the p-parameter for the tranche;

(b) N is the effective number of underlying exposures of the pool of underlying exposures of the transaction calculated in accordance with section 261 or 263;

(c) K_{IRB} is the K_{IRB} calculated in accordance with section 254 (and section 252 if applicable) for the pool;

(d) LGD_{SEC} is the exposure-weighted average LGD of the pool calculated in accordance with section 262 or 263;

(e) M_T is the tranche maturity of the tranche calculated in accordance with section 248; and

(f) A, B, C, D, and E are values determined in accordance with Part 1 or 2 of Table 24 based on whether the tranche is a senior tranche or a non-senior tranche, the type of underlying exposures and the value of N.

Table 24

Inputs for Calculation of p-parameter

Part 1

Applicable to Underlying Exposures that are Wholesale Exposures

	A	B	C	D	E
Senior tranche, $N \geq 25$	0	3.56	-1.85	0.55	0.07
Senior tranche, $N < 25$	0.11	2.61	-2.91	0.68	0.07
Non-senior tranche, $N \geq 25$	0.16	2.87	-1.03	0.21	0.07
Non-senior tranche, $N < 25$	0.22	2.35	-2.46	0.48	0.07

Part 2

Applicable to Underlying Exposures that are Retail Exposures

	A	B	C	D	E
Senior tranche	0	0	-7.48	0.71	0.24
Non-senior tranche	0	0	-5.78	0.55	0.27

(2) In Table 24—

(a) ***retail exposures*** (零售風險承擔) mean underlying exposures that would fall within the IRB class of retail exposures under the IRB approach if they were not securitized; and

(b) ***wholesale exposures*** (批發風險承擔) mean underlying exposures that are not retail exposures.

(3) For a pool of underlying exposures of a securitization transaction that consists of both retail exposures and wholesale exposures—

(a) if the pool is an IRB pool, an authorized institution must—

(i) divide the pool into 2 sub-pools, one comprising retail exposures and the other comprising wholesale exposures;

(ii) calculate separate p-parameters for the 2 sub-pools by using Formula 27C; and

(iii) then calculate the p-parameter for the tranche concerned as the weighted average of the 2 separate p-parameters using the nominal amount of the underlying exposures in each sub-pool as the weight; or

(b) if the pool is a mixed pool, an authorized institution must calculate the p-parameter for the tranche concerned based only on the underlying exposures in the pool for which the institution is able to calculate a K_{IRB} in accordance with section 254(1).

(4) To avoid doubt, in calculating the p-parameter for a sub-pool by using Formula 27C under subsection (3)(a)(ii), the N, K_{IRB} and LGD_{SEC} in that Formula must be calculated based only on the underlying exposures in the sub-pool.

260A. *(Repealed L.N. 175 of 2017)*

261. Effective number of underlying exposures

The effective number of underlying exposures of a pool of underlying exposures of a securitization transaction is calculated by using Formula 27D.

Formula 27D

Effective Number of Underlying Exposures

$$N = \frac{(\sum_i EAD_i)^2}{\sum_i EAD_i^2}$$

where—

(a) N is the effective number of underlying exposures of the pool; and

(b) EAD_i is the EAD associated with the i^{th} obligor in the pool determined by regarding all the underlying exposures to the i^{th} obligor as one single exposure.

262. Exposure-weighted average LGD

(1) The exposure-weighted average LGD of a pool of underlying exposures of a securitization transaction is calculated by using Formula 27E.

Formula 27E

Exposure-weighted Average LGD

$$LGD_{SEC} = \frac{\sum_i LGD_i \cdot EAD_i}{\sum_i EAD_i}$$

where—

(a) LGD_{SEC} is the exposure-weighted average LGD of the pool;

(b) LGD_i is the average LGD associated with all the underlying exposures to the i^{th} obligor in the pool; and

(c) EAD_i is the EAD associated with the i^{th} obligor in the pool determined by regarding all the underlying exposures to the i^{th} obligor as one single exposure.

(2) If—

(a) the underlying exposures of a securitization transaction to the i^{th} obligor are purchased receivables whose default risk and dilution risk are treated in an aggregate manner as described in section 252(2); or

(b) the SEC-IRBA is used to determine the risk-weight of the purchased receivables covered by the first-loss protection mentioned in section 237(3), and both default risk and dilution risk of the receivables are covered by the same recognized collateral or recognized guarantee,

the LGD_i in Formula 27E must be calculated as the weighted average of the LGD for the default risk of the i^{th} obligor and the 100% LGD for the dilution risk in respect of the receivables.

(3) For the purposes of subsection (2)—

(a) the LGD for default risk must be weighted by using the IRB capital charge calculated for the default risk; and

(b) the LGD for dilution risk must be weighted by using the IRB capital charge calculated for the dilution risk.

263. Simplified method for calculating N and LGD_{SEC}

(1) In this section—

(a) C_1, in relation to a pool of underlying exposures of a securitization transaction, is the ratio of the amount specified in subparagraph (i) to the amount specified in subparagraph (ii)—

(i) the nominal amount of the largest underlying exposure in the pool;

(ii) the total nominal amount of all the underlying exposures in the pool; and

(b) C_m, in relation to a pool of underlying exposures of a securitization transaction, is the ratio of the amount specified in subparagraph (i) to the amount specified in subparagraph (ii)—

(i) the sum of the nominal amounts of the largest m underlying exposures in the pool, where m is a number set by an authorized institution for the purposes of this section;

(ii) the total nominal amount of all the underlying exposures in the pool.

(2) If C_1 calculated for a pool of underlying exposures of a securitization transaction is not more than 0.03, the authorized institution concerned may—

(a) instead of calculating the exposure-weighted average LGD (***LGD_{SEC}***) of the pool in accordance with section 262, set the LGD_{SEC} of the pool at 0.5; and

(b) instead of using Formula 27D to calculate the effective number of underlying exposures (***N***) of the pool—

(i) if both C_1 and C_m are known to the institution—calculate N in accordance with Formula 27F; or

Formula 27F

Calculation of N when C_1 and C_m are Known

$$N = \left(C_1 \cdot C_m + \left(\frac{C_m - C_1}{m - 1} \right) \cdot \max\{1 - m \cdot C_1, 0\} \right)^{-1}$$

(ii) if only C_1 is known to the institution—calculate N as $1/C_1$.

Division 8—Risk-weighting Requirements under SEC-ERBA

(Division 8 added L.N. 175 of 2017)

264. Application of Division 8

This Division applies to an authorized institution that is required to use the SEC-ERBA to determine the risk-weight of a securitization exposure to a securitization transaction under section 15.

265. Determination of risk-weights of securitization exposures with long-term ratings

(1) An authorized institution must determine the risk-weight of a securitization exposure that has a long-term ECAI issue specific rating or a long-term inferred rating by applying the following steps—

(a) map the rating of the exposure to a credit quality grade in accordance with the LT ECAI rating mapping table for securitization exposures; *(L.N. 167 of 2023)*

(b) determine whether the exposure is in a senior tranche or a non-senior tranche and calculate the tranche maturity applicable to the exposure in accordance with section 248;

(c) determine a risk-weight in accordance with subsection (4) or (5), as the case requires, based on the results obtained under paragraphs (a) and (b); and

(d) allocate to the exposure the risk-weight determined in accordance with subsection (2) or (3).

(2) If the exposure is in a senior tranche, the risk-weight of the exposure is the one determined under subsection (1)(c).

(3) If the exposure is in a non-senior tranche, the risk-weight of the exposure is the one calculated by using Formula 27G.

Formula 27G

Risk-weight Formula for Non-senior Tranche

$$RW = (RW_{LT}) \cdot [1\text{–}\min(T;50\%)]$$

where—

(a) RW is the risk-weight of the exposure;

(b) RW_{LT} is the risk-weight determined under subsection (1)(c); and

(c) T is the tranche thickness of the tranche, which is equal to the DP of the tranche minus the AP of the tranche.

(4) If the exposure is in a tranche with a tranche maturity of 1 year or 5 years, the institution must determine the risk-weight in accordance with Table 25 based on the credit quality grade, tranche maturity and seniority of the exposure.

Table 25

Risk-weights for Credit Quality Grades

(L.N. 167 of 2023)

Credit quality grade	Senior tranche		Non-senior tranche	
	Tranche maturity of 1 year	Tranche maturity of 5 years	Tranche maturity of 1 year	Tranche maturity of 5 years
1	15%	20%	15%	70%
2	15%	30%	15%	90%
3	25%	40%	30%	120%
4	30%	45%	40%	140%
5	40%	50%	60%	160%
6	50%	65%	80%	180%
7	60%	70%	120%	210%
8	75%	90%	170%	260%
9	90%	105%	220%	310%
10	120%	140%	330%	420%
11	140%	160%	470%	580%
12	160%	180%	620%	760%
13	200%	225%	750%	860%
14	250%	280%	900%	950%

Credit quality grade	Senior tranche		Non-senior tranche	
	Tranche maturity of 1 year	Tranche maturity of 5 years	Tranche maturity of 1 year	Tranche maturity of 5 years
15	310%	340%	1,050%	1,050%
16	380%	420%	1,130%	1,130%
17	460%	505%	1,250%	1,250%
18	1,250%	1,250%	1,250%	1,250%

(L.N. 167 of 2023)

(5) If the exposure is in a tranche with a tranche maturity of neither 1 year nor 5 years, the institution must—

(a) determine the risk-weights for a tranche maturity of 1 year and a tranche maturity of 5 years that are corresponding to the credit quality grade and the seniority of the exposure in accordance with subsection (4); and

(b) calculate the risk-weight applicable to the tranche maturity of the exposure by using linear interpolation between the 2 risk-weights determined under paragraph (a).

266. Determination of risk-weights of securitization exposures with short-term ratings

An authorized institution must determine the risk-weight of a securitization exposure that has a short-term ECAI issue specific rating or a short-term inferred rating by applying the following steps—

(a) map the rating of the exposure to a credit quality grade in accordance with the ST ECAI rating mapping table for securitization exposures; and *(L.N. 167 of 2023)*

(b) allocate a risk-weight to the exposure in accordance with Table 26 based on the grade so mapped.

Table 26

Risk-weights for Credit Quality Grades

(L.N. 167 of 2023)

Credit quality grade	Risk-weight
1	15%
2	50%
3	100%
4	1,250%

(L.N. 167 of 2023)

266A. Internal assessment approach: determination of risk-weights of eligible ABCP exposures with internal credit ratings

(1) An authorized institution having an IAA approval must, in determining the risk-weight of an eligible ABCP exposure by using the SEC-ERBA based on the internal credit rating of the exposure—

(a) map the internal credit rating to an equivalent long-term ECAI issue specific rating or an equivalent short-term ECAI issue specific rating, as the case requires; and

(b) treat the long-term ECAI issue specific rating or short-term ECAI issue specific rating so obtained as that of the exposure and, on that basis, determine the risk-weight of the exposure in accordance with section 265 or 266, as the case requires.

(2) For the purposes of subsection (1)(a), an internal credit rating and an ECAI issue specific rating are considered to be equivalent to each other if both of them represent broadly the same credit characteristics and creditworthiness.

(L.N. 222 of 2018)

267. Use of ECAI issue specific ratings or internal credit ratings for determination of risk-weights

(L.N. 222 of 2018)

(1) An authorized institution must, in using an ECAI issue specific rating issued by an ECAI for the purposes of determining the risk-weight of a securitization exposure to a securitization transaction—

(a) ensure that it has nominated the ECAI for the purposes of this Part in accordance with section 4C; and *(L.N. 167 of 2023)*

(b) if 2 or more ECAIs have different ECAI issue specific ratings applicable to the exposure—determine the rating applicable to the exposure in the manner set out in section 54E(2)(b) and (c). *(L.N. 167 of 2023)*

(2) If credit protection is provided to specific underlying exposures, or the entire pool of underlying exposures, of a securitization transaction and the credit protection has been reflected in the ECAI issue specific rating or the internal credit rating assigned to a securitization exposure to the transaction— *(L.N. 222 of 2018)*

(a) for credit protection provided by a credit protection provider falling within section 99A(2)(a), the institution— *(L.N. 167 of 2023)*

(i) must determine the risk-weight of the exposure by reference to that rating; and

(ii) must not include the credit risk mitigation effect of that credit protection in any other calculations under this Part; or

(b) for credit protection not provided by a credit protection provider falling within section 99A(2)(a)—the institution must treat the exposure as unrated for the purposes of this Part. *(L.N. 167 of 2023)*

(3) If Part 7 credit risk mitigation is provided to protect only a specific securitization exposure within a given structure or tranche of a securitization transaction and has been reflected in the ECAI issue specific rating or the internal credit rating assigned to the exposure, the institution must— *(L.N. 222 of 2018)*

(a) regard the exposure as unrated for the purposes of this Part; and

(b) take into account the credit risk mitigation effect of the Part 7 credit risk mitigation in accordance with Division 5.

(4) If an ECAI issue specific rating or an internal credit rating assigned to a securitization exposure to a securitization transaction is wholly or partly based on unfunded support (including a liquidity facility or credit enhancement) provided by the institution to the transaction, the institution must calculate the risk-weighted amount of the exposure in accordance with this Part as if it were unrated. *(L.N. 222 of 2018)*

(5) To avoid doubt, an authorized institution falling within subsection (4) must continue to hold regulatory capital for its other securitization exposures (including the unfunded support) to the transaction.

268. Inferred ratings

An authorized institution may use the credit assessment rating attributed by it to a securitization exposure (***principal exposure***) by making reference to another securitization exposure that has an ECAI issue specific rating (***reference exposure***) to risk-weight the principal exposure only if—

(a) the principal exposure has no applicable ECAI issue specific rating;

(b) the reference exposure, in all respects, ranks equally with, or is subordinated to, the principal exposure, after taking into account credit enhancements, if any, in the assessment of the relative subordination of the principal exposure and the reference exposure;

(c) the maturity of the reference exposure is not shorter than that of the principal exposure;

(d) the reference exposure has not ceased to exist;

(e) the credit assessment rating attributed to the principal exposure is updated on an ongoing basis in order to reflect any subordination of the principal exposure or any changes in the ECAI issue specific rating of the reference exposure;

(f) the ECAI issuing the ECAI issue specific rating of the reference exposure has been nominated for the purposes of this Part in accordance with section 4C and, if applicable, the rating is determined in compliance with section 267(1)(b); and *(L.N. 167 of 2023)*

(g) the reference exposure is not required to be treated as an unrated securitization exposure under section 267(2), (3) or (4).

268A. *(Repealed L.N. 175 of 2017)*

Division 9—Risk-weighting Requirements under SEC-SA

(Division 9 added L.N. 175 of 2017)

269. Application of Division 9

This Division applies to an authorized institution that is required to use the SEC-SA to determine the risk-weight of a securitization exposure to a securitization transaction under section 15.

270. Determination of risk-weights of securitization exposures

(1) If, for a securitization transaction, the total nominal amount of the underlying exposures whose delinquency status is unknown to an authorized institution is equal to or less than 5% of the total nominal amount of the entire pool of underlying exposures, the institution must determine the risk-weight of a securitization exposure to the transaction in accordance with section 271.

(2) If, for a securitization transaction, the total nominal amount of the underlying exposures whose delinquency status is unknown to an authorized institution exceeds 5% of the total nominal amount of the entire pool of underlying exposures, the institution must allocate a risk-weight of 1 250% to a securitization exposure to the transaction.

(L.N. 167 of 2023)

271. Risk-weights of securitization exposures falling within section 270(1)

(1) The risk-weight of a securitization exposure in a tranche of a securitization transaction falling within section 270(1) (***relevant tranche***) must be determined in accordance with this section.

(2) If the DP of the relevant tranche is less than or equal to the K_A calculated in accordance with section 273 for the pool of underlying exposures of the transaction (***relevant K_A value***), the institution must assign a risk-weight of 1,250% to the exposure.

(3) If—

(a) the AP of the relevant tranche is less than the relevant K_A value; and

(b) the DP of the relevant tranche is greater than the relevant K_A value,

the institution must determine the risk-weight (expressed in decimals) of the exposure by using Formula 27H.

Formula 27H

Risk-weight Formula when DP > K_A > AP

$$RW = \left[\left(\frac{K_A - AP}{DP - AP}\right) \cdot 12.5\right] + \left[\left(\frac{DP - K_A}{DP - AP}\right) \cdot 12.5 \cdot K_{SSFA(K_A)}\right]$$

where—

(a) RW is the risk-weight of the exposure;

(b) K_A is the relevant K_A value; and

(c) $K_{SSFA(KA)}$ is the capital charge per unit of securitization exposure calculated in accordance with section 272 for the relevant tranche.

(4) If the AP of the relevant tranche is greater than or equal to the relevant K_A value, the institution must determine the risk-weight (expressed in decimals) of the exposure by using Formula 27I.

Formula 27I

Risk-weight Formula when AP ≥ K_A

$$RW = K_{SSFA(K_A)} \cdot 12.5$$

where—

(a) RW is the risk-weight of the exposure; and

(b) $K_{SSFA(KA)}$ is the capital charge per unit of securitization exposure calculated in accordance with section 272 for the relevant tranche.

272. Capital charge per unit of securitization exposure under SEC-SA

An authorized institution must calculate the capital charge per unit of securitization exposure for a tranche of a securitization transaction (***relevant tranche***) by using Formula 27J.

Formula 27J

Capital Charge per unit of Securitization Exposure under SEC-SA

$$K_{SSFA(K_A)} = \frac{e^{a \cdot u} - e^{a \cdot l}}{a(u - l)}$$

where—

(a) $K_{SSFA(KA)}$ is the capital charge per unit of securitization exposure for the relevant tranche;

(b) $a = -(1/(p \cdot K_A))$, where p is equal to—

(i) 1 if the securitization exposures in the tranche are not re-securitization exposures; or

(ii) 1.5 if the securitization exposures in the tranche are re-securitization exposures;

(c) $u = DP - K_A$;

(d) $l = \max(AP - K_A; 0)$;

(e) e is a constant that is the base of the natural logarithm; and

(f) K_A is the capital charge factor for the pool of underlying exposures of the transaction calculated in accordance with section 273.

273. Calculation of capital charge factor for underlying exposures

(1) If an authorized institution knows the delinquency status for the entire pool of underlying exposures of a securitization transaction, the institution must calculate the capital charge factor for the pool by using Formula 27K.

Formula 27K

K_A when Delinquency Status for all of Total Nominal Amount of Pool of Underlying Exposures is Known

$$K_A = (1 - W) \cdot K_{SA} + W \cdot 0.5$$

where—

(a) K_A is the capital charge factor for the pool;

(b) K_{SA} is the K_{SA} calculated in accordance with section 275 for the pool; and

(c) W is the delinquency ratio of the pool.

(2) If an authorized institution does not know the delinquency status for the entire pool of underlying exposures of a securitization transaction, but the total nominal amount of the underlying exposures whose delinquency status is unknown to the institution is equal to or less than 5% of the total nominal amount of the pool, the institution must determine the capital charge factor for the pool by applying the following steps— *(L.N. 167 of 2023)*

(a) divide the entire pool into 2 subpools so that—

(i) subpool 1 comprises underlying exposures of which the delinquency status is known; and

(ii) subpool 2 comprises underlying exposures of which the delinquency status is unknown; and

(b) calculate the capital charge factor for the entire pool by using Formula 27L.

Formula 27L

K_A when 5% or less (but not 0%) of Total Nominal Amount of Pool of Underlying Exposures whose Delinquency Status is Unknown

(L.N. 167 of 2023)

$$K_A = \left(\frac{EAD_{Subpool\ 1}}{EAD_{entire\ pool}} \cdot K_A^{Subpool\ 1}\right) + \frac{EAD_{Subpool\ 2}}{EAD_{entire\ pool}}$$

where—

(a) K_A is the capital charge factor for the pool;

(b) $EAD_{Subpool\ 1}$ is the total exposure amount of the underlying exposures in subpool 1;

(c) $EAD_{Subpool\ 2}$ is the total exposure amount of the underlying exposures in subpool 2;

(d) $EAD_{entire\ pool}$ is the total exposure amount of the underlying exposures in the entire pool; and

(e) $K_A^{Subpool\ 1}$ is the capital charge factor calculated in accordance with subsection (1) for subpool 1.

(3) In this section—

delinquency ratio (拖欠比率)—

(a) in relation to a pool of underlying exposures that are non-securitization exposures, means the ratio of the amount specified in subparagraph (i) to the amount specified in subparagraph (ii)—

(i) the total nominal amount of delinquent underlying exposures in the pool;

(ii) the total nominal amount of all the underlying exposures in the pool; or

(b) in relation to a pool of underlying exposures that are securitization exposures, is zero;

delinquent underlying exposure (拖欠組成項目) means an underlying exposure that is—

(a) 90 days or more past due;

(b) subject to bankruptcy or insolvency proceedings;

(c) in the process of foreclosure;

(d) held as real estate owned; or

(e) in default as defined in the documents of the securitization transaction concerned.

274. Provisions supplementary to section 273

For the purposes of section 273, if the underlying exposures of a securitization transaction consist of both non-securitization exposures and securitization exposures, an authorized institution must—

(a) classify underlying exposures that are securitization exposures into subset 1 and underlying exposures that are non-securitization exposures into subset 2;

(b) determine the capital charge factor for each of the subsets in accordance with section 273, using the delinquency ratio (within the meaning of section 273(3)) determined for the underlying exposures in each subset; and

(c) determine the capital charge factor for the entire pool of the underlying exposures as the weighted-average of the 2 capital charge factors calculated under paragraph (b), using the nominal amount of the underlying exposures in each subset as the weight.

275. Calculation of K_{SA} for underlying exposures

The K_{SA} (expressed in decimals) of a pool of underlying exposures of a securitization transaction (including assets or exposures that are treated as the underlying exposures of the transaction under section 277 or 278) is the ratio of the amount specified in paragraph (a) to the amount specified in paragraph (b)—

(a) the SA capital charge calculated for the underlying exposures in the pool in accordance with section 276;

(b) the total exposure amount of the underlying exposures in the pool.

276. Calculation of SA capital charge for underlying exposures

(1) Subject to sections 277, 278 and 279, the SA capital charge for the underlying exposures in a pool is calculated as the product of—

(a) the risk-weighted amount of the underlying exposures calculated—

(i) in accordance with Part 4 (for underlying exposures that are non-securitization exposures); or

(ii) in accordance with this Part (for underlying exposures that are securitization exposures),

as if the underlying exposures were held directly by the authorized institution concerned if they are not held by the institution; and

(b) 0.08.

(2) For the purposes of subsection (1), an authorized institution may take into account the credit risk mitigation effect of any Part 4 credit risk mitigation or Part 7 credit risk mitigation afforded to individual underlying exposures, or to the entire pool of the underlying exposures, in the manner set out in—

(a) Part 4 (for Part 4 credit risk mitigation afforded to underlying exposures that are non-securitization exposures); and

(b) this Part (for Part 7 credit risk mitigation afforded to underlying exposures that are securitization exposures).

277. Specific requirements applicable to calculation of K_{SA}—SPE's exposure

(1) If a securitization transaction involves an SPE, all exposures incurred by the SPE (***SPE's exposure***) in respect of the transaction (including assets in which the SPE may have invested a reserve account or cash collateral account, and claims on counterparties resulting from derivative contracts entered into by the SPE with the counterparties) must be treated as underlying exposures of the transaction in calculating the K_{SA} in accordance with section 275.

(2) However, the authorized institution concerned is not required to comply with subsection (1) in respect of an SPE's exposure if the institution has assessed prudently that the risk of the exposure—

(a) is immaterial; or

(b) does not have any adverse effect on the securitization exposure concerned.

(3) If the SPE's exposure arises from a derivative contract other than a credit derivative contract, in calculating the SA capital charge for the underlying exposures in the pool concerned in accordance with section 276, the risk-weighted amount of the SPE's exposure is the product of—

(a) the current exposure of the derivative contract; and

(b) the risk-weight of the counterparty concerned determined in accordance with Part 4.

278. Specific requirements applicable to calculation of K_{SA}—collateral for funded synthetic securitization transaction

(1) This section applies to the calculation of the K_{SA} in accordance with section 275 for a pool of underlying exposures of a funded synthetic securitization transaction if—

(a) assets are held under the transaction as collateral for the repayment of the securitization exposure concerned; and

(b) the default risk of the collateral is subject to tranched loss allocation.

(2) The authorized institution concerned must—

(a) treat the collateral as an underlying exposure of the transaction; and

(b) include the risk-weighted amount of the collateral (calculated as the product of the exposure amount of the collateral and its risk-weight determined in accordance with Part 4 or this Part) in the calculation of the SA capital charge for the underlying exposures in the pool under section 276.

(3) However, the institution is not required to comply with subsection (2) if it has assessed prudently that the exposure amount of the collateral or the default risk of the collateral is immaterial.

279. Further provisions to sections 277 and 278

(1) A derivative contract or collateral that has been included in the calculation of the SA capital charge for the underlying exposures in a pool under section 277(3) or 278(2) must not be included in the calculation of the total exposure amount of the underlying exposures in the pool under section 275(b).

(2) The K_{SA} of the pool of underlying exposures (including those exposures referred to in section 277(1) or 278(2)) must be calculated by using the exposure amounts of those underlying exposures without deducting—

(a) any specific provisions or partial write-offs made for the exposures; or

(b) any non-refundable purchase price discounts on the exposures.

Division 10—Risk-weighting Requirements under SEC-FBA

(Division 10 added L.N. 175 of 2017)

280. Application of Division 10

This Division applies to an authorized institution that is required to use the SEC-FBA to determine the risk-weight of a securitization exposure to a securitization transaction under section 15.

280A. Risk-weights of securitization exposures

An authorized institution must allocate a risk-weight of 1,250% to a securitization exposure to a securitization transaction.

Division 11—Non-performing Loan Securitization Transactions

(Division 11 added L.N. 167 of 2023)

280B. Interpretation of Division 11

(1) In this Division—

non-performing loan securitization transaction (不履約貸款證券化交易)—

(a) means a traditional securitization transaction where its pool of underlying exposures—

(i) has a delinquency ratio (within the meaning of paragraph (a) of the definition of ***delinquency ratio*** in section 273(3)) equal to or higher than 90%—

(A) at the origination cut-off date; and

(B) at any subsequent date on which assets are added to or removed from the pool due to replenishment, restructuring or any other relevant reason;

(ii) only comprises—

(A) loans;

(B) loan-equivalent financial instruments, such as bonds not listed on a trading venue; or

(C) tradable instruments used for the sole purpose of loan sub-participation in relation to securitization of assets; and

(iii) does not contain any securitization exposures; and

(b) does not include a transaction specified by the Monetary Authority under subsection (2);

NPL securitization exposure (NPL證券化類別風險承擔) means a securitization exposure to an NPL securitization transaction;

NPL securitization transaction (NPL證券化交易) means a non-performing loan securitization transaction.

(2) The Monetary Authority may, by written notice given to a locally incorporated authorized institution, specify that a securitization transaction originated by the institution is not an NPL securitization transaction, if the Monetary Authority is of the opinion that the transaction was executed with the sole or main purpose of regulatory capital arbitrage (within the meaning of section 4).

(3) An authorized institution must comply with a notice given to it under subsection (2).

280C. Capital treatment of NPL securitization exposures

(1) Subject to subsection (2), an authorized institution must—

(a) determine the approach to be used to determine the risk-weight of an NPL securitization exposure in accordance with Division 4 of Part 2; and

(b) calculate the risk-weighted amount of the NPL securitization exposure in accordance with Divisions 1 to 10, subject to the requirements set out in sections 280D and 280E.

(2) If an authorized institution would use the foundation IRB approach to calculate the capital charge of the underlying exposures of the NPL securitization transaction concerned if the underlying exposures were held by the institution directly, the institution must not use the SEC-IRBA to determine the risk-weight of the NPL securitization exposure.

280D. Risk-weights of NPL securitization exposures under SEC-IRBA and SEC-SA

(1) Subject to subsection (2), if according to section 280C an authorized institution must use the SEC-IRBA or the SEC-SA to determine the risk-weight of an NPL securitization exposure, the institution must allocate to the NPL securitization exposure a risk-weight that is the higher of the following—

(a) 100%;

(b) the risk-weight applicable to the NPL securitization exposure determined under the SEC-IRBA, the SEC-SA or section 241, as the case requires.

(2) Where according to section 280C an authorized institution must use the SEC-IRBA or the SEC-SA to determine the risk-weight of an NPL securitization exposure to an NPL securitization transaction, the institution may allocate a risk-weight of 100% to the senior tranche of the transaction if—

(a) the transaction is a traditional securitization transaction; and

(b) the sum of the non-refundable purchase price discounts is equal to or higher than 50% of the outstanding balance of the pool of underlying exposures of the transaction.

(3) For the purposes of subsection (2), non-refundable purchase price discount (***NRPPD***), in relation to an NPL securitization transaction—

(a) subject to paragraph (b), is the amount arrived at by subtracting the amount referred to in subparagraph (ii) from the amount referred to in subparagraph (i)—

(i) the outstanding balance of the underlying exposures of the transaction at the time those exposures were sold by the originator to the SPE in the transaction;

(ii) the price at which those exposures were sold by the originator to the SPE; and

(b) does not include any amount that is refundable to either the originator or the original lender.

(4) If an originator underwrites tranches of an NPL securitization transaction for subsequent sale, the NRPPD may include the differences between—

(a) the nominal amount of the tranches; and

(b) the price at which the tranches are first sold by the originator to unrelated third parties.

(5) To avoid doubt, in the determination of NRPPD, for any given piece of a securitization tranche—

(a) only its initial sale from the originator to investors is taken into account; and

(b) the purchase prices of subsequent resales are not considered.

280E. Caps on capital requirements for NPL securitization exposures

If an authorized institution is the originator of an NPL securitization transaction, the institution may apply the cap specified in section 242 to the aggregated capital requirement for its NPL securitization exposures to the NPL securitization transaction.

Part 8

Calculation of Market Risk Capital Charge

(L.N. 167 of 2023)

Division 1—General

281. Interpretation of Part 8 and Schedule 3

(L.N. 167 of 2023)

In this Part and Schedule 3— *(L.N. 167 of 2023)*

commodity-related derivative contract (商品關聯衍生工具合約) means a futures contract, forward contract, swap contract, option contract or similar derivative contract the value of which is determined by reference to the value of, or any fluctuation in the value of, an underlying commodity or an underlying commodity index (being an index calculated by reference to a basket of commodities);

conversion factor (換算因數) means a number published by a futures exchange for determining the price for each debt security deliverable against a bond futures contract;

correlation trading portfolio (相關交易組合), in relation to an authorized institution, means—

(a) a portfolio of securitization exposures or n^{th}-to-default credit derivative contracts, or both—

(i) that are not—

(A) re-securitization exposures; or

(B) derivatives of securitization exposures that do not provide a pro-rata share in the proceeds of a securitization tranche;

(ii) where the underlying exposures of the securitization exposures, or the reference obligations of the n^{th}-to-default credit derivative contracts, are not—

(A) a regulatory retail exposure within the meaning of section 51(1);

(B) an exposure that is subject to the IRB approach for retail exposures under section 144;

(C) a credit facility secured on one or more than one residential property for the purposes of financing or re-financing the purchase of the property or properties concerned; or

(D) a credit facility secured on one or more than one commercial property for the purposes of financing or re-financing the purchase of the property or properties concerned;

(iii) that do not reference a claim on a special purpose entity; and

(iv) where all reference obligations, in the case of the n^{th}-to-default credit derivative contracts, are single-name products (including single-name credit derivative contracts and commonly traded indices based on single-name products) for which a liquid two-way market exists; and

(b) any positions that hedge the securitization exposures or n^{th}-to-default credit derivative contracts referred to in paragraph (a) where—

(i) the positions are not securitization exposures or n^{th}-to-default credit derivative contracts; and

(ii) a liquid two-way market exists for the positions and the underlying exposures of the positions; *(L.N. 137 of 2011)*

covered bond (資產覆蓋債券) has the meaning given by rule 17 of the Banking (Liquidity) Rules (Cap. 155 sub. leg. Q); *(L.N. 167 of 2023)*

credit migration risk (信用遷移風險), in relation to an exposure of an authorized institution, means the potential for direct and indirect losses to the institution if there were an internal or external rating downgrade or upgrade; *(L.N. 137 of 2011)*

CTP means a correlation trading portfolio; *(L.N. 167 of 2023)*

current ES (現行ES), in relation to a portfolio of exposures held by an authorized institution, means an ES calculated by the institution under the IMA with model inputs calibrated to historical data from the most recent 12-month period; *(L.N. 167 of 2023)*

debt-related derivative contract (債務關聯衍生工具合約) means a futures contract, forward contract, swap contract, option contract or similar derivative contract the value of which is determined by reference to the value of, or any fluctuation in the value of, an underlying debt security or an underlying debt security index (being an index calculated by reference to a basket of debt securities);

debt security (債務證券) means—

(a) a fixed or floating rate bond;

(b) a negotiable certificate of deposit;

(c) a non-convertible preference share; or

(d) a convertible bond, preference share, or any other instrument, which trades like a bond, certificate or share falling within paragraph (a), (b) or (c);

default risk (違責風險), in relation to an exposure of an authorized institution, means the potential for direct and indirect losses to the institution if the obligor were to default or a default event were to occur; *(L.N. 137 of 2011)*

default risk charge (違責風險資本要求), in relation to the IMA, means the greater of the following—

(a) the most recent market risk capital charge calculated by an authorized institution's internal models to capture the risk of direct loss due to a default event as well as the potential for indirect loss that may arise from a default event in respect of its trading book positions in credit instruments and equity instruments;

(b) the average of all such market risk capital charges calculated by the institution's internal models over the previous 12-week period; *(L.N. 167 of 2023)*

delta (得爾塔), in relation to the calculation of an authorized institution's market risk capital charge for an option contract under the SSTM approach, means a measure of the rate of change in the value of the option contract to changes in the value of the underlying exposure of the option contract; *(L.N. 167 of 2023)*

delta-plus approach (得爾塔附加計算法), in relation to the calculation of an authorized institution's market risk capital charge for its option exposures to debt securities, interest rates, equities, foreign exchange (including gold) and commodities, means the approach set out in Division 9;

delta-weighted position (得爾塔加權持倉), in relation to an option contract, means the value of the underlying exposure of the option contract multiplied by the corresponding delta;

eligible internal risk transfer (合資格內部風險轉移), in relation to the calculation of an authorized institution's market risk capital charge, means an internal risk transfer that is recognized under section 281D; *(L.N. 167 of 2023)*

equity (股權) means—

(a) an ordinary share (whether voting or non-voting); or

(b) a convertible bond, preference share, or any other instrument, which trades like a share falling within paragraph (a);

equity-related derivative contract (股權關聯衍生工具合約) means a futures contract, forward contract, swap contract, option contract or similar derivative contract the value of which is determined by reference to the value of, or any fluctuation in the value of, an underlying equity or an underlying equity index (being an index calculated by reference to a basket of equities);

ES means expected shortfall; *(L.N. 167 of 2023)*

exchange rate-related derivative contract (匯率關聯衍生工具合約) means a futures contract, forward contract, swap contract, option contract or similar derivative contract the value of which is determined by reference to the value of, or any fluctuation in the value of, an underlying currency (including gold) or an underlying currency index (being an index calculated by reference to a basket of currencies);

expected shortfall (預期損失值), in relation to a portfolio of exposures, means the average of all potential losses exceeding the VaR over a period of time at a given confidence level; *(L.N. 167 of 2023)*

gamma (伽馬), in relation to the calculation of an authorized institution's market risk capital charge for an option contract under the SSTM approach, means a measure of the rate of change in delta of the option contract to changes in the value of the underlying exposure of the option contract; *(L.N. 167 of 2023)*

general market risk (一般市場風險), in relation to an authorized institution, means the risk of loss, arising from changes in interest rates, exchange rates, equity prices or commodity prices, in the value of—

(a) the institution's trading book positions held in—

(i) debt securities;

(ii) debt-related derivative contracts;

(iii) interest rate derivative contracts;

(iv) equities; and

(v) equity-related derivative contracts; and

(b) the institution's positions held in—

(i) foreign exchange (including gold);

(ii) exchange rate-related derivative contracts;

(iii) commodities; and

(iv) commodity-related derivative contracts;

GIRR means general interest rate risk; *(L.N. 167 of 2023)*

gross jump-to-default risk amount (突發違責風險總額), in relation to the SA-DRC, means the estimated loss or gain on an individual exposure as a result of the default of an obligor; *(L.N. 167 of 2023)*

idiosyncratic credit spread NMRF (獨特信用利差NMRF), in relation to the IMA, means a credit spread NMRF that is associated with a particular issuance, including default provisions, maturity and seniority; *(L.N. 167 of 2023)*

idiosyncratic equity NMRF (獨特股權NMRF), in relation to the IMA, means an equity NMRF that is associated with a particular equity; *(L.N. 167 of 2023)*

interest rate derivative contract (利率衍生工具合約) means a futures contract, forward contract, swap contract, option contract or similar derivative contract—

(a) the value of which changes in response to changes in interest rates; but

(b) the underlying exposure of which is neither a debt security nor an index calculated by reference to a basket of debt securities;

internal risk transfer (內部風險轉移), in relation to the calculation of an authorized institution's market risk capital charge, means a transfer of risk, confirmed by an internal written record—

(a) within the institution's banking book;

(b) between the institution's banking book and trading book; or

(c) between different desks within the institution's trading book; *(L.N. 167 of 2023)*

investment grade (投資等級) means—

(a) a credit quality grade of 1, 2, 3 or 4 derived from mapping the ECAI issuer rating assigned to an issuer, being a sovereign, of any debt security to a credit quality grade in the LT ECAI rating mapping table for Type A ECAIs;

(b) a credit quality grade of 1, 2, 3 or 4 derived from mapping the ECAI issue specific rating assigned to any debt security issued by a bank or securities firm to a credit quality grade in the LT ECAI rating mapping table, or ST ECAI rating mapping table, for Type A ECAIs;

(c) a credit quality grade of 1, 2, 3 or 4 derived from mapping the ECAI issue specific rating assigned to any debt security issued by a corporate (within the meaning of section 51(1) or 139(1), as the case requires) to a credit quality grade in the LT ECAI rating mapping table, or ST ECAI rating mapping table, for Type A ECAIs; or

(d) a credit quality grade of 1, 2, 3 or 4 derived from mapping the ECAI issue specific rating assigned to any debt security issued by a corporate (within the meaning of section 51(1) or 139(1), as the case requires) incorporated in India to a credit quality grade in the LT ECAI rating mapping table, or ST ECAI rating mapping table, for Type B ECAIs; *(L.N. 167 of 2023)*

look-through approach (透視計算法) means the decomposition of an instrument into its underlying exposures or its individual components that, in the case of a collective investment scheme, is based on sufficient and frequent information verified by an independent third party; *(L.N. 167 of 2023)*

market risk capital charge (市場風險資本要求), in relation to an authorized institution, means the amount of the institution's capital required to cover specific risk or general market risk, or both, for an exposure or a portfolio of exposures;

market risk capital charge factor (市場風險資本要求因數), in relation to an authorized institution, means a percentage specified in this Part for the calculation of the institution's market risk capital charge;

matched positions (配對持倉), in relation to an authorized institution, means 2 opposite positions held by the institution where the risk of loss arising from either position can be offset by the other position;

maturity method (到期方法), in relation to the calculation of an authorized institution's market risk capital charge for general market risk for its interest rate exposures, means the approach set out in section 288;

modellable risk factor (可模式化風險因素), in relation to the IMA, means a risk factor that passes the risk factor eligibility test under an authorized institution's internal models; *(L.N. 167 of 2023)*

net jump-to-default risk amount (突發違責風險淨額), in relation to the SA-DRC, means the estimated loss or gain for an authorized institution as a result of the default of an obligor after offsetting gross jump-to-default risk amounts with respect to that obligor; *(L.N. 167 of 2023)*

NMRF means a non-modellable risk factor; *(L.N. 167 of 2023)*

non-modellable risk factor (不可模式化的風險因素), in relation to the IMA, means a risk factor that is not a modellable risk factor; *(L.N. 167 of 2023)*

n^{th}-to-default credit derivative contract (n^{th}違責者信用衍生工具合約) means a credit derivative contract under which—

(a) the protection buyer obtains credit protection for a basket of exposures; and

(b) the n^{th} default among the obligations specified in the contract for the purposes of determining whether a credit event has occurred triggers the credit protection and terminates the contract; *(L.N. 137 of 2011)*

position (持倉), in relation to an authorized institution, means the holding or disposal by the institution of an exposure, or a portfolio of exposures, resulting in risk being taken by the institution on market price movements in respect of the exposure, or portfolio of exposures, as the case may be;

qualifying covered bond (合資格資產覆蓋債券) means a covered bond that meets all the conditions in rule 70(3) of the Banking (Exposure Limits) Rules (Cap. 155 sub. leg. S) at the inception of the covered bond and throughout its remaining maturity; *(L.N. 167 of 2023)*

real price observation (真實價格觀察), for an authorized institution in relation to a risk factor under the IMA, means—

(a) a price at which the institution has conducted a transaction;

(b) a verifiable price for an actual transaction between other arms-length parties;

(c) a price obtained from a committed quote made by the institution itself or another party that has been collected and verified through a third-party vendor, a trading platform or an exchange; or

(d) a price obtained from a third-party vendor if—

(i) the transaction or committed quote has been processed through the vendor;

(ii) the vendor agrees to provide evidence of the transaction or committed quote to the Monetary Authority at the request of the institution; and

(iii) the price meets any of the criteria in paragraph (a), (b) or (c); *(L.N. 167 of 2023)*

reduced set of modellable risk factors (可模式化風險因素的簡化組合), for an authorized institution in relation to the IMA, means a set of modellable risk factors approved for the institution by the Monetary Authority under section 322D(5)(a); *(L.N. 167 of 2023)*

residual risk add-on (剩餘風險附加額) means a component of the STM approach under Division 1C to capture any additional risks beyond the main risk factors already captured in the SBM and the SA-DRC; *(L.N. 167 of 2023)*

risk category (風險類別), in relation to the calculation of an authorized institution's market risk, means the class of the institution's market risk exposures which are at risk from—

(a) changes in debt security prices or interest rates;

(b) changes in exchange rates;

(c) changes in equity prices; or

(d) changes in commodity prices;

risk factor (風險因素) means a variable that affects the value of an instrument; *(L.N. 167 of 2023)*

risk factor eligibility test (風險因素合資格測試), in relation to the IMA, means a test to check whether there are a sufficient number of real price observations that are representative of a risk factor; *(L.N. 167 of 2023)*

RRAO means the residual risk add-on; *(L.N. 167 of 2023)*

SA-DRC means the standardized default risk charge; *(L.N. 167 of 2023)*

SA-DRC (non-securitization) (SA-DRC(非證券化)) means the SA-DRC for the exposures set out in section 281T(1); *(L.N. 167 of 2023)*

SA-DRC (securitization: CTP) (SA-DRC(證券化：CTP)) means the SA-DRC for the exposures to instruments set out in section 281W(1); *(L.N. 167 of 2023)*

SA-DRC (securitization: non-CTP) (SA-DRC(證券化：非CTP)) means the SA-DRC for the exposures set out in section 281V(1); *(L.N. 167 of 2023)*

SBM means the sensitivities-based method; *(L.N. 167 of 2023)*

SBM curvature (SBM曲率) means a sensitivity to capture the changes in the value of an authorized institution's position due to movements in its non-volatility risk factors not captured by the SBM delta; *(L.N. 167 of 2023)*

SBM curvature risk (SBM曲率風險) means the risk of changes in the value of an authorized institution's position due to movements in its non-volatility risk factors captured by SBM curvature; *(L.N. 167 of 2023)*

SBM delta (SBM得爾塔) means a first order sensitivity to capture the changes in the value of an authorized institution's position due to movements in its non-volatility risk factors; *(L.N. 167 of 2023)*

SBM delta risk (SBM得爾塔風險) means the risk of changes in the value of an authorized institution's position due to movements in its non-volatility risk factors captured by SBM delta; *(L.N. 167 of 2023)*

SBM vega (SBM維加) means a first order sensitivity to capture the changes in the value of an authorized institution's position due to movements in its volatility risk factors; *(L.N. 167 of 2023)*

SBM vega risk (SBM維加風險) means the risk of changes in the value of an authorized institution's position due to movements in its volatility risk factors captured by SBM vega; *(L.N. 167 of 2023)*

sensitivities-based method (敏感度基準方法) means a component of the STM approach to capture SBM delta risks, SMB vega risks and SBM curvature risks, within a particular risk class under Division 1B; *(L.N. 167 of 2023)*

simplified approach (簡化計算法), in relation to the calculation of an authorized institution's market risk capital charge for its option exposures to debt securities, interest rates, equities, foreign exchange (including gold) and commodities, means the approach set out in Division 8;

special purpose entity (特定目的實體), in relation to an authorized institution's CTP, means a company, trust or other entity— *(L.N. 167 of 2023)*

(a) organized for a specific purpose;

(b) the activities of which are limited to those appropriate to accomplish that purpose; and

(c) the structure of which is intended to isolate the obligations of the company, trust or other entity, as the case may be, from the credit risk of an originator or a seller of exposures; *(L.N. 137 of 2011)*

specific risk (特定風險), in relation to an authorized institution, means—

(a) the risk of loss, arising from changes in the price of debt securities owing to factors relating to the issuers of the debt securities, in the value of the institution's trading book positions held in the debt securities;

(b) the risk of loss, arising from changes in the price of equities owing to factors relating to the issuers of the equities, in the value of the institution's trading book positions held in the equities;

(c) the risk of loss, arising from changes in the price of debt-related derivative contracts owing to factors relating to the issuers of the underlying debt securities, in the value of the institution's trading book positions held in the debt-related derivative contracts; and

(d) the risk of loss, arising from changes in the price of equity-related derivative contracts owing to factors relating to the issuers of the underlying equities, in the value of the institution's trading book positions held in the equity-related derivative contracts;

specific risk-free security (無特定風險證券) means a hypothetical debt security, free of specific risk, used for the calculation of the market risk capital charge for general market risk relating to derivative contracts;

specific risk interest rate exposures (特定風險利率風險承擔), in relation to an authorized institution, means the interest rate exposures of the institution that are subject to market risk capital charge for specific risk; *(L.N. 137 of 2011)*

standardized default risk charge (標準違責風險資本要求) means a component of the STM approach to capture jump-to-default risk for credit instruments and equity instruments under Division 1D; *(L.N. 167 of 2023)*

stress scenario capital charge (壓力情況資本要求), in relation to an authorized institution, means the market risk capital charge for an NMRF calculated by the institution under the IMA with model inputs calibrated to a relevant continuous 12-month period of significant financial stress; *(L.N. 167 of 2023)*

stressed ES (受壓ES), in relation to a portfolio of exposures held by an authorized institution, means an ES calculated by the institution under the IMA with model inputs calibrated to historical data from a stressed ES relevant period; *(L.N. 167 of 2023)*

stressed ES relevant period (受壓ES有關期間), in relation to a portfolio of exposures held by an authorized institution, means a continuous 12-month period of significant financial stress for which the portfolio experienced the largest loss since at least 2007; *(L.N. 167 of 2023)*

transitional period (securitization) (過渡期(證券化)) means the period from and including 1 January 2012 to and including 31 December 2013; *(L.N. 137 of 2011)*

two-way market (雙向市場) means a market where there are independent bona fide offers to buy or sell such that—

(a) a price reasonably related to the last sales price or current bona fide competitive bid and offer quotations can be determined within one business day; and

(b) transactions can be settled at such price within a relatively short time in accordance with trade custom; *(L.N. 137 of 2011)*

underlying exposure (基礎風險承擔), in relation to a derivative contract (including a credit derivative contract) for the calculation of an authorized institution's market risk, means the underlying asset, index, financial instrument, rate or thing as designated in the derivative contract;

vega (維加), in relation to the calculation of an authorized institution's market risk capital charge for an option contract under the SSTM approach, means a measure of the rate of change in the value of the option contract to changes in the volatility of the value of the underlying exposure of the option contract. *(L.N. 167 of 2023)*

(L.N. 137 of 2011; L.N. 167 of 2023)

281A. Banking book

(1) Subject to subsections (2) and (4), an authorized institution must assign the following instruments to its banking book—

(a) unlisted equities;

(b) instruments designated for securitization warehousing;

(c) direct holdings of real estate and derivatives on direct holdings of real estate;

(d) retail and small or medium-sized enterprise credit;

(e) equity investments in a collective investment scheme;

(f) hedge funds;

(g) derivative contracts and collective investment schemes that have instruments of a kind referred to in paragraph (a), (b), (c), (d), (e) or (f) as underlying assets;

(h) instruments held for the purpose of hedging a particular risk of a position in instruments of a kind referred to in paragraph (a), (b), (c), (d), (e), (f) or (g).

(2) Subsection (1)(e) does not apply to a collective investment scheme if—

(a) the institution is able to apply the look-through approach to the scheme; or

(b) the institution obtains daily price quotes for the scheme and has access to the information contained in the scheme's mandate or in the relevant regulations governing the scheme.

(3) The Monetary Authority may, by written notice, require an authorized institution to provide to the Monetary Authority, within the period specified in the notice, evidence that an instrument (other than an instrument of a kind referred to in subsection (1)) assigned to the institution's banking book is not held for a purpose referred to in section 281B(1).

(4) If—

(a) the institution does not, within the period specified in a notice under subsection (3), provide sufficient evidence to satisfy the Monetary Authority that the instrument is not held for a purpose referred to in section 281B(1); or

(b) the Monetary Authority is satisfied that the instrument customarily belongs to the trading book,

the Monetary Authority may, by written notice, require the institution to assign the instrument to the institution's trading book within the period specified in the notice.

(L.N. 167 of 2023)

281B. Trading book

(1) Subject to subsection (6)(a) and section 281A, an authorized

institution must assign to its trading book, on the initial recognition on its books, an instrument that is held for one or more of the following purposes—

(a) short-term resale;

(b) profiting from short-term price movements;

(c) locking in arbitrage profits;

(d) hedging risks that arise from an instrument held for one or more purposes referred to in paragraphs (a), (b) and (c).

(2) Subject to subsection (6)(a) and section 281A, and without limiting subsection (1), the following instruments are taken to be held for a purpose referred to in subsection (1) and must be assigned to the trading book—

(a) instruments in the institution's CTP;

(b) instruments that would give rise to a net short credit or equity position in the institution's banking book;

(c) instruments resulting from securities underwriting commitments relating only to securities that are expected to be actually purchased by the institution on the settlement date.

(3) Subject to subsections (4) and (6)(a) and section 281A, and without limiting subsection (1), the following instruments are taken to be held for a purpose referred to in subsection (1) and must be assigned to the trading book—

(a) instruments held as accounting trading assets or liabilities;

(b) instruments resulting from market making activities;

(c) equity investments in a collective investment scheme to which section 281A(1)(e) does not apply because of section 281A(2);

(d) listed equities;

(e) trading-related repo-style transactions;

(f) options (including embedded derivatives from instruments that the institution issued out of its banking book and that relate to credit risk or equity risk),

unless the Monetary Authority gives written approval under subsection (4) for the institution to assign the instrument to its banking book.

(4) An authorized institution may assign an instrument referred to in subsection (3) to its banking book if—

(a) the institution submits a written request to the Monetary Authority and provides evidence that the instrument is not held for a purpose referred to in subsection (1); and

(b) the Monetary Authority gives written approval to the institution to assign the instrument to its banking book.

(5) The institution must keep a record of an approval under subsection (4)(b) and document all the evidence referred to in subsection (4)(a).

(6) An authorized institution—

(a) must not assign an instrument to its trading book if there is any legal impediment to selling or fully hedging it; and

(b) must fair value daily each instrument assigned to its trading book and recognize any valuation change in its profit and loss account.

(7) The Monetary Authority may, by written notice, require an authorized institution to provide to the Monetary Authority, within the period specified in the notice, evidence that an instrument (other than an instrument of a kind referred to in subsection (2)) assigned to the institution's trading book is held for a purpose referred to in subsection (1).

(8) If—

(a) the institution does not, within the period specified in a notice under subsection (7), provide sufficient evidence to satisfy the Monetary Authority that the instrument is held for a purpose referred to in subsection (1); or

(b) the Monetary Authority is satisfied that the instrument customarily belongs to the banking book,

the Monetary Authority may, by written notice, require the institution to assign the instrument to the institution's banking book within the period specified in the notice.

(9) An authorized institution—

(a) must have clearly defined policies, procedures and documented practices for determining which instruments are to be included in or excluded from its trading book;

(b) must have effective internal controls to ensure that all instruments are properly assigned initially to its trading book or banking book;

(c) must keep comprehensive records to demonstrate its compliance with the policies and procedures referred to in paragraph (a); and

(d) must conduct by its internal auditors, at least annually, an independent review or audit of its compliance with the policies and procedures referred to in paragraph (a).

(10) In this section—

embedded derivative (嵌入式衍生工具) means an instrument referred to in paragraph (b) of the definition of ***derivative contract*** in section 2(1).

(L.N. 167 of 2023)

281C. Restriction on moving instruments between books

(1) Subject to sections 281A and 281B, an authorized institution must not move an instrument between its banking book and trading book after its initial assignment unless—

(a) the instrument is reclassified as an accounting trading asset or liability (in which case there is a presumption that the instrument is in the trading book, as required by section 281B(3)(a)); or

(b) the Monetary Authority, on the application of the institution, gives written approval for the instrument to be moved.

(2) The Monetary Authority may give approval under subsection (1)(b) only if satisfied that there are extraordinary circumstances.

(3) If an authorized institution moves an instrument between its banking book and trading book in accordance with this section, it must, after the move—

(a) determine whether the total capital charge across its banking book and trading book is reduced by the move; and

(b) if so, impose the reduced amount as a fixed market risk capital surcharge, to run off in a manner agreed with the Monetary Authority as the position matures or expires.

(4) An authorized institution—

(a) must have policies in place in relation to the moving of instruments between its banking book and trading book;

(b) must review and, if necessary, based on an analysis of all extraordinary circumstances referred to in subsection (2), update those policies annually; and

(c) must give written notice to the Monetary Authority of any changes to those policies.

(L.N. 167 of 2023)

281D. Treatment of internal risk transfers

(1) An authorized institution may recognize an internal risk transfer in any of the circumstances set out in this section for the purpose of calculating its market risk capital charge.

(2) The institution may recognize an internal risk transfer from its banking book to its trading book that aims to hedge a credit risk exposure in the banking book if it fulfils the requirements of section 99B or 213, as the case requires.

(3) The institution may recognize an internal risk transfer from its banking book to its trading book that aims to hedge a GIRR exposure in the banking book if—

(a) the institution documents the internal risk transfer with respect to the interest rate risk being hedged and the sources of the risk;

(b) the institution conducts the internal risk transfer with a dedicated trading desk that obtains the approval of the Monetary Authority and—

(i) obtains an external hedge directly from an external counterparty; or

(ii) obtains an external hedge from the market via a separate non-internal risk transfer trading desk acting as an agent and that transfer exactly matches an external hedge obtained from an external counterparty; and

(c) the institution calculates the market risk capital charge for the dedicated trading desk on a standalone basis.

(L.N. 167 of 2023)

281E. Positions to be used to calculate market risk capital charge

(1) Subject to subsections (2) and (3), an authorized institution

must calculate its market risk capital charge for—

(a) the institution's trading book positions; and

(b) the foreign exchange risk, and commodity risk, of the institution's banking book positions.

(2) An authorized institution must not include a position in the calculation of its market risk capital charge if the position is—

(a) the banking book leg of an eligible internal risk transfer;

(b) an exposure that, under Division 4 of Part 3, is required to be deducted from any of the institution's CET1 capital, Additional Tier 1 capital or Tier 2 capital; or

(c) an eligible CVA hedge obtained from an external counterparty or the CVA leg of an eligible CVA hedge obtained from its trading book internally.

(3) An authorized institution may exclude a foreign exchange risk position from the calculation of its market risk capital charge for its foreign exchange risk if—

(a) the position is taken or maintained by the institution for the purpose of hedging partially or totally against any adverse effect of exchange rate movements on its capital adequacy ratio;

(b) the position is of a structural (that is, non-dealing) nature;

(c) the institution's risk management policy for structural foreign exchange positions is approved by the Monetary Authority;

(d) the establishment of, and any changes to, the position follow the policy referred to in paragraph (c);

(e) the exclusion is limited to the amount of the position that neutralizes the sensitivity of the capital adequacy ratio to movements in exchange rates;

(f) the exclusion is made for at least 6 months;

(g) the institution applies the exclusion consistently, with the exclusion treatment of the hedge remaining in place for the life of the assets or other items to which the position relates; and

(h) the institution keeps comprehensive records of the position and the amount excluded from the market risk capital charge.

(4) If a position of an authorized institution does not fall within subsection (1) because of subsection (2)(a) or (b), the institution must apply Part 4, 5, 6 or 7, as the case requires, to calculate the credit risk for that position.

(L.N. 167 of 2023)

Division 1A—Calculation of Market Risk Capital Charge under STM Approach: General

(Division 1A added L.N. 167 of 2023)

281F. Application of Divisions 1A to 1D

(1) Divisions 1A, 1B, 1C and 1D apply to an authorized institution that uses the STM approach to calculate its market risk capital charge.

(2) A reference to an authorized institution in Divisions 1A, 1B, 1C and 1D is a reference to an authorized institution that uses the STM approach to calculate its market risk capital charge.

281G. Calculation of market risk capital charge and risk-weighted amount for market risk

(1) An authorized institution must calculate its market risk capital charge as the sum of—

(a) the ultimate SBM capital charge under section 281H(2);

(b) the RRAO under section 281R; and

(c) the SA-DRC under section 281S.

(2) An authorized institution must calculate its risk-weighted amount for market risk by multiplying the market risk capital charge as calculated under subsection (1) by 12.5.

Division 1B—Calculation of Market Risk Capital Charge under STM Approach: SBM Capital Charge

(Division 1B added L.N. 167 of 2023)

281H. Calculation of SBM capital charge

(1) An authorized institution must calculate its SBM capital charge for each of the 3 correlation scenarios set out in section 281L as the sum of the following capital charges for each risk class—

(a) the SBM delta risk capital charge under section 281I;

(b) the SBM vega risk capital charge under section 281J;

(c) the SBM curvature risk capital charge under section 281K.

(2) An authorized institution's ultimate SBM capital charge is the SBM capital charge that is the largest of the SBM capital charges calculated under subsection (1) for the 3 correlation scenarios.

(3) An authorized institution must calculate the SBM delta risk capital charge for all instruments in the respective portfolios included in the calculation except for any position for which the value at any point in time is purely driven by an exotic

underlying and that is subject to the RRAO in accordance with section 281R(1)(a).

(4) An authorized institution must calculate the SBM vega risk capital charge for—

(a) any instrument with optionality; and

(b) any instrument the cashflows of which cannot be written as a linear function of the underlying notional amount,

except for any position for which the value at any point in time is purely driven by an exotic underlying and that is subject to the RRAO in accordance with section 281R(1)(a).

(5) An authorized institution must calculate the SBM curvature risk capital charge consistently over time—

(a) for—

(i) any instrument with optionality; and

(ii) any instrument the cashflows of which cannot be written as a linear function of the underlying notional amount,

except for any position for which the value at any point in time is purely driven by an exotic underlying and that is subject to the RRAO in accordance with section 281R(1)(a); or

(b) for all instruments subject to SBM delta risk capital charge except for any position—

(i) for which the value at any point in time is purely driven by an exotic underlying; and

(ii) that is subject to the RRAO in accordance with section 281R(1)(a).

(6) In this section—

instrument with optionality (包含選擇權的工具) means an option contract or an instrument that includes an option component.

281I. Calculation of SBM delta risk capital charge

(1) An authorized institution must calculate its SBM delta risk capital charge separately for each risk class in accordance with this section.

(2) For each risk class, the institution must—

(a) subject to subsection (3), calculate an SBM delta sensitivity $delta_{k,i}$ for each instrument i subject to each SBM delta risk factor k (as defined under section 281M(2)(a)) in accordance with Formula 27M;

Formula 27M

Calculation of SBM Delta Sensitivity

$$delta_{k,i} = \frac{V_i(k + 0.0001) - V_i(k)}{0.0001}$$

for GIRR, credit spread risk (non-securitization), credit spread risk (securitization: non-CTP), credit spread risk (securitization: CTP) and equity repo rate risk factors; or

$$delta_{k,i} = \frac{V_i(1.01k) - V_i(k)}{0.01}$$

for equity price risk, commodity risk and foreign exchange risk factors,

where—

(i) $delta_{k,i}$ is the SBM delta sensitivity for instrument i with respect to SBM delta risk factor k; and

(ii) $V_i(k)$ is the value of instrument i as a function of SBM delta risk factor k.

(b) calculate the net sensitivity s_k for each SBM delta risk factor by netting all SBM delta sensitivities across all instruments in the risk class in accordance with Formula 27N;

Formula 27N

Calculation of Net Sensitivity

$$s_k = \sum_i delta_{k,i}$$

where—

(i) $delta_{k,i}$ is the SBM delta sensitivity for instrument i with respect to SBM delta risk factor k; and

(ii) s_k is the net sensitivity across all instruments for SBM delta risk factor k.

(c) calculate the risk-weighted sensitivity WS_k as the product of the net sensitivity s_k and the risk-weight RW_k (as allocated under section 281O(1));

(d) calculate the capital charge for each SBM delta bucket b, K_b, by aggregating the risk-weighted sensitivities in the same bucket, using the correlation parameters ρ_{kl}

depending on the correlation scenarios set out in section 281L, in accordance with Formula 27O; and

Formula 27O

Calculation of Capital Charge for SBM Delta Bucket

$$K_b = \sqrt{\max\left(\sum_k WS_k^2 + \sum_k \sum_{l \neq k} \rho_{kl} WS_k \, WS_l \, , 0\right)}$$

where—

(i) K_b is the capital charge for SBM delta bucket b;

(ii) k and l are SBM delta risk factors;

(iii) ρ_{kl} is the correlation parameter for SBM delta risk factors k and l referred to in section 281O(2)(a); and

(iv) WS_k and WS_l are the risk-weighted sensitivities calculated under paragraph (c).

(e) subject to subsection (4), calculate the SBM delta risk capital charge by aggregating the capital charges calculated under paragraph (d) for each of the SBM delta buckets in the risk class, using the correlation parameters γ_{bc} depending on the correlation scenarios set out in section 281L, in accordance with Formula 27P.

Formula 27P

Calculation of SBM Delta Risk Capital Charge

$$\text{SBM delta risk capital charge} = \sqrt{\sum_{b} K_b^2 + \sum_{b}\sum_{c\neq b} \gamma_{bc} S_b S_c}$$

where—

(i) $S_b = \sum_k WS_k$ for all SBM delta risk factors in SBM delta bucket b;

(ii) $S_c = \sum_k WS_k$ for all SBM delta risk factors in SBM delta bucket c;

(iii) K_b is the capital charge for SBM delta bucket b;

(iv) γ_{bc} is the correlation parameter for SBM delta buckets b and c referred to in section 281O(2)(b); and

(v) WS_k is the risk-weighted sensitivity calculated under paragraph (c).

(3) The institution may determine an SBM delta sensitivity by another formulation if the institution demonstrates to the satisfaction of the Monetary Authority that the other formulation is conceptually sound and yields results very close to Formula 27M.

(4) If the values of S_b and S_c calculated under subsection (2)(e) produce a negative number for the overall sum of $\Sigma_b K_b^2 + \Sigma_b \Sigma_{c\neq b} \gamma_{bc} S_b S_c$, the institution must calculate the SBM delta risk capital charge using an alternative specification in which—

(a) $S_b = \max[\min(\sum_k WS_k, K_b), -K_b]$ for all SBM delta risk factors in SBM delta bucket b; and

(b) $S_c = \max[\min(\sum_k WS_k, K_c), -K_c]$ for all SBM delta risk factors in SBM delta bucket c.

281J. Calculation of SBM vega risk capital charge

(1) An authorized institution must calculate its SBM vega risk capital charge separately for each risk class in accordance with this section.

(2) For each risk class, the institution must—

(a) subject to subsection (3), determine an SBM vega sensitivity $vega_{k,i}$ for each instrument i subject to each SBM vega risk factor k (as defined under section 281M(2)(b)) in accordance with Formula 27Q;

Formula 27Q

Calculation of SBM Vega Sensitivity

$$vega_{k,i} = \frac{\partial V_i}{\partial k} \times k$$

where—

(i) $vega_{k,i}$ is the SBM vega sensitivity for instrument i with respect to SBM vega risk factor k; and

(ii) $\frac{\partial Vi}{\partial k}$ is the change in value V_i of instrument i as a result of a small amount of change to k.

(b) calculate the net sensitivity s_k for each SBM vega risk factor by netting all SBM vega sensitivities across all instruments in the risk class in accordance with Formula 27R;

Formula 27R

Calculation of Net Sensitivity

$$s_k = \sum_i vega_{k,i}$$

where—

(i) s_k is the net sensitivity across all instruments for SBM vega risk factor k; and

(ii) $vega_{k,i}$ is the SBM vega sensitivity for instrument i with respect to SBM vega risk factor k.

(c) calculate the risk-weighted sensitivity WS_k as the product of the net sensitivity s_k and the risk-weight RW_k (as allocated under section 281P(1));

(d) calculate the capital charge for each SBM vega bucket b, K_b, by aggregating the risk-weighted sensitivities in the same bucket, using the correlation parameters ρ_{kl} depending on the correlation scenarios set out in section 281L, in accordance with Formula 27S; and

Formula 27S

Calculation of Capital Charge for SBM Vega Bucket

$$K_b = \sqrt{\max\left(\sum_k WS_k^2 + \sum_k \sum_{l \neq k} \rho_{kl} WS_k \, WS_l \, , 0\right)}$$

where—

(i) K_b is the capital charge for SBM vega bucket b;

(ii) k and l are SBM vega risk factors;

(iii) ρ_{kl} is the correlation parameter for SBM vega risk factors k and l referred to in section 281P(2)(a); and

(iv) WS_k and WS_l are the risk-weighted sensitivities calculated under paragraph (c).

(e) subject to subsection (4), calculate the SBM vega risk capital charge by aggregating the capital charges calculated under paragraph (d) for each of the SBM vega buckets in the risk class, using the correlation parameters γ_{bc} depending on the correlation scenarios set out in section 281L, in accordance with Formula 27T.

Formula 27T

Calculation of SBM Vega Risk Capital Charge

$$\text{SBM vega risk capital charge} = \sqrt{\sum_b K_b^2 + \sum_b \sum_{c \neq b} \gamma_{bc} S_b S_c}$$

where—

(i) $S_b = \sum_k WS_k$ for all SBM vega risk factors in SBM vega bucket b;

(ii) $S_c = \sum_k WS_k$ for all SBM vega risk factors in SBM vega bucket c;

(iii) K_b is the capital charge for SBM vega bucket b;

(iv) γ_{bc} is the correlation parameter for SBM vega buckets b and c referred to in section 281P(2)(b); and

(v) WS_k is the risk-weighted sensitivity calculated under paragraph (c).

(3) The institution may determine an SBM vega sensitivity by another formulation if the institution demonstrates to the satisfaction of the Monetary Authority that the other formulation is conceptually sound and yields results very close to Formula 27Q.

(4) If the values of S_b and S_c calculated under subsection (2)(e) produce a negative number for the overall sum of $\sum_b K_b^2 + \sum_b \sum_{c \neq b} \gamma_{bc} S_b S_c$, the institution must calculate the SBM vega risk capital charge using an alternative specification in which—

(a) $S_b = \max[\min(\sum_k WS_k, K_b), -K_b]$ for all SBM vega risk factors in SBM vega bucket b; and

(b) $S_c = \max[\min(\sum_k WS_k, K_c), -K_c]$ for all SBM vega risk factors in SBM vega bucket c.

281K. Calculation of SBM curvature risk capital charge

(1) An authorized institution must calculate its SBM curvature risk capital charge separately for each risk class in accordance with this section.

(2) For each risk class, the institution must—

(a) subject to subsection (3), apply an upward shock to calculate CVR_k^+ and apply a downward shock to calculate CVR_k^- to each instrument i subject to the SBM curvature risk associated with each SBM curvature risk factor k (as defined under section 281M(2)(c)) in accordance with Formula 27U;

Formula 27U

Calculation of CVR_k^+ and CVR_k^-

$$CVR_k^+ = -\sum_i \left\{ \begin{matrix} V_i\left(x_k^{RW(Curvature)^+}\right) - \\ V_i(x_k) - RW_k^{Curvature} \cdot s_{ik} \end{matrix} \right\}$$

$$CVR_k^- = -\sum_i \left\{ \begin{matrix} V_i\left(x_k^{RW(Curvature)^-}\right) - \\ V_i(x_k) + RW_k^{Curvature} \cdot s_{ik} \end{matrix} \right\}$$

where—

(i) CVR_k^+ is the incremental loss beyond the SBM delta risk capital charge across all instruments by applying an upward shock to the SBM curvature risk factor k;

(ii) CVR_k^- is the incremental loss beyond the SBM delta risk capital charge across all instruments by applying a downward shock to the SBM curvature risk factor k;

(iii) $RW_k^{Curvature}$ is the risk-weight for SBM curvature risk factor k as allocated under section 281Q(1);

(iv) s_{ik} is—

(A) for equity risk and foreign exchange risk—the SBM delta sensitivity of instrument i with respect to the SBM delta risk factor that corresponds to SBM curvature risk factor k; or

(B) for any other risk class—the sum of SBM delta sensitivities to all tenors of the relevant curve or curves of instrument i with respect to SBM curvature risk factor k;

(v) $V_i(x_k)$ is the value of instrument i depending on x_k;

(vi) $V_i(x_k^{RW(Curvature)^+})$ is the value of instrument i after x_k is shocked upward;

(vii) $V_i(x_k^{RW(Curvature)^-})$ is the value of instrument i after x_k is shocked downward; and

(viii) x_k is the current level of SBM curvature risk factor k.

(b) calculate the capital charge for each SBM curvature bucket b, K_b, using the correlation parameters ρ_{kl} depending on the correlation scenarios set out in section 281L, in accordance with Formula 27V; and

Formula 27V

Calculation of Capital Charge for SBM Curvature Bucket

$$K_b = \max(K_b^+, K_b^-)$$

$$\text{where} \begin{cases} K_b^+ = \sqrt{\max\left(0, \sum_k \max(CVR_k^+, 0)^2 + \sum_k \sum_{l \neq k} \rho_{kl} CVR_k^+ CVR_l^+ \psi(CVR_k^+, CVR_l^+)\right)} \\ K_b^- = \sqrt{\max\left(0, \sum_k \max(CVR_k^-, 0)^2 + \sum_k \sum_{l \neq k} \rho_{kl} CVR_k^- CVR_l^- \psi(CVR_k^-, CVR_l^-)\right)} \end{cases}$$

where—

(i) K_b is the capital charge for SBM curvature bucket b and is determined as the greater of K_b^+ and K_b^-, where—

(A) the upward scenario is selected if $K_b = K_b^+$;

(B) the downward scenario is selected if $K_b = K_b^-$; and

(C) if $K_b^+ = K_b^-$, the upward scenario is selected if $\sum_k CVR_k^+$ is greater than $\sum_k CVR_k^-$, otherwise the downward scenario is selected;

(ii) CVR_k^+ and CVR_l^+ are the incremental loss beyond the SBM delta risk capital charge across all instruments by applying an upward shock to the SBM curvature risk factors k and l respectively;

(iii) CVR_k^- and CVR_l^- are the incremental loss beyond the SBM delta risk capital charge across all instruments by applying a downward shock to the SBM curvature risk factors k and l respectively;

(iv) K_b^+ is the capital charge for SBM curvature bucket b under the upward scenario;

(v) K_b^- is the capital charge for SBM curvature bucket b under the downward scenario;

(vi) ρ_{kl} is the correlation parameter for SBM curvature risk factors k and l referred to in section 281Q(2)(a);

(vii) $\psi(CVR_k^+, CVR_l^+)$ is—

(A) zero, if both CVR_k^+ and CVR_l^+ have negative signs; or

(B) one, in any other case; and

(viii) $\psi(\mathrm{CVR}_k^-, \mathrm{CVR}_l^-)$ is—

(A) zero, if both CVR_k^- and CVR_l^- have negative signs; or

(B) one, in any other case.

(c) calculate the SBM curvature risk capital charge by aggregating the capital charges calculated under paragraph (b) for each of the SBM curvature buckets in the risk class, using the correlation parameters γ_{bc} depending on the correlation scenarios set out in section 281L, in accordance with Formula 27W.

Formula 27W

Calculation of SBM Curvature Risk Capital Charge

SBM curvature risk capital charge =

$$\sqrt{\max\left(0, \sum_b K_b^2 + \sum_b \sum_{c \neq b} \gamma_{bc} S_b\, S_c \psi(S_b, S_c)\right)}$$

where—

(i) S_b =

(A) $\sum_k CVR_k^+$ for all SBM curvature risk factors in SBM curvature bucket b if the upward scenario has been selected for SBM curvature bucket b; or

(B) $\sum_k CVR_k^-$ for all SBM curvature risk factors in SBM curvature bucket b otherwise;

(ii) S_c =

(A) $\sum_k CVR_k^+$ for all SBM curvature risk factors in SBM curvature bucket c if the upward scenario has been selected for SBM curvature bucket c; or

(B) $\sum_k CVR_k^-$ for all SBM curvature risk factors in SBM curvature bucket c otherwise;

(iii) K_b is the capital charge for SBM curvature bucket b;

(iv) γ_{bc} is the correlation parameter for SBM curvature buckets b and c referred to in section 281Q(2)(b); and

(v) $\psi(S_b, S_c)$ is—

(A) zero, if both S_b and S_c have negative signs; or

(B) one, in any other case.

(3) For the purposes of subsection (2)—

(a) the institution may divide CVR_k^+ and CVR_k^- under foreign exchange risk by 1.5 for any exchange rate-related option contract that does not reference the Hong Kong dollar or the institution’s base currency as an underlying; or

(b) with the approval of the Monetary Authority, the institution may divide CVR_k^+ and CVR_k^- under foreign exchange risk by 1.5 for all foreign exchange instruments if the SBM curvature sensitivities are calculated for all currencies, including sensitivities determined by shocking—

(i) the Hong Kong dollar relative to all other currencies; or

(ii) the institution’s base currency relative to all other currencies.

281L. Correlation scenarios

For the purposes of this Division, the correlation scenarios are—

(a) the medium scenario, in which the correlation parameters ρ_{kl} and γ_{bc} are as referred to in sections 281O(2), 281P(2) and 281Q(2);

(b) the high scenario, in which the correlation parameters ρ_{kl}^{high} and γ_{bc}^{high} are determined by multiplying ρ_{kl} and γ_{bc} under the medium scenario by 1.25, subject to a cap of 100%; and

(c) the low scenario, in which the correlation parameters ρ_{kl}^{low} and γ_{bc}^{low} are determined in accordance with Formula 27X.

Formula 27X

Calculation of Low Scenario Correlation Parameters

$$\rho_{kl}^{low} = \max(2 \cdot \rho_{kl} - 100\%, 75\% \cdot \rho_{kl})$$

$$\gamma_{kl}^{low} = \max(2 \cdot \gamma_{bc} - 100\%, 75\% \cdot \gamma_{bc})$$

where—

(i) ρ_{kl} is the correlation parameter ρ_{kl} under the medium scenario; and

(ii) γ_{bc} is the correlation parameter γ_{bc} under the medium scenario.

281M. SBM risk factors

(1) An authorized institution must, in respect of a risk class—

(a) determine buckets as specified by the Monetary Authority for the risk class that appropriately distinguish the risk characteristics of risk factors across different buckets; and

(b) allocate each risk-weighted sensitivity calculated under section 281I(2)(c) and 281J(2)(c) and each CVR_k^+ and CVR_k^- calculated under section 281K(2)(a) to an appropriate bucket.

(2) Depending on the positions held, an authorized institution must—

(a) define the SBM delta risk factors, at a level of granularity specified by the Monetary Authority, as—

(i) risk-free interest rates, market-implied inflation rates and cross-currency basis for GIRR;

(ii) credit spreads for credit spread risk (non-securitization), credit spread risk (securitization: non-CTP) and credit spread risk (securitization: CTP);

(iii) equity prices and equity repo rates for equity risk;

(iv) commodity prices for commodity risk; and

(v) foreign exchange rates between the Hong Kong dollar and each foreign currency or, with the approval of the Monetary Authority, the exchange rates between a base currency other than the Hong Kong dollar and each foreign currency;

(b) define the SBM vega risk factors, at a level of granularity specified by the Monetary Authority, as implied volatilities of the underlying exposure; and

(c) define the SBM curvature risk factors, at a level of granularity specified by the Monetary Authority, as—

(i) risk-free interest rates for GIRR;

(ii) credit spreads for credit spread risk (non-securitization), credit spread risk (securitization: non-CTP) and credit spread risk (securitization: CTP);

(iii) equity prices for equity risk;

(iv) commodity prices for commodity risk; and

(v) foreign exchange rates between the Hong Kong dollar and each foreign currency or, with the approval of the Monetary Authority, the exchange rates between a base currency other than the Hong Kong dollar and each foreign currency.

281N. Instruments with multiple constituents

(1) Subject to subsections (2), (4), (5) and (7), an authorized

institution must apply the look-through approach to calculate the SBM delta risk capital charge and the SBM curvature risk capital charge for any—

(a) index instruments;

(b) multi-underlying options; and

(c) equity investments in a collective investment scheme.

(2) Subject to subsection (7), an authorized institution may opt not to apply the look-through approach under subsection (1), but instead may calculate a single sensitivity for SBM delta and SBM curvature with respect to each index that an instrument references or a collective investment scheme tracks, for any—

(a) index instrument that references a qualified index;

(b) index instrument referred to in paragraph (a) that is held by a collective investment scheme in respect of which the institution can apply the look-through approach; or

(c) collective investment scheme that can be looked through and tracks a qualified index if—

(i) the scheme has an absolute value of a tracking difference (ignoring fees and commissions) of less than 1%; and

(ii) the tracking difference is checked at least annually.

(3) If an authorized institution opts to calculate a single sensitivity for a qualified index under subsection (2), the institution must assign the sensitivity to—

(a) an appropriate sector-specific bucket if more than 75% of the constituents in the qualified index (taking into account their weightings in that index) would be mapped to a specific sector; or

(b) an appropriate non-sector-specific index bucket otherwise.

(4) An authorized institution must not break an index CTP instrument down into its constituents but must consider the index CTP a risk factor as a whole.

(5) An authorized institution may opt not to apply the look-through approach under subsection (1) for an equity investment in a collective investment scheme that cannot be looked through and for which the institution has access to daily price quotes and the information contained in the mandate of the scheme or in the relevant regulations governing the scheme, but instead—

(a) may assume that the scheme is a position in a tracked index and assign the sensitivity for the tracked index to relevant sector-specific buckets or non-sector-specific index buckets as set out in subsection (3), if—

(i) the scheme tracks a qualified index;

(ii) the scheme has an absolute value of a tracking difference (ignoring fees and commissions) of less than 1%; and

(iii) the tracking difference is checked at least annually;

(b) with the approval of the Monetary Authority, may calculate on a standalone basis the capital charge of a hypothetical portfolio in which the scheme invests, to the maximum possible extent allowed under its mandate, in assets attracting the highest risk-weight and then progressively in other assets attracting a lower risk-weight; or

(c) subject to sections 281R(4) and 281S(5), may treat the scheme as an unrated equity exposure and assign it to “other sectors” under the sector classification.

(6) An authorized institution must exclude any net short position in a collective investment scheme from other positions subject to the market risk capital charge and subject the net short position to a 100% capital charge if—

(a) the scheme cannot be looked through; and

(b) the institution cannot access daily price quotes and the information contained in the mandate of the scheme or in the relevant regulations governing the scheme.

(7) If an authorized institution has applied the look-through approach under subsection (1) to instruments with an identical underlying, the institution must not opt to use the approach referred to in subsection (2) in relation to the instruments except with the approval of the Monetary Authority.

(8) An authorized institution may determine the SBM vega risk factor for a multi-underlying option as the implied volatility of the option rather than the implied volatility of its underlying constituents and, if so, must assign the SBM vega sensitivity to—

(a) an appropriate sector-specific bucket if more than 75% of the constituents (taking into account their weightings in the option) would be mapped to a specific sector; or

(b) an appropriate non-sector-specific index bucket otherwise.

(9) In this section—

qualified index (合資格指數), in relation to the calculation of the market risk capital charge for instruments with multiple constituents, means an exchange-traded and widely recognized and accepted equity or credit index where—

(a) the constituents of the index and their respective weightings are known;

(b) the index contains at least 20 constituents;

(c) no single constituent represents more than 25% of the total index;

(d) the largest 10% of the constituents represents less than 60% of the total index; and

(e) the total market capitalization of all the constituents is no less than $312 billion;

tracking difference (追縱差異), in relation to a collective investment scheme, means the annualized return difference between the scheme and its tracked benchmark over the last 12 months of available data (or a shorter period in the absence of a full 12 months of data).

281O. SBM delta risk-weights and correlation parameters

(1) An authorized institution must allocate a risk-weight to each SBM delta risk factor at a level specified by the Monetary Authority that sufficiently represents stressed market conditions.

(2) An authorized institution—

(a) for the purpose of aggregating SBM delta risk-weighted sensitivities within the same bucket, must use the correlation parameters ρ_{kl} specified by the Monetary Authority that appropriately recognize a degree of diversification benefit within the bucket; and

(b) for the purpose of aggregating SBM delta risk capital charges across buckets within the same risk class, must use the correlation parameters γ_{bc} specified by the Monetary Authority that appropriately recognize a degree of diversification benefit across the buckets.

281P. SBM vega risk-weights and correlation parameters

(1) An authorized institution must allocate a risk-weight to each SBM vega risk factor at a level specified by the Monetary

Authority that sufficiently represents stressed market conditions.

(2) An authorized institution—

(a) for the purpose of aggregating SBM vega risk-weighted sensitivities within the same bucket, must use the correlation parameters ρ_{kl} specified by the Monetary Authority that appropriately recognize a degree of diversification benefit within the bucket; and

(b) for the purpose of aggregating SBM vega risk capital charges across buckets within the same risk class, must use the correlation parameters γ_{bc} specified by the Monetary Authority that appropriately recognize a degree of diversification benefit across the buckets.

281Q. SBM curvature risk-weights and correlation parameters

(1) An authorized institution must allocate a risk-weight to each SBM curvature risk factor at a level specified by the Monetary Authority that sufficiently represents stressed market conditions.

(2) An authorized institution—

(a) for the purpose of aggregating SBM curvature risk-weighted sensitivities within the same bucket, must use the correlation parameters ρ_{kl} specified by the Monetary Authority that appropriately recognize a degree of diversification benefit within the bucket; and

(b) for the purpose of aggregating SBM curvature risk capital charges across buckets within the same risk class, must use the correlation parameters γ_{bc} specified by the Monetary Authority that appropriately recognize a degree of diversification benefit across the buckets.

Division 1C—Calculation of Market Risk Capital Charge

under STM Approach: RRAO

(Division 1C added L.N. 167 of 2023)

281R. Calculation of RRAO

(1) Subject to subsections (2) and (3), an authorized institution must calculate the RRAO for any instrument in its trading book—

(a) with an exotic underlying, if the risk profile of the underlying exposure of the instrument is not captured by the SBM or SA-DRC; or

(b) bearing other residual risks, if—

(i) the instrument is subject to SBM vega risk capital charges or SBM curvature risk capital charges in the trading book and with pay-offs that cannot be written or perfectly replicated as a finite linear combination of vanilla options with a single underlying equity price, commodity price, exchange rate, bond price, credit default swap price or interest rate swap; or

(ii) the instrument is in the institution's CTP and is not recognized as an eligible hedge of risks within the CTP.

(2) The institution is not required to calculate the RRAO for an instrument that is a back-to-back transaction that exactly matches with a third-party transaction in the trading book and, in that case, both the back-to-back transaction and the third-party transaction may be excluded from the institution's RRAO.

(3) The institution is not required to calculate the RRAO for an instrument that bears other residual risks as referred to in subsection (1)(b), if the instrument—

(a) is listed on an exchange; or

(b) is eligible for central clearing.

(4) If, under section 281N(5)(c), the institution treats an equity investment in a collective investment scheme as an unrated equity exposure and assigns it to "other sectors" under the sector classification, the institution must assume that the scheme is exposed to exotic underlying exposures, and to other residual risks, to the maximum possible extent allowed under the scheme's mandate.

(5) The institution must calculate the RRAO as the sum of the gross (long plus short) notional amounts of the instruments bearing residual risks multiplied by the following risk-weights—

(a) 1.0% for instruments with an exotic underlying;

(b) 0.1% for instruments bearing other residual risks.

Division 1D—Calculation of Market Risk Capital Charge under STM Approach: SA-DRC

(Division 1D added L.N. 167 of 2023)

281S. Calculation of SA-DRC generally

(1) An authorized institution must calculate the SA-DRC for instruments in its trading book as the sum of—

(a) the SA-DRC (non-securitization) under section 281T;

(b) the SA-DRC (securitization: non-CTP) under section 281V; and

(c) the SA-DRC (securitization: CTP) under section 281W.

(2) For the purpose of calculating the SA-DRC—

(a) a long exposure is an exposure for which a default of the underlying obligor results in a loss to the institution; and

(b) a short exposure is an exposure for which a default of the underlying obligor results in a gain to the institution.

(3) For the purpose of calculating the SA-DRC—

(a) the notional amount of a long exposure is to be recorded as a positive value; and

(b) the notional amount of a short exposure is to be recorded as a negative value.

(4) For the purpose of calculating the SA-DRC, the institution must allocate a default risk-weight of 0% to any exposure of the institution to sovereigns, public sector entities and multilateral development banks that would be allocated a 0% risk-weight under the standardized (credit risk) approach set out in sections 55, 56, 57 and 58.

(5) If, under section 281N(5)(c), the institution treats an equity investment in a collective investment scheme as an unrated equity exposure and assigns it to “other sectors” under the sector classification—

(a) the institution—

(i) must treat the equity investment in the scheme as an unrated equity exposure; or

(ii) if the scheme’s mandate allows the scheme to invest primarily in names of certain credit qualities, must apply the maximum default risk-weight as referred to in section 281T(8) that is achievable under the scheme’s mandate and must not offset or aggregate, with correlation, the generated exposure with other exposures; and

(b) the institution must reasonably consider whether, given the scheme's mandate, that default risk-weight is sufficiently prudent.

281T. Calculation of SA-DRC (non-securitization)

(1) Subject to subsection (2), an authorized institution must calculate the SA-DRC (non-securitization) for any non-securitization exposure in its trading book subject to default risk that is a credit instrument or equity instrument.

(2) The institution must exclude from the calculation of the SA-DRC (non-securitization) any non-securitization exposure—

(a) that hedges a CTP instrument; or

(b) that is held for the purpose of offsetting and hedging any non-CTP securitization exposure if that non-securitization exposure together with other exposures is decomposed proportionately into the equivalent replicating tranches that span the entire tranche structure.

(3) The institution must—

(a) include any exposure referred to in subsection (2)(a) in SA-DRC (securitization: CTP); and

(b) include any exposure referred to in subsection (2)(b) in SA-DRC (securitization: non-CTP).

(4) For the purpose of calculating the SA-DRC (non-securitization), the institution must—

(a) calculate the gross jump-to-default risk amount in accordance with section 281U for each instrument referred to in subsection (1);

(b) subject to subsection (5), calculate the net jump-to-default risk amount with respect to each obligor by offsetting the gross jump-to-default risk amounts of long and short exposures with respect to the same obligor;

(c) calculate the risk-weighted net jump-to-default risk amount with respect to an obligor as the product of—

(i) the net jump-to-default risk amount calculated under paragraph (b); and

(ii) the default risk-weights referred to in subsection (8);

(d) allocate the risk-weighted net jump-to-default risk amount to the following buckets according to the nature of the obligor—

(i) corporates;

(ii) sovereigns;

(iii) local governments and municipalities;

(e) calculate the bucket level SA-DRC in accordance with subsection (9); and

(f) calculate the SA-DRC (non-securitization) as the sum of the bucket level SA-DRC for each bucket.

(5) The institution must offset the gross jump-to-default risk amounts of long and short exposures with respect to the same obligor if—

(a) the short exposure has the same or lower seniority relative to the long exposure; and

(b) any of the following applies—

(i) the maturity of both exposures is equal to or longer than one year;

(ii) the maturity of either or both exposures is shorter than one year.

(6) If the maturity of either or both exposures referred to in subsection (5) is shorter than one year, the institution must scale down the gross jump-to-default risk amounts of those

exposures in accordance with section 281U(1)(b) or (2)(b), as the case requires.

(7) The institution may consistently assign to cash equity positions a maturity of either—

(a) more than one year; or

(b) 3 months.

(8) Subject to section 281S(4)—

(a) subject to paragraph (b), the institution must calculate the default risk-weight in accordance with the credit quality of the obligor as set out in Table 27C or, if the obligor is a corporate incorporated in the home jurisdiction of a Type B ECAI, Table 27D; and

(b) if the institution uses the IRB approach to calculate its credit risk for non-securitization exposures, the institution may map the internal rating of an obligor without an ECAI issuer rating to one of the ECAI issuer ratings based on a mapping scheme approved in writing by the Monetary Authority to determine the credit quality for the purpose of calculating the default risk-weight of the obligor under Table 27C or 27D, as the case requires.

Table 27C

Default Risk-Weights Applicable to All Obligors

Column 1	Column 2	Column 3
Item	Credit quality	Default risk-weight
1.	Credit quality grade 1 in the LT ECAI rating mapping table for Type A ECAIs	0.5%
2.	Credit quality grade 2 in the LT ECAI rating mapping table for Type A ECAIs	2%
3.	Credit quality grade 3 in the LT ECAI rating mapping table for Type A ECAIs	3%
4.	Credit quality grade 4 in the LT ECAI rating mapping table for Type A ECAIs	6%
5.	Credit quality grade 5 in the LT ECAI rating mapping table for Type A ECAIs	15%
6.	Credit quality grade 6 in the LT ECAI rating mapping table for Type A ECAIs	30%
7.	Credit quality grade 7 in the LT ECAI rating mapping table for Type A ECAIs	50%
8.	Unrated	15%
9.	Defaulted	100%

Table 27D

Default Risk-Weights Applicable to Obligors that are Corporates Incorporated in Home Jurisdiction of Type B ECAI

Column 1	Column 2	Column 3
Item	Credit quality	Default risk-weight
1.	Credit quality grade 1 in the LT ECAI rating mapping table for Type B ECAIs	0.5%
2.	Credit quality grade 2 in the LT ECAI rating mapping table for Type B ECAIs	2%
3.	Credit quality grade 3 in the LT ECAI rating mapping table for Type B ECAIs	3%
4.	Credit quality grade 4 in the LT ECAI rating mapping table for Type B ECAIs	6%
5.	Credit quality grade 5 in the LT ECAI rating mapping table for Type B ECAIs	15%
6.	Credit quality grade 6 in the LT ECAI rating mapping table for Type B ECAIs	30%
7.	Credit quality grade 7 in the LT ECAI rating mapping table for Type B ECAIs	50%
8.	Unrated	15%
9.	Defaulted	100%

(9) The institution must calculate the bucket level SA-DRC in accordance with Formulas 27Y and 27Z.

Formula 27Y

Calculation of Bucket Level SA-DRC

$$\text{SA-DRC}_b =$$

$$\max\left[\left(\sum_{i \in \text{Long}} \text{RW}_i \cdot \text{net JTD}_i\right) - \text{HBR} \cdot \left(\sum_{i \in \text{Short}} \text{RW}_i \cdot |\text{net JTD}_i|\right), 0\right]$$

where—

(a) SA-DRC_b is the SA-DRC for bucket b;

(b) i is the obligor belonging to bucket b;

(c) HBR is the hedge benefit ratio determined in accordance with Formula 27Z;

(d) net JTD_i is the net jump-to-default risk amount with respect to the obligor i; and

(e) RW_i is the default risk-weight of the obligor i.

Formula 27Z

Determination of Hedge Benefit Ratio

$$\text{HBR} = \frac{\sum \text{net JTD}_{\text{long}}}{\sum \text{net JTD}_{\text{long}} + \sum |\text{net JTD}_{\text{short}}|}$$

where—

(a) HBR is the hedge benefit ratio for the purposes of Formula 27Y;

(b) $\sum$ net JTD_{long} is the sum of all net long jump-to-default risk amounts within bucket b; and

(c) $\sum|\text{net } JTD_{short}|$ is the sum of all net short jump-to-default risk amounts in absolute value within bucket b.

281U. Calculation of gross jump-to-default risk amount for SA-DRC (non-securitization)

(1) Subject to subsections (3), (4) and (5), an authorized institution must calculate the gross jump-to-default risk amount of a long exposure as—

(a) if the exposure has a maturity that is equal to or longer than one year, the greater of zero and the sum of—

(i) the product of—

(A) subject to subsection (6), the notional amount of the instrument recorded as a positive value; and

(B) the LGD as set out in subsection (7) if the price of the instrument is linked to the recovery rate of the defaulter or 1 otherwise; and

(ii) the cumulative mark-to-market gain or loss over the face value already taken on the exposure, with a gain being recorded as a positive value and a loss being recorded as a negative value; or

(b) if the exposure has a maturity that is shorter than one year, the product of—

(i) the amount that would be calculated under paragraph (a) if the exposure had a maturity equal to or longer than one year; and

(ii) a scaling factor that is equal to the greater of 0.25 and the ratio of its maturity relative to one year.

(2) Subject to subsections (3), (4) and (5), an authorized institution must calculate the gross jump-to-default risk amount of a short exposure as—

(a) if the exposure has a maturity that is equal to or longer than one year, the lesser of zero and the sum of—

(i) the product of—

(A) subject to subsection (6), the notional amount of the instrument recorded as a negative value; and

(B) the LGD as set out in subsection (7) if the price of the instrument is linked to the recovery rate of the defaulter or 1 otherwise; and

(ii) the cumulative mark-to-market gain or loss over the face value already taken on the exposure, with a gain being recorded as a positive value and a loss being recorded as a negative value; or

(b) if the exposure has a maturity that is shorter than one year, the product of—

(i) the amount that would be calculated under paragraph (a) if the exposure had a maturity equal to or longer than one year; and

(ii) a scaling factor that is equal to the greater of 0.25 and the ratio of its maturity relative to one year.

(3) The institution must treat the gross jump-to-default risk amount of an instrument as zero if the instrument could be unwound with no exposure to default risk.

(4) The institution must treat the gross jump-to-default risk amount of a cash-equity position as the market value of the position.

(5) The institution must decompose an instrument with multiple constituents into exposures in the individual constituents to calculate the gross jump-to-default risk amount of each individual constituent.

(6) The institution must set the notional amount of an instrument as zero if the payoffs of the instrument are not related to its notional amount in the event of default.

(7) The institution must apply the LGD in Table 27E to calculate the gross jump-to-default risk amount.

Table 27E

LGD for Calculating Gross Jump-to-default Risk Amount

Column 1	Column 2	Column 3
Item	Underlying instrument	LGD
1.	Equity	100%
2.	Non-senior debt security	100%
3.	Senior debt security	75%
4.	Qualifying covered bond	25%

281V. Calculation of SA-DRC (securitization: non-CTP)

(1) An authorized institution must calculate the SA-DRC (securitization: non-CTP) for any—

(a) non-CTP securitization exposure in its trading book; and

(b) non-securitization exposure in its trading book that is held for the purpose of offsetting and hedging any exposure referred to in paragraph (a) if that non-securitization exposure together with other exposures is decomposed proportionately into the equivalent replicating tranches that span the entire tranche structure.

(2) For the purpose of calculating the SA-DRC (securitization: non-CTP), the institution must—

(a) calculate the gross jump-to-default risk amount in accordance with subsection (3) for each exposure referred to in subsection (1);

(b) calculate the net jump-to-default risk amount by offsetting the gross jump-to-default risk amounts of long and short exposures if any of the conditions referred to in section 281T(5)(b) applies and—

(i) the long and short exposures arise from the same underlying asset pool and the same tranche; or

(ii) the exposures are perfect replications in the opposite direction of the exposures to be offset through decomposition by a collection of non-securitization positions, securitization exposures with different securitized portfolios, or both;

(c) calculate the risk-weighted net jump-to-default risk amount as the product of—

(i) the net jump-to-default risk amount calculated under paragraph (b); and

(ii) the default risk-weight allocated in accordance with subsection (4);

(d) allocate the risk-weighted net jump-to-default risk amount to buckets in accordance with subsection (6);

(e) calculate the bucket level SA-DRC in accordance with section 281T(9); and

(f) calculate the SA-DRC (securitization: non-CTP) as the sum of the bucket level SA-DRC for each bucket.

(3) Subject to section 281U(3) and (4) and, for exposures with a maturity of less than one year, applying the scaling factor referred to in section 281U(1)(b)(ii) or (2)(b)(ii), the institution must calculate the gross jump-to-default risk amount for each non-CTP securitization exposure as—

(a) for a long exposure, the greater of zero and the sum of—

(i) the notional amount of the instrument recorded as a positive value; and

(ii) the cumulative mark-to-market gain or loss over the principal already taken on the exposure, with a gain being recorded as a positive value and a loss being recorded as a negative value; or

(b) for a short exposure, the lesser of zero and the sum of—

(i) the notional amount of the instrument recorded as a negative value; and

(ii) the cumulative mark-to-market gain or loss over the principal already taken on the exposure, with a gain being recorded as a positive value and a loss being recorded as a negative value.

(4) Subject to section 281S(4), the institution must allocate to each non-CTP securitization tranche a default risk-weight that is equal to the product of—

(a) 8%; and

(b) the applicable risk-weight of the credit risk for the securitization exposure as set out in Part 7.

(5) For the purposes of subsection (4)(b)—

(a) the institution must apply the prescribed approach required under section 15 to determine the risk-weight based on the pool of underlying exposures;

(b) a maturity of one year is assumed for each securitization exposure under the SEC-IRBA, SEC-ERBA and SEC-SA; and

(c) the total market risk capital charge for an individual cash securitization exposure is capped at the fair value of the exposure.

(6) The institution must allocate the risk-weighted net jump-to-default risk amount to the following buckets—

(a) a unique bucket for all corporates (excluding small-and-medium sized corporates), regardless of their region; and

(b) another 44 buckets consisting of each of the 11 asset classes specified in subsection (7) in each of the 4 regions specified in subsection (8).

(7) The asset classes are—

(a) asset-backed commercial paper (ABCP);

(b) auto loans or leases;

(c) residential mortgage-backed securities (RMBS);

(d) credit cards;

(e) commercial mortgage-backed securities (CMBS);

(f) collateralized loan obligations;

(g) collateralized debt obligations (CDO) squared;

(h) small-and-medium sized corporates;

(i) student loans;

(j) other retail; and

(k) other wholesale.

(8) The regions are—

(a) Asia;

(b) Europe;

(c) North America; and

(d) other.

281W. Calculation of SA-DRC (securitization: CTP)

(1) An authorized institution must calculate the SA-DRC (securitization: CTP) for any—

(a) CTP instrument in its trading book; and

(b) non-securitization instrument in its trading book that hedges a CTP instrument referred to in paragraph (a).

(2) For the purpose of calculating the SA-DRC (securitization: CTP), the institution must treat an n^{th}-to-default credit derivative contract as a tranche in a CTP securitization transaction with the value of—

(a) attachment point calculated as $(n-1)/N$; and

(b) detachment point calculated as n/N,

where N is the total number of names in the underlying basket or pool.

(3) For the purpose of calculating the SA-DRC (securitization: CTP), the institution must—

(a) subject to applying the scaling factor referred to in section 281U(1)(b)(ii) or (2)(b)(ii), for exposures with a maturity of less than one year, calculate the gross jump-to-default risk amount—

(i) for each instrument referred to in subsection (1)(a), in accordance with section 281V(3) as if it were a non-CTP securitization exposure; and

(ii) for each instrument referred to in subsection (1)(b), as its market value;

(b) subject to subsections (4) and (5), calculate the net jump-to-default risk amount by offsetting the gross jump-to-default risk amounts of long and short exposures if—

(i) the long and short exposures—

(A) where the underlying is a credit index, must arise from the same index, the same series and the same tranche; or

(B) otherwise, must arise from the same underlying basket or pool and the same tranche; and

(ii) the exposures are perfect replications in the opposite direction of the exposures to be offset through decomposition by a collection of non-securitization positions, securitization tranches or index tranches, but the decomposed exposures are not re-securitization exposures;

(c) calculate the risk-weighted net jump-to-default risk amount as the product of—

(i) the net jump-to-default risk amount calculated under paragraph (b); and

(ii) the default risk-weight allocated in accordance with subsection (6);

(d) allocate the risk-weighted net jump-to-default risk amount to buckets in accordance with subsection (7);

(e) calculate the bucket level SA-DRC in accordance with subsection (8); and

(f) calculate the SA-DRC (securitization: CTP) in accordance with subsection (9).

(4) The institution—

(a) must offset the gross jump-to-default risk amounts of long and short exposures; and

(b) if the maturity of any one or more of those exposures is less than one year, must apply the scaling factor referred to in section 281U(1)(b)(ii) or (2)(b)(ii) to each such exposure.

(5) If—

(a) a perfect replication referred to in subsection (3)(b)(ii) is not possible; and

(b) the long and short securitization exposures are otherwise equivalent except for a residual component,

the institution may offset the exposures and reflect the net jump-to-default risk amount for the residual exposure.

(6) The institution must allocate a default risk-weight—

(a) in accordance with section 281V(4) for net jump-to-default risk amounts resulting from exposures referred to in subsection (1)(a) as if they were non-CTP securitization exposures; and

(b) in accordance with section 281T(8) for net jump-to-default risk amounts resulting from exposures referred to in subsection (1)(b).

(7) The institution must allocate the risk-weighted net jump-to-default risk amounts to buckets that correspond to a credit index or an underlying basket.

(8) The institution must calculate the bucket level SA-DRC in accordance with Formulas 27ZA and 27ZB.

Formula 27ZA

Calculation of Bucket Level SA-DRC

$$\text{SA-DRC}_b = \left(\sum_{i \in \text{Long}} RW_i \cdot \text{net JTD}_i\right) - \text{HBR} \cdot \left(\sum_{i \in \text{Short}} RW_i \cdot |\text{net JTD}_i|\right)$$

where—

(a) SA-DRC_b is the SA-DRC for bucket b;

(b) i is an exposure belonging to bucket b;

(c) HBR is the hedge benefit ratio determined in accordance with Formula 27ZB;

(d) net JTD_i is the net jump-to-default risk amount with respect to the exposure i; and

(e) RW_i is the default risk-weight of the exposure i.

Formula 27ZB

Determination of Hedge Benefit Ratio

$$\text{HBR} = \frac{\sum \text{net JTD}_{\text{long}}}{\sum \text{net JTD}_{\text{long}} + \sum |\text{net JTD}_{\text{short}}|}$$

where—

(a) HBR is the hedge benefit ratio for the purposes of Formula 27ZA;

(b) $\sum$ net JTD_{long} is the sum of all net long jump-to-default risk amounts across all buckets; and

(c) $\sum|$net $JTD_{short}|$ is the sum of all net short jump-to-default risk amounts in absolute value across all buckets.

(9) The institution must calculate the SA-DRC (securitization: CTP) in accordance with Formula 27ZC.

Formula 27ZC

Calculation of SA-DRC (Securitization: CTP)

$$\text{SA-DRC (securitization: CTP)} = \max\left\{\sum_{b}\left(\max(\text{SA-DRC}_b, 0) + 0.5 \cdot \min(\text{SA-DRC}_b, 0)\right), 0\right\}$$

where SA-DRC_b is the bucket-level SA-DRC calculated under subsection (8).

Division 2—Calculation of Market Risk Capital Charge under SSTM Approach: General

(L.N. 167 of 2023)

282. Application of Divisions 2 to 10

(1) Divisions 2, 3, 4, 5, 6, 7, 8, 9 and 10 apply to an authorized institution that uses the SSTM approach to calculate its market risk capital charge.

(2) A reference to an authorized institution in Divisions 2, 3, 4, 5, 6, 7, 8, 9 and 10 is a reference to an authorized institution that uses the SSTM approach to calculate its market risk capital charge.

(3) Divisions 3, 4, 5 and 6 do not apply to an authorized institution's option exposures in debt securities, interest rates, equities, foreign exchange (including gold) and commodities except to the extent, if any, specified in Division 7, 8 or 9.

(L.N. 167 of 2023)

283. *(Repealed L.N. 167 of 2023)*

284. Calculation of market risk capital charge for each risk category

(1) An authorized institution must calculate the market risk capital charge for its exposures falling into each risk category by multiplying the capital charge calculated in accordance with Divisions 2, 3, 4, 5, 6, 7, 8, 9 and 10 with a scaling factor of—

(a) 1.3 for interest rate exposures;

(b) 3.5 for equity exposures;

(c) 1.2 for foreign exchange exposures; and

(d) 1.9 for commodity exposures. *(L.N. 167 of 2023)*

(2) Subject to subsection (3) and section 306(2), an authorized institution shall use the fair value of its positions to calculate the market risk capital charge.

(3) Where the stated notional amount of an exposure held by an authorized institution is leveraged or enhanced by the structure of the exposure, the institution shall use the effective notional amount of the exposure (being the stated notional amount of the exposure adjusted to take into account the effect of the leverage or enhancement provided by the

structure of the exposure) for the purposes of this Part. *(L.N. 267 of 2006)*

285. Calculation of risk-weighted amount for market risk

An authorized institution shall calculate its risk-weighted amount for market risk by multiplying the aggregate of the market risk capital charge as calculated pursuant to section 284(1) by 12.5.

Division 3—Calculation of Market Risk Capital Charge for Interest Rate Exposures

286. Calculation of market risk capital charge

An authorized institution shall, for the purposes of calculating the market risk capital charge for its interest rate exposures—

(a) calculate the market risk capital charge for specific risk for each of its trading book positions (whether long or short) in debt securities and debt-related derivative contracts—

(i) in accordance with section 287 if those positions arise from non-securitization exposures that do not fall within subparagraph (iv) or a CTP;

(ii) in accordance with section 287A if those positions arise from securitization exposures that do not fall within a CTP; or

(iii) *(Repealed L.N. 167 of 2023)*

(iv) in accordance with section 287 and Division 10 if those positions arise from credit derivative contracts that do not fall within subparagraph (ii) or a CTP; *(L.N. 137 of 2011; L.N. 167 of 2023)*

(b) subject to paragraph (c), calculate in accordance with section 288 the market risk capital charge for general market risk for— *(L.N. 137 of 2011)*

(i) its trading book positions (whether long or short) in debt securities, debt-related derivative contracts and interest rate derivative contracts;

(ii) the interest rate exposures arising from its trading book positions (whether long or short) in equity-related derivative contracts; and

(iii) the interest rate exposures arising from its positions (whether long or short) in commodity-related derivative contracts; and *(L.N. 137 of 2011)*

(c) calculate in accordance with section 288 and Division 10 the market risk capital charge for general market risk for the interest rate exposures arising from its trading book positions (whether long or short) in credit derivative contracts. *(L.N. 137 of 2011)*

287. Calculation of market risk capital charge for specific risk for interest rate exposures that fall within section 286(a)(i) or (iv)

(L.N. 137 of 2011)

(1) Subject to subsections (2), (3), (4), (5), (6), (7), (8), (9), (9A) and (10), an authorized institution shall, for the purposes of calculating the market risk capital charge for specific risk for its trading book positions (whether long or short) in debt securities and debt-related derivative contracts arising from its interest rate exposures that fall within section 286(a)(i) or (iv)— *(L.N. 137 of 2011)*

(a) assign those positions into the classes specified in column 1 of Table 28, the credit quality grades specified in column 2 of that Table and, if applicable, the residual maturities specified in column 3 of that Table;

(b) multiply those positions by the appropriate market risk capital charge factors for specific risk specified in column 3 of Table 28; and

(c) subject to subsection (1A), calculate the total market risk capital charge for specific risk as the sum of the market risk capital charge for specific risk for each of those positions. *(L.N. 137 of 2011)*

Table 28

Market Risk Capital Charge Factors for Specific Risk

Class	Credit quality grade	Market risk capital charge factor for specific risk
sovereign	1 or 2	0%
	3 or 4	0.25% (residual maturity of not more than 6 months)
		1.00% (residual maturity of more than 6 months but not more than 24 months)
		1.60% (residual maturity of more than 24 months)
	5 or 6	8.00%
	7	12.00%
	unrated	8.00%
qualifying		0.25% (residual maturity of not more than 6 months)
		1.00% (residual maturity of more than 6 months but not more than 24 months)

Class	Credit quality grade	Market risk capital charge factor for specific risk
		1.60% (residual maturity of more than 24 months)
non-qualifying	5	8.00%
	6	12.00%
	unrated	8.00%

(L.N. 167 of 2023)

(1A) For the purposes of subsection (1), the total market risk capital charge for specific risk for n^{th}-to-default credit derivative contracts that fall within section 286(a)(iv) must, during the transitional period (securitization), be calculated as the higher of—

(a) the total market risk capital charge for specific risk for the long positions; or

(b) the total market risk capital charge for specific risk for the short positions. *(L.N. 137 of 2011)*

(2) An authorized institution shall not offset between positions referred to in subsection (1) for the purposes of that subsection except for—

(a) long and short positions in identical issues (including positions in derivative contracts); and *(L.N. 137 of 2011)*

(b) credit derivative contracts set out in section 309, 310 or 311.

(3) For the purposes of subsection (1)—

(a) if—

(i) the issuer of any debt securities referred to in that subsection or, in the case of debt-related derivative contracts referred to in that subsection, the issuer of any underlying debt securities, has an ECAI issuer rating; or

(ii) any debt securities referred to in that subsection or, in the case of debt-related derivative contracts referred to in that subsection, any underlying debt securities, have an ECAI issue specific rating,

an authorized institution must, subject to paragraphs (b), (c) and (d), map the ECAI issuer rating or the ECAI issue specific rating, as the case may be, to a credit quality grade in the LT ECAI rating mapping table and ST ECAI rating mapping table; *(L.N. 167 of 2023)*

(b) subject to paragraph (c), if the debt securities referred to in that subsection are issued by a sovereign or, in the case of debt-related derivative contracts referred to in that subsection, if the underlying debt securities are issued by a sovereign, an authorized institution shall determine the credit quality grade by reference to the ECAI issuer rating of that sovereign;

(c) an authorized institution shall treat as unrated the issuer of any debt securities or, in the case of debt-related derivative contracts, the issuer of any underlying debt securities, referred to in paragraph (b) which does not have an ECAI issuer rating;

(d) subject to paragraph (e), if the debt securities or debt-related derivative contracts referred to in that subsection do not fall within paragraph (b), an authorized institution shall determine the credit quality grade to be used by reference to, in the case of debt securities, the ECAI issue specific rating of the debt securities or, in the case of debt-related derivative contracts, the ECAI issue specific rating of the underlying debt securities;

(e) an authorized institution shall treat as unrated any debt securities or, in the case of debt-related derivative contracts, any underlying debt securities, referred to in paragraph (d) which do not have an ECAI issue specific rating;

(f) an authorized institution may only assign a market risk capital charge factor of 0% to—

(i) debt securities referred to in that subsection issued by a sovereign with a credit quality grade of 3 or 4 as determined under paragraph (b); or

(ii) debt-related derivative contracts referred to in that subsection in respect of which the underlying debt securities are issued by a sovereign with a credit quality grade of 3 or 4 as determined under paragraph (b),

if, and only if, those debt securities or, in the case of those debt-related derivative contracts, those underlying debt securities, are denominated in the domestic currency of that sovereign and funded by the institution in that currency. *(L.N. 167 of 2023)*

(4) An authorized institution may only include in the qualifying class in Table 28—

(a) debt securities issued by multilateral development banks and debt-related derivative contracts where the underlying debt securities are issued by multilateral development banks;

(aa) debt securities issued by public sector entities, and debt-related derivative contracts where the underlying debt securities are issued by public sector entities, where—

(i) subject to subparagraphs (ii) and (iii), the debt securities or the underlying debt securities, as the case may be, are assigned a credit quality grade of 3 or 4; *(L.N. 167 of 2023)*

(ii) for the purposes of subparagraph (i), the credit quality grade is determined as one grade below that assigned to the sovereign, pursuant to subsection (3)(b) and (c), of the jurisdiction in which the public sector entity concerned is incorporated or, if there is no such lower credit quality grade, the credit quality grade assigned to that sovereign pursuant to that subsection; and

(iii) the institution treats as unrated any of those debt securities, or any of those underlying debt securities, as the case may be, where—

(A) they do not have an ECAI issue specific rating; or

(B) the sovereign of the jurisdiction in which the public sector entity is incorporated does not have an ECAI issuer rating; *(L.N. 137 of 2011)*

(b) debt securities, not falling within paragraph (a) or (aa), that are rated investment grade and debt-related derivative contracts where the underlying debt securities, not falling within paragraph (a) or (aa), that are rated investment grade; and *(L.N. 137 of 2011)*

(c) if the institution uses the IRB approach to calculate its credit risk, unrated debt securities, and debt-related derivative contracts if the underlying debt securities are unrated, where—

(i) the debt securities, or the underlying debt securities, as the case may be, are assessed as equivalent to investment grade under the institution's rating system on the basis that the debt securities, or the underlying debt securities, as the case may be, have a PD assigned by the institution's rating system of not more than the PD implied by the long run average PD (being a period which captures a reasonable mix of high-default and low-default years of an economic cycle) of a debt security rated investment grade; and

(ii) the issuer of the debt securities, or the issuer of the underlying debt securities, as the case may be—

(A) has any debt securities or equities listed on a recognized stock exchange; or

(B) is subject to supervisory arrangements regarding the maintenance of adequate capital to support its business activities comparable to those prescribed for authorized institutions under the Ordinance and these Rules.

(5) An authorized institution shall—

(a) include any debt securities in the non-qualifying class in Table 28 if—

(i) the debt securities are not issued by a sovereign; or

(ii) the debt securities are not included in the qualifying class under subsection (4);

(b) include any debt-related derivative contracts in the non-qualifying class in Table 28 if—

(i) the underlying debt securities are not issued by a sovereign; or

(ii) the debt-related derivative contracts are not included in the qualifying class under subsection (4); *(L.N. 137 of 2011)*

(c) include any debt securities issued by public sector entities, and any debt-related derivative contracts where the underlying debt securities are issued by public sector entities, in the non-qualifying class in Table 28 that assigns a credit quality grade of 6 if the application of subsection (4)(aa)(ii) to the debt securities or the underlying debt securities, as the case may be, results in the debt securities or underlying debt securities, as the case may be, being assigned a credit quality grade of 7. *(L.N. 137 of 2011; L.N. 167 of 2023)*

(6) If the issuer of any debt securities referred to in this section or, in the case of any debt-related derivative contracts referred to in this section, the issuer of any underlying debt securities, has more than one ECAI issuer rating assigned to the issuer, an authorized institution must, for the purposes of this section, apply section 54E(2), with all necessary modifications, to the ECAI issuer ratings concerned (as if the references to ECAI issue specific ratings in that subsection were references to ECAI issuer ratings) to ascertain which one of them must be used for those purposes. *(L.N. 167 of 2023)*

(7) If any debt securities referred to in this section or, in the case of any debt-related derivative contracts referred to in this section, any underlying debt securities, have more than one ECAI issue specific rating assigned to them, an authorized institution must, for the purposes of this section, apply section 54E(2), with all necessary modifications, to the ECAI issue specific ratings concerned to ascertain which one of them must be used for those purposes. *(L.N. 167 of 2023)*

(8) Where the Monetary Authority is satisfied that an authorized institution's market risk capital charge for specific risk is underestimated for any non-qualifying debt securities (being debt securities falling within subsection (5)(a)) or non-qualifying debt-related derivative contracts (being debt-related derivative contracts falling within subsection (5)(b)) which have a high yield to redemption relative to debt securities

or debt-related derivative contracts falling within subsection (3)(b), the Monetary Authority may, by notice in writing given to the institution—

(a) require the institution to apply a higher market risk capital charge factor for specific risk to such non-qualifying debt securities or debt-related derivative contracts, as the case may be, as specified in the notice;

(b) prohibit offsetting, for the purposes of calculating the institution's market risk capital charge for general market risk between such debt securities or debt-related derivative contracts and such other debt securities or debt-related derivative contracts as specified in the notice.

(9) An authorized institution shall comply with the requirements of a notice given to it under subsection (8).

(9A) For the purposes of subsection (1)—

(a) subject to paragraph (b), the market risk capital charge for specific risk for an authorized institution's positions in a credit derivative contract (other than an n^{th}-to-default credit derivative contract) may be capped at the maximum possible loss arising from the contract calculated for each individual position as—

(i) if the institution is a protection buyer, the change in the value of the contract in the event that all the reference obligations specified in the contract were to become immediately default risk-free; or

(ii) if the institution is a protection seller, the change in the value of the contract in the event that all the reference obligations specified in the contract were to default immediately with zero recoveries; and

(b) for each position an authorized institution has in an n^{th}-to-default credit derivative contract or n^{th}-to-default credit-linked note, irrespective of whether the institution is a protection buyer or a protection seller—

(i) the market risk capital charge for specific risk for the contract or note, where n is equal to 1, is to be the lesser of—

(A) the sum of the market risk capital charge for specific risk for the individual reference obligations in the basket of reference obligations specified in the contract or note, as the case may be; or

(B) the institution's maximum liability under the contract or the fair value of the note, as the case may be; and

(ii) the market risk capital charge for specific risk for the contract or note, where n is greater than 1, is to be the lesser of—

(A) the sum of the market risk capital charge for specific risk for the individual reference obligations in the basket of reference obligations specified in the contract or note, as the case may be, but disregarding the (n-1) obligation with the lowest market risk capital charge for specific risk; or

(B) the institution's maximum liability under the contract or the fair value of the note, as the case may be. *(L.N. 137 of 2011)*

(10) For the avoidance of doubt, it is hereby declared that this section does not apply to interest rate derivative contracts.

(11) In this section—

ECAI issue specific rating (ECAI特定債項評級), in relation to a debt security or, in the case of a debt-related derivative contract, the underlying debt security, means a short-term credit assessment rating or long-term credit assessment rating that is assigned to the debt security or underlying debt security, as the case may be, by a Type A ECAI or a Type B ECAI; *(L.N. 167 of 2023)*

ECAI issuer rating (ECAI發債人評級), in relation to the issuer of a debt security or, in the case of a debt-related derivative contract, the underlying debt security, means a long-term credit assessment rating that is assigned to the issuer by a Type A ECAI or a Type B ECAI; *(L.N. 167 of 2023)*

sovereign (官方實體) includes a sovereign foreign public sector entity.

287A. Calculation of market risk capital charge for specific risk for interest rate exposures that fall within section 286(a)(ii)

An authorized institution must calculate the market risk capital charge for specific risk arising from each of its net positions in securitization exposures held in the trading book that fall within section 286(a)(ii) by multiplying each of those net positions by a market risk capital charge factor that is equal to the risk-weight, determined as if the net position were held in the banking book in accordance with Part 7, divided by 12.5.

(L.N. 167 of 2023)

287B. *(Repealed L.N. 167 of 2023)*

288. Calculation of market risk capital charge for general market risk

(1) An authorized institution shall, for the purposes of calculating the market risk capital charge for general market risk—

(a) multiply its long and short positions in interest rate exposures in each time band specified in column 1 of Table 30 within the maturity ladder constructed in accordance with section 289 by the appropriate risk-weight specified in column 4 of that Table;

(b) offset the total risk-weighted long and short positions in each time band to produce a single net risk-weighted long or short position for each time band;

(c) apply a market risk capital charge factor of 10% on the matched position (being the lesser of the absolute values of the total risk-weighted long and short positions) of each time band, whether long or short, to arrive at a market risk capital charge for each matched position (referred to in this section as ***vertical disallowance***);

(d) subject to subsections (2) and (3)—

(i) first conduct a round of horizontal offsetting between the net risk-weighted positions for the time bands in each of the 3 zones subject to a scale of market risk capital charge factors, expressed as a percentage of the matched positions for each zone, as set out in Table 29;

(ii) then conduct a round of horizontal offsetting between the total net risk-weighted positions for the zones across the 3 zones (being between adjacent zones and between zone 1 and zone 3) subject to a scale of market risk capital charge factors, expressed as a percentage of the matched positions between the zones, as set out in Table 29,

to arrive at a market risk capital charge for each matched position (referred to in this section as ***horizontal disallowance***); and

(e) apply a market risk capital charge factor of 100% on the remaining net risk-weighted long or short position in interest rate exposures after carrying out the offsetting referred to in paragraphs (b) and (d).

Table 29

Horizontal Disallowance

Zone	Time band: Coupon of not less than 3% per annum	Time band: Coupon of less than 3% per annum	Market risk capital charge factor: Within the zone	Market risk capital charge factor: Between adjacent zones	Market risk capital charge factor: Between zones 1 and 3
Zone 1	not more than 1 month	not more than 1 month	40%	40%	100%
	more than 1 month but not more than 3 months	more than 1 month but not more than 3 months			
	more than 3 months but not more than 6 months	more than 3 months but not more than 6 months			
	more than 6 months but not more than 12 months	more than 6 months but not more than 12 months			
Zone 2	more than 1 year but not more than 2 years	more than 1.0 year but not more than 1.9 years	30%		
	more than 2 years but not more than 3 years	more than 1.9 years but not more than 2.8 years			
	more than 3 years but not more than 4 years	more than 2.8 years but not more than 3.6 years			
Zone 3	more than 4 years but not more than 5 years	more than 3.6 years but not more than 4.3 years	30%		
	more than 5 years but not more than 7 years	more than 4.3 years but not more than 5.7 years			
	more than 7 years but not more than 10 years	more than 5.7 years but not more than 7.3 years			
	more than 10 years but not more than 15 years	more than 7.3 years but not more than 9.3 years			
	more than 15 years but not more than 20 years	more than 9.3 years but not more than 10.6 years			
	more than 20 years	more than 10.6 years but not more than 12 years			
		more than 12 years but not more than 20 years			
		more than 20 years			

(2) For the purposes of an authorized institution conducting horizontal offsetting under subsection (1)(d)(i), the institution shall—

(a) calculate the net risk-weighted long or short position of each time band after separately adding—

(i) long positions to long positions; and

(ii) short positions to short positions;

(b) in the case of long and short positions in the same zone, subject the matched position (being the lesser of the absolute values of the total net risk-weighted long and short positions for the zone) to a market risk capital charge factor of 40% for zone 1 and 30% for zone 2 and zone 3; and

(c) offset the positions of time bands within the same zone to create the matched position to which the market risk capital charge factor is applied under paragraph (b) and a total net risk-weighted long or short position for each zone.

(3) For the purposes of an authorized institution conducting horizontal offsetting under subsection (1)(d)(ii), the institution shall—

(a) in the case of opposite positions between adjacent zones (being one zone having a total net risk-weighted long position while another zone having a total net risk-weighted short position), subject the matched position (being the lesser of the absolute values of the total net risk-weighted long position in one zone and the total net risk-weighted short position in another zone) to a market risk capital charge factor of 40%;

(b) offset the positions between adjacent zones to create the matched position to which the market risk capital charge factor is applied under paragraph (a) and a total net risk-weighted long or short position;

(c) subject to paragraph (d), in the case of opposite positions between zone 1 and zone 3, subject the matched position (being the lesser of the absolute values of the total net risk-weighted long or short position in zone 1 and the total net risk-weighted short or long position respectively in zone 3) to a market risk capital charge factor of 100%; and

(d) in order to calculate the horizontal disallowance between zone 1 and zone 3 for the purposes of paragraph (c)—

(i) if the total net risk-weighted positions of zone 1 and zone 2 are netted, treat any full or partial position that cannot be offset as remaining in its zone; and *(L.N. 167 of 2023)*

(ii) if the total net risk-weighted positions of zone 2, after taking into account the offsetting referred to in subparagraph (i), and those of zone 3 are netted, treat any full or partial position that cannot be offset as remaining in its zone. *(L.N. 167 of 2023)*

(4) An authorized institution shall derive the market risk capital charge for general market risk for its portfolio of interest rate exposures by aggregating—

(a) the total market risk capital charge for vertical disallowance for all time bands calculated in accordance with subsection (1)(c);

(b) the total market risk capital charge for horizontal disallowance for individual zones and across different zones calculated in accordance with subsection (1)(d); and

(c) the market risk capital charge for the remaining net risk-weighted long or short position calculated in accordance with subsection (1)(e).

(5) An authorized institution shall calculate the market risk capital charge for general market risk for each currency separately, convert each amount so calculated into Hong Kong dollars at current market rates and then aggregate the amounts so calculated.

289. Construction of maturity ladder

(1) Subject to subsections (2), (3), (4), (5) and (6), for the purposes of making the calculation required by section 288(1), an authorized institution shall—

(a) slot all of its long or short positions in debt securities, debt-related derivative contracts, interest rate derivative contracts and interest rate exposures arising from equity-related derivative contracts and commodity-related derivative contracts with a coupon of not less than 3% per annum into a maturity ladder comprising the 13 time bands set out in columns 1 and 2 of Table 30; and

(b) slot all of its long or short positions in debt securities, debt-related derivative contracts, interest rate derivative contracts and interest rate exposures arising from equity-related derivative contracts and commodity-related derivative contracts with a coupon of less than 3% per annum into a maturity ladder comprising the 15 time bands set out in columns 1 and 3 of Table 30.

Table 30

Time Bands and Risk-weights

Time Band	Coupon of not less than 3% per annum	Coupon of less than 3% per annum	Risk-weight
1	not more than 1 month	not more than 1 month	0.00%
2	more than 1 month but not more than 3 months	more than 1 month but not more than 3 months	0.20%
3	more than 3 months but not more than 6 months	more than 3 months but not more than 6 months	0.40%
4	more than 6 months but not more than 12 months	more than 6 months but not more than 12 months	0.70%
5	more than 1 year but not more than 2 years	more than 1.0 year but not more than 1.9 years	1.25%
6	more than 2 years but not more than 3 years	more than 1.9 years but not more than 2.8 years	1.75%
7	more than 3 years but not more than 4 years	more than 2.8 years but not more than 3.6 years	2.25%
8	more than 4 years but not more than 5 years	more than 3.6 years but not more than 4.3 years	2.75%

Time Band	Coupon of not less than 3% per annum	Coupon of less than 3% per annum	Risk-weight
9	more than 5 years but not more than 7 years	more than 4.3 years but not more than 5.7 years	3.25%
10	more than 7 years but not more than 10 years	more than 5.7 years but not more than 7.3 years	3.75%
11	more than 10 years but not more than 15 years	more than 7.3 years but not more than 9.3 years	4.50%
12	more than 15 years but not more than 20 years	more than 9.3 years but not more than 10.6 years	5.25%
13	more than 20 years	more than 10.6 years but not more than 12 years	6.00%
14		more than 12 years but not more than 20 years	8.00%
15		more than 20 years	12.50%

(2) For the purposes of subsection (1), an authorized institution shall—

(a) slot fixed rate exposures into the time bands set out in Table 30 in accordance with their respective residual maturities;

(b) slot floating rate exposures into the time bands set out in Table 30 in accordance with their respective residual terms to the next interest fixing date;

(c) regard interest rate exposures arising from derivative contracts as long and short positions and slot such positions into the time bands set out in Table 30 such that—

(i) interest rate futures contracts, interest rate forward contracts and forward rate agreements are treated as a combination of the long and short positions in a zero-coupon specific risk-free security whereby—

(A) a long or short position in an interest rate futures contract or interest rate forward contract is to be regarded as—

(I) a short or long position respectively with a maturity being the remaining period up to and including the delivery date of the underlying interest rate contract; and

(II) a long or short position respectively with a maturity being the remaining period up to and including the delivery date of the underlying interest rate contract plus the contract period of the underlying interest rate contract; or

(B) a sold or purchased forward rate agreement is to be regarded as—

(I) a short or long position respectively with a maturity being the remaining period up to and including the settlement date of the agreement; and

(II) a long or short position respectively with a maturity being the remaining period up to and including the settlement date of the agreement plus the contract period of the agreement;

(ii) bond futures contracts and bond forward contracts are treated as a combination of the long and short positions in a zero-coupon specific risk-free security and the underlying bond whereby a long or short position in a bond futures contract or bond forward contract is to be regarded as—

(A) a short or long position respectively in a zero-coupon specific risk-free security with a maturity being the remaining period up to and including the delivery date of the underlying bond; and

(B) a long or short position respectively in the underlying bond with a maturity being the remaining period up to and including the delivery date of the underlying bond plus the tenor of the underlying bond;

(iii) interest rate swap contracts under which the institution receives or pays floating rate interest and pays or receives respectively fixed rate interest are to be regarded as—

(A) a short or long position respectively in a fixed rate instrument with a maturity being the remaining period up to and including the maturity date of the swap contract concerned; and

(B) a long or short position respectively in a floating rate instrument with a maturity being the remaining period up to and including the next interest fixing date.

(3) For the purposes of subsection (1), an authorized institution may—

(a) exclude from the maturity ladder long and short positions in identical instruments having the same issuer, coupon, currency and maturity;

(b) fully offset the matched positions in a futures contract or forward contract and the underlying exposure of the futures contract or forward contract, as the case may be, except that the position in a zero-coupon specific risk-free security referred to in subsection (2)(c)(ii)(A) shall be included in the calculation of the institution's market risk capital charge for general market risk.

(4) For the purposes of subsection (1), an authorized institution—

(a) in the case of a futures contract or forward contract providing for a range of bonds to be delivered, may only offset positions in the contract and the underlying bond which is readily identifiable as the most profitable for the institution with a short position to deliver;

(b) shall, after offsetting the positions in the futures contract or forward contract and the underlying bond pursuant to paragraph (a), record the amount of the remaining long position of the contract, up to and including the delivery date of the contract, as the face value of the contract divided by the conversion factor applicable to the contract and multiplied by the current market price of that bond as determined in accordance with section 4A as if measured at fair value. *(L.N. 137 of 2011)*

(5) Subject to subsection (6), for the purposes of subsection (1), an authorized institution may treat opposite positions in the same type of derivative contract (including the delta-weighted position of option contracts calculated in accordance with section 303) as matched and may fully offset them.

(6) For the purposes of subsection (5), positions in the same type of derivative contract are opposite only if—

(a) the positions relate to derivative contracts with the same underlying exposures, are of the same nominal value and denominated in the same currency;

(b) in the case of futures contracts, the offsetting positions in the underlying interest rate exposures to which the futures contracts relate are for identical exposures and mature within 7 days of each other;

(c) in the case of swap contracts and forward rate agreements, the rates (for floating rate positions) of the contracts or agreements, as the case may be, are identical and the coupons are within 15 basis points; and

(d) in the case of swap contracts, forward rate agreements and forward contracts, the next interest fixing date or, for fixed coupon positions or forward contracts, the residual maturity, corresponds within the following limits—

(i) if either of the contracts or agreements, as the case may be, to be offset has an interest fixing date or residual maturity of not more than one month, the interest fixing date or residual maturity, as the case may be, is the same for both contracts or agreements, as the case may be;

(ii) if either of the contracts or agreements, as the case may be, to be offset has an interest fixing date or residual maturity of more than one month but not more than one year, the interest fixing dates or residual maturities, as the case may be, are within 7 days of each other; and

(iii) if either of the contracts or agreements, as the case may be, to be offset has an interest fixing date or residual maturity of more than one year, the interest fixing dates or residual maturities, as the case may be, are within 30 days of each other.

290. Use of alternatives requires Monetary Authority's prior consent

An authorized institution shall—

(a) use the methodology prescribed in this Division to calculate its positions to be included in the maturity ladder unless it has the prior consent of the Monetary Authority to use a different methodology; and

(b) use the maturity method to calculate the market risk capital charge for general market risk for its portfolio of interest rate exposures unless it has the prior consent of the Monetary Authority to use a different method.

Division 4—Calculation of Market Risk Capital Charge for Equity Exposures

291. Calculation of market risk capital charge

An authorized institution shall, for the purposes of calculating the market risk capital charge for its trading book positions (whether long or short) in equities and equity-related derivative contracts—

(a) calculate the market risk capital charge for specific risk for each of those positions; and

(b) calculate the market risk capital charge for general market risk for those positions.

(L.N. 137 of 2011)

292. Preliminary steps to calculating market risk capital charge

(1) For the purposes of section 291—

(a) subject to paragraph (b), an authorized institution shall make a separate calculation for each of its positions in equities and equity-related derivative contracts for each exchange where the equities or, in the case of equity-related derivative contracts, the underlying equities concerned are listed or traded;

(b) if an equity is listed on more than one exchange, an authorized institution shall make the calculation referred to in paragraph (a) only in respect of that exchange which is the primary listing of the equity;

(c) an authorized institution shall convert its equity-related derivative contracts into positions in the underlying equity by—

(i) valuing its futures contracts and forward contracts relating to an individual equity at the fair value of the underlying equity;

(ii) valuing its futures contracts relating to equity indices as—

(A) the current index value multiplied by the monetary value of one index point set by the futures exchange where the futures contract is traded; or

(B) the fair value of the underlying basket of equities used to compile the index;

(d) an authorized institution shall regard each of its equity swap contracts as long and short positions such that—

(i) in the case of an equity swap contract under which the institution—

(A) is receiving an amount based on the change in value of a particular equity or equity index; and

(B) is paying an amount based on the change in value of a different equity or equity index,

the position in sub-subparagraph (A) is the long position, and the position in sub-subparagraph (B) is the short position, of the equity swap contract;

(ii) in the case of an equity swap contract which involves a position requiring the receipt or payment of fixed or floating rate interest, the institution treats the position under the maturity method;

(e) if equities are to be received or delivered under a forward contract, an authorized institution shall treat any interest rate exposure arising out of the contract under the maturity method; and

(f) an authorized institution shall treat any interest rate exposure arising out of an equity futures contract or an equity index futures contract under the maturity method.

(2) For the purposes of section 291, an authorized institution may—

(a) fully offset its matched positions in each identical equity or equity index with the same delivery month in each exchange in order to produce a single net long or short position;

(b) offset a futures contract in a given equity against an opposite position in the same equity.

293. Calculation of market risk capital charge for specific risk

Subject to section 292, an authorized institution shall calculate the market risk capital charge for specific risk for the institution's trading book positions in equities and equity-related derivative contracts as 8% of its total gross (long plus short) position.

(L.N. 137 of 2011)

294. Calculation of market risk capital charge for general market risk

(1) Subject to subsection (2) and section 292, an authorized institution shall calculate the market risk capital charge for general market risk for the institution’s trading book positions in equities and equity-related derivative contracts as 8% of its total net position in equities and equity-related derivative contracts (being the difference between the sum of the institution’s long positions and the sum of the institution’s short positions). *(L.N. 137 of 2011)*

(2) An authorized institution shall not, for the purposes of subsection (1), offset net long and short positions on different exchanges.

Division 5—Calculation of Market Risk Capital Charge for Foreign Exchange (Including Gold) Exposures

295. Preliminary steps to calculating market risk capital charge

(1) An authorized institution shall, for the purposes of calculating the market risk capital charge for its positions in foreign exchange (including gold) and exchange rate-related derivative contracts— *(L.N. 167 of 2023)*

(a) determine the amount of its net open position (being the sum of the net spot position and the net forward position) in each currency and in gold;

(b) convert each amount determined under paragraph (a) into Hong Kong dollars at current market rates; and

(c) subject to Division 7, in relation to those positions arising from foreign currency option contracts, apply paragraphs (a) and (b) to each currency to which the option contracts relate.

(2)-(3) *(Repealed L.N. 167 of 2023)*

296. Calculation of market risk capital charge

(1) Subject to subsection (2) and section 295, an authorized institution shall calculate the market risk capital charge for the institution's positions in foreign exchange (including gold) as 8% of its total net open position derived by aggregating—

(a) the sum of the institution's net long or short positions less its United States dollars position against its Hong Kong dollars position; and

(b) the institution's net position in gold (whether long or short).

(2) For the purposes of subsection (1)(a)—

(a) the sum of an authorized institution's net long or short positions is the sum of—

(i) its total net long or short position in each foreign currency (including gold and, if applicable, the net delta-weighted position of option contracts in each such currency); and

(ii) its Hong Kong dollars position; *(L.N. 267 of 2006)*

(b) the United States dollars position against the Hong Kong dollars position in respect of an authorized institution is—

(i) zero if the institution's net open positions in United States dollars and Hong Kong dollars are both long or both short;

(ii) the smaller of the 2 positions (expressed as the absolute value) if the institution's net open positions in United States dollars and Hong Kong dollars are opposite positions.

Division 6—Calculation of Market Risk Capital Charge for Commodity Exposures

297. Preliminary steps to calculating market risk capital charge

(1) An authorized institution shall, for the purposes of calculating the market risk capital charge for its positions in commodities and commodity-related derivative contracts—

(a) convert its gross (long plus short) position in each commodity to which those positions relate (measured in barrels, kilograms or grams or such other standard unit of measurement as is applicable to the commodity concerned) into monetary terms at the current market price of the commodity;

(b) subject to Division 7, treat positions arising from commodity option contracts as commodity exposures;

(c) value a futures contract or forward contract relating to a commodity by reference to the notional amount of the standard unit of measurement of the commodity converted into monetary terms at current market price and apply the maturity method to any interest rate exposure arising out of that contract;

(d) in the case of a commodity swap contract under which one leg of the swap contract relates to a position or series of positions referenced to a fixed price and the other leg of the swap contract relates to a position or series of positions referenced to the current market price of a reference commodity or commodities—

(i) for each payment under the swap contract, value each of the positions at the notional amount of the swap contract;

(ii) treat each such position—

(A) as long if the institution is paying at a fixed price and receiving at a floating market price; and

(B) as short if the institution is receiving at a fixed price and paying at a floating market price; and

(iii) treat any such leg which involves receiving or paying at a fixed or floating interest rate as an interest rate exposure to which the maturity method applies.

(2) An authorized institution—

(a) subject to paragraph (b), may, for the purposes referred to in subsection (1), offset long and short positions in the same commodity when calculating its open positions;

(b) shall not so offset its positions in different types of commodities.

(3) In this section—

current market price (現行市場價格) means the current market price as determined in accordance with section 4A as if measured at fair value. *(L.N. 137 of 2011)*

298. Calculation of market risk capital charge

An authorized institution shall calculate the market risk capital charge for its commodity exposures as the sum of—

(a) 15% of the institution's net position in each commodity; and

(b) 3% of the institution's gross (long plus short) position in each commodity.

Division 7—Calculation of Market Risk Capital Charge for Option Exposures: General

299. Approaches which authorized institution may use to calculate market risk capital charge for option exposures

An authorized institution shall, for the purposes of calculating the market risk capital charge for its option exposures to debt securities, interest rates, equities, foreign exchange (including gold) and commodities—

(a) subject to paragraph (c) and section 300, use the simplified approach;

(b) subject to paragraph (c) and section 302, use the delta-plus approach; or

(c) with the prior consent of the Monetary Authority, use another approach.

Division 8—Calculation of Market Risk Capital Charge for Option Exposures: Simplified Approach

300. Application of Division 8

(1) An authorized institution shall not use the simplified approach to calculate the market risk capital charge for its option exposures unless the institution—

(a) purchases option contracts but does not write option contracts; or

(b) purchases option contracts and only writes option contracts which are fully hedged by matched long positions in the same option contracts.

(2) An authorized institution which uses the simplified approach to calculate the market risk capital charge for its option exposures shall—

(a) exclude from that calculation—

(i) option contracts written by it; and

(ii) the corresponding purchased option contracts which fully hedge the option contracts referred to in subparagraph (i); and

(b) only use its outstanding purchased option contracts for that calculation.

301. Calculation of market risk capital charge for outstanding purchased option contracts

(1) Subject to subsection (3), an authorized institution shall, for the purposes of calculating the market risk capital charge for its outstanding purchased option contracts (with or without related positions in the underlying exposures of those option contracts)—

(a) where the institution has—

(i) a long position in a put option contract and a long position in the underlying exposure of the put option contract; or

(ii) a long position in a call option contract and a short position in the underlying exposure of the call option contract,

multiply the fair value of the position in the underlying exposure of the option contract by the sum of the market risk capital charge factors for general market risk and specific risk for the position in the underlying exposure of such option contract as set out in Table 31 less the amount by which the option contract is in-the-money (if any);

(b) where the institution has a long position in a put option contract or a long position in a call option contract, use the lesser of—

(i) the fair value of the underlying exposure of the option contract multiplied by the sum of the market risk capital charge factors for general market risk and specific risk for the underlying exposure of such option contract as set out in Table 31; or

(ii) the fair value of the option contract; and

(c) calculate in a way such that—

(i) the market risk capital charge is calculated separately for individual option contracts but together with the related position in the underlying exposure of such option contracts;

(ii) the institution uses the sum of the market risk capital charge for individual option contracts to calculate the total market risk capital charge for its portfolio of option exposures.

Table 31

Market Risk Capital Charge Factor for Each Risk Category

Risk category	Market risk capital charge factor for specific risk	Market risk capital charge factor for general market risk
interest rate	as per the market risk capital charge factors for specific risk set out in Table 28 according to the class, credit quality grade and residual maturity	as per the risk-weights set out in Table 30 according to the residual maturity for fixed rate exposures or residual term to next interest fixing date for floating rate exposures and coupon rate

Risk category	Market risk capital charge factor for specific risk	Market risk capital charge factor for general market risk
equity	8.00%	8.00%
foreign exchange	0.00%	8.00%
commodity	0.00%	15.00%

(2) For the purposes of subsection (1)(a), where the amount derived from the calculation under that subsection is negative, an authorized institution shall treat the market risk capital charge for the relevant outstanding purchased option contract and the position in the underlying exposure of such option contract as zero.

(3) Where it is unclear to an authorized institution which side of an option contract purchased by it constitutes the underlying exposure for the purposes of the simplified approach, the institution shall take the exposure which would be received by it if the option under the contract were exercised to be the underlying exposure for this purpose.

(4) An authorized institution shall, for the purposes of calculating the market risk capital charge for an option contract purchased by it which has a residual maturity of more than 6 months—

(a) subject to paragraph (b), compare the strike price of the option contract with the forward price of the underlying exposure of the option contract;

(b) if it is not practicable for the institution to comply with paragraph (a), take the amount by which the option contract is considered to be in-the-money as zero.

(5) An authorized institution shall add the market risk capital charge calculated under this Division to the market risk capital charge calculated for the risk category concerned.

Division 9—Calculation of Market Risk Capital Charge for Option Exposures: Delta-plus Approach

302. Application of Division 9

An authorized institution which writes option contracts (other than such an authorized institution which, by virtue of section 300(1)(b), uses the simplified approach) shall—

(a) incorporate the delta-weighted positions of its outstanding option contracts into their respective risk categories; and

(b) calculate and provide the following market risk capital charges against those positions—

(i) the market risk capital charge for general market risk and specific risk for delta risk;

(ii) the market risk capital charge for gamma risk; and

(iii) the market risk capital charge for vega risk.

303. Delta risk

An authorized institution shall, for the purposes of calculating its delta risk—

(a) slot its delta-weighted positions which have debt securities or interest rates as the underlying exposures of the relevant option contracts into the time bands set out in Table 30;

(b) treat its interest rate option contracts as having long and short positions such that—

(i) one position is referenced to the time the option contract concerned takes effect; and

(ii) the other position is referenced to the time the option contract concerned matures;

(c) subject to paragraph (d), calculate the market risk capital charge for its option contracts with equities or equity indices as the underlying exposure by applying the calculation treatment under Division 4 to the delta-weighted positions of those option contracts;

(d) for the purposes of paragraph (c), treat equities or equity indices on each exchange as a separate underlying exposure;

(e) calculate the market risk capital charge for its option contracts with foreign exchange or gold as the underlying exposure by applying the calculation treatment under Division 5 to the net delta-weighted positions (being the difference between the institution's total delta-weighted long positions and its total delta-weighted short positions) of those option contracts; and

(f) calculate the market risk capital charge for its option contracts with commodities as the underlying exposure by applying the calculation treatment under Division 6 to the delta-weighted positions of those option contracts.

304. Gamma risk

(1) An authorized institution shall calculate the gamma impact of each of its option contracts by the use of Formula 28.

Formula 28

Calculation of Gamma Impact of Option Contracts

$$\text{Gamma impact} = 1/2 \times \text{Gamma} \times VU^2$$

where—

VU = variation of the underlying exposure of the option contract calculated as—

(a) for option contracts relating to debt securities, debt security indices and interest rates, the fair value of that underlying exposure multiplied by the risk-weight for the appropriate time band set out in Table 30;

(b) for option contracts relating to equities and equity indices, the fair value of that underlying exposure multiplied by 8%;

(c) for option contracts relating to foreign exchange (including gold), the fair value of that underlying exposure multiplied by 8%; and

(d) for option contracts relating to commodities, the fair value of that underlying exposure multiplied by 15%.

(2) For the purposes of subsection (1), an authorized institution shall treat the following positions as the same underlying exposure—

(a) for interest rate exposures, positions within each time band set out in Table 30;

(b) for equities and equity indices exposures, positions on each exchange;

(c) for foreign exchange and gold exposures, positions in each currency pair and gold; and

(d) for commodity exposures, positions in each commodity.

(3) An authorized institution shall—

(a) offset the positive and negative gamma impacts for each option contract on the same underlying exposure to produce a positive or negative net gamma impact for that exposure; and

(b) only use negative net gamma impacts to calculate the market risk capital charge for gamma risk.

(4) An authorized institution shall calculate the total market risk capital charge for gamma risk as the sum of the absolute value of the negative net gamma impacts.

305. Vega risk

(1) An authorized institution shall calculate the market risk capital charge for vega risk by multiplying the sum of the vegas for all its option contracts on the same underlying exposure, applying section 304(2) by a positive or negative change of 25% in the volatility of the value of the underlying exposures of those option contracts. *(L.N. 267 of 2006)*

(2) An authorized institution shall calculate the total market risk capital charge for vega risk as the sum of the absolute value of the individual market risk capital charges for vega risk calculated under subsection (1).

Division 10—Calculation of Market Risk Capital Charge for Credit Derivative Contracts Booked in Authorized Institutions' Trading Book

306. Application of Division 10

(1) This Division applies to credit derivative contracts booked in an authorized institution's trading book.

(2) An authorized institution shall use the notional amount of the credit derivative contract to calculate the market risk capital charge for its credit derivative contracts except for section 312(6) and (7) where the fair value of the credit-linked note shall be used.

307. Specific risk

(1) Where an authorized institution has entered into a total return swap or credit default swap as the protection seller, the institution shall record a long position in the reference obligation specified in the swap contract.

(2) Where an authorized institution has entered into a total return swap or credit default swap as the protection buyer, the institution shall record a short position in the reference obligation specified in the swap contract.

(3) Where an authorized institution has purchased a credit-linked note, the institution shall record a long position in—

(a) the reference obligation specified in the note; and

(b) the note issuer.

(4) Where an authorized institution has issued a credit-linked note, the institution shall record a short position in the reference obligation specified in the note.

(5) Subject to subsection (6), an authorized institution must, for the purposes of calculating the market risk capital charge for specific risk for n^{th}-to-default credit derivative contracts that fall within section 286(a)(iv)—

(a) subject to paragraph (b), apply section 287 and Division 10; and

(b) if the n^{th}-to-default credit derivative contract has an ECAI issue specific rating, in respect of positions in which the institution is the protection seller, apply section 287A as if that contract were a securitization exposure. *(L.N. 137 of 2011; L.N. 156 of 2012; L.N. 175 of 2017; L.N. 167 of 2023)*

(6) Subject to subsection (7), for the purposes of subsection (5)—

(a) subject to paragraph (b), where an authorized institution has a position in one of the reference obligations underlying a first-to-default credit derivative contract and the contract hedges that position, the institution may offset with respect to the hedged amount—

(i) the market risk capital charge for specific risk for its position in the reference obligation; and

(ii) that part of the market risk capital charge for specific risk for the credit derivative contract that relates to the reference obligation in which the institution has that position; and

(b) where an authorized institution has multiple positions in the reference obligations underlying a first-to-default credit derivative contract, the offsetting of market risk capital charge otherwise allowed under paragraph (a) is allowed only for its positions in the underlying reference obligation having the lowest market risk capital charge for specific risk. *(L.N. 137 of 2011)*

(7) For the purposes of subsection (6), an authorized institution—

(a) must offset the long and short positions in identical first-to-default credit derivative contracts before applying that subsection; and

(b) must not offset the market risk capital charge for specific risk for its position in any n^{th}-to-default credit derivative contract, where n is greater than 1, with the market risk capital charge for its position in any underlying reference obligation. *(L.N. 137 of 2011)*

(8) *(Repealed L.N. 137 of 2011)*

(9) Where an authorized institution enters into a credit default swap, total return swap or credit-linked note which provides for payment to be made proportionately in respect of the reference obligations in the basket of reference obligations specified in the swap contract or note, as the case may be, the institution shall record its positions in the reference obligations according to their respective proportions specified in the swap contract or note, as the case may be.

(10) Where an authorized institution has purchased or issued a credit-linked note which is referenced to multiple reference obligations and satisfies the conditions for a qualifying debt security or debt-related derivative contract set out in section 287(4), the institution may—

(a) if it has purchased the note, record the specific risk arising from its long positions in the multiple reference obligations specified in the note as a single long position in the note;

(b) if it has issued the note, record the specific risk arising from its short positions in the multiple reference obligations specified in the note as a single short position in the note.

308. Use of credit derivative contracts to offset specific risk

(1) Subject to subsection (2) and section 307(6), an authorized institution may use a credit derivative contract booked in the institution's trading book to offset the market risk capital charge for specific risk calculated for the institution's trading book position in the underlying exposure in accordance with section 309, 310 or 311. *(L.N. 137 of 2011)*

(1A) Subject to subsection (2), an authorized institution may use a credit derivative contract booked in the institution's trading book to offset the market risk capital charge for specific risk calculated for the institution's trading book position in another credit derivative contract in accordance with—

(a) section 309 (excluding section 309(1)(b)) with all necessary modifications;

(b) section 310 with all necessary modifications; or

(c) section 311 (excluding section 311(1)(a)) with all necessary modifications. *(L.N. 51 of 2013)*

(2) Where section 309, 310 or 311 does not permit an authorized institution to use a credit derivative contract booked in the institution's trading book to offset the market risk capital charge for specific risk calculated for the institution's trading book position in the underlying exposure or in another credit derivative contract, the institution shall calculate and provide the market risk capital charge against both trading book positions.

(L.N. 51 of 2013)

309. Offsetting in full

(1) For the purposes of section 308(1), an authorized institution may offset 100% of the market risk capital charge for specific risk for its position in a credit derivative contract against that for a position in the underlying exposure which is identical to the reference obligation specified in the contract where the values of the 2 positions, being the long or short position in the contract, and the short or long position respectively in the underlying exposure which is identical to the reference obligation specified in the contract, always move in the opposite direction and broadly to the same extent due to— *(L.N. 51 of 2013)*

(a) the 2 positions consisting of identical exposures; or

(b) a long or short position in the underlying exposure being hedged by a total return swap and there being a match between the reference obligation specified in the total return swap and the position in the underlying exposure in every respect, and notwithstanding that the maturity of the total return swap may be different from that of the position in the underlying exposure.

(2) Where an authorized institution offsets the market risk capital charge for specific risk for its positions pursuant to subsection (1), no market risk capital charge for specific risk is required to be calculated in respect of those positions. *(L.N. 51 of 2013)*

310. Offsetting by 80%

(1) For the purposes of section 308(1), an authorized institution may offset 80% of the market risk capital charge for specific risk for its position in a credit derivative contract against that for a position in the underlying exposure which is identical to the reference obligation specified in the contract where— *(L.N. 137 of 2011; L.N. 51 of 2013)*

(a) the values of the 2 positions, being the long or short position in the contract, and the short or long position respectively in the underlying exposure which is identical to the reference obligation specified in the contract, always move in the opposite direction but not broadly to the same extent as set out in section 309(1); and

(b) the institution demonstrates to the satisfaction of the Monetary Authority that the contract can mitigate the credit risk of the institution's position in the underlying exposure effectively.

(2) For the purposes of the demonstration referred to in subsection (1)(b), an authorized institution falls within that subsection in any case where—

(a) subject to paragraphs (b), (c) and (d), the institution's long or short position in the underlying exposure referred to in that subsection is effectively hedged by a credit default swap or credit-linked note;

(b) there is a match between—

(i) the reference obligation specified in the credit default swap or credit-linked note referred to in paragraph (a) and the position in the underlying exposure;

(ii) the maturity of the reference obligation specified in the credit default swap or credit-linked note referred to in paragraph (a) and of the swap contract or note, as the case may be; and

(iii) the currency in which the credit default swap or credit-linked note referred to in paragraph (a) and the position in the underlying exposure are denominated; *(L.N. 51 of 2013)*

(c) the credit event definitions and settlement mechanisms and other key factors of the credit default swap or credit-linked note referred to in paragraph (a) do not cause the price movement of the swap contract or note, as the case may be, to materially deviate from the price movement of the position in the underlying exposure; and

(d) the credit default swap or credit-linked note referred to in paragraph (a) transfers risk effectively taking account of any restrictive payout provisions (including fixed payouts and materiality thresholds).

(3) Where an authorized institution offsets the market risk capital charge for specific risk for its positions pursuant to subsection (1)— *(L.N. 51 of 2013)*

(a) only 20% of the market risk capital charge for specific risk is required to be calculated for the position with the higher market risk capital charge for specific risk; and

(b) the market risk capital charge for specific risk to be calculated for the other position shall be zero.

311. Other offsetting

(1) For the purposes of section 308(1), an authorized institution may offset partially the market risk capital charge for specific risk for its position in a credit derivative contract against that for a position in the underlying exposure where the values of the 2 positions, being the long or short position in the contract, and the short or long position respectively in the underlying exposure, usually move in the opposite direction in any case where— *(L.N. 137 of 2011; L.N. 51 of 2013)*

(a) the positions would fall within section 309(1)(b) but for there being an asset mismatch between the reference obligation specified in the contract and the position in the underlying exposure (being that the reference obligation and the position in the underlying exposure are similar but not identical) and— *(L.N. 51 of 2013)*

(i) the reference obligation specified in the contract ranks for payment or repayment equally with, or junior to, the position in the underlying exposure; and

(ii) the obligor in respect of the position in the underlying exposure is the same legal entity as the obligor in respect of the reference obligation and legally enforceable cross default or cross acceleration clauses are included in the terms of the position in the underlying exposure and the reference obligation;

(b) the positions would fall within section 309(1)(a) or 310 but for there being a currency or maturity mismatch between the contract and the position in the underlying exposure; or

(c) the positions would fall within section 310 but for there being an asset mismatch between the reference obligation specified in the contract and the position in the underlying exposure (being that the reference obligation and the position in the underlying exposure are similar but not identical) and the position in the underlying exposure is included in one of the deliverable obligations specified in the contract. *(L.N. 51 of 2013)*

(2) Where an authorized institution offsets the market risk capital charge for specific risk for its positions pursuant to subsection (1)—

(a) 100% of the market risk capital charge for specific risk is required to be calculated for the position with the higher market risk capital charge for specific risk; and

(b) the market risk capital charge for specific risk to be calculated for the other position is to be zero. *(L.N. 51 of 2013)*

312. General market risk

(1) Where an authorized institution has entered into a total return swap as the protection seller, the institution shall—

(a) record a long position in the reference obligation specified in the swap contract;

(b) if there are periodic interest payments under the swap contract, record a short position in a specific risk-free security with fixed or floating rate interest according to the payment terms of the swap contract.

(2) Where an authorized institution has entered into a total return swap as the protection buyer, the institution shall—

(a) record a short position in the reference obligation specified in the swap contract;

(b) if there are periodic interest payments under the swap contract, record a long position in a specific risk-free security with fixed or floating rate interest according to the payment terms of the swap contract.

(3) Where an authorized institution has entered into a credit default swap with no periodic premiums or interest payments under the swap contract, the institution is not required to calculate or provide the market risk capital charge for general market risk for the swap contract.

(4) Where an authorized institution has entered into a credit default swap as the protection seller with periodic premiums or interest payments under the swap contract, the institution shall record a long position in a specific risk-free security with fixed or floating rate interest according to the payment terms of the swap contract.

(5) Where an authorized institution has entered into a credit default swap as the protection buyer with periodic premiums or interest payments under the swap contract, the institution shall record a short position in a specific risk-free security with fixed or floating rate interest according to the payment terms of the swap contract.

(6) Where an authorized institution has purchased a credit-linked note, the institution shall record a long position in the note.

(7) Where an authorized institution has issued a credit-linked note, the institution shall record a short position in the note.

313-314. *(Repealed L.N. 167 of 2023)*

Division 11—*(Repealed L.N. 167 of 2023)*

315-317. *(Repealed L.N. 167 of 2023)*

317A. *(Repealed L.N. 167 of 2023)*

317B. *(Repealed L.N. 167 of 2023)*

317C. *(Repealed L.N. 167 of 2023)*

318-319. *(Repealed L.N. 167 of 2023)*

Division 12—*(Repealed L.N. 167 of 2023)*

320-322. *(Repealed L.N. 167 of 2023)*

Division 13—Calculation of Market Risk Capital Charge under IMA

(Division 13 added L.N. 167 of 2023)

322A. Application of Division 13

(1) This Division applies to an authorized institution that uses the IMA to calculate its market risk capital charge.

(2) In this Division—

(a) a reference to an authorized institution is a reference to an authorized institution that uses the IMA to calculate its market risk capital charge; and

(b) a reference to an approved trading desk is a reference to a trading desk specified in an approval under section 18(2)(a).

322B. Calculation of risk-weighted amount for market risk before first anniversary of commencement of profit and loss attribution test

(1) This section applies at any time before the first anniversary of the day on which section 322G comes into operation*.

(2) An authorized institution must calculate its risk-weighted amount for market risk as the sum of—

(a) the product of 12.5 and the market risk capital charge calculated under section 322D for all approved trading desks that fulfil the back-testing requirements in section 322G(1), independent of the zone they are assigned to in the profit and loss attribution test; and

(b) the risk-weighted amount for market risk calculated under the STM approach for—

(i) approved trading desks to which section 19A applies; and

(ii) trading desks that are not approved trading desks.

Editorial Note:

* Operation date: 1 January 2025.

322C. Calculation of risk-weighted amount for market risk on and after first anniversary of commencement of profit and loss attribution test

(1) This section applies at any time on or after the first anniversary of the day on which section 322G comes into operation*.

(2) If none of the approved trading desks of an authorized institution is assigned to the yellow zone in the profit and loss attribution test under section 322G(4), the institution must

calculate its risk-weighted amount for market risk as the sum of—

(a) the product of 12.5 and the market risk capital charge calculated under section 322D for all approved trading desks that fulfil the back-testing requirements in section 322G(1) and are assigned to the green zone in the profit and loss attribution test; and

(b) the risk-weighted amount for market risk calculated under the STM approach for—

(i) approved trading desks to which section 19A applies; and

(ii) trading desks that are not approved trading desks.

(3) If at least one approved trading desk of an authorized institution is assigned to the yellow zone in the profit and loss attribution test under section 322G(4), the institution must calculate its risk-weighted amount for market risk in accordance with Formula 28A.

Formula 28A

Calculation of Risk-weighted Amount with at least One Approved Trading Desk in Yellow Zone

$$\mathrm{RWA} = 12.5 \cdot \left[\min\left(\mathrm{IMA}_{G,Y} + \text{Capital surcharge} + C_u\ ,\ \mathrm{SA}_{\text{all desks}}\right) + \max\left(0, \mathrm{IMA}_{G,Y} - \mathrm{SA}_{G,Y}\right)\right]$$

where—

(a) RWA is the risk-weighted amount;

(b) Capital surcharge is the surcharge calculated in accordance with section 322H;

(c) C_u is the market risk capital charge calculated under the STM approach for approved trading desks to which section 19A applies and trading desks that are not approved trading desks;

(d) $IMA_{G,Y}$ is the market risk capital charge calculated under section 322D for all approved trading desks that fulfil the back-testing requirements in section 322G(1) and are assigned to the green or yellow zone in the profit and loss attribution test;

(e) $SA_{all\ desks}$ is the market risk capital charge for all trading desks calculated under the STM approach; and

(f) $SA_{G,Y}$ is the market risk capital charge calculated under the STM approach for all approved trading desks that fulfil the back-testing requirements in section 322G(1) and are assigned to the green or yellow zone in the profit and loss attribution test.

Editorial Note:

* Operation date: 1 January 2025.

322D. Calculation of market risk capital charge for approved trading desks under IMA

(1) This section applies to the calculation of an authorized institution's market risk capital charge for approved trading desks that fulfil the back-testing requirements in section 322G(1) and are assigned to the green or yellow zone in the profit and loss attribution test.

(2) The institution must calculate the market risk capital charge by using its internal models as the sum of—

(a) the greater of the following—

(i) the sum of—

(A) the institution's latest available market risk capital charge for modellable risk factors, calculated in accordance with subsection (3); and

(B) the institution's latest available market risk capital charge for NMRFs, calculated in accordance with subsection (4);

(ii) the sum of—

(A) the average market risk capital charge for modellable risk factors, calculated in accordance with subsection (3), for the last 60 trading days, multiplied by a multiplication factor m_c determined under section 322E(1); and

(B) the average market risk capital charge for NMRFs, calculated in accordance with subsection (4), for the last 60 trading days; and

(b) the default risk charge.

(3) The institution must calculate the market risk capital charge for modellable risk factors by using its internal models in accordance with Formula 28B.

Formula 28B

Calculation of Market Risk Capital Charge for Modellable Risk Factors

$$\mathrm{IMCC} = 0.5 \cdot (\mathrm{IMCC(C)}) + 0.5 \cdot \left(\sum_{i=1}^{5} \mathrm{IMCC}(\mathrm{C_i}) \right)$$

where—

(a) IMCC is the market risk capital charge for modellable risk factors;

(b) IMCC(C) is the unconstrained ES capital charge at the portfolio-wide level, with no constraint on cross-risk class correlations, calculated in accordance with Formula 28C; and

Formula 28C

Calculation of Unconstrained ES Capital Charge

$$\mathrm{IMCC(C)} = \mathrm{ES_{R,S}} \cdot \max\left(\frac{\mathrm{ES_{F,C}}}{\mathrm{ES_{R,C}}}, 1 \right)$$

where—

(i) IMCC(C) is the unconstrained ES capital charge at the portfolio-wide level;

(ii) $\mathrm{ES_{F,C}}$ is the current ES calculated under subsection (7) with the full set of modellable risk factors across all 5 risk classes;

(iii) $ES_{R,C}$ is the current ES calculated under subsection (7) with the reduced set of modellable risk factors across all 5 risk classes; and

(iv) $ES_{R,S}$ is the stressed ES calculated under subsection (7) with the reduced set of modellable risk factors across all 5 risk classes.

(c) $IMCC(C_i)$ is the constrained ES capital charge at the risk class level calculated in accordance with Formula 28D.

Formula 28D

Calculation of Constrained ES Capital Charge

$$IMCC(C_i) = ES_{R,S,i} \cdot \max\left(\frac{ES_{F,C,i}}{ES_{R,C,i}}, 1\right)$$

where—

(i) $IMCC(C_i)$ is the constrained ES capital charge at the risk class level;

(ii) $ES_{F,C,i}$ is the current ES calculated under subsection (7) with the full set of modellable risk factors within risk class i;

(iii) $ES_{R,C,i}$ is the current ES calculated under subsection (7) with the reduced set of modellable risk factors within risk class i; and

(iv) $ES_{R,S,i}$ is the stressed ES calculated under subsection (7) with the reduced set of modellable risk factors within risk class i.

(4) The institution must calculate the market risk capital charge for NMRFs by using its internal models in accordance with Formula 28E.

Formula 28E

Calculation of Market Risk Capital Charge for NMRFs

$$SES = \sqrt{\sum_{i=1}^{I} ISES_{NM,i}^2} + \sqrt{\sum_{j=1}^{J} ISES_{NM,j}^2} + \sqrt{\left(0.6 \cdot \sum_{k=1}^{K} SES_{NM,k}\right)^2 + 0.64 \cdot \sum_{k=1}^{K} SES_{NM,k}^2}$$

where—

(a) SES is the market risk capital charge for NMRFs;

(b) $ISES_{NM,i}$ is the stress scenario capital charge for the idiosyncratic credit spread NMRF i from the I risk factors where the institution has demonstrated to the satisfaction of the Monetary Authority that it is appropriate to aggregate all I idiosyncratic credit spread NMRFs with a zero correlation assumption;

(c) $ISES_{NM,j}$ is the stress scenario capital charge for the idiosyncratic equity NMRF j from the J risk factors where the institution has demonstrated to the satisfaction of the Monetary Authority that it is appropriate to aggregate all J idiosyncratic equity NMRFs with a zero correlation assumption; and

(d) $SES_{NM,k}$ is the stress scenario capital charge for the NMRF k other than the I idiosyncratic credit spread NMRFs and the J idiosyncratic equity NMRFs.

(5) For the purposes of calculating the current ES and stressed ES for the purposes of subsection (3), the institution must—

(a) obtain the approval of the Monetary Authority to use a reduced set of modellable risk factors and for any update of the set;

(b) regularly review, and update if necessary, the reduced set of modellable risk factors on at least a quarterly basis or whenever there is an update on the stressed ES relevant period under paragraph (c); and

(c) regularly review, and update if necessary, the stressed ES relevant period on at least a quarterly basis or whenever there are material changes in the composition of the portfolio or in the time series of the relevant risk factors in the portfolio.

(6) The Monetary Authority may grant an approval to an authorized institution under subsection (5)(a) if the Monetary Authority is satisfied that—

(a) the reduced set of modellable risk factors are relevant for the institution's portfolio of exposures;

(b) there is a sufficiently long history of observations for the reduced set of modellable risk factors; and

(c) the ES of the reduced set of modellable risk factors is able to explain at least 75% of the variation of the fully specified ES based on all modellable risk factors on average measured over the preceding 12-week period.

(7) The institution must calculate the current ES and stressed ES in accordance with Formula 28F.

Formula 28F

Calculation of Current ES and Stressed ES

$$\mathrm{ES} = \sqrt{\mathrm{ES_T}(\mathrm{P})^2 + \sum_{j\geq 2}\left(\mathrm{ES_T}(\mathrm{P}, \mathrm{j}) \cdot \sqrt{\frac{(\mathrm{LH_j} - \mathrm{LH_{j-1}})}{\mathrm{T}}}\right)^2}$$

where—

(a) ES is current ES or stressed ES (as the case requires);

(b) P are positions that are exposed to a set of modellable risk factors;

(c) T is the length of the base liquidity horizon of 10 days;

(d) $\mathrm{ES_T(P)}$ is the ES at horizon T of a portfolio with positions P with respect to shocks to the modellable risk factors to which positions P are exposed;

(e) $ES_T(P,j)$ is the ES at horizon T of a portfolio with positions P with respect to shocks to a subset of modellable risk factors with a liquidity horizon that is equal to or longer than LH_j to which positions P are exposed, with other modellable risk factors held constant; and

(f) LH_j is the liquidity horizon where j ranges from 1 to 5 as follows—

(i) LH_1 is 10 days;

(ii) LH_2 is 20 days;

(iii) LH_3 is 40 days;

(iv) LH_4 is 60 days; and

(v) LH_5 is 120 days.

322E. Multiplication factor

(1) The multiplication factor m_c to be used by an authorized institution for the purposes of section 322D(2)(a)(ii)(A) is the sum of—

(a) 1.5;

(b) a back-testing add-on specified for the number of back-testing exceptions in Table 32A for the most recent 250 trading days, determined on the basis of—

(i) all the positions of all approved trading desks using the IMA; and

(ii) the VaR calibrated at a one-tailed 99% confidence level; and

(c) any additional back-testing add-on assigned to the institution under subsection (3).

Table 32A

Add-on Factor for Back-testing Exceptions

Column 1 Item	Column 2 Zone	Column 3 Number of back-testing exceptions	Column 4 Add-on factor
1.	Green	4 or less	0.00
2.	Yellow	5	0.20
3.	Yellow	6	0.26
4.	Yellow	7	0.33
5.	Yellow	8	0.38
6.	Yellow	9	0.42
7.	Red	10 or more	0.50

(2) For the purpose of calculating the number of back-testing exceptions under subsection (1)(b), the institution may exclude any back-testing exception if the institution demonstrates to the satisfaction of the Monetary Authority that—

(a) the back-testing exception relates to an NMRF the market risk capital charge for which exceeds the actual or the hypothetical loss for the day on which the exception occurs; or

(b) the back-testing exception does not result from deficiencies of the relevant internal models.

(3) The Monetary Authority may, by written notice given to an authorized institution, assign an additional back-testing add-on to the institution if the Monetary Authority is satisfied that—

(a) the institution has ceased to satisfy any of the requirements specified in Schedule 3 applicable to or in relation to the institution; or

(b) the institution satisfies all the requirements specified in Schedule 3 applicable to or in relation to the institution but there is a minor imperfection in the relevant internal models due to an assumption or approximation underlying the models.

322F. Calculation of stress scenario capital charge

(1) For the purpose of calculating its stress scenario capital charge, an authorized institution must—

(a) determine a common stress scenario across all idiosyncratic credit spread NMRFs;

(b) determine a common stress scenario across all idiosyncratic equity NMRFs;

(c) determine a common stress scenario across all NMRFs within the same risk class that are not idiosyncratic credit spread NMRFs or idiosyncratic equity NMRFs; or

(d) with the approval of the Monetary Authority, determine a common stress scenario across the NMRFs that belong to the same bucket within a curve, surface or cube.

(2) For the purposes of subsection (1), the model inputs must be calibrated to a 12-month period of significant financial stress to which the institution experiences the largest loss within the set of NMRFs referred to in subsection (1)(a), (b), (c) or (d).

322G. Back-testing requirements and profit and loss attribution test

for approved trading desks

(1) Subject to subsection (5), an approved trading desk fulfils the back-testing requirements if—

(a) there are no more than 12 back-testing exceptions against the VaR calibrated at a one-tailed 99% confidence level for the most recent 250 trading days; and

(b) there are no more than 30 back-testing exceptions against the VaR calibrated at a one-tailed 97.5% confidence level for the most recent 250 trading days.

(2) An approved trading desk is assigned to the green zone in the profit and loss attribution test if—

(a) the Spearman correlation metric is higher than 0.80; and

(b) the Kolmogorov-Smirnov distribution test metric is lower than 0.09.

(3) An approved trading desk is assigned to the red zone in the profit and loss attribution test if—

(a) the Spearman correlation metric is lower than 0.70; or

(b) the Kolmogorov-Smirnov distribution test metric is higher than 0.12.

(4) An approved trading desk is assigned to the yellow zone in the profit and loss attribution test if it is not assigned to the green zone under subsection (2) or the red zone under subsection (3).

(5) For the purpose of calculating the number of back-testing exceptions under subsection (1), an authorized institution may exclude any back-testing exception if the institution demonstrates to the satisfaction of the Monetary Authority that the back-testing exception relates to an NMRF the market risk capital charge for which exceeds the actual or the hypothetical loss for the day on which the exception occurs.

322H. Calculation of capital surcharge for approved trading desks assigned to yellow zone

At any time on or after the first anniversary of the day on which section 322G comes into operation*, the capital surcharge for an approved trading desk that fulfils the back-testing requirements in section 322G(1) and is assigned to the yellow zone in the profit and loss attribution test under section 322G(4) is calculated as the product of—

(a) the market risk capital charge calculated under the STM approach for trading desks that are assigned to the green or yellow zone in the profit and loss attribution test minus the market risk capital charge calculated under the IMA for those trading desks, subject to a floor of zero;

(b) the ratio $\frac{\sum_{i \in Y} SA_i}{\sum_{i \in G,Y} SA_i}$, where—

(i) $\sum_{i \in Y} SA_i$ is the market risk capital charge calculated under the STM approach for approved trading desks that fulfil the back-testing requirements and are assigned to the yellow zone in the profit and loss attribution test; and

(ii) $\sum_{i \in G,Y} SA_i$ is is the market risk capital charge calculated under the STM approach for approved trading desks that fulfil the back-testing requirements and are assigned to the green or yellow zone in the profit and loss attribution test; and

(c) 0.5.

Editorial Note:

* Operation date: 1 January 2025.

Part 8A

Calculation of CVA Risk Capital Charge

(Part 8A added L.N. 167 of 2023)

Division 1—General

322I. Interpretation of Part 8A

In this Part—

CVA delta (CVA得爾塔) means a first order sensitivity to capture the changes in CVA values of an authorized institution's covered transactions and contracts set out in section 322J due to movements in its non-volatility risk factors;

CVA delta risk (CVA得爾塔風險) means the risk of changes in CVA values of an authorized institution's covered transactions and contracts set out in section 322J due to movements in its non-volatility risk factors captured by CVA delta;

CVA vega (CVA維加) means a first order sensitivity to capture the changes in CVA values of an authorized institution's covered transactions and contracts set out in section 322J due to movements in its volatility risk factors;

CVA vega risk (CVA維加風險) means the risk of changes in CVA values of an authorized institution's covered transactions and contracts set out in section 322J due to movements in its volatility risk factors captured by CVA vega;

risk factor (風險因素) has the meaning given by section 281;

RRAO has the meaning given by section 281;

SBM curvature risk (SBM曲率風險) has the meaning given by section 281.

322J. Transactions and contracts to be covered

(1) An authorized institution must calculate the CVA risk capital charge for the following transactions and contracts in both its trading book and its banking book—

(a) its OTC derivative transactions;

(b) if required by the Monetary Authority under subsection (2)—its SFTs that are fair-valued for accounting purposes;

(c) hedges falling within paragraph (a) or (b) that are entered into by it with external counterparties, whether or not those hedges are eligible CVA hedges,

other than any transactions and contracts specified in Schedule 1A.

(2) If the Monetary Authority determines an authorized institution's CVA risk arising from SFTs that are fair-valued for accounting purposes is material, the Monetary Authority may, by written notice given to the institution, require the institution to calculate the CVA risk capital charge for those SFTs.

(3) An authorized institution must include a hedge referred to in subsection (1)(c) in the CVA risk capital charge with respect to the counterparty providing the hedge.

Division 2—Reduced Basic CVA Approach

322K. Application of Division 2

(1) This Division applies to an authorized institution that uses the reduced basic CVA approach to calculate its CVA risk capital charge.

(2) A reference to an authorized institution in this Division is a reference to an authorized institution that uses the reduced basic CVA approach to calculate its CVA risk capital charge.

322L. Calculation of CVA risk capital charge

(1) An authorized institution must calculate its CVA risk capital charge for a portfolio of counterparties by using Formula 28G.

Formula 28G

Calculation of CVA Risk Capital Charge for Portfolio of Counterparties under Reduced Basic CVA Approach

$$\mathrm{BA\_CVA}_{\mathrm{reduced}} = 0.65 \cdot \sqrt{\left(0.5 \cdot \sum_{c} \mathrm{SCVA}_{c}\right)^{2} + 0.75 \cdot \sum_{c} \mathrm{SCVA}_{c}^{2}}$$

where—

(a) $\mathrm{BA\_CVA}_{\mathrm{reduced}}$ is the CVA risk capital charge under the reduced basic CVA approach; and

(b) SCVA_{C} is the standalone CVA risk capital charge applicable to counterparty c calculated under subsection (2).

(2) The institution must calculate its standalone CVA risk capital charge for each counterparty by using Formula 28H.

Formula 28H

Calculation of CVA Risk Capital Charge for Each Counterparty under Reduced Basic CVA Approach

$$\mathrm{SCVA_c} = \frac{1}{1.4} \cdot \mathrm{RW_c} \cdot \sum_{\mathrm{N}} \mathrm{M_N} \cdot \mathrm{EAD_N} \cdot \mathrm{DF_N}$$

where—

(a) $\mathrm{SCVA_C}$ is the standalone CVA risk capital charge applicable to counterparty c;

(b) $\mathrm{RW_C}$ is the risk-weight applicable to counterparty c determined under subsection (3);

(c) $\mathrm{M_N}$ is the effective maturity of a netting set N with counterparty c determined under subsection (5);

(d) $\mathrm{EAD_N}$ is the default risk exposure of a netting set N with counterparty c calculated in a manner permitted under the IMM(CCR) approach or SA-CCR approach or the current exposure method or any of the methods set out in Division 2B of Part 6A, as the case may be; and

(e) $\mathrm{DF_N}$ is a supervisory discount factor of a netting set N with counterparty c, being—

(i) if the institution calculates the default risk exposure of the netting set by using the IMM(CCR) approach—a factor of 1; or

(ii) if the institution does not have an approval to use the IMM(CCR) approach to calculate the default risk exposure of the netting set—a factor equal to $\frac{1-e^{-0.05\ \mathrm{M_N}}}{0.05\ \mathrm{M_N}}$.

(3) For the purposes of paragraph (b) of Formula 28H, the institution must determine the risk-weight applicable to a counterparty—

(a) if the counterparty has an ECAI issuer rating—by mapping the sector and credit quality of the counterparty based on its ECAI issuer rating to the risk-weights in Table 32B; or

(b) if the counterparty does not have an ECAI issuer rating—

(i) where the institution uses the IRB approach to calculate its credit risk for non-securitization exposures to the counterparty—by mapping the internal rating of the counterparty to one of the ECAI issuer ratings based on a mapping scheme approved in writing by the Monetary Authority; or

(ii) where the institution uses the STC approach or BSC approach to calculate its credit risk for non-securitization exposures to the counterparty—by considering the counterparty as unrated and allocating a risk-weight to the counterparty as such under Table 32B.

Table 32B

Risk-weights of Counterparties under Reduced Basic CVA Approach

Column 1	Column 2	Column 3	Column 4
		Risk-weight	
Item	Sector	Investment credit quality grade	Non-investment credit quality grade or unrated
1.	Sovereigns including central banks and multilateral development banks	0.5%	2.0%
2.	Local government, government-backed non-financials, education and public administration	1.0%	4.0%
3.	Financials including government-backed financials	5.0%	12.0%
4.	Basic materials, energy, industrials, agriculture, manufacturing, mining and quarrying	3.0%	7.0%

Column 1	Column 2	Column 3	Column 4
		Risk-weight	
Item	Sector	Investment credit quality grade	Non-investment credit quality grade or unrated
5.	Consumer goods and services, transportation and storage, and administrative and support service activities	3.0%	8.5%
6.	Technology and telecommunications	2.0%	5.5%
7.	Health care, utilities, and professional and technical activities	1.5%	5.0%
8.	Other sector	5.0%	12.0%

(4) For the purposes of paragraph (b) of Formula 28H and subsection (3)—

(a) if a counterparty has 2 ECAI issuer ratings the use of which would result in the allocation of different risk-weights to the counterparty under Table 32B, the institution must use the higher risk-weight; and

(b) if a counterparty has 3 or more ECAI issuer ratings the use of which would result in the allocation of different risk-weights to the counterparty under Table 32B—

(i) if the 2 lowest risk-weights are the same—the institution must use that risk-weight; or

(ii) if the 2 lowest risk-weights are different—the institution must use the higher risk-weight.

(5) For the purposes of paragraph (c) of Formula 28H, the institution must determine the effective maturity of a netting set as M calculated in accordance with section 168 without having regard to section 168(2), as the case requires.

(6) An approval of a mapping scheme by the Monetary Authority under paragraph (b)(i) of Formula 23J that was in force immediately before the commencement date* of Part 3 of the Banking (Capital) (Amendment) Rules 2023 is taken, on and after that date, to be an approval of a mapping scheme by the Monetary Authority under subsection (3)(b)(i) if the mapping scheme is used to map the internal rating of the counterparty to one of the ECAI issuer ratings.

Editorial Note:

* Commencement date: 1 January 2025.

Division 3—Full Basic CVA Approach

322M. Application of Division 3

(1) This Division applies to an authorized institution that uses the full basic CVA approach to calculate its CVA risk capital charge.

(2) A reference to an authorized institution in this Division is a reference to an authorized institution that uses the full basic CVA approach to calculate its CVA risk capital charge.

322N. Calculation of CVA risk capital charge

(1) An authorized institution must calculate its CVA risk capital charge for a portfolio of counterparties by using Formula 28I.

Formula 28I

Calculation of CVA Risk Capital Charge for Portfolio of Counterparties under Full Basic CVA Approach

$$\mathrm{BA\_CVA}_{\mathrm{full}} = 0.25 \cdot \mathrm{BA\_CVA}_{\mathrm{reduced}} + 0.75 \cdot \mathrm{BA\_CVA}_{\mathrm{hedged}}$$

where—

(a) $\mathrm{BA\_CVA}_{\mathrm{full}}$ is the CVA risk capital charge under the full basic CVA approach;

(b) $\mathrm{BA\_CVA}_{\mathrm{reduced}}$ is the CVA risk capital charge under the reduced basic CVA approach calculated in accordance with section 322L; and

(c) $\mathrm{BA\_CVA}_{\mathrm{hedged}}$ is the amount calculated under subsection (2).

(2) For the purposes of paragraph (c) of Formula 28I, the institution must calculate $\mathrm{BA\_CVA}_{\mathrm{hedged}}$ by using Formula 28J.

Formula 28J

Calculation of $\mathrm{BA\_CVA}_{\mathrm{hedged}}$

$$BA\_CVA_{hedged}=0.65\cdot\sqrt{\left(0.5\cdot\sum_c(SCVA_c-SNH_c)-IH\right)^2+0.75\cdot\sum_c(SCVA_c-SNH_c)^2+\sum_c HMA_c}$$

where—

(a) $SCVA_c$ is the standalone CVA risk capital charge applicable to counterparty c calculated under section 322L(2);

(b) SNH_c is a quantity that gives recognition to the reduction in CVA risk of counterparty c arising from a single-name eligible CVA hedge, calculated under subsection (3);

(c) IH is a quantity that gives recognition to the reduction in CVA risk across the portfolio of counterparties arising from index eligible CVA hedges, calculated under subsection (4); and

(d) HMA_c is a quantity that characterizes the hedging misalignment of indirect eligible CVA hedges if the hedges do not directly reference counterparty c, calculated under subsection (5).

(3) For the purposes of paragraph (b) of Formula 28J, the institution must calculate SNH_c by using Formula 28K.

Formula 28K

Calculation of SNH_c

$$SNH_c=\sum_{h\in c} r_{hc}\cdot RW_h\cdot M_h^{SN}\cdot B_h^{SN}\cdot DF_h^{SN}$$

where—

(a) r_{hc} is set at—

(i) 100% if the single-name eligible CVA hedge h directly references counterparty c;

(ii) 80% if the single-name eligible CVA hedge h has a legal relationship with counterparty c; or

(iii) 50% if the single-name eligible CVA hedge h shares the same sector and region as counterparty c;

(b) RW_h is the risk-weight applicable to the reference name under a single-name eligible CVA hedge h, determined in the same manner as the risk-weight applicable to counterparty c is determined under section 322L(3);

(c) M_h^{SN} is the remaining maturity of the single-name eligible CVA hedge h expressed in years;

(d) B_h^{SN} is—

(i) subject to subparagraph (ii), the notional amount of the single-name eligible CVA hedge h; or

(ii) if the hedge is a single-name contingent credit default swap, the current market value of the reference obligation specified in the contract; and

(e) DF_h^{SN} is a supervisory discount factor equal to $\frac{1-e^{-0.05 \cdot M_h^{SN}}}{0.05 \cdot M_h^{SN}}$.

(4) For the purposes of paragraph (c) of Formula 28J, the institution must calculate IH by using Formula 28L.

Formula 28L

Calculation of IH

$$IH = \sum_i RW_i \cdot M_i^{ind} \cdot B_i^{ind} \cdot DF_i^{ind}$$

where—

(a) RW_i is the risk-weight applicable to index eligible CVA hedge i, determined by—

(i) if all the index constituents belong to the same sector and are of the same credit quality—calculating the risk-weight in the same manner as calculating the risk-weight applicable to counterparty c under section 322L(3) and multiplying the result by 0.7; or

(ii) if the index spans multiple sectors or has a mixture of investment grade constituents or non-investment grade or unrated constituents—calculating the weighted average of the risk-weights attributable to each constituent calculated in the same manner as the risk-weight applicable to counterparty c under section 322L(3) and multiplying the result by 0.7;

(b) M_i^{ind} is the remaining maturity of index eligible CVA hedge i expressed in years;

(c) B_i^{ind} is the notional amount of index eligible CVA hedge i; and

(d) DF_i^{ind} is a supervisory discount factor equal to $\frac{1-e^{-0.05 \cdot M_i^{ind}}}{0.05 \cdot M_i^{ind}}$.

(5) For the purposes of paragraph (d) of Formula 28J, the institution must calculate HMA_c by using Formula 28M.

Formula 28M

Calculation of HMA_c

$$HMA_c = \sum_{h \in c} \left(1 - r_{hc}^2\right) \cdot \left(RW_h \cdot M_h^{SN} \cdot B_h^{SN} \cdot DF_h^{SN}\right)^2$$

where—

(a) r_{hc} has the same meaning as in paragraph (a) of Formula 28K;

(b) RW_h has the same meaning as in paragraph (b) of Formula 28K;

(c) M_h^{SN} has the same meaning as in paragraph (c) of Formula 28K;

(d) B_h^{SN} has the same meaning as in paragraph (d) of Formula 28K; and

(e) DF_h^{SN} has the same meaning as in paragraph (e) of Formula 28K.

Division 4—Standardized CVA Approach

322O. Application of Division 4

(1) This Division applies to an authorized institution that uses the standardized CVA approach to calculate its CVA risk capital charge.

(2) A reference to an authorized institution in this Division is a reference to an authorized institution that uses the standardized CVA approach to calculate its CVA risk capital charge.

322P. Calculation of CVA risk capital charge

An authorized institution must calculate its CVA risk capital charge as the sum of—

(a) its CVA delta risk capital charge under section 322Q for all risk classes; and

(b) its CVA vega risk capital charge under section 322R for all risk classes except the counterparty credit spread risk class.

322Q. Calculation of CVA delta risk capital charge

(1) An authorized institution must calculate its CVA delta risk capital charge separately for each risk class in accordance with this section.

(2) For each risk class, the institution must—

(a) subject to subsection (3), determine a CVA delta sensitivity, delta_k^{CVA}, for each CVA delta risk factor k (as defined under section 322S(2)(a)) in accordance with Formula 28N;

Formula 28N

Determination of CVA Delta Sensitivity

$$\mathrm{delta}_k^{\mathrm{CVA}} = \frac{\mathrm{CVA}(k + 0.0001) - \mathrm{CVA}(k)}{0.0001}$$

for interest rate, counterparty credit spread and reference credit spread risk factors; or

$$\mathrm{delta}_k^{\mathrm{CVA}} = \frac{\mathrm{CVA}(1.01k) - \mathrm{CVA}(k)}{0.01}$$

for equity, commodity and foreign exchange risk factors,

where CVA(k) is the aggregate CVA as a function of the CVA delta risk factor k.

(b) subject to subsection (4), in relation to all eligible CVA hedges, determine a fair value delta sensitivity, $\mathrm{delta}_k^{\mathrm{Hdg}}$, for each CVA delta risk factor k (as defined under section 322S(2)(a)) in accordance with Formula 28O;

Formula 28O

Determination of Fair Value Delta Sensitivity in relation to Eligible CVA Hedges

$$\mathrm{delta}_k^{\mathrm{Hdg}} = \frac{V(k + 0.0001) - V(k)}{0.0001}$$

for interest rate, counterparty credit spread and reference credit spread risk factors; or

$$\mathrm{delta}_k^{\mathrm{Hdg}} = \frac{V(1.01k) - V(k)}{0.01}$$

for equity, commodity and foreign exchange risk factors,

where V(k) is the market value of all eligible CVA hedges as a function of the CVA delta risk factor k.

(c) calculate the risk-weighted CVA delta sensitivity, $\mathrm{WS\_delta}_k^{\mathrm{CVA}}$, for each CVA delta risk factor k as the product of $\mathrm{delta}_k^{\mathrm{CVA}}$ and the risk-weight determined under section 322T;

(d) calculate the risk-weighted fair value delta sensitivity, $\mathrm{WS\_delta}_k^{\mathrm{Hdg}}$, for each CVA delta risk factor k as the product of $\mathrm{delta}_k^{\mathrm{Hdg}}$ and the risk-weight determined under section 322T;

(e) calculate the net risk-weighted CVA delta sensitivity, $\mathrm{WS\_delta}_k$, for each CVA delta risk factor k by subtracting the $\mathrm{WS\_delta}_k^{\mathrm{Hdg}}$ from the $\mathrm{WS\_delta}_k^{\mathrm{CVA}}$;

(f) calculate the capital charges for each CVA delta bucket b, K_{b_delta}, by aggregating the net risk-weighted CVA delta sensitivities within the same bucket in accordance with Formula 28P; and

Formula 28P

Calculation of Capital Charges for Each CVA Delta Bucket

$$K_{b\_delta} = \sqrt{\sum_{k\in b} WS\_delta_k^2 + \sum_{k\in b}\sum_{l\in b, l\neq k} \rho_{kl} \cdot WS\_delta_k \cdot WS\_delta_l + 0.01 \cdot \sum_{k\in b}\left(WS\_delta_k^{Hdg}\right)^2}$$

where ρ_{kl} is the correlation parameter between 2 net risk-weighted CVA delta sensitivities within the same bucket that is specified by the Monetary Authority so that it appropriately captures the extent to which the 2 CVA delta risk factors are related.

(g) calculate the CVA delta risk capital charge by aggregating the CVA delta buckets within the risk class in accordance with Formula 28Q.

Formula 28Q

Calculation of CVA Delta Risk Capital Charge

$$K_{CVA\_delta} = m_{CVA} \cdot \sqrt{\sum_{b} K_{b\_delta}^2 + \sum_{b}\sum_{c\neq b} \gamma_{bc} \cdot S_{b\_delta} \cdot S_{c\_delta}}$$

where—

(i) K_{CVA_delta} is the CVA delta risk capital charge;

(ii) m_{CVA} is 1 or the larger number that is assigned by the Monetary Authority by written notice given to the institution, taking into account the level of model risk for the calculation of the CVA sensitivities;

(iii) γ_{bc} is the correlation parameter between 2 CVA delta buckets that is specified by the Monetary Authority so that it appropriately captures the extent to which the 2 CVA delta buckets are related;

(iv) $S_{b\_delta} = \max[-K_{b\_delta}, \min(\sum_k WS\_delta_k, K_{b\_delta})]$ for all CVA delta risk factors in bucket b; and

(v) $S_{c\_delta} = \max[-K_{c\_delta}, \min(\sum_k WS\_delta_k, K_{c\_delta})]$ for all CVA delta risk factors in bucket c.

(3) For the purposes of subsection (2)(a), the institution may determine a CVA delta sensitivity by another formulation if the institution demonstrates to the satisfaction of the Monetary Authority that the other formulation is conceptually sound and yields results very close to Formula 28N.

(4) For the purposes of subsection (2)(b), the institution may determine a fair value delta sensitivity by another formulation if the institution demonstrates to the satisfaction of the Monetary Authority that the other formulation is conceptually sound and yields results very close to Formula 28O.

322R. Calculation of CVA vega risk capital charge

(1) An authorized institution must calculate its CVA vega risk capital charge separately for each risk class except the counterparty credit spread risk class, in accordance with this section.

(2) For each risk class except the counterparty credit spread risk class, the institution must—

(a) subject to subsection (3), determine a CVA vega sensitivity, $vega_k^{CVA}$, for each CVA vega risk factor k (as defined under section 322S(2)(b)) in accordance with Formula 28R;

Formula 28R

Determination of CVA Vega Sensitivity

$$\mathrm{vega}_{k}^{CVA} = \frac{\mathrm{CVA}(1.01k) - \mathrm{CVA}(k)}{0.01}$$

where CVA(k) is the aggregate CVA as a function of the CVA vega risk factor k.

(b) subject to subsection (4), in relation to all eligible CVA hedges, determine a fair value vega sensitivity, vega_{k}^{Hdg}, for each CVA vega risk factor k (as defined under section 322S(2)(b)) in accordance with Formula 28S;

Formula 28S

Determination of Fair Value Vega Sensitivity in relation to Eligible CVA Hedges

$$\mathrm{vega}_{k}^{Hdg} = \frac{V(1.01k) - V(k)}{0.01}$$

where V(k) is the market value of all eligible CVA hedges as a function of the CVA vega risk factor k.

(c) calculate the risk-weighted CVA vega sensitivity, $\mathrm{WS\_vega}_{k}^{CVA}$, for each CVA vega risk factor k as the product of vega_k^{CVA} and the risk-weight determined under section 322T;

(d) calculate the risk-weighted fair value vega sensitivity, $\mathrm{WS\_vega}_k^{Hdg}$, for each CVA vega risk factor k as the product of vega_k^{Hdg} and the risk-weight determined under section 322T;

(e) calculate the net risk-weighted CVA vega sensitivity, $\mathrm{WS\_vega}_k$, for each CVA vega risk factor k by subtracting the $\mathrm{WS\_vega}_k^{Hdg}$ from the $\mathrm{WS\_vega}_k^{CVA}$;

(f) calculate the capital charges for each CVA vega bucket b, K_{b_vega}, by aggregating the net risk-weighted CVA vega sensitivities within the same bucket in accordance with Formula 28T; and

Formula 28T

Calculation of Capital Charges for Each CVA Vega Bucket

$$K_{b\_vega} = \sqrt{\sum_{k \in b} \mathrm{WS\_vega}_k^2 + \sum_{k \in b} \sum_{l \neq k} \rho_{kl} \cdot \mathrm{WS\_vega}_k \cdot \mathrm{WS\_vega}_l + 0.01 \cdot \sum_{k \in b} \left(\mathrm{WS\_vega}_k^{Hdg}\right)^2}$$

where ρ_{kl} is the correlation parameter between 2 net risk-weighted CVA vega sensitivities within the same bucket that is specified by the Monetary Authority so that it appropriately captures the extent to which the 2 CVA vega risk factors are related.

(g) calculate the CVA vega risk capital charge by aggregating the CVA vega buckets within the risk class in accordance with Formula 28U.

Formula 28U

Calculation of CVA Vega Risk Capital Charge

$$K_{CVA\_vega} = m_{CVA} \cdot \sqrt{\sum_{b} K_{b\_vega}^{2} + \sum_{b}\sum_{c \neq b} \gamma_{bc} \cdot S_{b\_vega} \cdot S_{c\_vega}}$$

where—

(i) K_{CVA_delta} is the CVA vega risk capital charge;

(ii) m_{CVA} is 1 or the larger number that is assigned by the Monetary Authority by written notice given to the institution, taking into account the level of model risk for the calculation of the CVA sensitivities;

(iii) γ_{bc} is the correlation parameter between 2 CVA vega buckets that is specified by the Monetary Authority so that it appropriately captures the extent to which the 2 CVA vega buckets are related;

(iv) $S_{b\_vega} = \max[-K_{b\_vega}, \min(\sum_{k} WS\_vega_{k}, K_{b\_vega})]$ for all CVA vega risk factors in bucket b; and

(v) $S_{c\_vega} = \max[-K_{c\_vega}, \min(\sum_k WS\_vega_k, K_{c\_vega})]$ for all CVA vega risk factors in bucket c.

(3) For the purposes of subsection (2)(a), the institution may determine a CVA vega sensitivity by another formulation if the institution demonstrates to the satisfaction of the Monetary Authority that the other formulation is conceptually sound and yields results very close to Formula 28R.

(4) For the purposes of subsection (2)(b), the institution may determine a fair value vega sensitivity by another formulation if the institution demonstrates to the satisfaction of the Monetary Authority that the other formulation is conceptually sound and yields results very close to Formula 28S.

322S. CVA risk factors

(1) An authorized institution must, in respect of a risk class—

(a) determine buckets as specified by the Monetary Authority for the risk class that appropriately distinguish the risk characteristics of risk factors across different buckets; and

(b) allocate each risk-weighted sensitivity calculated under section 322Q(2)(e) and 322R(2)(e) to an appropriate bucket.

(2) An authorized institution must, in respect of a risk class—

(a) define the CVA delta risk factors for its portfolio, at a level of granularity specified by the Monetary Authority, as—

(i) risk-free yields and inflation rates for interest rate risk;

(ii) credit spreads for counterparty credit spread risk and reference credit spread risk;

(iii) equity prices for equity risk;

(iv) commodity prices for commodity risk; and

(v) foreign exchange rates between the Hong Kong dollar and each foreign currency for foreign exchange risk; and

(b) define the CVA vega risk factors for its portfolio, at a level of granularity specified by the Monetary Authority, as the simultaneous relative change of all relevant volatilities of the underlying exposure.

322T. CVA risk-weights

An authorized institution must allocate a risk-weight to each CVA delta risk factor and each CVA vega risk factor at a level specified by the Monetary Authority that sufficiently represents stressed market conditions.

Division 5—Eligible CVA Hedges

322U. Eligible CVA hedges

(1) A hedge is eligible to be taken into account in the calculation of an authorized institution's CVA risk capital charge only if—

(a) the hedge is entered into with an external counterparty or, subject to subsection (2), entered into internally with the trading book;

(b) where the institution uses the full basic CVA approach to calculate its CVA risk capital charge, the hedge is used and managed for the purpose of mitigating the counterparty credit spread component of CVA risk and the hedging instrument used in the hedge is—

(i) subject to subsection (3), a single-name credit default swap;

(ii) subject to subsection (3), a single-name contingent credit default swap; or

(iii) an index credit default swap; and

(c) where the institution uses the standardized CVA approach to calculate its CVA risk capital charge, the hedge is used and managed for the purpose of mitigating the CVA risk and the hedging instrument—

(i) is not split into several effective transactions;

(ii) hedges either the counterparty credit spread component or the exposure component of the CVA risk;

(iii) in relation to the credit spread delta risk, is assigned entirely to the counterparty credit spread risk class or the reference credit spread risk class; and

(iv) is not a securitization exposure or a collective investment scheme that cannot be looked through but is assigned to the trading book.

(2) If the institution enters into an internal CVA hedge with its trading book and the hedge involves an instrument that is subject to the SBM curvature risk, SA-DRC or RRAO under the STM approach, the hedge is eligible only if the trading book additionally enters into a hedge with an external counterparty that exactly offsets the trading book leg of the internal CVA hedge.

(3) If the institution uses the full basic CVA approach to calculate its CVA risk capital charge, the institution may include a single-name credit default swap or single-name contingent credit default swap as an eligible credit default swap only if the swap references—

(a) the counterparty concerned directly;

(b) an entity legally related to the counterparty concerned; or

(c) an entity that belongs to the same sector and region as the counterparty concerned.

(4) For the purposes of subsection (3)(b), a reference entity and a counterparty are legally related if they are—

(a) a holding company and its subsidiary; or

(b) subsidiaries of a common holding company.

(5) If the institution has included in its CVA risk capital charge calculation—

(a) an eligible CVA hedge obtained from an external counterparty, the institution must exclude the hedge from its market risk capital charge calculation; and

(b) the CVA leg of an eligible hedge obtained from its trading book internally, the institution must include the trading book leg of the hedge in its market risk capital charge calculation.

(6) The institution must include all ineligible CVA hedges in the trading book, irrespective of whether the CVA hedge is obtained from an external counterparty or from its trading book and, for an ineligible CVA hedge obtained from its trading book, both the CVA leg and the trading book leg must be included in the trading book.

Part 9

Calculation of Operational Risk

(Part 9 replaced L.N. 167 of 2023)

Division 1—General

323. Interpretation of Part 9

(1) In this Part—

BI means business indicator;

BIC means business indicator component;

bucket 1 AI (組別1 AI) means an authorized institution that is classified into bucket 1 under section 331;

bucket 2 AI (組別2 AI) means an authorized institution that is classified into bucket 2 under section 331;

bucket 3 AI (組別3 AI) means an authorized institution that is classified into bucket 3 under section 331;

business indicator (業務指標), in relation to an authorized institution's calculation of its capital charge for operational risk, means the amount calculated by the institution under section 325(1)(a);

business indicator component (業務指標組成部分), in relation to an authorized institution's calculation of its capital charge for operational risk, means the amount calculated by the institution under Division 4;

dividend income (股息收入) means income of a type specified by the Monetary Authority under subsection (2)(a);

fee and commission expenses (費用及佣金開支) means expenses of a type specified by the Monetary Authority under subsection (2)(b);

fee and commission income (費用及佣金收入) means income of a type specified by the Monetary Authority under subsection (2)(c);

financial component (金融組成部分), in relation to an authorized institution, means the amount calculated by the institution under section 325(2);

first year (第一年度), in relation to the last n years, means the last calendar quarter of those years and the 3 immediately preceding calendar quarters;

formula approach (公式計算法), in relation to an authorized institution's calculation of its ILM, means the approach set out in section 334;

high quality operational loss data (高質業務操作虧損數據) means data that meets the standards specified by the Monetary Authority under subsection (3);

ILM means internal loss multiplier;

interest earning assets (有息資產) means assets of a type specified by the Monetary Authority under subsection (2)(f);

interest expenses (利息開支) means expenses of a type specified by the Monetary Authority under subsection (2)(g);

interest income (利息收入) means income of a type specified by the Monetary Authority under subsection (2)(h);

interest, leases and dividend component (利息、租賃及股息組成部分), in relation to an authorized institution, means the amount calculated by the institution under section 325(3);

internal loss multiplier (內部損失倍率), in relation to an authorized institution's calculation of its capital charge for operational risk, means the multiplier calculated by the institution under Division 5;

last n years (最近n個年度)—

(a) in relation to the calculation of BI, means the last 3 years ending on a calendar quarter end date; and

(b) in relation to the calculation of LC, means the last 5, 6, 7, 8, 9 or 10 years ending on a calendar quarter end date (as the case requires);

LC means loss component;

loss component (損失組成部分), in relation to an authorized institution, means the amount calculated by the institution under section 335;

net interest income (淨利息收入), in relation to an authorized institution, means its interest income after deducting its interest expenses;

net P&L on banking book (銀行帳淨損益), in relation to an authorized institution, means the gains minus losses arising from assets and liabilities booked in the institution's banking book as specified by the Monetary Authority under subsection (2)(d);

net P&L on trading book (交易帳淨損益), in relation to an authorized institution, means the gains minus losses arising from assets and liabilities booked in the institution's trading book as specified by the Monetary Authority under subsection (2)(e);

operational loss event (業務操作虧損事件) means an event specified by the Monetary Authority under subsection (4);

other operating expenses (其他營運開支) means expenses of a type specified by the Monetary Authority under subsection (2)(i);

other operating income (其他營運收入) means income of a type specified by the Monetary Authority under subsection (2)(j);

second year (第二年度), in relation to the last n years, means the year immediately preceding the first year;

services component (服務組成部分), in relation to an authorized institution, means the amount calculated by the institution under section 325(4);

third year (第三年度), in relation to the last n years, means the year immediately preceding the second year;

year (年度) means a period of 4 consecutive calendar quarters.

(2) For the purpose of calculating the BI of an authorized institution, the Monetary Authority may, having regard to Chapter OPE10 of the current Basel Framework, specify the following types of income statement or balance sheet items—

(a) dividend income;

(b) fee and commission expenses;

(c) fee and commission income;

(d) gains minus losses arising from assets and liabilities booked in the banking book;

(e) gains minus losses arising from assets and liabilities booked in the trading book;

(f) interest earning assets;

(g) interest expenses;

(h) interest income;

(i) other operating expenses;

(j) other operating income.

(3) For the purposes of this Part, the Monetary Authority may, having regard to the minimum standards for the use of loss data under the standardized approach set out in Chapter

OPE25 of the current Basel Framework, specify standards in relation to the identification, collection, treatment, validation, review, scope and content of data on operational loss.

(4) For the purposes of this Part, the Monetary Authority may, having regard to Table 2 in Chapter OPE25 of the current Basel Framework, specify events the classification of an operational loss into which forms part of the requirements that the data of an authorized institution must meet for the data to be high quality operational loss data.

Division 2—Calculation of Capital Charge and Risk-weighted Amount for Operational Risk

324. Calculation of capital charge and risk-weighted amount for operational risk

(1) Subject to subsection (3), an authorized institution must calculate its capital charge for operational risk by multiplying its BIC by its ILM.

(2) An authorized institution must calculate its risk-weighted amount for operational risk by multiplying its capital charge for operational risk by 12.5.

(3) An authorized institution that has been in operation for less than 18 months on any calendar quarter end date after this section comes into operation* must obtain the prior consent of the Monetary Authority to calculate its capital charge for operational risk—

(a) by the method specified in subsection (1); or

(b) by an alternative method.

Editorial Note:

* Operation date: 1 January 2025.

Division 3—Calculation of BI

325. Calculation of BI

(1) An authorized institution must—

(a) after each calendar quarter end date, calculate its BI as the sum of—

(i) the financial component;

(ii) the interest, leases and dividend component; and

(iii) the services component; and

(b) in calculating each component, include the data of any acquired business and merged activities over the period prior to the acquisition or merger that is relevant to the calculation.

(2) An authorized institution must calculate the financial component as the sum of—

(a) the arithmetic mean of the absolute value of its net P&L on banking book for the last 3 years; and

(b) the arithmetic mean of the absolute value of its net P&L on trading book for the last 3 years.

(3) An authorized institution must calculate the interest, leases and dividend component as the sum of—

(a) the lower of—

(i) the arithmetic mean of the absolute value of its net interest income for the last 3 years; and

(ii) 2.25% of the arithmetic mean of its interest earning assets for the last 3 years; and

(b) the arithmetic mean of its dividend income for the last 3 years.

(4) An authorized institution must calculate the services component as the sum of—

(a) the higher of—

(i) the arithmetic mean of its fee and commission expenses for the last 3 years; and

(ii) the arithmetic mean of its fee and commission income for the last 3 years; and

(b) the higher of—

(i) the arithmetic mean of its other operating expenses for the last 3 years; and

(ii) the arithmetic mean of its other operating income for the last 3 years.

326. Supplementary provisions for calculation of BI

(1) Subject to section 327, an authorized institution must calculate the arithmetic mean of the absolute value of each of its net P&L on banking book and net P&L on trading book under section 325(2) and its net interest income under section 325(3)(a)(i) for the last 3 years by—

(a) calculating the absolute value of each of the net P&L on banking book, net P&L on trading book and net interest income recognized by the institution in the first year;

(b) calculating the absolute value of each of the net P&L on banking book, net P&L on trading book and net interest income recognized by the institution in the second year;

(c) calculating the absolute value of each of the net P&L on banking book, net P&L on trading book and net interest income recognized by the institution in the third year; and

(d) for each of the net P&L on banking book, net P&L on trading book and net interest income, dividing the sum of the respective absolute values calculated under paragraphs (a), (b) and (c) by 3.

(2) Subject to section 327, an authorized institution must calculate the arithmetic mean of its interest earning assets under section 325(3)(a)(ii) for the last 3 years by—

(a) calculating the arithmetic mean of the interest earning assets as at each of the 4 calendar quarter end dates of the first year;

(b) calculating the arithmetic mean of the interest earning assets as at each of the 4 calendar quarter end dates of the second year;

(c) calculating the arithmetic mean of the interest earning assets as at each of the 4 calendar quarter end dates of the third year; and

(d) dividing the sum of the arithmetic means calculated under paragraphs (a), (b) and (c) by 3.

(3) Subject to section 327, an authorized institution must calculate the arithmetic mean of each of its dividend income under section 325(3)(b) and its fee and commission expenses, fee and commission income, other operating expenses and other operating income under section 325(4) for the last 3 years by, for each of the dividend income, fee and commission expenses, fee and commission income, other operating expenses and other operating income—

(a) aggregating the respective values for the last 3 years; and

(b) dividing the respective aggregate amount by 3.

327. Calculation of BI for authorized institutions operating for 18 months or more but less than 3 years

(1) If, on any calendar quarter end date after this section

comes into operation*, an authorized institution has been in operation for 18 months or more but less than 3 years, the institution must, for the purpose of calculating any arithmetic mean in accordance with section 326—

(a) treat any partial year of operation of 6 months or more as a full year; and

(b) treat any partial year of operation of less than 6 months as zero.

(2) Without prejudice to subsection (1), if, on any calendar quarter end date after this section comes into operation, an authorized institution has been in operation for 2 years and 6 months or more but less than 3 years, the institution must—

(a) calculate the arithmetic mean of the absolute value of each of its net P&L on banking book and net P&L on trading book under section 325(2) and its net interest income under section 325(3)(a)(i) for the last 3 years by—

(i) calculating the absolute value of each of the net P&L on banking book, net P&L on trading book and net interest income recognized by the institution in the first year;

(ii) calculating the absolute value of each of the net P&L on banking book, net P&L on trading book and net interest income recognized by the institution in the second year;

(iii) annualizing the absolute value of each of the net P&L on banking book, net P&L on trading book and net interest income recognized by the institution for the partial year; and

(iv) for each of the net P&L on banking book, net P&L on trading book and net interest income, dividing the sum of the respective absolute values calculated under subparagraphs (i), (ii) and (iii) by 3;

(b) calculate the arithmetic mean of its interest earning assets under section 325(3)(a)(ii) for the last 3 years by—

(i) calculating the arithmetic mean of the interest earning assets as at each of the 4 calendar quarter end dates of the first year;

(ii) calculating the arithmetic mean of the interest earning assets as at each of the 4 calendar quarter end dates of the second year;

(iii) calculating the arithmetic mean of the interest earning assets as at the end of each full calendar quarter within the partial year; and

(iv) dividing the sum of the arithmetic means calculated under subparagraphs (i), (ii) and (iii) by 3; and

(c) calculate the arithmetic mean of each of its dividend income under section 325(3)(b) and its fee and commission expenses, fee and commission income, other operating expenses and other operating income under section 325(4) for the last 3 years by, for each of the dividend income, fee and commission expenses, fee and commission income, other operating expenses and other operating income—

(i) aggregating the respective values for the first year and the second year;

(ii) annualizing the respective values for the partial year; and

(iii) dividing the sum of the respective amounts under subparagraphs (i) and (ii) by 3.

(3) Without prejudice to subsection (1), if, on any calendar quarter end date after this section comes into operation, an authorized institution has been in operation for 2 years or more but less than 2 years and 6 months, the institution must—

(a) calculate the arithmetic mean of the absolute value of each of its net P&L on banking book and net P&L on trading book under section 325(2) and its net interest income under section 325(3)(a)(i) for the last 3 years by—

(i) calculating the absolute value of each of the net P&L on banking book, net P&L on trading book and net interest income recognized by the institution in the first year;

(ii) calculating the absolute value of each of the net P&L on banking book, net P&L on trading book and net interest income recognized by the institution in the second year; and

(iii) for each of the net P&L on banking book, net P&L on trading book and net interest income, dividing the sum of the respective absolute values calculated under subparagraphs (i) and (ii) by 2;

(b) calculate the arithmetic mean of its interest earning assets under section 325(3)(a)(ii) for the last 3 years by—

(i) calculating the arithmetic mean of the interest earning assets as at each of the 4 calendar quarter end dates of the first year;

(ii) calculating the arithmetic mean of the interest earning assets as at each of the 4 calendar quarter end dates of the second year; and

(iii) dividing the sum of the arithmetic means calculated under subparagraphs (i) and (ii) by 2; and

(c) calculate the arithmetic mean of each of its dividend income under section 325(3)(b) and its fee and commission expenses, fee and commission income, other operating expenses and other operating income under section 325(4) for the last 3 years by, for each of the dividend income, fee and commission expenses, fee and commission income, other operating expenses and other operating income—

(i) aggregating the respective values for the first year and the second year; and

(ii) dividing the respective aggregate amount by 2.

(4) Without prejudice to subsection (1), if, on any calendar quarter end date after this section comes into operation, an authorized institution has been in operation for 18 months or more but less than 2 years, the institution must—

(a) calculate the arithmetic mean of the absolute value of each of its net P&L on banking book and net P&L on trading book under section 325(2) and its net interest income under section 325(3)(a)(i) for the last 3 years by—

(i) calculating the absolute value of each of the net P&L on banking book, net P&L on trading book and net interest income recognized by the institution in the first year;

(ii) annualizing the absolute value of each of the net P&L on banking book, net P&L on trading book and net interest income recognized by the institution for the partial year; and

(iii) for each of the net P&L on banking book, net P&L on trading book and net interest income, dividing the sum of the respective absolute values calculated under subparagraphs (i) and (ii) by 2;

(b) calculate the arithmetic mean of its interest earning assets under section 325(3)(a)(ii) for the last 3 years by—

(i) calculating the arithmetic mean of the interest earning assets as at each of the 4 calendar quarter end dates of the first year;

(ii) calculating the arithmetic mean of the interest earning assets as at the end of each full calendar quarter within the partial year; and

(iii) dividing the sum of the arithmetic means calculated under subparagraphs (i) and (ii) by 2; and

(c) calculate the arithmetic mean of each of its dividend income under section 325(3)(b) and its fee and commission expenses, fee and commission income, other operating expenses and other operating income under section 325(4) for the last 3 years by, for each of the dividend income, fee and commission expenses, fee and commission income, other operating expenses and other operating income—

(i) calculating the respective values for the first year;

(ii) annualizing the respective values for the partial year; and

(iii) dividing the sum of the respective amounts under subparagraphs (i) and (ii) by 2.

Editorial Note:

* Operation date: 1 January 2025.

328. Exclusions from BI

(1) An authorized institution must not take into account any of the following in calculating its BI—

(a) expenses or income arising from the institution's insurance or reinsurance underwriting businesses;

(b) premiums paid, or reimbursements or other payments received, in relation to insurance or reinsurance policies purchased;

(c) expenses of an administrative nature, including—

(i) staff expenses;

(ii) outsourcing fees paid for the supply of non-financial services (for example, logistical, information technology or human resources); and

(iii) other administrative expenses;

(d) recovery of administrative expenses, including recovery of payments on behalf of customers;

(e) expenses of premises and fixed assets, other than expenses that result from operational loss events;

(f) depreciation or amortization of tangible and intangible assets, other than depreciation arising from operating lease assets which must be included in interest expenses;

(g) provisions or reversal of provisions (for example, on pensions, commitments and guarantees given) other than provisions arising from operational loss events;

(h) expenses due to share capital repayable on demand;

(i) impairment or reversal of impairment (for example, on financial assets, non-financial assets, investments in subsidiaries, joint ventures and associates);

(j) changes in goodwill recognized in profit and loss accounts;

(k) corporate income tax (being tax based on profits, including current tax and deferred tax).

(2) The Monetary Authority may give approval for an authorized institution to exclude data related to its divested businesses and activities from the calculation of its BI if the institution demonstrates to the satisfaction of the Monetary Authority that the divested businesses and activities are no longer relevant to the institution's risk profile.

Division 4—Calculation of BIC

329. Calculation of BIC

An authorized institution must, after each calendar quarter end date, calculate its BIC by—

(a) separating its BI into 3 portions in accordance with Table 33;

(b) multiplying each portion with the marginal coefficient applicable to that portion as set out in that Table; and

(c) aggregating the 3 products.

Table 33

Calculation of BIC

Column 1	Column 2	Column 3
Item	Portion of BI ($ Billion)	Marginal coefficient
1.	10 or less	12%
2.	More than 10 but not more than 300	15%

Column 1	Column 2	Column 3
Item	Portion of BI ($ Billion)	Marginal coefficient
3.	More than 300	18%

Division 5—Calculation of ILM

330. Calculation of ILM: General

An authorized institution must calculate its ILM in accordance with this Division.

331. Classification of authorized institution for purpose of calculating ILM

For the purpose of calculating its ILM, an authorized institution is classified into one of the buckets set out in Table 33A based on the size of its BI as set out in that Table.

Table 33A

Buckets for Calculating ILM

Column 1	Column 2	Column 3
Item	Bucket	Authorized institution's BI ($ Billion)
1.	1	10 or less
2.	2	More than 10 but not more than 300
3.	3	More than 300

332. ILM for bucket 1 AI

(1) Subject to subsection (2), a bucket 1 AI has an ILM of 1.

(2) A bucket 1 AI may calculate its ILM using the formula approach if—

(a) the bucket 1 AI—

(i) is a subsidiary of a bank; and

(ii) has notified the Monetary Authority, at least 3 months before the bucket 1 AI intends calculating its ILM using the formula approach, that the following conditions have been met—

(A) the bucket 1 AI has maintained high quality operational loss data for at least the last 5 years;

(B) the bucket 1 AI's parent company calculates its ILM on a consolidated basis under the capital rules applicable to the parent company; and

(C) the bucket 1 AI's operational loss data are either included in the calculation of its parent company's ILM or would be included in that calculation were it not for justifiable considerations such as the materiality of the bucket 1 AI in relation to the banking group; or

(b) the bucket 1 AI has obtained the prior consent of the Monetary Authority.

333. ILM for bucket 2 AI and bucket 3 AI

(1) A bucket 2 AI or bucket 3 AI that has maintained high quality operational loss data for at least the last 5 years must calculate its ILM using the formula approach.

(2) Subject to subsections (3), (4) and (5), a bucket 2 AI or bucket 3 AI that has not maintained high quality operational loss data for at least the last 5 years has an ILM of 1.25.

(3) A newly established bucket 2 AI or bucket 3 AI that has been in operation for less than 5 years has an ILM of 1, unless otherwise required by the Monetary Authority.

(4) An authorized institution, on first becoming a bucket 2 AI or bucket 3 AI, may initially have an ILM of 1 for a transitional period of no longer than 9 months, or the longer period agreed with the Monetary Authority.

(5) If a bucket 2 AI or bucket 3 AI is required to calculate its capital adequacy ratio on both a solo basis and a consolidated basis under section 3C and has only maintained high quality operational loss data for at least the last 5 years on a solo basis, it has the following ILM on a consolidated basis—

(a) 1.25, if its ILM calculated on a solo basis using the formula approach is less than or equal to 1;

(b) the higher of 1.25 or its ILM calculated on a solo basis using the formula approach, if the latter is higher than 1.

(6) If a bucket 2 AI or bucket 3 AI has been granted approval under section 28(2)(a) to calculate its capital adequacy ratio on a solo-consolidated basis, a reference in subsection (5) to the institution calculating its capital adequacy ratio on a solo basis is a reference to the institution calculating it on a solo-consolidated basis.

334. Formula approach for calculating ILM

The formula approach for an authorized institution to calculate its ILM is set out in Formula 29.

Formula 29

$$ILM = \ln\left[\exp(1) - 1 + \left(\frac{LC}{BIC}\right)^{0.8}\right]$$

335. Calculation of LC

(1) An authorized institution must calculate its LC by using only high quality operational loss data.

(2) An authorized institution must calculate its LC by multiplying the arithmetic mean of its annual operational risk losses incurred over the following period by 15—

(a) the last 10 years, if the institution has maintained high quality operational loss data for the last 10 years or more;

(b) the number of years for which the institution has maintained high quality operational loss data, if the institution has maintained high quality operational loss data for the last 5 years or more but less than the last 10 years.

(3) For the purposes of subsection (2), an authorized institution must calculate the arithmetic mean of its annual operational risk losses incurred over a period of years by—

(a) calculating the amounts of its operational risk losses for the first year and each year preceding the first year in the period;

(b) aggregating the amounts of its operational risk losses for each year in the period; and

(c) dividing the aggregate amount by the number of years in the period.

(4) For the purposes of subsection (3), if, on any calendar quarter end date after this section comes into operation*, the number of years in the period is between 5 and 10, an authorized

institution must treat any partial year of operational loss data maintained of 6 months or more as a full year and any partial year of operational loss data maintained of less than 6 months as zero.

(5) For the purposes of this section, an authorized institution's operational risk losses incurred in a year is the sum of the gross loss amounts of any operational loss events recognized by the institution in the year less the recovery amounts of any operational loss events received by the institution in the year.

Editorial Note:

* Operation date: 1 January 2025.

336. Exclusions from LC

(1) For the purpose of calculating its LC, an authorized institution must exclude the losses arising from an operational loss event under any of the following situations—

(a) where the cumulative losses after deduction of recoveries arising from the event over the period for which the LC is calculated is less than the threshold specified by the Monetary Authority under subsection (2);

(b) where the losses have been accounted for in the risk-weighted amount for credit risk;

(c) where the Monetary Authority has approved the institution to exclude the losses arising from the event from the calculation of its LC.

(2) For the purposes of subsection (1)(a), the Monetary Authority may specify a threshold, having regard to OPE25.18 of the current Basel Framework.

(3) The Monetary Authority may grant approval under subsection (1)(c) if the Monetary Authority considers it prudent to do so, having regard to the risk profile of the authorized institution.

337-341. *(Repealed L.N. 167 of 2023)*

Part 10

Calculation of Sovereign Concentration Risk

(Part 10 added L.N. 222 of 2018)

Division 1—Interpretation

342. Interpretation of Part 10

(1) In this Part—

concentrated sovereign exposure (集中官方實體風險承擔)—see section 343(2);

Exposure Limits Rules (《風險承擔限度規則》) means the Banking (Exposure Limits) Rules (Cap. 155 sub. leg. S); *(E.R. 4 of 2019)*

specified sovereign entity (指明官方實體) means an exempted sovereign entity, as defined by rule 39(1) of the Exposure Limits Rules, but excludes—

(a) the Central People's Government of the People's Republic of China;

(b) the People's Bank of China;

(c) a sovereign foreign public sector entity of the Mainland of China;

(d) the Government of the United States of America; and

(e) the Government;

specified sovereign exposure (指明官方實體風險承擔)—see section 342A. *(L.N. 167 of 2023)*

(L.N. 167 of 2023)

(2) In this Part, the amount of an authorized institution's specified sovereign exposure to a jurisdiction is the amount calculated in accordance with section 343(1). *(L.N. 167 of 2023)*

Division 2—Calculation of Risk-weighted Amount for Sovereign Concentration Risk

342A. Calculation of specified sovereign exposure to specified sovereign entity

(1) An authorized institution must calculate the amount of its specified sovereign exposure to a specified sovereign entity as the sum of—

(a) the institution's ASC exposure to that specified sovereign entity determined in accordance with Part 7 of the Exposure Limits Rules as if rule 48(1)(c) of those Rules were not applicable;

(b) if, in relation to that specified sovereign entity, the institution makes a deduction of exposure in accordance with rule 57(1)(c) of the Exposure Limits Rules in determining the institution's ASC exposure to another counterparty of the institution for Part 7 of those Rules—the amount of the exposure deducted; and

(c) if, in relation to that specified sovereign entity, the institution makes a deduction of exposure in accordance with rule 57(1)(c) of the Exposure Limits Rules in determining the institution's ASC exposure to another specified sovereign entity for this Part—the amount of the exposure deducted.

(2) In this section—

ASC exposure (ASC風險承擔) has the meaning given by rule 39(1) of the Exposure Limits Rules.

(L.N. 167 of 2023)

343. Specified sovereign exposure to jurisdiction and concentrated sovereign exposure

(L.N. 167 of 2023)

(1) An authorized institution must calculate the amount of its specified sovereign exposure to each jurisdiction by aggregating the amounts of its specified sovereign exposures to the specified sovereign entities of the jurisdiction, each exposure calculated in accordance with section 342A.

(2) An authorized institution's specified sovereign exposure to a jurisdiction is a concentrated sovereign exposure if the amount of the specified sovereign exposure exceeds 100% of the Tier 1 capital of the institution.

(L.N. 167 of 2023)

344. Calculation of risk-weighted amount of concentrated sovereign exposure to jurisdiction

(L.N. 167 of 2023)

If an authorized institution's specified sovereign exposure to a jurisdiction is a concentrated sovereign exposure, the institution must calculate the risk-weighted amount of its concentrated sovereign exposure to the jurisdiction by— *(L.N. 167 of 2023)*

(a) dividing the exposure into the portions as specified in column 2 of Table 34;

(b) for each portion of the exposure exceeding 100% of the Tier 1 capital of the institution as specified in items 2, 3, 4, 5 and 6 (as applicable) in column 2 of Table 34—multiplying the amount of the exposure in the portion by the risk weight specified in column 3 of that Table opposite the portion; and

(c) aggregating the results from paragraph (b) for the portions specified in items 2, 3, 4, 5 and 6 (as applicable) in column 2 of Table 34.

Table 34

Risk-weights for Portions of Concentrated Sovereign Exposure to Jurisdiction

(L.N. 167 of 2023)

Item	Portion of concentrated sovereign exposure to jurisdiction (expressed as percentage of Tier 1 capital)	Risk-weight
1.	Portion exceeding 0% but not exceeding 100%	not applicable
2.	Portion exceeding 100% but not exceeding 150%	5%
3.	Portion exceeding 150% but not exceeding 200%	6%
4.	Portion exceeding 200% but not exceeding 250%	9%
5.	Portion exceeding 250% but not exceeding 300%	15%
6.	Portion exceeding 300%	30%

(L.N. 167 of 2023)

345. Calculation of risk-weighted amount for sovereign concentration risk

An authorized institution must calculate the risk-weighted amount for sovereign concentration risk by aggregating the risk-weighted amounts of the institution’s concentrated sovereign exposures to all jurisdictions calculated in accordance with section 344.

(L.N. 167 of 2023)

Division 3—*(Repealed L.N. 167 of 2023)*

346-350. *(Repealed L.N. 167 of 2023)*

Division 4—*(Repealed L.N. 167 of 2023)*

351-353. *(Repealed L.N. 167 of 2023)*

Part 11

Output Floor

(Part 11 added L.N. 167 of 2023)

354. Application of Part 11

This Part applies to an authorized institution that uses a model-based approach to calculate its credit risk or market risk or both.

355. Interpretation of Part 11

In this Part—

model-based approach (模式基準計算法) means any of the following—

(a) IRB approach;

(b) SEC-IRBA;

(c) internal assessment approach;

(d) IMM(CCR) approach;

(e) value-at-risk model as set out in section 226ML;

(f) IMA;

output floor (出項下限), in relation to an authorized institution, means its floor risk-weighted amount for credit risk, market risk, CVA risk and operational risk calculated under section 356.

356. Calculation of output floor

(1) Subject to subsection (9), an authorized institution must calculate its floor risk-weighted amount for credit risk, market risk, CVA risk and operational risk by multiplying the amount

determined under subsection (2) by the corresponding output floor level specified in Table 36.

(2) An authorized institution must arrive at the relevant amount for the purposes of subsection (1) by—

(a) calculating its risk-weighted amount for credit risk by using—

(i) subject to subsections (3), (4), (5) and (6), the STC approach for non-securitization exposures; and

(ii) the SEC-ERBA (except the use of internal assessment approach), SEC-SA or SEC-FBA for securitization exposures;

(b) calculating its risk-weighted amount for market risk and CVA risk respectively by using—

(i) subject to subsection (7), the STM approach or, with the Monetary Authority's approval under section 17A, the SSTM approach; and *(L.N. 167 of 2023)*

(ii) the calculation approach used by the institution for CVA risk;

(c) calculating its risk-weighted amount for operational risk by using the calculation approach used by the institution for operational risk; and

(d) aggregating the amounts calculated under paragraphs (a), (b)(i) and (ii) and (c).

(3) For the purposes of subsection (2)(a)(i), an authorized institution must use—

(a) subject to subsection (6)(b), the SA-CCR approach to calculate its default risk exposures in respect of derivative contracts; and

(b) the methods set out in Division 2B of Part 6A (except the use of value-at-risk model set out in section 226ML) to calculate its default risk exposures in respect of SFTs.

(4) For the purposes of subsection (2)(a)(i), an authorized institution may, subject to subsection (5) and section 61(3) and (4), allocate to all of its general corporate exposures that are unrated exposures that fall under section 61(2)(a) (***concerned exposures***) risk-weights specified in Table 35 according to the loan classification category of the exposure in compliance with the Guideline on Loan Classification System (***loan classification method***).

Table 35

Risk-weights for Concerned Exposures

Column 1	Column 2	Column 3
Item	Loan classification category of concerned exposures	Risk-weight
1.	Pass	85%
2.	Special Mention	125%
3.	Substandard	150%
4.	Doubtful	150%
5.	Loss	150%

(5) If an authorized institution chooses to allocate the risk-weights to its concerned exposures in accordance with the loan classification method set out in subsection (4), the institution must apply the method consistently over time and must not change the method without the prior consent of the Monetary Authority.

(6) An authorized institution that uses the BSC approach to calculate its credit risk for all its non-securitization exposures may choose to use—

(a) the BSC approach for the purposes of subsection (2)(a)(i); and

(b) the current exposure approach to calculate its default risk exposures in respect of derivative contracts unless, under section 10A(2B), the Monetary Authority has required the institution to use the SA-CCR approach to calculate its default risk exposures.

(7) For the purposes of subsection (2)(b)(i), an authorized institution must apply the SEC-ERBA (except the use of internal assessment approach), SEC-SA or SEC-FBA to determine the market risk capital charge for securitization exposures in its trading book.

(8) Subject to subsection (9), an authorized institution must use the corresponding output floor level specified in Table 36.

Table 36

Output Floor Levels

Column 1 Item	Column 2 Applicable dates for output floor level	Column 3 Output floor level
1.	On and after the commencement date of Part 3 of the Banking (Capital) (Amendment) Rules 2023 (***commencement date****) but not after 31 December of the year within which the commencement date falls (***year of commencement***)	50%
2.	Any date within the first year after the year of commencement	55%
3.	Any date within the second year after the year of commencement	60%
4.	Any date within the third year after the year of commencement	65%
5.	Any date within the fourth year after the year of commencement	70%
6.	On and after 1 January of the fifth year after the year of commencement	72.5%

(9) The Monetary Authority may, by written notice given to one or more authorized institutions, require the institution to apply an output floor level specified in the notice to the calculation of its output floor if the Monetary Authority considers that—

(a) a rating system or an internal model used by the institution to calculate its credit risk or market risk or both causes, or could reasonably be construed as potentially causing, whether by itself or in conjunction with any other event, adverse impacts on the financial soundness of the institution; or

(b) a prudential concern causes or could reasonably be construed as potentially causing, whether by itself or in conjunction with any other event, the financial soundness of the institution or the stability of the financial system in Hong Kong to be put at risk in prevailing, or likely prevailing, economic and market conditions.

(10) An authorized institution must comply with the requirements of a notice given to it under subsection (9).

(11) In this section—

Doubtful (呆滯), ***Loss*** (虧損), ***Pass*** (合格), ***Special Mention*** (需要關注) and ***Substandard*** (次級) mean the category of that name into which an exposure can be classified under the Guideline on Loan Classification System;

general corporate exposure (一般法團風險承擔) has the meaning given by section 51(1);

Guideline on Loan Classification System (《貸款分類制度指引》) means the guideline set out in Appendix 2 to the Completion Instructions of return “Quarterly Analysis of Loans and Advances and Provisions” as amended from time to time, published on the Monetary Authority’s website;

unrated exposure (無評級風險承擔) has the meaning given by section 51(1).

Editorial Note:

* Commencement date: 1 January 2025.

357. Calculation of actual risk-weighted amount

An authorized institution must calculate its actual risk-weighted amount for credit risk, market risk, CVA risk and operational risk by—

(a) calculating its risk-weighted amount for credit risk by using the calculation approach used by the institution for credit risk;

(b) calculating its risk-weighted amount for market risk by using the calculation approach used by the institution for market risk;

(c) calculating its risk-weighted amount for CVA risk by using the calculation approach used by the institution for CVA risk;

(d) calculating its risk-weighted amount for operational risk by using the calculation approach used by the institution for operational risk; and

(e) aggregating the amounts calculated under paragraphs (a), (b), (c) and (d).

358. Adjustment of capital adequacy ratio if output floor is larger than actual risk-weighted amount

An authorized institution—

(a) must calculate the difference between—

(i) its output floor; and

(ii) its actual risk-weighted amount for credit risk, market risk, CVA risk and operational risk calculated under section 357; and

(b) if the output floor is larger than the actual risk-weighted amount referred to in paragraph (a)(ii)—must add the difference to the total risk-weighted amount for credit risk, market risk, CVA risk and operational risk for the calculation of its capital adequacy ratio.

Schedule 1

[ss. 2, 139, 166, 182 & 226MD & Sch. 6]

(L.N. 156 of 2012; L.N. 44 of 2020; L.N. 167 of 2023)

Specifications for Purposes of Certain Definitions in these Rules

(L.N. 156 of 2012)

Part 1

Domestic Public Sector Entities

1. MTR Corporation Limited

2. Kowloon-Canton Railway Corporation

3. Hong Kong Housing Authority

4. Hospital Authority

5. Airport Authority

6. The Hong Kong Mortgage Corporation Limited

7. Urban Renewal Authority

8. 香港五隧一橋有限公司 Hong Kong Link 2004 Limited

9. Hong Kong Trade Development Council

10. Ocean Park Corporation

11. Hong Kong Science and Technology Parks Corporation *(L.N. 175 of 2017)*

12. HKMC Insurance Limited *(L.N. 222 of 2018)*

13. HKMC Annuity Limited *(L.N. 222 of 2018)*

14. Hong Kong Export Credit Insurance Corporation *(L.N. 54 of 2022)*

15. Hong Kong Housing Society *(L.N. 167 of 2023)*

16. West Kowloon Cultural District Authority *(L.N. 167 of 2023)*

(E.R. 7 of 2020)

Part 2

Relevant CCF in respect of Certain Off-balance Sheet Exposures

Part 3

Restricted Collective Investment Schemes

Part 4

Restricted Debt Securities

Part 5

Restricted Foreign Public Sector Entities

Part 6

Restricted Insurance Regulators

Part 7

Restricted Jurisdictions

Part 8

Restricted Securities Regulators

Part 9

Restricted Sovereigns

Part 10

Relevant International Organizations

1. Bank for International Settlements

2. International Monetary Fund

3. European Central Bank

4. European Union *(L.N. 167 of 2023)*

5. European Financial Stability Facility *(L.N. 128 of 2014)*

6. European Stability Mechanism *(L.N. 128 of 2014)*

(E.R. 7 of 2020)

Part 11

Financial Services Activities of Financial Institutions

(L.N. 156 of 2012)

Schedule 1A

[s. 322J]
(L.N. 167 of 2023)

Transactions and Contracts not Subject to CVA Risk Capital Charge

(L.N. 167 of 2023)

1. Excepted transactions and contracts

The following transactions and contracts are specified for the purposes of section 322J(1) of these Rules—

(a) OTC derivative transactions and SFTs with a qualifying CCP where the authorized institution concerned is a clearing member of the CCP; *(L.N. 44 of 2020)*

(b) OTC derivative transactions and SFTs with a clearing member of a qualifying CCP for which the risk-weighted amount of the default risk exposure incurred by an authorized institution as a direct client of the clearing member is calculated in accordance with section 226ZA(3) or (4) of these Rules; *(L.N. 44 of 2020)*

(c) OTC derivative transactions and SFTs with a qualifying CCP for which the risk-weighted amount of the default risk exposure incurred by an authorized institution as a direct client of a clearing member of the CCP is calculated in accordance with section 226ZB(2) or (3) of these Rules; *(L.N. 44 of 2020)*

(ca) OTC derivative transactions and SFTs with a higher level client within a multi-level client structure associated with a qualifying CCP for which the risk-weighted amount of the default risk exposure incurred by an authorized institution within the structure to the higher level client is calculated in accordance with section 226ZBA(5) of these Rules; *(L.N. 44 of 2020)*

(d) recognized credit derivative contracts (within the meaning of section 51(1), 105, 139(1) or 227(1) of these Rules, as the case requires) purchased by an authorized institution to provide credit protection to the institution's banking book exposures where— *(L.N. 175 of 2017)*

(i) the exposures are—

(A) credit risk exposures other than default risk exposures in respect of OTC derivative transactions and (if the Monetary Authority requires the institution to calculate a CVA risk capital charge in respect of its SFTs under section 322J(2) of these Rules) SFTs; or *(L.N. 167 of 2023)*

(B) default risk exposures in respect of OTC derivative transactions and SFTs that fall within paragraph (a), (b), (c), (ca) or (e); and *(L.N. 44 of 2020)*

(ii) the recognized credit derivative contracts are not treated as recognized credit derivative contracts or eligible CVA hedges for any other exposures of the institution;

(e) OTC derivative transactions and SFTs (other than those falling within paragraph (a), (b), (c), (ca) or (d))— *(L.N. 44 of 2020)*

(i) that are in default as determined under the terms and conditions of the transactions; *(L.N. 44 of 2020)*

(ii) in respect of which the losses due to the default have been recognized by the authorized institution concerned for accounting and reporting purposes; and

(iii) the exposures in respect of which have been transformed into simple claims that do not have the risk characteristics of derivative contracts or SFTs. *(L.N. 51 of 2013)*

2. *(Repealed L.N. 44 of 2020)*

(Schedule 1A added L.N. 156 of 2012)

Schedule 1B

[s. 23D]

Minimum Requirements to be Satisfied for Approval under Section 23D(2) of these Rules to Use Standardized CVA Approach

1. General requirements

An authorized institution that makes an application under section 23D(1) of these Rules to use the standardized CVA approach must demonstrate to the satisfaction of the Monetary Authority that—

(a) the senior management of the institution is actively involved in the CVA risk control process with sufficient resources to be allocated for the purpose of the institution's CVA risk control;

(b) the institution uses the exposure models used in the calculation of its CVA risk capital charge (***exposure models***) for its CVA risk management framework that includes the identification, measurement, management, approval and internal reporting of the institution's CVA risk;

(c) the institution has a CVA desk (or a similar dedicated function) that is responsible for the risk management and hedging of CVA;

(d) the institution has a risk control unit that—

(i) is functionally independent of the institution's business credit and trading units (including the CVA desk);

(ii) reports directly to the institution's senior management; and

(iii) has a sufficient number of staff who are qualified and trained to conduct the testing, validation and implementation of the institution's exposure models used for the calculation of CVA;

(e) the institution—

(i) clearly documents the exposure models and the internal policies, controls and procedures relating to the operation of the exposure models, including—

(A) the calculation of the exposures generated by the models with sufficient details for a third party to understand the operation, limitations and key assumptions, and to re-create the analysis;

(B) the model validation process, including frequency and methodologies of validation and analyses used; and

(C) criteria and process to analyse the performance of the exposure models including the model inputs and process to remedy any unacceptable performance; and

(ii) has a system for monitoring and ensuring compliance with those internal policies, controls and procedures;

(f) an independent review of the soundness and adequacy of the institution's CVA risk management process and the institution's compliance with internal policies, controls and procedures, including the requirements specified in this Schedule, is conducted regularly by the institution's internal auditors; and

(g) the review or audit referred to in paragraph (f) includes the activities of the CVA desk and the independent risk control unit.

2. Specific requirements relating to principles in determining CVA for each counterparty

For the purpose of determining the CVA for each counterparty and without limiting section 1 of this Schedule, an authorized institution must adhere to, and demonstrate to the satisfaction of the Monetary Authority that it adheres to, the following principles—

(a) the institution calculates the CVA for each counterparty with at least one covered transaction as specified in section 322J of these Rules as the expectation of future losses resulting from the default of the counterparty under the assumption that the institution itself is free from default risk;

(b) the institution calculates the CVA based on sets of inputs that include at a minimum—

(i) the term structure of market implied probability of default, which is determined based on the credit spread of market instruments of the counterparty but, if no market instrument of the counterparty is available—

(A) a proxy credit spread is determined based on credit spreads of market instruments of the liquid peers of the counterparty via an algorithm that discriminates on variables that include at a minimum the credit quality, industry and region of the counterparty;

(B) a proxy credit spread may be determined based on a single liquid reference name with proper justification; or

(C) if no credit spreads of any liquid peers of the counterparty are available because of the specific type of the counterparty, a fundamental analysis of credit risk may be conducted to proxy the credit spread of the counterparty on condition that the resulting proxy credit spread relates to credit markets;

(ii) market-consensus expected loss given default values that are consistent with the ones used to calculate the probability of default in subparagraph (i) and take into account the seniority of the exposure; and

(iii) simulated paths of discounted future exposures that are calculated by pricing all exposures with the counterparty along simulated paths of relevant market risk factors and discounting the prices back to the reporting date using risk-free rates along the path;

(c) in relation to the calculation of the simulated paths of discounted future exposures set out in paragraph (b)(iii), the exposure models—

(i) capture and accurately reflect, on a continuing basis, all material market risk factors affecting the pricing of the exposures, and those factors are simulated as stochastic processes appropriately;

(ii) take into account any significant level of dependence between an exposure and the credit quality of the counterparty;

(iii) are consistent with the exposure models used in the calculation of front office or accounting CVA (including the netting recognition), with adjustments if needed, to fulfil other requirements specified in this Schedule;

(iv) account for the possible non-normality of the distribution of exposures in the distribution of risk factors being modelled;

(v) capture transaction-specific information in order to aggregate exposures at netting set level; and

(vi) reflect transaction terms and specifications in a timely, complete and conservative manner;

(d) the exposure models have a proven track record of acceptable accuracy in measuring the CVA and CVA sensitivity to the market risk factors;

(e) the option pricing models embedded in the exposure models account for the non-linearity of option value with respect to market risk factors;

(f) the exposure models use current and historical data acquired in a timely and complete manner, and independently of the business lines and are compliant with the relevant financial reporting standards; and

(g) the use of any proxy market data provides a conservative representation of the underlying risk factor under adverse market conditions.

3. Additional requirements relating to exposure models

Without limiting section 1 or 2 of this Schedule, an authorized institution must demonstrate to the satisfaction of the Monetary Authority that, if the exposure models used by the institution capture the effects of margin agreements when estimating the simulated paths of discounted future exposure—

(a) the institution has a collateral management unit as required by section 1(e) of Schedule 2A;

(b) all documentation used in collateralized transactions are binding on all parties and legally enforceable in all relevant jurisdictions; and

(c) the exposure models—

(i) include transaction-specific information in order to capture the effects of margining along each exposure path; and

(ii) account for the nature of margin agreements (including whether the agreement concerned is unilateral or bilateral), the frequency of margin calls, the type of collateral, the margin thresholds, the independent amounts, the initial margins, the minimum transfer amounts and the margin period of risk.

(Schedule 1B added L.N. 167 of 2023)

Schedule 2

[ss. 8, 9, 10 & 259 & Sch. 3]
(L.N. 175 of 2017; L.N. 167 of 2023)

Minimum Requirements to be Satisfied for Approval under Section 8 of these Rules to Use IRB Approach

1. General requirements

An authorized institution which makes an application under section 8 of these Rules to use the IRB approach shall demonstrate to the satisfaction of the Monetary Authority that—

(a) the board of directors (or a committee designated by the board) and the senior management of the institution—

(i) approve all the key elements of, and any material changes to, the institution's rating system;

(ii) possess an understanding of the design and operation of, and the management reports generated by, the institution's rating system adequate for them to perform their functions specified in this paragraph;

(iii) exercise oversight of the institution's rating system sufficient to ensure that the rating system complies with paragraph (b); and

(iv) ensure that there is a reporting system within the institution to provide information (including, but not limited to, information relating to any material changes to, or deviations from, established policies and procedures or any material findings identified in a review or audit referred to in paragraph (j)) to them regularly and in sufficient detail as will enable them to—

(A) exercise the oversight referred to in subparagraph (iii); and

(B) make informed decisions relating to credit approval, risk management and corporate governance and (where paragraph (b)(vi)(A) is applicable) internal capital adequacy assessment based on the information generated by the institution's rating system;

(b) the institution's rating system—

(i) is suitable for the purposes of identifying, measuring and controlling the institution's credit risk taking into account the characteristics and extent of the institution's exposures;

(ii) is capable of generating reasonably accurate, consistent and verifiable credit risk components and of calculating the institution's regulatory capital for credit risk;

(iii) is operated in a prudent and consistently effective manner;

(iv) is operated in compliance with Part 6 of these Rules or in a manner which although not fully in compliance with that Part, will not result in any material non-compliance with other requirements specified in this section;

(v) plays an essential role in the institution's ongoing credit approval, risk management and corporate governance functions;

(vi) either—

(A) plays an essential role in the institution's ongoing internal capital adequacy assessment; or

(B) will eventually play, within a period and in a manner agreed to by the Monetary Authority, an essential role in the institution's ongoing internal capital adequacy assessment once the systems and procedures being developed by the institution as at the date of the institution's application to use the IRB approach under section 8 of these Rules for conducting the assessment are implemented in accordance with a plan agreed to by the Monetary Authority; and *(L.N. 167 of 2023)*

(vii) *(Repealed L.N. 167 of 2023)*

(viii) enables the institution to comply with the Banking (Disclosure) Rules (Cap. 155 sub. leg. M) in respect of any disclosures by the institution in respect of— *(L.N. 156 of 2012)*

(A) the institution's credit risk; and

(B) the manner in which the institution manages its credit risk;

(c) the institution has a credit risk control unit—

(i) which is functionally independent of the institution's staff and management responsible for credit initiation;

(ii) which reports directly to the institution's senior management; and

(iii) which is responsible for—

(A) the design or selection, testing and implementation of the institution’s rating system;

(B) the oversight of the effectiveness of the institution’s rating system for the purposes of paragraph (b)(i), (ii) and (iii);

(C) the monitoring and review of any override relating to the inputs to, or the outputs of, the institution’s rating system;

(D) the production and analysis of the management reports generated by the institution’s rating system; and

(E) the ongoing review of, and changes to, the institution’s rating system;

(d) the institution has a sufficient number of staff who are qualified and trained to use the institution’s rating system in the institution’s business, risk control, audit and back office functions as will enable these functions to work effectively in identifying, measuring and controlling the institution’s credit risk;

(e) the institution clearly documents all the key elements of, and the history of major changes in, the institution’s rating system and the contents of the documentation are consistent with, and evidence the institution’s compliance with, the requirements specified in this section;

(f) the institution has an effective system to collect, store, process, retrieve and utilize data on obligor and facility characteristics and default and loss information in respect of the institution's exposures in a reliable and consistent manner, and the data stored are in sufficient detail as will enable the institution to comply with the requirements specified in this section;

(g) where the institution uses models which are based on statistical techniques or expert judgment, or both, to assign exposures to obligor grades and facility grades, or pools, and to estimate the credit risk components in respect of those grades or pools, the use of those models will not result in any distortion in the calculation of the institution's regulatory capital for credit risk;

(h) the institution has a comprehensive stress-testing programme conducted regularly for the assessment of the adequacy of—

(i) the institution's regulatory capital and (where paragraph (b)(vi)(A) is applicable) internal capital for credit risk; and

(ii) the institution's ability to withstand any future events or changes in economic conditions which may have adverse effects on credit quality of the institution's exposures;

(i) the institution has a reliable system for validating regularly the accuracy and consistency of the institution's rating system (including models used as referred to in paragraph (g)), by persons who are qualified and trained to do so and who are independent of the development of the institution's rating system, through—

(i) vetting data inputs to the institution's rating system;

(ii) reviewing the outputs of the institution's rating system;

(iii) evaluating the logic and conceptual soundness of the institution's rating system;

(iv) implementing an effective control process for making changes to the institution's rating system in response to the results of the validation; and

(v) reviewing any proposed development of, or any proposed significant change to, the institution's rating system to assess whether the rating system will function effectively as intended if the proposed development is implemented or the proposed change made, as the case may be; and *(L.N. 137 of 2011)*

(j) an independent review or audit of the institution's compliance with the requirements specified in this section is conducted regularly by the institution's internal auditors or by independent external parties which are qualified to do so.

2. Specific requirements

Without prejudice to the generality of section 1, an authorized institution shall demonstrate to the satisfaction of the Monetary Authority that—

(a) the suitability and capability of the institution's rating system for the purposes of section 1(b)(i) and (ii) are supported by parallel calculations carried out prior to the use of the IRB approach for the calculation of the institution's regulatory capital for credit risk for such period as the Monetary Authority considers reasonable in all the circumstances of the case; and

(b) the institution has been using a rating system, and estimates of credit risk components generated by that rating system, which are broadly consistent with the requirements of Part 6 of these Rules for the estimation of credit risk components and the calculation of credit risk under the IRB approach, in the institution's credit approval, risk management and corporate governance functions and (where section 1(b)(vi)(A) is applicable) internal capital adequacy assessment prior to the use of the IRB approach for the calculation of the institution's regulatory capital for credit risk for such period as the Monetary Authority considers reasonable in all the circumstances of the case.

3. Meaning of *parallel calculations*

In section 2(a), ***parallel calculations*** (對比計算), in relation to an authorized institution, means calculations—

(a) of which—

(i) one set consists of those calculations derived from the approach the institution actually uses during the period covered by the parallel calculations to calculate its credit risk; and

(ii) the other set consists of those calculations derived from the IRB approach the subject of an application made by the institution under section 8 of these Rules;

(b) which are in such form as agreed between the Monetary Authority and the institution; and

(c) which contain such information, and use such data and methodology, as agreed between the Monetary Authority and the institution.

Schedule 2A

[ss. 10B, 10D & 226D & Sch. 1B]

(L.N. 167 of 2023)

Minimum Requirements to be Satisfied for Approval under Section 10B(2)(a) of these Rules to Use IMM(CCR) Approach

1. General requirements

An authorized institution that makes an application under section 10B(1) of these Rules to use the IMM(CCR) approach must demonstrate to the satisfaction of the Monetary Authority that—

(a) the board of directors (or a committee designated by the board) and the senior management of the institution—

(i) approve all the key elements of, and any material changes to, the institution's counterparty credit risk management system (being the methods, models, processes, controls, and data collection and information technology systems used by the institution that enable the identification, measurement, management and control of counterparty credit risk by the institution);

(ii) possess an understanding of the design and operation of, and the management reports generated by, the institution's counterparty credit risk management system adequate for them to perform their functions specified in this paragraph;

(iii) exercise oversight of the institution's counterparty credit risk management system sufficient to ensure that the system complies with paragraph (b); and

(iv) ensure that there is a reporting system within the institution to provide information (including information relating to any material changes to, or deviations from, established policies and procedures or any material findings identified in a review or audit referred to in paragraph (k)) to them regularly and in sufficient detail as will enable them to—

(A) exercise the oversight referred to in subparagraph (iii); and

(B) make informed decisions relating to the institution's counterparty credit risk exposures;

(b) the institution's counterparty credit risk management system—

(i) is suitable for the purposes of identifying, measuring, managing, controlling and reporting the institution's counterparty credit risk taking into account the characteristics and extent of the institution's counterparty credit risk exposures;

(ii) identifies, measures, monitors and controls counterparty credit risk over the life of transactions;

(iii) measures and manages both current exposures (gross and net of collateral held, where appropriate) and future exposures; and

(iv) is operated in a prudent and consistently effective manner that is also consistent with sound practices for counterparty credit risk management;

(c) the institution—

(i) clearly documents the counterparty credit risk management system and the internal policies, controls and procedures relating to the operation of the system, including—

(A) the internal models to which the application relates (***relevant models***);

(B) the calculation of the risk measures generated by the relevant models with sufficient details for a third party to re-create the risk measures; and

(C) the model validation process, including frequency and methodologies of validation and analyses used; and

(ii) has a system for monitoring and ensuring compliance with those internal policies, controls and procedures;

(d) the institution has a risk control unit—

(i) that is functionally independent of the institution's staff and management responsible for originating counterparty credit risk exposures;

(ii) that reports directly to the institution's senior management;

(iii) that is responsible for—

(A) the design or selection of the institution's counterparty credit risk management system;

(B) the testing, validation and implementation of the institution's counterparty credit risk management system;

(C) the oversight of the effectiveness of the institution's counterparty credit risk management system for the purposes of paragraph (b), including the control of data integrity;

(D) the production and analysis of daily management reports on the output of the relevant models, including an evaluation of the relationship between measures of counterparty credit risk exposure and credit and trading limits;

(E) the ongoing review of, and changes to, the institution's counterparty credit risk management system; and

(F) the conduct of a regular back-testing programme to verify the accuracy and reliability of the relevant models;

(iv) the work of which is an integral part of the day-to-day credit risk management process of the institution, including the planning, monitoring and controlling of the institution's credit and overall risk profile; and

(v) the daily management reports of which are reviewed by a level of management with sufficient seniority and authority to enforce both reductions of positions taken by individual traders and reductions in the institution's overall risk exposure;

(e) the institution has a collateral management unit—

(i) that is adequately staffed and with sufficient resources to process margin calls and disputes in a timely and accurate manner at all times (including during periods of severe market crisis), and to enable the institution to limit its number of large disputes caused by trade volumes; and

(ii) that is responsible for—

(A) calculating and making margin calls, managing margin call disputes and reporting levels of independent amounts, initial margins (within the meaning of section 226A of these Rules) and variation margins (within the meaning of section 226A of these Rules) accurately on a daily basis; *(L.N. 44 of 2020)*

(B) controlling the integrity of the data used to make margin calls and ensuring that such data are consistent and reconciled regularly with all relevant data sources within the institution;

(C) tracking the extent of reuse of collateral posted to the institution (both cash and non-cash) and the rights ceded by the institution in respect of the collateral that it posts;

(D) tracking concentration in individual types of collateral accepted by the institution; and

(E) producing and maintaining appropriate collateral management information (including information on the type of collateral (both cash and non-cash) received and posted, categories of collateral reused and the terms of the reuse, the size, aging and cause of margin call disputes, and the trends in the areas to which such information relates) and reporting the information to the institution's senior management on a regular basis;

(f) the institution has a sufficient number of staff who are qualified and trained to use the relevant models in the institution's business, risk control, audit and back office functions as will enable those functions to work prudently and effectively in identifying, measuring, managing, controlling and reporting the institution's counterparty credit risk;

(g) the use of the relevant models is part of the institution's counterparty credit risk management system and plays an essential role in the institution's daily risk management, capital planning and corporate governance functions, with—

(i) the results generated by the relevant models being used in—

(A) planning, measuring, monitoring and controlling the institution's counterparty credit risk exposures;

(B) determining the institution's trading and credit risk exposure limits and measuring the usage of those limits;

(C) credit approval; and

(D) internal capital allocation; and

(ii) the relationship between the relevant models and the limits referred to in subparagraph (i)(B) being maintained consistently over time and understood by the institution's senior management, credit function and staff engaged in trading activity;

(h) the institution—

(i) uses stress-testing and scenario analysis to identify risk factors that give rise to general wrong-way risk (being the risk that arises when the probability of default of counterparties is positively correlated with general market risk factors) and address the possibility of severe shocks;

(ii) monitors general wrong-way risk by product, by region, by industry, or by other categories that are relevant to the business of the institution;

(iii) has policies and procedures for identifying, monitoring and controlling transactions with specific wrong-way risk at the inception and throughout the life of the transactions; and

(iv) provides regular reports on wrong-way risks to its senior management and board of directors (or a committee designated by the board);

(i) the cash management policy of the institution takes account of the liquidity risks arising from potential incoming margin calls (including calls for posting of collateral due to adverse market shocks or potential downgrade of the institution's external credit rating and calls for return of collateral);

(j) the institution ensures that the nature and horizon of collateral reuse are consistent with its liquidity needs and do not jeopardize its ability to post or return collateral in a timely manner;

(k) an independent review or audit of the soundness and adequacy of the institution's counterparty credit risk management system and the institution's compliance with internal policies, controls and procedures, including the requirements specified in this Schedule, in respect of the system is conducted regularly by the institution's internal auditors or by independent external parties that are qualified to do so; and

(l) the institution, before being granted an IMM(CCR) approval—

(i) has been using internal models that are broadly consistent with the requirements set out in this Schedule, for a period (not less than one year in any case) that is considered by the Monetary Authority as reasonable in all the circumstances of the case, to estimate the distribution of exposures (within the meaning given in section 226H(2) of these Rules) using current market data; and

(ii) has been conducting back-testing, being back-testing that is broadly consistent with the requirements set out in this Schedule relating to back-testing, using historical data on movements in market risk factors.

2. Specific requirements relating to relevant models

Without limiting section 1 of this Schedule, an authorized institution must demonstrate to the satisfaction of the Monetary Authority that—

(a) the relevant models specify the forecast of the probability distribution of changes in the market value of a netting set attributable to changes in relevant market factors and calculate the institution's counterparty credit risk exposure for the netting set at each future date given the changes in the market factors;

(b) the relevant models capture and accurately reflect, on a continuing basis, all material factors affecting counterparty credit risk inherent in the institution's transactions;

(c) the relevant models capture transaction specific information in order to aggregate exposures at netting set level;

(d) the institution calculates counterparty credit risk on the basis of a distribution of exposures that accounts for the possible non-normality of the distribution of exposures;

(e) the relevant models have a proven track record of acceptable accuracy in measuring counterparty credit risk;

(f) the relevant models used for pricing options account for the non-linearity of option value with respect to market risk factors; and

(g) the relevant models are capable of estimating EE on a daily basis (unless the institution is able to otherwise demonstrate to the satisfaction of the Monetary Authority that a less frequent calculation is warranted) and the EE is estimated along a time profile of forecasting horizons that adequately reflects the time structure of future cash flows and maturity of transactions.

(L.N. 167 of 2023)

3. Specific requirements relating to integrity of modelling process

Without limiting sections 1 and 2 of this Schedule, an authorized institution must demonstrate to the satisfaction of the Monetary Authority that—

(a) transaction terms and specifications are reflected in the relevant models in a timely, complete, and conservative manner, and maintained in a secure database that is subject to formal and periodic audit;

(b) the terms and specifications of any valid bilateral netting agreements or valid cross-product netting agreements are input into the database by an independent unit;

(c) the transmission of data on transaction terms and specifications to the relevant models is subject to internal audit and the institution has formal processes for reconciliation between the relevant models and the source data systems to verify on an ongoing basis that transaction terms and specifications are reflected in EE correctly or at least conservatively;

(d) the institution has internal procedures to verify that—

(i) before including a transaction in a netting set, the transaction is covered by a valid bilateral netting agreement or a valid cross-product netting agreement, as the case may be, and the legal enforceability of the agreement has been verified by legal staff; and

(ii) before recognizing the effect of collateral in the calculation of counterparty credit risk, the collateral meets the legal certainty standards set out in section 77 of these Rules; *(L.N. 167 of 2023)*

(e) the institution, when calibrating its relevant models using historical market data—

(i) uses current market data to compute current exposures;

(ii) estimates the parameters of the models using either—

(A) at least 3 years of historical market data; or

(B) market implied data; and

(iii) updates the data quarterly, or more frequently if market conditions warrant it;

(f) for the purposes of performing the calculations referred to in section 226D(1)(b) of these Rules, the institution calibrates its relevant models and estimates the parameters of the models using either—

(i) 3 years of data that include a period of stress to the credit default spreads of the institution's counterparties; or

(ii) market implied data from a suitable period of stress; and

(g) the institution adopts the following measures to ensure the soundness and adequacy of the stress calibration referred to in paragraph (f)—

(i) the institution demonstrates, at least quarterly, that—

(A) the period of stress referred to in paragraph (f) coincides with a period of increased credit default swap spreads or other credit spreads of a representative selection of the institution's counterparties with traded credit spreads; and

(B) where adequate credit spread data for a counterparty is not available for the purposes of sub-subparagraph (A), the institution maps the counterparty to specific credit spread data based on the counterparty's geographical location, internal rating and business type;

(ii) the relevant models use data (either historical or implied) that include data from a period of credit stress and use such data in a manner that is consistent with the method used for the calibration of the relevant models to current market data;

(iii) for the purposes of evaluating the effectiveness of its stress calibration, the institution creates several benchmark portfolios that are vulnerable to the same main risk factors to which the institution is exposed and compares the exposures to the benchmark portfolios calculated using—

(A) current positions at current market prices, and model parameters calibrated in the manner set out in paragraph (f)(i); and

(B) current positions at market prices at the end of the 3 years referred to in paragraph (f)(i), and model parameters calibrated in the manner set out in that paragraph.

4. Specific requirements relating to stress-testing

Without limiting sections 1, 2 and 3 of this Schedule, an authorized institution must demonstrate to the satisfaction of the Monetary Authority that—

(a) the institution has a comprehensive stress-testing programme for counterparty credit risk that is conducted regularly and includes the following elements—

(i) the programme comprehensively captures transactions and aggregates exposures across all forms of trading and across different product categories at the counterparty-specific level, and the time frame selected for the capturing and aggregation is commensurate with the frequency with which stress tests are conducted;

(ii) there is at least monthly stress-testing of principal market risk factors, including interest rates, exchange rates, equities prices, credit spreads and commodity prices, for all counterparties of the institution to assess and address concentration in specific directional risks;

(iii) there is at least quarterly multifactor stress-testing to assess material non-directional risks including yield curve exposures and basis risks, and the stress-testing addresses, at a minimum, the following scenarios—

(A) severe economic or market events;

(B) significant decrease in broad market liquidity;

(C) the liquidation of a large financial intermediary;

(iv) there is at least quarterly stress-testing of joint movement of counterparty credit risk exposures and related counterparty creditworthiness;

(v) the stress tests (including those referred to in subparagraphs (i), (ii), (iii) and (iv)) are conducted at the counterparty-specific level and the counterparty-group level (grouped by industry, region or other relevant criteria), and in aggregate at the institution-wide level;

(vi) the severity of shocks is consistent with the purpose of the stress test;

(vii) the programme includes provision, where appropriate, for reverse stress tests to identify extreme, but plausible, scenarios that could result in significant adverse outcomes; and

(b) the stress-testing results—

(i) are reported regularly to the institution's senior management and periodically to the institution's board of directors (or a committee designated by the board) and cover the largest counterparty-level impacts across the institution's portfolio, material segmental concentrations (within the same industry or region) and portfolio and counterparty specific trends; and

(ii) are used in—

(A) managing the institution's counterparty credit risk, including the setting of policies, risk appetite and exposure limits and the identification and mitigation of excessive or concentrated risks relative to the institution's risk appetite; and

(B) performing the assessment of the adequacy of the institution's regulatory capital and internal capital for counterparty credit risk and the institution's ability to withstand any future events, or changes in economic conditions, that could have adverse effects on the institution's counterparty credit risk exposures.

5. Specific requirements relating to model validation

Without limiting sections 1, 2, 3 and 4 of this Schedule, an authorized institution must demonstrate to the satisfaction of the Monetary Authority that—

(a) the institution has a reliable validation system for validating the accuracy, comprehensiveness and consistency of the relevant models (including the risk measures and risk factor predictions generated by or used in the models) by parties—

(i) who are qualified and trained to do so and who are independent of the staff and management responsible for originating counterparty credit risk and the development of the relevant models; and

(ii) whose aim is to ascertain whether the relevant models are conceptually sound, able to capture all material factors affecting counterparty credit risk, and continue to perform as intended; *(L.N. 167 of 2023)*

(b) the validation referred to in paragraph (a) must meet the following requirements—

(i) the validation is conducted—

(A) when a relevant model is initially developed and thereafter regularly at a frequency that is adequate to reflect the recent performance of the model; and

(B) when any significant changes are made to a relevant model or when there have been significant structural changes in the market or changes to the composition of the institution's portfolio of exposures that might lead to the relevant model concerned no longer being adequate to capture all material factors affecting counterparty credit risk; *(L.N. 167 of 2023)*

(ii) the validation assesses the accuracy, comprehensiveness and consistency of the relevant models in respect of the results generated by the models at both the institution-wide level and the netting set level;

(iii) the validation procedures—

(A) are clearly documented in sufficient detail as will enable a third party to evaluate the appropriateness of the procedures and re-create the analysis performed by the institution;

(B) define assessment criteria and describe the process by which unacceptable performance will be determined and remedied;

(C) ensure that the relevant models cover all factors and products that have a material contribution to counterparty credit risk exposure; *(L.N. 167 of 2023)*

(D) ensure that all counterparties for which the relevant models are used are covered by the validation;

(E) ensure that both the assumptions and approximations underlying the relevant models are prudent and appropriate for the measurement of the institution's counterparty credit risk exposures; and *(L.N. 167 of 2023)*

(F) define how representative counterparty portfolios are constructed under paragraph (d)(v) for the purposes of the validation;

(c) the validation of the relevant models and the risk measures that produce forecasts of distributions assesses more than a single statistic of the distributions;

(d) as part of the initial and on-going validation process, the institution—

(i) conducts appropriate back-testing to—

(A) assess the performance of the relevant models and the risk measures and market risk factor predictions that are used to estimate EE; and

(B) test the key assumptions of the relevant models and the risk measures;

(ii) includes in back-testing—

(A) a number of distinct prediction time horizons set out to at least one year, over a range of various start dates and covering a wide range of market conditions; and

(B) for collateralized transactions, prediction time horizons that reflect typical margin periods of risk applied in such transactions and long time horizons that are at least one year;

(iii) tests the pricing models used to calculate counterparty credit risk exposure for a given scenario of future shocks to market risk factors and against appropriate independent benchmarks; *(L.N. 167 of 2023)*

(iv) verifies that transactions are assigned to an appropriate netting set within the relevant models;

(v) conducts static, historical back-testing on representative counterparty portfolios, with the representative counterparty portfolios chosen based on their sensitivity to the material risk factors and correlations to which the institution is exposed;

(vi) validates the relevant models and risk measures out to time horizons that are commensurate with the maturity of transactions covered by the institution's IMM(CCR) approval; and

(vii) assesses the frequency with which the parameters of the relevant models are updated; and

(e) the validation results, including those of back-testing, are reviewed periodically by a level of management with sufficient authority to decide the actions that will be taken to address any weaknesses identified in the relevant models.

6. Additional requirements relating to relevant models that capture effects of margin agreements

Without limiting sections 1, 2, 3, 4 and 5 of this Schedule, an authorized institution must demonstrate to the satisfaction of the Monetary Authority that, if the relevant models used by the institution capture the effects of margin agreements when estimating EE, the models—

(a) meet the requirements of sections 1, 2, 3, 4 and 5 of this Schedule in respect of the prediction of future collateral values;

(b) include transaction-specific information in order to capture the effects of margining;

(c) take into account both the current amount of collateral and collateral that would be passed between counterparties in the future;

(d) account for the nature of margin agreements (whether the agreement concerned is unilateral or bilateral), the frequency of margin calls, the margin period of risk, the margin thresholds, and the minimum transfer amount; and

(e) either estimate the mark-to-market change in the value of collateral posted, or apply the rules for recognized collateral set out in Part 4, 5 or 6 of these Rules, as the case requires.

7. *(Repealed L.N. 44 of 2020)*

(Schedule 2A added L.N. 156 of 2012)

Schedule 3

[ss. 18, 19, 226ML, 281 & 322E]

Minimum Requirements to be Satisfied for Approval under Section 18 of these Rules to Use IMA

1. General requirements

(1) An authorized institution that applies under section 18 of these Rules to use the IMA must demonstrate to the satisfaction of the Monetary Authority that—

(a) the institution's market risk management system is conceptually sound and implemented with integrity;

(b) the institution has a sufficient number of staff who are qualified and trained to use the institution's internal models to which the application relates (***relevant models***) in the institution's business, risk control, audit and back office functions;

(c) the relevant models have a proven track record of reasonable accuracy in measuring market risk and demonstrate that accuracy during a period of initial monitoring and live testing of the relevant models at the request of the Monetary Authority;

(d) the institution clearly documents the relevant models with—

(i) the core model documentation, which covers all key components of the relevant models; and

(ii) the non-core model documentation, which covers a comprehensive range of detailed aspects of the relevant models;

(e) the institution has an appropriate organizational infrastructure (including the definition and structure of trading desks) and its firm-wide internal models meet the qualitative evaluation criteria specified by the Monetary Authority;

(f) the institution has a comprehensive stress-testing programme conducted regularly and has a robust system for validating the accuracy and consistency of the relevant models;

(g) the relevant models capture and accurately reflect, on a continuing basis, all material risk factors affecting market risk inherent in the institution's market risk exposures and determine whether each risk factor is modellable through identifying a sufficient number of real price observations in the risk factor eligibility test;

(h) in respect of the relevant models for modellable risk factors—

(i) $ES_{F,C}$, $ES_{R,C}$ and $ES_{R,S}$, as referred to in Formula 28C of these Rules, are calculated on a daily basis for each approved trading desk and across all approved trading desks;

(ii) subject to subsection (3), $ES_{F,C,i}$, $ES_{R,C,i}$ and $ES_{R,S,i}$, as referred to in Formula 28D of these Rules, are calculated at least on a weekly basis for each approved trading desk and across all approved trading desks on the basis that the weekly calculation does not lead to a systematic underestimation of risks relative to a daily calculation;

(iii) a 97.5% confidence level is used in calculating ES;

(iv) the length of the base liquidity horizon used by the relevant models is 10 days;

(v) an appropriate liquidity horizon applicable to individual risk factors or sets of risk factors, that—

(A) is capped at the maturity of the related instrument; and

(B) is set in accordance with Table A or, with the approval of the Monetary Authority, at a higher level than that in Table A, where the increased liquidity horizon must be in the value of 20, 40, 60 or 120 days,

is properly documented and reflected in the relevant models;

(vi) subject to subparagraph (vii), the historical observation period for calculating current ES and stressed ES under these Rules is a 12-month period;

(vii) the institution is able to use a historical observation period for calculating current ES that is shorter than 12 months but not shorter than 6 months, if the Monetary Authority requests it to do so, being of the opinion that there has been a significant increase in volatility in the price of the institution's portfolio of exposures;

(viii) data sets used for calculating current ES are updated at least once every 3 months and are reassessed whenever market prices are subject to material change, and the updating process is flexible enough to allow for more frequent updates as necessary; and

(ix) the relevant models only recognize empirical correlations of risk factors as permitted in Formula 28B of these Rules; and

(i) in respect of the relevant models for NMRFs—

(i) the stress scenario capital charge for all NMRFs is calculated on a daily basis for each approved trading desk and across all approved trading desks;

(ii) the stress scenario capital charge for an NMRF is calibrated to be at least as prudent as the stressed ES for a modellable risk factor;

(iii) an appropriate liquidity horizon applicable to individual risk factors or sets of risk factors, that—

(A) is capped at the maturity of the related instrument and floored at 20 days; and

(B) is set in accordance with Table A or at a higher level required by the Monetary Authority,

is properly documented and reflected in the relevant models; and

(iv) the relevant models only recognize the prescribed correlations of NMRFs as permitted in Formula 28E of these Rules.

Table A

Liquidity Horizon of Risk Factors

Column 1	Column 2	Column 3	Column 4
Item	Risk class	Type of risk factors	Liquidity horizon (in days)
1.	GIRR	Interest rate in relation to HKD, AUD, CAD, EUR, GBP, JPY, SEK and USD	10
		Interest rate in relation to currencies other than HKD, AUD, CAD, EUR, GBP, JPY, SEK and USD	20
		Interest rate volatility	60
		Other types	60
2.	Credit spread risk	Credit spread in relation to investment grade sovereign	20
		Credit spread in relation to non-investment grade sovereign	40

Column 1	Column 2	Column 3	Column 4
Item	Risk class	Type of risk factors	Liquidity horizon (in days)
		Credit spread in relation to investment grade corporate	40
		Credit spread in relation to non-investment grade corporate	60
		Credit spread volatility	120
		Other types	120
3.	Equity risk	Equity price in relation to equity with market capitalization, based on the sum of market values of all the outstanding shares issued by the same legal entity across all stock exchanges—	
		(a) of $15.6 billion or above;	10

Column 1	Column 2	Column 3	Column 4
Item	Risk class	Type of risk factors	Liquidity horizon (in days)
		(b) lower than \$15.6 billion	20
		Equity volatility in relation to equity with market capitalization, based on the sum of market values of all the outstanding shares issued by the same legal entity across all stock exchanges—	
		(a) of \$15.6 billion or above;	20
		(b) lower than \$15.6 billion	60
		Other types	60

Column 1	Column 2	Column 3	Column 4
Item	Risk class	Type of risk factors	Liquidity horizon (in days)
4.	Foreign exchange risk	Foreign exchange rate in relation to USD/AUD, USD/BRL, USD/CAD, USD/CHF, USD/CNY, USD/EUR, USD/GBP, USD/HKD, USD/INR, USD/JPY, USD/KRW, USD/MXN, USD/NOK, USD/NZD, USD/RUB, USD/SEK, USD/SGD, USD/TRY, USD/ZAR and their first-order cross-currency pairs between each other	10

Column 1	Column 2	Column 3	Column 4
Item	Risk class	Type of risk factors	Liquidity horizon (in days)
		Foreign exchange rate in relation to currency pairs other than USD/AUD, USD/BRL, USD/CAD, USD/CHF, USD/CNY, USD/EUR, USD/GBP, USD/HKD, USD/INR, USD/JPY, USD/KRW, USD/MXN, USD/NOK, USD/NZD, USD/RUB, USD/SEK, USD/SGD, USD/TRY, USD/ZAR and their first-order cross-currency pairs between each other	20

Column 1	Column 2	Column 3	Column 4
Item	Risk class	Type of risk factors	Liquidity horizon (in days)
		Foreign exchange volatility	40
		Other types	40
5.	Commodity risk	Energy and carbon emissions trading prices	20
		Precious metals and non-ferrous metals price	20
		Other commodity price	60
		Energy and carbon emissions and trading volatility	60
		Precious metals and non-ferrous metals volatility	60
		Other commodity volatility	120
		Other types	120

(2) For the purposes of subsection (1)(d), the institution must—

(a) obtain the approval of the Monetary Authority for any model changes that affect the institution's core model documentation; and

(b) promptly notify the Monetary Authority of any update of the institution's non-core model documentation.

(3) If the Monetary Authority considers that a weekly calculation of $ES_{F,C,i}$, $ES_{R,C,i}$ and $ES_{R,S,i}$, as referred to in Formula 28D of these Rules, leads to a systematic underestimation of risks relative to a daily calculation, the Monetary Authority may require the institution to calculate $ES_{F,C,i}$, $ES_{R,C,i}$ and $ES_{R,S,i}$ on a daily basis.

2. Additional requirements relating to use of relevant models to calculate default risk charge

(1) In addition to section 1 of this Schedule, an authorized institution must demonstrate to the satisfaction of the Monetary Authority that, if the institution uses the relevant models to calculate the default risk charge—

(a) the relevant models capture and adequately reflect, on a continuing basis, the default risk inherent in the institution's relevant positions as specified in paragraph (a) of the definition of ***default risk charge*** in section 281 of these Rules;

(b) the default risk charge is measured as a VaR at a 99.9% confidence level over a one-year liquidity horizon;

(c) except for the equity positions referred to in paragraph (d), the default risk charge must be based on the assumption of constant positions over a one-year horizon;

(d) the liquidity horizon for designated sets of equity positions may be set with a floor of 60 days instead of the one-year liquidity horizon and, consistently and across all designated sets of equity positions, the default risk charge must be based on the assumption of constant positions over the liquidity horizon;

(e) the relevant models simulate the default event for each obligor, taking into account—

(i) 2 types of systematic risk factors; and

(ii) the economic cycle, including the dependence of the recovery on the systematic risk factors referred to in subparagraph (i);

(f) where the institution uses the IRB approach, the relevant models apply a probability of default, subject to a floor of 0.03%, and the loss given default, estimated under the IRB approach;

(g) where the institution uses the IRB approach and the estimates referred to in paragraph (f) do not exist, or where the institution does not use the IRB approach, the relevant models apply—

(i) a probability of default for each obligor, subject to a floor of 0.03%, and the relevant models must—

(A) estimate the probability of default based on historical data of both formal default events and price declines equivalent to default losses over a one-year period, where that data is based on publicly traded securities over a complete economic cycle with a minimum historical observation period of 5 years; or

(B) use the probability of default provided by external sources that are relevant to the institution's portfolio; and

(ii) the loss given default that reflects the type and seniority of the position, and the relevant models must—

(A) estimate the loss given default based on historical data that is sufficient to derive robust and accurate estimates; or

(B) use the loss given default provided by external sources that are relevant to the institution's portfolio;

(h) the relevant models incorporate correlation effects between defaults among obligors, including the effect on correlations of periods of stress, that—

(i) are based on objective data of credit spreads and listed equity prices;

(ii) are calibrated with data covering a period of at least 10 years that includes the stressed ES relevant period and are measured over a one-year liquidity horizon; and

(iii) the institution must reflect all significant basis risks in recognizing the correlations;

(i) the relevant models reflect netting of long and short exposures to the same obligor and that netting accounts for different losses in different instruments with exposures to the same obligor (for example, differences in seniority);

(j) the relevant models capture explicitly the basis risk between long and short exposures to different obligors;

(k) the relevant models capture explicitly any material mismatch between a position and its hedge as well as any maturity mismatch between a long and a short position with a maturity of less than one year;

(l) the relevant models reflect—

(i) issuer and market concentration; and

(ii) concentrations that may arise within and across product classes under stressed conditions;

(m) the relevant models reflect the nonlinear impact of options and other positions with material nonlinear behaviour with respect to default, taking account of model risk inherent in the valuation and estimation of price risks associated with those positions; and

(n) the default risk charge is computed at least once a week.

(2) For the purposes of subsection (1)(j), the potential for offsetting default risk among long and short exposures across different obligors must be included through the modelling of defaults.

(3) To avoid doubt, an authorized institution must not pre-net positions before input into its internal model other than as specified in subsection (1)(i).

(Schedule 3 replaced L.N. 167 of 2023)

Schedule 4

(Repealed L.N. 167 of 2023)

Schedule 4A

[s. 2 & Sch. 4D]

Qualifying Criteria to be Met to be CET1 Capital

1. Qualifying criteria

A capital instrument qualifies as CET1 capital of an authorized institution only if the following criteria are met—

(a) the instrument entitles the holder of the instrument to the most subordinated claim in a liquidation of the institution;

(b) the instrument entitles the holder of the instrument to a claim on the residual assets of the institution, that, in the event of its liquidation, and after the payment of all senior claims, is proportional with the holder's share of issued capital and is not fixed or subject to a cap (that is, the holder has an unlimited and variable claim);

(c) the instrument is perpetual and the principal amount of the instrument must not be repaid outside of a liquidation (except discretionary repurchases or other discretionary means of reducing capital that is permitted under applicable law);

(d) the institution has not created, and has not done anything to create, an expectation at issuance that the instrument will be bought back, redeemed or cancelled, and there are no statutory or contractual terms that might reasonably give rise to such an expectation;

(e) for distributions to holders of the instrument—

(i) the distributions are paid only out of distributable items;

(ii) the level of distributions is not in any way tied or linked to the amount paid up at issuance;

(iii) the terms and conditions of the instrument do not include a cap or other restrictions on the maximum level of distributions except to the extent that the institution is unable to pay distributions that exceed the level of distributable items;

(iv) the terms and conditions of the instrument do not include any obligation for the institution to make distributions to holders of the instrument;

(v) the non-payment of distributions does not constitute an event of default of the institution; and

(vi) there are no preferential distributions, including in respect of CET1 capital instruments, and distributions are paid only after all legal and contractual obligations have been met and payments on more senior capital instruments have been made;

(f) subject to section 2 of this Schedule, the instrument takes the first and proportionately greatest share of losses as they occur;

(g) the instrument absorbs losses on a going concern basis proportionately and pari passu with all other CET1 capital instruments of the same quality issued by the institution;

(h) the paid-up amount is recognized as equity capital for the purposes of determining balance sheet insolvency;

(i) the paid-up amount is classified as equity within the meaning of applicable accounting standards;

(j) the instrument is directly issued by the institution and paid up;

(k) the institution has not directly or indirectly funded the purchase of the instrument;

(l) the paid-up amount is not secured or covered by a guarantee of the institution or by an affiliate of the institution, and is not subject to any other arrangement that legally or economically enhances the seniority of the claim;

(m) the instrument is only issued with the approval of the shareholders of the institution, either given directly by the shareholders or, if permitted by applicable law, given by the board of directors or by other persons duly authorized by the shareholders;

(n) the instrument is clearly and separately disclosed on the balance sheet in the financial statements of the institution.

2. Provision supplementary to section 1(f) of this Schedule

Where the capital instrument referred to in section 1(f) of this Schedule is an ordinary share, and the authorized institution concerned has any other capital instrument that has a permanent write-down feature, the criterion set out in that section is to be assessed in respect of the ordinary share as if the institution had no such other capital instrument.

(Schedule 4A added L.N. 156 of 2012)

Schedule 4B

[ss. 2 & 39 & Sch. 4D]
(L.N. 167 of 2023)

Qualifying Criteria to be Met to be Additional Tier 1 Capital

1. Qualifying criteria

A capital instrument qualifies as Additional Tier 1 capital of an authorized institution only if the following criteria are met—

(a) the instrument is issued and paid up;

(ab) subject to section 3 of this Schedule, the instrument, if issued in Hong Kong, must be issued to a professional investor; *(L.N. 222 of 2018)*

(b) the instrument is subordinated to depositors, general creditors and other subordinated debt of the institution;

(c) the paid-up amount is not secured or covered by a guarantee of the institution or by an affiliate of the institution, and is not subject to any other arrangement that legally or economically enhances the seniority of the claim;

(d) the instrument is perpetual and the terms and conditions of the instrument contain no step-ups or other incentives to redeem;

(e) if the terms and conditions of the instrument include one or more call options, any such option may only be exercised at the initiative of the issuer after at least 5 years, and—

(i) to exercise a call option, the institution must have the prior consent of the Monetary Authority;

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

(iii) the institution must not exercise a call option unless it—

(A) replaces the called instrument with capital of the same or better quality and the replacement of the capital is effected on conditions that are sustainable for the income capacity of the institution; or

(B) demonstrates that its capital position is well above the minimum capital requirements applicable to it, and will remain to be well above those requirements after the call option is exercised;

(f) any repayment of principal (whether through repurchase, redemption or otherwise) can only be made with the prior consent of the Monetary Authority and the institution has not assumed or created market expectations that the Monetary Authority's consent will be given;

(g) the dividend or coupon distributions in respect of the instrument are subject to the following—

(i) the institution has full discretion at all times to cancel the distributions on the instrument for an unlimited period and on a non-cumulative basis;

(ii) the institution has full access to cancelled payments to meet its obligations as they fall due;

(iii) the cancellation of distributions on the instrument does not constitute an event of default for the instrument;

(iv) the cancellation of distributions on the instrument imposes no restrictions on the institution except in relation to distributions to ordinary shareholders;

(h) dividends or coupons are paid only out of distributable items;

(i) the instrument does not have a credit sensitive dividend feature such that the level of dividend or coupon to be paid is reset periodically based in whole or in part on the institution's own credit risk;

(j) the instrument does not contribute to liabilities exceeding assets of the institution if a balance sheet test forms part of national insolvency law applicable to the insolvency of the issuing institution;

(k) where the instrument is classified as a liability for accounting purposes—

(i) the terms and conditions of the instrument include a provision requiring the amount of the instrument to be written down, or converted to ordinary shares, when the CET1 capital ratio of the institution reaches—

(A) a level at or below 5.125%; or

(B) a level higher than 5.125% where determined by the institution and specified in the terms and conditions of the instrument;

(ii) the write-down or conversion to be effected under subparagraph (i) generates equity capital under applicable accounting standards and the instrument only receives recognition in Additional Tier 1 capital up to the minimum level of CET1 capital generated by a full write-down or conversion of the instrument; and

(iii) under the terms and conditions of the instrument, the write-down or conversion will occur at least to the extent necessary to return the institution's CET1 capital ratio to a level specified in subparagraph (i) or to the extent of the full amount of the instrument, whichever is the lower;

(l) for the purposes of paragraph (k), the write-down mechanism that allocates losses to the instrument when the CET1 capital ratio falls to a level specified in paragraph (k)(i) has the following effects—

(i) it reduces the claim of the holder of the instrument in a liquidation of the institution;

(ii) it reduces the amount to be re-paid when a call option is exercised;

(iii) it partially or fully reduces dividend or coupon distributions in respect of the instrument;

(m) neither the institution nor an affiliate of the institution over which the institution exercises control or significant influence (excluding the holding company of the institution) has purchased the instrument;

(n) the institution has not directly or indirectly funded the purchase of the instrument;

(o) the instrument has no features that hinder recapitalization (for example, provisions that require the issuer to compensate holders of the instrument if a new instrument is issued at a lower price during a specified time frame);

(p) if the instrument is not issued out of an operating entity (being an entity established to conduct business with clients with a view to making a profit in its own right) or any holding company of the institution (for example, the instrument is issued by a special purpose vehicle), proceeds are immediately available without limitation to an operating entity or the holding company of the institution, as the case may be, in a form that meets all of the other qualifying criteria set out in this Schedule for inclusion in Additional Tier 1 capital;

(q) the terms and conditions of the instrument contain a provision requiring the instrument to be written down, or converted into ordinary shares, at the point of non-viability and, in this regard, the institution ensures that—

(i) the instrument will be either written off or converted into ordinary shares on the occurrence of the trigger event;

(ii) any compensation paid to the holders of the instrument as a result of a write-off will be paid immediately in the form of ordinary shares of the institution or, with the Monetary Authority's prior consent, of any other company;

(iii) the trigger event is the earlier of—

(A) the Monetary Authority notifying the institution in writing that the Monetary Authority is of the opinion that a write-off or conversion is necessary, without which the institution would become non-viable; or

(B) the Monetary Authority notifying the institution in writing that a decision has been made by the government body, a government officer or other relevant regulatory body with the authority to make such a decision, that a public sector injection of capital or equivalent support is necessary, without which the institution would become non-viable;

(iv) the issuance of new ordinary shares as a result of the trigger event can occur promptly following the occurrence of such trigger event so that, in the case of the trigger event referred to in subparagraph (iii)(B), it can occur before any public sector injection of capital thereby ensuring that the capital provided by the public sector will not be diluted;

(v) (if the institution wishes any instrument issued by an overseas subsidiary of the institution to be included in the capital base for the purposes of calculating its consolidated capital adequacy ratio pursuant to a section 3C requirement in addition to being included in the overseas subsidiary's solo capital adequacy ratio) the terms and conditions of the instrument specify that the Monetary Authority, in addition to the relevant authority in the jurisdiction of the overseas subsidiary, may trigger the write-down or conversion of the instrument;

(vi) (if the institution issuing the instrument is a Hong Kong subsidiary of an overseas banking group and the institution wishes the instrument to be included in the calculation of the capital adequacy ratio of its parent bank on a consolidated basis in addition to being included in its solo capital adequacy ratio) the terms and conditions of the instrument specify an additional trigger event, being the earlier of—

(A) the home authority notifying the parent bank of the institution in writing that the authority is of the opinion that a write-off or conversion is necessary, without which the institution or the parent bank of the institution would become non-viable; or

(B) the home authority notifying the parent bank of the institution in writing that the authority has decided that a public sector injection of capital or equivalent support, in the jurisdiction of the home authority, is necessary, without which the institution or the parent bank of the institution would become non-viable;

(vii) the institution maintains, at all times, all prior authorization necessary to immediately issue the relevant number of ordinary shares specified in the terms and conditions of the instrument, and there are no impediments to the write-off or automatic conversion of the instrument into ordinary shares of the institution if the trigger event or additional trigger event occurs; *(L.N. 128 of 2014)*

(viia) the institution obtains the prior consent of the Monetary Authority before including, as Additional Tier 1 capital, any issuance of a capital instrument the terms and conditions of which provide for trigger events in addition to the trigger events specified under this paragraph; and *(L.N. 128 of 2014)*

(viii) the institution submits the following information and documents to the Monetary Authority before including any issuance of a capital instrument as Additional Tier 1 capital— *(L.N. 128 of 2014)*

(A) if the terms and conditions of the instrument provide for trigger events in addition to the trigger events specified under this paragraph, a notice in writing to the Monetary Authority containing—

(I) the rationale for those additional trigger events; and

(II) an assessment by the institution of the possible market implications that might arise from the inclusion of those additional trigger events or on the occurrence of those additional trigger events;

(B) a detailed description of the rationale for the specified conversion method, including computations of the indicative dilution of the institution's ordinary shares that would occur on the occurrence of the trigger event and the resulting ordinary shareholder structure, and an explanation of why such a conversion method would help to ensure or maintain the viability of the institution; *(23 of 2016 s. 212)*

(r) if the instrument is issued on or after the commencement date* of Part 5 of the Financial Institutions (Resolution) Ordinance (Cap. 628), the terms and conditions of the instrument contain a provision to the effect that the holder of the instrument— *(E.R. 2 of 2017)*

(i) acknowledges that the instrument is subject to being written off, cancelled, converted or modified, or to having its form changed, in the exercise of powers under that 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; *(23 of 2016 s. 212; L.N. 222 of 2018)*

(s) subject to section 3 of this Schedule—

(i) the terms and conditions of the instrument contain a provision that the instrument is intended to qualify as Additional Tier 1 capital under these Rules; and

(ii) any prospectus or offering document prepared by or for the issuer in relation to the instrument—

(A) adequately 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 of high risk; and

(C) contains a statement that the instrument, if issued in Hong Kong, must be issued to a professional investor; *(L.N. 222 of 2018)*

(t) subject to section 3 of this Schedule, 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—Euro 200,000; 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. *(L.N. 222 of 2018)*

Editorial Note:

* Commencement date: 7 July 2017.

2. Application of section 1(k) and (q) of this Schedule to capital instruments other than ordinary shares

Section 1(k) and (q) of this Schedule, with necessary modifications, applies to a capital instrument that is equivalent to an ordinary share in the case of an entity other than a joint-stock company as it applies to an ordinary share in the case of a joint-stock company.

3. Section 1(ab), (s) and (t) of this Schedule not applicable to certain instruments

(1) Section 1(ab), (s) and (t) of this Schedule does not apply to an instrument issued before 11 January 2019.

(2) Section 1(ab), (s)(ii) and (t) of this Schedule does not apply in determining whether an instrument qualifies as Additional Tier 1 capital of an authorized institution if the instrument is issued to and held by an entity within the same banking group as the institution.

(L.N. 222 of 2018)

4. Interpretation of certain expressions in section 1(q)(v) and (vi)

(1) In section 1(q)(v), a reference to an overseas subsidiary of an authorized institution does not include a subsidiary of the institution that is a re-domiciled entity.

(2) In section 1(q)(vi), a reference to a Hong Kong subsidiary of an overseas banking group includes a subsidiary of the banking group that is a re-domiciled entity.

(14 of 2025 s. 180)

(Schedule 4B added L.N. 156 of 2012)

Schedule 4C

[ss. 2 & 40 & Sch. 4D]
(L.N. 167 of 2023)

Qualifying Criteria to be Met to be Tier 2 Capital

1. Qualifying criteria

A capital instrument qualifies as Tier 2 capital of an authorized institution only if the following criteria are met—

(a) the instrument is issued and paid up;

(ab) subject to section 3 of this Schedule, the instrument, if issued in Hong Kong, must be issued to a professional investor; *(L.N. 222 of 2018)*

(b) the instrument is subordinated to depositors and general creditors of the institution;

(c) the paid-up amount is not secured or covered by a guarantee of the institution or by an affiliate of the institution, and is not subject to any other arrangement that legally or economically enhances the seniority of the claim;

(d) the instrument has a minimum original maturity of at least 5 years, the terms and conditions of the instrument contain no step-ups or other incentives to redeem, and the recognition of the instrument in regulatory capital in the remaining 5 years before maturity is amortized on a straight line basis of 20% per year;

(e) if the terms and conditions of the instrument include one or more call options, any such option may only be exercised at the initiative of the issuer after at least 5 years, and—

(i) to exercise a call option, the institution must have the prior consent of the Monetary Authority;

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

(iii) the institution must not exercise a call option unless it—

(A) replaces the called instrument with capital of the same or better quality and the replacement of the capital is effected on conditions that are sustainable for the income capacity of the institution; or

(B) demonstrates that its capital position is well above the minimum capital requirements applicable to it, and will remain to be well above those requirements after the call option is exercised;

(f) the holders of the instrument have no rights to accelerate the payment or repayment of future scheduled payments (coupon or principal) except in the event of a liquidation of the institution;

(g) the instrument does not have a credit sensitive dividend feature such that the level of dividend or coupon to be paid is reset periodically based in whole or in part on the institution's own credit risk;

(h) neither the institution nor an affiliate of the institution over which the institution exercises control or significant influence (excluding the holding company of the institution) has purchased the instrument;

(i) the institution has not directly or indirectly funded the purchase of the instrument;

(j) if the instrument is not issued out of an operating entity (being an entity established to conduct business with clients with a view to making a profit in its own right) or any holding company of the institution (for example, the instrument is issued by a special purpose vehicle), proceeds are immediately available without limitation to an operating entity or the holding company of the institution, as the case may be, in a form that meets all of the other qualifying criteria set out in this Schedule for inclusion in Tier 2 capital;

(k) the terms and conditions of the instrument contain a provision requiring the instrument to be written down, or converted into ordinary shares, at the point of non-viability and, in this regard, the institution ensures that—

(i) the instrument will be either written off or converted into ordinary shares on the occurrence of the trigger event;

(ii) any compensation paid to the holders of the instrument as a result of a write-off will be paid immediately in the form of ordinary shares of the institution or, with the Monetary Authority's prior consent, of any other company;

(iii) the trigger event is the earlier of—

(A) the Monetary Authority notifying the institution in writing that the Monetary Authority is of the opinion that a write-off or conversion is necessary, without which the institution would become non-viable; or

(B) the Monetary Authority notifying the institution in writing that a decision has been made by the government body, a government officer or other relevant regulatory body with the authority to make such a decision, that a public sector injection of capital or equivalent support is necessary, without which the institution would become non-viable;

(iv) the issuance of new ordinary shares as a result of the trigger event can occur promptly following the occurrence of such trigger event so that, in the case of the trigger event referred to in subparagraph (iii)(B), it can occur before any public sector injection of capital thereby ensuring that the capital provided by the public sector will not be diluted;

(v) (if the institution wishes any instrument issued by an overseas subsidiary of the institution to be included in the capital base for the purposes of calculating its consolidated capital adequacy ratio pursuant to a section 3C requirement in addition to being included in the overseas subsidiary's solo capital adequacy ratio) the terms and conditions of the instrument specify that the Monetary Authority, in addition to the relevant authority in the jurisdiction of the overseas subsidiary, may trigger the write-down or conversion of the instrument;

(vi) (if the institution issuing the instrument is a Hong Kong subsidiary of an overseas banking group and the institution wishes the instrument to be included in the calculation of the capital adequacy ratio of its parent bank on a consolidated basis in addition to being included in its solo capital adequacy ratio) the terms and conditions of the instrument specify an additional trigger event, being the earlier of—

(A) the home authority notifying the parent bank of the institution in writing that the authority is of the opinion that a write-off or conversion is necessary, without which the institution or the parent bank of the institution would become non-viable; or

(B) the home authority notifying the parent bank of the institution in writing that the authority has decided that a public sector injection of capital or equivalent support, in the jurisdiction of the home authority, is necessary, without which the institution or the parent bank of the institution would become non-viable;

(vii) the institution maintains, at all times, all prior authorization necessary to immediately issue the relevant number of ordinary shares specified in the terms and conditions of the instrument and there are no impediments to the write-off or automatic conversion of the instrument into ordinary shares of the institution if the trigger event or additional trigger event occurs; *(L.N. 128 of 2014)*

(viia) the institution obtains the prior consent of the Monetary Authority before including, as Tier 2 capital, any issuance of a capital instrument the terms and conditions of which provide for trigger events in addition to the trigger events specified under this paragraph; and *(L.N. 128 of 2014)*

(viii) the institution submits the following information and documents to the Monetary Authority before including any issuance of a capital instrument as Tier 2 capital— *(L.N. 128 of 2014)*

(A) if the terms and conditions of the instrument provide for trigger events in addition to the trigger events specified under this paragraph, a notice in writing to the Monetary Authority containing—

(I) the rationale for those additional trigger events; and

(II) an assessment by the institution of the possible market implications that might arise from the inclusion of those additional trigger events or on the occurrence of those additional trigger events;

(B) a detailed description of the rationale for the specified conversion method, including computations of the indicative dilution of the institution's ordinary shares that would occur on the occurrence of the trigger event and the resulting ordinary shareholder structure, and an explanation of why such a conversion method would help to ensure or maintain the viability of the institution; *(23 of 2016 s. 213)*

(l) if the instrument is issued on or after the commencement date* of Part 5 of the Financial Institutions (Resolution) Ordinance (Cap. 628), the terms and conditions of the instrument contain a provision to the effect that the holder of the instrument— *(E.R. 2 of 2017)*

(i) acknowledges that the instrument is subject to being written off, cancelled, converted or modified, or to having its form changed, in the exercise of powers under that 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; *(23 of 2016 s. 213; L.N. 222 of 2018)*

(m) subject to section 3 of this Schedule—

(i) the terms and conditions of the instrument contain a provision that the instrument is intended to qualify as Tier 2 capital under these Rules; and

(ii) any prospectus or offering document prepared by or for the issuer in relation to the instrument—

(A) adequately 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 of high risk; and

(C) contains a statement that the instrument, if issued in Hong Kong, must be issued to a professional investor; *(L.N. 222 of 2018)*

(n) subject to section 3 of this Schedule, 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—Euro 200,000; 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. *(L.N. 222 of 2018)*

Editorial Note:

* Commencement date: 7 July 2017.

2. Application of section 1(k) of this Schedule to capital instruments other than ordinary shares

Section 1(k) of this Schedule, with necessary modifications, applies to a capital instrument that is equivalent to an ordinary share in the case of an entity other than a joint-stock company as it applies to an ordinary share in the case of a joint-stock company.

3. Section 1(ab), (m) and (n) of this Schedule not applicable to certain instruments

(1) Section 1(ab), (m) and (n) of this Schedule does not apply to an instrument issued before 11 January 2019.

(2) Section 1(ab), (m)(ii) and (n) of this Schedule does not apply in determining whether an instrument qualifies as Tier 2 capital of an authorized institution if the instrument is issued to and held by an entity within the same banking group as the institution.

(L.N. 222 of 2018)

4. Interpretation of certain expressions in section 1(k)(v) and (vi)

(1) In section 1(k)(v), a reference to an overseas subsidiary of an authorized institution does not include a subsidiary of the institution that is a re-domiciled entity.

(2) In section 1(k)(vi), a reference to a Hong Kong subsidiary of an overseas banking group includes a subsidiary of the banking group that is a re-domiciled entity.

(14 of 2025 s. 181)

(Schedule 4C added L.N. 156 of 2012)

Schedule 4D

[ss. 38, 39 & 40]

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. Interpretation of Schedule 4D

In this Schedule—

retained earnings (保留溢利) has the meaning given by section 35 of these Rules;

Tier 1 capital instrument (一級資本票據) means CET1 capital instrument and Additional Tier 1 capital instrument.

2. Minority interests and capital instruments

(1) For inclusion of a minority interest arising from the CET1 capital instruments issued by a consolidated bank subsidiary of an authorized institution and held by third parties (***minority interest***) in the institution's CET1 capital calculated on a consolidated basis, the following requirements must be met—

(a) the CET1 capital instruments would, if they were issued by the institution, meet the qualifying criteria set out in Schedule 4A for inclusion in CET1 capital;

(b) the minority interest must include retained earnings and reserves and share premium accounts, if any, of the consolidated bank subsidiary that are attributable to third parties resulting from the issue of the CET1 capital instruments.

(2) For inclusion of a capital instrument issued by a consolidated bank subsidiary of an authorized institution and held by third parties (***minority capital instrument***) in the institution's Additional Tier 1 capital, Tier 1 capital, Tier 2 capital and Total capital calculated on a consolidated basis, the following requirements must be met—

(a) for inclusion in the institution's Additional Tier 1 capital, the minority capital instrument would, if it were issued by the institution, meet the qualifying criteria set out in Schedule 4B;

(b) for inclusion in the institution's Tier 2 capital, the minority capital instrument would, if it were issued by the institution, meet the qualifying criteria set out in Schedule 4C;

(c) the minority capital instrument must include share premium accounts, if any, of the consolidated bank subsidiary that are attributable to third parties resulting from the issue of the instrument.

(3) For inclusion of a minority interest or minority capital instrument in an authorized institution's capital base calculated on a consolidated basis, the institution or an affiliate of the institution must not fund directly or indirectly (whether through a special purpose vehicle or through any other vehicle or arrangement) the purchase of the interest or instrument in the relevant consolidated bank subsidiary of the institution.

(4) *(Repealed L.N. 222 of 2018)*

3. Computation of applicable amount of minority interests for inclusion in authorized institution's CET1 capital on consolidated basis

(1) Where a bank subsidiary of an authorized institution is

a member of the institution's consolidation group, the maximum amount of minority interests in the subsidiary that may be included in the CET1 capital of the institution on a consolidated basis is the total amount of minority interests arising from the issuance by the subsidiary to third parties of CET1 capital instruments that meet the requirements of section 2 of this Schedule, less the amount of surplus CET1 capital of the subsidiary attributable to third parties calculated under subsections (1A), (1B) and (1C).

(1A) If the subsidiary is incorporated in Hong Kong or is a re-domiciled entity, the surplus CET1 capital of the subsidiary is calculated as the CET1 capital of the subsidiary less the lower of— *(14 of 2025 s. 182)*

(a) the sum of the risk-weighted amount for credit risk, risk-weighted amount for market risk, risk-weighted amount for CVA risk, risk-weighted amount for operational risk and risk-weighted amount for sovereign concentration 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— *(L.N. 222 of 2018; L.N. 167 of 2023)*

(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 section 3B and, if applicable, as varied by the Monetary Authority under section 97F of the Ordinance (specified minimum ratio); and

(ii) the buffer level applicable to the subsidiary under section 3G; and

(b) the portion of the sum of the risk-weighted amount for credit risk, risk-weighted amount for market risk, risk-weighted amount for CVA risk, risk-weighted amount for operational risk and risk-weighted amount for sovereign concentration risk of the authorized institution calculated on a consolidated basis, that relates to the subsidiary, multiplied by a percentage equal to the sum of— *(L.N. 222 of 2018; L.N. 167 of 2023)*

(i) subject to subsection (2), the minimum CET1 capital ratio that the institution must comply with, on a consolidated basis, under section 3B and, if applicable, as varied by the Monetary Authority under section 97F of the Ordinance (specified minimum ratio); and

(ii) the buffer level applicable to the institution under section 3G. *(L.N. 212 of 2015; L.N. 167 of 2023)*

(1B) If the subsidiary is not incorporated in Hong Kong and is not a re-domiciled entity, 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, risk-weighted amount for CVA risk, risk-weighted amount for operational risk and risk-weighted amount for sovereign concentration risk of the authorized institution calculated on a consolidated basis, that relates to the subsidiary, multiplied by a percentage equal to the sum of— *(L.N. 222 of 2018; L.N. 167 of 2023; 14 of 2025 s. 182)*

(a) subject to subsection (2), the minimum CET1 capital ratio that the institution must comply with, on a consolidated basis, under section 3B and, if applicable, as varied by the Monetary Authority under section 97F of the Ordinance (specified minimum ratio); and

(b) the buffer level applicable to the institution under section 3G. *(L.N. 212 of 2015; L.N. 167 of 2023)*

(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. *(L.N. 212 of 2015)*

(2) Subject to subsection (3), an authorized institution may choose to use 4.5% instead of the specified minimum ratio referred to in subsections (1A)(a)(i) and (b)(i) and (1B)(a).

(3) For the purposes of subsection (2)—

(a) an authorized institution must notify the Monetary Authority before it uses the substitute percentage referred to in that subsection; and

(b) if an authorized institution has chosen to use the substitute percentage referred to in that subsection, the institution must not, without the Monetary Authority's prior consent, use the specified minimum ratio referred to in subsections (1A)(a)(i) and (b)(i) and (1B)(a).

(4) To avoid doubt—

(a) the calculation under subsection (1) must be undertaken for each individual bank subsidiary separately; and

(b) an authorized institution must use only either the specified minimum ratio referred to in subsections (1A)(a)(i) and (b)(i) and (1B)(a) or the substitute percentage referred to in subsection (2) in respect of all the bank subsidiaries of the institution that are members of the institution's consolidation group.

(L.N. 212 of 2015)

4. Computation of applicable amount of minority interests and minority capital instruments for inclusion in authorized institution's Tier 1 capital on consolidated basis

(1) Subject to subsection (2), where a bank subsidiary of an authorized institution is a member of the institution's consolidation group, the maximum amount of Tier 1 capital instruments issued by the subsidiary to third parties that may be included in the Tier 1 capital of the institution on a consolidated basis is the total amount of Tier 1 capital instruments held by third parties that meet the requirements of section 2 of this Schedule, less the amount of surplus Tier 1 capital of the subsidiary attributable to third parties calculated under subsections (1A), (1B) and (1C).

(1A) If the subsidiary is incorporated in Hong Kong or is a re-domiciled entity, the surplus Tier 1 capital of the subsidiary is calculated as the Tier 1 capital of the subsidiary less the lower of— *(14 of 2025 s. 182)*

(a) the sum of the risk-weighted amount for credit risk, risk-weighted amount for market risk, risk-weighted amount for CVA risk, risk-weighted amount for operational risk and risk-weighted amount for sovereign concentration 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— *(L.N. 222 of 2018; L.N. 167 of 2023)*

(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 section 3B and, if applicable, as varied by the Monetary Authority under section 97F of the Ordinance (specified minimum ratio); and

(ii) the buffer level applicable to the subsidiary under section 3G; and

(b) the portion of the sum of the risk-weighted amount for credit risk, risk-weighted amount for market risk, risk-weighted amount for CVA risk, risk-weighted amount for operational risk and risk-weighted amount for sovereign concentration risk of the authorized institution calculated on a consolidated basis, that relates to the subsidiary, multiplied by a percentage equal to the sum of— *(L.N. 222 of 2018; L.N. 167 of 2023)*

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

(ii) the buffer level applicable to the institution under section 3G. *(L.N. 212 of 2015; L.N. 167 of 2023)*

(1B) If the subsidiary is not incorporated in Hong Kong and is not a re-domiciled entity, 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, risk-weighted amount for CVA risk, risk-weighted amount for operational risk and risk-weighted amount for sovereign concentration risk of the authorized institution calculated on a consolidated basis, that relates to the subsidiary, multiplied by a percentage equal to the sum of— *(L.N. 222 of 2018; L.N. 167 of 2023; 14 of 2025 s. 182)*

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

(b) the buffer level applicable to the institution under section 3G. *(L.N. 212 of 2015; L.N. 167 of 2023)*

(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. *(L.N. 212 of 2015)*

(2) The amount of Tier 1 capital recognized in the consolidated Additional Tier 1 capital of an authorized institution must exclude the portion that has been recognized in the consolidated CET1 capital under section 3 of this Schedule.

(3) Subject to subsection (4), an authorized institution may choose to use 6% instead of the specified minimum ratio referred to in subsections (1A)(a)(i) and (b)(i) and (1B)(a).

(4) For the purposes of subsection (3)—

(a) an authorized institution must notify the Monetary Authority before it uses the substitute percentage referred to in that subsection; and

(b) if an authorized institution has chosen to use the substitute percentage referred to in that subsection, the institution must not, without the Monetary Authority's prior consent, use the specified minimum ratio referred to in subsections (1A)(a)(i) and (b)(i) and (1B)(a).

(5) To avoid doubt—

(a) the calculation under subsection (1) must be undertaken for each individual bank subsidiary separately; and

(b) an authorized institution must use only either the specified minimum ratio referred to in subsections (1A)(a)(i) and (b)(i) and (1B)(a) or the substitute percentage referred to in subsection (3) in respect of all the bank subsidiaries of the institution that are members of the institution's consolidation group.

(L.N. 212 of 2015)

5. Computation of applicable amount of minority interests and minority capital instruments for inclusion in authorized institution's Total capital on consolidated basis

(1) Subject to subsection (2), where a bank subsidiary of an authorized institution is a member of the institution's consolidation group, the maximum amount of Tier 1 capital instruments and Tier 2 capital instruments issued by the subsidiary to third parties that may be included in the Total capital of the institution on a consolidated basis is the total amount of Tier 1 capital instruments and Tier 2 capital instruments held by third parties that meet the requirements of section 2 of this Schedule, less the amount of surplus Total capital of the subsidiary attributable to third parties calculated under subsections (1A), (1B) and (1C).

(1A) If the subsidiary is incorporated in Hong Kong or is a re-domiciled entity, the surplus Total capital of the subsidiary is calculated as the Total capital of the subsidiary less the lower of— *(14 of 2025 s. 182)*

(a) the sum of the risk-weighted amount for credit risk, risk-weighted amount for market risk, risk-weighted amount for CVA risk, risk-weighted amount for operational risk and risk-weighted amount for sovereign concentration 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— *(L.N. 222 of 2018; L.N. 167 of 2023)*

(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 section 3B and, if applicable, as varied by the Monetary Authority under section

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

(ii) the buffer level applicable to the subsidiary under section 3G; and

(b) the portion of the sum of the risk-weighted amount for credit risk, risk-weighted amount for market risk, risk-weighted amount for CVA risk, risk-weighted amount for operational risk and risk-weighted amount for sovereign concentration risk of the authorized institution calculated on a consolidated basis, that relates to the subsidiary, multiplied by a percentage equal to the sum of— *(L.N. 222 of 2018; L.N. 167 of 2023)*

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

(ii) the buffer level applicable to the institution under section 3G. *(L.N. 212 of 2015; L.N. 167 of 2023)*

(1B) If the subsidiary is not incorporated in Hong Kong and is not a re-domiciled entity, 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, risk-weighted amount for CVA risk, risk-weighted amount for operational risk and risk-weighted amount for sovereign concentration risk of the authorized institution calculated on a consolidated basis, that relates to the subsidiary, multiplied by a percentage equal to the sum of— *(L.N. 222 of 2018; L.N. 167 of 2023; 14 of 2025 s. 182)*

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

(b) the buffer level applicable to the institution under section 3G. *(L.N. 212 of 2015; L.N. 167 of 2023)*

(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. *(L.N. 212 of 2015)*

(2) The amount of Total capital recognized in the consolidated Tier 2 capital of an authorized institution must exclude the portion that has been recognized in the consolidated Tier 1 capital under section 4 of this Schedule.

(3) Subject to subsection (4), an authorized institution may choose to use 8% instead of the specified minimum ratio referred to in subsections (1A)(a)(i) and (b)(i) and (1B)(a).

(4) For the purposes of subsection (3)—

(a) an authorized institution must notify the Monetary Authority before it uses the substitute percentage referred to in that subsection; and

(b) if an authorized institution has chosen to use the substitute percentage referred to in that subsection, the institution must not, without the Monetary Authority's prior consent, use the specified minimum ratio referred to in subsections (1A)(a)(i) and (b)(i) and (1B)(a).

(5) To avoid doubt—

(a) the calculation under subsection (1) must be undertaken for each individual bank subsidiary separately; and

(b) an authorized institution must use only either the specified minimum ratio referred to in subsections (1A)(a)(i) and (b)(i) and (1B)(a) or the substitute percentage referred to in subsection (3) in respect of all the bank subsidiaries of the institution that are members of the institution's consolidation group.

(L.N. 212 of 2015)

(Schedule 4D added L.N. 156 of 2012)

Schedule 4E

[ss. 43, 47 & 48]

Deduction of Holdings of Own CET1 Capital Instruments, Additional Tier 1 Capital Instruments and Tier 2 Capital Instruments

1. Deduction of holdings of own CET1 capital instruments, Additional Tier 1 capital instruments and Tier 2 capital instruments

(1) For the purposes of sections 43(1)(l), 47(1)(a) and 48(1)(a) of these Rules, an authorized institution must, subject to subsections (2), (3) and (4)—

(a) calculate the amount of any direct holdings, indirect holdings or synthetic holdings of its own CET1 capital instruments, Additional Tier 1 capital instruments and Tier 2 capital instruments (***own capital instruments***) to be deducted from its capital base 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 such deductions from its CET1 capital, Additional Tier 1 capital or Tier 2 capital, as the case requires.

(2) An authorized institution must calculate the amount of holdings of its own capital instruments 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) An authorized institution 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 capital instruments included in the underlying index.

(4) An authorized institution must net gross long positions in its own capital instruments resulting from holdings of index securities against short positions in its own capital instruments resulting from short positions in the same underlying index, including where those short positions involve counterparty credit risk.

(Schedule 4E added L.N. 156 of 2012)

Schedule 4F

[ss. 2, 43, 47, 48, 70A & 117F]

(L.N. 54 of 2022; L.N. 167 of 2023)

Deduction of Holdings where Authorized Institution has Insignificant LAC Investments in Financial Sector Entities that are outside Scope of Consolidation under Section 3C Requirement

1. Interpretation

In this Schedule—

(a) ***CET1 Capital (post-regulatory deduction)*** (CET1資本(經監管扣減後)), in relation to an authorized institution, means the amount of the institution's CET1 capital that is calculated after applying all regulatory deductions under sections 38(2) and 43(1) of these Rules, except those set out in section 43(1)(n), (o), (p) and (q) of these Rules;

(b) ***Inv(CET1)*** (投資額(CET1)), in relation to an authorized institution, means the amount of the institution's holdings of insignificant LAC investments that are CET1 capital investments in financial sector entities;

(c) ***Inv(AT1)*** (投資額(AT1)), in relation to an authorized institution, means the amount of the institution's holdings of insignificant LAC investments that are Additional Tier 1 capital investments in financial sector entities;

(d) ***Inv(T2)*** (投資額(T2)), in relation to an authorized institution, means the amount of the institution's holdings of insignificant LAC investments that are Tier 2 capital investments in financial sector entities;

(e) ***NCLAC investment*** (NCLAC投資) and ***Inv(NCLAC)*** (投資額(NCLAC)), in relation to an authorized institution, respectively mean the institution's holdings of insignificant LAC investments that are non-capital LAC liabilities in financial sector entities, and the amount of the holdings;

(f) ***10% threshold*** (10%門檻) is the amount calculated as follows—

CET1 Capital (post-regulatory deduction) × 10%;

(g) ***5% threshold*** (5%門檻) is the amount calculated as follows—

CET1 Capital (post-regulatory deduction) × 5%.

2. Deduction of holdings by resolution entity and material subsidiary

(1) In this section—

section 2 institution (第2條機構)—

(a) means an authorized institution that is a resolution entity or material subsidiary; but

(b) excludes an authorized institution if, because of subsection (2), it may be treated as a section 3 institution (within the meaning of section 3 of this Schedule).

(2) With the Monetary Authority's prior consent, an authorized institution which is a material subsidiary may be treated as a section 3 institution (within the meaning of section 3 of this Schedule).

(3) For the purposes of this section—

(a) a section 2 institution may designate any holdings in the institution's NCLAC investment as gross long deduction position if the holdings—

(i) are booked in the institution's trading book; and

(ii) are sold within 30 business days of the date of their acquisition;

(b) once any holdings in the institution's NCLAC investment have been designated under paragraph (a) as gross long deduction position, the holdings must not subsequently be included within the 10% threshold; and

(c) any holdings in the institution's NCLAC investment, despite having been designated under paragraph (a) as gross long deduction position, must cease to be treated as so designated if either or both of the conditions under that paragraph is or are no longer met in respect of the holdings.

(4) For the purposes of this section—

(a) ***Inv(CurDsg NCLAC)*** (投資額(現行指定NCLAC)), in relation to a section 2 institution, means the amount of the institution's holdings of NCLAC investment that are currently designated under subsection (3)(a) as gross long deduction position;

(b) ***Inv(NvDsg NCLAC)*** (投資額(從未指定NCLAC)), in relation to a section 2 institution, means the amount of the institution's holdings of NCLAC investment that have never been designated under subsection (3)(a) as gross long deduction position;

(c) ***Inv(FmDsg NCLAC)*** (投資額(曾指定NCLAC)), in relation to a section 2 institution, means the amount of the institution's holdings of NCLAC investment that were formerly designated under subsection (3)(a) as gross long deduction position but in respect of which either or both of the conditions under that subsection is or are no longer met;

(d) in determining Inv(CET1), Inv(AT1), Inv(T2) and Inv(NvDsg NCLAC)—

(i) the net long positions in both the institution's banking book and trading book must be included; and

(ii) 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;

(e) in determining Inv(CurDsg NCLAC), the gross long positions in the trading book must be included;

(f) ***Excess(10% threshold)(net long)*** (超出額(10%門檻)(淨長倉)) is the greater of the following—

(i) the amount calculated as follows—

[Inv(CET1) + Inv(AT1) + Inv(T2) + Inv(NvDsg NCLAC)] – 10% threshold;

(ii) zero;

(g) ***Excess(5% threshold)(gross long)*** (超出額(5%門檻)(總長倉)) is the greater of the following—

(i) the amount calculated as follows—

Inv(CurDsg NCLAC) – 5% threshold;

(ii) zero;

(h) ***CET1 percentage*** (CET1百分比) is the percentage calculated as follows—

100% × {Inv(CET1) / [Inv(CET1) + Inv(AT1) + Inv(T2) + Inv(NvDsg NCLAC)]};

(i) ***AT1 percentage*** (AT1百分比) is the percentage calculated as follows—

100% × {Inv(AT1) / [Inv(CET1) + Inv(AT1) + Inv(T2) + Inv(NvDsg NCLAC)]}; and

(j) ***T2 percentage*** (T2百分比) is the percentage calculated as follows—

100% × {[Inv(T2) + Inv(NvDsg NCLAC)] / [Inv(CET1) + Inv(AT1) + Inv(T2) + Inv(NvDsg NCLAC)]}.

(5) For the purposes of section 43(1)(o) of these Rules, the applicable amount of a section 2 institution's holdings of insignificant LAC investments that are CET1 capital investments in financial sector entities to be deducted from the institution's CET1 capital must be calculated as follows—

Excess(10% threshold)(net long) × CET1 percentage.

(6) For the purposes of section 47(1)(c) of these Rules, the applicable amount of a section 2 institution's holdings of insignificant LAC investments that are Additional Tier 1 capital investments in financial sector entities to be deducted from the institution's Additional Tier 1 capital must be calculated as follows—

Excess(10% threshold)(net long) × AT1 percentage.

(7) For the purposes of section 48(1)(c) of these Rules, the applicable amount of a section 2 institution's holdings of insignificant LAC investments that are Tier 2 capital investments in, or non-capital LAC liabilities of, financial sector entities to be deducted from the institution's Tier 2 capital must be calculated as follows—

[Excess(10% threshold)(net long) × T2 percentage] + Excess(5% threshold)(gross long) + Inv(FmDsg NCLAC).

3. Deduction of holdings by authorized institution, not being resolution entity or material subsidiary

(1) In this section—

section 3 institution (第3條機構) means an authorized institution which—

(a) is not a resolution entity or material subsidiary; or

(b) is a material subsidiary which, because of section 2(2) of this Schedule, may be treated as a section 3 institution.

(2) For the purposes of this section, a section 3 institution may allocate any holdings in the institution's NCLAC investment as gross long deduction position.

(3) For the purposes of this section—

(a) ***Inv(Alc NCLAC)*** (投資額(現行分配NCLAC)), in relation to a section 3 institution, means the amount of the institution's holdings of NCLAC investment that are currently allocated under subsection (2) as gross long deduction position;

(b) ***Inv(Non-Alc NCLAC)*** (投資額(未分配NCLAC)), in relation to a section 3 institution, means the amount of the institution's holdings of NCLAC investment that are not currently allocated under subsection (2) as gross long deduction position;

(c) in determining Inv(CET1), Inv(AT1), Inv(T2) and Inv(Non-Alc NCLAC)—

(i) the net long positions in both the institution's banking book and trading book must be included; and

(ii) 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;

(d) in determining Inv(Alc NCLAC), the gross long positions in both the banking book and trading book must be included;

(e) ***Excess(10% threshold)(net long)*** (超出額(10%門檻)(淨長倉)) is the greater of the following—

(i) the amount calculated as follows—

[Inv(CET1) + Inv(AT1) + Inv(T2) + Inv(Non-Alc NCLAC)] – 10% threshold;

(ii) zero;

(f) ***Excess(5% threshold)(gross long)*** (超出額(5%門檻)(總長倉)) is the greater of the following—

(i) the amount calculated as follows—

Inv(Alc NCLAC) – 5% threshold;

(ii) zero;

(g) ***CET1 percentage*** (CET1百分比) is the percentage calculated as follows—

100% × {Inv(CET1) / [Inv(CET1) + Inv(AT1) + Inv(T2) + Inv(Non-Alc NCLAC)]};

(h) ***AT1 percentage*** (AT1百分比) is the percentage calculated as follows—

100% × {Inv(AT1) / [Inv(CET1) + Inv(AT1) + Inv(T2) + Inv(Non-Alc NCLAC)]}; and

(i) ***T2 percentage*** (T2百分比) is the percentage calculated as follows—

100% × {[Inv(T2) + Inv(Non-Alc NCLAC)] / [Inv(CET1) + Inv(AT1) + Inv(T2) + Inv(Non-Alc NCLAC)]}.

(4) For the purposes of section 43(1)(o) of these Rules, the applicable amount of a section 3 institution's holdings of insignificant LAC investments that are CET1 capital investments in financial sector entities to be deducted from the institution's CET1 capital must be calculated as follows—

Excess(10% threshold)(net long) × CET1 percentage.

(5) For the purposes of section 47(1)(c) of these Rules, the applicable amount of a section 3 institution's holdings of insignificant LAC investments that are Additional Tier 1 capital investments in financial sector entities to be deducted from the institution's Additional Tier 1 capital must be calculated as follows—

Excess(10% threshold)(net long) × AT1 percentage.

(6) For the purposes of section 48(1)(c) of these Rules, the applicable amount of a section 3 institution's holdings of insignificant LAC investments that are Tier 2 capital investments in, or non-capital LAC liabilities of, financial sector entities to be deducted from the institution's Tier 2 capital must be calculated as follows—

[Excess(10% threshold)(net long) × T2 percentage] + Excess(5% threshold)(gross long).

4. Calculation of insignificant LAC investments holdings

(1) An authorized institution's aggregate holdings of insignificant LAC investments in financial sector entities must be calculated as follows—

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

(b) the underwriting positions held for 5 business days or less (or for any longer period approved by the Monetary Authority) must be excluded;

(c) subject to subsection (3), if the capital instrument of the entity in which the institution has invested does not meet the qualifying criteria for CET1 capital, Additional Tier 1 capital or Tier 2 capital, the institution must treat the capital instrument as a CET1 capital instrument for the purposes of the deduction; and

(d) the institution may, with the prior consent of the Monetary Authority, temporarily exclude certain investments if they have been made in the context of resolving, or providing financial assistance to reorganize, a distressed financial sector entity.

(2) For the purposes of subsection (1)(b), an authorized institution must risk-weight the underwriting positions referred to in that subsection in accordance with one or more of Parts 4, 5, 6 and 8 of these Rules, as the case requires. *(L.N. 167 of 2023)*

(3) An authorized institution may, with the prior consent of the Monetary Authority, map the capital instrument referred to in subsection (1)(c) to Additional Tier 1 capital or Tier 2 capital, as appropriate, whichever is of the closest corresponding quality for the purposes of the deduction.

5. Undeducted insignificant LAC investments to be risk-weighted

(1) The amount of an authorized institution's holdings of insignificant LAC investments in financial sector entities that are covered either by the 10% threshold or by the 5% threshold and that are not deducted from the institution's CET1 capital, Additional Tier 1 capital or Tier 2 capital under section 2 or 3 of this Schedule is to continue to be risk-

weighted in accordance with one or more of Parts 4, 5, 6 and 8 of these Rules, as the case requires. *(L.N. 167 of 2023)*

(2) For determining the investments that are covered by the 10% threshold and are subject to risk-weighting, the amount of holdings of the investments must be allocated on a pro rata basis between those below and those above that threshold.

(Schedule 4F replaced L.N. 222 of 2018)

Schedule 4G

[ss. 2, 43, 47, 48, 70A & 117F]

(L.N. 54 of 2022; L.N. 167 of 2023)

Deduction of Holdings where Authorized Institution has Significant LAC Investments in Financial Sector Entities that are outside Scope of Consolidation under Section 3C Requirement

(L.N. 222 of 2018)

1. Deduction of holdings

(1) For the purposes of section 43(1)(p) of these Rules, an authorized institution must—

(a) calculate the applicable amount of its significant LAC investments in CET1 capital instruments issued by financial sector entities to be deducted from CET1 capital; and

(b) make such deductions from its CET1 capital.

(2) The amount of an authorized institution's significant LAC investments in CET1 capital instruments issued by financial sector entities to be deducted from the institution's CET1 capital is the amount by which the shares concerned in aggregate exceed 10% of the institution's CET1 capital (calculated after applying all regulatory deductions under sections 38(2) and 43(1) of these Rules except those set out in section 43(1)(p) of these Rules).

(3) All significant LAC investments in capital instruments issued by financial sector entities that are not in the form of CET1

capital instruments must be fully deducted from an authorized institution's Additional Tier 1 capital or Tier 2 capital, as the case requires, by reference to the tier of capital for which the capital instruments would qualify if they were issued by the institution itself.

(3A) All significant LAC investments in non-capital LAC liabilities of financial sector entities must be fully deducted from an authorized institution's Tier 2 capital. *(L.N. 222 of 2018)*

(4) An authorized institution's aggregate holdings of significant LAC investments in capital instruments issued by, and non-capital LAC liabilities of, financial sector entities must be calculated as follows— *(L.N. 222 of 2018)*

(a) the direct holdings, indirect holdings and synthetic holdings by the institution of the following must be included—

(i) capital instruments; and

(ii) non-capital LAC liabilities; *(L.N. 222 of 2018)*

(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 for such longer period as the Monetary Authority may approve) must be excluded;

(d) subject to subsection (6), if the capital instrument of the entity in which the institution has invested does not meet the qualifying criteria for CET1 capital, Additional Tier 1 capital or Tier 2 capital, the institution must treat the capital instrument as a CET1 capital instrument for the purposes of the deduction; and

(e) the institution may, with the prior consent of the Monetary Authority, temporarily exclude certain investments where they have been made in the context of resolving, or providing financial assistance to reorganize, a distressed financial sector entity.

(5) For the purposes of subsection (4)(c), an authorized institution must risk-weight underwriting positions referred to in that subsection in accordance with one or more of Parts 4, 5, 6 and 8 of these Rules, as the case requires. *(L.N. 51 of 2013; L.N. 167 of 2023)*

(6) An authorized institution may, with the prior consent of the Monetary Authority, map the capital instrument referred to in subsection (4)(d) to Additional Tier 1 capital or Tier 2 capital, as appropriate, whichever is of the closest corresponding quality for the purposes of the deduction.

(7) The amount of an authorized institution's significant LAC investment in CET1 capital instruments of a financial sector entity that does not exceed the 10% threshold referred to in subsection (2) and that is not deducted from an authorized institution's CET1 capital must be risk-weighted at 250%.

(L.N. 222 of 2018)

(Schedule 4G added L.N. 156 of 2012)

Schedule 4H

(Repealed L.N. 167 of 2023)

Schedule 5

(Repealed L.N. 156 of 2012)

Schedule 6

[ss. 2, 51, 64, 71, 105, 118, 163 & 235]

Credit Conversion Factors

1. The CCF applicable to an off-balance sheet exposure specified in column 2 of the Table is specified in column 3 of the Table opposite the exposure.

Table

Column 1	Column 2	Column 3
Item	Off-balance sheet exposure	CCF
1.	Direct credit substitutes	100%
2.	Asset sales with recourse	100%
3.	Sale and repurchase agreements (excluding those that are repo-style transactions)	100%
4.	Forward asset purchases	100%
5.	Forward forward deposits placed	100%
6.	Partly paid-up shares and securities	100%
7.	Note issuance and revolving underwriting facilities	50%
8.	Transaction-related contingencies	50%
9.	Trade-related contingencies	20%
10.	Exempt commitments	0%

Column 1	Column 2	Column 3
Item	Off-balance sheet exposure	CCF
11.	Commitments that do not fall within any of items 1, 2, 3, 4, 5, 6, 7, 8, 9 and 10 and that— (a) may be cancelled at any time unconditionally by the authorized institution concerned without prior notice; or (b) provide for automatic cancellation due to deterioration in the creditworthiness of the person to whom the institution has made the commitment	10%
12.	Commitments that do not fall within any of items 1, 2, 3, 4, 5, 6, 7, 8, 9, 10 and 11	40%

Column 1	Column 2	Column 3
Item	Off-balance sheet exposure	CCF
13.	Off-balance sheet exposures that do not fall within— (a) for the purposes of the STC approach—any other item in this Schedule and sections 68C and 71(2) and (5); or (b) for the purposes of the BSC approach—any other item in this Schedule and sections 117C and 118(2) and (3)	The CCF specified in Part 2 of Schedule 1 applicable to the exposures or 100% if no such CCF is specified

2. In the Table in section 1 of this Schedule—

commitment (承諾) means any contractual arrangement that has been offered by an authorized institution and accepted by its customer to extend credit, purchase assets or issue credit substitutes, including such an arrangement—

(a) that is in the form of a general banking facility consisting of 2 or more credit lines;

(b) that can be unconditionally cancelled by the institution at any time without prior notice to the customer; or

(c) that can be cancelled by the institution if the customer fails to meet conditions set out in the facility documentation, including conditions that must be met by the customer prior to any initial or subsequent drawdown under the arrangement;

exempt commitment (獲豁免承諾), in relation to an authorized institution, means a commitment that satisfies all of the following conditions—

(a) the person to whom the institution has made the commitment is a corporate (within the meaning of section 51(1) or 105, as the case requires);

(b) the credit quality of the person is closely monitored by the institution on an ongoing basis;

(c) the institution receives no fees or commissions to establish or maintain the commitment;

(d) the person is required to apply to the institution for the initial and each subsequent drawdown;

(e) the institution has full authority, regardless of the fulfilment by the person of the conditions set out in the facility documentation, over the execution of each drawdown;

(f) the institution's decision on the execution of each drawdown is only made after assessing the creditworthiness of the person immediately prior to drawdown.

(Schedule 6 replaced L.N. 167 of 2023)

Schedule 7

[ss. 2, 92, 94, 163, 226BJ, 226K & 226MK]

(L.N. 222 of 2018; L.N. 44 of 2020 and E.R. 3 of 2021; L.N. 167 of 2023)

Standard Supervisory Haircuts

(L.N. 44 of 2020)

1. The standard supervisory haircuts for taking into account the volatilities of the values of exposures (including exposures in the form of unsegregated collateral posted) and collateral are set out in Tables A, B and C.

Table A

Standard Supervisory Haircuts for Debt Securities other than Securitization Issues

Part 1

Debt Securities Issued by Sovereigns or Sovereign Issuers

Column 1	Column 2	Column 3	Column 4
Item	Type of exposure or recognized collateral	Residual maturity of debt security	Standard supervisory haircuts
1.	(a) A debt security— (i) issued by a sovereign or sovereign issuer; and (ii) having an ECAI issue specific rating mapped to a credit quality grade of 1 or 2 in the LT ECAI rating mapping table for Type A ECAIs or a credit quality grade of 1 in the ST ECAI rating mapping table for Type A ECAIs	(a) not more than one year	0.5%
		(b) more than one year but not more than 5 years	2%
		(c) more than 5 years	4%

Column 1	Column 2	Column 3	Column 4
Item	Type of exposure or recognized collateral	Residual maturity of debt security	Standard supervisory haircuts
	(b) A debt security that— (i) does not have an ECAI issue specific rating; and (ii) is issued by a sovereign having an ECAI issuer rating mapped to a credit quality grade of 1 or 2 in the LT ECAI rating mapping table for Type A ECAIs		

Column 1	Column 2	Column 3	Column 4
Item	Type of exposure or recognized collateral	Residual maturity of debt security	Standard supervisory haircuts
2.	(a) A debt security— (i) issued by a sovereign or sovereign issuer; and (ii) having an ECAI issue specific rating mapped to a credit quality grade of 3 or 4 in the LT ECAI rating mapping table for Type A ECAIs or a credit quality grade of 2 or 3 in the ST ECAI rating mapping table for Type A ECAIs	(a) not more than one year	1%
		(b) more than one year but not more than 5 years	3%
		(c) more than 5 years	6%

Column 1	Column 2	Column 3	Column 4
Item	Type of exposure or recognized collateral	Residual maturity of debt security	Standard supervisory haircuts
	(b) A debt security that— (i) does not have an ECAI issue specific rating; and (ii) is issued by a sovereign having an ECAI issuer rating mapped to a credit quality grade of 3 or 4 in the LT ECAI rating mapping table for Type A ECAIs		

Column 1	Column 2	Column 3	Column 4
Item	Type of exposure or recognized collateral	Residual maturity of debt security	Standard supervisory haircuts
3.	(a) A debt security— (i) issued by a sovereign or sovereign issuer; and (ii) having an ECAI issue specific rating mapped to a credit quality grade of 5 in the LT ECAI rating mapping table for Type A ECAIs	all	15%

Column 1	Column 2	Column 3	Column 4
Item	Type of exposure or recognized collateral	Residual maturity of debt security	Standard supervisory haircuts
	(b) A debt security that— (i) does not have an ECAI issue specific rating; and (ii) is issued by a sovereign having an ECAI issuer rating mapped to a credit quality grade of 5 in the LT ECAI rating mapping table for Type A ECAIs		

Part 2

Debt Securities Issued by Issuers other than Sovereigns and Sovereign Issuers

Column 1	Column 2	Column 3	Column 4
Item	Type of exposure or recognized collateral	Residual maturity of debt security	Standard supervisory haircuts
1.	A debt security having an ECAI issue specific rating mapped to one of the following credit quality grades— (a) 1 or 2 in the LT ECAI rating mapping table for Type A ECAIs; (b) 1 in the ST ECAI rating mapping table for Type A ECAIs; (c) 1 or 2 in the LT ECAI rating mapping table or ST ECAI rating mapping table for Type B ECAIs	(a) not more than one year	1%
		(b) more than one year but not more than 3 years	3%
		(c) more than 3 years but not more than 5 years	4%
		(d) more than 5 years but not more than 10 years	6%
		(e) more than 10 years	12%

Column 1	Column 2	Column 3	Column 4
Item	Type of exposure or recognized collateral	Residual maturity of debt security	Standard supervisory haircuts
2.	A debt security having an ECAI issue specific rating mapped to one of the following credit quality grades—	(a) not more than one year	2%
	(a) 3 or 4 in the LT ECAI rating mapping table for Type A ECAIs;	(b) more than one year but not more than 3 years	4%
	(b) 2 or 3 in the ST ECAI rating mapping table for Type A ECAIs;	(c) more than 3 years but not more than 5 years	6%
	(c) 3 or 4 in the LT ECAI rating mapping table or ST ECAI rating mapping table for Type B ECAIs	(d) more than 5 years but not more than 10 years	12%
		(e) more than 10 years	20%

Column 1	Column 2	Column 3	Column 4
Item	Type of exposure or recognized collateral	Residual maturity of debt security	Standard supervisory haircuts
3.	A debt security issued by a bank that— (a) does not have an ECAI issue specific rating; and (b) meets the criteria set out in section 79(1)(l)	(a) not more than one year	2%
		(b) more than one year but not more than 3 years	4%
		(c) more than 3 years but not more than 5 years	6%
		(d) more than 5 years but not more than 10 years	12%
		(e) more than 10 years	20%

Table B

Standard Supervisory Haircuts for Securitization Issues other than Re-securitization Exposures

Column 1	Column 2	Column 3	Column 4
Item	Type of exposure or recognized collateral	Residual maturity of securitization issue	Standard supervisory haircuts
1.	Securitization issue having an ECAI issue specific rating mapped to— (a) a credit quality grade of 1, 2, 3 or 4 in the LT ECAI rating mapping table for securitization exposures; or (b) a credit quality grade of 1 in the ST ECAI rating mapping table for securitization exposures	(a) not more than one year	2%
		(b) more than one year but not more than 5 years	8%
		(c) more than 5 years	16%

Column 1	Column 2	Column 3	Column 4
Item	Type of exposure or recognized collateral	Residual maturity of securitization issue	Standard supervisory haircuts
2.	Securitization issue having an ECAI issue specific rating mapped to— (a) a credit quality grade of 5, 6, 7, 8, 9 or 10 in the LT ECAI rating mapping table for securitization exposures; or (b) a credit quality grade of 2 or 3 in the ST ECAI rating mapping table for securitization exposures	(a) not more than one year	4%
		(b) more than one year but not more than 5 years	12%
		(c) more than 5 years	24%

Table C

Standard Supervisory Haircuts for Exposures and Collateral not Falling within Table A or B in this Section

Column 1 Item	Column 2 Type of exposure or recognized collateral	Column 3 Standard supervisory haircuts
1.	Exposures in the form of cash	0%
2.	Recognized collaterals that fall within section 79(1)(a), (b) or (c)	0%
3.	Exposures arising from currency mismatch	8%
4.	Equities (including convertible bonds) included in main indices	20%
5.	Gold bullion	20%
6.	Equities (including convertible bonds) listed on recognized exchanges that do not fall within item 4	30%

Column 1	Column 2	Column 3
Item	Type of exposure or recognized collateral	Standard supervisory haircuts
7.	Units or shares in collective investment schemes	(a) the highest haircut applicable to any financial instruments in which the scheme can invest; or (b) if the authorized institution concerned is able to use the look-through approach (within the meaning of section 226ZG) to determine the risk-weighted amount of the underlying exposures of the scheme—the weighted average haircut applicable to the financial instruments held by the scheme

Column 1	Column 2	Column 3
Item	Type of exposure or recognized collateral	Standard supervisory haircuts
8.	Exposures arising from financial instruments sold, lent, or posted as collateral under securities financing transactions where the financial instruments do not fall within Table A or B in this section or item 4, 6 or 7	30%
9.	Securities received under repo-style transactions booked in trading book where the securities— (a) do not fall within Table A or B in this section or item 4, 6 or 7; and (b) are eligible for being included in trading book	30%
10.	Exposures not specified in this Table	30%

(L.N. 167 of 2023)

2. In the Tables in section 1— *(L.N. 167 of 2023)*

(a) the haircuts may only be applied to an exposure or collateral—

(i) that is subject to—

(A) daily marking-to-market;

(B) daily revaluation; or

(C) daily marking-to-market and daily remargining; and

(ii) whose applicable minimum holding period or margin period of risk determined under these Rules is 10 business days; *(L.N. 44 of 2020)*

(b) ***sovereign issuer*** (官方實體發行人) means—

(i) a sovereign foreign public sector entity; or

(ii) a multilateral development bank where an exposure to it would be eligible for a risk-weight of 0% under section 58; *(L.N. 167 of 2023)*

(c) *(Repealed L.N. 167 of 2023)*

(ca) *(Repealed L.N. 167 of 2023)*

(d) ***debt securities*** (債務證券) has the meaning assigned to it by section 51(1) of these Rules; *(L.N. 137 of 2011)*

(e) ***recognized collateral*** (認可抵押品)—

(i) unless subparagraph (ii) applies—means recognized collateral within the meaning of section 51(1) or recognized financial collateral within the meaning of section 139(1); or

(ii) in relation to the calculation of default risk exposure by using the SA-CCR approach or IMM(CCR) approach—means collateral referred to in section 226BJ(5) or 226H(3). *(L.N. 44 of 2020; L.N. 167 of 2023)*

(f)-(h) *(Repealed L.N. 167 of 2023)*

3. The standard supervisory haircut must be adjusted by using Formula 33 if any of the following, determined under these Rules, is not 10 business days—

   (a) the minimum holding period or the margin period of risk of the transaction giving rise to the exposure concerned;

   (b) the minimum holding period or the margin period of risk of the transaction giving rise to the exposure secured by the recognized collateral concerned;

   (c) the minimum holding period of the unsegregated collateral concerned.

Formula 33

Adjustment of Standard Supervisory Haircuts

$$H = H_{10} \times \sqrt{\frac{P}{10}}$$

where—

H = haircut applicable to an exposure or recognized collateral, as the case requires, capped at 100%;

H_{10} = standard supervisory haircut appropriate for the type of exposure or recognized collateral to which the exposure or recognized collateral belongs; and

P = the following, as the case requires, determined in accordance with these Rules—

(i) the minimum holding period or the margin period of risk of the transaction giving rise to the exposure or of the transaction giving rise to the exposure secured by the recognized collateral; or

(ii) the minimum holding period of the unsegregated collateral.

(L.N. 44 of 2020)

Schedule 8

(Repealed L.N. 167 of 2023)

Schedule 9

[s. 229 & Sch. 10A]
(L.N. 175 of 2017)

Requirements to be Satisfied for Traditional Securitization Transaction to be Eligible Traditional Securitization Transaction

(L.N. 175 of 2017)

The requirements specified for the purposes of section 229(1)(a)(i) in respect of an originating institution of a traditional securitization transaction are— *(L.N. 175 of 2017)*

(a) significant credit risk associated with the underlying exposures in the transaction has been transferred from the institution to third parties;

(b) the institution does not maintain effective control, directly or indirectly, over the underlying exposures in the transaction;

(c) the underlying exposures in the transaction have been validly transferred and none of the institution or the institution's creditors, or any liquidator or receiver or like officer appointed in respect of the institution, is able, or will be able, to avoid, set aside or successfully contest the transfer;

(d) the institution has obtained an opinion in writing from qualified legal counsel (whether in-house or external) confirming that, in all relevant jurisdictions, the transaction falls within paragraph (c); *(L.N. 175 of 2017)*

(e) the institution has obtained an adjudication from relevant tax authorities, or a tax opinion has been obtained from an accountant or tax adviser, or a person who holds such qualification as the Monetary Authority may accept as being of a standard comparable to that of an accountant or tax adviser, on whether any direct or indirect tax obligations arise as a result of any transfer of interests in underlying exposures and related collateral under the transaction;

(f) the documentation for the transaction accurately reflects the economic substance of the transaction;

(g) the documentation for the transaction does not contain any clause that—

(i) directly or indirectly makes any representation or provides any warranty as to the future credit performance of the underlying exposures;

(ii) obliges the institution to repurchase any of the underlying exposures, at any time, except where—

(A) the obligation arises from a claim arising from a representation or warranty given by the institution to another person in the documentation solely in respect of the status of any underlying exposure at the time of the transfer and that is capable of being verified at that time; or

(B) the obligation is accepted by and imposed on the institution for legitimate and sound commercial reasons and does not expose the institution to excessive credit risk; *(L.N. 137 of 2011)*

(iii) requires the institution to alter the pool of underlying exposures such that the pool's credit quality is improved unless this is achieved through the purchase of underlying exposures by independent and unaffiliated third parties at market prices;

(iv) allows for increases in a first loss tranche retained, or credit enhancement provided, by the institution after the commencement of the transaction; or

(v) increases the return to parties other than the institution, such as investors in securitization issues and third party providers of credit enhancements to the transaction, in response to a deterioration in the credit quality of the pool of underlying exposures;

(h) the securitization issues under the transaction do not represent payment obligations of the institution such that investors who purchase the securitization issues only have recourse for payment to the pool of underlying exposures;

(i) the securitization issues under the transaction are issued by an SPE and the holders of the securitization issues have the right to pledge or transfer them without restriction;

(j) if the transaction includes a clean-up call—all the requirements set out in section 1 of Schedule 10A are met in respect of the clean-up call; *(L.N. 175 of 2017)*

(k) if the transaction is subject to an early amortization provision—any one or more of the requirements set out in section 2 of Schedule 10A are met in respect of the early amortization provision; and *(L.N. 175 of 2017)*

(l) the securitization transaction does not include a termination option or trigger except—

(i) a clean-up call in respect of which all the requirements set out in section 1 of Schedule 10A are met;

(ii) any termination provision for specific changes in tax or regulation; and

(iii) an early amortization provision in respect of which any one or more of the requirements set out in section 2 of Schedule 10A are met. *(L.N. 175 of 2017)*

(m) *(Repealed L.N. 175 of 2017)*

Schedule 10

[ss. 229 & 230 & Sch. 10A]

(L.N. 175 of 2017; L.N. 44 of 2020)

Requirements to be Satisfied for Synthetic Securitization Transaction to be Eligible Synthetic Securitization Transaction

(L.N. 175 of 2017)

1. Requirements

The requirements specified for the purposes of section 229(1)(b)(i) in respect of an originating institution of a synthetic securitization transaction are— *(L.N. 175 of 2017)*

(a) subject to section 2 of this Schedule, significant credit risk associated with the underlying exposures of the transaction has been transferred from the institution to third parties through relevant credit protection that is recognized collateral, a recognized guarantee or a recognized credit derivative contract under Part 4 (regardless of whether the institution uses the STC approach to calculate the credit risk of the underlying exposures if they were not securitized); *(L.N. 175 of 2017)*

(b)-(c) *(Repealed L.N. 175 of 2017)*

(d) the institution has obtained an opinion in writing from qualified legal counsel (whether in-house or external) confirming that, in all relevant jurisdictions, the documentation for the transaction— *(L.N. 175 of 2017)*

(i) enables the institution to have valid, legally binding and enforceable rights over any collateral taken in respect of the transaction; and

(ii) constitutes valid, legally binding and enforceable obligations of any credit protection provider in respect of the transaction;

(e) the documentation for the transaction accurately reflects the economic substance of the transaction;

(f) the documentation for the transaction does not contain any clause that—

(i) materially limits the credit protection if a credit event occurs or the credit quality of the pool of underlying exposures deteriorates;

(ii) requires the institution to alter the pool of underlying exposures such that the pool's credit quality is improved unless this is achieved through the purchase of underlying exposures by independent and unaffiliated third parties at market prices;

(iii) allows for increases in a first loss tranche retained, or credit enhancement provided, by the institution after the commencement of the transaction;

(iv) allows for increases in the cost of credit protection to the institution in response to a deterioration in the credit quality of the pool of underlying exposures; or

(v) increases the return to parties other than the institution, such as investors in securitization issues and third party providers of credit enhancements to the transaction, in response to a deterioration in the credit quality of the pool of underlying exposures;

(g) if the transaction includes a clean-up call—all the requirements set out in section 1 of Schedule 10A are met in respect of the clean-up call; and *(L.N. 175 of 2017)*

(h) if the transaction is subject to an early amortization provision—any one or more of the requirements set out in section 2 of Schedule 10A are met in respect of the early amortization provision. *(L.N. 175 of 2017)*

(i)-(j) *(Repealed L.N. 175 of 2017)*

2. Provisions supplementary to section 1(a)

For the purposes of section 1(a) of this Schedule—

(a) the SPE in the securitization transaction concerned may be recognized as a credit protection provider for the purposes of section 98 or 99 if—

(i) the SPE owns assets that fall within one or more than one category of asset specified in sections 79(1) (excluding section 79(1)(o)) and 80(1)(b) and (c) and none of the SPE's assets is a securitization exposure; *(L.N. 167 of 2023)*

(ii) relevant legal documentation provides that the SPE's assets can be applied to pay any amounts that the SPE may become obliged to pay from time to time to the originating institution pursuant to the credit protection concerned;

(iii) there are no claims or contingent claims (other than those for administrative fees, operating expenses and other similar payments) that rank senior to, or equally with, the rights of the originating institution receiving payments pursuant to the credit protection; and

(iv) the arrangements through which the security interests in the SPE’s assets are granted for the benefit of the originating institution and the control procedures in place, if they were carried out by an authorized institution, would meet the criteria specified in section 77(2); and *(L.N. 44 of 2020; L.N. 167 of 2023)*

(b) if the underlying exposures concerned consist of securitization exposures, the reference to “an entity not listed in subparagraphs (i) to (vii) that has an ECAI issuer rating” in section 99A(2)(a)(viii) is taken to be a reference to an entity specified in section 243(3). *(L.N. 167 of 2023)*

(L.N. 175 of 2017)

Schedule 10A

[Schs. 9 & 10]

Requirements Supplementary to Schedules 9 and 10

1. Requirements in respect of clean-up calls

The requirements set out in respect of a clean-up call for the purposes of paragraph (j) of Schedule 9 and section 1(g) of Schedule 10 are the following—

(a) the exercise of the clean-up call is entirely at the discretion of the originating institution concerned except where the clean-up call is exercised under circumstances beyond the control of any party to the securitization transaction concerned;

(b) the clean-up call is not structured—

(i) to reduce or avoid potential or actual losses to investors or other parties to the transaction; or

(ii) to provide credit enhancement to those investors and parties; and

(c) the clean-up call is exercisable only when 10% or less of the principal amount of the securitization issues or underlying exposures at the commencement of the transaction remains outstanding.

2. Requirements in respect of early amortization provision

The requirements set out in respect of an early amortization provision for the purposes of paragraph (k) of Schedule 9 and section 1(h) of Schedule 10 are the following—

(a) the securitization transaction subject to the provision includes a replenishment structure under which—

(i) underlying exposures that are revolving in nature (***revolving underlying exposures***) are to be replenished by exposures that are non-revolving in nature; and

(ii) the early amortization ends the ability of the originating institution of the transaction to add new underlying exposures; *(L.N. 222 of 2018)*

(b) the provision—

(i) has features that are akin to a structure that is non-revolving in nature in that the credit risk in respect of the revolving underlying exposures does not return to the originating institution of the transaction; and

(ii) does not result in subordination of the institution's interest;

(c) investors in the securitization issues concerned remain fully exposed to future drawdowns by the borrowers in respect of the revolving underlying exposures even if the provision has been triggered; and *(L.N. 222 of 2018)*

(d) the provision is solely triggered by events not related to the performance of the underlying exposures of the securitization transaction or of the originating institution of the transaction.

(Schedule 10A added L.N. 175 of 2017)

Schedule 11

(Repealed L.N. 167 of 2023)

Schedule 12

(Repealed L.N. 175 of 2017)

Schedule 13

(Repealed L.N. 175 of 2017)

Schedule 14

(Repealed L.N. 175 of 2017)

Schedule 15

(Repealed L.N. 167 of 2023)

Schedule 16

[ss. 226V, 226X & 226Y]

Transitional Provisions for Banking (Capital) (Amendment) Rules 2020

1. CCP not using SA-CCR approach regarded as qualifying CCP in certain circumstances

(1) Subject to subsections (2) and (3), a CCP in a jurisdiction outside Hong Kong may be regarded as a qualifying CCP for the purposes of these Rules despite the fact that the CCP does not meet the description in paragraph (a)(iii) and (iv) of the definition of ***qualifying CCP*** in section 226V(1) of these Rules in that the CCP's exposure amount to its clearing members is calculated not by using the applicable SA-CCR method.

(2) Subsection (1) applies only if—

(a) except as mentioned in subsection (1), the CCP otherwise meets the description in the definition of ***qualifying CCP*** in section 226V(1) of these Rules;

(b) the CCP is a CCP in a jurisdiction in which the jurisdiction's SA-CCR rule is published on or before 30 June 2021; and

(c) the earliest date by which any bank subject to the jurisdiction's SA-CCR rule must begin to use the applicable SA-CCR method to calculate the exposure amount of counterparty credit risk (***mandatory compliance date***) does not fall on a date before 1 July 2021. *(L.N. 167 of 2023)*

(3) Subsection (1) ceases to apply to a CCP in a jurisdiction on the mandatory compliance date for the jurisdiction's SA-CCR rule.

(4) In this section—

(a) a CCP is a CCP in a jurisdiction if—

(i) the CCP's place of incorporation or equivalent location (in the case of a non-corporate entity) is the jurisdiction; or

(ii) where a branch of the CCP is involved—the branch is located in the jurisdiction;

(b) a law, regulation or directive (however described) of a jurisdiction to implement a calculation method for measuring counterparty credit risk exposures of banks based on the standardized approach to counterparty credit risk, set out in the Basel CCR Rules (within the meaning given in section 226V(1)) (***Basel SA-CCR approach***), is the jurisdiction's SA-CCR rule; *(L.N. 167 of 2023)*

(c) the Basel SA-CCR approach, or that approach as modified under a jurisdiction's SA-CCR rule, is the applicable SA-CCR method.

(5) For the purposes of subsection (2)(b), a jurisdiction's SA-CCR rule is regarded as having been published in the jurisdiction on the completion of the procedure required by the law of the jurisdiction for bringing into force the rule, regardless of whether the mandatory compliance date is specified.

2. Exposures of clearing members to CCP regarded as qualifying CCP

(1) If a CCP is regarded as a qualifying CCP under section 1, an authorized institution that is a clearing member of the CCP must calculate the regulatory capital for the default fund

contribution made by the institution to the CCP in accordance with sections 226X(4) and (6) and 226Y of the pre-amended Rules (instead of sections 226X(4), (5), (6) and (7) and 226Y of these Rules).

(2) In this section—

pre-amended Rules (原有規則) means these Rules as in force immediately before 30 June 2021.

(Schedule 16 added L.N. 44 of 2020)