

L.N. 54 of 2022

**Banking (Capital) (Amendment) Rules 2022****Contents**

Section	Page
1. Commencement .....	B635
2. Banking (Capital) Rules amended .....	B635
3. Section 2 amended (interpretation).....	B635
4. Section 52 amended (calculation of risk-weighted amount of exposures).....	B643
5. Part 4, Division 3 heading amended (determination of risk-weights applicable to on-balance sheet exposures).....	B645
6. Part 4, Division 3, Subdivision 1 heading and section 54A added.....	B645
<b>Subdivision 1—Exposures other than CIS Exposures</b>	
54A. Application of Subdivision 1 .....	B647
7. Section 62 repealed (collective investment scheme exposures) .....	B647
8. Section 66 amended (other exposures which are not past due exposures) .....	B647
9. Section 67 amended (past due exposures).....	B647
10. Section 68 amended (credit-linked notes) .....	B649
11. Section 69 amended (application of ECAI ratings).....	B649

Section	Page
12.	Section 70 amended (authorized institutions required to nominate ECAIs to be used).....B651
13.	Part 4, Division 3, Subdivisions 2 and 3 added .....B651
<b>Subdivision 2—CIS Exposures</b>	
70AA.	Interpretation of Subdivision 2.....B651
70AAB.	Treatment of CIS exposure held by authorized institution.....B653
70AAC.	Treatment of CIS exposure constituting deductible holding.....B655
<b>Subdivision 3—Treatment of Certain Types of Off-balance Sheet Exposures</b>	
70AAD.	Determination of risk-weights applicable to certain types of off-balance sheet exposures .....B657
14.	Section 74 repealed (determination of risk-weights applicable to off-balance sheet exposures) .....B663
15.	Section 82 amended (determination of risk-weight to be allocated to recognized collateral under simple approach) .....B663
16.	Section 94 amended (on-balance sheet netting) .....B665
17.	Section 106 amended (calculation of risk-weighted amount of exposures).....B665
18.	Section 108 amended (classification of exposures) .....B667
19.	Part 5, Division 3 heading amended (determination of risk-weights applicable to on-balance sheet exposures).....B667

Section	Page
20.	Part 5, Division 3, Subdivision 1 heading and section 108A added.....B667
	<b>Subdivision 1—Exposures other than CIS Exposures</b>
	108A. Application of Subdivision 1 .....B669
21.	Section 116 amended (other exposures).....B669
22.	Section 117 amended (credit-linked notes).....B669
23.	Part 5, Division 3, Subdivisions 2 and 3 added .....B669
	<b>Subdivision 2—CIS Exposures</b>
	117AB. Interpretation of Subdivision 2.....B669
	117AC. Treatment of CIS exposure held by authorized institution.....B671
	117AD. Treatment of CIS exposure constituting deductible holding.....B673
	<b>Subdivision 3—Treatment of Certain Types of Off-balance Sheet Exposures</b>
	117AE. Determination of risk-weights applicable to certain types of off-balance sheet exposures .....B675
24.	Section 121 repealed (determination of risk-weights applicable to off-balance sheet exposures) .....B681
25.	Section 130 amended (on-balance sheet netting) .....B681
26.	Section 139 amended (interpretation of Part 6).....B683
27.	Section 140 amended (calculation of risk-weighted amount of exposures).....B683

Section	Page
28. Section 142 amended (classification of exposures) .....	B685
29. Section 145 amended (equity exposures) .....	B685
30. Section 147 amended (IRB calculation approaches).....	B687
31. Section 183 amended (equity exposures—general) .....	B687
32. Section 184 amended (market-based approach).....	B689
33. Section 202 amended (securities financing transactions) .....	B689
34. Section 222 amended (equity exposures—market-based approach).....	B689
35. Section 223 heading amended (equity exposures—PD/ LGD approach) .....	B691
36. Section 226BW amended (calculation of add-on for subsets in asset class of credit-related derivative contracts).....	B691
37. Section 226BZA amended (calculation of effective notional amount for hedging sets etc.).....	B693
38. Section 226MD amended (calculation of potential future exposure of derivative contract).....	B693
39. Section 226S amended (standardized CVA method).....	B695
40. Part 6B added .....	B697

### **Part 6B**

#### **Calculation of Risk-weighted Amounts of CIS Exposures**

##### **Division 1—Preliminary**

226ZF. Application of Part 6B.....	B699
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Section	Page
226ZG.	Interpretation of Part 6B .....B699
226ZH.	Interpretation: levels of collective investment scheme etc. ....B703
<b>Division 2—Calculation of Risk-weighted Amounts of CIS Exposures to Collective Investment Schemes</b>	
226ZI.	Calculation of risk-weighted amount of CIS exposure .....B707
226ZJ.	Calculation of effective risk-weight applicable to CIS exposure for purposes of section 226ZI.....B711
<b>Division 3—Determination of Approaches to be Used</b>	
226ZK.	Approaches to be used in calculating risk- weighted amounts of CIS exposures etc. ....B715
226ZL.	Approaches to be used in calculating risk- weighted amounts of CIS exposures to Level 1 CIS: BSC AI .....B719
226ZM.	LTA conditions .....B719
226ZN.	TPA conditions .....B721
<b>Division 4—Determination of Risk-weight under Different Approaches</b>	
226ZO.	Look-through approach: calculation of risk- weighted amount of underlying exposures.....B727
226ZP.	Use of risk-weighted amount obtained by using third-party approach.....B735

Section	Page
226ZQ.	Mandate-based approach: general requirements .....B735
226ZR.	Mandate-based approach: calculation of risk-weighted amounts of underlying exposures .....B743
226ZS.	Fall-back approach .....B749
<b>Division 5—Regulatory Deductible Items Held by Level 1 CIS</b>	
226ZT.	Certain regulatory deductible items held by Level 1 CIS may be excluded from underlying exposures.....B751
<b>Division 6—CIS Exposures Held by Collective Investment Schemes</b>	
226ZU.	Calculation of risk-weighted amounts of CIS exposures held by Level 1 CIS .....B753
226ZV.	Calculation of risk-weighted amounts of CIS exposures held by Level 2 CIS onwards.....B755
226ZW.	Calculation of risk-weighted amounts of CIS exposures held by Level 2 CIS onwards: conditions for using look-through approach.....B757
226ZX.	Calculation of risk-weighted amounts of CIS exposures held by Level 1 CIS onwards: certain regulatory deductible items may be excluded .....B759
41.	Schedule 1 amended (specifications for purposes of certain definitions in these Rules) .....B761

Section	Page
42. Schedule 4F amended (deduction of holdings where authorized institution has insignificant LAC investments in financial sector entities that are outside scope of consolidation under section 3C requirement) .....	B761
43. Schedule 4G amended (deduction of holdings where authorized institution has significant LAC investments in financial sector entities that are outside scope of consolidation under section 3C requirement) .....	B763
44. Schedule 6 amended (credit quality grades).....	B763

## **Banking (Capital) (Amendment) Rules 2022**

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

### **1. Commencement**

These Rules come into operation on 1 July 2022.

### **2. Banking (Capital) Rules amended**

The Banking (Capital) Rules (Cap. 155 sub. leg. L) are amended as set out in sections 3 to 44.

### **3. Section 2 amended (interpretation)**

- (1) Section 2(1), definition of *ECAI issue specific rating*, paragraphs (a) and (d)—

#### **Repeal**

“, (e)”.

- (2) Section 2(1), definition of *ECAI issue specific rating*—

#### **Repeal paragraph (e).**

- (3) Section 2(1), definition of *external credit assessment institution*, paragraph (f)—

#### **Repeal**

“Credit Analysis and Research Limited”

#### **Substitute**

“CARE Ratings Limited”.



- (4) Section 2(1), definition of *external credit assessment institution*, paragraph (g)—

**Repeal**

“CRISIL Limited”

**Substitute**

“CRISIL Ratings Limited”.

- (5) Section 2(1), definition of *underlying exposures*, paragraph (a)—

**Repeal**

“or”.

- (6) Section 2(1), definition of *underlying exposures*, after paragraph (a)—

**Add**

“(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”.
- (7) Section 2(1), definition of *underlying exposures*, paragraph (b)—

**Repeal**

“paragraph (a)”

**Substitute**

“paragraphs (a) and (ab)”.

- (8) Section 2(1)—
- (a) definition of *Credit Analysis and Research Limited*;
  - (b) definition of *CRISIL Limited*—

**Repeal the definitions.**

- (9) Section 2(1)—

**Add in alphabetical order**

“*CARE Ratings Limited* means the company incorporated in India under that name;

*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;

***CRISIL Ratings Limited*** means the company incorporated in India under that name;

***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;

***regulatory deductible item*** (監管可扣減項目) means a Type A deductible item or a Type B deductible item;

***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;

***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;”.

**4. Section 52 amended (calculation of risk-weighted amount of exposures)**

- (1) Section 52(2)—

**Repeal paragraph (a)**

**Substitute**

- “(a) subject to paragraph (b), an authorized institution must calculate the risk-weighted amount of each of the institution’s on-balance sheet exposures—
- (i) if the exposure is not a CIS exposure—by multiplying the principal amount of the exposure, net of specific provisions, by the relevant risk-weight attributable to the exposure determined under Subdivision 1 of Division 3; or
  - (ii) if the exposure is a CIS exposure—in accordance with Subdivision 2 of Division 3;”.

- (2) Section 52(3)—

**Repeal paragraph (ab)**

**Substitute**

“(ab) subject to paragraph (b), in the case of an authorized institution’s off-balance sheet exposures that do not fall within paragraph (a), the institution must calculate the risk-weighted amount of each of the exposures—

(i) if the exposure is not a CIS exposure—by multiplying the credit equivalent amount of the exposure by the relevant risk-weight attributable to the exposure determined under Subdivision 1 of Division 3; or

(ii) if the exposure is a CIS exposure—in accordance with Subdivision 2 of Division 3;”.

(3) Section 52(4), definition of *ECAI issue specific rating*, paragraph (a), after “ECAI;”—

**Add**

“or”.

(4) Section 52(4), definition of *ECAI issue specific rating*—

**Repeal paragraph (b).**

**5. Part 4, Division 3 heading amended (determination of risk-weights applicable to on-balance sheet exposures)**

Part 4, Division 3, heading, after “On-balance Sheet Exposures”—

**Add**

“and Off-balance Sheet Exposures”.

**6. Part 4, Division 3, Subdivision 1 heading and section 54A added**

Before section 55—

**Add**

**“Subdivision 1—Exposures other than CIS Exposures****54A. Application of Subdivision 1**

This Subdivision applies to the determination of risk-weights applicable to an authorized institution’s on-balance sheet exposures, and off-balance sheet exposures, that are not CIS exposures.”.

**7. Section 62 repealed (collective investment scheme exposures)**

Section 62—

**Repeal the section.**

**8. Section 66 amended (other exposures which are not past due exposures)**

(1) Section 66(1)(b)(i)—

**Repeal**

“62 or”.

(2) Section 66(1)(b)—

**Repeal subparagraph (ii)**

**Substitute**

“(ii) any other exposures of the institution that do not fall within any of sections 55, 56, 57, 58, 59, 60, 61, 63, 63A, 64, 65 and 67 (including accrued interest if subsection (5) is applicable).”.

**9. Section 67 amended (past due exposures)**

Section 67(1)—

**Repeal**

“62,”.

**10. Section 68 amended (credit-linked notes)**

- (1) Section 68(d)(i)—

**Repeal**

“62,”.

- (2) Section 68(e)—

**Repeal**

“74(3)(b), (4)(b), (5) or (6)”

**Substitute**

“70AAD(6), (7), (8) or (9)”.

**11. Section 69 amended (application of ECAI ratings)**

- (1) Section 69—

**Repeal subsection (1)****Substitute**

“(1) An authorized institution must, in complying with a requirement under section 55, 57, 59, 60 or 61 in relation to an exposure (*concerned exposure A*) of the institution consisting of a debt obligation issued or undertaken by a person where the debt obligation has one or more than one ECAI issue specific rating assigned to it, determine the rating to be used in accordance with subsection (2).”.

- (2) Section 69(11), definition of *ECAI issue specific rating*, paragraph (a), after “ECAI;”—

**Add**

“or”.

- (3) Section 69(11), definition of *ECAI issue specific rating*—

**Repeal paragraph (b).**

**12. Section 70 amended (authorized institutions required to nominate ECAIs to be used)**

(1) Section 70(7)—

**Repeal**

“, debt obligation, or collective investment scheme,”

**Substitute**

“or debt obligation”.

(2) Section 70(8), definition of *ECAI ratings based portfolio*, paragraph (d), after “exposures;”—

**Add**

“or”.

(3) Section 70(8), definition of *ECAI ratings based portfolio*, paragraph (e)—

**Repeal**

“; or”

**Substitute a full stop.**

(4) Section 70(8), definition of *ECAI ratings based portfolio*—

**Repeal paragraph (f).**

**13. Part 4, Division 3, Subdivisions 2 and 3 added**

Part 4, Division 3, after Subdivision 1—

**Add**

**“Subdivision 2—CIS Exposures**

**70AA. Interpretation of Subdivision 2**

In this Subdivision—



***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.

**70AAB. 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 1 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 70AAC 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.

**70AAC. 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 of deductible holding 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 of 100% to any amount of deductible holding determined under subsection (2)(b) if the deductible holding is—
    - (i) an insignificant LAC investment; or
    - (ii) a holding of non-capital LAC liabilities falling within section 48A; and

- (b) 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.
- (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  $\geq 2$ ) to which the Level 1 CIS has an indirect CIS exposure.

### **Subdivision 3—Treatment of Certain Types of Off-balance Sheet Exposures**

#### **70AAD. Determination of risk-weights 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 or a forward asset purchase, the risk-weight applicable to the subject exposure is the risk-weight applicable to the assets sold or to be purchased.
- (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 institution's banking book, subject to subsections

(6), (7), (8) and (9), 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 residential mortgage loan, the risk-weight determined in accordance with section 65(1) may be applicable to the exposure if the institution has no reason to believe that any of the provisions of that section will not be satisfied immediately after the loan that is the subject of that commitment is drawn down.
- (6) If the subject exposure mentioned in subsection (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%.
- (7) If the subject exposure mentioned in subsection (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%.
- (8) If the subject exposure mentioned in subsection (3) arises from any other subsequent-to-default credit derivative contract, subsection (7), 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 (7)(a) is construed to mean—
  - (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 subsequent-to-default credit derivative contracts.
- (9) If the subject exposure mentioned in subsection (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 by using Formula 1B.

**Formula 1B****Calculation of Risk-weight of Off-balance Sheet Exposure Arising from Credit Derivative Contract under Section 70AAD(9)**

$$RW_a = \sum_i (a_i \cdot RW_i)$$

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  $i$ .”.

**14. Section 74 repealed (determination of risk-weights applicable to off-balance sheet exposures)**

Section 74—

**Repeal the section.**

**15. Section 82 amended (determination of risk-weight to be allocated to recognized collateral under simple approach)**

Section 82(1)(a)(i)—

**Repeal**

“sections 55, 56, 57, 58, 59, 60, 61, 62, 63, 66 and 68”

**Substitute**

“section 55, 56, 57, 58, 59, 60, 61, 63, 66, 68 or 226ZJ, as the case requires,”.

**16. Section 94 amended (on-balance sheet netting)**

Section 94(1), after “on-balance sheet exposures”—

**Add**

“(other than CIS exposures)”.

**17. Section 106 amended (calculation of risk-weighted amount of exposures)**

(1) Section 106(2)—

**Repeal paragraph (a)**

**Substitute**

“(a) subject to paragraph (b), an authorized institution must calculate the risk-weighted amount of each of the institution’s on-balance sheet exposures—

(i) if the exposure is not a CIS exposure—by multiplying the principal amount of the exposure, net of specific provisions, by the relevant risk-weight attributable to the exposure determined under Subdivision 1 of Division 3; or

(ii) if the exposure is a CIS exposure—in accordance with Subdivision 2 of Division 3;”.

(2) Section 106(3)—

**Repeal paragraph (ab)**

**Substitute**

- “(ab) subject to paragraph (b), in the case of an authorized institution’s off-balance sheet exposures that do not fall within paragraph (a), the institution must calculate the risk-weighted amount of each of the exposures—
- (i) if the exposure is not a CIS exposure—by multiplying the credit equivalent amount of the exposure by the relevant risk-weight attributable to the exposure determined under Subdivision 1 of Division 3; or
  - (ii) if the exposure is a CIS exposure—in accordance with Subdivision 2 of Division 3;”.

**18. Section 108 amended (classification of exposures)**

After section 108(f)—

**Add**

“(fa) CIS exposures;”.

**19. Part 5, Division 3 heading amended (determination of risk-weights applicable to on-balance sheet exposures)**

Part 5, Division 3, heading, after “**On-balance Sheet Exposures**”—

**Add**

“**and Off-balance Sheet Exposures**”.

**20. Part 5, Division 3, Subdivision 1 heading and section 108A added**

Before section 109—

**Add**



**“Subdivision 1—Exposures other than CIS Exposures****108A. Application of Subdivision 1**

This Subdivision applies to the determination of risk-weights applicable to an authorized institution’s on-balance sheet exposures, and off-balance sheet exposures, that are not CIS exposures.”.

**21. Section 116 amended (other exposures)**

Section 116(1)(b)(ii)—

**Repeal**

“on-balance sheet”.

**22. Section 117 amended (credit-linked notes)**

Section 117(a)(ii)—

**Repeal**

“121(3), (4), (5) or (6)”

**Substitute**

“117AE(6), (7), (8) or (9)”.

**23. Part 5, Division 3, Subdivisions 2 and 3 added**

Part 5, Division 3, after Subdivision 1—

**Add****“Subdivision 2—CIS Exposures****117AB. Interpretation of Subdivision 2**

In this Subdivision—

***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.

**117AC. 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 1 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 117AD 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.

**117AD. 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 of deductible holding 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 of 100% to any amount of deductible holding determined under subsection (2)(b) if the deductible holding is—
    - (i) an insignificant LAC investment; or
    - (ii) a holding of non-capital LAC liabilities falling within section 48A; and

- (b) 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.
- (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  $\geq 2$ ) to which the Level 1 CIS has an indirect CIS exposure.

### **Subdivision 3—Treatment of Certain Types of Off-balance Sheet Exposures**

#### **117AE. Determination of risk-weights 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 or a forward asset purchase, the risk-weight applicable to the subject exposure is the risk-weight applicable to the assets sold or to be purchased.
- (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 institution's banking book, subject to subsections

(6), (7), (8) and (9), 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 residential mortgage loan, the risk-weight determined in accordance with section 115(1) may be applicable to the exposure if the institution has no reason to believe that any of the provisions of that section will not be satisfied immediately after the loan that is the subject of that commitment is drawn down.
- (6) If the subject exposure mentioned in subsection (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%.
- (7) If the subject exposure mentioned in subsection (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%.
- (8) If the subject exposure mentioned in subsection (3) arises from any other subsequent-to-default credit derivative contract, subsection (7), 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 (7)(a) is construed to mean—
  - (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 subsequent-to-default credit derivative contracts.
- (9) If the subject exposure mentioned in subsection (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 by using Formula 12A.

**Formula 12A****Calculation of Risk-weight of Off-balance Sheet Exposure Arising from Credit Derivative Contract under Section 117AE(9)**

$$RW_a = \sum_i (a_i \cdot RW_i)$$

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  $i$ .”.

**24. Section 121 repealed (determination of risk-weights applicable to off-balance sheet exposures)**

Section 121—

**Repeal the section.**

**25. Section 130 amended (on-balance sheet netting)**

Section 130(1), after “on-balance sheet exposures”—

**Add**

“(other than CIS exposures)”.

**26. Section 139 amended (interpretation of Part 6)**

Section 139(1)—

**Add in alphabetical order**

“**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;

**fall-back approach** (備選方法) has the meaning given by section 226ZG;

**look-through approach** (透視計算法) has the meaning given by section 226ZG;

**mandate-based approach** (授權基準計算法) has the meaning given by section 226ZG;

**third-party approach** (第三方計算法) has the meaning given by section 226ZG;”.

**27. Section 140 amended (calculation of risk-weighted amount of exposures)**

- (1) Section 140(1), after “(1B)”—

**Add**

“, (1BA)”.

- (2) Section 140(1A), after “(1B)”—

**Add**

“, (1BA)”.



- (3) After section 140(1B)—

**Add**

“(1BA) For an equity exposure that is 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.”.

**28. Section 142 amended (classification of exposures)**

- (1) Section 142(1)(b)—

**Repeal**

“26”

**Substitute**

“27”.

- (2) Section 142(1), Table 16, item 5, column 3, after paragraph (f)—

**Add**

“(g) Equity exposures (CIS exposures)”.

**29. Section 145 amended (equity exposures)**

- (1) Section 145(1)(b)—

**Repeal subparagraph (iii)**

**Substitute**

“(iii) holdings of any CIS exposures;”.

- (2) Section 145(1)(b)(vii), after “scheme”—

**Add**

“(other than a collective investment scheme)”.

- (3) Section 145(1)(c), after “equity holding”—

**Add**

“(other than equity holding in a collective investment scheme)”.

**30. Section 147 amended (IRB calculation approaches)**

Section 147(1), Table 17, item 5, column 3, after paragraph (c)—

**Add**

“(d) CIS calculation approach”.

**31. Section 183 amended (equity exposures—general)**

(1) Section 183(1), after “subsections”—

**Add**

“(1A),”.

(2) Section 183(1)(a)—

**Repeal**

“or”.

(3) Section 183(1)(b)—

**Repeal**

“approach.”

**Substitute**

“approach; or”.

(4) After section 183(1)(b)—

**Add**

“(c) the CIS calculation approach.”.

(5) After section 183(1)—

**Add**

“(1A) An authorized institution must use the CIS calculation approach to calculate the risk-weighted amount of a CIS exposure that does not constitute a deductible holding in accordance with Part 6B.”.

(6) Section 183—

**Repeal subsection (4).**

**32. Section 184 amended (market-based approach)**

Section 184(1), after “and (3)”—

**Add**

“and Part 6B”.

**33. Section 202 amended (securities financing transactions)**

(1) Section 202(4)(b)—

**Repeal**

“or”.

(2) Section 202(4)(c)—

**Repeal**

“exposures,”

**Substitute**

“exposures (other than CIS exposures); or”.

(3) After section 202(4)(c)—

**Add**

“(d) Part 6B for CIS exposures that do not constitute a deductible holding.”.

**34. Section 222 amended (equity exposures—market-based approach)**

(1) Section 222, heading—

**Repeal**

**“Equity exposures—market-based approach”**

**Substitute**

**“EL amount—equity exposures subject to market-based approach and CIS exposures”.**

(2) Section 222—

**Renumber the section as section 222(1).**

(3) After section 222(1)—

**Add**

“(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.”.

**35. Section 223 heading amended (equity exposures—PD/LGD approach)**

Section 223, heading—

**Repeal**

**“Equity exposures—”**

**Substitute**

**“EL amount—equity exposures subject to”.**

**36. Section 226BW amended (calculation of add-on for subsets in asset class of credit-related derivative contracts)**

(1) Section 226BW(2)(b), Table 23AC, column 1—

**Repeal**

**“, Ir BB-”.**

(2) Section 226BW(2)(b), Table 23AC, column 1—

**Repeal**

“, [ICRA] BB- or Ir BB-”

**Substitute**

“or [ICRA] BB-”.

**37. Section 226BZA amended (calculation of effective notional amount for hedging sets etc.)**

Section 226BZA—

**Repeal subsection (5)**

**Substitute**

“(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.”.

**38. Section 226MD amended (calculation of potential future exposure of derivative contract)**

(1) Section 226MD(5)(b)(iii)—

**Repeal**

“, Ir BB-”.

(2) Section 226MD(5)(c)(ii)—

**Repeal**

“, [ICRA] BB- or Ir BB-”

**Substitute**

“or [ICRA] BB-”.

**39. Section 226S amended (standardized CVA method)**

- (1) Section 226S(1), Table 23B—

**Repeal**

“Credit Analysis and Research Limited”

**Substitute**

“CARE Ratings Limited”.

- (2) Section 226S(1), Table 23B—

**Repeal**

“CRISIL Limited”

**Substitute**

“CRISIL Ratings Limited”.

- (3) Section 226S(1), Table 23B—

**Repeal column 3**

**Substitute**

“ICRA  
Limited

[ICRA]AAA

[ICRA]AA+

[ICRA]AA

[ICRA]AA-

[ICRA]A+

[ICRA]A

[ICRA]A-

[ICRA]BBB+

[ICRA]BBB

[ICRA]BBB-

[ICRA]BB+

[ICRA]BB

[ICRA]BB-

[ICRA]B+

[ICRA]B

[ICRA]B-

[ICRA]C+

[ICRA]C

[ICRA]C-”.

**40. Part 6B added**

After Part 6A—

**Add**

## **“Part 6B**

# **Calculation of Risk-weighted Amounts of CIS Exposures**

## **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 is granted an exemption under section 12(2)(a) for its CIS exposures and is required to use the STC approach to calculate the risk-weighted amounts of its CIS exposures;

**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);

*simple risk-weight method* (簡單風險權重方法) has the meaning given by 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.

## **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  $\geq 3$ ) 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  $(n-1)^{\text{th}}$  interposed CIS (*Level  $n$  CIS*) is held directly by the  $(n-2)^{\text{th}}$  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  $\geq 1$ ) 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**

$$RWA_{\text{CIS exposure}} = \text{Effective RW} * P_{\text{CIS exposure}}$$

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),  $P_{\text{CIS exposure}}$  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<sub>CIS</sub> 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) or (3); and

- 
- (e) an external auditor has confirmed the correctness of the calculations that generate the third-party output.
- (2) If the institution is an STC AI, a BSC AI, or an exempted IRB AI, the condition in subsection (1)(d) is met if the third party calculates the third-party output—
- (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 66(1)(a) and (2)(b), 68A, 70AAC, 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 section 66(1)(a) and (2), in so far as it relates to regulatory deductible items, and sections 68A and 70AAC); and
- (iii) Parts 6A and 7, in so far as they relate to an STC AI.
- (3) If the institution is an IRB AI, the condition in subsection (1)(d) is met if the third party calculates the third-party output—
- (a) by using the look-through approach in the same way as an IRB AI that holds a CIS exposure to the scheme directly would be required to do under section 226ZO as if sections 226ZT and

226ZX did not exist and the requirements in section 226ZO(6), (7) and (8) were replaced by the requirements to calculate the risk-weighted amount of an underlying exposure that does not fall within section 226ZO(2), (3) or (4)—

- (i) if the exposure is an equity exposure (other than CIS exposure)—by using the simple risk-weight method;
  - (ii) if the exposure is a securitization exposure—by using the SEC-ERBA, SEC-SA or SEC-FBA under Part 7, as the case requires; or
  - (iii) if the exposure does not fall within subparagraph (i) or (ii)—by applying Part 4, or Division 4 of Part 6A, as the case requires (except that section 66(1)(a) and (2), in so far as it relates to regulatory deductible items, and sections 68A and 70AAC do not apply to the determination of the third-party output); 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 the requirements mentioned in paragraph (a).

## **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  $\geq 2$ ) 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 68A did not exist;

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- (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 117A did not exist; or
  - (c) if the institution is an IRB AI—in accordance with those provisions of Part 6 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 183(5) and (6) did not exist.
- (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 Division 3 of Part 6A—
- (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 default risk exposure of the derivative contracts or SFTs;
    - (ii) 0.5; and
    - (iii) the risk-weight applicable to the default risk exposure; or

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- (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 sections 88 and 93, 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.
- (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.



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- (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, to determine the risk-weighted amount of the underlying exposure, the IRB AI must determine the risk-weighted amount of the underlying exposure by—
- (a) if the exposure is an equity exposure (other than CIS exposure)—using the simple risk-weight method;
  - (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 (a) or (b)—applying Part 4.

- (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—

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- (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 or an exempted IRB AI—this Part and Parts 4 and 7;
    - (ii) if the institution is a BSC AI—this Part and Parts 5 and 7; or
    - (iii) if the institution is an IRB AI—this Part and Parts 4, 6 and 7,to the maximum extent allowed under the mandate of the scheme (or, if applicable, under the relevant legislation or regulations governing the scheme); and
  - (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).

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- (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.

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- (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  $\geq 2$ ) 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 68A 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 117A did not exist; or
  - (c) if the institution is an IRB AI—in accordance with those provisions of Part 6 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 183(5) and (6) did not exist.
- (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 Division 3 of Part 6A—
- (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 default risk exposure of the derivative contracts or SFTs;
    - (ii) 0.5; and
    - (iii) the risk-weight applicable to the default risk exposure; or

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- (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 sections 88 and 93, 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.
  - (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.



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- (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) using the simple risk-weight method—if the exposure is an equity exposure not covered by an existing exemption (within the meaning of section 12(5)(a));
    - (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 (i) or (ii).
- (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 70AAC(3), 117AD(3) or 183(1) or (7); or
- (iii) fully risk-weighted under section 70AAC(3), 117AD(3) or 183(1) or (7).
- (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  $\geq 1$ ) 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 70AAC(3), 117AD(3) or 183(1) or (7); or

(iii) fully risk-weighted under section 70AAC(3), 117AD(3) or 183(1) or (7).

(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.”.

**41. Schedule 1 amended (specifications for purposes of certain definitions in these Rules)**

Schedule 1, Part 1, after item 13—

**Add**

“14. Hong Kong Export Credit Insurance Corporation”.

**42. Schedule 4F amended (deduction of holdings where authorized institution has insignificant LAC investments in financial sector entities that are outside scope of consolidation under section 3C requirement)**

Schedule 4F—

**Repeal**

“[ss. 43, 47 & 48]”

**Substitute**

“[ss. 2, 43, 47, 48, 70AAC & 117AD]”.

**43. Schedule 4G amended (deduction of holdings where authorized institution has significant LAC investments in financial sector entities that are outside scope of consolidation under section 3C requirement)**

Schedule 4G—

**Repeal**

“[ss. 43, 47 & 48]”

**Substitute**

“[ss. 2, 43, 47, 48, 70AAC & 117AD]”.

**44. Schedule 6 amended (credit quality grades)**

(1) Schedule 6—

**Repeal**

“[ss. 2, 55, 59, 60, 61, 61A, 62, 79, 98, 99]”

**Substitute**

“[ss. 2, 55, 59, 60, 61, 61A, 79]”.

(2) Schedule 6, Table C, Part 2—

**Repeal**

“Credit Analysis and Research Limited”

**Substitute**

“CARE Ratings Limited”.

(3) Schedule 6, Table C, Part 2—

**Repeal**

“CRISIL Limited”

**Substitute**

“CRISIL Ratings Limited”.

(4) Schedule 6, Table C, Part 2, column 4—



**Repeal**

“IrAAA”.

- (5) Schedule 6, Table C, Part 2, column 4—

**Repeal**

“IrAA+

IrAA

IrAA-”.

- (6) Schedule 6, Table C, Part 2, column 4—

**Repeal**

“IrA+

IrA

IrA-”.

- (7) Schedule 6, Table C, Part 2, column 4—

**Repeal**

“IrBBB+

IrBBB

IrBBB-”.

- (8) Schedule 6, Table C, Part 2, column 4—

**Repeal**

“IrBB+

IrBB

IrBB-

IrB+

IrB

IrB-

IrC+

IrC

IrC-”.

(9) Schedule 6—

**Repeal Table D.**

(10) Schedule 6, Table E, Part 2—

**Repeal**

“Credit Analysis and Research Limited”

**Substitute**

“CARE Ratings Limited”.

(11) Schedule 6, Table E, Part 2—

**Repeal**

“CRISIL Limited”

**Substitute**

“CRISIL Ratings Limited”.

Eddie YUE  
Monetary Authority

12 April 2022

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## Explanatory Note

These Rules amend the Banking (Capital) Rules (Cap. 155 sub. leg. L) (*principal Rules*).

2. The main purpose of these Rules is to amend the principal Rules to provide for the capital treatment of banks' equity investments in funds, as set out in the document entitled "Capital requirements for banks' equity investments in funds" published in December 2013 (and revised in 2019) by the Basel Committee on Banking Supervision.
3. The capital treatment is mainly set out in the new Part 6B of the principal Rules (see section 40).
4. Consequential amendments arising from the capital treatment are also made to Parts 4, 5 and 6 of the principal Rules (see sections 4 to 35).
5. These Rules also seek to—
  - (a) include the Hong Kong Export Credit Insurance Corporation as a domestic public sector entity under the principal Rules (see section 41); and
  - (b) introduce other minor amendments to improve the clarity of certain provisions of the principal Rules.
6. These Rules come into operation on 1 July 2022.