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來函檔號 YOUR REF.: LS/S/21/12-13

19 April 2013

Mr Bonny Loo  
Assistant Legal Advisor  
Legislative Council  
Hong Kong  
(Fax: 2877 5029)

Dear Mr Loo,

### **Banking (Capital) (Amendment) Rules 2013**

Thank you for your letter of 16 April. The Administration's response to your observations is set out below –

#### **Sections 22 and 23**

##### **Item (a)**

The second reference to “section 216(3)” in sections 265(b)(ii) and 278(b)(ii) respectively is not redundant. This reference, which is included between commas in the phrase “section 216(3) and (3A)”, is intended to emphasize that, where applicable, section 216(3) and (3A) should be **applied together** to derive the risk-weight of the securitization exposure concerned. As explained in item (b) below, section 216(3A) is supplementary to section 216(3).

##### **Item (b)**

2. Section 216(3), (3A) and (3B) prescribes the capital calculation methodology for the portion of an exposure of an authorized institution

(“AI”) that is covered by a recognized guarantee or a recognized credit derivative contract under the internal ratings-based approach for credit risk –

- Subsection (3) prescribes the general treatment for the recognition of the credit risk mitigating effect of a recognized guarantee or a recognized credit derivative contract. This subsection is made subject to subsection (3B) as the latter prescribes an alternate treatment (please see below);
- Subsection (3A) stipulates the treatment where an exposure of an AI is covered by both a recognized guarantee (“original guarantee”) and an eligible counter-guarantee. It is “**supplementary**” to subsection (3) in that, in cases where the AI’s exposure falls within subsection (3A), the AI should still follow subsection (3) except that it may treat the counter-guarantee as if it were the original guarantee; and
- Subsection (3B) sets out an “**alternative**” treatment to that prescribed under subsection (3). In the specified case (i.e. where an AI’s exposure is covered by a recognized credit derivative contract cleared by a qualifying central counterparty (“CCP”)), the AI may assign a risk-weight of 2% or 4% (instead of applying subsection (3)) to the exposure to derive the capital requirement.

Item (c)

3. For the purposes of sections 265(b)(ii) and 278(b)(ii) (as amended), the risk-weight applicable to the securitization exposure is –

- where the exposure is covered by a recognized guarantee or a recognized credit derivative contract but the exposure does not fall within section 216(3A) or section 216(3B) (i.e. section 216(3) is applicable), the risk-weight of the recognized credit protection provider;
- where the exposure is covered by a recognized guarantee and the exposure is also covered by a counter-guarantee meeting certain conditions (i.e. section 216(3) and (3A) is applicable), the risk-weight of the counter-guarantee provider; or
- where the exposure is covered by a recognized credit derivative contract cleared by a qualifying CCP (i.e. section 216(3B) is applicable),

- (i) 2% if (a) the AI is a clearing member of the qualifying CCP, or (b) the AI is a client of a clearing member of the qualifying CCP, and certain conditions are met, or
- (ii) 4% if the AI is a client of a clearing member of the qualifying CCP, and certain other conditions (which differ from the conditions referred to in (i) above) are met.

Item (d)

4. Section 216(3), (3A) and (3B) reflects the Monetary Authority's intent with regard to the recognition of the credit risk mitigating effect of recognized guarantees and recognized credit derivative contracts. These provisions govern the treatment of the credit risk mitigation in its various forms, whilst section 216(2)(a) is intended to indicate that the covered portion of the exposure should receive the applicable treatment specified in subsections (3), (3A) and (3B). We therefore do not consider it necessary to amend section 216(2)(a) as suggested.

**Section 27**

Item (e)

5. We believe that the current text can suitably reflect the intent and operation of the relevant provisions of the subsidiary legislation.

**Section 28**

Item (f)

6. The word "recognized" in the new paragraph (e)(ii) of section 1 of Schedule 1A essentially means that the losses concerned are formally acknowledged as losses in financial statements. "Recognized" in this context is commonly rendered as "確認". The rendition is also used in section 41(1)(f) of the BCR and in paragraph (a)(i) of the definition of "cash flow hedge" under section 35 of the BCR.

7. As regards the rendition used in section 226S(2A), “認可.....的效果” is a standard rendition for “recognizing the effect of ...”. The same can be found in section 226K(3) and paragraph (f)(ii) of section 232 of, as well as paragraph 3(d)(ii) of Schedule 2A, to the BCR.

Yours sincerely,



(Jackie Liu)

for Secretary for Financial Services and the Treasury

c.c. Chief Executive, Hong Kong Monetary Authority

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