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**Legislative Council**

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**Paper for the House Committee**

**Report of the Subcommittee on Financial Institutions (Resolution)  
(Loss-absorbing Capacity Requirements — Banking Sector) Rules**

**Purpose**

This paper reports on the deliberations of the Subcommittee on Financial Institutions (Resolution) (Loss-absorbing Capacity Requirements — Banking Sector) Rules ("the Subcommittee").

**Background**

2. During the financial crisis which began in 2007/2008, a number of governments around the world intervened to support their largest financial institutions ("FIs"), including by bailing them out with public money, in order to allow the financial system to continue to function. This was necessary because of the reliance of individuals, businesses and governments on the services FIs provided and the inadequacy of tools at that time for dealing with the failure of systemically important FIs.

3. The Legislative Council ("LegCo") enacted the Financial Institutions (Resolution) Ordinance (Cap. 628) ("FIRO") in June 2016 (the major provisions of which came into operation on 7 July 2017) to provide for the legal basis in respect of the establishment of a cross-sectoral resolution regime for within scope FIs<sup>1</sup> in Hong Kong which is designed to meet the international standards

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<sup>1</sup> Within scope financial institutions ("FIs") under the Financial Institutions (Resolution) Ordinance (Cap. 628) ("FIRO") include all authorized institutions ("AIs"), certain financial market infrastructures, certain licensed corporations, certain authorized insurers, certain settlement institutions and system operators of designated clearing and settlement systems, and recognized clearing houses. The scope of FIRO also extends to holding companies and affiliated operational entities of within scope FIs.

set by the Financial Stability Board ("FSB")<sup>2</sup> in its "Key Attributes of Effective Resolution Regimes for Financial Institutions". Under FIRO, the Monetary Authority ("MA"), the Securities and Futures Commission and the Insurance Authority are resolution authorities ("RAs") vested with a range of powers necessary to effect an orderly resolution of a non-viable systemically important FI for the purpose of maintaining financial stability.

4. There are five stabilization options that an RA may apply to a within scope FI in resolving such FI, and these options fall under the following two broad categories:

- (a) four transfer stabilization options, whereby some or all of the assets, rights or liabilities of, or securities issued by, a within scope FI, are transferred to –
  - (i) a purchaser;
  - (ii) a bridge institution;
  - (iii) an asset management vehicle; and/or
  - (iv) a temporary public ownership company; and
- (b) the bail-in stabilization option, whereby certain liabilities issued by the within scope FI are written down or converted into equity so as to reduce the issuer's debt, thereby absorbing losses and recapitalizing the within scope FI.

5. To enable resolution to be carried out successfully, RAs are empowered to devise strategies for securing an orderly resolution of a within scope FI and make resolvability assessment to determine whether there are any impediments to the orderly resolution of the FI, and to require the FI to remove any substantive barrier to its orderly resolution.

6. Under FIRO, MA is the RA in respect of authorized institutions ("AIs").<sup>3</sup> MA can initiate a bail-in stabilization option for a failing AI to write down or

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<sup>2</sup> Financial Stability Board ("FSB") was established in April 2009 to coordinate at the international level the work of national financial authorities and international standard-setting bodies and promote the reform of international financial regulations. Hong Kong is a member of FSB.

<sup>3</sup> Under Banking Ordinance (Cap. 155), an AI means a bank, a restricted licence bank or a deposit-taking company.

convert into equity certain liabilities of the AI, thereby restoring the AI to viability. But some liabilities (e.g. subordinated, unsecured debt) can be more easily bailed in than others. For the bail-in stabilization option to be effective, AIs in resolution must have a sufficient stock of liabilities that can be readily bailed in, i.e. sufficient loss-absorbing capacity ("LAC").

## **Financial Institutions (Resolution) (Loss-absorbing Capacity Requirements — Banking Sector) Rules**

7. The Financial Institutions (Resolution) (Loss-absorbing Capacity Requirements — Banking Sector) Rules ("LAC Rules") are made by MA under section 19 of FIRO to prescribe LAC requirements for AIs and their group companies. According to the Administration, the development of LAC requirements for AIs (as opposed to other within scope FIs) should be accorded priority given the size, systemic importance, level of concentration, and scale of critical financial functions provided by the banking sector in Hong Kong. The making of the LAC Rules is also necessary in keeping with the development of international guidelines on LAC requirements for banks, in particular FSB's Principles on Loss-absorbing and Recapitalisation Capacity of global systemically important banks ("G-SIBs") in Resolution and Total Loss-absorbing Capacity ("TLAC") Term Sheet ("FSB TLAC Term Sheet").

8. The major proposals and provisions of the LAC Rules are set out below:

- (a) Part 1 of the LAC Rules provides for commencement (i.e. the Rules will commence on 14 December 2018), sets out definitions of terms used in the Rules, and provides for MA to notify a classifiable entity (an entity that can be classified as a resolution entity or material subsidiary, and will therefore be subject to LAC requirements under the LAC Rules) of the preferred resolution strategy covering that entity;
- (b) Part 2 of the LAC Rules states what types of entity are classifiable entity, i.e. AIs and their holding companies or affiliated operational entities, which in each case is incorporated in Hong Kong.<sup>4</sup> Part 2 also empowers MA to classify a classifiable entity (i) where a preferred resolution strategy envisages the application of one or more stabilization options to the relevant entity, as a

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<sup>4</sup> Under FIRO, an affiliated operational entity, in relation to a within scope FI, means a body corporate that is a group company of the FI and that provides services, directly or indirectly, to the FI.

resolution entity; or (ii) if the entity is in a resolution group but is not itself a resolution entity, and subject to certain materiality criteria, as a material subsidiary;

- (c) Part 3 of the LAC Rules sets out the rules to determine the relevant external LAC ratios for a resolution entity and the relevant internal LAC ratios for a material subsidiary;
- (d) Part 4 of the LAC Rules establishes the requirements for resolution entities and material subsidiaries to maintain specified minimum LAC ratios at all times after the relevant period, which is generally a period of 24 months following their classification as a resolution entity or material subsidiary. There are further minimum LAC ratio requirements on certain G-SIBs;<sup>5</sup>
- (e) Part 5 of the LAC Rules sets out the methodology for calculating the LAC for a resolution entity and a material subsidiary;
- (f) Part 6 of the LAC Rules imposes disclosure requirements on resolution entities and material subsidiaries in relation to their LAC, including specifying the subject matter, the medium, the frequency and the timing for disclosure;
- (g) Part 7 of the LAC Rules imposes obligation on an entity to notify MA of its failure or likely failure to comply with a requirement under the LAC Rules. It also empowers MA to require the entity contravening the LAC Rules to take remedial action. Failure to comply with these requirements under Part 7 of the LAC Rules is an offence under section 19 of FIRO;
- (h) Part 8 of the LAC Rules sets out the procedure for the aggrieved entity to apply to the Resolvability Review Tribunal (established under Part 7 of FIRO) for a review of a reviewable decision made by MA under the LAC Rules;

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<sup>5</sup> Where a resolution entity or a material subsidiary is part of a global systematically important banks group that is required to meet requirements from 1 January 2019 under Financial Stability Board Total Loss-absorbing Capacity Term Sheet ("FSB TLAC Term Sheet"), it will be required to meet LAC requirements based on the FSB "floors" within three months of being classified as a resolution entity or a material subsidiary. Under FSB TLAC Term Sheet, the "floors" are set as 16% of risk-weighted assets and 6% of the Basel III leverage ratio denominator, whichever is higher.

- (i) Schedules 1 and 2 to the LAC Rules set out the criteria that must be met by an instrument in order to qualify as an external LAC debt instrument and internal LAC debt instrument, respectively, for inclusion in a resolution entity's external LAC and a material subsidiary's internal LAC; and
- (j) Schedules 3 and 4 to the LAC Rules set out how deductions are to be made from the LAC of a resolution entity or material subsidiary in relation to holdings of its own non-capital LAC liabilities, and holdings of other entities' non-capital LAC liabilities, respectively.

### **The Subcommittee**

9. At the House Committee ("HC") meeting on 26 October 2018, Members agreed to form a subcommittee to study the LAC Rules. The membership list of the Subcommittee is in **Appendix I**. Under the chairmanship of Mr CHAN Chun-ying, the Subcommittee has held three meetings with the Administration to examine the LAC Rules including one meeting to meet with deputations. A list of the deputations which have provided views to the Subcommittee is in **Appendix II**.

10. To allow sufficient time for the Subcommittee to scrutinize the LAC Rules, the Chairman moved a resolution at the Council meeting of 21 November 2018 to extend the scrutiny period of the Rules to the Council meeting of 12 December 2018.

### **Deliberations of the Subcommittee**

#### Scope of authorized institutions subject to the loss-absorbing capacity requirements

11. The Subcommittee notes that some small and medium sized ("SMS") AIs have expressed grave concern that they might be subject to the LAC Rules. These AIs consider that as they are not systemically important banks and hence their non-viability would not pose a risk to the financial stability of Hong Kong, they should not be classified as resolution entities or material subsidiaries and so not be subject to LAC requirements. These AIs have pointed out that the LAC requirements will create a disproportionate cost on SMS banks, adversely reduce their profitability and affect their competitiveness especially amidst the great uncertainties in the global and Hong Kong economy arising from the recent US-China trade conflicts and slowing down in economic growth. These AIs

further consider that only G-SIBs and domestic systemically important banks ("D-SIBs") should be subject to the LAC Rules.

12. Subcommittee members including Mr James TO, Mr CHAN Kin-por, Mr Jeffrey LAM, Dr LO Wai-kwok, Mr Christopher CHEUNG and Mr YIU Si-wing have stressed that the objective of FIRO is to address the non-viability of FIs which are "too big to fail", thereby containing the risks posed by their non-viability to the financial stability of Hong Kong. Therefore, small AIs should not be the targets of FIRO and covering such AIs under the LAC Rules is not consistent with the objectives of FIRO. These members have further pointed out that given the robust regulatory regime of banks in Hong Kong with the Hong Kong Monetary Authority ("HKMA")'s close supervisory oversight, with banks generally maintaining capital well above the minimum regulatory capital requirements, it is unnecessary to impose LAC requirements on small AIs. The Subcommittee has urged the Administration to consider that only G-SIBs and D-SIBs should be subject to the LAC Rules. The Subcommittee has further enquired about the consultation with banks on the LAC Rules and the criteria MA will adopt in determining the classification of AIs as resolution entities and material subsidiaries.

13. HKMA has responded that a public consultation on the legislative proposals on LAC was conducted from January to March 2018, and the draft text of the LAC Rules was also issued for consultation of the banking industry from July to September 2018. The respondents to the consultations are generally supportive of the proposals of implementing the LAC requirements in Hong Kong and have provided comments on technical matters which have been duly taken into account in finalizing the LAC Rules. On the criteria MA will adopt in determining the classification for AIs, HKMA has responded that a FIRO Code of Practice chapter for LAC requirements ("LAC CoP") would provide guidance on how MA intended to exercise its powers under the LAC Rules, including classification of resolution entities and material subsidiaries. The draft LAC CoP have been issued for industry consultation from 19 October to 3 December 2018. HKMA will consider carefully the views of respondents in finalizing the LAC CoP.

14. HKMA has clarified that according to section 2(1) of the FIRO, all AIs are banking sector entities and hence within scope of FIRO. Nevertheless, no AI will be automatically subject to LAC requirements under the LAC Rules or LAC CoP. It is only where the failure of an AI is expected to pose a risk to financial stability, including to depositors, that it would be subject to LAC requirements. As regards whether an AI itself or its group companies (if any) will be classified as a resolution entity or a material subsidiary, and whether the LAC requirements will apply to any entities that are so classified, this will depend on the circumstances of that particular AI, in particular the preferred

resolution strategy (if any) developed or adopted by MA for that AI. Moreover, depending on the circumstances of individual AIs, MA may vary the LAC requirements applicable to them if necessary.

15. On the timeline for prioritizing AIs for the development of preferred resolution strategies, HKMA has pointed out that after the LAC Rules have come into operation, MA will be able to classify resolution entities and material subsidiaries. Non-Chinese G-SIBs will be required to meet LAC requirements three months after classification. For all other AIs, classification will be made no earlier than 1 January 2020. With LAC requirements to be met under the LAC Rules 24 months after classification (or such longer period specified by MA), these AIs will need to meet LAC requirements no earlier than 1 January 2022. In addition, classification will be prioritized starting with D-SIBs. In practice, non-D-SIBs are therefore likely to be classified sometime after 1 January 2020, with their need to meet LAC requirements being pushed back a corresponding period after 1 January 2022.

16. Regarding the suggestion that only G-SIBs and D-SIBs should be subject to the LAC Rules, HKMA has responded that this would undermine the resolution objectives set out in FIRO and lead to increased risks for Hong Kong taxpayers and depositors. A key objective of making banks resolvable is to avoid publicly funded bail-outs. The resolution regime also provides a mechanism for managing in an orderly manner the failure of certain banks, which could not otherwise be dealt with through insolvency given the potential impact of undermining the general confidence of participants in the financial market and thus adversely affecting financial stability in Hong Kong. Under a bank's insolvency, all depositors will lose access to their funds and their accounts for some period of time, pending a pay-out under the Deposit Protection Scheme ("DPS"). HKMA has stressed that the only realistic alternative to a publicly funded bail-out or insolvency is an orderly resolution that minimizes the risk to public funds. This is only achievable if on failure a bank has sufficient LAC to provide the financial resources to support such a resolution.

17. The Subcommittee has enquired about the scope of AIs subject to the LAC rules of other jurisdictions. HKMA has provided a comparison between Hong Kong and other jurisdictions in respect of their scope of AIs subject to LAC requirements, which is set out in **Appendix III**. The conclusion is that the proposed scope of AIs subject to the LAC Rules is broadly aligned with comparable international financial market jurisdictions including European Banking Union jurisdictions, the United Kingdom ("UK") and the United States ("US").

18. Some Subcommittee members including Mr CHAN Chun-ying, Mr CHAN kin-por, Mr James TO and Mr YIU Si-wing are not convinced that

imposing LAC requirements on small banks is an appropriate tool to ensure the protection of Hong Kong depositors which should be the objective of DPS. Should the Administration consider it necessary to enhance protection for depositors, relevant amendments should be made to the legislation on DPS. Mr James TO has remarked that he will raise objection to the LAC Rules if the Administration has not fully addressed his concern about the objectives of FIRO in particular relating to protection for depositors.

19. HKMA has pointed out that MA as the RA under FIRO for all banking sector entities must have regard to the objectives as set out in section 8(1) of FIRO which includes promoting and seeking to maintain the stability and effective working of the financial system of Hong Kong, including the continued performance of critical financial functions. Allowing certain non-D-SIB, non-G-SIB AIs to go into insolvency on failure would likely undermine the general confidence of participants in the financial market in Hong Kong and give rise to contagion within the financial system of Hong Kong, thereby affecting the stability and effective working of the financial system of Hong Kong. It should be noted that many non-D-SIB, non-G-SIB AIs have a large number of depositors, with many depositors not fully covered by DPS. Therefore, allowing banks at this scale to go into insolvency would not be a realistic option. No AI will be automatically subject to LAC requirements under the LAC Rules or LAC CoP. It is only where the failure of an AI, assessed on a case-by-case basis, is expected to pose a risk to financial stability that it would be subject to LAC requirements. As a result, where an AI could demonstrate to MA that its failure could be managed via insolvency without posing such a risk, it would not be subject to LAC requirements.

Asset threshold for prioritizing authorized institutions for the development of preferred resolution strategies

20. The Subcommittee notes that SMS AIs have suggested that MA should develop objective criteria or thresholds for classifying resolution entities and material subsidiaries so that smaller AIs will be excluded from the LAC Rules. The Subcommittee notes the grave concern of SMS AIs over the proposed threshold of HK\$ 150 billion on total consolidated assets of an AI set out in the draft LAC CoP as the criterion for determining in-scope AIs under the LAC Rules ("the asset threshold"), and such criterion will cover almost all locally-incorporated licensed banks in Hong Kong.

21. HKMA has stressed that the draft LAC CoP proposes an indicative threshold of HK\$ 150 billion for AIs to be prioritized for resolution planning but it does not imply that an AI will automatically be required to meet LAC requirements (and vice versa). Recognizing the concerns raised by small AIs and Subcommittee members that the proposed threshold of HK\$ 150 billion



may have a disproportionate impact on some smaller AIs, with adverse cost and competitiveness implications, HKMA has expressed its intention to increase the asset threshold to HK\$ 300 billion in the final version of the LAC CoP. All AIs with total consolidated assets above HK\$ 300 billion have around 200 000 depositors or more.

22. Subcommittee members generally welcome raising the asset threshold to HK\$ 300 billion. As informed by HKMA, if the asset threshold of HK\$ 300 billion is adopted, around 12 AIs will potentially be covered under the LAC Rules as compared to around 17 AIs under the asset threshold of HK\$ 150 billion. The Subcommittee has also called on HKMA to conduct a review of the asset threshold at regular intervals.

23. HKMA has undertaken to conduct a review on the LAC CoP every three years. The review will cover all key aspects of the code and HKMA will consider factors including the prevailing circumstances of Hong Kong, the situations of AIs, and latest development in international standards on resolution and LAC requirements. Following the usual practice, HKMA will issue the draft CoP for consultation with the banking industry and engage other stakeholders in the wider financial market during the consultation process.

#### Timeline for implementation of loss-absorbing capacity rules in Hong Kong and other jurisdictions

24. The Subcommittee notes that some other international financial centres and Asian jurisdictions are implementing their resolution regimes and LAC rules at a slower pace. For instance, some SMS AIs have pointed out that there are no concrete plans for regulators in Singapore and Australia for implementing LAC requirements especially for smaller banks not classified as D-SIBs or G-SIBs. The Mainland will adopt a phased-in approach for LAC implementation from 2025 with full implementation by 2028, which is on a much slower timetable than that proposed in Hong Kong. The Subcommittee is concerned that HKMA's proposed implementation timeline would be ahead of other major international financial centres and this would put the Hong Kong banking industry in a competitive disadvantage position. Some small AIs have suggested adopting a phased implementation timetable with large banks and other banks meeting the LAC requirements in 2022 and 2024/2025 respectively.

25. HKMA has provided a comparison of the implementation progress between Hong Kong and other major jurisdictions on the resolution regimes and LAC requirements, which is set out in **Appendix IV**. HKMA has pointed out that Hong Kong is not a front-runner in implementing LAC requirements. For instance, the final TLAC requirements will be applied from 1 January 2019 in the US. G-SIBs in the UK will be required from 1 January 2019 to meet the

minimum requirements set out in FSB TLAC Term Sheet. LAC requirements in Switzerland are being phased in and are expected to achieve full implementation by end of 2019, whereas TLAC requirements in Japan will be phased in from 21 March 2019.

26. HKMA has re-iterated that according to its plan for classifying AIs, no AIs (other than a non-Chinese G-SIB) will be required to meet LAC requirements earlier than 2022. In the light of concerns expressed by the Subcommittee and SMS AIs, HKMA has agreed to adjust the implementation timetable so that the earliest at which any D-SIB (other than a non-Chinese G-SIB) will be required to meet LAC requirements is 1 January 2022, and the earliest at which any non-D-SIB will be required to meet LAC requirements is 1 January 2023. Where MA determines that an entity will not be able to meet its LAC requirements to this timetable, it has the flexibility to consider allowing a longer implementation period on a case by case basis.

#### Regulatory capital treated as meeting the loss-absorbing capacity requirements

27. Some Subcommittee members including Mr CHAN Kin-por and Mr CHAN Chun-ying have requested the Administration to consider (a) allowing an AI to use at least part of its capital that counts towards meeting minimum regulatory capital requirements to also count towards meeting minimum LAC requirements; and (b) the suggestion of some AIs to count part of an AI's regulatory capital such as Additional Tier 1 ("AT1") capital instruments as a debt component for LAC. It is because although AT1 capital instruments are accounted for as equity on the AI's balance sheet, they are available for absorbing losses during resolution situations.

28. On issue (a) referred to in paragraph 27 above, HKMA has explained that the policy intention is that, generally speaking, items that count towards meeting an entity's minimum regulatory capital requirements can also count towards meeting minimum LAC requirements. However, it should be noted that Common Equity Tier 1 capital instruments that count towards LAC requirements will not also be able to count towards regulatory capital buffers. These regulatory capital buffers are designed to be able to be used by an AI on a going concern, pre-resolution basis. They therefore need to be separate from and additional to LAC requirements, so that they can be used without an AI breaching its LAC requirements. On issue (b), following on going dialogue with the industry, MA proposes to permit eligible AT1 capital instruments to count towards the minimum LAC debt requirement, irrespective of whether they are accounted for as debt or equity.

### Issuance of loss-absorbing capacity debt instruments by small banks

29. As AIs will need to issue LAC debt instruments in order to meet the LAC requirements, the Subcommittee notes that SMS AIs have raised concern about the cost burden on them, and the ability of the debt market to absorb LAC debt instruments and thus the impact on the interest rates on the instruments. In particular AIs may issue LAC debt instruments at similar times resulting in a substantial amount of LAC issuances in the market in a certain period.

30. HKMA has advised that it conducted an impact assessment on the imposition of LAC requirements in Hong Kong, and in this assessment used an estimated annual cost of non-capital LAC debt instruments of 4%. The figure has been worked out by adopting a conservative approach using the slightly below 4% weighted average cost of locally-incorporated licensed banks for issuing Tier 2 capital instruments as reported by these banks to HKMA in October 2017. HKMA has supplemented that it is envisaged that the majority of AIs in Hong Kong that may be subject to LAC requirements will not issue LAC debt instruments to the external market, but will instead be issuing internal LAC to foreign parent companies within international financial groups. The funding for such LAC will ultimately be raised by cross-border banks with ready access to deep and active global debt markets. For such banks, the ability of the markets to cope with additional supply is not a question. It should be noted that many G-SIBs have already successfully issued a lot of TLAC instruments that are required for their global and Hong Kong operations. On the other hand, locally-incorporated AIs are already likely to have issued AT1 capital instruments and/or Tier 2 capital instruments into the market. They already have an established investor base for the issuance of LAC instruments. HKMA has further pointed out that should there be unforeseen changes to market conditions that warrant exceptional treatment, MA has the flexibility under the LAC Rules to address them. For example, MA would be able to defer the classification of a resolution entity or material subsidiary under rules 5(1) and 6(1) of the LAC Rules respectively, and to extend the implementation period beyond 24 months under rule 31 of the LAC Rules, where appropriate.

### **Recommendation**

31. The Subcommittee will not propose amendments to the LAC Rules. The Subcommittee also notes that the Administration and HKMA will not propose amendments to the LAC Rules.

**Advice sought**

32. The Subcommittee Chairman gave a verbal report on the deliberations of the Subcommittee at the HC meeting on 30 November 2018. Members are requested to note this written report.

Council Business Division 1  
Legislative Council Secretariat  
5 December 2018

**Subcommittee on Financial Institutions (Resolution)  
(Loss-absorbing Capacity Requirements - Banking Sector) Rules**

**Membership list**

**Chairman** Hon CHAN Chun-ying, JP

**Members** Hon James TO Kun-sun  
Hon Abraham SHEK Lai-him, GBS, JP  
Hon Jeffrey LAM Kin-fung, GBS, JP  
Hon WONG Ting-kwong, GBS, JP  
Hon CHAN Kin-por, GBS, JP  
Hon YIU Si-wing, BBS  
Hon Kenneth LEUNG  
Hon Dennis KWOK Wing-hang  
Hon Christopher CHEUNG Wah-fung, SBS, JP  
Ir Dr Hon LO Wai-kwok, SBS, MH, JP  
Hon YUNG Hoi-yan

(Total : 12 members)

**Clerk** Ms Connie SZETO

**Legal Adviser** Mr Mark LAM

**Subcommittee on Financial Institutions (Resolution)  
(Loss-absorbing Capacity Requirements - Banking Sector) Rules**

**List of organizations from which the Subcommittee has received views**

1. Bank of China (Hong Kong) Limited
2. The Bank of East Asia Limited
3. Chong Hing Bank Limited
4. CMB Wing Lung Bank Limited
5. Dah Sing Bank
6. Fubon Bank (Hong Kong) Limited
7. Nanyang Commercial Bank Limited
8. OCBC Wing Hang Bank Limited
9. Public Bank (Hong Kong) Limited
10. Shanghai Commercial Bank Limited

Table 1 – implementation progress of developing LAC requirements with respect to G-SIBs, D-SIBs and others

Region	Scope of LAC requirements	Non-G-SIBs / D-SIBs in scope of requirements ?
Hong Kong	All AIs were brought in scope of the Financial Institutions (Resolution) Ordinance (Cap. 628) ("FIRO") when it came into force in July 2017. However, under the Rules, an AI can only be classified as a resolution entity if its preferred resolution strategy involves the application of resolution tools under the FIRO. Resolution tools can only be applied under the FIRO where the failure of an AI would pose a risk to financial stability. More generally, the Rules are designed to ensure that <b>it is <u>only</u> where the failure of an AI is expected to pose a risk to financial stability, including to depositors, that it would be subject to LAC requirements.</b>	Yes
Australia	Under a proposal published on 8 November 2018, all D-SIBs must meet additional LAC requirements through higher capital requirements. <b>Other authorised deposit-taking institutions will be assessed individually</b> in light of their resolution strategies.	Yes
European Union	The Bank Recovery and Resolution Directive ("BRRD") requires Member States to ensure that institutions meet minimum requirements on own funds and eligible liabilities ("MREL", a measure of loss-absorbing capacity). <sup>1</sup> <b>All credit institutions are in scope</b> , with resolution authorities to ensure that the MREL of each institution is sufficient to ensure that it can be resolved in a way that meets the resolution objectives, which include protecting public funds and depositors. For example,	Yes

<sup>1</sup> See: <https://eur-lex.europa.eu/legal-content/EN/TXT/PDF/?uri=CELEX:02014L0059-20171228&from=EN>.

Region	Scope of LAC requirements	Non-G-SIBs / D-SIBs in scope of requirements ?
	Sweden has set MREL requirements for ten institutions, with the requirements ranging from 19.3% to over 52.1% of risk-weighted assets ("RWAs"). <sup>2</sup>	
UK	In line with the BRRD, the UK has set indicative MREL requirements <b>not only for G-SIBs and D-SIBs but also for other firms.</b> All relevant firms need to start meeting MREL requirements from 1 January 2020. The indicative MREL requirements (including capital buffers) range from 26.2% to 30.4% of RWAs. <sup>3</sup> The smallest firm subject to MREL requirements has total consolidated assets of around GBP 15 billion (around HKD 150 billion).	Yes
US	Final Total Loss-Absorbing Capacity ("TLAC") requirements apply to <b>G-SIBs</b> . <sup>4</sup> The resolution of other bank failures are typically funded by the Federal Deposit Insurance Corporation ("FDIC").	No, but FDIC funds available.
Japan	In scope AIs <b>include G-SIBs and D-SIBs</b> . <sup>5</sup>	No
Mainland	Imposition of TLAC requirements pending.	N/A
Singapore	Imposition of TLAC requirements pending.	N/A

<sup>2</sup> See: <https://www.riksdagen.se/en/press/press-releases/2017/requirements-set-and-plans-established-for-how-swedish-banks-are-to-be-managed-in-a-crisis/>.

<sup>3</sup> See: <https://www.bankofengland.co.uk/-/media/boe/files/financial-stability/resolution/indicative-firm-mrels-2018>.

<sup>4</sup> See: <https://www.federalreserve.gov/newsevents/pressreleases/files/bcreg20161215a1.pdf>.

<sup>5</sup> See: <https://www.fsa.go.jp/en/news/2018/20180413/01.pdf>.

(Source : Table 1 of LC Paper No. CB(1)218/18-19(02)).



Table 1 – implementation progress on developing (i) a resolution regime; and (ii) LAC requirements

Region	Resolution regime <sup>1</sup>	LAC requirements
Hong Kong	<i>FSB Peer Review Feb. 2018</i> : "Hong Kong now has legal powers ... related to resolution that are consistent with those required under the [Key Attributes]."	Once the LAC Rules have come into operation, the resolution authority will be able to classify resolution entities and material subsidiaries. Non-Mainland global systemically important banks ("G-SIBs") can be required to meet LAC requirements three months after classification. For all other AIs, the resolution authority's intention is that classification will be no earlier than 1 January 2020, with LAC requirements to be met under the LAC Rules 24 months after classification, i.e. no earlier than 1 January 2022. In addition, classification will be prioritised starting with domestic systemically important banks ("D-SIBs"). In practice, non-D-SIBs are therefore likely to be classified some time after 1 January 2020, with their need to meet LAC requirements being pushed back a corresponding period after 1 January 2022.
Japan	<i>FSAP July 2017</i> : "While efforts to align the resolution framework with the [Key Attributes] have progressed, the resolution framework has some remaining gaps."	Total loss-absorbing capacity ("TLAC") requirements being phased in from 31 March 2019. <sup>2</sup>
Mainland	<i>FSAP Dec. 2017</i> : "In line with the FSB requirements, Crisis Management Groups and recovery and resolution plans are in place for all five of China's [global systemically important financial institutions], and resolvability assessments and cross-border co-operation agreements are in progress."	Imposition of TLAC requirements pending. Under the TLAC term sheet issued by the FSB on 9 November 2015, Mainland G-SIBs do not have to meet TLAC requirements before 1 January 2025, subject to this deadline being brought forward if the corporate debt to GDP ratio exceeds 55%

<sup>1</sup> For each jurisdiction, an assessment of the resolution regime has been extracted from the more recent of (i) the most recent Financial Stability Board ("FSB") Peer Review for that jurisdiction; and (ii) the most recent IMF Financial Sector Assessment Program ("FSAP") for that jurisdiction. Reference to the "Key Attributes" are to the FSB's "Key Attributes of Effective Resolution Regimes for Financial Institutions", published in October 2011 and updated in October 2014.

<sup>2</sup> See: <https://www.fsa.go.jp/en/news/2018/20180413/01.pdf>.

Region	Resolution regime <sup>1</sup>	LAC requirements
	"Further work is needed to align approaches to resolving weak [financial institutions] with the [Key Attributes]."	before the end of 2020. This ratio was close to 50% at the end of 2017.
Singapore	<i>FSB Peer Review Feb. 2018</i> : "Singapore has a resolution regime broadly in line with the Key Attributes."	Eligibility criteria for bail-in instruments set out in regulations <sup>3</sup> that came into force on 29 October 2018. Imposition of TLAC requirements pending.
Switzerland	<i>FSAP May 2014</i> : "The authorities are ahead of many jurisdictions in adopting reforms broadly aligned with the [Key Attributes]."	Final loss-absorbency requirements published in October 2015, phased in linearly until end of 2019. <sup>4</sup>
UK	<i>FSAP June 2016</i> : "The transposition of the EU Bank Recovery and Resolution Directive has completed the reform of the UK's Special Resolution Regime for banks, which is now broadly aligned with global standards."	UK firms will become subject to interim minimum requirements for own funds and eligible liabilities (which broadly correspond to LAC requirements) on 1 January 2020, prior to the final requirements coming into force in 2022. <sup>5</sup> In addition, UK G-SIBs will be required from 1 January 2019 to meet the minimum requirements set out in the FSB TLAC term sheet. <sup>6</sup>
US	<i>FSAP July 2015</i> : "Title II ("Orderly Liquidation Authority", OLA) of the [Dodd-Frank Wall Street Reform and Consumer Protection Act] sets forth a new resolution regime for "covered financial companies", granting resolution powers to the [Federal Deposit Insurance Corporation]. The OLA powers are extensive [and] align broadly with international best practice ..."	Final TLAC requirements to apply from 1 January 2019. <sup>7</sup>

<sup>3</sup> See: <https://sso.agc.gov.sg/SL/MASA1970-S714-2018?DocDate=20181026#pr23->.

<sup>4</sup> See: <https://www.finma.ch/en/news/2015/10/mm-tbtf-20151021/>.

<sup>5</sup> See: <https://www.bankofengland.co.uk/financial-stability/resolution/indicative-mrels>.

<sup>6</sup> See: <https://www.bankofengland.co.uk/-/media/boe/files/financial-stability/resolution/indicative-firm-mrels-2018.pdf?la=en&hash=4553DF2579E49077E92C6BD39A8C07C5D08D72D9>.

<sup>7</sup> See: <https://www.federalreserve.gov/newsevents/pressreleases/files/bcreg20161215a1.pdf>.