AIFC BANKING BUSINESS PRUDENTIAL RULES

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CHAPTER 1 General

1.1 Introduction

The purpose of these Banking Business Rules (BBR) is to establish the prudential framework for Authorised Firms carrying out Banking Business. These rules are based on the Basel Accords and on the Basel Core Principles for Effective Banking Supervision, issued by the Basel Committee on Banking Supervision.

1.2 Commencement

These rules commence on 30 July 2018.

1.3 Effect of definitions, notes and examples

(1) A definition in the AIFC Glossary also applies to any instructions or document made under these rules.

(2) A note in or to these rules is explanatory and is not part of these rules. However, examples and guidance are part of these rules.

(3) An example is not exhaustive, and may extend, but does not limit, the meaning of these rules or a provision of these rules to which it relates.

(4) Unless the contrary intention appears, a reference in these rules to an accord, principle, standard or other similar instrument is a reference to that instrument as amended from time to time.

1.4 Banking Business firms

(1) Banking Business comprises the Regulated Activities of Accepting Deposits, Dealing in Investments as Principal and Providing Credit. An Authorised Firm that has a license from the AFSA to conduct any of those activities is a Banking Business firm.

(2) However, an Authorised Firm that is an Islamic Bank or an Islamic Broker dealer or an Islamic Financing Company (as defined in the IBB Rules) is not a Banking Business firm for the purposes of these Rules.

(3) A Banking Business firm may be a Bank or a Broker Dealer or a Credit Provider.

Guidance

A firm that conducts any of the activities that make up Banking Business, or a combination of those activities, will need to consider the extent to which its business model is subject to the prudential requirements set out in these rules. These rules are designed to address the different prudential risks that could arise from the broad range of business models, risk appetites and risk profiles of Banking Business firms.

For example, a firm that solely conducts the activity of Dealing in Investments as Principal (that is, a Broker Dealer) will need to consider the extent to which its activities in buying, selling, subscribing to or underwriting investments attract prudential risks that are subject to the requirements of these rules. In contrast, a firm that is a Bank and that also conducts the activity of Dealing in Investments as Principal would be subject to a broader range of prudential requirements. In both examples, these rules apply in accordance with the nature, scale and complexity of the firm’s business.

1.5 Bank

(1) An Authorised Firm is a Bank if it is authorised to conduct the Regulated Activity of Accepting Deposits and/or Opening and Operating Bank Accounts.

(2) An Authorised Firm is a Bank even if it is also authorised to conduct any other Regulated Activity or activity. The authorisation for Accepting Deposits and/or Opening and Operating Bank Accounts qualifies an Authorised Firm as a Bank.

1.6 Broker Dealer

(1) An Authorised Firm is a Broker Dealer if it is authorised to conduct the Regulated Activity of Dealing in Investments as Principal and it is not a Bank.

(2) A Broker Dealer may raise funds from capital markets or money markets using debt instruments of any type but must not accept deposits.

(3) An Authorised Firm is a Broker Dealer even if it is also authorised to conduct any other Regulated Activity (except Accepting Deposits). The authorisation for Dealing in investments as a Principal and the absence of an authorisation for Accepting Deposits qualifies an Authorised Firm as a Broker Dealer.

(4) An Authorised Firm licensed to conduct the Regulated Activity of Dealing in Investments as Principal on a matched principal basis does not fall under the category of Broker Dealer. Such firms are subject to the AIFC PRU INV Rules and are not subject to the BBR Rules.

1.7 Credit Provider

(1) An Authorised Firm is a Credit Provider if it is authorised to conduct the Regulated Activity of Providing Credit and it is not a Bank.

(2) Credit Providers may raise funds from capital markets or money markets using debt instruments of any type but must not accept Deposits.

(3) An Authorised Firm is a Credit Provider even if it is also authorised to conduct any Regulated Activity (except Accepting Deposits). The authorisation for Providing Credit and the absence of an authorisation for Accepting Deposits qualifies an Authorised Firm as a Credit Provider.

(4) A Credit Provider may conduct the Regulated Activity of Dealing in Investments as Principal, if it receives the necessary authorisation from the AFSA.

1.8 Application of these rules — general

(1) Except as stated otherwise, these rules apply to a Person that has, or is applying for, a license to conduct Banking Business, as defined in Rule 1.4(1).

(2) Except as stated otherwise, all references to a Bank in the BBR Rules must be read as referring also to Broker Dealers, defined in Rule 1.6 and Credit Providers, defined in Rule 1.7. Consequently, all the regulatory requirements imposed by these BBR Rules apply to all entities licensed to carry out Banking Business as defined in Rule 1.4 (1), except for specific sections or rules wherein their applicability is defined in a particular manner. For clarity, all the regulatory requirements imposed by the BBR Rules apply to Banks, Broker Dealers and Credit Providers as defined in Rules 1.5, 1.6 and 1.7, unless otherwise specified in the BBR.

(3) Firms licensed by the AFSA to conduct the Regulated Activities of Advising on a Credit Facility, Arranging a Credit Facility or Providing Money Services are subject only to Base Capital Requirements set out in Rule 4.10.

Guidance

It is possible for an Authorised Firm to be authorised both as a Bank under these rules and to hold a license to carry on one or more other Regulated Activities defined in Schedule 1 of the AIFC GEN Rules. Both these rules and the relevant rules for those activities could apply to such an Authorised Firm in relation to the activities they are involved in. In relation to such an Authorised Firm, however, the Capital requirements in these rules apply. If that Authorised Firm complies with the Capital requirements in these rules, it is taken to comply with the prudential rule requirements specified in AIFC PRU INV Rules.

1.9 Application of these rules—branches

(1) Chapter 4 (Capital adequacy) does not apply to a Bank operating in the form of a branch in the AIFC, in respect of the quantitative capital requirements and related rules specified in Chapter 4. The rules specifying non-quantitative requirements in respect of governance, board responsibilities, policies, systems and controls apply to Banks operating as branches in the AIFC.

(2) However, the AFSA may require a branch to have Capital resources or to comply with any other Capital requirement if the AFSA considers it necessary or desirable to do so in the interest of effective supervision of the branch.

1.10 Requirement for policy also requires procedures and systems

In these rules, a requirement for a Bank to have a policy also requires such a firm to have the procedures, systems, processes, controls and limits needed to give effect to the policy.

1.11 Responsibility for principles

(1) A Bank's Governing Body is responsible for the firm's compliance with the principles and requirements set out in these rules.

(2) The Governing Body must ensure that the firm's senior management establishes and implements policies to give effect to these rules. The Governing Body must approve significant policies and any changes to them (other than formal changes) and must ensure that the policies are fully integrated with each other.

Note: The significant policies relate to the adequacy of capital and the management of various prudential risks faced by a Bank and group risk, as set out in the following Chapters.

(3) The Governing Body must review and appropriately adjust the firm's policies from time to time, taking into account changed operating circumstances, market conditions, activities and risk profiles. The interval between reviews must be appropriate for the nature, scale and complexity of the Bank's business, but must not be longer than 12 months.

(4) The Governing Body must ensure that the policies are made known to, and understood by, all relevant staff.

CHAPTER 2 Principles relating to Banking Business

2.1 Principle 1—Capital Adequacy

A Bank must have capital, of adequate amount and appropriate quality, for the nature, scale and complexity of its business and for its risk profile. A Bank must have appropriate risk management strategies that have been approved by the Bank's Governing Body. The Governing Body of the Bank must set its risk appetite to define the level of risk the Bank is willing to assume.

2.2 Principle 2—Credit Risk and Problem Assets

(1) A Bank must have an adequate Credit Risk management policy that takes into account the Bank's risk tolerance, its risk profile and the market and macroeconomic conditions. This policy must identify, measure, evaluate, monitor, report and control or mitigate Credit Risk in a timely way.

(2) A Bank must have adequate policies for the early identification and management of problem assets, and the maintenance of adequate provisions and reserves.

2.3 Principle 3—Transactions with Related Parties

A Bank must enter into transactions with related parties on an arm's-length basis to avoid conflicts of interest.

2.4 Principle 4—Concentration Risk

A Bank must have adequate policies to identify, measure, evaluate, manage and control or mitigate concentrations of risk in a timely way.

2.5 Principle 5—Market Risk

A Bank must have an adequate Market Risk management policy that takes into account the firm's risk tolerance, its risk profile, the market and macroeconomic conditions and the risk of a significant deterioration in market liquidity. This policy must identify, measure, evaluate, manage and control or mitigate Market Risk in a timely way.

2.6 Principle 6—Operational Risk

A Bank must have an adequate operational risk management policy that takes into account the firm's risk tolerance, its risk profile and market and macroeconomic conditions. This policy must identify, measure, evaluate, manage and control or mitigate operational risk in a timely way.

2.7 Principle 7— Interest Rate Risk in the Banking Book

A Bank must have an adequate management policy for Interest Rate Risk in the Banking Book that takes into account the firm's risk tolerance, its risk profile and the market and macroeconomic conditions. This policy must identify, measure, evaluate, manage and control or mitigate interest rate risk in the Banking Book in a timely way.

2.8 Principle 8—Liquidity Risk

A Bank must have prudent and appropriate quantitative and qualitative liquidity requirements. A Bank must also have adequate policies to identify, measure, evaluate, manage and control or mitigate Liquidity Risk in a timely way.

2.9 Principle 9—Group Risk

A Bank must effectively manage risks arising from its membership in a group.

CHAPTER 3 Prudential Reporting Requirements

3.1 Introduction

(1) This Chapter sets out the prudential reporting requirements for a Bank.

(2) The prudential returns of a Bank must reflect its management accounts, financial statements and ancillary reports. A Bank's prudential returns, accounts, statements and reports must all be prepared using the same standards and practices and must be easily reconcilable with one another.

(3) A prudential return is referred to as a Solo prudential return if it reflects the individual Bank's accounts, statements and reports.

(4) A Consolidated prudential return means a prudential return which reflects the accounts, statements and reports of a Bank consolidated with those of the other members of its Financial Group.

Note Financial Group is defined in Chapter 10 of BBR and is used for consolidated reporting instead of 'corporate group'.

3.2 Information about Financial Group

If directed by the AFSA, a Bank must give the AFSA the following information about its Financial Group:

(a) details about the entities in the group;

(b) the structure of the group;

(c) how the group is managed;

(d) any other information that the AFSA requires.

Note The processes and procedures relating to flow of management information, decision-making, oversight, control and review of the operations and activities of the group are collectively referred to as managing the group in (c) above.

3.3 Financial Group risk

(1) If a Bank is part of a Financial Group, Credit Risk, market risk, operational risk, Interest Rate Risk in the Banking Book (IRRBB) and liquidity risk exposures (collectively referred to as prudential risk exposures) apply on a consolidated basis to the Bank and the other members that constitute its Financial Group.

(2) Preparing returns on a consolidated basis means including the financial effects and risk exposures arising from all the activities of all the members or entities forming part of the Bank's Financial Group. Such returns are not restricted to just reflecting the financial activities or positions of the Bank.

Note: A Bank is required to have systems to enable it to calculate its financial group capital requirement and resources, according to rules in Chapter 10 of the BBR.

3.4 Preparing returns

(1) A Bank must prepare the prudential returns that it is required to prepare by a notice published by the AFSA on its own website. Such a notice may also require Banks to give other information to the AFSA.

(2) The Bank must give the return to the AFSA within the period stated in the notice.

(3) The AFSA may, by written notice:

(a) require a Bank to prepare additional prudential returns;

(b) exempt a Bank from a requirement to prepare annual, biannual, quarterly or monthly returns (or a particular return); or

(c) extend the period within which to give a return.

(4) An exemption may be subject to one or more conditions. The Bank availing the exemption must comply with any condition attached to an exemption.

(5) The Bank must prepare and submit its prudential returns in accordance with the AFSA's instructions. Such instructions may require that the return be prepared or given through an electronic submission system.

(6) The instructions may be set out in these rules, in the return itself, in a separate document published by the AFSA on its own approved website or by written notice. These instructions, wherever or however they are given, are collectively referred to as instructions for preparing returns.

Note: Instructions may be in the form of formulae or blank spaces that a Bank is expected to use or fill in which would automatically compute the amounts to be reported.

3.5 Giving information

(1) The AFSA may, by written notice, require a Bank to provide information in addition to that required under these rules.

(2) A Bank must submit the required information to the AFSA in accordance with the AFSA's instructions and within the period stated in the written notice seeking such information. The AFSA may extend the period for the submission of such information.

(3) The AFSA may exempt a Bank from giving information. The Bank must comply with any conditions attached to such an exemption.

3.6 Accounting standards

A Bank must prepare and maintain its financial accounts and prepare its financial statements in accordance with the International Financial Reporting Standards (IFRS).

3.7 Signing returns

(1) A prudential return must be signed by 2 individuals, who are Approved Individuals for the Bank and who occupy any of the Controlled Functions of Director, Senior Executive Officer or Finance Officer. The AFSA, by way of a notice, may prescribe acceptable modes of affixing a signature for the prudential returns, including but not limited to electronic signatures.

(2) If these Approved Individuals are not available or are unable to sign, the prudential return must be signed by both of the individuals approved to exercise the following Controlled Functions:

(a) the Risk Manager function;

(b) the Compliance Officer function.

3.8 Obligation to notify the AFSA

(1) A Bank must notify the AFSA if it becomes aware, or has reasonable grounds to believe, that the Bank has breached, or is about to breach, a prudential requirement.

(2) In particular, the Bank must notify the AFSA as soon as practicable of:

(a) any breach or potential breach of its minimum capital requirement;

(b) any concern it has about its solvency or capital adequacy position;

(c) any indication of significant adverse change in the market price of, or trading volume of, the equity capital or other capital instruments of the Bank or those of its Financial Group (including pressure on the Bank to purchase its own equity or debt);

(d) any other significant adverse change in its capital; and

(e) any significant departure from its Internal Capital Adequacy Assessment Process (ICAAP).

(3) The Bank must also notify the AFSA of any measures planned or taken to deal with any real or potential breach or concerns related to its solvency or capital adequacy position.

CHAPTER 4 Capital Adequacy

4.1 Introduction

(1) This Chapter sets out capital adequacy requirements for a Bank.

(2) A Bank's total Regulatory Capital is the sum of its Tier 1 Capital and Tier 2 Capital. The categories and elements of Regulatory Capital, as well as the limits, restrictions and adjustments to which they are subject are set out in this Chapter.

(3) Capital adequacy and capital management must be an integral part of a Bank's overall governance and its bank-wide risk management process. Capital management must align the Bank's risk appetite and risk profile with its capacity to absorb losses.

4.2 Application to branches

(1) This Chapter does not apply to a Bank that is licensed to operate as a branch in the AIFC, insofar as this Chapter would require the branch to hold capital.

(2) A branch is required to comply with the reporting requirements under this Chapter. In relation to the branch's ICAAP, the branch may rely on the ICAAP for the bank of which it is a part (if available), to demonstrate compliance.

4.3 Governing Body's responsibilities

(1) A Bank's Governing Body must consider, on a periodic basis, whether the minimum capital and liquidity resources required by these rules are adequate to ensure there is no significant risk that the Bank's liabilities cannot be met as they fall due. The Bank must take material and effective measures to obtain additional capital and liquidity resources if its Governing Body considers that the minimum requirements defined in these rules do not adequately reflect the risks of its business.

(2) The Governing Body is also responsible for:

(a) ensuring that capital management is part of the Bank's bank-wide risk management framework and is aligned with its risk appetite and risk profile;

(b) ensuring that the Bank has, at all times, capital and liquidity resources of the kinds and amounts required by these rules;

(c) ensuring that the Bank has capital, of adequate amount and appropriate quality, for the nature, scale and complexity of its business and for its risk profile;

(d) ensuring that the amount of capital it has exceeds its minimum capital requirement, calculated according to these rules;

(e) reviewing the Bank's annual ICAAP and approving it, including but not limited to taking decisions to raise additional capital for the Bank; and

(f) monitoring the adequacy and appropriateness of the Bank's systems and controls to ensure the Bank's compliance with these rules.

4.4 Systems and controls

(1) A Bank must have adequate systems and controls to allow it to calculate and monitor its minimum capital requirement.

(2) The systems and controls must be documented and must be appropriate for its risk profile and proportionate to the nature, scale and complexity of its business.

(3) The systems and controls employed by a Bank must include the ICAAP process which is defined in greater detail in a separate chapter of these rules.

(4) The systems and controls must, at all times, enable the Bank to demonstrate its compliance with the rules in this Chapter.

(5) The systems and controls of the Bank must enable it to manage available capital in anticipation of events or changes in market conditions.

(6) A Bank must have adequate and proportionate contingency plans to maintain or increase its capital in times of stress, whether idiosyncratic or systemic.

4.5 Use of internal models

A Bank must not use its internal models to calculate regulatory capital requirements and assess capital adequacy in accordance with the BBR Rules or to achieve compliance with the BBR Rules, except for the instances permitted by Rule 6.7 for calculation of market risk capital requirements.

4.6 References to particular currencies

In these rules, the specification of an amount of money in a particular currency is also taken to specify the equivalent sum in any other currency at the relevant time.

Initial and ongoing capital requirements

Section 4A – Capital Requirements and Ratios

4.7 Capital Requirements

(1) A Bank is required to meet minimum risk-based capital requirements for exposure to Credit Risk, market risk and operational risk, under these rules. The Bank’s capital ratios (consisting of CET 1 ratio, total tier 1 ratio and total capital ratio) are calculated by dividing its Regulatory Capital by total Risk-Weighted Assets (RWAs).

(2) Total RWAs of a Bank is the sum of:

(a) the Bank’s RWAs for all on-balance-sheet and off-balance-sheet Credit Risk exposures calculated in accordance with the rules in Chapter 5 of BBR; and

(b) 12.5 times the sum of the Bank’s market and operational risk capital requirements (to the extent that each of those requirements applies to the Bank) calculated in accordance with the rules in Chapters 6 and 7 of BBR respectively

(3) In this Chapter, ***consolidated Subsidiary***, of a Bank, means:

(a) a Subsidiary of the Bank; or

(b) a Subsidiary of a Subsidiary of the Bank.

4.8 Required Tier 1 Capital on authorisation

A Bank must have, at the time of its authorisation and at all times thereafter, Common Equity Tier 1 Capital (CET1 Capital) as defined in Rule 4.14, at least equal to the Base Capital Requirement

applicable to it. The AFSA will not grant an authorisation for conducting Banking Business unless it is satisfied that the entity complies with this requirement.

4.9 Required ongoing capital

(1) A Bank must have at all times, Capital at least equal to the higher of:

(a) its Base Capital requirement; and

(b) its Risk-based Capital requirement.

Note A Bank whose minimum capital requirement is determined by its risk-based capital requirement is subject to the additional requirement to maintain a Capital Conservation Buffer, as defined in Rule 4.31.

(2) The amount of Capital that a Bank must have, in accordance with these rules, is its Minimum Capital Requirement.

4.10 Base Capital Requirement

The Base Capital Requirement is:

(a) for a Bank — USD 10 million;

(b) for a Broker Dealer — USD 500,000;

(c) for a Credit Provider – USD 2 million;

(d) for an Authorised Firm Arranging Credit Facility – USD 10,000;

(e) for an Authorised Firm Advising on Credit Facility – USD 10,000;

(f) for an Authorised Firm Providing Money Services – USD 200,000.

4.11 Risk-based Capital Requirement

(1) The Risk-based Capital Requirement for a Bank is the sum of:

(a) its Credit Risk capital requirement;

(b) its Market Risk Capital Requirement; and

(c) its Operational Risk Capital Requirement.

(2) The Market Risk and Operational Risk Capital Requirements are required to be calculated according to the rules in Chapters 6 and 7 of BBR respectively.

(3) The Credit Risk Capital Requirement must be calculated as 8% of the Bank's risk-weighted on-balance-sheet and off-balance-sheet Credit Risk exposures calculated in accordance with the rules in Chapter 5 of BBR.

4.12 Capital ratios

(1) A Bank's capital adequacy is measured in terms of 3 capital ratios expressed as percentages of its total Risk-Weighted Assets (RWAs).

(2) A Bank's minimum capital ratios are:

(a) a CET 1 Capital ratio of 4.5%;

(b) a Tier 1 Capital (T1 Capital) ratio of 6%; and

(c) a Total Capital ratio of 8%.

(3) The AFSA may, if it believes it is prudent to do so, increase any or all of a Bank's minimum capital ratios. The AFSA will notify the Bank in writing about a higher capital ratio and the timeframe available for the Bank to meet it.

(4) A Bank must maintain at all times capital ratios higher than the required minimum levels specified in Rule 4.12 (2).

Section 4B – Elements of Regulatory Capital

4.13 Total Capital

(1) The Total Capital of a Bank is the sum of its Tier 1 (T1) Capital and Tier 2 (T2) Capital.

(2) T1 Capital is the sum of a Bank's Common Equity Tier 1 (CET 1) Capital and Additional Tier 1 (AT1) Capital. T1 Capital is also known as going-concern capital because it is meant to absorb losses while the Bank is viable.

(3) T2 Capital is defined in Rule 4.18. T2 Capital is also known as gone-concern capital because it is meant to absorb losses after the Bank ceases to be viable.

(4) For these rules, the 3 categories of Regulatory Capital are CET 1 Capital, AT1 Capital and T2 Capital.

4.14 Common Equity Tier 1 (CET1) Capital

CET 1 Capital is the sum of the following elements:

(a) common shares issued by the Bank that satisfy the criteria in Rule 4.15 for classification as common shares for regulatory purpose (or the equivalent for legal entities which are not);

(b) share premium resulting from the issue of instruments included in CET 1 Capital;

(c) retained earnings;

(d) accumulated other comprehensive income and other disclosed reserves;

(e) common shares, issued by a consolidated Subsidiary of the Bank and held by third parties, that satisfy the criteria in Rule 4.22 for inclusion in CET 1 Capital;

(f) regulatory adjustments applied in the calculation of CET 1 Capital in accordance with Rule 4.29.

4.15 Criteria for classification as CET1 Capital

A capital instrument issued by a Bank is eligible for classification as common equity and for inclusion in CET 1 Capital, only if all of the following criteria in sub-rules (1) to (14) below are satisfied:

(1) The instrument is the most subordinated claim in case of the liquidation of the Bank.

(2) The holder of the instrument is entitled to a claim on the residual assets that is proportional with its share of issued capital, after all senior claims have been repaid in liquidation. The claim must be unlimited and variable and must be neither fixed nor capped.

(3) The principal amount of the instrument is perpetual and never repayable except in liquidation. Discretionary repurchases and other discretionary means of reducing capital allowed by law do not constitute repayment.

(4) The Bank must not create an expectation at issuance that the instrument will be bought back, redeemed or cancelled. The statutory or contractual terms must not provide anything that might give rise to such an expectation.

(5) Distributions are paid out of distributable items of the Bank (including retained earnings) and the amount of distributions:

(a) is not tied or linked to the amount paid in at issuance; and

(b) is not subject to a contractual cap (except to the extent that a Bank may not pay distributions that exceed the amount of its distributable items).

(6) There are no circumstances under which the distributions are obligatory. Non-payment of distributions must not lead to default.

(7) Distributions are paid only after all legal and contractual obligations have been met and payments on all more senior capital instruments have been made. There are no preferential distributions to any pre-defined specified parties, including in relation to other CET1 Capital instruments and the terms of the instrument must not provide any preferential rights for payment of distributions.

(8) Compared to all the capital instruments issued by the Bank, the instrument must absorb the first and proportionately greatest share of any losses as they occur, and each instrument absorbs losses on a going-concern basis to the same degree as all other CET1 Capital instruments.

Note This criterion in (8) above would be considered as fulfilled if the instrument includes a permanent write-down mechanism, as referred in Rule 4.17 (11) and 4.20.

(9) The paid-up amount is recognised as equity capital (rather than as a liability) for determining balance-sheet insolvency.

(10) The paid-in amount is classified as equity in accordance with the relevant accounting standards.

(11) The instrument is directly issued and paid-in, and the Bank has not directly or indirectly funded the purchase of the instrument.

(12) The paid-in amount is neither secured nor covered by a guarantee of the Bank or a related party, nor subject to any other arrangement that legally or economically enhances the seniority of the holder's claim in relation to the claims of the Bank's creditors.

(13) The instrument is issued only with the approval of the owners of the Bank, either given directly by the owners or, if permitted by the applicable law, given by its Governing Body or by other persons authorised by the owners.

(14) The instrument is clearly and separately disclosed on the Bank's balance sheet.

4.16 Additional Tier 1 (AT1) Capital

AT 1 Capital is the sum of the following elements:

(a) instruments issued by a Bank that satisfy the criteria in Rule 4.17 for inclusion in AT1 Capital (and are not included in CET 1 Capital);

(b) share premium resulting from the issue of instruments included in AT1 Capital, according to (a) above, if any;

(c) instruments, issued by consolidated Subsidiaries of the Bank and held by third parties, that satisfy the criteria in Rule 4.23 for inclusion in AT1 Capital (and are not included in CET 1 Capital of the respective Banks);

(d) regulatory adjustments applied in the calculation of AT1 Capital in accordance with Rule 4.28.

4.17 Criteria for inclusion in AT1 Capital

A capital instrument is eligible for inclusion in AT1 Capital only if that instrument meets all of the following criteria in sub-rules (1) to (15):

(1) The instrument is issued and paid-up.

(2) The instrument is the most subordinated claim after those of depositors, general creditors and holders of the subordinated debt of the Bank.

(3) The instrument is neither secured nor covered by a guarantee of the Bank or a related party, nor subject to any other arrangement that legally or economically enhances the seniority of the holder's claim in relation to the claims of the Bank's creditors.

(4) The instrument is perpetual. It has no maturity date and there are no step-ups or other incentives to redeem.

(5) If the instrument is callable by the Bank, it can only be called 5 years or more after the instrument is paid-up and only with the approval of the AFSA. The Bank must not do anything to create an expectation that the exercise of the option will be approved, and, if the exercise is approved, the Bank:

(a) must replace the called instrument with capital of the same or better quality and at conditions sustainable for the income generation capacity of the Bank; or

(b) must demonstrate to the AFSA that its capital will exceed the Bank's minimum capital requirement after the call option is exercised.

(6) A repayment of principal through repurchase, redemption or other means must be approved by the AFSA. The Bank must not assume, or create a market expectation, that such approval will be given.

(7) In respect of the dividend or coupon payable on the instrument

(a) The Bank has full discretion at all times to cancel distributions or payments;

(b) Any cancellation of a dividend or coupon is not an event of default;

(c) The Bank has full access to cancelled payments to meet obligations as they fall due; and

(d) Any cancellation of dividend or coupon does not impose restrictions on the Bank, except in

relation to distributions to common shareholders.

(8) Dividends and coupons must be paid out of distributable items.

(9) The instrument must not have a credit-sensitive dividend feature under which a dividend or coupon is periodically reset based (wholly or partly) on the Bank's credit standing.

(10) The instrument must not contribute to the Bank's liabilities exceeding its assets if such a balance-sheet test forms part of any insolvency law applying in the jurisdiction where the instrument was issued.

(11) An instrument classified as a liability for accounting purposes must have principal loss absorption through conversion to common shares, or a write-down mechanism that allocates losses to the instrument, at a pre- specified trigger point. The conversion must be made in accordance with Rule 4.20.

(12) A write-down of the instrument has the following effects:

(a) reducing the claim of the instrument in liquidation;

(b) reducing the amount repaid when a call option is exercised;

(c) reducing or eliminating dividend or coupon payments on the instrument.

(13) Neither the Bank nor a related party over which the Bank exercises control or significant influence has purchased the instrument, nor has the Bank directly or indirectly funded the purchase of the instrument.

(14) The instrument has no features that hinder recapitalisation. For example, it must not require the Bank to compensate investors if a new instrument is issued at a lower price during a specified period.

(15) If the instrument is issued by a special purpose vehicle, the proceeds are immediately available without limitation to the Bank through an instrument that satisfies the other criteria for AT1 Capital.

4.18 Tier 2 Capital (T2 Capital)

T2 Capital is the sum of the following elements:

(a) instruments issued by the Bank that satisfy the criteria in Rule 4.19 for inclusion in T2 Capital (and are not included in T1 Capital);

(b) share premium resulting from the issue of instruments included in T2 Capital according to (a), if any;

(c) instruments, issued by consolidated Subsidiaries of the Bank and held by third parties, that satisfy the criteria in Rule 4.24 for inclusion in T2 Capital (and are not included in T1 Capital);

(d) regulatory adjustments applied in the calculation of T2 Capital in accordance with Rule 4.28;

(e) general provisions or general reserves held against future, presently unidentified losses (but only up to a maximum of 1.25% of risk-weighted assets for Credit Risk, calculated using the standardised approach in Chapter 5 of BBR).

Note General provisions and reserves are freely available to meet losses that subsequently materialise and therefore qualify for inclusion in T2 Capital. In contrast, provisions for identified deterioration

of particular assets or known liabilities, whether individual or grouped, must be excluded because they would not be available to meet losses.

4.19 Criteria for inclusion in T2 Capital

A capital instrument is eligible for inclusion in T2 Capital only if all the criteria in sub-rules (1) to (10) below are satisfied.

(1) The instrument is issued and paid up.

(2) The instrument is subordinated to the claims of depositors and general creditors.

(3) The paid-in amount is neither secured nor covered by a guarantee of the Bank or a related party, nor subject to any other arrangement that legally or economically enhances the seniority of the holder's claim in relation to the claims of the Bank's depositors and general creditors.

(4) The original maturity of the instrument is at least 5 years.

(5) The recognition in regulatory capital in the remaining 5 years before maturity is amortised on a straight line basis and there are no incentives to redeem.

(6) If the instrument is callable by the Bank, it can only be called 5 years or more after the instrument is paid-in and only with the approval of the AFSA. The Bank must not do anything to create an expectation that the exercise of the option will be approved, and, if the exercise is approved, the Bank:

(a) must replace the called instrument with capital of the same or better quality with servicing costs sustainable for the income capacity of the Bank; or

(b) must demonstrate to the AFSA that its capital will exceed the Bank's minimum capital requirement after the call option is exercised.

(7) The holder has no right to accelerate future scheduled payments of coupon or principal, except in bankruptcy or liquidation.

(8) The instrument does not have a credit-sensitive-dividend feature under which a dividend or coupon is periodically reset based (wholly or partly) on the Bank's credit standing.

(9) Neither the Bank nor a related party over which the Bank exercises control or significant influence has purchased the instrument, nor has the Bank directly or indirectly funded the purchase of the instrument.

(10) If the instrument is issued by a special purpose vehicle, the proceeds are immediately available without limitation to the Bank through an instrument that satisfies the other criteria for T2 Capital.

4.20 Requirements—loss absorption at point of non-viability

(1) This rule applies to an AT1 or T2 Capital instrument issued by a Bank. It sets out additional requirements to ensure loss absorption at the point of non-viability.

(2) The terms and conditions of an instrument must give the AFSA the discretion to direct that the instrument be written-off or converted to common equity on the happening of a Trigger event.

(3) The Bank must be able to issue the required number of shares specified in the instrument if a trigger event happens. The issuance of any new shares because of a trigger event must happen before any public sector injection of capital so that capital provided by the public sector is not

diluted.

(4) Trigger event, for the purposes of (2) above, in relation to the Bank that issued the instrument, is the earliest of:

(a) a decision of the AFSA that a write-off (without which the Bank would become non-viable) is necessary; and

(b) a decision by the relevant authority to make a public sector injection of capital, or give equivalent support (without which injection or support the Bank would become non-viable, as determined by that authority).

(5) If the Bank is a member of a financial group and the Bank wishes the instrument to be included in the Group's Capital in addition to its solo capital, the trigger event must be the earliest of:

(a) the decision in sub-rule (4) (a);

(b) the decision in sub-rule (4) (b);

(c) a decision, by the relevant authority in the Bank's home jurisdiction, that a write-off (without which the Bank would become non-viable) is necessary; and

(d) a decision, by the relevant authority in the jurisdiction of the financial regulator that regulates the parent entity of the Bank, to make a public sector injection of capital, or give equivalent support, in that jurisdiction (without which injection or support the Bank would become non-viable, as determined by that authority).

(6) Any compensation paid to the holder of an instrument because of a write-off must be paid immediately in the form of common shares.

(7) If the Bank is a member of a financial group, any common shares paid as compensation to the holder of the instrument must be common shares of the Bank or of the parent entity of the group.

Section 4C – Treatment of Minority interests

4.21 Introduction

This section sets out the criteria and formulae for the treatment of minority interests in a Bank's Regulatory Capital.

4.22 Criteria for third party interests— CET 1 Capital

(1) For Rule 4.14 (e), CET1 Capital issued by a consolidated Subsidiary of a Bank and held by a third party as a non-controlling interest, may be included in the Bank's CET 1 Capital if:

(a) the share would be included in the Bank's CET 1 Capital had it been issued by the Bank; and

(b) the Subsidiary that issued the share is itself a Bank or a Broker Dealer (or an equivalent entity in its home jurisdiction).

(2) The amount to be included in the consolidated CET 1 Capital of a Bank is calculated in accordance with the following formula:

$$\mathbf{NCI - ((CET1s - Min) \times SS)}$$

where:

NCI is the total of the non-controlling interests of minority shareholders in a consolidated Subsidiary of the Bank.

CET1s is the amount of CET 1 Capital of the Subsidiary.

Min is the lower of:

(a) 0.07 × total RWAs, as defined in Rule 4.7 (2), of the Subsidiary; and

(b) 0.07 × share of consolidated RWAs of the group attributable to the Subsidiary.

SS means the percentage of the shares in the Subsidiary (being shares included in CET 1 Capital) held by those third parties.

4.23 Criteria for third party interests—AT1 Capital

(1) For Rule 4.16 (c), an instrument (including a common share) issued by a consolidated Subsidiary of a Bank and held by a third party as a non-controlling interest may be included in the Bank's AT1 Capital if the instrument would be included in the Bank's AT1 Capital had it been issued by the Bank.

(2) Subject to (3), the amount to be included in the consolidated AT1 Capital of a Bank is calculated in accordance with the following formula:

NCI – ((T1s – Min) × SS)

where:

NCI is the total of the non-controlling interests of third parties in a consolidated Subsidiary of the Bank.

T1s is the amount of Tier 1 Capital of the Subsidiary.

Min is the lower of:

(a) 8.5% of the total RWAs, as defined in Rule 4.7 (2), of the Subsidiary; and

(b) 8.5% of the share of consolidated RWAs of the group attributable to the Subsidiary.

SS means the percentage of the shares in the Subsidiary (being shares included in additional Tier 1 Capital) held by those third parties.

(3) A Bank must determine the amount of qualifying T1 Capital of a Subsidiary that is included in consolidated AT1 Capital by excluding the minority interests of that Subsidiary that are included in consolidated CET1 Capital, in accordance with Rule 4.22.

4.24 Criteria for Minority interests— Tier 2 Capital

(1) For Rule 4.18 (c), an instrument (including common equity or any other T1 Capital instrument) issued by a consolidated Subsidiary of a Bank and held by a third party as a non-controlling interest may be included in the Bank's T2 Capital if the instrument would be included in the Bank's T2 Capital had it been issued by the Bank.

(2) The amount to be included in the consolidated T2 Capital of a Bank is calculated in accordance

with the following formula:

$$NCI - ((T2s - Min) \times SS)$$

where:

NCI is the total of the non-controlling interests of third parties in a consolidated Subsidiary of the Bank.

T2s is the amount of Tier 2 Capital of the Subsidiary.

Min is the lower of:

(a) 10.5% of the total RWAs, as defined in Rule 4.7 (2), of the Subsidiary; and

(b) 10.5% of the share of consolidated RWAs of the group attributable to the Subsidiary.

SS means the percentage of the shares in the Subsidiary (being shares included in Tier 2 Capital) held by those third parties.

(3) A Bank must determine the amount of qualifying Total Capital of a Subsidiary that is included in consolidated T2 Capital by excluding the minority interests of that Subsidiary that are included in consolidated CET1 Capital and consolidated AT1 Capital, in accordance with Rules 4.22 and 4.23.

4.25 Treatment of third party interests from special purpose vehicles

(1) An instrument issued out of a special purpose vehicle and held by a third party must not be included in a Bank's CET 1 Capital. Such an instrument may be included in the Bank's AT1 or T2 Capital (and treated as if it had been issued by the Bank itself directly to the third party), if:

(a) the instrument satisfies the criteria for inclusion in the relevant category of Regulatory Capital; and

(b) the only asset of the special purpose vehicle is its investment in the capital of the Bank and that investment satisfies the criterion in Rule 4.17 (15) or 4.19 (10) for the immediate availability of the proceeds.

(2) A capital instrument described in sub-rule (1) above that is issued out of a special purpose vehicle through a consolidated Subsidiary of a Bank may be included in the Bank's consolidated AT 1 or T2 Capital if the instrument satisfies the criteria in Rule 4.23 or 4.24, as the case requires. Such an instrument is treated as if it had been issued by the Subsidiary itself directly to the third party.

Section 4D Regulatory Adjustments

4.26 Valuation approaches and related adjustments

(1) A Bank must use the same approach for valuing regulatory adjustments to its capital as it does for balance-sheet valuations. An item that is deducted from capital must be valued in the same way as it would be for inclusion in the Bank's balance sheet.

(2) The Bank must use the corresponding deduction approach and the threshold deduction rule referred in Rules 4.29 and 4.30, in making adjustments to its capital.

4.27 Definitions for Section 4D

In this Section:

entity concerned means any of the following entities:

(a) a Bank;

(b) any other financial or insurance entity;

(c) an entity over which a Bank exercises control.

significant investment, by a Bank in an entity concerned, means an investment of 10% or more in the common shares, or other instruments that qualify as capital, of the entity concerned.

investment includes a direct, indirect and synthetic holding of capital instruments.

4.28 Adjustments to CET1 Capital

(1) Form of adjustments: Adjustments to CET 1 Capital must be made in accordance with this rule. Regulatory adjustments are generally in the form of deductions, but they may also be in the form of recognition or derecognition of items in the calculation of a Bank's capital.

(2) Goodwill and intangible assets: A Bank must deduct from CET 1 the amount of its goodwill and all other intangible assets (except mortgage servicing rights). The amount must be net of any related deferred tax liability that would be extinguished if the goodwill or assets become impaired or derecognised under IFRS or any other relevant accounting standards.

(3) Deferred tax assets:

(a) A Bank must deduct from CET 1 Capital the amount of deferred tax assets (except those that relate to temporary differences) that depend on the future profitability of the Bank.

(b) A deferred tax asset may be netted with a deferred tax liability only if the asset and liability relate to taxes levied by the same taxation authority and offsetting is explicitly permitted by that authority. A deferred tax liability must not be used for netting if it has already been netted against a deduction of goodwill, other intangible assets or defined benefit pension assets.

(4) Cash flow hedge reserve: In the calculation of CET 1 Capital, a Bank must derecognise the amount of the cash flow hedge reserve that relates to the hedging of items that are not fair valued on the balance sheet (including projected cash flows).

(5) Cumulative gains and losses from changes to own Credit Risk: In the calculation of CET 1 Capital, a Bank must not take into account any unrealised gains and unrealised losses that have resulted from changes in the fair value of liabilities that are due to changes in the Bank's own Credit Risk.

(6) Defined benefit pension fund assets:

(a) A Bank must deduct from CET 1 Capital the amount of a defined benefit pension fund that is an asset on the Bank's balance sheet. The amount must be net of any related deferred tax liability that would be extinguished if the asset becomes impaired or derecognised under IFRS or any other relevant accounting standards.

(b) The Bank may apply to the AFSA for approval to offset from the deduction any asset in the defined benefit pension fund to which the Bank has unrestricted and unfettered access. Such an asset must be assigned the risk-weight that would be assigned if it were owned directly by the Bank.

(7) Securitisation gains on sale: In the calculation of CET 1 capital, a Bank must derecognise any

increase in equity capital or CET 1 capital from a securitisation transaction (for example, an increase associated with expected future margin income resulting in a gain-on- sale).

(8) Higher capital imposed on overseas branch

(a) If a Bank has an overseas branch, the Bank must deduct from CET 1 capital whichever is the higher of any capital requirement imposed by the AFSA or the financial regulator in the jurisdiction in which the branch is located.

(b) This rule does not apply if the overseas branch is a consolidated entity of the Bank. A branch is a consolidated entity if it is included in the Bank's consolidated returns.

(c) Despite sub-rule (b) above, if the financial regulator in the jurisdiction in which a branch is located imposes a capital requirement for the foreign branch, a Bank must deduct from CET 1 capital the amount of any shortfall between the actual capital held by the foreign branch and that capital requirement.

(9) Assets lodged or pledged to secure liabilities

(a) A Bank must deduct from CET 1 capital the amount of any assets lodged or pledged by the Bank if:

(i) the assets were lodged or pledged to secure liabilities incurred by the Bank; and

(ii) the assets are not available to meet the liabilities of the Bank.

(b) The AFSA may determine that, in the circumstances, the amount of assets lodged or pledged need not be deducted from the Bank's CET 1 capital. The determination must be in writing.

(10) Acknowledgments of debt

(a) A Bank must deduct from CET 1 capital the net present value of an acknowledgement of debt outstanding issued by it to directly or indirectly fund instruments that qualify as CET 1 capital.

(b) This rule does not apply if the acknowledgement is subordinated in rank similar to that of instruments that qualify as CET 1 capital.

(11) Accumulated losses: A Bank must deduct from CET 1 Capital the amount of any accumulated losses.

4.29 Deductions from Regulatory Capital

(1) **Deductions using corresponding deduction approach:**

(a) The deductions that must be made from CET 1 capital, AT 1 capital or T2 capital under the corresponding deduction approach are set out in the sub-rules (2) to (7) of this rule. A Bank must examine its holdings of index securities and identify any underlying exposures to its own CET1, AT1 or T2 capital instruments in those index securities to determine whether any deductions are required as a result of such indirect holdings.

(b) Deductions must be made from the same Tier for which the capital would qualify if it were issued by the Bank itself or, if there is not enough capital at that category, from the next higher category.

(c) The corresponding deduction approach applies regardless of whether the positions or exposures are held in the Banking Book or Trading Book.

Note If the amount of T2 capital is insufficient to cover the amount of deductions required to be made from T2 capital, the shortfall must be deducted from AT1 capital and, if AT1 capital is still insufficient, the remaining amount must be deducted from CET 1 capital.

(2) Investments in own shares and capital instruments

(a) A Bank must deduct direct or indirect investments in its own common shares or own capital instruments (except those that have been derecognised under IFRS). The Bank must also deduct any of its own common shares or instruments that it is contractually obliged to purchase.

(b) The gross long positions may be deducted net of short positions in the same underlying exposure only if the short positions involve no counterparty risk. However, gross long positions in its own shares resulting from holdings of index securities may be netted against short positions in its own shares resulting from short positions in the same underlying index, even if those short positions involve counterparty risk.

(3) Reciprocal cross holdings**:** A Bank must deduct reciprocal cross holdings in shares, or other instruments that qualify as capital, of an entity concerned.

(4) Non-significant investments—where the Bank does not own more than 10% of issued common equity of the entity

(a) This rule applies if:

(i) a Bank makes a non-significant investment in an entity concerned;

(ii) the entity concerned is an unconsolidated entity (that is, the entity is not one that is included in the firm's consolidated returns);

(iii) the Bank does not own more than 10% of the common shares of the entity concerned; and

(iv) after applying all other regulatory adjustments, the total of the deductions required to be made under this rule is less than 10% of the Bank's CET 1 capital.

(b) A Bank must deduct any investments in common shares, or other instruments that qualify as capital, of an entity concerned.

(c) The amount to be deducted is the net long position (that is, the gross long position net of short positions in the same underlying exposure if the maturity of the short position either matches the maturity of the long position or has a residual maturity of at least 1 year).

(d) Underwriting positions held for more than 5 business days must also be deducted.

(e) If a capital instrument is required to be deducted and it is not possible to determine whether it should be deducted from CET 1 capital, additional tier 1 capital or tier 2 capital, the deduction must be made from CET 1 capital.

(5) Non-significant investments—aggregate is 10% or more of Bank's CET 1 capital

(a) This rule applies if, after applying all other regulatory adjustments, the total of the deductions required to be made under Rule 4.29 (4) is 10% or more of the Bank's CET 1 Capital.

(b) A Bank must deduct the amount by which the total of the deductions required to be made under Rule 4.29 (4) exceeds 10% of the Bank's CET 1 Capital. This amount to be deducted is referred to as the excess.

(c) How much of the excess gets to be deducted from each category of regulatory capital under the corresponding deduction approach is calculated in accordance with the following formula:

$$Excess * \frac{A}{B}$$

where:

A is the amount of CET 1 capital, additional tier 1 capital or tier 2 capital of the Bank, as the case may be;

B is the total capital holdings of the Bank.

(6) Significant investments

(a) This rule applies if:

(i) a Bank makes a significant investment in an entity concerned;

(ii) the entity concerned is an unconsolidated entity (that is, the entity is not one that is included in the Bank's consolidated returns); and

(iii) the Bank owns 10% or more of the common shares of the entity concerned.

(b) A Bank must deduct the total amount of investments in the entity concerned (other than investments in common shares, or other instruments that qualify as CET 1 capital, of the entity).

(c) The amount to be deducted is the net long position (that is, the gross long position net of short positions in the same underlying exposure if the maturity of the short position either matches the maturity of the long position or has a residual maturity of at least 1 year).

(d) Underwriting positions held for more than 5 business days must also be deducted.

(e) If a capital instrument is required to be deducted and it is not possible to determine whether it should be deducted from CET 1 capital, AT1 capital or T2 capital, the deduction must be made from CET 1 capital.

(7) Banks may use estimates or exclude deductions

(a) If it is impractical for a Bank to examine and monitor the Bank's exposures to the capital of entities concerned (including through holdings of indexed securities), the Bank may apply to the AFSA for approval to use an estimate of such exposures. The AFSA will grant such an approval only after the Bank satisfies the AFSA that the estimate is conservative, well-founded and reasonable.

(b) A Bank may also apply to the AFSA for approval not to deduct an investment made to resolve, or provide financial assistance to reorganise, a distressed entity.

4.30 Deductions from CET1 Capital

(1) In addition to the other deductions to CET 1 Capital under this Chapter, deductions may be

required to CET 1 Capital under the threshold deduction rule.

(2) The threshold deduction rule provides recognition for particular assets that are considered to have some limited capacity to absorb losses. The following items come within the threshold deduction rule:

(a) significant investments in the common shares, or other instruments that qualify as CET 1 Capital, of an unconsolidated entity concerned;

(b) mortgage servicing rights;

(c) deferred tax assets that relate to temporary differences (for example, allowance for credit losses).

(3) Instead of full deduction, the items that come within the threshold deduction rule receive limited recognition when calculating CET 1 Capital. The total of each of the items in sub-rule (2) do not require adjustment from CET 1 Capital and are risk-weighted at 300% (for items listed on a regulated exchange) or 400% (for items not so listed) provided that:

(a) each item is no more than 10% of the Bank's CET 1 Capital (net of all regulatory adjustments except those under this Subdivision); or

(b) in total, the 3 items are no more than 15% of the Bank's CET 1 Capital (net of all regulatory adjustments except those under this Subdivision).

(4) A Bank must deduct from CET 1 Capital any amount in excess of the threshold in sub-rule (3) (a) or (b) above.

Section 4E Capital Buffers

4.31 Capital Conservation Buffer

(1) A Bank whose risk-based capital requirement is higher than its base capital requirement must maintain a minimum Capital Conservation Buffer of:

(a) 2.5% of the Bank's total risk-weighted assets; or

(b) a higher amount that the AFSA may, by written notice, set from time to time.

(2) A Bank's capital conservation buffer must be made up of CET 1 Capital above the amounts used to meet the Bank's CET 1 Capital ratio, T1 Capital ratio and Total Capital ratio in Rule 4.12.

4.32 Capital conservation ratios

(1) If a Bank's capital conservation buffer falls below the required minimum, the Bank must immediately conserve its capital by restricting its distributions.

(2) This rule sets out, in column 3 of table 4A below, the minimum capital conservation ratios for Banks that are required to maintain a capital conservation buffer. Capital conservation ratio is the percentage of earnings that a Bank must not distribute if its CET 1 capital ratio falls within the corresponding ratio in column 2 of that table.

(3) A Bank must have adequate systems and controls to ensure that the amount of distributable profits and maximum distributable amount are calculated accurately. The Bank must be able to demonstrate that accuracy if directed by the AFSA.

(4) If the Bank is a member of a financial group, the capital conservation buffer applies at group level.

Table 4A Minimum capital conservation ratios

column 1 item	column 2 CET1 capital ratio	column 3 capital conservation ratio (% of earnings)
1	4.5% to 5.125%	100
2	≥5.125% to 5.75%	80
3	≥5.75% to 6.375%	60
4	≥6.375% to 7.0%	40
5	>7%	0

4.33 Powers of the AFSA

(1) The AFSA may impose a restriction on capital distributions by a Bank even if the amount of the Bank's CET 1 Capital is greater than its CET 1 Capital ratio and required capital conservation buffer.

(2) The AFSA may, by written notice, impose a limit on the period during which a Bank may operate within a specified capital conservation ratio.

(3) A Bank may apply to the AFSA to make a distribution in excess of a limit imposed by this Chapter. The AFSA will grant approval only if it is satisfied that the Bank has appropriate measures to raise capital equal to, or greater than, the amount the Bank wishes to distribute above the limit.

4.34 Capital reductions

(1) A Bank must not reduce its capital and reserves without the AFSA's written approval.

(2) A Bank planning a reduction must prepare a forecast (for at least 2 years) showing its projected capital after the reduction. The Bank must satisfy the AFSA that the Bank's capital will still comply with these rules after the reduction.

4.35 The AFSA can require other matters

Despite anything in these rules, the AFSA may require a Bank to have capital resources, comply with any other capital requirement or use a different approach to, or method for, capital management. The AFSA may also require a Bank to carry out stress- testing at any time.

Section 4F Leverage Ratio

4.36 Application

The rules in this section apply only to Banks. For the sake of clarity, the rules in this section apply only to Banks licensed by the AFSA to conduct the Regulated Activity of "Accepting Deposits".

4.37 Calculation of Leverage Ratio

(1) A Bank must calculate its Leverage Ratio in accordance with the following formula:

$$Leverage\ Ratio = \frac{Capital\ Measure}{Exposure\ Measure}$$

Where:

(a) "Capital Measure" represents T1 Capital of the Bank calculated in accordance with Rule 4.13; and

(b) "Exposure Measure" represents the value of exposures of the Bank calculated in accordance with (2) of this rule.

(2) For the purpose of determining the Exposure Measure, the value of exposures of a Bank must be calculated in accordance with the International Financial Reporting Standards (IFRS) subject to the following adjustments:

(a) on-balance sheet, non-derivative exposures must be net of specific allowances and valuation adjustments (e.g. credit valuation adjustments);

(b) physical or financial collateral, guarantees or Credit Risk mitigation purchased must not be used to reduce on-balance sheet exposures; and

(c) loans must not be netted with deposits.

Note Detailed guidance specifying the methodologies, parameters and formulae for calculating the Leverage Ratio are set out in Section D of Chapter 4 of the Banking Prudential Guideline (BPG) issued by the AFSA.

CHAPTER 5 Credit Risk and Concentration Risk

Part I Credit Risk

Introduction

Guidance

(1) This chapter sets out the regulatory requirements in respect of managing the Credit Risk exposures of a Bank. Credit Risk refers to the risk of incurring losses due to failure on the part of a borrower or a counterparty to fulfil their obligations in respect of a financial transaction. This chapter aims to ensure that a Bank holds sufficient regulatory capital of a quality, acceptable to the AFSA, so that it can absorb unexpected losses arising out of its Credit Risk exposures, should the need arise and continue to operate in a sustainable manner.

(2) This chapter requires a Bank to:

(a) implement a comprehensive Credit Risk management framework to manage, measure and monitor Credit Risk commensurate with the nature, scale and complexity of its operations;

(b) calculate the Credit Risk Capital Requirement for its on-balance sheet and off- balance sheet credit exposures after adjusting for applicable levels of Credit Risk mitigation, according to the norms, methodologies, standards and guidance provided in the BPG issued by the AFSA;

(c) implement a sound framework for managing concentration risk and large exposures, including limits for concentration of such exposures to individual and group borrowers.

(3) This Chapter also deals with the following elements of determination of regulatory capital requirements to support a Bank's Credit Risk exposures:

(a) the risk-weighted assets approach;

(b) Credit Risk Mitigation (CRM) techniques;

(c) provisioning requirements for impaired assets of the Bank.

(4) To guard against abuses and to address conflicts of interest, this Chapter requires transactions with related parties to be at arm's length.

(5) The detailed requirements specifying the calculation methodologies, parameters, metrics and formulae in respect of the primary Credit Risk management and Credit Risk capital requirements outlined in this Chapter are provided in the Banking Prudential Guideline (BPG) issued by the AFSA. The BPG also provides detailed guidance on calculation methodologies, formulae, parameters and norms involved in calculation of Credit Risk capital requirements which is an element used to calculate the capital ratios for a Bank, as set out in Chapter 4 of BBR. It is suggested that this Chapter of the BBR, be read in conjunction with Chapter 5 of the BPG issued by the AFSA to facilitate understanding of the regulatory requirements and compliance with them.

5.1 Credit Risk Management – Systems and Controls

(1) A Bank must implement and maintain comprehensive Credit Risk management systems and controls which:

(a) are appropriate to the Bank's type, scope, complexity and scale of operations;

(b) enable the Bank to effectively identify, assess, monitor, mitigate and control Credit Risk and

to ensure that adequate Capital is available to support the Credit Risk exposures assumed; and

(c) ensure effective implementation of the Credit Risk strategy and policy.

(2) A Bank must:

(a) identify, assess, monitor, mitigate and, control its Credit Risk; and

(b) implement and maintain a prudent Credit Risk management policy which enables it to identify, assess, monitor, control and mitigate its Credit Risk.

(3) The Credit Risk management policy must:

(a) be documented and approved by its governing body;

(b) include the Bank's risk appetite for Credit Risk;

(c) be appropriate to the nature, scale and complexity of its activities and for its risk profile;

(d) must establish procedures, systems, processes, controls and approaches to identify, measure, evaluate, manage and control or mitigate its Credit Risk and to ensure the integrity of its Credit Risk management;

(e) must set out the organizational structure, and must define the responsibilities and roles, for managing Credit Risk;

(f) ensure that its risk management framework including but not limited to tools, methodologies and, systems enable it to implement its Credit Risk management policy; and

(g) be reviewed and updated at a reasonable frequency, but at least on an annual basis.

(4) A Bank's Credit Risk management policy must establish:

(a) a well-documented and effectively-implemented process for assuming Credit Risk that does not rely unduly on external credit assessments;

(b) well-defined criteria for approving credit (including prudent underwriting standards), and renewing, refinancing and restructuring existing credit;

(c) a process for identifying the approving authority for credit, given its size and complexity;

(d) effective Credit Risk administration, including:

(i) regular analysis of counterparties' ability and willingness to repay; and

(ii) monitoring of documents, legal covenants, contractual requirements, and collateral and other Credit Risk Mitigation techniques;

(e) effective systems for the accurate and timely identification, measurement, evaluation, management and control or mitigation of Credit Risk, and reporting to the Bank's Governing Body and senior management;

(f) prudent and appropriate credit limits that are consistent with the Bank's risk tolerance, risk profile and capital;

(g) provide for process and criteria for identification and recognition of problem assets as well as systems for measurement and reporting of problem assets;

(h) the criteria and responsibility for Credit Risk reporting, and the scope, manner and frequency of reporting, to the Governing Body or a committee of the governing body;

(i) establish, and must provide for the regular review of, the Bank's Credit Risk tolerance and credit exposure limits to control credit exposures of the Bank;

(j) procedures for tracking and reporting exceptions to credit limits and deviations from Credit Risk management policies; and

(k) effective controls for the quality, reliability and relevance of data and validation procedures.

Note Guidance in respect of the contents of a Bank's Credit Risk management policy which is required to satisfy the regulatory requirement in the Rule 5.1 is provided in Chapter 5 of the BPG issued by the AFSA.

(5) A Bank's Credit Risk management policy must ensure that credit decisions are free of conflicts of interest and are made on an arm's-length basis. In particular, the credit approval and credit review functions must be independent of the credit initiation function.

(6) A Bank's Credit Risk management policy must provide for monitoring the total indebtedness of each counterparty and any risk factors that might result in default (including any significant unhedged foreign exchange risk).

(7) A Bank must give the AFSA full access to information about its credit portfolio. The Bank must also give the AFSA access to staff involved in assuming, managing, controlling and reporting on Credit Risk.

(8) The Credit Risk management policy must enable the Bank to carry out stress-tests on its credit portfolio at intervals appropriate for the nature, scale and complexity of the Bank's business and using various scenarios based on appropriate assumptions. The policy must take into account the Bank's Credit Risk profile (including on-balance-sheet and off-balance-sheet exposures) and tolerance in the context of the markets and macroeconomic conditions in which the Bank operates. The Bank's Credit Risk stress testing must include procedures to make any changes to its Credit Risk management framework based on the results from the stress testing.

Note Guidance in respect of a Bank's policies for Credit Risk assessment which is required to satisfy the regulatory requirement in the Rule 5.1 is provided in paragraphs 10 and 11 of Chapter 5 of the BPG issued by the AFSA.

5.2 Role of Governing Body—Credit Risk

(1) A Bank's Governing Body must ensure that its Credit Risk management policy enables it to obtain a comprehensive bank-wide view of its Credit Risk exposures and covers the full credit lifecycle including credit underwriting, credit evaluation, and the Credit Risk management of the Bank's trading activities.

(2) A Bank must ensure that its Governing Body is responsible for monitoring the nature and level of Credit Risk assumed by it and for monitoring the Credit Risk management process.

(3) The Governing Body of the Bank must also ensure that:

(a) an appropriate senior management structure with clearly defined responsibilities and roles for Credit Risk management and for compliance with the Bank's Risk strategy, is established

and maintained;

(b) the Credit Risk management framework is consistent with the Bank's risk profile and its systemic importance.

(c) the Bank's senior management and other relevant staff have the necessary experience to manage Credit Risk and to effectively implement the Credit Risk management policy;

(d) appropriate Credit limits covering Credit Risk management in both day-to-day and stressed conditions are set;

(e) stress-tests, funding strategies, contingency funding plans and holdings of high-quality liquid assets are effective and appropriate for the Bank;

(f) the Bank's senior management:

(i) develops a Credit Risk management policy in accordance with the Bank's Credit Risk tolerance;

(ii) monitors the Bank's Credit Risk profile and reports to the Governing Body regularly;

(iii) determines, and sets out in the Bank's Credit Risk management policy, the structure, responsibilities and controls for managing Credit Risk and for overseeing the Credit Risk of all legal entities, branches and subsidiaries in the jurisdictions in which the Bank is active; and

(iv) monitors trends and market developments that could present significant, unprecedented or complex challenges for managing Credit Risk so that appropriate and timely changes to the Credit Risk management policy can be made.

(4) The Governing Body must regularly review reports on the Bank's Credit Risk profile and portfolio returns and, where necessary, information on new or emerging problem assets. The Governing Body of the Bank must also review the Credit Risk tolerance and strategy at least on an annual basis.

(5) The Governing Body must approve:

(a) the Bank's Credit Risk management policy; and

(b) its Credit Risk tolerance and risk strategy.

5.3 Classification of Credit exposures

(1) Unless a Bank has established something more detailed, the Bank must classify credits into 1 of the 5 categories in table 5A. Nothing in the table prevents a Bank from classifying a credit under a higher risk category than the table requires.

(2) Unless there is good reason not to do so, the same category must be given to all credit exposures to the same counterparty.

Table 5A Categories of credit

Column 1 Item	Column 2 Category	Column 3 Description

1	performing	In this category, there is no uncertainty about timely repayment of the outstanding amounts. This category comprises credits that are currently in regular payment status with prompt payments.
2	special mention	This category comprises: (a) credits with deteriorating or potentially deteriorating credit quality that may adversely affect the counterparty's ability to make scheduled payments on time; (b) credits that are 30 to 90 days in arrears; (c) credits showing weakness arising from the customer's financial position; (d) credits affected by market circumstances or any other industry- related concerns; and (e) credits that have been restructured and are not classified into a higher risk category.
3	substandard	This category comprises: (a) credits that show definite deterioration in credit quality and impaired repayment ability of the counterparty; and (b) credits that are 91 to 180 days in arrears.
4	doubtful	This category comprises: (a) credits that show significant credit quality deterioration, worse than those in the substandard category, to the extent that the prospect of full recovery of all the outstanding amounts is questionable and the probability of a credit loss is high (though the exact amount of loss cannot be determined yet); and (b) credits that are 181 to 270 days in arrears.
5	loss	This category comprises: (a) credits that are assessed as uncollectable; (b) credits where the probability of recovering the amount due is very low; and (c) credits that are more than 270 days in arrears.

5.4 Problem Assets and Impaired Assets

(1) A Bank's Credit Risk management policy must facilitate the Bank's collection of past-due obligations, and its management of problem assets through:

(a) monitoring of their credit quality;

(b) early identification and ongoing oversight; and

(c) review of their classification, provisioning and write-offs.

(2) The refinancing of a special mention or impaired credit must not be used to reclassify the credit to a more favourable category.

(3) The AFSA may require a special mention credit to be managed individually, and may set a higher level of provision for the credit, if the AFSA is of the view that market circumstances or any other industry-related concerns require such action.

5.5 Using ratings from External Credit Rating Agencies (ECRAs)

(1) A Bank must use only a solicited Credit Risk rating determined by an ECRA in determining the risk-weights for the Bank's exposures. The Bank must use the ratings determined by an ECRA consistently and in accordance with these rules and its Credit Risk management policy.

(2) If there is only one assessment by an ECRA for a particular claim or asset, that assessment must be used to determine the risk-weight of the claim or asset. If there are two assessments by ECRAs and the assessments map into different risk weights, the higher risk-weight must be applied. If there are three or more assessments with different risk weights, the assessments corresponding to the two lowest risk-weights should be referred to, and the higher of those two risk-weights must be applied.

(3) If a Bank invests in an instrument with an issue-specific rating, the risk-weight to be applied to the instrument must be based on that rating.

(4) If the Bank invests in an unrated instrument and the issuer of the instrument is assigned a rating that results in a lower risk-weight than the risk-weight normally applied to an unrated position, the Bank may apply the lower risk-weight to the instrument but only if the claim for the instrument has the same priority as, or is senior to, the claims to which the issuer rating relates. If the instrument is junior to the claims to which the issuer rating relates, the Bank must apply the risk-weight normally applied to an unrated position.

(5) If the Bank invests in an unrated instrument and the issuer of the instrument is assigned a rating that results in a higher risk-weight than the risk-weight normally applied to an unrated position, the Bank must apply the higher risk-weight to the instrument if the claim for that instrument has the same priority as, or is junior to, the claims to which the issuer rating relates.

(6) A Bank must not use a Credit Risk rating for one entity in a Financial Group to determine the risk-weight for an unrated entity in the same Financial Group. If the rated entity has guaranteed the unrated entity's exposure to the Bank, the guarantee may be recognised for risk- weighting purposes if it satisfies the criteria set out in this Chapter on Guarantees.

(7) If an issuer rating is assigned to a counterparty and a Bank applies a risk-weight to an unrated position based on the rating of an equivalent exposure to the same counterparty:

(a) the Bank must use that counterparty's domestic-currency rating for any exposure denominated in the currency of the counterparty's place of residence or incorporation; and

(b) the Bank must use that counterparty's foreign-currency rating for any exposure denominated in a foreign currency.

(8) A short-term Credit Risk rating must be used only for short-term claims relating to banks and

corporations (such as those arising from the issuance of commercial paper). The rating is taken to be issue-specific and must be used only to assign risk-weights for claims arising from a rated facility.

(9) If a short-term rated exposure is assigned a risk-weight of 50%, an unrated short-term exposure to the same counterparty cannot be assigned a risk-weight lower than 100%. If a short-term facility of an issuer is assigned a risk-weight of 150% based on the facility's Credit Risk rating, all unrated claims of the issuer (whether long-term or short-term) must be assigned a risk-weight of 150%.

5.6 Calculation of Risk-Weighted Assets (RWAs)

(1) A Bank must apply risk-weights to all of its on-balance-sheet and off-balance-sheet asset items using the Risk-Weighted Assets method, defined in this Rule.

(2) If a claim or asset to which a risk-weight must be applied by a Bank is secured by eligible financial collateral or a guarantee (or there is mortgage indemnity insurance, or a credit derivative instrument or netting agreement), the Credit Risk Mitigation techniques allowed in this Chapter may be used to reduce the Bank's Credit Risk capital requirement.

(3) A Bank must not rely only on a rating determined by an ECRA to assess the risks associated with an exposure. The Bank must also carry out its own Credit Risk assessment of each exposure (rated or unrated) to determine whether the risk-weights applied to each of them are appropriate. The determination must be based on each exposure's inherent risk.

(4) If there are reasonable grounds to believe that the inherent risk of an exposure is significantly higher than that implied by the risk-weight assigned to it, the Bank must consider the higher risk (and apply a higher risk-weight) in calculating the Credit Risk capital requirement.

(5) A Bank must take into account all commitments in calculating its Credit Risk capital requirement, whether or not those commitments contain material adverse change clauses or other provisions that are intended to relieve the Bank of its obligations under particular conditions.

(6) Notwithstanding the provisions of these rules, the AFSA may determine the risk-weighted amount of a particular on-balance-sheet or off-balance-sheet Exposure of a Bank, if the AFSA considers that the Bank has not risk-weighted the Exposure appropriately. Such a determination must be issued by the AFSA, in writing.

(7) The AFSA may also impose specific capital requirements or limits on significant risk exposures, including those that the AFSA considers have not been adequately transferred or mitigated.

5.7 Calculation of RWAs – for On-Balance Sheet Exposures

(1) A Bank's total RWAs for its on-balance-sheet items must be calculated as the sum of the risk-weighted amounts of each of its on-balance-sheet items.

(2) The RWA of an on-balance-sheet item must be calculated by multiplying its exposure (after taking into account any applicable Credit Risk Mitigation) by the applicable risk-weight in table 5B.

(3) If column 3 of table 5B states that the risk weight is "based on ECRA rating" for a particular asset, the applicable risk-weight for that asset item must be derived from the table 5C. If a claim or asset's risk-weight is to be based on the ECRA rating and there is no such rating from an ECRA, the Bank must apply the risk-weight in the last column of table 5C.

Table 5B Risk-weights for on-balance-sheet items

Column 1 Item	Column 2 Description of Assets or Items	Column 3 Risk-Weight (%)
1	cash	
	(a) notes, gold bullion	0
	(b) cash items in the process of collection	20
2	claims on sovereigns	0
	(a) claims on Kazakhstan including National Bank of Kazakhstan	0
	(b) claims on other sovereigns including respective central banks	based on ECRA rating
3	claims on public sector enterprises:	
	(a) claims on non-commercial public sector enterprises in Kazakhstan	0
	(b) claims on other sovereign non- commercial public sector enterprises	based on ECRA rating
	(c) claims on commercial public sector enterprises	based on ECRA rating
4	claims on multilateral development banks:	
	(a) claims on multilateral development banks eligible for 0% risk-weight	0
	(b) claims on other multilateral development banks	based on ECRA rating
5	claims on banks (financial undertakings)	
	(a) claims on banks with an original maturity of more than 3 months	based on ECRA rating
	(b) claims on banks with an original maturity of 3 months or less	based on ECRA rating
6	claims on securities and investment entities	
	(a) claims on securities and investment entities that are subject to capital requirements similar to banks	based on ECRA rating
	(b) claims on securities and investment entities that are not subject to capital requirements similar to banks	based on ECRA rating

7	claims on corporates	based on ECRA rating
8	claims on small and medium enterprises	100
9	claims on securitisation exposures	based on ECRA rating
10	claims secured against mortgages	
	(a) residential mortgages	
	(i) if the loan-to-value ratio is 0% to 80%	35
	(ii) if the loan-to-value ratio is more than 80% but less than 100%	75
	(iii) if the loan-to-value ratio is 100% or more	100
	(b) commercial mortgages	100
11	Unsettled and failed transactions— delivery-versus-payment transactions:	
	(a) 5 to 15 days	100
	(b) 16 to 30 days	625
	(c) 31 to 45 days	937.5
	(d) 46 or more days	1250
12	Unsettled and failed transactions—non-delivery-versus-payment transactions	100
13	Investments in funds	
	(a) rated funds	based on ECRA rating
	(b) unrated funds that are listed	100
	(c) unrated funds that are unlisted	150
14	Equity exposures	
	(a) equity exposures that are not deducted from capital and are listed on a regulated exchange	300

	(b) equity exposures that are not deducted from capital and are not listed on a regulated exchange	400
15	Investment property	150
16	all other items	100

Table 5C Risk-weights based on ratings determined by ECRAs

Note In table 5C, the ratings are shown according to Standard & Poor's conventions. If a claim or asset is not rated by Standard & Poor's, its rating must be mapped to the equivalent Standard & Poor's rating.

item	description of claim or asset	AAA to AA-	A+ to A-	BBB+ to BBB-	BB+ to BB-	B+ to B-	below B-	unrated
1	claims on other sovereigns including central bank	0	20	50	100	100	150	100
2	claims on other sovereign non-commercial public sector enterprises -	20	50	100	100	100	150	100
3	claims on commercial public sector enterprises	20	50	100	100	100	150	100
4	claims on multilateral development banks not eligible for 0% risk- weight	20	50	50	100	100	150	50
5	claims on banks with an original maturity of more than 3 months	20	50	50	100	100	150	50
6	claims on banks with an original maturity of 3 months or less	20	20	20	50	50	150	20
7	claims on securities and investment entities that are subject to capital requirements similar to banks	20	50	50	100	100	150	50
8	claims on securities and investment entities that are not subject to capital requirements similar to banks	20	50	100	100	150	150	100
9	claims on corporates	20	50	100	100	150	150	100
10	securitisation exposures	50	100	100	150	150	250	150

11	investments in rated funds	20	50	100	100	150	150	n/a

5.8 Specialised lending

A specialised lending exposure is risk-weighted one rating less favourable than the rating that would apply, under table 5C, to the counterparty to the transaction (or to the party to whom that counterparty has the right of recourse).

5.9 Risk-weights for unsecured part of claim that is past due for more than 90 days

(1) The risk-weight for the unsecured part of a claim (other than a claim secured by an eligible residential mortgage) that is past due for more than 90 days is:

(a) 150% if the specific provisions are less than 20% of the past due claim;

(b) 100% if the specific provisions are 20% or more, but less than 50%, of the past due claim; or

(c) 50% if the specific provisions are 50% or more of the past due claim.

(2) The risk-weight for the unsecured part of a claim secured by an eligible residential mortgage that is past due for more than 90 days is:

(a) 100% if the specific provisions are less than 20% of the past due claim; or

(b) 50% if the specific provisions are 20% or more of the past due claim.

5.10 Calculation of RWAs – for Off-Balance Sheet Exposures

(1) A Bank's total risk-weighted off-balance-sheet items is the sum of the risk-weighted amounts of its market-related and non- market-related off-balance-sheet items. An off-balance-sheet item must be converted to a credit equivalent amount before it can be risk- weighted.

(2) The risk-weighted amount of an off-balance-sheet item is calculated using the following steps in the same sequence:

(a) convert the notional principal amount of the item to its on-balance-sheet equivalent (credit equivalent amount).

(b) multiply the resulting credit equivalent amount by the risk-weight in table 5B or 5C, as applicable to the claim or asset.

(3) A Bank must include derivatives and all market-related off-balance-sheet items (including on-balance-sheet unrealised gains on market-related off-balance-sheet items) in calculating its risk-weighted credit exposures. A market-related item must be valued at its current market price.

5.11 Credit equivalent amounts for market-related items

(1) A Bank must calculate the credit equivalent amount of each of its market-related items. Unless the item is covered by an eligible netting agreement, the credit equivalent amount of a market- related off-balance-sheet item is the sum of the current credit exposure and the potential future credit exposure from the item.

(2) The procedure, formula and the credit conversion factors for this rule are provided in Section E (14) of Chapter 5 of the BPG.

(3) Potential future credit exposure must be based on an effective, rather than an apparent, notional principal amount. If the stated notional principal amount of an item is leveraged or enhanced by the structure of the item, the Bank must use the effective notional principal amount in calculating the potential future credit exposure. No potential future credit exposure is calculated for a single-currency floating/floating interest rate swap. The credit exposure from such an interest rate swap must be based on mark-to-market values.

5.12 Calculation of credit equivalent amounts

(1) Credit conversion factors for items with terms subject to reset: In case of an item structured to settle outstanding exposures after specified payment dates on which the terms are reset (that is, the mark- to-market value of the item becomes zero on the specified dates), the period up to the next reset date must be taken as the item's residual maturity. For an interest rate item of that kind that is taken to have a residual maturity of more than 1 year, the credit conversion factor to be applied must not be less than 0.5% even if there are reset dates of a shorter maturity. For an item with 2 or more exchanges of principal, the credit conversion factor must be multiplied by the number of remaining exchanges under the item.

(2) The procedure, formula and the credit conversion factors for the calculation of risk-weighted assets for single-name swaps are detailed in Section E (15) of Chapter 5 of the BPG.

(3) A Bank must calculate the credit equivalent amount of each of its non-market-related items. The procedure, formula and the credit conversion factors for the calculation of risk-weighted assets for single-name swaps are detailed in Section E (16) of Chapter 5 of the BPG.

(4) In calculating the credit equivalent amount of a non-market-related off- balance-sheet item that is an undrawn (or partly drawn) commitment, a Bank must use the undrawn amount of the commitment.

(5) For an irrevocable commitment to provide an off-balance-sheet facility, the original maturity must be taken to be the period from the commencement of the commitment until the associated facility expires.

5.13 Policies—foreign exchange rollovers

(1) A Bank must have policies for entering into and monitoring rollovers on foreign exchange transactions and the policies must restrict the Bank's capacity to enter into such rollovers. The Bank must notify the AFSA if it enters into a rollover in breach of its policy. Such rollovers must be approved by the Governing Body of the Bank. The AFSA may direct how the rollover is to be treated for capital adequacy purposes.

(2) A bank should have systems and controls to identify, monitor, control and report off-market transactions.

(3) The Bank must not enter into a transaction at an off-market price, unless the transaction is a historical rate rollover on a foreign exchange transaction. A historical rate rollover on a foreign exchange transaction may be entered into at an off-market price (instead of current market price).

Credit Risk Mitigation

5.14 Requirements—Credit Risk Mitigation techniques

(1) A Bank's Credit Risk management policy must set out the conditions under which Credit Risk Mitigation techniques may be used. The policy must enable the Bank to manage Credit Risk Mitigation techniques and the risks associated with their use.

(2) The Bank must analyse the protection given by Credit Risk Mitigation techniques to ensure that any residual Credit Risk is identified, measured, evaluated, managed and controlled or mitigated. If the Bank accepts collateral, its policy must state the types of collateral that it will accept, and the basis and procedures for valuing collateral.

(3) If the Bank uses netting agreements, it must have a netting policy that sets out its approach. The netting policy must provide for monitoring netting agreements and must enable the Bank to monitor and report netted transactions on both gross and net bases.

(4) To obtain capital relief, the Credit Risk Mitigation technique and every document giving effect to it must be binding on all parties and enforceable in all the relevant jurisdictions. A Bank must review the enforceability of a Credit Risk Mitigation technique that it uses. The Bank must have a well-founded legal basis for any conclusion about enforceability and must carry out further reviews to ensure that the technique remains enforceable.

(5) The effects of a Credit Risk Mitigation technique must not be double-counted. The Bank is not allowed to obtain capital relief if:

(a) the risk-weight for the claim or asset is based on an issue-specific rating; and

(b) the ECRA that determined the rating had taken the technique into consideration in doing so.

5.15 Standard haircuts for Credit Risk Mitigation calculations

(1) A Bank must use the standard haircuts (expressed in percentages) set out in this rule in any calculation relating to Credit Risk mitigation. The haircuts are applied after risk mitigation to calculate adjusted exposures and are intended to take into account possible future price fluctuations.

(2) In table 5 D:

other issuers include banks, corporates, and public sector enterprises that are not treated as sovereigns.

sovereign includes a multilateral development bank, and a non- commercial public sector enterprise, that has a zero per cent risk-weight.

Table 5 D Haircuts for debt securities

column 1 item	column 2 credit rating for debt securities	column 3 residual maturity %	column 4 sovereigns %	column 5 other issuers %
1	AAA to AA-/A-1 (long-term and short-term)	≤1 year	0.5	1
		>1 year, ≤ 5 years	2	4
		> 5 years	4	8
2	A+ to BBB-/ A-	≤1 year	1	2

	2/A-3/P-3 (long- term and short- term) and unrated bank securities that are eligible financial collateral	>1 year, ≤ 5 years	3	6
		> 5 years	6	12
3	BB+ to BB- (long-term)	All	15	Not applicable
4	securities issued by the Republic of Kazakhstan or the National Bank of Kazakhstan	≤1 year	1	Not applicable
		>1 year, ≤5 years	3	Not applicable
		>5 years	6	Not applicable

Note Table 5 D item 3, column 5: securities rated BB+ or below are eligible financial collateral only if issued by a sovereign or non-commercial public sector enterprise—see Rule 5.17 (1) (c) (i).

Table 5 E Haircuts for other instruments

Column 1 item	Column 2 Description of assets	Column 3 Haircut (%)
1	main index equities (including convertible bonds) and gold	15
2	other equities (including convertible bonds) listed on a regulated exchange	25
3	units in listed trusts, undertakings for collective investments in transferable securities (***UCITS***), mutual funds and tracker funds	highest haircut applicable to any security in which the entity can invest
4	cash collateral denominated in the same currency as the collateralised exposure	0

(3) The procedure, formulas and the methods for the calculation of haircuts for Credit Risk Mitigation techniques with various types of currency mismatches are detailed in Section F (8 to 10) of Chapter 5 of the BPG.

5.16 Collateral

(1) A Bank is able to obtain capital relief by accepting collateral only if the collateral is eligible financial collateral. Collateral may be lodged by the counterparty of the Bank holding a credit exposure (or by a third party on behalf of the counterparty). If collateral is lodged by a third party, the third party must guarantee the counterparty's obligation to the Bank and must indemnify the Bank if the counterparty fails to fulfil its obligation. The Bank must ensure that the guarantee does not fail for

lack of consideration.

(2) The Bank must enter into a written agreement with the party lodging the collateral. The agreement must establish the Bank's direct, explicit, irrevocable and unconditional recourse to the collateral. The mechanism by which collateral is lodged must allow the Bank to liquidate or take possession of the collateral in a timely way. The Bank must take all steps necessary to satisfy the legal requirements applicable to its interest in the collateral.

(3) There must not be a significant positive correlation between the value of the collateral and the credit quality of the borrower.

5.17 Eligible financial collateral

(1) The following are eligible financial collateral if they satisfy the criteria in sub-rule (2):

(a) gold bullion;

(b) cash;

(c) debt securities that are assigned, by an ECRA, a rating of:

(i) for sovereign or non-commercial public-sector enterprise securities that are eligible for zero per cent risk-weight—at least BB-;

(ii) for short-term debt securities—at least A-3/P-3; or

(iii) for any other securities—at least BBB-;

(d) subject to sub-rule (3), debt securities that have not been assigned a rating by an ECRA if:

(i) the securities are issued by a bank (in or outside the AIFC) as senior debt and are listed on a regulated exchange;

(ii) all rated issues of the same seniority issued by the bank have a credit rating of at least BBB-(for long-term debt instruments) or A-3/P-3 (for short-term debt instruments); and

(iii) the Bank and the holder of the collateral have no information suggesting that the securities should have a rating below BBB- or A-3/P-3;

(e) equities (including convertible bonds) that are included in a main index;

(f) tracker funds, mutual funds and undertakings for collective investments in transferable securities (UCITS) if:

(i) a price for the units is publicly quoted daily; and

(ii) the funds or UCITS are limited to investing in instruments listed in this sub-rule;

(g) equities (including convertible bonds) that are not included in a main index but are listed on a regulated exchange, and funds and UCITS described in paragraph (f) that include such equities.

(2) For collateral to be eligible financial collateral, it must be lodged for at least the life of the exposure and must be marked-to-market at least once a month. The release of collateral must be conditional on the repayment of the exposure, but collateral may be reduced in proportion to the amount of

any reduction in the exposure.

(3) Collateral in the form of securities issued by the counterparty or a person connected to the counterparty is not eligible financial collateral. Insurance contracts, put options, and forward sales contracts or agreements are not eligible financial collateral.

(4) Cash collateral, in relation to a credit exposure, means collateral in the form of:

(a) notes and coins;

(b) certificates of deposit, bank bills and similar instruments issued by the Bank holding the exposure; or

(c) cash-funded credit-linked notes issued by a Bank against exposures in its Banking Book, if the notes satisfy the criterion for credit derivatives in Rule 5.19(2).

(5) Eligible financial collateral must be held by:

(a) the Bank;

(b) a branch (in or outside the AIFC) of the Bank;

(c) an entity that is a member of the financial group of which the Bank is a member;

(d) an independent custodian; or

(e) a central counterparty.

(6) The holder of cash collateral in the form of a certificate of deposit or bank bill issued by a Bank must keep possession of the instrument while the collateralised exposure exists. If the collateral is held by an independent custodian or central counterparty, the Bank must take reasonable steps to ensure that the holder segregates the collateral from the holder's own assets.

(7) If collateral is held by a branch of a Bank and the branch is outside the AIFC, the agreement between the Bank and the party lodging the collateral must require the branch to act in accordance with the agreement.

Risk-weight for cash collateral

(8) A Bank may apply a zero per cent risk-weight to cash collateral if the collateral is held by the Bank itself. The Bank may apply a zero per cent risk-weight to cash collateral held by another member of the financial group of which the Bank is a member if the agreement between the Bank and the party lodging the collateral requires the holder of the collateral to act in accordance with the agreement.

(9) If cash collateral is held by a bank under a non-custodial arrangement, and the collateral is lodged with the Bank under an agreement that establishes the Bank's irrevocable and unconditional recourse to the collateral, the exposure covered by the collateral (after any necessary haircuts for currency risk) may be assigned the risk-weight of the bank.

(10) If cash collateral is held by an independent custodian (other than a central counterparty), the risk-weight of the holder of the collateral must be used. However, the Bank may apply a zero per cent risk-weight to notes and coins held by an independent custodian.

(11) The secured part of a claim must be risk-weighted at whichever is the higher of 20% or the risk-weight applicable to the eligible financial collateral. However, a risk-weight lower than 20% may be

applied to the secured part if Rule 5.17(12) applies. The unsecured part of the claim must be weighted at the risk-weight applicable to the original counterparty.

(12) A zero per cent risk-weight may be applied to a collateralised transaction if:

(a) there is no currency mismatch; and

(b) any one of the following applies:

(i) the collateral is in the form of sovereign securities that are eligible for zero per cent risk-weight;

(ii) the collateral is in the form of cash collateral on deposit with the Bank; or

(iii) if the collateral is in the form of non-commercial public sector enterprise securities:

(A) the securities are eligible for zero per cent risk-weight; and

(B) the market value of the collateral has been discounted by 20%.

(13) A 0 % risk-weight may be applied to an OTC derivative transaction if there is no currency mismatch and the transaction is fully collateralised by cash and marked-to-market daily.

(14) A 10% risk-weight may be applied to an over the counter derivative transaction to the extent that the transaction is collateralised by sovereign or non-commercial public sector enterprise securities that are eligible for 0 % risk-weight.

5.18 Guarantees

(1) Capital relief is allowed from a guarantee if the guarantor is an eligible guarantor and the guarantee satisfies the criteria in sub-rules (2) to (4). Before accepting a guarantee, a Bank must consider the legal and financial ability of the guarantor to fulfil the guarantee.

(2) A guarantee must be a direct claim on the guarantor and must clearly state the extent of the cover. A letter of comfort is not a guarantee for the purposes of this Division.

(3) A guarantee must be irrevocable and unconditional. It must not include a term or condition:

(a) that allows the guarantor to cancel it unilaterally; or

(b) that increases the effective cost of cover if the credit quality of the guaranteed exposure deteriorates; or

(c) that allows the guarantor not to indemnify the Bank in a timely way if the counterparty defaults.

(4) If a claim on a counterparty is secured by a guarantee, the part of the claim that is covered by the guarantee may be weighted at the risk- weight applicable to the guarantor. The unsecured part of the claim must be weighted at the risk-weight applicable to the original counterparty.

Eligible guarantors

(5) Eligible guarantor means:

(a) the Republic of Kazakhstan or any other sovereign;

(b) an entity that is treated as a sovereign in accordance with the Basel Accords; or

(c) a public sector enterprise or other entity that has:

(i) a risk-weight of 20% or lower; and

(ii) a lower risk-weight than the counterparty.

(6) A parent entity, Subsidiary or affiliate of a counterparty may be an eligible guarantor if it has a lower risk-weight than the counterparty.

5.19 Credit derivatives

(1) Capital relief is allowed if a Bank uses an eligible credit derivative. Each of the following is an eligible credit derivative if it satisfies sub-rule (2):

(a) a single-name credit-default swap;

(b) a total-rate-of-return swap for which the Bank has recorded any deterioration in the value of the underlying exposure, in addition to recording the net payments received on the swap as net income;

(c) a cash-funded credit-linked note;

(d) a first and second-to-default credit derivative basket product.

(2) The credit derivative must not include a term or condition that terminates the credit protection, or increases the Bank's costs for the protection, if the credit quality of the underlying exposure deteriorates.

(3) If a claim on a counterparty is protected by a credit derivative, the part of the claim that is protected may be weighted at the risk-weight applicable to the issuer of the credit derivative. The unprotected part of the claim must be weighted at the risk-weight applicable to the original counterparty.

5.20 Netting agreements

(1) A Bank is able to obtain capital relief from a netting agreement with a counterparty only if the agreement is an eligible netting agreement. A Bank that has entered into a netting agreement must consistently net all the transactions included in the agreement. The Bank must not selectively pick which transactions to net.

(2) The eligibility criteria, conditions for enforceability, procedures, and the methods for the use of netting agreements as a Credit Risk mitigant to avail of eligible capital relief are detailed in Section G of Chapter 5 of the BPG. In order to avail of capital relief by using netting agreements to mitigate Credit Risk, a Bank is expected to fully comply with the provisions detailed in Section G of Chapter 5 of the BPG. Failure to do so, would be seen as attempts to unduly overstate the capital position of the Bank.

5.21 Securitisation and Re-securitisation

(1) The Part sets out the framework for determining a Bank's minimum capital requirement to cover the Bank's exposures arising from traditional and synthetic securitisations.

(2) The background and description of the use of securitisation to obtain capital relief as well as to ensure appropriate risk-weighting of securitisation positions held by a Bank, eligibility criteria, conditions for enforceability, procedures, and the methods for the capital treatment of securitisation

and re-securitisation are detailed in Section H of Chapter 5 of the BPG. In order to avail of capital relief while using securitisation or to ensure that the securitisation positions are appropriately risk-weighted, a Bank is expected to fully comply with the provisions detailed in Section H of Chapter 5 of the BPG. Failure to do so, would be seen as attempts to unduly overstate the capital position of the Bank.

Governance for securitisation

(3) A Bank's Governing Body must oversee the Bank's securitisation exposures. The governing body:

(a) must understand, and set the scope and purpose of, the Bank's securitisations; and

(b) must be aware of the risks and other implications associated with securitisation.

(4) The Governing Body must ensure that the Bank's senior management establishes and implements securitisation policies that include:

(a) appropriate risk management systems to identify, measure, monitor, report on and control or mitigate the risks arising from the Bank's involvement in securitisation; and

(b) how the Bank monitors, and reports on, the effect of securitisation on its risk profile.

(5) A Bank must be able to demonstrate to the AFSA that the Bank's ICAAP captures the following specific risks relating to securitisation:

(a) Credit Risk, Market Risk, Liquidity Risk and reputation risk for each securitisation exposure;

(b) potential delinquencies and losses on the exposures;

(c) risks arising from the provision of credit enhancements and liquidity facilities; and

(d) risks arising from guarantees provided by monoline insurers and other third parties.

Calculation of RWAs for securitisation

(6) A Bank that is an originator or sponsor of a traditional securitisation may exclude, from the calculation of its risk-weighted assets, exposures relating to the securitised assets only if:

(a) the immediate transferee of the underlying assets is an SPE, and the holders of the legal or beneficial interests in the SPE have the right to pledge or exchange those interests without restriction;

(b) substantially all Credit Risk associated with the securitised assets have been transferred;

(c) the Bank has no direct or indirect control over the securitised assets;

(d) the securitised assets are legally isolated from the Bank (through the sale of the assets or through sub-participation) so that the assets are beyond the reach of the Bank and its creditors even in case of bankruptcy or insolvency;

(e) a qualified legal counsel (whether external or in-house) has given a written reasoned opinion that paragraph (d) is satisfied;

(f) any clean-up call complies with rules in this section;

(g) the securities issued are not obligations of the Bank, so that investors have a claim only on

the securitised assets and have no claim against the Bank;

(h) the securitisation does not include any term or condition that:

(i) requires the Bank to alter the underlying exposures to improve the pool's weighted average credit quality (unless the improvement is achieved by selling exposures at market prices to parties who are neither affiliated, connected or related to the Bank);

(ii) allows increases in a retained first loss position or credit enhancement; or

(iii) increases the yield payable to parties other than the Bank (for example, payments to investors and providers of credit enhancement) in response to a deterioration in the credit quality of the underlying assets; and

(i) the securitisation does not have:

(i) termination provisions for specific changes in tax and regulation;

(ii) termination options or triggers (except clean-up calls that comply with relevant rules in this section); or

(iii) early amortisation provisions that, according to rules in this section, would result in the securitisation not meeting the other requirements in paragraphs (a) to (h).

Due diligence requirements

(7) A Bank must not apply a risk-weight to a securitisation exposure using table 5 H, unless the Bank meets the following due diligence requirements:

(a) The Bank must have, in relation to securitisation, appropriate policies:

(i) to ensure that the economic substance of each securitisation is taken into account in managing the risks arising from the Bank's involvement in securitisation;

(ii) to document its systems and controls in relation to securitisation and the risks that arise from it; and

(iii) that set out the effects of securitisation on capital.

(b) The Bank must have, on an ongoing basis, a clear understanding of the risk characteristics of its individual securitisation exposures (whether on-balance-sheet or off-balance-sheet) and the risk characteristics of the pool underlying those exposures.

(c) The Bank must understand, at all times, the structural features that may materially affect the performance of its securitisation exposures (such as contractual waterfall and waterfall-related triggers, credit enhancements, liquidity facilities, market value triggers, and deal-specific definitions of default).

(d) The Bank must have continuous access to performance information about its underlying assets.

(8) If the Bank fails to meet a due diligence requirement in relation to a securitisation exposure, the AFSA may direct the Bank:

(a) to apply a risk-weight of 1,250% to the exposure; or

(b) to deduct the amount of the exposure from its regulatory capital.

(9) For re-securitisation, the Bank must have not only information on the securitisation tranches (such as the issuer name and credit quality) but also the characteristics and performance of the pools underlying those tranches.

Capital treatment to be based on economic substance

(10) The capital treatment of a securitisation exposure must be determined on the basis of the economic substance, rather than the legal form, of the securitisation structure. If a Bank is uncertain about whether a transaction is a securitisation, the Bank must consult with the AFSA.

(11) Despite anything in these rules, the AFSA may look through the structure to the economic substance of the transaction, and:

(a) vary the capital treatment of a securitisation exposure; or

(b) reclassify a transaction as a securitisation or not a securitisation and impose a capital requirement or limit on the transaction.

Retained securitisation exposures

(12) A Bank that is an originator or sponsor of a securitisation might, despite having transferred the underlying assets or the Credit Risk to those assets, continue to be exposed (through retained securitisation exposures) in relation to the securitisation. The Bank must hold regulatory capital against all of its retained securitisation exposures.

(13) The sources of retained securitisation exposures include:

(a) investments in the securitisation;

(b) investments in asset-backed securities (including mortgage- backed securities);

(c) retention of a subordinated tranche;

(d) credit enhancements provided by the Bank; and

(e) liquidity facilities provided by the Bank.

A repurchased securitisation exposure must be treated as a retained securitisation exposure.

(14) A Bank that is an originator or sponsor of a securitisation must retain 5% of the total issuance.

Effect of giving implicit support

(15) A Bank that gives implicit support to a securitisation:

(a) must include the underwriting exposures of the securitisation in its calculation of risk-weighted assets (as if those assets had not been securitised and had remained on its balance sheet);

(b) must not recognise any gain-on-sale of the underlying assets; and

(c) must disclose to investors that it has provided implicit support and the effect on regulatory capital of doing so.

Treatment of on-balance-sheet retained securitisation exposures

(16) The RWA amount of an on-balance-sheet retained securitisation exposure is calculated by multiplying the exposure by the applicable risk-weight in table 5 H.

Table 5 H Risk-weights based on ECRA rating

Note In the table, the ratings are given according to Standard & Poor's conventions. If a claim or asset is not rated by Standard & Poor's, its ratings must be mapped to the equivalent Standard & Poor's rating.

long-term rating	securitisation exposure %	re-securitisation exposure %
AAA to AA-	20	40
A+ to A-	50	100
BBB+ to BBB-	100	225
BB+ to BB-	350	650
B+ and below or unrated	As directed by the AFSA apply 1,250% risk-weight or deduct the amount of the exposure from the Bank's regulatory capital	

short-term rating	securitisation exposure %	re-securitisation exposure %
A-1	20	40
A-2	50	100
A-3	100	225
Below A-3	As directed by the AFSA, apply 1,250% risk-weight or deduct the amount of the exposure from the Bank's regulatory capital	

(17) If an exposure is to be deducted from the Bank's regulatory capital, the amount of the deduction may be calculated net of any specific provision taken against the exposure.

Exceptions to treatment of unrated securitisation exposures

(18) The rule that the treatment of unrated securitisation exposures is as directed by the AFSA (to either apply 1,250% risk- weight or deduct the amount) does not apply to:

(a) the most senior exposure in a securitisation;

(b) exposures:

(i) that are in a second loss position or better in ABCP programmes; and

(ii) that meet the requirements in paragraph 36 of Section H in the BPG; and

(c) eligible liquidity facilities.

Treatment of off-balance-sheet retained securitisation exposures

(19) A 100% credit conversion factor must be applied to an off-balance-sheet retained securitisation exposure unless the exposure qualifies as:

(a) an eligible liquidity facility, or

(b) an eligible servicer cash advance facility.

(20) The description, operational requirements, eligibility criteria, terms and conditions, procedures, formulae, parameters and the methods for the treatment of eligible liquidity facilities referred in paragraph (19) above are detailed in Section H of Chapter 5 of the BPG. In order to use such liquidity facilities and to assign appropriate capital requirements to the resulting risk exposures, a Bank must fully comply with the relevant paragraphs in Section H of Chapter 5 of the BPG. Failure to do so, would be seen by the AFSA as attempts to overstate the capital position of the Bank.

Capital relief from Credit Risk Mitigation techniques obtained by Bank

(21) A Bank that has obtained a Credit Risk Mitigation technique (such as eligible financial collateral, an eligible credit derivative, a guarantee or an eligible netting agreement) applicable to a securitisation exposure may reduce its capital requirement for the exposure. Collateral pledged by an SPE as part of the securitisation may be used as a Credit Risk Mitigation technique if it is eligible financial collateral. However, an SPE of a securitisation cannot be an eligible protection provider in the securitisation. In this rule, collateral is used to hedge the Credit Risk of a securitisation exposure rather than to mitigate the underlying exposures of the securitisation.

Note For eligible financial collateral see Rule 5.17. For eligible protection provider, see paragraph 47 in Chapter 5 of the BPG.

Treatment of Credit Risk Mitigation techniques provided by Bank

(22) If a Bank provides a Credit Risk Mitigation technique to a securitisation exposure, the calculation of its risk-weighted assets for Credit Risk must be in accordance with the Rules from 5.14 to 5.20 in this Chapter. The Bank must calculate the capital requirement as if it were an investor in the securitisation. If a Bank provides a Credit Risk Mitigation technique to an unrated credit enhancement, it must treat the protection provided as if it were directly holding the unrated credit enhancement.

Treatment of enhanced portions

(23) The RWA for a credit-enhanced portion of a securitisation must be calculated in accordance with the standardised approach in Rules 5.5 to 5.10 of this Chapter.

Effect of Credit Risk Mitigation techniques

(24) The description, operational requirements, eligibility criteria, terms and conditions, procedures, formulae, parameters and the methods for considering the effect of providing Credit Risk Mitigation to a securitisation in the calculation of RWAs are detailed in Section H of Chapter 5 of the BPG. In order to calculate the RWAs appropriately in such cases, a Bank must fully comply with the relevant paragraphs in Section H of Chapter 5 of the BPG. Failure to do so, would be seen by the AFSA as

attempts to overstate the capital position of the Bank.

Early amortisation provisions

Definitions

(25) In relation to early amortization provisions, the following are the definitions used:

excess spread, in relation to a securitisation, means finance charge collections and other income received by the SPV or trust, minus certificate interest, servicing fees, charge-offs, costs and expenses. Excess spread is also known as future margin income.

securitisation involving revolving exposures means a securitisation in which 1 or more of the underlying exposures represents, directly or indirectly, current or future draws on a revolving credit facility (such as a credit card facility, home equity line of credit or commercial line of credit).

uncommitted credit line is a credit line that may be cancelled at any time, without any condition and without any need to give advance notice. Any other credit line is a ***committed credit line***.

(26) The description, operational requirements, eligibility criteria, terms and conditions, procedures, formulae, parameters and the methods for the treatment of securitisations with early amortization provisions and calculation of RWAs are detailed in Section H of Chapter 5 of the BPG. In order to calculate the RWAs appropriately in such cases, a Bank must fully comply with the relevant paragraphs in Section H of Chapter 5 of the BPG. Failure to do so, would be seen by the AFSA as attempts to overstate the capital position of the Bank.

5.22 Provisioning requirements

(1) Provisioning means setting aside an amount to cover expected losses on special mention credits, impaired credits and other problem assets, based on loan-loss probability. Provisioning is made before profit is earned.

Policies on provisioning

(2) Depending on the nature, scale and complexity of a Bank's business, and of the credit it provides, the Bank's provisioning policy must set out:

(a) the areas of its business to which the policy applies;

(b) whether the Bank uses different approaches to those areas, and the significant differences in approach;

(c) who is responsible for regularly monitoring its assets, to identify problem or potential problem assets, and the factors it takes into account in identifying them;

(d) the extent to which the value of any collateral, guarantees or insurance that the Bank holds affects the need for, or the level of, provisions;

(e) the basis on which the Bank makes its provisions, including the extent to which their levels are left to managerial judgement or to a committee;

(f) the methods, debt management systems or formulae used to set the levels of provisions and the factors that must be considered in deciding whether the provisions are adequate;

(g) the reports to enable the Bank's Governing Body and senior management to ensure that the Bank maintains adequate provisions;

(h) the procedures and responsibilities for arrears management and the recovery of exposures in arrears or exposures that have had provisions made against them;

(i) the procedures for writing off and writing back provisions; and

(j) the procedures for calculating and making provisions for contingent and other liabilities (such as contingent liabilities that have crystallised from acceptances, endorsements, guarantees, performance bonds, indemnities, irrevocable letters of credit and the confirmation of documentary credits).

Adequacy of Provisions

(3) A Bank must ensure that the Bank maintains provisions that, taken together, are prudent, reasonable and adequate to absorb credit losses, given the facts and circumstances. The losses covered must include losses incurred, losses incurred but not yet reported, and losses estimated but not certain to arise, extending over the life of the individual credits that make up its credit portfolio.

(4) The Bank must also ensure that provisions and write-offs are timely and reflect realistic repayment and recovery expectations, taking into account market and macroeconomic conditions. The Bank must consider all the significant factors that affect the likelihood of collecting on the transactions that make up its credit portfolio and the estimated future credit losses on those transactions.

(5) The Bank must make minimum provisions which meet the requirements in table 5 K.

Table 5 K Provisioning requirements

Column 1 Item	Column 2 Category	Column 3 Minimum provisioning requirement (% of the unsecured part of the credit)
1	performing	0
2	special mention	5
3	substandard	20
4	doubtful	50
5	loss	100

(6) Provisions may be general (assessed collectively against the whole of a portfolio) or specific (assessed against individual credits), or both. The Bank must take into account off-balance-sheet exposures in its categorisation of credits and in provisioning.

(7) The levels of provisions and write-offs must be reviewed regularly to ensure that they are consistent with identified and estimated losses.

(8) A Bank must not restructure, refinance or reclassify assets with a view to circumventing the requirements on provisioning.

(9) The AFSA may at any time require a Bank to demonstrate that the Bank's classification of its assets,

and its provisions, are adequate for prudential purposes.

(10) The AFSA may require the Bank to reclassify its assets or increase the levels of its provisions if the AFSA considers that the asset classifications are inaccurate, or the provisions are inadequate, for prudential purposes.

(11) A Bank's Governing Body must obtain timely information on the condition of the Bank's assets, including the classification of assets, the levels of provisions and problem assets. The information must include summary results of the latest asset review, comparative trends in the overall quality of problem assets, and measurements of existing or anticipated deterioration in asset quality and losses expected.

5.23 Transactions with related parties

(1) The detailed requirements specifying the description, additional clarifications on definition of related parties, methodologies, parameters, and controls formulae in respect of the primary regulations on related party transactions are provided in Section J of Chapter 5 of the Baking Prudential Guideline (BPG) issued by the AFSA. It is suggested that this rule on related party transactions, be read in conjunction with Chapter 5 of the BPG issued by the AFSA to facilitate understanding of the regulatory requirements and compliance with them.

Related parties

(2) Related parties, of a Bank, includes:

(a) any other member of the Bank's corporate group;

(b) any individual who is able to exercise significant influence over the Bank;

(c) any affiliate of the Bank; and

(d) any entity that the AFSA directs the Bank to include.

Related party transactions – governance and controls

(3) A Bank must establish and implement a documented policy for transactions with related parties, which is approved by its Governing Body and includes:

(a) effective systems to identify, monitor and report individual and total exposures to, and transactions with, related parties;

(b) procedures to prevent a member of the governing body, a member of the Bank's senior management or any other person who stands to gain a benefit from a related-party transaction from being part of the process of granting and managing the transaction;

(c) well-defined criteria for the write-off of exposures to related parties;

(d) prudent and appropriate limits to prevent or address conflicts of interest; and

(e) procedures for tracking and reporting exceptions to, and deviations from, limits or policies.

(4) A Bank's Governing Body must ensure that the Bank's policies relating to related-party transactions are complied with and that any exceptions are reported to the appropriate level of the senior management, and, if necessary, to the governing body.

(5) The Governing Body must also ensure that the Bank's senior management monitors transactions

with related parties, takes appropriate steps to control or mitigate the risks from such transactions and writes off exposures to related parties only in accordance with the Bank's policies.

(6) The Governing Body must approve transactions with related parties, and the write-off of related-party exposures, if such transactions or write-off exceeds specified amounts or otherwise poses any special risk.

(7) A transaction with a related party must not be undertaken on terms more favourable to the party than a corresponding transaction with a non- related party.

Limits on lending to related parties

(8) A Bank must not enter into a transaction that would cause it to exceed the limits set out in table 5 L unless it has the written approval of the AFSA to do so.

Table 5 L Limits on Banks' exposure to related parties

Column 1 Item	Column 2 Kind of exposure	Column 3 Limit (% of total assets)
1	exposures to a member of the Governing Body or senior management of the Bank, or a person connected to either of them	0.5
2	the total of exposures under item 1	3
3	exposures to a significant shareholder of the Bank (other than exposures to a shareholder that is a Bank or an equivalent entity regulated in a way comparable to a Bank in the AIFC))	2
4	the total of exposures under item 3	5
5	exposures to a related party or a party connected to the related party (other than exposures to a Bank or an equivalent entity that is regulated in a way comparable to a Bank in the AIFC)	2
6	the total of exposures under item 5	5

Powers of the AFSA

(9) Despite anything in these rules, the AFSA may, in writing, set specific limits on a Bank's exposures to a related party or to related parties in total.

(10) The AFSA may direct such exposures to be deducted from regulatory capital when assessing capital adequacy or direct that such exposures be collateralised.

Part II Concentration risk and related matters

5.24 General

(1) This Chapter sets out the requirements for a Bank's policy to identify, measure, evaluate, manage and control or mitigate concentrations of Credit Risk exposures. This Chapter also sets limits on a Bank's Credit Risk exposures to individual counterparties and to groups of connected counterparties.

(2) The detailed requirements for managing the concentration risk including but not limited to methodologies, guidance, eligibility criteria, terms, parameters, and formulae which are required to comply with the primary regulations addressing concentration risk management and related regulatory limits outlined in this Part II of Chapter 5 of BBR are provided in section K of Chapter 5 of the Banking Prudential Guideline (BPG) issued by the AFSA. The relevant sections of the BPG also provide the supervisory expectations of the AFSA in relation to management of concentration risk.

(3) Banks are expected to comply with the provisions outlined in Section K of Chapter 5 of the BPG, in order to ensure compliance with the rules in this Part II. Failure to do so, would be assessed by the AFSA as inadequate risk management and governance implying non-compliance with basic regulatory requirements applicable to Banks. It is suggested that this Chapter of the BBR, be read in conjunction with Chapter 5 of the BPG issued by the AFSA to facilitate understanding of the regulatory requirements and compliance with them.

Concept of connected parties

(4) The concept of parties being connected to one another is used in these rules in relation to counterparties or issuers with which a Bank has exposures. Connected counterparties are the basis for the measurement of concentration risk and large exposures.

(5) In contrast, the concept of parties being related to the Bank (which is discussed with Credit Risk in part I of this Chapter) is primarily used in relation to the requirement that the Bank's transactions be at arm's length. It is of course possible for a Bank's related parties to be connected counterparties (such as when the Bank has exposures to them). For purposes of concentration risk, the Bank's exposure to connected counterparties (whether related or not) is taken to be a single risk.

Connected parties

(6) A party is connected to another party if they are linked by:

(a) cross guarantees;

(b) common ownership;

(c) common management;

(d) one having the ability to exercise control over the other, whether direct or indirect;

(e) financial interdependency—that is, the financial soundness of one may affect the financial soundness of the other; or

(f) any combination of the factors mentioned in paragraphs (a) to (e).

(7) A counterparty may be connected to another counterparty by other linkages that, in the Bank's assessment, connect the counterparties as constituting a single risk. A connected party can be an individual or other entity.

Role of Governing Body - concentration risk

(8) A Bank's Governing Body must ensure that the Bank's concentration risk management policy gives a comprehensive bank-wide view of the significant sources of concentration risk (including on-balance-sheet exposures, off-balance-sheet exposures and exposures from contingent liabilities).

(9) The Governing Body must also ensure that the Bank's senior management monitors the limits set

in this Chapter and that those limits are not exceeded on a solo or consolidated basis.

5.25 Concentration risk

(1) Concentration risk to a Bank arises if the Bank is exposed to 1 counterparty, or to 2 or more counterparties that are not truly independent of each other, and the total of the exposures to the counterparty or counterparties is large enough to endanger the Bank's liquidity or solvency.

Policies—Concentration risk policy

(2) A Bank's concentration risk policy must set limits for acceptable concentrations of risk, consistent with the Bank's risk tolerance, risk profile and capital. The limits must be made known to, and must be understood by, all relevant staff.

(3) The policy must ensure that:

(a) the Bank's information systems identify exposures creating risk concentrations and large exposures to single counterparties or connected counterparties, aggregate those exposures and facilitate their management; and

(b) all significant such concentrations and exposures are reviewed regularly and reported to the Bank's Governing Body or senior management.

Relation to stress-testing

(4) When carrying out stress-testing or review of stress scenarios, a Bank must take into account significant risk concentrations and large exposures, and the effects of changes in market conditions and risk factors on them.

5.26 Management of Concentration risk exposures

Calculating exposures

(1) Large exposure means a gross exposure to a counterparty or connected counterparties that is 10% or more of the Bank's regulatory capital. In this rule:

gross exposure to a counterparty or connected counterparties is the total of the following exposures:

(a) on-balance-sheet and off-balance-sheet exposures;

(b) debt securities held by the Bank;

(c) equity exposures.

(2) In calculating the gross exposure, a Bank must include:

(a) the outstanding balances of all loans and advances, including balances with other banks;

(b) holdings of debt or equity securities;

(c) unused off-balance-sheet commitments, whether revocable or irrevocable; and

(d) the credit equivalent amounts of all market-related transactions (calculated in accordance with the rules in this Chapter).

(3) However, in calculating the gross exposure, a Bank must not include:

(a) claims, equity investments and other exposures deducted from the Bank's capital;

(b) exposures arising in the course of settlement of market-related contracts; and

(c) exposures that have been written off.

(4) For this Part II:

(a) a Bank must treat an exposure as reduced (to the extent permitted by the provisions on Credit Risk Mitigation in part I of this chapter) by any applicable Credit Risk Mitigation technique; and

(b) a Bank that is part of a financial group may offset intragroup amounts due to other deposit takers within the group.

Policies—large exposures

(5) A Bank's large exposure policy must include:

(a) exposure limits, commensurate with the Bank's risk tolerance, risk profile and capital, for:

(i) categories of counterparties (for example, sovereigns, other Banks and other financial entities, corporate and individual borrowers);

(ii) connected counterparties;

(iii) particular industries or sectors;

(iv) particular countries; and

(v) asset classes (for example, property holdings);

(b) the circumstances in which the exposure limits may be exceeded;

(c) the procedures for approving exceptions to, and deviations from, exposure limits or policies; and

(d) the procedures for identifying, measuring, managing and reporting large exposures.

Limits on exposures

(6) A Bank must not become exposed without limit to a single counterparty. The Bank must not give a general guarantee of the obligations of a counterparty.

(7) The total of the Bank's net exposures to any 1 counterparty or any 1 group of connected counterparties must not exceed 25% of the Bank's regulatory capital.

(8) The total of all of the Bank's net large exposures must not exceed 800% of that capital.

(9) A Bank may apply to the AFSA for approval for a proposed exposure in excess of the limits set out in this Chapter. An approval will be granted only in exceptional circumstances and only after the Bank satisfies the AFSA that the proposed exposure does not expose the Bank to excessive risk.

(10) The AFSA may impose a higher capital ratio on the Bank to compensate for the additional risk

associated with the proposed exposure.

Obligation to measure

(11) A Bank must measure, classify and make provision for each large exposure individually.

(12) The Bank must immediately notify the AFSA if it is concerned that risk concentrations or large exposures might significantly affect its capital adequacy. The notice must describe the Bank's proposed measures to address its concerns.

5.27 Powers of the AFSA

(1) If the AFSA considers it necessary or desirable to do so in the interest of effective supervision of a Bank, the AFSA may direct the Bank to treat a party as connected to another party.

The AFSA can set different limits and ratios

(2) Despite anything in these rules, the AFSA may, in writing, set specific limits on a Bank's exposure to particular counterparties, groups of counterparties, industries, sectors, regions, countries or asset classes on a case-by-case basis.

(3) If a Bank has 1 or more large exposures (excluding exposures to sovereigns and central banks) or if, in the AFSA's opinion, the Bank is exposed to a significant level of risk concentration, the AFSA may impose a higher capital ratio on the Bank.

(4) In considering whether to increase the Bank's capital ratio, the AFSA will take into account:

(a) whether the increased capital ratio would be consistent with the Bank's concentration risk and large exposure policies;

(b) the number of exposures, and the size and nature of each; and

(c) the nature, scale and complexity of the Bank's business and the experience of its Governing Body and senior management.

(5) The AFSA may also direct the Bank to take measures to reduce its level of risk concentration.

CHAPTER 6 Market Risk

Introduction

Guidance

(1) This Chapter addresses the regulatory requirements in respect of managing the Market Risk exposures of a Bank. Market Risk refers to the risk of incurring losses on positions held by a Bank with trading intent (usually in its Trading Book), caused by adverse movements in market prices or in underlying value drivers. This chapter aims to ensure that a Bank engaging in activities exposing it to such Market risks adopts appropriate and effective risk management practices and holds adequate regulatory capital of the right quality required to support the level of such risks assumed.

(2) This Chapter includes requirements that a Bank:

(a) implement a comprehensive Market Risk management framework to manage, measure and monitor Market Risk commensurate with the nature, scale and complexity of its operations; and

(b) calculate and hold the Market Risk Capital Requirement, according to the methodologies provided in the BPG issued by the AFSA.

(3) This Chapter includes rules requiring Banks to determine Market Risk Capital Requirement on exposures involving interest rate risk, equity risk, foreign exchange risk, commodities risk, options risk, collective investment fund risk and securities underwriting risk. The rules in this Chapter allow the use of standard pre-defined methodologies for estimating the Market Risk Capital Requirement as well as the use of AFSA-approved internal models to calculate a Bank's Market Risk Capital Requirement.

(4) The detailed requirements specifying the calculation methodologies, parameters, metrics and formulae in respect of the primary requirements outlined in this chapter are provided in the Banking Prudential Guideline (BPG) issued by the AFSA. The BPG also provides detailed guidance on criteria on Trading Book and inclusion of exposures in a Trading Book, criteria for approval of internal models for calculation of Market Risk Capital Requirement, incorporation of incremental risk charges in internal models, if allowed and guidance on the required level of stress testing.

6.1 Market Risk Management – Systems and Controls

(1) A Bank must implement and maintain a Market Risk management policy which enables it to identify, assess, monitor, control and mitigate Market Risk.

(2) The Market Risk management policy must be documented and include the Bank's risk appetite for Market Risk exposures. The policy must also set out as to how the Bank identifies, assesses, mitigates, controls and monitors that risk.

(3) A Bank must:

(a) identify, assess, monitor, mitigate and, control its Market Risk exposures;

(b) hold adequate Capital, at all times, to support Market Risk exposures assumed as part of its Trading Book and Banking Book activities;

(c) ensure that its risk management framework including but not limited to tools, methodologies and, systems enable it to implement its Market Risk management policy;

(d) review and update its Market Risk management policy at a frequency appropriate to the

nature, scale and complexity of its Trading Book activities.

(4) A Bank's Governing Body must ensure that its Market Risk management policy enables it to obtain a comprehensive bank-wide view of its Market Risk exposures and takes into account the risk of a significant deterioration in market liquidity of its exposures.

Guidance

Guidance in respect of the contents of a Bank's Market Risk management policy which is required to satisfy the regulatory requirement in the Rule 6.1 is provided in the BPG issued by the AFSA.

6.2 Trading Book

(1) A Bank's Trading Book consists of the positions held by the Bank (whether on-balance-sheet or off-balance-sheet) that must be included in the Trading Book in accordance with these rules. Other positions held by the Bank must be included in its Banking Book.

Note A Bank is required to have policies to distinguish consistently between trading activities and banking activities

(2) A Bank must have a Trading Book if:

(a) it has positions that must be included in the Trading Book; and

(b) the total value of the positions described in paragraph (a) has exceeded 5% of the total of the Bank's on-balance-sheet and off- balance-sheet positions at any time in the previous 12 months.

(3) The Bank must include, in the Trading Book, positions and exposures of the following kinds:

(a) a position in a financial instrument, commodity or commodity derivative;

(b) a principal broking position in a financial instrument, commodity or commodity derivative;

(c) a position taken to hedge an exposure in the Trading Book;

(d) an exposure from a repurchase agreement, or securities or commodities lending, that is based on a position in a security or commodity included in the Trading Book;

(e) an exposure from a reverse repurchase agreement, or securities and commodities borrowing, that is based on a position in a security or commodity included in the Trading Book;

(f) an exposure from an unsettled transaction, a free delivery or an over the counter derivative;

(g) an exposure in the form of a fee, commission, interest, dividend or margin on an exchange-traded derivative directly related to a position included in the Trading Book.

(4) The Bank must also include in its Trading Book:

(a) total-rate-of-return swaps (except those that have been transacted to hedge a Banking Book credit exposure); and

(b) open short positions in credit derivatives.

(5) The Bank must not include in its Trading Book:

(a) positions held for liquidity management; and

(b) loans (unless they are used to hedge a position in the Trading Book).

(6) The Bank's positions must be valued in accordance with the relevant accounting standards and prudent valuation guidance provided in the BPG issued by the AFSA.

(7) The Bank must have a well-documented Trading Book policy for keeping the Trading Book up-to-date and to ensure the inclusion of appropriate positions accurately.

(8) The Trading Book policy must be approved by the Bank's governing body, and the Bank must be able to demonstrate compliance with it if directed by the AFSA to do so.

Guidance

Guidance relating to the contents of a Bank's Trading Book policy, the detailed requirements in relation to switching of positions between its Trading Book and Banking Book which are required to satisfy the regulatory requirement in the Rule 6.2 and the related supervisory expectations of the AFSA are provided in the BPG issued by the AFSA.

6.3 Switching of positions or instruments between Books

(1) A Bank must not switch a position or an instrument between its Trading Book and Banking Book, unless it has received a written approval from the AFSA, allowing it to do so. The AFSA may approve such a switch subject to 1 or more conditions.

(2) The Bank must not benefit from any lower regulatory capital requirement resulting from such a switch even if that is approved by the AFSA.

6.4 Valuation of positions

(1) A Bank must use the mark-to-market method to value its positions and exposures in its Trading Book, if there is a market to mark the positions and exposures to. Mark-to-market means a valuation that is based on current market value.

(2) A position that is marked-to-market must be revalued daily, based on independently sourced current market prices.

(3) If it is not possible to value any of the positions in the Trading Book on a mark-to-market basis (for example, in the case of unlisted securities or where the market is illiquid), a Bank may use the mark-to-model method to value its positions and exposures. Mark-to-model means a valuation that has to be benchmarked, extrapolated or otherwise calculated from a market input, using a pre-defined model.

(4) A Bank must be able to demonstrate that its marking-to-model is prudent.

(5) A Bank must independently verify market prices and model inputs, to check that those prices and inputs are accurate. The verification must be done at least once a month.

(6) A Bank must consider making adjustments for positions that cannot be prudently valued (such as those that have become concentrated, less liquid or stale). For example, valuation adjustment would be appropriate if pricing sources are more subjective (such as when there is only one available broker quote).

(7) A Bank must establish and maintain procedures for considering valuation adjustments, irrespective of whether:

(a) the Bank uses the mark-to-market or mark-to-model method; and

(b) whether the valuation is done internally by the Bank or by a third party.

Guidance

Detailed guidance relating to the different valuation methods for the positions in a Bank's Trading Book, the AFSA's expectations regarding the use of those methods, the expectations of the AFSA regarding independent price verification as well as the issues to be considered as part of the valuation adjustments, are provided in the BPG issued by the AFSA.

6.5 Calculation of the Market Risk Capital Requirement

(1) A Bank must calculate its Market Risk Capital Requirement as the sum of the following components:

(a) Interest Rate Risk Capital Requirement;

(b) Equity Risk Capital Requirement;

(c) Foreign Exchange Risk Capital Requirement;

(d) Commodities Risk Capital Requirement; and

(e) Option Risk Capital Requirement.

(2) A Bank must calculate the Market Risk Capital Requirement for the following components, in respect of its Trading Book and Non-Trading Book positions for the relevant component, by applying the methodology, parameters, formulae and guidance set out in the BPG issued by the AFSA:

(a) Foreign Exchange Risk Capital Requirement;

(b) Commodities Risk Capital Requirement;

(3) A Bank must calculate the Market Risk Capital Requirement for the following components, in respect of its Trading Book positions for the relevant component, by applying the methodology, parameters, formulae and guidance set out in the BPG issued by the AFSA:

(a) Interest Rate Risk Capital Requirement;

(b) Equity Risk Capital Requirement; and

(c) Option Risk Capital Requirement.

Guidance

Detailed guidance specifying the tools, methodologies, parameters and formulae for calculating the various components of the Market Risk Capital Requirement outlined in Rule 6.2 above are included in the BPG issued by the AFSA.

6.6 Foreign Exchange Risk Capital Requirement

(1) A Bank must, subject to (2), calculate its Foreign Exchange Risk Capital Requirement in respect of Trading Book and Non-Trading Book foreign exchange positions.

(2) A Bank need not calculate a Foreign Exchange Risk Capital Requirement if:

(a) its foreign currency business, defined as the greater of the sum of its gross long positions and the sum of its gross short positions in all foreign currencies, does not exceed 100% of its Regulatory Capital as defined in Rule 4.13; and

(b) its overall net open position as defined in the BPG does not exceed 2% of its Regulatory Capital as defined in Rule 4.13.

6.7 Standard method and use of Internal Models

(1) A Bank is expected to use the standard methods for calculation of any component of the Market Risk Capital Requirement, which are detailed in the BPG.

(2) A Bank may use an internal model to calculate any specific component of its Market Risk Capital Requirement, if that internal model and its use have been approved in writing by the AFSA.

Guidance

Detailed Guidance in respect of criteria for approval and use of internal models for calculation of Market Risk capital requirement is provided in the BPG issued by the AFSA.

(3) If the AFSA approves the use of an internal model, it may:

(a) impose, withdraw or amend at any time conditions in respect of the use of the internal model; and

(b) withdraw approval if it forms the view that the internal model or its use is no longer suitable for the calculation of the Bank's Market Risk Capital Requirement or any component of it.

(4) A Bank which uses an internal model in accordance with Rule 6.7 (2) must have in place a rigorous and comprehensive stress-testing programme which meets the criteria set out in the BPG issued by the AFSA.

(5) A Bank that has received approval for the use of an internal model may only revert to the use of standard method for calculating its Market Risk Capital Requirement or any component of it, with the prior written consent of the AFSA.

(6) In the standard method, capital requirement is the sum of the capital charges, calculated in accordance with this Chapter, for the risks included in Market Risk.

CHAPTER 7 Operational Risk

Introduction

Guidance

(1) This chapter sets out the regulatory requirements in respect of a Bank's obligation to manage effectively its Operational Risk exposures. Operational Risk refers to the risk of incurring losses due to inadequate or failed internal systems, processes, and people, or from external events. Operational Risk losses also include losses arising out of legal risk but excludes strategic and reputational risk. This chapter aims to ensure that a Bank has a robust Operational Risk management framework commensurate with the nature, scale and complexity of its operations and that it holds sufficient regulatory capital against Operational Risk exposures.

(2) This chapter includes requirements that a Bank:

(a) implement a comprehensive Operational Risk management framework to manage, measure and monitor its operational Risk exposures commensurate with the nature, scale and complexity of its operations;

(b) address specific elements of an Operational Risk management framework relating to IT systems, information security, outsourcing, business continuity and disaster recovery and the management of Operational Risks in trading rooms; and

(c) calculate and hold the Operational Risk Capital Requirement, according to the methodologies provided in the BPG issued by the AFSA.

(3) The detailed requirements specifying the calculation methodologies, parameters, metrics and formulae in respect of the primary requirements outlined in this Chapter are provided in the BPG issued by the AFSA. The BPG also provides detailed guidance on the elements to be included in the policies, systems and controls for managing operational risk, qualitative guidance and standards to be followed in addressing specific components of operational risk like Business continuity risk, detailed parameters, formulae and methodology for calculation of Operational risk capital requirements mandated by this Chapter.

7.1 Operational Risk Management Framework and Governance

(1) A Bank must implement and maintain an Operational Risk management policy which enables it to identify, assess, monitor, control and mitigate its Operational Risk exposures.

(2) The Operational Risk management policy must be documented and include the Bank's risk appetite for Operational Risk exposures. The policy must also set out as to how the Bank identifies, assesses, mitigates, controls and monitors Operational Risk.

(3) The Operational Risk management policy of a Bank must be approved by its Governing Body.

(4) A Bank must:

(a) identify, assess, monitor, mitigate and, control its Operational Risk exposures;

(b) ensure that its risk management framework including but not limited to tools, methodologies and, systems enable it to implement its Operational Risk management policy;

(c) hold adequate Capital, at all times, to support its Operational risk exposures;

(d) review and update its Operational Risk management policy at a frequency appropriate to the

nature, scale and complexity of its Trading Book activities.

(5) A Bank's Governing Body must ensure that its Operational risk management policy enables it to obtain a comprehensive bank-wide view of its Market Risk exposures and takes into account the risk of a significant deterioration in market liquidity of its exposures.

Note: Guidance in respect of the contents of a Bank's Operational Risk management policy, systems and controls which is required to satisfy the regulatory requirement in the Rule 7.1 is provided in the BPG issued by the AFSA.

7.2 Technology Risk and Business Continuity – Policies

(1) A Bank's operational risk management policy must include effective and comprehensive procedures for disaster recovery and business continuity. The Bank must have a business continuity plan for possible scenarios of severe business disruption. The plan must provide for the Bank to continue to operate as a going concern, and to minimise losses (especially those from disturbances to payment and settlement systems), in those scenarios.

(2) A Bank must establish and implement appropriate information technology policies for the accurate and timely identification, measurement, evaluation, management and control or mitigation of operational risk. In particular, the policies must enable the Bank to maintain an adequate and sound information infrastructure:

(a) that meets the Bank's current and projected requirements (under normal circumstances and in times of stress);

(b) that ensures that the data, and the system itself, remain secure and available; and

(c) that supports integrated and comprehensive risk management

(3) The Bank's information infrastructure must enable it to compile and analyse operational risk data, and must facilitate reporting to its Governing Body and senior management and the AFSA.

(4) A Bank must establish and maintain appropriate systems and controls to manage its information security risk.

7.3 Outsourcing risk - Policies

(1) A Bank must establish appropriate policies to assess, manage and monitor the operational risk associated with its outsourced activities. The management of those risks must include the following elements:

(a) carrying out due diligence for selecting service providers

(b) structuring outsourcing arrangements

(c) managing and reporting the risks associated with an outsourcing

(d) ensuring effective control over an outsourcing; and

(e) contingency planning

(2) The outsourcing policies must require a Bank to have comprehensive contracts and service level agreements. The contracts and agreements must clearly state the allocation of responsibilities between service providers and the Bank.

7.4 Powers of the AFSA

Despite anything in these rules, if the AFSA identifies points of exposure or vulnerability to operational risk that are common to 2 or more Banks, it may impose specific capital requirements or limits on each affected Bank.

7.5 Operational Risk Management

(1) A Bank must:

(a) ensure that it identifies and assesses the Operational Risks inherent in all the Bank's products, activities, processes and systems;

(b) ensure the inherent risks identified are understood by relevant Employees of the Bank;

(c) systematically track Operational Risk events and any financial impact associated with such events; and

(d) ensure that the tracking in (c) is consistent with the Operational Risk event types described in the Basel III framework.

(e) regularly monitor material Exposures to Operational Risk losses;

(f) ensure that appropriate reporting mechanisms are in place at its Governing Body, senior management, and business line levels to support effective management of the Bank's Operational Risk;

(g) have appropriate reporting procedures to keep the AFSA informed of developments affecting its operational risk profile; and

(h) immediately notify the AFSA of any material Operational Risk event including notification of any resulting financial impact, positive or negative, associated with such event.

(2) A Bank must ensure that its Operational Risk management policy referred in the Rule 7.1 (1):

(a) includes an approval process for all new products, activities, processes and systems; and

(b) such a process enables the Bank to identify and assess the Operational Risk exposures inherent in its new products, activities, processes and systems.

7.6 Basic indicator approach

(1) A Bank must use the basic indicator approach to operational risk. Operational risk capital requirement is the amount of capital that the Bank must have to cover its operational risk.

(2) The Bank's Operational Risk capital requirement is calculated in accordance with the following formula:

$$\frac{GI * \alpha}{n}$$

where:

GI is the Bank's average annual gross income (as defined in sub-rule (3) or (4)) for those years (out of the previous 3 years) for which the Bank's annual gross income is more than zero.

α is 15% or a higher percentage set by the AFSA.

n is the number of years out of the previous 3 years for which the Bank's gross income is more than zero.

(3) Because of the definitions of GI and n in (2) above, figures for any year in which the annual gross income of a Bank is negative or zero must be excluded from both the numerator and denominator when calculating the average.

(4) For a Bank, gross income, for a year, means net interest income plus net non-interest income for the year. It must be gross of:

(a) any provisions (including provisions for unpaid interest);

(b) operating expenses; and

(c) losses from the sale of securities in the 'Held to Maturity' and 'Available for Sale' categories in the Banking Book.

(5) For a Bank, gross income excludes:

(a) realised profits from the sale of securities in the Banking Book;

(b) realised profits from securities in the 'Held to Maturity' category in the Banking Book;

(c) extraordinary or irregular items of income;

(d) income derived from insurance;

(e) any collection from previously written-off loans; and

(f) income obtained from the disposal of real estate and other assets during the year

CHAPTER 8 Interest Rate Risk in the Banking Book

Introduction

Guidance

(1) Interest rate risk in the Banking Book or IRRBB is the risk to earnings or capital arising from movement of interest rates. IRRBB arises from changing rate relationships among yield curves that affect bank activities (basis risk), from changing rate relationships across the spectrum of maturities (yield curve risk), and from interest- rate-related options embedded in bank products (option risk).

(2) IRRBB is normally a major source of risk for a bank and for Broker Dealers that deal on their own account (including underwriting on a firm commitment basis). IRRBB is a significant risk driver for banks whose Banking Book assets equal or exceed 15% of their total assets. IRRBB may arise from a number of sources, for example:

(a) risks related to the mismatch of repricing of assets and liabilities and off balance sheet short and long-term positions;

(b) risks arising from hedging exposure to one interest rate with exposure to a rate which reprices under slightly different conditions;

(c) risks related to the uncertainties of occurrence, timing, pricing or value of transactions, for example, when expected future transactions do not equal the actual transactions;

(d) risks arising from consumers redeeming fixed rate products when market rates change; and

(e) risks from underwriting on a firm-commitment basis

(4) This Chapter relates to Interest rate risk in the Banking Book. Interest rate risk in the Trading Book is addressed as part of Market Risk in Chapter 6 of BBR.

(5) This Chapter sets out the regulatory requirements in respect of a Bank's obligation to manage effectively its exposure to Interest Rate Risk in the Banking Book (IRRBB). This Chapter aims to ensure that a Bank has a robust framework commensurate with the nature, scale and complexity of its operations, for managing its exposure to IRRBB. In that regard, this Chapter sets out requirements that a Bank:

(a) implement IRRBB management framework to manage, measure and monitor its exposure to IRRBB, in a manner commensurate with the nature, scale and complexity of its operations;

(b) develop and implement policies to identify, measure, assess, manage, control and mitigate IRRBB;

(c) address stress testing of the Bank's exposures to IRRBB; and

(d) address the relationship between IRRBB and the ICAAP.

(6) The detailed requirements specifying the methodologies, guidance and, parameters in respect of the primary requirements outlined in this chapter are provided in the Banking Prudential Guideline (BPG) issued by the AFSA. The BPG also provides detailed guidance on the elements to be included in the policies, systems and controls for managing IRRBB,

qualitative guidance and standards to be followed in meeting the rules in this chapter.

8.1 IRRBB - Risk Management Framework and Governance

(1) A Bank must implement and maintain a policy for management of IRRBB which enables it to identify, assess, monitor, control and mitigate its exposure to IRRBB.

(2) This IRRBB management policy must be documented and must include the Bank's risk appetite for IRRBB. The policy must also include an appropriate interest rate risk strategy as well as a bank-wide interest rate risk management framework appropriate to the nature, scale and complexity of the Bank's Banking Book activities. The policy must also set out as to how the Bank assesses, mitigates, controls and monitors IRRBB exposure.

(3) A Bank must:

(a) identify, assess, monitor, mitigate and, control its exposure to IRRBB exposures;

(b) ensure that its risk management framework including but not limited to tools, and, systems enable it to implement its IRRBB management policy;

(c) hold adequate Capital, at all times, to address its exposure to IRRBB;

(d) review and update its IRRBB management policy at a frequency appropriate to the nature, scale and complexity of its Banking Book activities.

(4) The interest rate risk strategy and IRRBB management framework must:

(a) enable the Governing Body and senior management of the Bank to have a bank-wide view of IRRBB as it applies to Banking Book activities;

(b) include a system for identifying and assessing IRRBB and its sources;

(c) include a process for the measurement and monitoring of IRRBB, using robust and consistent methods which enable the Bank to comply with the requirements set out in Rule 8.4 on Stress testing; and

(d) include a system for controlling and managing IRRBB which enables it to comply with the overall risk management standards expected of a Bank and ensure continued compliance with the BBR Rules.

(5) A Bank must identify the IRRBB impact of any new product, activity or service that it proposes to start and ensure that such impacts are duly addressed with adequate controls before the new product or activity is undertaken or introduced.

(6) The IRRBB management policy of a Bank must be approved by its Governing Body.

(7) A Bank's Governing Body must ensure that its IRRBB management policy enables it to obtain a comprehensive bank-wide view of its exposure to IRRBB in the light of the nature, scale and complexity of its Banking Book activities.

(8) The Governing Body must monitor:

(a) the nature and level of IRRBB assumed by the Bank;

(b) the bank's overall IRRBB profile; and

(c) any changes in market conditions that may affect the bank's current or prospective risk profile.

(9) The Governing Body must ensure that the Bank's senior management establishes and implements an IRRBB management policy that adequately identifies, measures, monitors, reports and controls or mitigates IRRBB.

Note: Guidance in respect of the contents of a Bank's IRRBB management framework, governance, policy, systems and controls which are required to satisfy the regulatory requirement in the Rule 8.1 is provided in the BPG issued by the AFSA.

8.2 Powers of the AFSA

A Bank must hold adequate capital to effectively mitigate its exposure to IRRBB. The AFSA may impose a capital requirement on a Bank based on the Bank's ICAAP, if the AFSA is of the view that the Bank's capital is insufficient to cover its exposure to IRRBB.

8.3 IRRBB Management – Processes and Standards

(1) A bank must not use an assumption or adjustment relating to the bank's exposure to IRRBB unless the assumption or adjustment has been approved by its governing body, or a relevant committee of its governing body. The AFSA may require a bank to seek its explicit approval before using an assumption or adjustment.

(2) If required to do so by the AFSA, the bank must demonstrate how the Bank used an assumption or adjustment (whether or not the AFSA required the assumption or adjustment to be approved).

(3) A banking business bank must set a prudent limit on the extent to which floating-rate exposures are funded by fixed-rate sources (and vice versa). In floating-rate lending, the Bank must set a prudent limit to the extent to which it runs any basis risk that would arise if lending and funding were not based on identical market interest rates.

(4) A Bank must set a prudent limit on the extent to which floating-rate exposures are funded by fixed-rate sources (and vice versa). In floating-rate lending, the Bank must set a prudent limit to the extent to which it runs any basis risk that would arise if lending and funding were not based on identical market interest rates.

(5) A Bank must identify the effect of IRRBB before it introduces a new product or activity. The Bank must consider managing the effect through hedging (using swaps or other derivatives).

8.4 Stress Testing and IRRBB

(1) A Bank must carry out an evaluation of its exposure to IRRBB, in each currency in which 5% or more of its Banking Book assets or Banking Book liabilities is denominated. This evaluation must be carried out at least on an annual basis.

(2) A Bank must carry out stress-testing of its exposures to IRRBB at least on a quarterly basis. This stress-testing must:

(a) determine the re-pricing gap between the bank's assets and liabilities, before and after the effect of derivative instruments is taken into consideration;

(b) determine the effect of a sudden and unexpected parallel change in interest rates of 200 basis points in both directions, on the Bank's net interest income from the forecast Banking Book; and

(c) apply a 200 basis point shock to each material currency in which 5% or more of its Banking Book assets or Banking Book liabilities is denominated.

(3) The AFSA may, in writing, specify a different level of interest rate shock as compared to the standard 200 basis point shock, for specific Banks.

(4) A Bank must include appropriate scenarios in its stress-testing to measure the Bank's vulnerability to loss under adverse interest rate movements. In determining the effect of a rate change on its net interest income, the Bank must not assume that the rate will become negative.

(5) A bank must report the results of its stress-testing to the AFSA, in the form prescribed by the AFSA.

(6) A Bank must immediately notify the AFSA, if any stress-testing under this Chapter involving an interest rate shock described in (2) above, indicates a potential decline in the economic value of the bank by an amount exceeding 20% of its Total Capital as defined in Chapter 4 of BBR.

8.5 Frequency of stress testing

(1) A Bank must carry out the stress testing required by Rule 8.4 (2) as frequently as necessary for it to be reasonably satisfied that it has at all times a sufficient understanding of the degree to which it is exposed to the risks referred to in that rule and the nature of that exposure. In any case it must carry out those evaluations no less frequently than required by Rule 8.4 (2).

(2) In order to carry out effectively the stress testing requirements specified in Rule 8.4 (2), a Bank must include appropriate scenarios into its stress testing programmes for measuring its vulnerability to loss arising from the impact of adverse interest rate movements on its Banking Book structure.

8.6 IRRBB and Relation to ICAAP

(1) A Bank must be able to demonstrate to the AFSA that its ICAAP adequately captures its exposure to IRRBB.

(2) In order to meet effectively the obligations it faced under ICAAP which includes the need to address IRRBB exposures, a Bank is required to make a written record of its assessments and stress testing made under this Chapter and rules relating to ICAAP.

CHAPTER 9 Liquidity Risk

Introduction

Guidance

(1) This Chapter addresses the regulatory requirements in respect of managing the Liquidity Risk exposures of a Bank. Liquidity risk is the risk that a Bank may not be able to meet its financial obligations as they fall due. Among all the prudential risks faced by a Bank, Liquidity Risk is highly related to group risk in that a Bank that is a member of a group could be called on to make good on commitments and guarantees in favour of the other members of its group, whether financial or non-financial members.

(2) This Chapter includes requirements that a Bank:

(a) implement a comprehensive Liquidity Risk management framework to manage, measure and monitor Liquidity Risk commensurate with the nature, scale and complexity of its operations;

(b) adopt prudent practices in managing Liquidity Risk;

(c) have adequate sources of stable long-term funding;

(d) have sufficient resources and funding to withstand severe liquidity stress; and

(e) maintain an adequate level of liquidity, according to the norms, methodologies, standards and guidance provided in the BPG issued by the AFSA.

(3) The detailed requirements specifying the calculation methodologies, parameters, metrics and formulae in respect of the primary liquidity requirements outlined in this Chapter are provided in the Banking Prudential Guideline (BPG) issued by the AFSA. The BPG also provides detailed guidance on calculation methodologies, formulae, parameters and norms involved in calculation of quantitative liquidity requirements like the Liquidity Coverage Ratio (LCR) and the Net Stable Funding Ratio (NSFR). It is suggested that this Chapter of the BBR, be read in conjunction with Chapter 9 of the BPG issued by the AFSA, to facilitate understanding of the regulatory requirements and compliance with them.

9.1 Liquidity Risk Management – Systems and Controls

(1) A Bank must:

(a) identify, assess, monitor, mitigate and, control its Liquidity Risk;

(b) implement and maintain a comprehensive Liquidity Risk management framework that is appropriate for the nature and level of its Liquidity Risk;

(c) hold adequate liquid assets, at all times, to ensure that it can meet all liabilities as they arise in the course of its business;

(d) maintain sufficient amount of high- quality liquid assets to enable it to withstand any reasonably foreseeable liquidity stress;

(e) develop and maintain a robust funding strategy to ensure that its activities are, and will continue to be, funded from stable sources;

(f) be able to identify potential liquidity shortfalls by constructing maturity ladders based on

appropriate periods and monitoring them;

(g) prepare a contingency funding plan to meet liquidity shortfalls; and

(h) implement and maintain a Liquidity Risk management policy which enables it to identify, assess, monitor, control and mitigate Liquidity Risk.

(2) The Liquidity Risk management policy must:

(a) be documented and include the Bank's risk appetite for Liquidity risk;

(b) be appropriate to the nature, scale and complexity of its activities;

(c) must establish procedures, systems, processes, controls and approaches to identify, measure, evaluate, manage and control or mitigate its Liquidity Riskand to ensure the integrity of its Liquidity Riskmanagement;

(d) establish, and must provide for the regular review of, the Bank's Liquidity Risktolerance and other quantitative and qualitative limits to control Liquidity Risk exposures and vulnerabilities;

(e) must set out the organizational structure, and must define the responsibilities and roles, for managing Liquidity Risk

(f) ensure that its risk management framework including but not limited to tools, methodologies and, systems enable it to implement its Liquidity Risk management policy; and

(g) be reviewed and updated at a reasonable frequency, but at least on an annual basis.

(3) The Liquidity Risk management policy must enable the Bank to carry out stress-tests using various scenarios based on appropriate assumptions. The policy must take into account the Bank's Liquidity Risk profile (including on-balance-sheet and off-balance-sheet risks) and tolerance in the context of the markets and macroeconomic conditions in which the Bank operates.

(4) The Bank must have specific policies on:

(a) the composition and maturity of assets and liabilities;

(b) the diversity and stability of funding sources; and

(c) the approach to managing liquidity in different currencies, across borders, and across business lines and legal entities.

Note Guidance in respect of the contents of a Bank's Liquidity Risk management policy which is required to satisfy the regulatory requirement in the Rule 9.1 is provided in the BPG issued by the AFSA.

9.2 Role of Governing Body—Liquidity Risk

(1) A Bank's Governing Body must ensure that its Liquidity risk management policy enables it to obtain a comprehensive bank-wide view of its Liquidity risk exposures and is consistent with the Bank's risk profile and systemic importance.

(2) A Bank's Governing Body must ensure that a comprehensive Liquidity Risk management framework is implemented and maintained; and that it is documented, and reviewed at least annually;

(3) A Bank must ensure that its Governing Body is responsible for monitoring the nature and level of Liquidity Risk assumed by it and for monitoring the Liquidity Risk management process.

(4) The Governing Body of the Bank must also ensure that:

(a) an appropriate senior management structure with clearly defined responsibilities and roles for Liquidity Risk management and for compliance with the Bank's Risk strategy, is established and maintained;

(b) the Bank's senior management and other relevant staff have the necessary experience to manage Liquidity Risk and to effectively implement the Liquidity Riskmanagement policy;

(c) appropriate liquidity limits covering Liquidity Risk management in both day-to-day and stressed conditions are set;

(d) stress-tests, funding strategies, contingency funding plans and holdings of high-quality liquid assets are effective and appropriate for the Bank;

(5) The Governing Body must regularly review reports on the Bank's liquidity and, where necessary, information on new or emerging Liquidity Risks, with a particular view towards monitoring Liquidity Risk. The Governing Body of the Bank must also review the Liquidity Risk tolerance and strategy at least on an annual basis.

(6) The Governing Body must approve:

(a) the Bank's Liquidity Risk management policy;

(b) its Liquidity Risk tolerance and risk strategy;

(c) its funding strategy; and

(d) its contingency funding plan.

9.3 Role of senior management – Liquidity Risk

In order to ensure sound management of the Bank's Liquidity Risk profile, the senior management of a Bank, must do all of the following:

(a) develop a Liquidity Riskmanagement policy in accordance with the Bank's approved Liquidity Risk tolerance;

(b) develop and implement a liquidity management strategy, processes and procedures, taking into account the Bank's approved Liquidity Risktolerance;

(c) ensure that the Bank maintains sufficient liquidity at all times;

(d) determine the structure, responsibilities and controls for managing Liquidity Risk, and for overseeing the liquidity positions, of the Bank and all of its branches and subsidiaries in all of the jurisdictions in which the Bank and its branches and subsidiaries are active, and set out that structure and those responsibilities and controls clearly in the Bank's liquidity policies;

(e) continuously monitor information on the Bank's liquidity developments and report to the Governing Body regularly.

(f) monitor market trends that could present significant, unprecedented or complex challenges for managing Liquidity Risk so that appropriate and timely changes can be made to its Liquidity

Riskmanagement policy.

(g) ensure that the Bank has adequate internal controls to ensure the integrity of its Liquidity Risk management processes;

(h) determine, and set out in the Bank's liquidity risk management policy, the structure, responsibilities and controls for managing Liquidity Risk and for overseeing the liquidity positions of all legal entities, branches and subsidiaries in the jurisdictions in which the Bank is active; and

(i) ensure that stress tests, contingency funding plans and holdings of high-quality liquid assets are effective and appropriate for the Bank;

(j) establish reporting criteria specifying the scope, manner and frequency of reporting for various recipients (such as the Bank's Governing Body and senior management and any relevant committee of the governing body) and fix who is responsible for preparing the reports; and

(k) establish the specific procedures and approvals necessary for making exceptions to policies and limits, including the escalation procedures and follow-up actions to be taken for breaches of limits.

9.4 Liquidity Risk tolerance

(1) A Bank's Liquidity Risk tolerance must be appropriate for the Bank's operations and strategy and its role in the financial systems in which it operates.

(2) The Bank must review its Liquidity Risk tolerance at least annually to reflect the Bank's financial condition and funding capacity.

(3) The Bank's Governing Body and senior management must ensure that the Bank's Liquidity Risk tolerance allows the Bank to effectively manage its liquidity in such a way that the Bank can withstand prolonged liquidity stress.

(4) The Bank must document its Liquidity Risk tolerance in a way that clearly states the trade-off between risks and profits.

9.5 Liquidity Risk Management – Processes and Procedures

(1) A Bank must have a sound process for identifying, measuring, monitoring and controlling Liquidity Risk. The process must include a robust framework for comprehensively projecting cashflows arising from assets, liabilities and off-balance-sheet items over an appropriate set of time horizons.

(2) A Bank must set limits to control its Liquidity Risk exposure and vulnerabilities. The limits and the corresponding escalation procedures must be reviewed regularly. The limits must be relevant to the business in terms of its location, the complexity of its operations, the nature of its products, and the currencies and markets it serves. If a limit is breached, the Bank must implement a plan of action to review the exposure and reduce it to a level that is within the limit.

(3) A Bank must actively manage its collateral positions, distinguishing between encumbered and unencumbered assets. The Bank must monitor the legal entity in which, and the physical location where, collateral is held and how collateral can be mobilised in a timely manner.

(4) A Bank must design a set of early warning indicators to help its daily Liquidity Risk management processes to identify the emergence of increased risk or vulnerabilities in its liquidity position or potential funding needs. The indicators must be structured so as to help identify negative trends in the Bank's liquidity position and to lead to an assessment and a potential response by management to mitigate the Bank's exposure to the trends.

(5) A Bank must have a reliable management information system that provides the governing body, senior management and other appropriate personnel with timely and forward-looking information on the Bank's liquidity position. A Bank must actively manage its intraday liquidity positions to meet payment and settlement obligations on a timely basis under both normal and stressed market conditions, thus contributing to the orderly functioning of payment and settlement systems.

(6) A Bank must develop and implement a costs and benefits allocation process for funding and liquidity. The process must appropriately apportion the costs of prudent liquidity management to the sources of Liquidity Risk, and must provide appropriate incentives to manage Liquidity Risk.

(7) A Bank that is active in multiple currencies:

(a) must assess its aggregate foreign currency liquidity needs and determine an acceptable level of currency mismatches; and

(b) must undertake a separate analysis of its strategy for each significant currency, considering possible constraints during periods of liquidity stress.

(8) Such a Bank must also maintain a portfolio of high-quality liquid assets consistent with the distribution of its liquidity needs by currency. A currency is considered as significant for a Bank if its liabilities denominated in that currency amount to 5% or more of its total liabilities.

9.6 Delegation of day-to-day Liquidity Risk Management

(1) A Bank may delegate the day-to-day management of its Liquidity Risk to another entity in the same Group for management on a Group basis only if:

(a) the Governing Body of the Bank has formally approved the delegation and keeps the delegation under review; and

(b) the Bank notifies the AFSA in writing of the delegation on a priori basis.

(2) If a Bank delegates the management of its Liquidity Risk in accordance with (1), the requirements in this Chapter continue to apply to the Bank.

9.7 Notification about liquidity concerns

(1) A Bank must ensure that its Governing Body and senior management are informed immediately of new and emerging liquidity concerns.

(2) The Bank must notify the AFSA of any significant concerns that the Bank may have about its current or future liquidity. In particular, the Bank must immediately notify the AFSA if the Bank experiences a severe liquidity stress. The notice must describe any remedial action taken, or planned, to address the concerns or liquidity stress.

9.8 Funding Strategy

(1) A Bank must establish, and must regularly review, strategies for the ongoing measurement and monitoring of funding requirements. The resultant funding strategy must provide effective diversification in the source and nature of its funding.

(2) A Bank must ensure that the funding strategy is documented and is approved by its Governing Body. A Bank must ensure that its funding strategy is reviewed regularly and at least annually and is updated as necessary in light of changed funding conditions and any change in the Bank's strategy.

(3) The Bank must promptly inform the AFSA of any material changes to its funding strategy.

(4) A Bank must assess regularly its capacity to raise funds quickly. A Bank must assess market access under a variety of normal and stressed conditions.

(5) A Bank must:

(a) develop and document a 3-yearly funding strategy;

(b) identify the main factors that affect its ability to raise funds;

(c) monitor those factors closely to ensure that estimates of fund raising capacity remain valid;

(d) maintain a continuing presence in its chosen funding markets; and

(e) maintain strong relationships with funds providers

9.9 Stress-testing and Liquidity Risk tolerance

(1) A Bank must carry out stress-testing using various short-term and long-term Bank-specific and market-wide liquidity stress scenarios, to identify sources of potential liquidity strain and to ensure that the Bank's exposures remain within its Liquidity Risk tolerance. The tests must be carried out at intervals appropriate for the nature, scale and complexity of the Bank's business and for its risk profile.

(2) In respect of the stress testing, a Bank must

(a) use conservative and regularly-reviewed assumptions;

(b) use scenarios based on varying degrees of short-term and protracted institution-specific and systemic market-wide stress (individually and in combination); and

(c) include a cash-flow projection for each scenario tested, based on reasonable estimates of the impact (both on and off-balance sheet) of that scenario on the Bank's funding needs and sources.

(3) A Bank's stress test scenarios and related assumptions must be fully documented and frequently reviewed to ensure they remain appropriate

(4) The Bank must report to the AFSA, in the form that the AFSA directs, the results of its stress-testing. The Bank must use results to adjust its positions, to review its Liquidity Risk management policy, and to develop effective contingency funding plans.

9.10 Contingency Funding Plan

(1) A Bank must have a documented Contingency Funding Plan (CFP) that sets out clearly its strategies for addressing liquidity shortfalls in emergency situations. The plan must set out available funding sources and the amount of funds that the Bank estimates can be obtained from those sources. A Bank must ensure that its CFP is approved by its Governing Body.

(2) The CFP must be flexible enough to enable the Bank to respond quickly in various situations. It must address the issues over various periods (including intraday) and must establish clear lines of responsibility and communication.

(3) The Bank must review and update its CFP every year (or more often as changing business or market circumstances require) for the governing body's approval.

(4) The CFP must be commensurate with a Bank's complexity, risk profile and scope of operations and its role in the financial systems in which it operates.

Note Detailed standards and guidance in respect of a Bank's Contingency Funding Plan which is required to satisfy the regulatory requirement in the Rule 9.10 is provided in the BPG issued by the AFSA.

(5) A Bank must review and update its CFP, at least annually for approval by its Governing Body, or more frequently if required by business or market circumstances. It must test its CFP regularly to ensure it is effective and operationally feasible.

(6) A Bank must ensure that its CFP is consistent with its business continuity and disaster recovery arrangements and can operate in situations where business continuity arrangements have been invoked.

9.11 Relation to Internal Capital Adequacy Assessment Process (ICAAP)

A Bank must be able to demonstrate to the AFSA that its ICAAP adequately captures Liquidity Risk. This is so even if the effect of Liquidity Risk on the Bank's capital is indirect (for example, by reducing the value of the Bank's assets at the time they are realised).

9.12 Liquidity Risk in foreign currency business

(1) This rule applies to a Bank if:

(a) the Bank's foreign currency business is significant; or

(b) the Bank has significant exposure in a particular foreign currency.

(2) A Bank's business in a currency is significant, and the Bank's exposure in a currency is significant, if 5% or more of the gross value of its balance-sheet assets, balance-sheet liabilities or off-balance-sheet financial activities is denominated in the currency.

(3) A Bank to which this rule applies must undertake separate analysis of its policies (and monitor its liquidity needs) for each significant currency.

(4) The Bank must carry out regular stress-testing to determine the extent of mismatches in each significant currency and, if appropriate, to set limits on its cash flow mismatches for each such currency and for all those currencies in total.

(5) The Bank must monitor its liquidity needs in each significant currency and must be able to demonstrate to the AFSA that it can transfer liquidity from one currency to another across jurisdictions and legal entities.

9.13 Management of encumbered assets

A Bank must set a prudent limit for encumbered assets. The Bank must keep adequate records to enable it to disclose the level of its encumbered assets to the AFSA, if required to do so.

9.14 Consequences of breaches and changes

(1) If a Liquidity Risk limit is breached, a Bank must review the exposure and reduce it to a level that is within the limit.

(2) The Bank must make appropriate adjustments to the management of its Liquidity Risk in the light of the Bank's changing risk profile, funding strategy, and developments in the markets and

macroeconomic conditions in which it operates.

9.15 Liquidity Requirements

(1) The quantitative liquidity requirements and liquid asset maintenance requirements defined in this Chapter, apply to a Bank on a solo basis, unless specified.

(2) The AFSA may require a Bank to comply with the liquidity requirements defined in this Chapter to its Financial Group, if the Bank and its Financial Group are subject to consolidated supervision.

(3) A Bank must calculate and comply with the following liquidity requirements, which are detailed in the remaining sections of this Chapter.

(a) Liquidity Coverage Ratio

(b) Net stable funding ratio

(c) Maturity Mismatch Limits

9.16 Liquidity Coverage Ratio (LCR)

(1) The Rules 9.16 to 9.18 apply only to Banks licensed to conduct the Regulated Activity of Accepting Deposits. These rules, regarding compliance with LCR requirement are not applicable to Broker Dealers.

Note Although the references in these rules are made to Banks, for the sake of clarity it is reiterated that the use of the term Bank in Rules 9.16 to 9.18 only apply to Banks conducting the Regulated Activity of Accepting Deposits.

(2) A Bank must, except as provided in Rule 9.17, maintain a LCR of at least 100% from 1st January 2019 and a LCR of at least 90% till 31st December 2018.

(3) A Bank must calculate its LCR using the following formula and in accordance with the methodology, formulae, parameters and guidance set out in Chapter 9 of the BPG issued by the AFSA. LCR is calculated in accordance with the following formula:

$$LCR = \frac{Value\ of\ stock\ of\ HQLA}{Total\ Net\ Cash\ Outflows\ over\ the\ next\ 30\ calendar\ days}$$

Note Detailed guidance specifying the tools, methodologies, parameters and formulae for calculating the LCR are set out in Section D of Chapter 9 of the BPG issued by the AFSA.

(4) A Bank must calculate its LCR on an ongoing basis and separately for each material currency, in which it does banking business. A Bank must report to the AFSA its aggregate LCR calculation in USD.

(5) The AFSA may by written notice to A Bank in relation to the LCR Requirement applying to it:

(a) adjust the LCR Requirement;

(b) adjust requirements under section D of Chapter 9 of the BPG for calculating its stock of HQLA or the Total Net Cash Outflows;

(c) alter the calculation methodologies or parameters for the purposes of the LCR

Requirement;

(d) disapply the LCR Requirement; or

(e) impose additional requirements based on its assessment of the Liquidity Risk exposure of that Bank.

(6) If the AFSA amends a requirement under (4)(a), (b), (c) or (e), the Bank must comply with the requirement as amended. If the AFSA disapplies a requirement under (1)(d), the Bank need not comply with that requirement.

(7) The procedures in Schedule 1 of the AIFC Financial Services Framework Regulations No 18 of 2017, will apply to a decision of the AFSA under (4)(a),(b),(c) or (e).

(8) If the AFSA decides to exercise its power under (4)(a),(b),(c) or (e), the Bank may refer the matter to the AIFC Court for review.

(9) If the AFSA considers that a Bank is overly reliant on cash inflows from a single wholesale counterparty or a small number of wholesale counterparties, the AFSA may direct the Bank as to how such cash flows are to be treated in the calculation of its LCR.

(10) The AFSA may allow a Bank that is a branch, or is a Subsidiary of an entity established outside the AIFC, to recognise, as cash inflow, access to its parent entity's funds by way of a committed funding facility, up to a limit specified in the facility documentation. The facility:

(a) must be an irrevocable commitment; and

(b) must be appropriately documented.

9.17 Liquidation of assets during periods of stress

During a period of financial or liquidity stress, a Bank may liquidate part of its stock of HQLA and use the cash generated to cover cash outflows. Its level of HQLA may fall below the levels required under its LCR Requirement to the extent necessary to deal with cash outflows during that period.

9.18 Notification if LCR Requirement not met

A Bank must notify the AFSA in writing immediately if it does not meet or becomes aware of circumstances that may result in it not meeting, its LCR Requirement. This obligation applies even during a period of stress referred to in Rule 9.17.

9.19 Net Stable Funding Ratio (NSFR)

(1) The Rules 9.19 to 9.20 apply only to Banks licensed to conduct the Regulated Activity of Accepting Deposits. These rules, regarding compliance with NSFR requirement are not applicable to Broker Dealers.

Note Although the references in these rules are made to Banks, for the sake of clarity it is reiterated that the use of the term Bank in Rules 9.19 to 9.20 only apply to Banks conducting the Regulated Activity of Accepting Deposits.

(2) A Bank must calculate its NSFR using the following formula and in accordance with the methodology, formulae, parameters and guidance set out in Section E of Chapter 9 of the BPG issued by the AFSA. NSFR is calculated in accordance with the following formula:

$$NSFR = \frac{Available\ Stable\ Funding\ (ASF)}{Required\ Stable\ Funding\ (RSF)} * 100$$

The ASF and RSF used in this calculation of NSFR are to be determined in accordance with the methodology, formulae and guidance provided in Section E of Chapter 9 of the BPG.

(3) A Bank must maintain a NSFR of at least 100%, at all times. That is, its ASF must always be equal to or greater than its RSF.

9.20 Notification of breach of NSFR Requirement

(1) A Bank must notify the AFSA in writing immediately if it fails to meet, or becomes aware of circumstances that may result in it not meeting, its NSFR Requirement. In the notification the Bank must clearly explain:

(a) why it ceased to meet, or thinks it may cease to meet, the requirement;

(b) when it expects to again be able to meet the requirement; and

(c) what it has done and will do to ensure that it meets the requirement in future, or continues to meet it, as the case requires.

(2) A Bank that gives such a notification should discuss with the AFSA what further steps it should take to deal with the situation.

9.21 The Maturity Mismatch approach

(1) A Bank must use the Maturity Mismatch approach, as set out in this rule, to measure liquidity. Under this approach, a Bank must determine the net cumulative Maturity Mismatch position for each time band by:

(a) determining, in accordance with the methodology in section F of Chapter 9 of the BPG, the inflows (assets) and outflows (liabilities) which are, subject to their falling within one of the time bands, to be included in the Maturity Ladder and at what maturities;

(b) inserting each inflow (asset) and outflow (liability) into one or more of the following time bands on the Maturity Ladder:

(i) sight – 8 days; or

(ii) sight – 1 month; and

(c) subtracting outflows (liabilities) from inflows (assets) in each time band.

Note Detailed guidance specifying the tools, methodologies, parameters and formulae for calculating the LCR are set out in Section F of Chapter 9 of the BPG issued by the AFSA.

(2) A Bank must determine a net cumulative Maturity Mismatch position for each time band in respect of each of the deposits it has raised as a means of funding.

(3) A Bank must calculate its net cumulative Maturity Mismatch position as a percentage of the means of funding in each time band in accordance with the following formula:

Total deposit liabilities net cumulative Maturity Mismatch (%) =

$$\frac{Net\ Cumulative\ Maturity\ Mismatch}{Total\ Deposits} * 100$$

(4) A Bank must ensure that its net cumulative Maturity Mismatch position as calculated in (3) above in each time band does not exceed the following:

(a) sight – 8 days, negative 15%; and

(b) sight – 1 month, negative 25%.

A Bank must notify the AFSA in writing immediately if it exceeds these net cumulative Maturity Mismatch limits.

9.22 Recognition of funding facility from parent entity

(1) This rule applies to a Bank that is operating as a branch in the AIFC.

(2) The AFSA may allow such a Bank to recognise, as an asset, access to its parent entity's funds by way of a committed funding facility, up to a limit specified in the facility documentation. The facility:

(a) must be an irrevocable commitment; and

(b) must be appropriately documented.

CHAPTER 10 Group Risk

Introduction

Guidance

(1) This Chapter deals with management of Group Risk exposure of a Bank. Group Risk refers to the risk of potential losses incurred by a Bank on account of its relationship with other members of its Financial Group, if it were to be part of one.

(2) This Chapter includes requirements that a Bank implement:

(a) an effective management framework for Group Risk exposure;

(b) a specified methodology for the calculation of Financial Group Capital Resources and Financial Group Capital Requirements.

(3) This Chapter also includes requirements limiting Financial Group exposures.

(4) The detailed requirements specifying the calculation methodologies, parameters, and guidance in respect of the primary rule requirements outlined in this Chapter are provided in Chapter 10 of the Banking Prudential Guideline (BPG) issued by the AFSA. It is suggested that this Chapter of the BBR, be read in conjunction with Chapter 10 of the BPG issued by the AFSA, to facilitate understanding of the regulatory requirements and compliance with them.

10.1 Financial Group – definition

(1) The AFSA may require a Bank to:

(a) form a Financial Group with any other entity within its Group; or

(b) include within its Financial Group any other entity within its Group;

where the AFSA considers it necessary or desirable to do so in the interests of effective supervision of the Bank.

(2) A Bank may, for the purposes of this section, exclude from its Financial Group any entity the inclusion of which would be misleading or inappropriate for the purposes of Financial Group supervision, provided the Bank has obtained the AFSA's prior written approval.

(3) A Bank must provide to the AFSA, if requested, any of the following information in relation to its Group or Financial Group:

(a) details as to the entities within the Group or Financial Group;

(b) the structure of the Group or Financial Group; and

(c) the systems and controls in place to manage Group Risk.

10.2 Group Risk – Systems and Controls

(1) A Bank that is a member of a Group must establish and maintain systems and controls for the purpose of:

(a) monitoring the effect on the Bank of:

(i) its relationship with other members of its Group;

(ii) its membership in its Group; and

(iii) the activities of other members of its Group;

(b) monitoring compliance with Financial Group supervision requirements below, including systems for the production of relevant data;

(c) monitoring funding within the Group; and

(d) monitoring compliance with Financial Group reporting requirements.

(2) A Bank must have systems and controls to enable it to determine and monitor:

(a) its Financial Group Capital Requirement; and

(b) whether its Financial Group Capital Resources is, and is likely to remain, in compliance with the regulatory capital ratios specified in Chapter 4 of BBR.

(3) Such systems and controls referred in (2), must include an analysis of:

(a) realistic scenarios which are relevant to the circumstances of the Financial Group; and

(b) the effects on the Financial Group Capital Requirement and on the Financial Group Capital Resources if those scenarios occurred.

(4) A Bank's Governing Body must ensure that the Bank's group risk management policy addresses, on a group-wide basis, all risks arising from the Bank's relationship with every other member of its group.

10.3 Financial Group Capital Requirement

(1) The Financial Group Capital requirements specified in this rule does not apply to a Bank if:

(a) the Bank's Financial Group is already the subject of Financial Group prudential supervision by the AFSA as a result of the authorisation of another Financial Group member;

(b) the AFSA has confirmed in writing, in response to an application from the Bank, that it is satisfied that the Bank's Group is the subject of consolidated prudential supervision by an appropriate regulator; or

(c) except where the AFSA has directed the inclusion of an entity pursuant to Rule 10.1, the percentage of total assets of Banks and Financial Institutions in the Financial Group is less than 40% of the total Financial Group assets.

(2) If a Bank receives confirmation in writing from the AFSA in accordance with (1)(b) above, it must immediately advise the AFSA in writing if there is any change in the circumstances upon which such a confirmation was based.

(3) The regulatory capital ratios specified in Rule 4.12, which applies to a Bank, also apply to its Financial Group. A Bank forming part of a Financial Group, must ensure that its Financial Group meets or exceeds the minimum level of regulatory capital ratios, as defined in Rule 4.12, calculated on a consolidated basis for the entire Financial Group.

(4) A Bank must ensure at all times that its Financial Group capital resources exceed its Financial

Group capital requirement.

(5) For the purpose of (3) above, Financial Group capital resources and Financial Group capital requirement must be calculated for the Financial Group as a whole, using the methods specified in Chapter 4 of BBR.

(6) An Bank must calculate its Financial Group Capital Requirement by applying the accounting consolidation method, which calculates the Capital Requirement of the Financial Group based on the Financial Group's consolidated financial statements, and using applicable prudential rules in BBR. For the purposes of this rule, the consolidated financial statements of the Financial Group must be prepared in accordance with International Financial Reporting Standards.

(7) A Bank must calculate its Financial Group Capital Resources by applying either of the following methods:

(a) the accounting consolidation method, which calculates the Capital Resources of the Financial Group based on the Financial Group's consolidated financial statements; or

(b) the aggregation method, which is the sum of:

(i) the Capital Resources of the Parent of the Financial Group;

(ii) subject to (2), the Capital Resources of any Banks and Financial Institutions included in the Financial Group, less amount of investments made by one Financial Group member in another; and

(iii) the Financial Group's proportionate share of Capital Resources in Financial Institutions not included in the Financial Group in which any member of the Financial Group has a participation.

(8) In calculating its financial group capital resources, the Bank must not include capital resources or adjusted capital resources (as the case may be) of subsidiaries or participations of that group to the extent that those capital resources or adjusted capital resources exceed the capital requirement for that Subsidiary or participation and are not freely transferable within the group.

(9) Deductions for Qualifying Holdings under Rule 4.29 may be calculated based on the Financial Group's total T1 and T2 Capital.

10.4 Financial Group Concentration Risk limits

(1) Unless the AFSA directs otherwise, a prudential limit imposed in the BBR rules that applies to a Bank, also applies to the Bank's Financial Group.

(2) A Bank must ensure that its Financial Group's Exposure, to a Counterparty or group of Closely Related Counterparties does not exceed 25% of its Financial Group's Capital Resources.

(3) A Bank must ensure that the sum of its Financial Group Large Exposures, to a Counterparty or group of Closely Related Counterparties does not exceed 800% of its Financial Group's Capital Resources.

CHAPTER 11 Supervisory Review and Evaluation Processes

Introduction

Guidance

(1) This Chapter implements the critical Pillar II of the Basel III framework. Pillar II offers an avenue for addressing all the risk exposures faced by a Bank, which have not been covered in the estimation of capital requirements to absorb potential unexpected losses. The rules in this Chapter set out the regulatory requirements for Banks to carry out a self-assessment of their risks which can be reviewed and assessed by the regulator. This Chapter details the rules stipulating the need for Banks to complete internal risk assessments followed by an internal capital adequacy assessment process (ICAAP). The AFSA will review the results of the ICAAP. This Chapter also sets out how the AFSA may impose an additional capital requirement on a bank-specific basis in addition to the minimum capital requirement specified in Chapter 4 of the BBR.

(2) The detailed requirements specifying the methodologies, parameters, and guidance in respect of the ICAAP and Supervisory review process requirements for a Bank are provided in Chapter 11 of the Banking Prudential Guideline (BPG) issued by the AFSA. It is suggested that this Chapter of the BBR, be read in conjunction with Chapter 11 of the BPG issued by the AFSA, to facilitate understanding of the regulatory requirements and compliance with them.

11.1 Application to a Financial Group

Where a Bank to which this Chapter applies is part of a Financial Group, this Chapter applies on a consolidated basis in relation to all the entities within the Financial Group.

11.2 Internal Capital Adequacy Assessment Process (ICAAP)

(1) A Bank must implement and maintain an ICAAP which details the processes and procedures by which the Bank will assess and maintain adequate Capital Resources in relation to the risks faced by it.

(2) The Bank must conduct an ICAAP assessment at least annually giving due regard to the guidance in Chapter 11 of the BPG.

(3) The ICAAP assessment conducted by the Bank pursuant to (2) must be approved by its Governing Body and then submitted to the AFSA within four months from the end of the Bank's financial year.

(4) In addition to (2), the Bank must conduct an ICAAP assessment:

(a) whenever there is material change to the business, strategy, nature or scale of the activities of the Bank which may have a significant impact on its risk profile or adequacy of its regulatory capital; or

(b) as and when required by the AFSA.

(5) The ICAAP assessment conducted by the Bank pursuant to (4) must be approved by its Governing Body and then submitted to the AFSA within two months from the date of such material change or requirement.

(6) A Bank must ensure that an ICAAP assessment is documented in writing and includes details of:

(a) the calculations and models used in the determination of the level of Capital Requirements which it considers will be adequate to cover all the risks identified by its ICAAP assessment;

(b) the Bank's strategies and plans to ensure availability of the level of capital determined by the ICAAP;

(c) specifications of any models used in the ICAAP, including the underlying assumptions, parameters, and results of back-testing; and

(d) any other relevant information, giving due and appropriate regard to the guidance in Chapter 11 of the BPG.

(7) A Bank must retain the records of an ICAAP assessment for at least six years.

11.3 Imposition of an Individual Capital Requirement

(1) The AFSA may, subject to (3) and (4), at any time by written notice to a Bank:

(a) impose an Individual Capital Requirement; or

(b) vary or withdraw an Individual Capital Requirement.

(2) The AFSA may impose or vary an Individual Capital Requirement by written notice, on its own initiative, where the AFSA forms the view that the Bank's Capital Requirement is insufficient to address adequately all its risks.

(3) The AFSA will, in addition to prescribing an Individual Capital Requirement, also specify in the notice the types and amounts of Capital Resources required to meet the Individual Capital Requirement.

(4) Any decisions made under this Rule 11.3 will be subject to the decision-making procedures set out in Schedule 1 of the AIFC Financial Services Framework Regulations (FSFR).

(5) If the AFSA decides to exercise its power under (2) after a Licence has been granted, the Bank may refer the matter to the AIFC Court for review.

(6) A Bank must have and maintain, at all times, regulatory capital as defined in by the rules in Chapter 4 of BBR as well as capital meeting the types and amounts specified in the notice issued to it under this rule to meet its Individual Capital Requirement.

CHAPTER 12 Public Disclosures Requirements

Introduction

Guidance

(1) This Chapter implements the Pillar III of the Basel III framework. Pillar III is aimed at facilitating market discipline which is considered as one of the effective mechanisms to achieve safety and soundness of banks. The rules in this Chapter set out the regulatory requirements for Banks to make periodic disclosures of relevant and material information about their business activities and data on risk exposures assumed by them.

(2) The detailed public disclosure requirements specifying the data items to be disclosed and related guidance are provided in Chapter 12 of the Banking Prudential Guideline (BPG) issued by the AFSA. It is suggested that this Chapter of the BBR, be read in conjunction with Chapter 12 of the BPG issued by the AFSA, to facilitate understanding of the regulatory requirements and compliance with them.

12.1 Application to a Financial Group

(1) A Bank, which is a member of a Financial Group, according to Chapter 10 of BBR, must ensure that the detailed disclosures specified in Chapter 12 of the BPG are made on a consolidated basis, at the level of the Financial Group.

(2) A Bank which is a Subsidiary of a regulated bank or financial institution or another Bank, which is already subject to equivalent public disclosure requirements, does not need to comply with the requirements in this Chapter to the extent that it meets those equivalent public disclosure requirements.

12.2 Disclosure policy

(1) A Bank must implement and maintain a written disclosure policy that:

(a) sets out the Bank's approach for determining which of the disclosures set out in Chapter 12 of the BPG it needs to make;

(b) details the processes and procedures and its internal controls in relation to such disclosure details the medium for disclosure that most appropriately meets the purposes of this chapter; and

(c) is approved by the Governing Body of the Bank.

(2) A Bank must ensure that appropriate verification, whether internal or external, is performed in relation to any disclosure, and take all reasonable steps to ensure its accuracy and timeliness.

(3) To the extent that any required disclosure is substantially similar to a disclosure required of the Bank under the International Financial Reporting Standards, a disclosure under such standards must be taken to meet the requirement for disclosure under this Chapter.

12.3 Disclosure frequency, locations and omissions

Frequency

(1) The disclosures set out in this Chapter must be made by the Bank at least once a year, other than disclosures of CET1 Capital, T1 Capital and T2 Capital, deductions from Capital Resources, Liquidity Coverage Ratio and Leverage Ratios which must be made on a quarterly basis.

(2) Reporting deadlines must be in accordance with quarterly and annual reporting obligations under Chapter 3 of BBR.

Locations

(3) A Bank must, subject to (2), make these disclosures either in its annual report or periodic financial statements.

(4) A Bank may disclose the items marked as quantitative in Chapter 12 of the BPG in a medium or location other than its annual report or periodic financial statements, provided that:

- (a) it has prior approval of the AFSA to do so;
- (b) the annual report or periodic financial statements contain clear references to the location of such disclosures; and
- (c) such disclosures are readily accessible by the market.

Omissions

(5) A Bank may omit certain disclosures if the omitted item is:

- (a) not material, in accordance with the concept of materiality under the International Financial Reporting Standards,
- (b) proprietary in nature, and the disclosure of the relevant information to the public would undermine the Bank's competitive position or render the Bank's investments in products and systems less valuable, or
- (c) confidential in nature, and the disclosure of the relevant information would violate or jeopardise confidentiality agreements with Clients or Counterparties.

(6) Where in reliance upon (5)(b) or (c) above, a Bank omits an item that is marked as a quantitative disclosure in Chapter 12 of the BPG, it must disclose general qualitative information about the subject matter of that particular requirement, together with the reasons for the omission.