

HKMA publishes Report on Loss-Absorbing Capacity Requirements Implementation in Hong Kong

The following is issued on behalf of the Hong Kong Monetary Authority:

The Hong Kong Monetary Authority (HKMA) published today (February 8) the Report on Loss-Absorbing Capacity Requirements Implementation in Hong Kong. This report provides an overview of the loss-absorbing capacity (LAC) requirements implementation programme in Hong Kong, outlines the progress made and summarises the HKMA's observations and related policy expectations.

LAC refers to financial resources of a financial institution (FI) which can be used to absorb losses and support recapitalisation in the event the FI becomes likely to fail. The availability of sufficient LAC is crucial for stabilising a failing FI and restoring it to viability in an orderly resolution (Note 1), thereby mitigating risks posed to financial stability. By allowing losses to be imposed on shareholders and LAC debt instruments holders, LAC serves as a disincentive to excessive risk-taking by an FI and protects public money.

To ensure adequate LAC resources for resolution purposes, the HKMA introduced the Financial Institutions (Resolution) (Loss-absorbing Capacity Requirements-Banking Sector) Rules (LAC Rules), which commenced operation on December 14, 2018. Over the past five years, the HKMA has been working closely with relevant authorized institutions (AIs), including all domestic systemically important AIs, to build up a layer of LAC resources as part of the resolution planning process (Note 2).

This report covers the LAC positions of AIs, issuances and features of LAC debt instruments, approaches to ensuring compliance with LAC Rules requirements, the interaction between LAC requirements and the capital regime, and other matters pertinent to the implementation.

The Chief Executive of the HKMA, Mr Eddie Yue, said, "Establishing sufficient LAC resources is an important aspect in enhancing the resolvability of banks and strengthening the resilience of the Hong Kong's banking system. We are delighted to share some of the key developments and milestones achieved. As part of our ongoing resolution planning process, the HKMA will continue to work closely with relevant banks on their build-up and maintenance of LAC resources in a prudent and proportionate manner, taking into account international experiences, as well as evolving economic and market conditions."

The [report](#) is available on the HKMA website.

Note 1: Resolution is a process to manage the potential failure of an FI in an orderly manner, with the purpose of maintaining the stability and

effective working of the financial system, while seeking to protect public money. The Financial Institutions (Resolution) Ordinance (FIRO), which came into effect on July 7, 2017, establishes the legal basis for a cross-sectoral resolution regime in Hong Kong. Under the FIRO, the Monetary Authority is the resolution authority for banking sector entities which include all AIs.

Note 2: In order for resolution to be feasible and credible, FIs need to be organised and managed at all times in a way that facilitates the effective use of powers by the resolution authorities in the event of a potential failure. To this end, the HKMA sets resolution standards and conducts resolution planning for individual AIs well in advance of any actual distress. Through the resolution planning process, the HKMA works with relevant AIs to implement necessary changes to their legal structures, business operations and/or financial resources in order to enhance their resolvability.