Reserve Bank of New Zealand
Te Pūtea Matua

Capital Review: Changes to Bank Disclosure

Dual reporting by modelling banks and other changes applying to all New Zealand-incorporated banks

22 February 2022

CONSULTATION PAPER

Who is this consultation aimed at?

The proposals we are consulting on will be relevant for anyone who takes an interest in the six-monthly disclosure statements published by New Zealand-incorporated banks.

The proposals will also be of interest to the banks that would need to make the proposed additional disclosures. Most of the changes only affect banks that are accredited to use modelling approaches to capital adequacy, but a few of the proposed changes would apply to all New Zealand-incorporated banks.

Submissions

The Reserve Bank of New Zealand - Te Pūtea Matua invites submissions on the proposed disclosure changes and draft new text for the disclosure Orders in Council by 5:00pm on 3 May 2022. Early submissions on priority issues are welcome, and would not preclude a fuller, later submission.

Please note the disclosure on the publications of submissions below.

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Publication of submissions:

All information in submissions will be made public unless you indicate you would like all or part of your submission to remain confidential. Respondents who would like part of their submission to remain confidential should provide both a confidential and public version of their submission. Apart from redactions of the information to be withheld (i.e. blacking out of text) the two versions should be identical. Respondents should ensure that redacted information is not able to be recovered electronically from the document (the redacted version will be published as received).

Respondents who request that all or part of their submission be treated as confidential should provide reasons why this information should be withheld if a request is made for it under the Official Information Act 1982 (OIA). These reasons should refer to section 105 of the Reserve Bank of New Zealand Act 1989, section 54 of the Non-Bank Deposit Takers Act, section 135 of the Insurance (Prudential) Supervision Act 2010 (as applicable); or the grounds for withholding information under the OIA. If an OIA request for redacted information is made the Reserve Bank will make its own assessment of what must be released taking into account the respondent's views.

We plan to publish an anonymised summary of the responses received in respect of this Consultation Paper.

Contents

1 Introduction

We launched a fundamental review of our capital adequacy framework for New Zealand (the 'Capital Review') in March 2017[1].

In the Capital Review consultation paper on the calculation of risk-weighted assets (December 2017), we proposed a number of different options for improving the transparency of capital calculations under the internal ratings-based ('IRB') approach to calculating risk-weighted assets ('RWAs') for credit risk. In the July 2018 feedback statement we confirmed that our preferred option was what we referred to as 'dual reporting'.

Under this approach, we would require banks that are accredited to use the IRB approach ('IRB banks') to include additional information in their six-monthly published disclosure statements. The additional information would cover RWAs and the resulting capital ratios recalculated as if the bank was subject to the standardised approach, alongside the actual RWAs and capital ratios already disclosed. (The standardised approach is the risk-weighting method used by banks other than IRB banks.)

In the final decisions on the Capital Review published in December 2019[2], we confirmed that we would go ahead with dual reporting. On the timetable included in the final decisions, we planned that the new capital framework documents would be imposed on banks via changes in conditions of registration from 1 July 2020, and that the dual reporting requirement would begin on 1 January 2021. We extended the planned dates of a number of our regulatory initiatives following the COVID-19 outbreak in March 2020[3]. On our current timetable we plan to implement dual reporting with effect from 1 July 2022.

In reaching our decision on dual reporting in July 2018, we noted that the decision was made on the understanding that the requirement would not be too onerous for IRB banks as long as it aligned with the 'standardised floor'. The standardised floor is another Capital Review decision, which imposes a minimum on the RWAs that an IRB bank calculates using its internal credit risk models, set at 85% of what the equivalent RWAs would be under the standardised approach. We also acknowledged that we would need to address the risk of confusion from banks publishing two alternative capital calculations. We noted that we would need to make further decisions on the detail of dual reporting.

This paper proposes changes needed to IRB banks' disclosure statements to implement dual reporting, taking those considerations into account.

This paper also proposes a few other additions to disclosure requirements, related to the Capital Review, and one removal. The paper goes through each of the following topics in turn, with tables to give examples of what the proposed disclosure would look like, with sample figures included:

- For an IRB bank, an explanation of how the standardised floor for RWAs under the IRB approach is reflected in the bank's capital ratio calculations (the floor came into effect on 1 January 2022).
- Dual reporting for IRB banks.

1 See rbnz.govt.nz/research-and-publications/speeches/2017/speech-2017-03-07
2 See rbnz.govt.nz/news/2019/12/higher-bank-capital-means-safer-banking-system-for-all-new-zealanders
3 See rbnz.govt.nz/news/2020/03/regulatory-relief-to-provide-headroom-for-customer-focus-and-risk-management

- For an IRB bank, a more detailed breakdown, by standardised risk-weight, of exposures previously in the bank's Sovereign and Bank IRB exposure classes, which all moved to the standardised approach from 1 January 2022.
- For all New Zealand-incorporated banks, requirements to disclose separately the Credit Valuation Adjustment (CVA) charge arising on derivatives, and exposures to Qualifying Central Counterparties.
- Removal of the columns for 'Minimum Pillar 1 capital requirements' and similar, from the tables showing the breakdowns of Credit Risk RWAs.

Annex A provides draft text to be inserted into the current Order in Council that sets disclosure requirements for New Zealand-incorporated banks ('the OIC'), to put into effect all the additional disclosure discussed in the body of the paper.

2 Disclosure of Standardised Floor Calculation

The standardised floor is a new part of the capital adequacy calculation for IRB banks. The floor applies to an IRB bank's aggregate RWAs on all exposure that the bank risk-weights using either one of its accredited models for credit risk, or the 'supervisory slotting' approach to certain types of corporate exposures. To apply the floor, the bank has to recalculate RWAs on all such exposures using the standardised approach, and the floor is set at 85% of the standardised equivalent RWAs. So for its capital ratio calculation, the aggregate value of RWAs the bank must use for these exposures is the greater of: modelled RWAs; and 85% of the standardised equivalent RWAs for the exposures.

In the interests of transparency, we think that it makes sense to require disclosure of how the floor applies. We propose a new table to show the components of the calculation, as follows:

Application of Standardised Floor to Total Credit Risk RWAs

	RWAs for modelled exposures		RWAs for standardised exposures	Total credit risk RWAs
	RWAs calculated using models	**RWAs recalculated using standardised approach**		
Total IRB and supervisory slotting exposures[1]	1060[1]	1300		
Standardised floor		1105		
RWAs with floor applied		1105	212[1]	1317

Footnote 1: a scalar of 1.06 currently applies to the RWA calculation of these amounts.

The footnote with an explanation of where the scalar applies is to comply with the existing disclosure requirement in Schedule 11, clause 9 of the OIC. We are not proposing any change to this clause and to the way that the scalar is reflected in disclosure. The numbers in this sample table reflect the capital requirements that apply from 1 January to 30 September 2022, during which time the current scalar of 1.06 continues to apply to all credit risk RWAs calculated by IRB banks.[4]

The 'supervisory slotting' approach is not a fully modelled approach, but it applies to a subset of the corporate exposure class under the IRB approach. Also, these exposures are subject to different risk-weightings under the standardised approach. For these reasons, the exposures subject to supervisory slotting are included in 'RWAs for modelled exposures' for the purpose of calculating the standardised floor, and will also remain subject to the scalar.

The disclosure will also require the bank to provide an explanation of how the floor applies: this might, for example, be added as another footnote to the table.

3 Dual Reporting

Our aim is that the dual reporting of standardised equivalent capital calculations should be clearly distinct in a bank's disclosure statement from the calculations that reflect the bank's capital ratio calculations for compliance purposes. To reflect this, we propose to insert the new clauses that will implement the various components of dual reporting between Clauses 15 and 16, in Schedule 11 of the OIC (Clause 15 requires disclosure of actual capital ratios, and is the last clause relating to the bank's own regulatory minimum ratios, while Clause 16 requires solo capital ratios, which is similar to dual reporting, in the sense that they are only calculated for disclosure purposes, not to meet regulatory minima). Although the new clauses could be added anywhere in the Schedule (banks do not have to follow the order in the Schedule in their disclosure statements), we think it is better to signal this distinction in the OIC.

We would expect banks to present all dual reporting information separately from the disclosure of their main actual capital compliance calculations, with possibly a subheading to explain the nature of the standardised equivalent disclosures.

Under the following three sub-headings we cover each of the possible components of dual reporting:

- summary disclosure of standardised equivalent capital ratio calculations;
- summary comparison of modelled exposure amounts and RWAs with their standardised equivalents, broken down by main IRB exposure class; and
- more detailed comparison of the risk-weighting of modelled exposures with their standardised equivalents, broken down into IRB banks' internal risk groupings.

Our preference is for all three components to be included.

4 As specified in Section C1.4 of BPR130: Credit Risk RWAs Overview. From 1 October 2022, the scalar will increase to 1.2 but will only apply to modelled RWAs.

3.1 Disclosure of Standardised Equivalent Capital Ratios

The current summary disclosure of actual capital ratios includes a summary of the RWAs for the main risk categories that make up total RWAs (required by Schedule 11, Clause 14 of the OIC), and a table showing the three capital ratios and buffer ratio alongside the regulatory minima (required by Schedule 11, Clause 15). We propose that dual reporting will cover standardised equivalents of this existing disclosure, with text explaining the nature of the information.

The equivalent of the RWA summary could look like the following table:

Comparison of Actual and Standardised-Equivalent Risk-Weighted Exposures

	Risk weighted exposure or implied risk weighted exposure	Standardised equivalents of risk weighted exposure or implied risk weighted exposure
Credit exposures subject to IRB approach or supervisory slotting	1105	1300
Credit exposures subject to standardised approach	212	200
Market risk implied RWAs	250	250
Operational risk implied RWAs	350	350
Supervisory adjustment	20	0
Total RWAs	1937	2100

(With a footnote, as already required, to explain where the scalar is reflected in the RWA figures: note that initially, while the actual credit risk RWAs will still include a scalar of 1.06, this is not part of the standardised equivalent calculation.)

The existing version of this table for actual risk-weighted exposures (in Schedule 11, clause 14) also includes a column for exposure amounts, although these are 'N/A' for the market risk, operational risk and supervisory adjustment rows. We could follow this approach with the above table to illustrate how exposure amounts differ between the IRB and standardised approach, but that would require two extra columns, which would be largely 'N/A'. So we propose to cover exposure amounts only in the more detailed breakdowns of credit risk RWEs (see below).

One point illustrated in the above example is that a supervisory adjustment, which is specified in a bank's conditions of registration and is added to the denominator of capital ratios, may or may not vary between the actual and the standardised equivalent calculations. For example, it would not apply to the standardised calculation if it represents an IRB model overlay.

New Clause 17A in Annex A is the proposed new OIC text to add this requirement.

Operational Risk

As illustrated above, we do not propose that an IRB bank should be required to recalculate its operational risk capital requirement using the standardised approach for the right-hand column of the table, when it uses the model-based Advanced Measurement Approach ('AMA') for its minimum ratio calculations. Although the objectives of dual reporting suggest that such a bank should re-calculate the operational risk charge on a standardised basis, to show how big a difference modelling makes, there are several reasons why we do not think this would be justified—

- We have firm plans to consult during the first half of this year, or by the third quarter at the latest, on replacing both of the current operational risk approaches with the Basel Committee's new standardised approach.
- Whereas IRB banks will have to calculate standardised equivalent RWAs for credit risk in any case (to carry out the standardised floor calculation), in order to carry out operational risk dual reporting they would have to put in place the systems needed to calculate the standardised equivalent operational risk charge solely for this dual reporting requirement. This extra calculation would be superseded once the new Basel standardised approach comes into effect, within the next year or so.
- The Capital Review final decisions were not explicit on whether dual reporting should cover operational risk as well as credit risk.

Standardised Equivalent Capital Base

One key difference between the IRB and standardised capital ratio calculations is the treatment of loan loss provisions. For calculating credit risk RWAs under the IRB approach gross exposure amount are used, while under the standardised approach exposure amounts are net of provisions. There is a corresponding difference between the IRB and standardised definitions of capital, namely that if the value of {IRB modelled expected losses *less* eligible provisions} is positive, it is deducted from CET1 capital; but if it is negative, the absolute value of the amount is added to Tier 2 capital (up to a limit). There is no such adjustment to the capital base under the standardised approach.

For these reasons, we think that dual reported capital ratios should use the standardised version of the components of regulatory capital. To clarify this distinction, we propose a table to show how these provisioning adjustments to CET1 capital or Tier 2 capital, under the IRB approach, are backed out to show the standardised capital base. A sample of this would appear as follows.

Adjustments to Capital Components for Standardised Equivalent Capital Ratios

	CET1 Capital	Tier 1 Capital	Total Capital
Capital components for compliance purposes	180	220	240
Eligible provisions included in IRB Tier 2 capital, removed from standardised Tier 2 capital	0	0	-5
Standardised equivalent capital components	**180**	**220**	**235**

Since the adjustments to CET1 capital or Tier 2 capital are mutually exclusive, the middle row in this table would only need to show the one or the other, and this would be specified in the relevant clause of the OIC: see the draft clause 17B in Annex A.

And the table showing standardised equivalent capital ratios (imposed by Clause 17C in Annex A) might look like this –

Standardised Equivalent Capital Ratios

	CET1 Capital	Tier 1 Capital	Total Capital
Denominator (standardised equivalent total RWAs)	2100	2100	2100
Capital amounts	180	220	235
Capital ratios	8.57%	10.48%	11.19%

There are a number of aspects of the disclosure of actual compliance figures that we do not see the need to replicate for the standardised equivalent disclosures.

Buffer Ratio

We do not propose to require IRB banks to also disclose their standardised equivalent buffer ratios. The main purpose of dual reporting is to show the difference between IRB and standardised credit risk RWA calculations, and the three main capital ratios should give a full enough picture of that. Also, the buffer ratio sets a trigger point for regulatory responses rather than a regulatory minimum.

Previous Period Comparatives

We currently require bank disclosure statements to include previous year comparison figures for the following: actual capital ratios (including the buffer ratio); solo capital ratios; the internal capital allocation for 'other material risks' (under ICAAP); and parent bank group capital ratios. We do not require previous year comparisons to be given for any of the other more detailed capital adequacy disclosures (in the interests of space, and readability of disclosure statements).

Requiring comparatives for standardised equivalent calculations, at the more summary level, would make it easier for readers to see how the gap between standardised and IRB capital ratios was changing over time. But we think that most readers who are interested in the trends in this material at any level of detail will have the ability to search out previous years' disclosure statements to make the comparison. However, we do propose (below) a very high-level historical summary.

Solo Capital Ratios

Banks currently have to disclose their three main capital ratios on a solo (as well as consolidated) basis. But we do not require solo disclosure for any of the other capital adequacy information. The main aim of this is to disclose enough information to show whether the registered bank's own capital is being down-streamed within the banking group. Our view is that the comparison between solo IRB capital ratios and standardised equivalent solo capital ratios would provide very little additional information benefit, on top of that already provided by (1) comparing actual group ratios to solo ratios, and (2) comparing actual group ratios to standardised equivalent group ratios.

On the cost side, this is not a calculation that IRB banks would need to make for any other purpose, and might require a material amount of extra work to implement.

Historical Summary

We propose that an IRB bank should include in its disclosure statements a table showing the most recent five years' figures for actual and standardised equivalent total capital ratios, and the total average risk weight for all modelled credit risk exposures on an actual and standardised equivalent basis. The following table gives an example of how such a table might look:

Historical Summary of Actual and Standardised Capital Ratios and Risk Weights

	2018	2019	2020	2021	2022
Actual total capital ratio	13.5%	13.8%	14.2%	13.9%	14.8%
Standardised equivalent total capital ratio	11.8%	11.7%	12.3%	12.0%	13.1%
Actual average risk weight for all modelled credit risk exposures	43%	42%	44%	46%	45%
Standardised-equivalent average risk weight for all modelled credit risk exposures	62%	63%	64%	64%	61%

(With some explanatory text required to be provided by the bank.)

The figures in the right-most column will correspond to capital ratio figures already included elsewhere in the disclosure statement, and to the ratios of total risk-weighted exposures to total exposure numbers given in the proposed more detailed table (see next section). We recognise that IRB banks are unlikely to have calculated standardised equivalent RWAs in the past, and it may be a significant task to go back and recreate the calculations. We therefore propose that a bank will only need to disclose the historical numbers to the extent that they can be calculated without unreasonable burden. This disclosure would be specified by the proposed new clause 17D shown in Annex A.

3.2 More detailed breakdown of IRB and standardised equivalent RWAs

The proposed tables above shows total IRB (and supervisory slotting) credit risk RWAs, and the standardised equivalent of that total. That is the 'headline' figure for the difference that IRB modelling makes (1105 versus 1300 in that example).

We think that a table to provide a more granular comparison by exposure class would be very informative, and at this level it will also be useful to show the comparison of the pre-risk-weight exposure amounts. We propose that IRB banks should be required to include a table along the following lines in their disclosure statements (the row labels for IRB exposure classes are illustrative only).

Credit Risk: Standardised Equivalents of IRB Risk-Weighted Assets ($Mn)

IRB exposure class	Exposure Under IRB Approach (EAD)	IRB Risk-Weighted Assets[1]	Equivalent Exposure Under Standardised Approach	Standardised Equivalents of Risk-Weighted Assets
Exposures secured by residential mortgages	180	80	170	120
Other retail exposures	25	20	22	25
Corporate – SME	28	30	26	40
Other corporate	60	50	57	60
Supervisory slotting	20	15	18	20
Total	**313**	**195**	**293**	**265**

Footnote 1: amounts shown in this column have been multiplied by a scalar of 1.06.

We have drafted the new clause of the OIC to implement this table with the aim that the figures in the first two columns of figures align exactly with the disclosure required by clauses 3 and 5 in Schedule 11 of the OIC (see Schedule 11, clause 17E in Annex A).

Schedule 11, clause 3 requires a detailed breakdown, by IRB exposure class and then by PD ('probability of default') ranges within each exposure class, of various steps in the capital requirement calculation. IRB banks present their IRB exposure classes in slightly different ways, as allowed for in the OICs – this reflects the flexibility of the IRB approach. We will ensure that the rows in the above table can use exactly the same labelling that banks currently use for their detailed disclosure of IRB exposures. The subtotals for each exposure class, under the headings of exposure amounts and RWAs, will exactly match the figures in rows 1 to 5 of the above table.

Schedule 11, clause 5 requires details of the risk-weight calculations under the supervisory slotting approach, separated into on and off-balance sheet: the sum of the subtotals of those two tables will match the figures in the 'supervisory slotting' row in the above table, under the headings of IRB exposures and IRB RWAs.

At this level of detail, requiring IRB and standardised equivalent exposure numbers (as well as risk-weighted assets) seems useful. In capital ratio calculations, standardised exposures are net of provisions while IRB exposures are not, and there are also some differences arising from IRB banks modelling EADs rather than using fixed percentages of gross exposures. It should be informative to see how big the difference is.

We think that this table meets the main objective of dual reporting, namely to show at aggregate level how RWAs for the same exposures differ between the IRB and standardised approach. It does not require a bank to give any information on which category of standardised exposure any given IRB exposure goes into. It is technically possible that (for example) an IRB SME ('small or medium-sized enterprise') corporate exposure will qualify for RML ('residential mortgage loan') treatment under the standardised approach. But in the above table, this exposure would appear all the way across the row for 'Corporate – SME'. The approach in this table provides a better like-for-like comparison than, for example, showing total IRB RML amounts alongside total standardised RML amounts. It essentially avoids the comparison problems caused by marginal differences between IRB and standardised exposure classes.

3.3 Full-Detail Breakdown by IRB Exposure Class and PD Range

We propose that IRB banks should also disclose IRB exposures by individual PD range alongside the standardised equivalents, and likewise show supervisory slotted exposures by risk grade next to the standardised equivalents.

The table for the IRB exposure classes could look as follows.

IRB credit exposures by class and PD grade				***Standardised equivalents***		
PD Range	Exposure Amount $Mn	Exposure-Weighted Risk Weight	RWAs $mns[1]	Standardised Equivalent RWAs $mn	Standardised Equivalent Exposure Amount $Mn	Average Standardised Risk Weight (%)
RML Exposure Class						
0-0.5%	2,090	9%	188	746	2,015	37%
0.5-0.8%	2,857	21%	600	1,148	2,670	43%
0.8-3.25%	...	...	...	...	...	...
3.25%-7.45%	...	...	...	...	...	...
etc....	...	...	...	...	...	...
Other Retail Exposure Class						
0-0.8%	...	...	...	...	...	...
etc ...	...	...	...	...	...	...

Footnote 1: includes scalar.

IRB banks already disclose the columns to the left of the bold line as part of their detailed breakdown of risk-weighting of their exposures under the IRB modelled approach. It would add less to the total volume of disclosure to add the right-hand three columns to that existing table. But we think it would be less confusing to have the above table given separately, as part of the disclosure of standardised equivalent calculations. We propose including the above subset of the columns from the existing IRB table, as these are the most relevant for the standardised comparison, and also allow the two tables to be read side by side if desired.

We propose a similar approach to showing how the standardised equivalents of supervisory slotting exposures compare with the actual (compliance) risk-weighting calculation, as follows –

Supervisory Slotting – On-Balance Sheet Exposure ***Standardised Equivalents***

Specialised Lending	Total Exposure After Credit Risk Mitigation $Mn	Risk Weight	RWAs $mn	Standardised Equivalent RWAs	Standardised Equivalent Exposure $Mn	Average Standardised Risk Weight
Strong	130	70%	91	125	125	100%
Good	200	90%	180	190	190	100%
Satisfactory	10	115%	11	10	8	125%
Weak	5	250%	13	6	4	150%
Totals	345		295	331	327	

Supervisory Slotting – Off-Balance Sheet Exposure

Specialised Lending	EAD $mn	Average Risk Weight	RWAs $mn	Standardised Equivalent RWAs	Standardised Equivalent Exposure $Mn	Average Standardised Risk Weight
Undrawn commitments and other off-balance sheet exposures	15	105%	16	15	15	100%

As with the less detailed breakdowns covered in the previous section, the approach for the above tables shows standardised equivalent RWA calculations categorised by existing IRB exposure categories, rather than reorganising individual exposures into the risk-weighting categories they would fall into under the standardised approach.

There are some alternative (or additional) approaches that could be used to show the standardised equivalent calculations, which would use tables to show all modelled exposures listed by standardised counterparty class and risk weight. However, as already discussed above, as this approach would not allow like-for-like comparisons of a bank's IRB and standardised risk-weights, we do not think it meets the objectives of dual reporting nearly as well.

4 Additional Disclosure of IRB Banks' Actual Standardised Exposures

IRB banks currently have to disclose the risk-weighting treatment of any of their credit exposures that are subject to the standardised approach (see OIC, Schedule 11, clause 6). But the required disclosure is in much more of a summary form than the equivalent for standardised banks. The disclosure table requires a breakdown into the main asset categories, but for each category there is only a single row showing the total RWAs and average risk weight. This is because for an IRB bank, these amounts are only a small part of total RWAs: they comprise exposures which are in IRB exposure classes but for which the bank has not got an accredited model, and other assets which are always standardised (such as cash and gold bullion, and premises, plant and equipment).[5]

Since 1 January 2022, when calculating capital ratios, IRB banks have had to apply the standardised approach to all of their exposures that currently fall within the IRB sovereign or bank exposure classes, not just those that are not covered by an accredited model. We propose to revise clause 6 of Schedule 11, to expand the rows covering these IRB exposure classes so that there is a separate row for each possible risk weight. These two IRB exposure classes correspond to separate risk-weight treatments for sovereigns, multilateral development banks and other international organisations, PSEs, and banks, under the standardised approach.

Annex A shows the revised clause 6 with the expanded table.

A similar issue arises with the disclosure of off-balance sheet contingent credit exposures and commitments to counterparties in these same categories. Standardised banks currently have to disclose these amounts separately from on-balance sheet exposures, broken down into separate rows for each contract type such as forward asset purchases, note issuance facilities, guarantees, and so on, but not further broken down by counterparty. IRB banks' current disclosure of any standardised exposures also splits these exposures from on-balance exposures, but only shows a single aggregate amount.

We could also expand this disclosure for IRB banks, in line with the equivalent disclosure by standardised banks. However, it does not seem likely to us that off-balance sheet contingent exposures to counterparties in the sovereign and bank exposure classes will be significant amounts. So we propose to leave this disclosure unchanged for IRB banks, but will monitor the amounts disclosed in future disclosure statements, with a view to requiring a more detailed breakdown if the amounts are large enough to need it.

5 Note that credit risk arising from an IRB bank's holdings of equity is also subject to standardised risk-weighting, but is disclosed separately (see OIC Schedule 11, clause 8). No change is needed to that.

5 Additional Counterparty Credit Risk Disclosure

The Credit Valuation Adjustment (CVA) capital charge, and the distinct treatment of credit risk arising from settling derivative trades directly or indirectly with a Central Counterparty ('CCP'), were added to the capital requirements in 2013. We did not make any corresponding changes to disclosure requirements at the time.

Currently, banks vary in whether they disclose a separate number for the CVA charge or include it within other RWA totals. It is effectively an add-on to the capital requirement for counterparty credit risk, and judging from the figures from banks that have disclosed the amount, the numbers are not immaterial. Given that the charge represents a distinct form of risk, we think it should be added as a separate disclosure requirement.

The proposed new OIC text to cover the CVA charge for standardised banks is an extra row to the counterparty credit risk table in Schedule 9, clause 3. For IRB banks, it is covered in the new Schedule 11, clause 6A. (See Annex A.)

Similarly, some banks separately disclose exposures to Qualifying Central Counterparties (QCCPs), others do not. Some exposures arising from trades settled on QCCPs receive concessionary risk weights of 0%, 2% or 4%, while others must be risk-weighted as an exposure to the relevant counterparty, with the risk weight of that counterparty applying (whether under the IRB or standardised approach). We think that the exposures subject to the concessionary risk weights could usefully be subject to separate disclosure, while other exposures related to trades settled on QCCPs should be included in the general disclosure of RWAs by counterparty category: there does not seem to be a strong case for separate disclosure in that case. Such a table might appear as follows:

Exposures arising from trades settled on Qualifying Central Counterparties

	Trade exposure or collateral amount	Average risk weight	Risk weighted exposures
Bank as QCCP clearing member, clearing own trades			
Collateral posted for clearing own trades			
Bank as client of QCCP member, clearing trades through that member			
Collateral posted for clearing via member bank			
Totals			

The OIC changes to achieve this are the new Schedule 9, Clause 3A (for standardised banks) and Schedule 11, Clause 6A (for IRB banks). (See Annex A.)

6 Removal of Columns for Pillar 1 Capital Requirement

For both IRB and standardised banks, a number of the required tables that show the breakdown of RWAs also include an extra column, showing the amounts of total required capital corresponding to the total RWAs in each row. When the capital ratio calculation directly involves calculating RWAs for a given risk, we do not think this adds much to the value of seeing the amount of RWAs in each category that feeds in to total RWAs for credit risk, which is the number used as part of RWA equivalents, for calculating the various capital ratios.

However, in the case of a capital charge that comes directly from a risk calculation, which is then multiplied by 12.5 to obtain the 'implied risk weighted exposure' number, that underlying capital charge number does seem worth disclosing. This arises with the market risk, operational risk and CVA capital charges.

We propose to remove the columns which are variously referred to as 'Minimum Pillar 1 capital requirement' and 'minimum capital requirement' in all cases apart from those in the previous paragraph. The details of the proposed changes to the OIC are set out in section (5) of Annex A.

7 Impact Assessment

As part of getting the required Amending Order made to implement these changes, we will need to prepare a Regulatory Impact Statement (RIS) to support our recommendations (unless it is agreed that the proposed new disclosure has no or minor impacts on affected parties). Although we published a full regulatory impact assessment and cost-benefit analysis on the Capital Review in December 2019, its main focus was on the proposed changes to the capital ratio calculations and the proposed increases in overall capital levels. At that point there was no detail on the implementation of dual reporting on which to base an impact assessment.

Broadly, the benefits of these proposed new disclosure requirements will take the form of improved market discipline, which cannot readily be expressed in dollar terms. The costs will fall mainly on the four IRB banks that will need to add the new disclosure to their six-monthly disclosure statements, although the new CVA and QCCP disclosure will also impose some costs on standardised banks.

To get a qualitative assessment of the benefits, we are keen to hear from as many interested parties as possible. They may include investors, other banks interested in a bank's disclosures, market analysts, financial commentators and academics. We will be interested in their views on which components of the additional disclosure are useful to them, and whether any of the components need to be revised to make the disclosure more effective.

We request that all New Zealand-incorporated banks provide us with information on the costs of adding the proposed additional disclosure to their disclosure statements. To the best of our understanding, none of the additional disclosure that we are proposing here, to cover dual reporting as well as the other changes, will require banks to carry out additional risk-weighting or ratio calculations on top of those needed for the purpose of ensuring compliance with their minimum capital ratios. IRB banks need to calculate standardised equivalent risk-weights for all of their IRB modelled exposures, in order to apply the standardised floor, while all New Zealand-incorporated banks need to calculate the CVA charge and QCCP RWA components (where applicable).

For this RIS, we only want to hear about the additional cost that will arise from having to include the extra information in disclosure statements, not the costs of preparing the information for compliance purposes. The latter costs are already borne by banks, regardless of any disclosure changes.

It would be helpful if banks can divide the cost estimates up into the cost of putting in place the new systems to deliver the new disclosures, and the continuing six-monthly costs of publishing the additional information thereafter.

8 Consultation Questions

We welcome feedback on any aspect of the proposed disclosure changes.

We would specifically be interested in getting responses from key groups of stakeholders as follows –

From Readers of Disclosure Statements

For each proposed new component of disclosure, please give us your views on whether it is a useful addition to a bank's disclosure statement, and whether you can suggest any improvement in the content or how it is laid out.

For the potential additional items of dual reporting disclosure that we propose not to add (as flagged at various points in this paper), please can you let us know whether or not you agree with their omission.

Please can you let us know whether or not you support the proposed removal of existing disclosure (the 'total capital requirement' columns).

From New Zealand-Incorporated Banks

For each proposed new component of disclosure that your bank would be required to publish, please can you give us estimates of the initial implementation cost and continuing compliance cost of that disclosure (as discussed above under Impact Assessment).

Please can you give us any suggested improvements to the proposed disclosure, including ways to make it easier for readers to understand.

Please can you give us any detailed drafting comments on the draft new OIC text set out in Annex A.

Please can you let us know whether your bank would have sufficient time to be able to comply with the proposed new requirements if they go ahead as planned, starting from a first reporting date of 30 September 2022.

9 Next Steps

The consultation is open until 5pm on Tuesday 3 May 2022. We will aim to publish a feedback statement by early June, including our final decisions on the disclosure changes we will recommend. Depending on the feedback we receive, we may need to carry out a limited further consultation at the same time, to confirm the text revisions needed to the OIC to implement the new disclosure.

To get the disclosure changes made, we will need to recommend to the Minister of Finance that he advises the Governor General, with the consent of the Executive Council, to make the necessary amending Order. In order to ensure that the amending Order comes into force by 30 September 2022, so that the changes will apply to disclosure statements with reporting dates from that date, we will need to have the required papers with the Minister by mid-July.

We will also be consulting in due course on some corresponding changes that may be needed to some of our statistical surveys.

Annex A:

Draft Changes to OIC to Implement Proposed New Disclosure

(1) Showing the standardised floor calculation for IRB banks

Clause to be inserted into Schedule 11 —

8A Effect of standardised floor on total risk-weighted exposures for credit risk

(1) The information in subclauses (2) and (3)—

(a) in respect of the registered bank's banking group; and

(b) derived in accordance with the conditions of registration relating to capital adequacy.

(2) The following information at the reporting date:

Application of Standardised Floor to Total Credit Risk RWAs

<table>
<tr><td></td><td colspan="2">RWAs for modelled exposures</td><td>RWAs for standardised exposures</td><td>Total credit risk RWAs</td></tr>
<tr><td></td><td>RWAs calculated using models</td><td>RWAs recalculated using standardised approach</td><td>N/A</td><td>N/A</td></tr>
<tr><td>Total IRB and supervisory slotting exposures</td><td></td><td></td><td>N/A</td><td rowspan="2">N/A</td></tr>
<tr><td>Standardised floor</td><td>N/A</td><td></td><td>N/A</td></tr>
<tr><td>RWAs with floor applied</td><td colspan="2"></td><td></td><td></td></tr>
</table>

(3) An explanation of how the standardised floor applies to the calculation of total RWAs for credit risk.

(4) For the purpose of the disclosure required by clause (2)—

(a) RWAs calculated using models refers to total risk-weighted assets that the registered bank calculates using either an accredited IRB model or the supervisory slotting approach to risk-weighting specialised corporate lending, including any applicable scalar;

(b) RWAs recalculated using standardised approach has the same meaning as standardised equivalent RWAs in Part C of BPR130: Credit Risk RWAs overview;

(c) the standardised floor is calculated as 85% of RWAs recalculated using standardised approach; and

(d) RWAs for standardised exposures refers to total risk-weighted assets that the registered bank calculates for credit risk exposures that are not covered by subclause (a), including any applicable scalar.

(2) Dual reporting by IRB banks

The following clauses to be inserted into Schedule 11

17A Standardised equivalents of risk-weighted exposures

(1) The information in subclause (2)—

(a) in respect of the registered bank's banking group; and

(b) derived in accordance with the conditions of registration relating to capital adequacy.

(2) The following information as at the reporting date:

Comparison of Actual and Standardised-Equivalent Risk-Weighted Exposures

	Risk weighted exposure or implied risk weighted exposure	Standardised equivalents of risk weighted exposure or implied risk weighted exposure
Credit exposures subject to IRB approach or supervisory slotting		
Credit exposures subject to standardised approach		
Market risk		
Operational risk		
Supervisory adjustment		
Total		

(3) For the purpose of the disclosure required by subclause (2)—

(a) in the column for risk-weighted exposure and implied risk-weighted exposure, the cells refer to the components of total RWA equivalents that the bank calculates when calculating its capital ratios for compliance purposes;

(b) the column for standardised equivalents of risk-weighted exposure shows the information referred to in clause (a), recalculated as if the bank was a standardised bank; and

(c) supervisory adjustment means an additional capital requirement (if any) imposed in the conditions of registration.

(4) For avoidance of doubt—

(a) the amounts to be shown for market and operational risk are the same in both columns;

(b) the standardised equivalent risk-weighted exposures should not include any scalar that applies to the bank's calculation of capital ratios for compliance purposes; and

(c) any supervisory adjustment that relates specifically to the registered bank's IRB models should be shown as nil for standardised equivalent purposes.

17B Standardised equivalents of components of capital

(1) The information in subclause (2) in respect of the registered bank's banking group.

(2) The following information as at the reporting date:

Adjustments to Capital Components for Standardised Equivalent Capital Ratios

	CET1 Capital	**Tier 1 capital**	**Total capital**
Capital components for compliance purposes			
Reversal of deduction from CET1 capital for excess expected losses (if applicable)			
Removal of excess eligible provisions included in Tier 2 capital (if applicable)			
Standardised equivalent capital components			

(3) For the purpose of the disclosure required by subclause (2)—

(a) Capital components for compliance purposes refers to the amounts of CET1 capital, Tier 1 capital and total capital with the meaning given in this Order;

(b) Standardised equivalent capital components refers to the amounts of CET1 capital, Tier 1 capital and Total Capital that would apply if the bank was a standardised bank;

(c) the row for reversal of deduction from CET1 capital refers to the amount, if applicable, that the bank deducts from CET1 capital in accordance with Part F of BPR133: IRB Credit Risk RWAs, in calculating its capital ratios for compliance purposes, which must be added back to CET1 capital to calculate standardised equivalent CET1 capital;

(d) the row for removal of excess eligible provisions included in Tier 2 capital refers to the amount, if applicable, that the bank adds to Tier 2 capital in accordance with Part F of BPR133: IRB Credit Risk RWAs in calculating its capital ratios for compliance purposes, which must be subtracted from Tier 2 capital to calculate standardised equivalent Tier 2 capital; and

(e) only the applicable row of the two rows referred to in subclauses (c) and (d) needs to be disclosed.

17C Standardised equivalent capital ratios

(1) The information in subclause (2)—

(a) in respect of the registered bank's banking group; and

(b) derived in accordance with the conditions of registration relating to capital adequacy.

(2) The following information as at the reporting date:

Standardised Equivalent Capital Ratios

	CET1 capital	Tier 1 capital	Total capital
Denominator (standardised equivalent total RWAs)			
Capital amounts			
Capital ratios			

(3) For the purpose of the disclosure required by subclause (2)—

(a) standardised equivalent total RWAs refers to the aggregate standardised equivalent amount required to be disclosed under Clause 17A;

(b) capital amounts are standardised equivalent capital components as required to be disclosed by Clause 17B; and

(b) capital ratios are the capital ratios that the bank would be required to calculate for compliance with its minimum capital ratio requirements if it was not an IRB bank.

17D Historical summary of actual and standardised capital ratios and risk weights

(1) An historical summary showing the information in subclause (2) in respect of the registered bank's banking group, for the reporting date and for each of the previous reporting dates

that are 1, 2, 3 and 4 years before the current reporting date, provided that the bank may exclude all information for any reporting date on or before 31 December 2021 if it cannot readily produce any of the standardised equivalent information for that date.

(2) The information required for each date specified under subclause (1) is—

(a) total capital ratio;

(b) total capital ratio recalculated as if the bank was not an IRB bank;

(c) actual average risk weight for all modelled credit risk exposures, which must be calculated as the ratio of—

(i) total risk-weighted assets for all exposures that are subject to the IRB modelling approach or the supervisory slotting approach, including any applicable scalar; to

(ii) total EAD for all exposures covered by subclause (i);

(d) standardised-equivalent average risk weight for all modelled credit risk exposures, which must be calculated as the ratio of—

(i) total risk-weighted assets for all exposures referred to in subclause (c)(i), recalculated as if the bank was a standardised bank; to

(ii) total on-balance sheet exposures and credit equivalent amounts for all exposures referred to in subclause (c)(i), defined in accordance with the standardised risk-weighting approach in BPR131: Standardised Credit Risk RWAs.

(3) An explanation of what each of the rows of the table represents.

17E Standardised equivalents of IRB risk-weighted credit exposures

(1) The information in subclause (2) in respect of the registered bank's banking group.

(2) The following information as at the reporting date:

Credit Risk: Standardised Equivalents of IRB Risk-Weighted Assets ($Mn)

IRB exposure class	Exposure under IRB approach	IRB risk-weighted assets	Equivalent exposure under standardised approach	Standardised equivalents of risk-weighted assets
First IRB exposure class				
Second IRB exposure class				
…				
Specialised lending subject to the slotting approach				
TOTAL				

(3) For the purpose of the disclosure required by subclause (2)—

(a) the bank must disclose the same IRB exposure classes that it uses for the breakdown of IRB risk-weighted exposures under Clause 3;

(b) for each IRB exposure class, the values for exposure under IRB approach and IRB risk-weighted assets are the aggregates shown for that exposure class in the columns 'Exposure amounts' and 'Risk weighted assets' required to be disclosed under Clause 3;

(c) in the row 'Specialised lending subject to the slotting approach'—

(i) the value for exposure under IRB approach is the aggregate amount of total exposures after credit risk mitigation for on-balance sheet exposures, and EAD for off-balance exposures, required to be disclosed under Clause 5; and

(ii) the value for IRB risk-weighted assets is the aggregate of risk-weighted assets for on-balance and off-balance sheet exposures required to be disclosed under Clause 5;

(d) the column 'equivalent exposure under standardised approach' must show for each row the aggregate on-balance sheet exposures and credit equivalent amounts for all exposures falling within the respective IRB exposure class or supervisory slotting, defined in accordance with the standardised risk-weighting approach in BPR131: Standardised Credit Risk RWAs; and

(e) the column 'standardised equivalents of risk-weighted exposures' must show for each row the aggregate risk-weighted assets for all exposures falling within the respective IRB exposure class or supervisory slotting, calculated in accordance with the standardised risk-weighting approach in BPR131: Standardised Credit Risk RWAs.

17F Standardised equivalents of IRB risk-weighted credit exposures by PD grade

(1) The information in subclause (2) in respect of the registered bank's banking group.

(2) For each exposure class where the IRB approach is applied, the following information as at the reporting date:

IRB Credit Exposures by Class and PD Grade				***Standardised Equivalents***		
Name of exposure class	Exposure amount	Exposure-weighted risk weight (%)	RWAs $mns	Standardised equivalent RWAs $mn	Standardised equivalent exposure amount $mn	Average standardised risk weight (%)
PD range 1 (%)						
PD range 2 (%)						
…						
…						
Default PD grade						
Totals						

(3) For the purpose of the disclosure required by subclause (2)—

(a) the bank must disclose the same exposure classes and PD ranges for each exposure class that it uses for disclosure required under clause 3;

(b) exposure-weighted values have the same meaning as in clause 3;

(c) for a given exposure class and PD range—

(i) standardised equivalent risk-weighted assets is the sum of risk-weighted assets for all exposures falling into that exposure class and PD range, calculated as if the bank was a standardised bank;

(ii) standardised equivalent exposure amount is the sum of exposure amounts all exposures falling into that exposure class and PD range, calculated as if the bank was a standardised bank; and

(iii) average standardised risk weight is calculated as the amount specified in subclause (i) divided by the amount specified in subclause (ii).

17G Standardised equivalents of specialised lending subject to the slotting approach

(1) If the slotting approach for specialised lending exposures as defined in BPR133: Credit Risk RWAs is used, the information in subclause (2) in respect of the registered bank's banking group.

(2) The following information as at the reporting date in respect of specialised exposures subject to the slotting approach:

Supervisory Slotting – On-Balance Sheet Exposure ***Standardised Equivalents***

Specialised lending	Total exposure after credit risk mitigation	Risk weight	Risk weighted assets	Standardised equivalent risk weighted assets	Standardised equivalent exposure	Average standardised risk weight
Strong		70%				
Good		90%				
Satisfactory		115%				
Weak		250%				
Totals		N/A				

Supervisory Slotting – Off-Balance Sheet Exposure ***Standardised Equivalents***

Specialised lending	EAD $mn	Average risk weight	Risk weighted assets $mn	Standardised equivalent risk weighted assets	Standardised equivalent exposure $mn	Average standardised risk weight
Undrawn commitments and other off-BS exposures						

(3) For the purpose of the disclosure required by subclause (2)—

(a) the information required in columns 2, 3 and 4 of the two tables is the same as that required by the corresponding columns in the two tables required by clause 5;

(b) for each row of the supervisory slotting categories in the first table, and for the total for off-balance sheet slotted exposures in the second table—

(i) standardised equivalent risk-weighted assets is the sum of the risk-weighted asset for each exposure falling into that slotting category, calculated as if the bank was a standardised bank;

(ii) standardised equivalent exposure is the sum of exposure amounts across all exposures falling into that slotting category, and the sum of credit-equivalent amounts for off-balance sheet slotted exposures, calculated as if the bank was a standardised bank; and

(iii) average standardised risk weight is calculated as the amount specified in subclause (i) divided by the amount specified in subclause (ii).

(3) Standardisation of IRB banks' sovereign and bank exposure classes

Revised clause 6 in Schedule 11, as follows:

6 Credit risk exposures subject to the standardised approach

(1) The information in subclause (2)—

(a) in respect of the registered bank's banking group; and

(b) in respect of any credit risk exposures that are not subject to the IRB approach or the slotting approach to specialised lending and do not arise from equity holdings.

(2) The following information as at the reporting date:

Credit risk exposures subject to the standardised approach

On-balance sheet exposures by separate risk weight

	Total exposure after credit risk mitigation	Risk weight	Risk weighted exposure
Cash and gold bullion		0%	
Sovereigns and central banks		0%	
		20%	
		50%	
		100%	
		150%	
Multilateral development banks and other international organisations		0%	
		20%	
		50%	
		100%	
		150%	
Public sector entities		20%	
		50%	
		100%	
		150%	
Banks		20%	
		50%	
		100%	
		150%	

Other on-balance sheet exposures by average risk weight

	Total exposure after credit risk mitigation	Average risk weight	Risk weighted exposure
Corporate			
Residential mortgages			
Past due assets			
Other assets			

Off-balance sheet exposures

	Total exposure or principal amount	Average credit conversion factor	Credit equivalent amount	Average risk weight	Risk weighted exposure
Total off balance sheet exposures subject to the standardised approach					

Counterparty credit risk for counterparties subject to the standardised approach

	Total exposure or principal amount	Credit equivalent amount	Average risk weight	Risk weighted exposure
(a) Foreign exchange contracts				
(b) Interest rate contracts				
(c) Other				

(3) For the purpose of the disclosure required by subclause (2)—

(a) average risk weight means the exposure-weighted average of the risk weights of individual exposures determined according to the counterparty or type of asset or issuer as appropriate; and

(b) average credit conversion factor means the exposure-weighted average of the credit conversion factors for individual exposures.

(4) Additional counterparty credit risk disclosure

This section sets out the amendments and additions to the OIC to implement the proposed separate disclosure of the CVA charge, and exposures arising in relation to trades cleared on Qualifying Central Counterparties.

For Standardised Banks

A new row to be added at the end of the 'Counterparty credit risk' table in Schedule 9, Clause 3 of the OIC, as follows:

Counterparty credit risk

	Total exposure	Credit equivalent amount	Average risk weight	Risk weighted exposure	Minimum Pillar 1 capital requirement
Foreign exchange contracts					
Interest rate contracts					
Other					
Credit Valuation Adjustment	n/a	n/a	n/a		

The following new clause to be added to Schedule 9 of the OIC:

3A QCCP exposures

(1) The information in subclause (2)—

(a) in respect of the registered bank's banking group; and

(b) derived in accordance with the conditions of registration relating to capital adequacy.

(2) The following information as at the reporting date:

Exposures Arising From Trades Settled on Qualifying Central Counterparties

	Trade exposure or collateral amount	Average risk weight	Risk weighted exposures
Bank as QCCP clearing member, clearing own trades			
Collateral posted for clearing own trades			
Bank as client of QCCP member, clearing trades through that member			
Collateral posted for clearing via member bank			

(3) For the purpose of the disclosure required by subclause (2), the following amounts must be excluded from the table and included as part of the risk-weighted exposure to the relevant individual counterparty in accordance with Clause 3:

(a) any trade exposure that the registered bank has to a clearing member of a QCCP, as a client of that clearing member, which is required for risk-weighting purposes to be treated as a bilateral exposure to that clearing member;

(b) any collateral posted by the registered bank as a client of a QCCP member which is required to be risk-weighted the same as a direct exposure to the QCCP member;

(c) any trade exposure that the registered bank has to a client bank, arising from the registered bank, as a member of a QCCP, clearing trades for that client bank via the QCCP; and

(d) any exposures arising from trades cleared on a central counterparty that is not a QCCP.

For IRB banks

The following new clause 6A to be inserted in Schedule 11 of the Local OiC:

6A Other counterparty credit risk exposures

(1) The information in subclauses (2) and (4)—

(a) in respect of the registered bank's banking group; and

(b) derived in accordance with the conditions of registration relating to capital adequacy.

(2) The following information as at the reporting date:

Exposures arising from trades settled on Qualifying Central Counterparties

	Trade exposure or collateral amount	Average risk weight	Risk weighted exposures
Bank as QCCP clearing member, clearing own trades			
Collateral posted for clearing own trades			
Bank as client of QCCP member, clearing trades through that member			
Collateral posted for clearing via member bank			

(3) For the purpose of the disclosure required by subclause (2), the following amounts must be excluded from the table and disclosed as part of the risk-weighted exposure to the relevant individual counterparty in accordance with Clause 3 or 6 as applicable:

(a) any trade exposure that the registered bank has to a clearing member of a QCCP, as a client of that clearing member, which is required for risk-weighting purposes to be treated as a bilateral exposure to that clearing member;

(b) any collateral posted by the registered bank as a client of a QCCP member which is required to be risk-weighted the same as a direct exposure to the QCCP member;

(c) any trade exposure that the registered bank has to a client bank, arising from the registered bank, as a member of a QCCP, clearing trades for that client bank via the QCCP; and

(d) any exposures arising from trades cleared on a central counterparty that is not a QCCP.

(4) The amount of the Credit Valuation Adjustment (CVA) capital charge, and the implied risk-weighted exposure for the CVA.

(5) Removal of total capital requirements columns

The changes to the OIC needed to achieve this proposed change are the removal of the rightmost column from the tables required under the following clauses –

Schedule 9: clause 3 (except for the Counterparty Credit Risk table)

Schedule 11: clauses 3, 5, 6 (except for the Counterparty Credit Risk table), and 8.