Reserve Bank of New Zealand
Te Pūtea Matua

BPR131

Standardised Credit Risk RWAs

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Purpose of document

This document sets out the standardised approach for calculating risk-weighted assets (**RWAs**) on **credit risk** exposures. The calculation of **credit risk RWAs** is part of the calculation of capital ratios, as defined in BPR100 and BPR130, which a bank must carry out to determine its compliance with minimum regulatory capital requirements. A bank must calculate all of its **credit risk RWAs** using the methodology in this document, unless it has been accredited by the Reserve Bank to use the internal-ratings based approach (an **IRB bank**). An **IRB bank** must also use the methodology in this document for calculating **RWAs** on certain **credit risk** exposures, in the cases specified in BPR130.

Document version history

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1 October 2021	Minor layout changes
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Conditions of registration

The Banking (Prudential Supervision) Act 1989 (the **Act**) permits the Reserve Bank to impose conditions of registration (conditions) on **registered banks**[1].

This document BPR131: Standardised Credit Risk RWAs forms part of the requirements for the following conditions:*

- A New Zealand-incorporated **registered bank** is normally subject to a condition requiring it to maintain capital ratios above specified minimum levels, and also to a condition imposing restrictions on its dividend payments when its **prudential capital buffer ratio** falls below specified levels[2]. This document sets out the standardised risk-weighting methodology for **credit risk RWAs** that will be needed by such a bank to allow it to calculate its day-to-day values for the capital ratios and the capital buffer ratio, and hence monitor its compliance with these capital adequacy conditions.

* All of the material set out in this document forms part of the requirements of the applicable condition, except material that is expressly identified as guidance by being included in a shaded box like this.

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[1] The conditions can relate to any of the matters referred to in sections 73 – 73B, 78 and 81. The standard conditions are contained in Appendix 1 of document BS1: Statement of Principles.
[2] These conditions of registration relate to the matter referred to in: section 78(1)(c) (capital in relation to the size and nature of the business).

BPR131: Standardised Credit Risk RWAs

Part A: Standardised approach to credit risk RWAs

Part B: Standardised rating grades

Part C: Risk weights for credit exposures

Part D: Equivalent exposure amounts for off-balance sheet exposures

Part E: Counterparty credit risk (CCR)

Part F: Credit Valuation Adjustment (CVA) capital charge

Part G: Central counterparties (CCPs)

Contents

Part A: Standardised approach to credit risk RWAs

A1 Overview

A1.1 Purpose of document

A1.2 When provisions of this document apply

A1.3 Calculation of credit risk RWAs

A1.4 Components of credit risk RWA calculation

A1.5 Calculation of risk-weighted exposures across all borrowers or counterparties

A1.6 Calculation of total RWAs for all other assets

A1.7 Calculation of RWA for CVA capital charge

A1.8 Credit risk RWAs from trades cleared across CCPs

Part B: Standardised rating grades

B1 Credit ratings

B1.1 Introduction

B1.2 Rating agency credit ratings

B1.3 Credit ratings must be solicited

B1.4 Issue-specific credit ratings

B1.5 Inferred ratings

B1.6 Restrictions on use of inferred ratings

B1.7 Multiple ratings

B2 Rating grades

B2.1 "Unrated" grade when no rating agency credit rating applies

B2.2 Rating grades for short-term credit ratings

B2.3 Rating grades for long-term ratings

Part C: Risk weights for credit exposures

C1 Overview

C1.1 Introduction

C2 Risk weights for items other than RMLs

C2.1 Currency, gold and cash items

C2.2 Claims on sovereigns and central banks

C2.3 Claims on public sector entities

C2.4 Multilateral development banks and other international organisations

C2.5 Claims on banks

C2.6 Banks: sovereign floor for unrated claims

C2.7 Claims on corporates

C2.8 Corporates: sovereign floor for unrated claims

C2.9 Banks and corporates: issue-specific short-term ratings

C2.10 Floor on unrated bank and corporate claims

C2.11 Banks: unrated claims up to 3 months when other claims have short-term credit ratings

SUPERSEDED

C2.12 Past due non-mortgage loans

C2.13 Measure of equity exposure

C2.14 Equity

C2.15 Fixed assets

C2.16 Leased assets

C2.17 Bank as lessor

C2.18 Other assets

C3 Risk weights for RMLs

C3.1 Introduction

C3.2 Meaning of RML

C3.3 Classification of RMLs

C3.4 C3.4 Definitions applying in relation to RMLs

C3.5 Loan-to-valuation ratio (LVR)

C3.6 Requirements for residential property valuation policy

C3.7 Eligible property valuer

C3.8 Valuation provided by professional valuation service

C3.9 Conditions for qualifying lender's mortgage insurance

C3.10 RMLs not past due

C3.11 Past due RMLs

Part D: Equivalent exposure amounts for off-balance sheet exposures

D1 Overview

D1.1 Introduction

D2 Credit equivalent amount (CEA)

D2.1 Calculating CEAs for off-balance sheet items

D2.2 CCFs for off-balance sheet exposures

Part E: Counterparty credit risk (CCR)

E1 Overview

E1.1 Introduction

E1.2 Recognition of collateral

E1.3 Calculation of RWAs for counterparty credit risk

E1.4 Other RWA calculations using CEA

E2 CEA for single derivative

E2.1 Calculation of CEA for derivatives

E2.2 Future risk factors for derivatives other than credit derivatives

E2.3 Future risk adjustments for credit derivatives

E3 CEA for bilaterally-netted derivatives

E3.1 Conditions

E3.2 Calculation of net credit equivalent exposure

E3.3 Calculation of net exposure for derivatives with same currency and maturity

E4 CEA for SFTs

E4.1 Calculation of CEA for SFTs

Part F: Credit Valuation Adjustment (CVA) capital charge

F1 Overview

F1.1 Introduction

F2 Calculation of CVA capital charge

F2.1 CVA capital charge calculation: general case

F2.2 CVA capital charge calculation: no eligible hedges

F2.3 CVA capital charge calculation: no eligible hedges, only one counterparty

F2.4 CVA capital charge: risk weights

F2.5 CVA capital charge: conditions on hedges

Part G: Central counterparties (CCPs)

G1 Introduction

G1.1 Exposures arising from trades settled via CCPs

G1.2 Meaning of qualifying central counterparty (QCCP)

G2 QCCP capital requirements

G2.1 Bank is QCCP clearing member acting on own behalf

G2.2 Bank is client of QCCP clearing member

G2.3 Bank is QCCP clearing member acting for client

G2.4 Treatment of posted collateral

SUPERSEDED

G3 Non-qualifying CCP capital requirements

G3.1 Requirements for exposures to non-qualifying CCPs

SUPERSEDED

Part A: Standardised approach to credit risk RWAs

A1 Overview

A1.1 Purpose of document

This document sets out the methodology for calculating risk-weighted assets (**RWAs**) for **credit risk**, under the standardised approach.

A1.2 When provisions of this document apply

1. A **standardised bank** must use the approach in this document to calculate **RWAs** for all of the credit exposures that fall within the scope of the definitions in this document.

2. An **IRB bank** must use the approach in this document to calculate **RWAs** in any of the cases where Part C of BPR130 specifies that standardised **RWAs** are required.

3. This document also requires the bank to calculate **RWAs** for certain other assets that are included on the accounting balance sheet but do not give risk to **credit risk**.

Guidance: These assets include, for example, fixed assets: see section C2.15.

4. The bank must calculate **RWAs** for all credit exposures and other assets covered by subsections (1) to (3) that fall within the scope specified in section A1.3 of BPR130.

A1.3 Calculation of credit risk RWAs

1. In the standardised approach, **RWAs** for **credit risk** are calculated by risk weighting on and off-balance sheet exposures to **credit risk** according to broad categories of relative credit risk, as set out in this Part.

2. The following general limitations and requirements apply in relation to the calculation of standardised **RWAs**:

   a. an asset deducted from capital must not be included in risk weighted exposures:

   b. the value of an exposure to be used for the calculation of **RWAs** must be the value after deducting any impairment allowances attributable to the exposure:

Guidance: The impairment allowances attributable to an exposure include any **loss allowance** for expected credit loss individually assessed on the exposure, and the portion of any collectively assessed impairment allowance that is allocated to the exposure. This deduction applies both to impairment allowances recognised on on-balance sheet assets, and to impairment allowances recognised on commitments and financial guarantee contracts, for which the calculation approach is set out in section D2.1

   c. where a net (unrealised) gain on a foreign exchange contract or an interest rate contract has been taken to retained earnings via the profit and loss account, the corresponding balance sheet asset must be excluded from **RWAs** in order to avoid double counting.

SUPERSEDED

A1.4 Components of credit risk RWA calculation

To calculate total **credit risk** **RWAs** under the standardised approach, a bank must sum the following amounts:

a. the total risk-weighted credit exposures across all counterparties calculated in accordance with section A1.5; and

b. the total **RWAs** for all other assets on the balance sheet in accordance with section A1.6; and

c. the **RWA** equivalent of the capital charge for **credit valuation adjustment** (**CVA**) in accordance with section A1.7; and

d. **credit risk** **RWAs** arising from trades settled on Central Counterparties (**CCPs**), other than exposures to counterparties already captured under subsection (a), calculated in accordance with section A1.8.

A1.5 Calculation of risk-weighted exposures across all borrowers or counterparties

To calculate risk-weighted exposures across all counterparties the bank must–

a. allocate each borrower or counterparty giving rise to an on- or off-balance sheet claim to the relevant exposure class; and

b. for any exposure other than a **residential mortgage loan** (**RML**), allocate a standardised rating grade to the exposure following the approach in Part B; and

Guidance: The standardised rating grades include a grade of "unrated" for any exposure meeting the conditions of section B2.1.

c. determine the applicable risk-weight for the exposure according to either–

   i. the exposure class and rating grade (see sections C2.2 to C2.12); or

   ii. in the case of a **RML**, the classification, loan-to-valuation ratio, and lender's mortgage insurance conditions (see subpart C3); and

d. calculate any on-balance sheet exposure amount for a borrower in accordance with section A1.3(2)(b); and

e. for any off-balance sheet exposure arising from a transaction of a type listed in Table D2.2, calculate the credit-equivalent amount (**CEA**) according to subpart D2 and use Table D2.2 to identify which entity determines the applicable risk weight; and

f. calculate the **CEA** for any counterparty **credit risk** (**CCR**) arising from **derivatives** or **securities financing transactions** (**SFTs**) with the counterparty according to Part E; and

SUPERSEDED

g. calculate the total risk-weighted exposure for each borrower or counterparty, by multiplying the risk-weight, determined under paragraph (c), by the sum of the on-balance sheet amounts and off-balance sheet **CEA** amounts for that counterparty, determined under paragraphs (d) to (f); and

h. if **credit risk** mitigation is in place on an exposure to a borrower or counterparty, apply any allowable adjustments to the risk-weight, the exposure amount, or both (as the case may be), in the calculation in paragraph (g), in accordance with BPR132; and

i. sum the total of all risk-weighted exposures.

A1.6 Calculation of total RWAs for all other assets

To calculate total **RWAs** for all other assets, the bank must–

a. allocate all amounts on the balance sheet (under the applicable scope of calculation) that are not specified in section A1.5 to one of the following categories:

   i. currency, gold and cash items (see section C2.1); or

   ii. **equity** holdings (see sections C2.13 and C2.14); or

   iii. fixed assets (see section C2.15); or

   iv. leased assets (see section C2.16); or

   v. exposures arising for the bank as lessor (see section C2.17); or

   vi. other assets (see section C2.18); and

b. multiply that amount by the risk weights indicated.

A1.7 Calculation of RWA for CVA capital charge

The bank must calculate the contribution of the **credit valuation adjustment** (**CVA**) capital charge to total risk-weighted credit exposures in accordance with the following formula:

$$12.5 \times K$$

where K is the **CVA** capital charge calculated in accordance with Part F.

Guidance: The **CVA** capital charge is a single number calculated across all of the bank's counterparties for non-centrally-cleared **derivatives**, based on the total **CEA** for each counterparty, calculated in accordance with Part E.

Part G provides that in some cases, the bank's involvement in the central clearing of a **derivative** gives rise to an exposure which the bank must treat as a bilateral trade, and in these cases the **CEA** of the trade must also be included in the **CVA** calculation.

SUPERSEDED

A1.8 Credit risk RWAs from trades cleared across CCPs

1. For a bank calculating capital ratios using the standardised approach, the contribution to **credit risk RWAs** from trades involving a **CCP** is the sum of the following amounts, as applicable to the particular bank:

   a. if the bank is a clearing member of a Qualifying **CCP** (**QCCP**) clearing its own trades, the risk-weighted exposure calculated in accordance with section G2.1:

   b. if the bank is a non-member transacting with a **QCCP** using a clearing member as intermediary, the risk-weighted exposure calculated using the applicable method specified in section G2.2:

Guidance: The method used depends on whether the transaction meets the conditions in subsections G2.2(3), G2.2(4) or G2.2(5) respectively.

   c. if the bank is a clearing member of a **QCCP** acting for a client, the risk-weighted exposure calculated in accordance with section G2.3:

   d. if the bank has posted collateral, either as a clearing member of a **QCCP** or as a client of a clearing member, the risk-weighted exposure amount calculated in accordance with section G2.4:

Guidance: This calculation includes the **credit risk** both on the assets posted and on the counterparty holding the collateral.

   e. for any trade settled through a non-qualifying **CCP**, a **credit risk** exposure calculated in accordance with subsection G3.1(1) and (2), following the treatment for a non-centrally cleared bilateral trade, with the **CEA** calculated under subsection A1.5(f) and the risk-weight determined under subsection A1.5(c):

   f. if the bank has contributed to a non-qualifying **CCP's** default fund, a risk-weighted exposure calculated in accordance with subsections G3.1(4) and (5).

Guidance: Unless the conditions for using the risk weights in Part G are satisfied, a bank must calculate the **RWA** for a trade exposure (**TE**) to a **CCP** using the **CEA** methodology in subsection A1.5(f) and the risk-weight determined under subsection A1.5(c).

2. For an **IRB bank**, the contribution to **credit risk RWAs** from trades involving a **CCP** is the sum of the amounts specified in subsection (1), except in the case of trades involving counterparties for which–

   a. Part G specifies that the trade exposure must be risk-weighted using the bank's approach applicable to a bilateral exposure to the counterparty; and

   b. the counterparty is a modelled exposure for the bank.

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Part B: Standardised rating grades

B1 Credit ratings

B1.1 Introduction

This subpart sets out the approach a bank must use to determine the standardised rating grades to be used for risk-weighting exposures to **credit risk** in accordance with Part C.

Guidance: For residential mortgages, the risk-weighting categories take into account loan-to-valuation ratios (LVRs) and lender's mortgage insurance arrangements. For other types of exposure, credit ratings from independent credit rating agencies are used as a basis for determining risk weights.

B1.2 Rating agency credit ratings

1. Only a credit rating produced by one of the rating agencies listed in subsection (2) may be used for determining the rating grade to be used for risk-weighting a **credit risk** exposure.

2. The rating agencies are–

   a. Standard & Poor's:

   b. Moody's Investor Services:

   c. Fitch Ratings:

   d. AM Best, but only for risk-weighting **credit risk** exposures to New Zealand licensed **insurers**.

Guidance: For details of the criteria the Reserve Bank uses for deciding whether or not to approve a credit rating agency see BS1: Statement of Principles, Appendix 3, and in relation specifically to licensed insurers, see the Reserve Bank document "Rating agency approval: Guidelines – Insurance Sector".

B1.3 Credit ratings must be solicited

A bank may determine the rating grade of a credit exposure by using a credit rating from one of the rating agencies specified in section B1.2, but only if the credit rating has been–

a. solicited from the rating agency; and

b. paid for by either–

   i. the entity giving rise to the credit exposure; or

   ii. a commercial associate of that entity.

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Guidance: This includes an issue-specific credit rating of a debt issue, in which case the entity giving rise to the credit exposure is the debt issuer.

B1.4 Issue-specific credit ratings

1. When the bank has a claim on a borrower in the form of a holding in a specific debt issue made by the borrower, and the debt issue carries a specific credit rating from a rating agency, the bank must determine the rating grade for the claim using that issue-specific credit rating.

2. If a debt issue has issue-specific credit ratings from two or more rating agencies, all such ratings apply to the determination of the rating grade, which must be determined in accordance with section B1.7.

B1.5 Inferred ratings

1. For the purpose of this section, an **unassessed claim** is any claim that the bank has on a borrower that is not a holding in a specific debt issue with one or more issue-specific ratings in terms of section B1.4.

2. Subject to section B1.6, if a borrower has a long-term issuer credit rating, the bank must treat any **unassessed claim** on the borrower falling within the scope of that rating as having the same credit rating.

Guidance: A long-term issuer rating typically applies to senior unsecured claims, and in that case, subsection (2) means that the bank must treat all senior unsecured claims on the borrower as having that issuer credit rating. The range of possible long-term and issuer credit ratings is shown in Table B2.3.

3. Subject to section B1.6, if the bank has an **unassessed claim** on an issuer that does not have an inferred rating arising from subsection (2), the bank must determine the rating grade for the claim using the long-term credit rating for another claim on the issuer if–

   a. the **unassessed claim** ranks pari passu or senior to that other claim in all respects; or

   b. both—

      i. the **unassessed claim** does not rank pari passu or senior to that other claim in all respects; and

      ii. that other claim has an rating that maps, via its rating grade, to a less favourable risk weight than that for an unrated claim of the same type.

Guidance: Subsection (3)(b) is intended to ensure that a claim on an issuer is not given a more favourable risk weight than a higher-ranking claim on the same issuer by relying on the treatment for unrated claims.

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4. The bank must not determine the rating grade for an **unassessed claim** on a borrower using an issue-specific short-term credit rating of another claim on the borrower.

Guidance: In the cases provided for in sections C2.10 and C2.11, a short-term credit rating of one claim on a borrower may affect the risk-weighting of another claim on the borrower that is unrated in terms of Part B. The range of possible rating agency short-term credit ratings is shown in Table B2.2.

5. If the requirements of this section result in an **unassessed claim** receiving inferred ratings from two or more rating agencies, the bank must take account of all such inferred ratings in determining the rating grade, following the approach set out in section B1.7.

B1.6 Restrictions on use of inferred ratings

The following restrictions apply to inferred ratings:

a. a credit rating of a claim denominated in domestic currency must not be inferred from a credit rating of a claim denominated in a foreign currency.

b. a credit rating of a claim denominated in a foreign currency must not be inferred from a credit rating of a claim denominated in a domestic currency.

c. a credit rating of a claim on an entity in a corporate group must not be inferred from a credit rating of a claim on another entity in the same group.

B1.7 Multiple ratings

1. If the approach in sections B1.2 to B1.6 applied to a particular claim produces two credit ratings that apply to the claim, and those two credit ratings correspond to different rating grades and different risk weights, the bank must use the credit rating that produces the higher risk weight.

2. If the approach in sections B1.2 to B1.6 applied to a particular claim produces three or more credit ratings that apply to the claim, and those credit ratings correspond to different rating grades and more than one risk weight, the bank must use a credit rating that produces the higher of the two lowest risk weights.

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B2 Rating grades

B2.1 "Unrated" grade when no rating agency credit rating applies

The rating grade for a claim is "unrated" if no credit rating produced by a rating agency applies to the claim.

Guidance: Typically, if a borrower has a long-term issuer rating, most claims on the borrower that do not have an issue-specific credit rating will have a credit rating inferred from the issuer rating. An unrated claim may for example be a claim in a different currency to the currency of the issuer rating, or a claim that is subordinated to senior claims to which the issuer rating applies.

B2.2 Rating grades for short-term credit ratings

The rating grade for a short-term rating is the rating grade that corresponds to a rating agency's credit rating according to Table B2.2.

Table B2.2

Rating grades for short-term credit ratings

Short-term rating grade	Rating agency credit ratings			
	Standard & Poor's Corporation	Moody's Investor Services	Fitch Ratings	AM Best
1	A-1	P-1	F-1	AMB-1
2	A-2	P-2	F-2	AMB-2
3	A-3	P-3	F-3	AMB-3
4	Other	Other	Other	Other

B2.3 Rating grades for long-term ratings

The rating grade for a long-term or issuer credit rating is the rating grade that corresponds to the rating agency's credit rating according to Table B2.3.

Table B2.3

Rating grades for long-term and issuer credit ratings

Rating grade	Rating agency credit ratings			
	Standard & Poor's Corporation	Moody's Investor Services	Fitch Ratings	AM Best
1	AAA AA+ AA AA-	Aaa Aa1 Aa2 Aa3	AAA AA+ AA AA-	aaa aa+ aa aa-
2	A+ A A-	A1 A2 A3	A+ A A-	a+ a a-
3	BBB+ BBB BBB-	Baa1 Baa2 Baa3	BBB+ BBB BBB-	bbb+ bbb bbb-
4	BB+ BB BB-	Ba1 Ba2 Ba3	BB+ BB BB-	bb+ bb bb-

SUPERSEDED

Rating grade	Rating agency credit ratings			
	Standard & Poor's Corporation	Moody's Investor Services	Fitch Ratings	AM Best
5	B+ B B-	B1 B2 B3	B+ B B-	b+ b b-
6	CCC+ CCC CCC- CC C D	Caa1 Caa2 Caa3 Ca C	CCC+ CCC CCC- CC C D	ccc+ ccc ccc- cc c

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Part C: Risk weights for credit exposures

C1 Overview

C1.1 Introduction

1. This Part sets out the risk weights to be applied to different categories of counterparty, for the purpose of calculating **RWAs** for credit exposures to those counterparties.

2. The risk-weights apply equally to credit exposures arising from on-balance sheet claims, and to the **CEAs** of off-balance sheet credit exposures and counterparty **credit risk** arising on **derivatives** and **SFTs**, as defined in Parts D and E.

3. Where the risk weight for a claim is determined by reference to the rating grade for the claim, the rating grade is as determined in Part B.

C2 Risk weights for items other than RMLs

C2.1 Currency, gold and cash items

1. A 0% risk weight applies to:

   a. notes and coins held on site; and

   b. gold bullion held:

      i. in own vaults; or

      ii. on an allocated basis and backed by bullion liabilities.

2. A cash item in the process of collection from another bank must be treated as a claim on that bank with a maturity of three months or less.

Guidance: Subsection (2) includes, for example, cheques, drafts, or other items drawn on other **registered banks** or **overseas banks** that are payable immediately upon presentation and that are in the process of collection.

C2.2 Claims on sovereigns and central banks

1. A 0% risk weight applies to a claim on the **Crown** or the Reserve Bank that is denominated in New Zealand dollars.

2. The risk weight for a claim on the **Crown** or the Reserve Bank that is not denominated in New Zealand dollars, or for a claim on any other **sovereign** or its central bank, is determined by the rating grade for the claim in accordance with Table C2.2.

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Table C2.2

Risk weights for claims on other sovereigns and their central banks

Rating grade	Risk weight (%)
1	0
2	20
3	50
4	100
5	100
6	150
unrated	100

If there is no credit rating for a central bank, a credit rating for its **sovereign** may be used to infer a rating grade for the central bank.

Guidance: An implicit guarantee from a **sovereign** to another entity does not qualify that other entity for a lower risk weight than would otherwise apply. Any consideration of the use of explicit guarantees should be done in accordance with BPR132: Credit Risk Mitigation.

As set out in BPR132, when there is an issue-specific rating, if the rating agency has considered the impact of the relevant guarantee in those credit ratings, then additional credit risk mitigation is not permitted.

C2.3 Claims on public sector entities

The risk weight for a claim on a **public sector entity** (**PSE**) is determined by the **sovereign** rating grade for a claim on the country in which the **PSE** is located, in accordance with Table C2.3.

Table C2.3

Risk weights for claims on PSEs

Sovereign rating grade	Risk weight (%)
1	20
2	50
3	100
4	100
5	100

SUPERSEDED

Sovereign rating grade	Risk weight (%)
6	150
unrated	100

Guidance: **Public sector entity** includes the New Zealand Local Government Funding Agency Limited. It does not include other council-controlled trading organisations, which will generally qualify as 'corporate' under BPR131.

C2.4 Multilateral development banks and other international organisations

1. A 0% risk weight applies to a claim on a body listed below (the **lowest-risk multilateral development banks and supranationals**)–

   a. World Bank Group, comprising–

      i. International Bank for Reconstruction and Development:

      ii. International Finance Corporation:

      iii. Multilateral Investment Guarantee Agency:

      iv. International Development Association:

   b. Asian Development Bank:

   c. African Development Bank:

   d. European Bank for Reconstruction and Development:

   e. Inter-American Development Bank:

   f. European Investment Bank:

   g. European Investment Fund:

   h. Nordic Investment Bank:

   i. Caribbean Development Bank:

   j. Islamic Development Bank:

   k. Council of Europe Development Bank:

   l. International Finance Facility for Immunization;

   m. Asian Infrastructure Investment Bank;

   n. Bank for International Settlements:

   o. International Monetary Fund:

   p. European Central Bank:

SUPERSEDED

q. European Union:

r. European Stability Mechanism:

s. European Financial Stability Facility.

2. The risk weight for a claim a **multilateral development bank** or **quasi-sovereign development bank** listed below (**other development bank**) is determined by the rating grade for the claim in accordance with Table C2.4.

a. Export Development Canada;

b. Export-Import Bank of Korea;

c. KfW Bankengruppe;

d. Landwirtschaftliche Rentenbank;

e. Korea Development Bank; and

f. Swedish Export Credit Corporation.

Table C2.4

Risk weights for claims on other development banks

Rating grade	Risk weight (%)
1	20
2	50
3	50
4	100
5	100
6	150
unrated	50

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C2.5 Claims on banks

1. The risk weight for a claim on a bank, other than a claim that has a short-term rating grade, is determined by the rating grade of the claim, in accordance with either–

a. columns 1 and 2 of Table C2.5, if the claim has an original and effective maturity of not more than 3 months; or

b. columns 1 and 3 Table C2.5, if the claim has an original and effective maturity of more than 3 months.

2. If the counterparty bank has issued any instrument that has an issue-specific short-term rating grade, the risk weights specified in subsection (1) are subject to the additional requirements of sections C2.9 to C2.11.

Table C2.5

Risk weights for claims on banks

Rating grade	Risk weight for a claim with an original maturity of 3 months or less (%)	Risk weight for a claim with an original maturity of more than 3 months (%)
1	20	20
2	20	50
3	20	50
4	50	100
5	50	100
6	150	150
unrated, subject to sections C2.6 and C2.10	20	50

C2.6 Banks: sovereign floor for unrated claims

The risk weight for an unrated claim on a bank (whether its **original maturity** is 3 months or less, or more than 3 months) is the greater of:

a. the risk weight for the claim under section C2.5; and

b. the risk weight of the sovereign territory in which the bank is incorporated.

C2.7 Claims on corporates

1. The risk weight for a claim on a corporate, other than a claim that has a short-term rating grade, is determined by the rating grade for the claim in accordance with Table C2.7.

Table C2.7

Risk weights for claims on corporates

Rating grade	Risk weight (%)
1	20
2	50
3	100
4	100
5	150
6	150
unrated, subject to sections C2.8 and C2.10	100

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2. If the corporate has issued any instrument that has an issue-specific short-term rating grade, the risk weights specified in subsection (1) are subject to the additional requirements of sections C2.9 and C2.10.

3. To avoid doubt, all aspects of the RWA treatment applying in this subpart to claims on corporates applies to all claims on all types of corporates, including, for example, claims on the following types of entity:

   a. a securities firm:

   b. an **insurance entity**:

   c. a **state enterprise**:

   d. a **Crown entity**:

   e. a **non-bank deposit-taker**.

C2.8 Corporates: sovereign floor for unrated claims

The risk weight for an unrated claim on a corporate is the greater of:

a. the risk weight determined for the claim under section C2.7; and

b. the risk weight of the sovereign territory in which the corporate is incorporated.

C2.9 Banks and corporates: issue-specific short-term ratings

1. This section specifies the risk weights to be applied where a claim on a bank or corporate has been given an issue-specific short-term credit rating by a rating agency.

Guidance: In subsection (1), "short-term" does not denote any particular maximum maturity: rather, it refers to the nature of the rating agency credit rating. The possible rating agency short-term credit ratings and the corresponding short-term rating grades are set out in Table B2.2.

2. The risk weight for a claim on a bank or corporate that has a short-term issue-specific credit rating is determined by the short-term rating grade for the claim in accordance with Table C2.9.

Table C2.9

Risk weights for claims on banks and corporates with short-term ratings

Short-term rating grade	Risk weight (%)
1	20
2	50
3	100
4	150

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C2.10 Floor on unrated bank and corporate claims

1. Subsection (2) applies to a counterparty **bank** that has any outstanding debt issue with a short-term rating grade that attracts a risk weight of either 50% or 100% under Table C2.9.

2. Any claim on a **bank** referred to in subsection (1) that has an original and effective maturity of 3 months or less and is unrated in terms of section B2.1 must be risk-weighted at 100%.

3. Subsection (4) applies to a counterparty **bank** or corporate that has any outstanding debt issue with a short-term rating grade that attracts a risk weight of 150% under Table C2.9.

4. Any claim on a **bank** or corporate referred to in subsection (3) that is unrated in terms of section B2.1 must be risk-weighted at 150%.

Guidance: Subsection C2.10(2) overrides the risk-weighting treatment for unrated claims on **banks** with up to 3 months' **original maturity**, provided in column 2 of Table C2.5. Subsection C2.10(4) overrides the risk-weighting treatment for unrated claims on **banks** or corporates in Tables C2.5 and C2.7, regardless of maturity. These treatments apply whether or not the bank owns any of the outstanding debt issue that determines the risk-weighting of the claim.

C2.11 Banks: unrated claims up to 3 months when other claims have short-term credit ratings

If a counterparty **bank** has one or more issues outstanding that have an issue-specific short-term credit rating, the bank must risk-weight any unrated claim on the counterparty that has an original and effective maturity of not more than 3 months using the greater of:

a. the risk weight derived in accordance with section C2.5 and columns 1 and 2 of Table C2.5; and

b. the highest risk weight applying under Table C2.9 to any of the issues with short-term rating grades.

Guidance: The effect of this section is that the general preferential risk-weighting treatment in Table C2.5 for claims up to 3 months on **banks** is overridden if the counterparty has issued any debt with an issue-specific short-term credit rating that leads to a higher risk weight under Table C2.9.

C2.12 Past due non-mortgage loans

1. The risk weights in this section apply to any 90 day past due asset other than a **RML**.

2. The amount to be risk-weighted is the portion of the asset that is not secured by eligible collateral, guarantee or **credit derivative** in accordance with BPR132, net of any allowance for expected credit losses that is attributable to the asset.

3. The risk weight is either:

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a. 150%, if the attributable allowance for expected credit losses for the loan is less than 20% of the outstanding amount of the loan; or

b. 100%, if the attributable allowance for expected credit losses for the loan is equal to or greater than 20% of the outstanding amount of the loan.

Guidance: The allowance for expected credit losses attributable to an asset refers to the loss allowance assessed on the asset on an individual basis, or the portion of any collectively assessed allowance that is allocated to the asset (or both).

C2.13 Measure of equity exposure

1. For risk-weighting an **equity** exposure as required by section C2.14, the measure of the exposure is the current book value, including revaluations, net of any allowances for impairment.

2. A short position in an individual **equity** or a **derivative**, held in the banking book, is permitted to offset a long position in the same individual **equity** provided that the instrument–

   a. has been explicitly designated as a hedge of the specific **equity** holding; and

   b. has remaining maturity of at least one year.

3. Any other short position in an **equity** must be treated as if it was a long position, with the relevant risk-weight applied to the absolute value of the position.

C2.14 Equity

The risk weight for an **equity** holding is:

a. 300% if the holding is in an **equity instrument** that is included in the NZX50 or an overseas equivalent share market index; or

b. if the holding is an equity stake in the New Zealand Business Growth Fund,

   i. 250% for a holding up to a maximum of 2% of the bank's **CET1 capital**; and

   ii. 400% for any holding in excess of 2% of the bank's **CET1 capital**; or

c. in all other cases, 400%.

C2.15 Fixed assets

The risk weight for any investment in premises, plant, equipment, or other fixed asset is 100%.

C2.16 Leased assets

If the bank or a member of the **banking group** has a right-of-use asset as lessee—

a. if the underlying asset is tangible the asset must be risk-weighted at 100%; and

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b. if the underlying asset is intangible, it must be included in the deduction from **CET1** capital for goodwill and other intangibles, required by section B1.3 of BPR110.

C2.17 Bank as lessor

1. If the bank has provided lease financing to a counterparty, except in the case that the bank is exposed to **residual value risk**, the value of the exposure must be risk-weighted using the risk weight applicable to the counterparty.

Guidance: If the leased asset is eligible as collateral in BPR132, the bank may adjust the **RWA** for **credit risk** mitigation.

2. If the bank is exposed to **residual value risk**–

   a. the discounted lease payment stream must be risk-weighted using the risk-weight applicable to the counterparty; and

   b. the residual value must be risk-weighted at 100%.

3. For the purpose of this section, **residual value risk** is the bank's exposure to potential loss due to the fair value of the equipment declining below its residual estimate at lease inception.

Guidance: For an **IRB bank** calculating the **RWA** for a counterparty within a **modelled exposure class**, the standardised risk-weighting treatment in section C2.17 applies to any **residual value risk**, but the applicable **IRB** risk-weighting treatment in BPR133 applies to the exposure to the lessee.

C2.18 Other assets

1. A 100% risk weight must be applied to any on-balance sheet asset that falls within the scope of calculation specified in section A1.3 of BPR130 and for which the bank has not calculated an **RWA** either as provided in this subpart or subpart C3 or, in the case of an **IRB bank**, as an **IRB** modelled exposure in accordance with BPR133.

Guidance: For a bank using the standardised methodology, these "other assets" include, for example, loans to personal customers other than RMLs.

2. Notwithstanding subsection (1) above, a risk weight of 20% applies to any Kāinga Whenua loan product (being a loan secured against a residential dwelling situated on Māori land, where Kāinga Ora–Home and Communities is the **LMI** provider), provided that the **LMI** covers 100% of the potential loss faced by the bank.

C3 Risk weights for RMLs

C3.1 Introduction

This subpart defines **residential mortgage loan** (**RML**), defines the subcategories of **RML**, defines the loan-to-valuation ratio (**LVR**) for an **RML**, and specifies eligibility conditions for

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lender's mortgage insurance (**LMI**), in order to specify the risk-weight to be applied to an **RML** based on the type of loan, the LVR of the loan, and whether **LMI** is in place.

C3.2 Meaning of RML

1. **RML** means a loan secured by a first ranking mortgage over a residential property used primarily for residential purposes by the mortgagor, a related party of the mortgagor, or a tenant of the mortgagor.

2. A loan may not be classified as a **RML** if the mortgaged property is predominantly used for farming or commercial activities.

3. A property will be considered to be predominantly used for farming or commercial activity if, for example,–

   a. the mortgaged property would be marketed as a farm or a commercial property; or

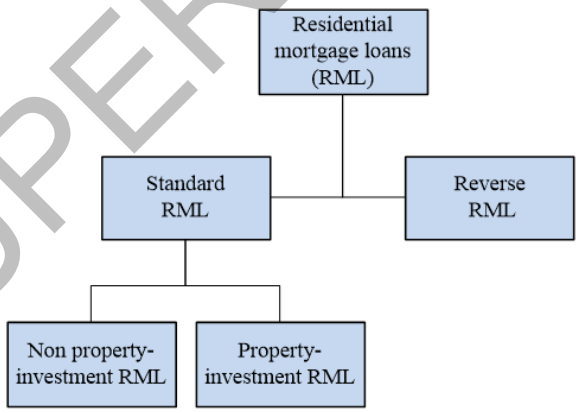
   b. the principal or interest payments are predominantly serviced from the income generated by the use of the property for farming or commercial activity, except where that income is rental income and the property is used for a residential purpose.

4. For the purpose of this section, predominantly means more than 50%.

C3.3 Classification of RMLs

1. A **RML** must be classified as either a **standard RML** or a **reverse RML**.

2. The diagram below depicts the sub-classification of **RMLs**.



3. A **standard RML** must be further sub-classified into either a **non property-investment RML** or a **property-investment RML**.

C3.4 Definitions applying in relation to RMLs

1. The following definitions apply in respect of **RMLs**:

non property-investment RML means a **standard RML** secured over only owner-occupied residential property

owner-occupied residential property means a property that meets the following criteria:

   a. a legal and/or beneficial interest is held in the property by–

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i. a natural person(s); and/or

ii. a related party(ies) of a natural person(s); and

b. a natural person(s) referred to in (i), or their spouse, civil union partner, or de facto partner, intends to occupy the property either as their principal or secondary residence (a secondary residence includes a holiday home or a second home that is primarily for the use of that person); and

c. in respect of a secondary residence, no rental income is derived from that property, except to the extent that the rental income is minimal

Guidance: For example, where the secondary residence is a bach that is rented out for six weeks a year.

property-investment RML means a **standard RML** that is not a **non property-investment RML**

reverse RML means an **RML** for which payments of principal or interest are not due in accordance with an agreed repayment schedule, but rather on the occurrence of a specified trigger event, in which case the repayment of the loan is made from the proceeds of sale of the property

standard RML means an **RML** that is not a **reverse RML**.

2. For the purposes of the definition of **owner-occupied residential property**, a person (A) is a related party of a natural person (B) in any of the following situations:

a. A is the trustee of a trust and B is a beneficiary of that trust (including where A and B are the same person):

b. A is a company or an unincorporated body of persons (including a company or unincorporated body of persons that owns the property as trustee) and B is a shareholder of, or otherwise controls, A:

c. A is the administrator of the estate of the deceased spouse or partner (civil union or de facto) of B.

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C3.5 Loan-to-valuation ratio (LVR)

1. Subject to subsection (2), the loan-to-valuation ratio (LVR) for an **RML** is calculated by the following formula:

$$Loan\text{-}to\text{-}vduation\ ratio = \frac{\text{loan value}}{\text{property value}} \times 100$$

where–

loan value is the total current amount of–

a. all claims secured by way of first ranking mortgage over residential property; and

b. all undrawn commitments to the borrower that when drawn down will be secured by way of first ranking mortgage over residential property.

Guidance: Lending facilities that are not tied to, nor managed as part of, the **RML** and that are not normally treated as secured over the residential property (for example, credit cards or personal loans), do not need to be included in the LVR calculation.

property value,–

a. for a **standard RML**, or a **reverse RML** at the time of origination, is the total value of the residential property that is security for the loan, determined, when the loan is originated, under a residential property valuation policy that meets the eligibility criteria in section C3.6; and

b. for a **reverse RML**, must be updated at least every three years and, at that time, is calculated using the following formula:

$$\text{Property value} = \begin{cases} \text{Max}(V_O, 80\% \times V_R) & \text{if } V_R > V_O, \text{ or} \\ V_R & \text{if } V_R \leq V_O \end{cases}$$

Where–

V_O is the total value of the residential property that is security for the **RML** determined at origination in accordance with subsection (a); and

V_R is the total value determined at the most recent three-yearly update under the bank's residential property valuation policy.

2. If the property value for an **RML** has not been determined using an eligible valuation approach in terms of subsection (1), the LVR of the loan for risk-weighting purposes is 150%.

C3.6 Requirements for residential property valuation policy

To be eligible for use in calculating LVRs, a bank's residential property valuation policy must–

a. be approved by the bank's board of directors; and

b. require that, for the purpose of calculating the LVR for a loan secured by a mortgage over a residential property, the bank uses one of the following methods of valuation:

i. the purchase price of the property;

ii. a property valuation provided by a valuer who meets the conditions in section C3.7, and who is not associated with a person who has an interest in the property; or

iii. a property valuation that is provided by a professional valuation service and meets the conditions in section C3.8.

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c. include guidance on the appropriate **credit risk**-related use of different valuation products; and

d. include guidance on the use of the purchase price of a residential property; and

e. include guidance on the determination of the origination date; and

f. ensure that its application is invariant to the direction of the movement of residential property prices; and

g. for reverse mortgage loans, require that the property value is updated at least three-yearly.

Guidance: The conditions set out in this section are the same as the conditions applying to residential property valuation policies for IRB **credit risk RWAs**, except that under the standardised approach, the additional condition (g) specific to reverse mortgage loans is included (compare section D3.4 of BPR133).

C3.7 Eligible property valuer

The eligibility criteria for a property valuer referred to in section C3.6 are that the valuer is –

a. a registered valuer, as defined in the Valuers Act 1948; or

b. another person approved to provide valuation services by rules made under the Rating Valuations Act 1998; or

c. a person who meets the definition of valuer under the laws of another country, provided that the Reserve Bank has confirmed in writing to the bank that it considers the laws of the other country to be at least as satisfactory as the requirements under the Valuers Act 1948.

C3.8 Valuation provided by professional valuation service

To be eligible for use in calculating an LVR, a property valuation provided by a professional valuation service must be either

a. a statistical or modelled valuation based on market sales price data; or

b. a valuation carried out by appropriately qualified valuation personnel overseen by a valuer who meets the conditions in section C3.7, and who is not associated with a person who has an interest in the property.

C3.9 Conditions for qualifying lender's mortgage insurance

1. **LMI** qualifies for the purpose of C3.10 and C3.11 if that insurance–

a. meets the conditions specified in subsections (2) and (3); or

b. is provided by Kāinga Ora–Home and Communities.

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2. The insurance provider providing the **LMI** must have an insurer financial strength rating provided by Standard & Poor's, Moody's Investor Services, Fitch Ratings or A M Best listed in Table C3.9.

Table C3.9

Insurer Financial Strength Ratings

Standard & Poor's	Moody's Investor Services	Fitch Ratings	A M Best
AAA	Aaa	AAA	aaa
AA+	Aa1	AA+	aa+
AA	Aa2	AA	aa
AA-	Aa3	AA-	aa-
A+	A1	A+	a+
A	A2	A	a

3. The **LMI** used in any case must cover all losses realised in a default on the mortgage up to an amount of no less than 40% of the loan value.

4. In this section, loan value has the same meaning as in section C3.5.

C3.10 RMLs not past due

1. The risk weight for a **RML** that is not a 90 day **past due** asset is determined by the classification, LVR and **LMI** status of the loan in accordance with Table C3.10.

Table C3.10

Risk weights for RMLs that are not 90 days past due

Risk weight for a standard RML in %					Risk weight for a reverse RML in %	
Loan-to-valuation ratio	If there is lender's mortgage insurance that qualifies under section C3.9		If there is no lender's mortgage insurance or lender's mortgage insurance that does not qualify under section C3.9			
	Non-property investment RML	Property investment RML	Non-property investment RML	Property investment RML		
Does not exceed 80%	35	40	35	40	LVR <30%	40
>80% and ≤90%	35	50	50	70	LVR ≥30% - ≤60%	50

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Risk weight for a standard RML in %					Risk weight for a reverse RML in %	
Loan-to-valuation ratio	If there is lender's mortgage insurance that qualifies under section C3.9		If there is no lender's mortgage insurance or lender's mortgage insurance that does not qualify under section C3.9			
	Non-property investment RML	Property investment RML	Non-property investment RML	Property investment RML		
>90% and ≤100%	50	75	75	90	LVR >60% and ≤80%	80
Exceeds 100%	100				LVR >80%	100

2. A reverse **RML** may only be recognised in the **RML** category up to the value of the residential property used as security for the loan. Any excess of the loan over the property value is deducted from **CET1 capital** in accordance with BPR110: Capital definitions.

Guidance: A reverse **RML** for which the loan amount is greater than the property value gives rise to a RWA equal to 100% of the property value and a deduction from **CET1 capital** equal to the loan value less the property value. There is no separate treatment for defaulted reverse **RMLs**.

C3.11 Past due RMLs

1. The risk weight for a **RML** without qualifying mortgage insurance that is a 90 day past due asset is 100%.

2. The risk weight for a **RML** with qualifying mortgage insurance is the risk weight that corresponds to the LVR and **LMI** conditions as set out in Table C3.10.

Source: BS2A, para 39.

C3.12 RMLs where Kāinga Ora is the LMI provider for 100% of losses

1. Notwithstanding C3.10 and C3.11, the risk weight for a **RML** which meets the criteria in subsection (2) is 20%.

2. The criteria is that:

   a. Kāinga Ora–Home and Communities is the **LMI** provider (as per subsection C3.9(1)(b)); and

   b. the **LMI** covers 100% of potential loss faced by the bank.

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Part D: Equivalent exposure amounts for off-balance sheet exposures

D1 Overview

D1.1 Introduction

This Part sets out the methodology to be used to define the credit equivalent amount (**CEA**) for the off-balance sheet credit exposure arising on specified types of transaction that create contingent liability, including lending commitments, and for identifying the entity to be used for determining the risk weight in accordance with Part C.

Guidance: The methodology in this Part only applies directly to exposures being risk-weighted using the standardised approach. For **IRB** corporate specialised lending subject to the slotting approach, the method for calculating the **CEA** of contingent liabilities is specified in Subpart C9 of BPR133, and is based on the method in this Part with certain adaptations. For any other exposure to a counterparty within a **modelled exposure class**, an **IRB bank** must follow the approach in Subpart C5 or D5 of BPR133 for estimating the credit conversion factor (**CCF**).

D2 Credit equivalent amount (CEA)

D2.1 Calculating CEAs for off-balance sheet items

1. The **CEA** for an off-balance sheet item is intended to represent the amount of an on-balance sheet exposure that would expose the bank to equivalent **credit risk**.

2. The bank must calculate the **CEA** for an off-balance sheet exposure using the following formula:

$$\text{credit equivalent amount} = \text{credit conversion factor} \times \left(\text{principal amount} - \text{provision amount}\right)$$

where–

credit conversion factor	is the credit conversion factor (**CCF**) specified in section D2.2 for the off-balance sheet exposure
principal amount	is the principal amount of the off-balance sheet exposure
provision amount	is the amount of any **loss allowance** for expected credit losses for the exposure.

3. For the purpose of subsection (2), the principal amount of an off-balance sheet exposure arising from a commitment or other lending facility is the undrawn amount of the facility.

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Guidance: Any amount that a borrower has drawn down under a commitment or other lending facility must be treated as an on-balance sheet exposure for the purpose of section A1.5.

4. For the purpose of this subpart, a commitment is any arrangement that has been offered by the bank and accepted by the borrower to extend credit, purchase assets or issue credit substitutes, and the bank is considered to have made an offer when it communicates a lending limit to a client, or potential client, in writing.

Guidance: An arrangement that does not advise a lending limit and solely stipulates the terms and conditions of future trades does not constitute a commitment for this purpose.

D2.2 CCFs for off-balance sheet exposures

1. The credit conversion factor (**CCF**) for an off-balance sheet exposure of the type specified in column 1 of Table D2.2 is the percentage specified in column 2 of Table D2.2.

2. The risk weight for an off-balance sheet exposure of the type specified in column 1 of Table D2.2 is determined in accordance with column 3 of Table D2.2.

Guidance: In Table D2.2, **counterparty type** means that the risk weight is the same as that applying to an on-balance sheet claim on the counterparty to the transaction. **Type of asset** or **issuer of securities** means the risk weight is the risk-weight that would apply to an asset of the type involved in the transaction if it was held on the balance sheet, rather than the risk weight for the counterparty: in particular, if the asset is a holding of securities, the risk weight is that applying to the issuer of securities. The applicable on-balance sheet risk weights are those specified in Part C.

A credit card facility with standard terms is normally eligible for a 0% **CCF**, provided that any outstanding unused balance is subject to review at least annually.

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Table D2.2

CCFs

Type of transaction	CCF (%)	Risk weight by:
direct credit substitute	100	counterparty type
asset sale with recourse	100	type of asset, or issuer of securities as appropriate
forward asset purchase	100	type of asset
commitment with certain draw-down	100	counterparty type

Type of transaction	CCF (%)	Risk weight by:
note issuance facility	50	counterparty type
revolving underwriting facility	50	counterparty type
performance-related contingency	50	counterparty type
trade-related contingent item	20	counterparty type
placements of forward deposits	100	counterparty type
undrawn commitments to the Business Growth Fund	20	equity exposure as per C2.14
other commitment where **original maturity** is more than 1 year	50	counterparty type
other commitment where **original maturity** is less than or equal to 1 year	20	counterparty type
other commitment that cancels automatically when the creditworthiness of the counterparty deteriorates or which can be cancelled unconditionally at any time without prior notice	0	not applicable

3. A commitment to provide an off-balance sheet facility should be assigned the lower of the **CCFs** applicable to the commitment and to the off-balance facility respectively, and more generally an arrangement involving more than one of the types of transaction in Table D2.2 is subject to the minimum of the **CCFs** applicable to those transactions.

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Part E: Counterparty credit risk (CCR)

E1 Overview

E1.1 Introduction

1. This Part sets out the methodology for calculating the **CEA** of the counterparty **credit risk** (**CCR**) arising from **derivatives** and **SFTs**.

2. Subpart E2 sets out the methodology to be used in relation to an individual **derivative** not covered by a bilateral netting agreement.

3. Subpart E3 sets out the methodology to be used in relation to a number of **derivatives** which are–

   a. with the same counterparty; and

   b. subject to a bilateral netting agreement with that counterparty.

4. Subpart E4 summarises the methodology for calculating the **CEA** on **SFTs**.

Guidance: This Part applies to the **CCR** that arises when a bank enters into a **derivative** contract or **SFT** that gives rise to a contracted future payment or flow of future payments to and from an identifiable counterparty that are based on market variables. The contract may be entered into via an exchange ("exchange-traded") or bilaterally ("over-the-counter" or "**OTC**"). If a contract is settled via a central counterparty (**CCP**), concessionary risk-weighting treatments may apply, as set out in Part G, but the relevant trade exposure amounts must in all cases be determined using the methods in this part.

Guidance: This Part applies regardless of whether the counterparty is subject to the standardised risk-weighting treatment or to the **IRB** modelling approach. The calculation of total **EAD** for an **IRB bank** set out in Subpart C5 and D5 of BPR133 cross-refers to this Part for the calculation of the **CCR** component of **EAD**.

E1.2 Recognition of collateral

1. If a bank holds collateral against the **CCR** exposure arising from a single **derivative** or bilaterally netted **derivatives**, the bank may recognise the collateral by adjusting the **CEA** calculated under subpart E2 or subpart E3.

2. However, such recognition is subject to the minimum requirements of, and using the methodology set out in, BPR132.

Guidance: The comprehensive approach for adjusting exposure for collateral is set out in section B2.2 of BPR132. The simple approach (subject to eligibility) is set out in section B3.2 of BPR132. For **SFTs**, recognising collateral is an integral part of the **CEA** calculation (see subpart E4 of this document).

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E1.3 Calculation of RWAs for counterparty credit risk

1. If a bank calculates credit exposure **RWAs** to a counterparty using the standardised approach, the bank must calculate the **RWA** amount for the **CCR** arising from any **derivative** or **SFT** with the counterparty in accordance with the following formula:

RWA amount = **CEA** x risk weight for the counterparty

where–

CEA	is the **CEA** determined in accordance with this Part
risk weight for the counterparty	is the risk weight specified in Part C that applies to the counterparty.

2. If a bank is accredited to use the **IRB approach** to model the credit risk weight for the counterparty, the CEA must be added to the EAD for that counterparty, as part of the calculation of total RWAs for that counterparty, as specified in subparts C5 and D5 of BPR133.

E1.4 Other RWA calculations using CEA

1. When calculating the capital charge for **CVA** (see Part F), a bank must include the bank's total **CEA** for each counterparty arising from **derivatives** that are not cleared through a central counterparty (**CCP**), calculated using the methodology in this Part.

2. When calculating the capital charge for **CCR** arising from a **derivative** or **SFT** cleared on a **CCP** (see Part G), a bank must use the **CEA** methodology in this Part to calculate the trade exposure (TE).

3. To avoid doubt, this section applies to both **IRB** and **standardised banks**.

E2 CEA for single derivative

E2.1 Calculation of CEA for derivatives

1. This section applies to a **derivative** that is not covered by a bilateral netting agreement.

2. The **CEA** for a **derivative** is calculated by marking it to its current market value and adding on an amount for potential future credit exposure.

3. Unless subsection (4) applies, the **CEA** for a **derivative** contract is calculated using the formulae–

CEA = current credit exposure + **PFCE**

PFCE = notional principal x future risk factor

where–

current credit exposure is the greater of—

a. zero; and

b. the current marked-to-market replacement cost for the contract.

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notional principal	is the effective notional principal amount of the contract. This is the stated notional principal amount unless the stated notional principal amount is leveraged or enhanced by the structure of the transaction. For example, a stated notional amount of $1 million with payments based on an internal rate of two times the bank bill rate would have an effective notional amount of $2 million.
future risk factor	is the conversion factor for the potential future credit exposure over the remaining life of the contract under sections E2.2 and E2.3.
PFCE	means the potential future credit exposure.

4. For a **derivative** that is a single currency floating-to-floating interest rate swap, **PFCE** is set to nil in the formula for **CEA** in subsection (3).

Guidance: This means that the **CEA** for a **derivative** referred to in subsection (4) is only the current credit exposure as defined in subsection (3).

E2.2 Future risk factors for derivatives other than credit derivatives

1. This section specifies the conversion factor to be used to determine **PFCE** in calculating the **CEA** on a **derivative** of a type specified in column 1 of Table E2.2.

2. These conversion factors must also be used for calculating **PFCE** on each **derivative** subject to a netting agreement, for calculating $\mathbf{PFCE}_{Gross}$ in terms of section E3.2.

3. The conversion factor for an exposure is, subject to subsections (4) and (5), the factor that corresponds to the type and residual maturity of the **derivative** that gives rise to the exposure, as set out in Table E2.2.

Table E2.2

Conversion factors

Type of derivative	Conversion factor (%) for an exposure with a residual maturity:		
	less than or equal to 1 year	more than 1 year and less than or equal to 5 years	more than 5 years
currency or gold derivative	1	5	7.5
interest rate derivative	0	0.5	1.5
equity derivative	6	8	10
precious metal (other than gold) derivative	7	7	8
commodity (other than precious metal) derivative	10	12	15

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4. The conversion factor for a **derivative** with multiple exchanges of principal is the factor in subsection (3) multiplied by the number of remaining payments under the **derivative** contract.

5. For **derivatives** that are structured to settle outstanding exposure on specified payment dates and where the terms are reset such that the market value of the derivative is zero on these specified dates, the residual maturity is the time until the next reset date.

E2.3 Future risk adjustments for credit derivatives

1. This section applies to the bank's exposure arising from a single name **credit derivative** that is of a type specified in Table E2.3 and that the bank holds in its trading book.

2. To determine **PFCE** for calculating the **CEA** of a **credit derivative** covered by this section, the bank must use the conversion factor determined under Table E2.3.

Table E2.3

Conversion factors

Type of transaction		Conversion factor (%) for a transaction including:	
		a qualifying reference obligation	a non-qualifying reference obligation
total-rate-of-return swap	bank buys	5	10
	bank sells	5	10
credit default swap	bank buys	5	10
	bank sells (subject to subsection (3))	5	10

3. In the case where the bank has sold credit protection via a **credit default swap**, the bank must apply a conversion factor that is–

   a. as specified in Table E2.3 (see last row) if the transaction is subject to close-out upon the insolvency of the protection buyer when the reference entity is still solvent, but subject to the resulting **PFCE** being no more than the amount of any unpaid premium; or

   b. in all other cases, 0%.

4. For the purpose of this section, a reference obligation is qualifying if it has two or more long-term or issuer credit ratings that give rise to a rating grade of 1, 2, or 3 determined in accordance with Table B2.3 and the requirements for eligibility and inferred ratings set out in Part B.

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E3 CEA for bilaterally-netted derivatives

E3.1 Conditions

1. A bank may calculate the **CEA** of its **CCR** exposure arising from forwards, swaps, options, and similar **derivatives** with a given counterparty, on a net basis if–

   a. the claims arising on the individual contracts are subject to a legally valid form of bilateral netting contract; and

   b. the conditions specified in subsection (2) are satisfied.

2. The conditions referred to in subsection (1)(b) are that–

   a. the bilateral netting agreement or contract with the counterparty must be in writing; and

   b. the agreement must create a single legal obligation in relation to the counterparty for all individual **derivatives** able to be netted under the agreement; and

   c. should the counterparty not meet the terms of the agreement due to a default, insolvency, bankruptcy, **statutory management**, liquidation, or similar circumstance, the agreement must ensure that there is an exposure that is either a single claim to receive or a single obligation to pay only the net amount that results from the sum of the positive and negative mark-to-market values of the individual **derivatives** covered by the agreement; and

   d. written and reasoned legal opinions must be held that conclude with a high degree of certainty that, in the event of a legal challenge, the exposure under the agreement would be found to be the net amount under the laws of all relevant jurisdictions including–

      i. the law of the jurisdiction in which the counterparty is incorporated or chartered and, if a foreign branch of the counterparty is involved, the law of the jurisdiction in which the branch is located; and

      ii. the law that governs the individual transactions covered by the agreement; and

      iii. the law that governs any contract or agreement necessary to effect the bilateral netting agreement; and

   e. procedures must be in place to ensure that the legal characteristics of netting arrangements are kept under review in the light of possible changes to relevant laws; and

   f. the agreement must not contain walkaway clauses that permit the non-defaulting party to make only limited or no payment to the estate of the defaulter, even if the defaulter is a net creditor under the agreement.

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Guidance: A payments netting contract intended only to reduce the operational costs of daily settlements typically does not meet the conditions in subsection (2), and hence does not allow the bank to net potential future exposures.

E3.2 Calculation of net credit equivalent exposure

1. The net **CEA** for the counterparty credit exposure arising from **derivatives** that are subject to a bilateral netting agreement must be calculated in accordance with the following formula:

$$\mathbf{CEA} = \text{NCCE} + \mathbf{PFCE}_{adj}$$

where–

NCCE means the net current credit exposure, being the greater of–

a. the net mark-to-market replacement cost of the **derivatives** subject to the netting agreement; and

b. zero

$\mathbf{PFCE}_{adj}$ is the adjusted add-on for potential future credit exposure, calculated in accordance with subsection (2)

Guidance: NCCE is the sum of all mark-to-market values of all individual **derivatives** covered by a netting agreement, allowing positive values of transactions covered by the netting agreement to be offset against negative values of other transactions covered by that agreement. If the net sum of individual mark-to-market values is positive, the NCCE is that sum. However, if the sum of mark-to-market values is zero or negative, the NCCE is set equal to zero. NCCE is also given as a formula in a guidance box in subsection (3).

2. The add-on for netted transactions $\mathbf{PFCE}_{adj}$ is calculated using the formula:

$$\mathbf{PFCE}_{adj} = 0.4 \times \mathbf{PFCE}_{Gross} + 0.6 \times \text{NGR} \times \mathbf{PFCE}_{Gross}$$

3. In subsection (2), NGR means the net-to-gross ratio, being the ratio of NCCE to GCCE, where–

GCCE means the gross current credit exposure, being the sum of the mark-to-market replacement costs across all transactions which have positive current mark-to-market value, but subject to any special treatment required under section E3.3

NCCE has the meaning given to it in subsection (1)

Guidance: Expressed in mathematical terms–

$$GCCE = \sum_i Max(MTM_i, 0)$$

$$NCCE = Max(\sum_i MTM_i, 0)$$

where, in each case,–

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i indexes all **derivatives** subject to the bilateral netting agreement.

MTM_i is the current mark-to-market value of **derivative** "i", which is positive if the **derivative** is in the money, and negative if out of the money.

PFCE$_{Gross}$ is the sum of the individual **PFCE** amounts for each of the transactions subject to the bilateral netting agreement, calculated using the formula for **PFCE** in section E2.1(3) and the future risk factors in Table E2.2.

Guidance: If any of the relevant transactions are matching transactions, as defined in section E3.3(4), those transactions are subject to the special treatment provided for in section E3.3(2).

E3.3 Calculation of net exposure for derivatives with same currency and maturity

1. This section adjusts the calculation of **PFCE**$_{Gross}$ and GCCE in section E3.2(3) where the transactions covered by a netting agreement with a given counterparty include matching transactions, as defined in subsection (4).

2. For the purposes of calculating the total **PFCE** (**PFCE**$_{Gross}$) for all **derivatives** with a given counterparty covered by a netting agreement, a bank may treat any group of matching transactions as a single transaction with a notional principal amount equal to the net receipts at the common maturity date of that group of transactions.

3. For the purposes of calculating the GCCE for calculating NGR, a bank may treat any group of matching transactions as a single transaction and calculate the mark-to-market replacement cost of the group as the net sum of the individual mark-to-market replacement costs (**MTM**$_i$) of the transactions in the group.

4. In this section, two or more transactions are matching if they–

   a. are forward foreign exchange contracts, or other similar contracts, in which notional principal is equivalent to the cashflow on the contract; and

   b. mature on the same date; and

   c. are denominated in the same currency.

Guidance: The effect of this treatment is that any group of matching transactions is treated on a netted basis, including in the calculation of the total gross exposure numbers. The reason for allowing this approach for matching transactions is that offsetting contracts in the same currency maturing on the same date will have lower potential future exposure as well as lower current exposure.

E4 CEA for SFTs

E4.1 Calculation of CEA for SFTs

1. A bank must calculate the **CEA** of the **CCR** arising from a single **SFT** using either the comprehensive approach to recognition of collateral set out in sections B2.2 to B2.7 of

SUPERSEDED

BPR132 or the simple approach set out in section B3.2 of BPR132, subject to the minimum requirements specified in that document.

Guidance: Under BPR132, the simple approach is not available for an **IRB bank**. The simple approach is only available for a non-accredited bank that holds the **SFT** in its banking book and has elected to apply the simple approach to all of its collateralised banking book exposures.

2. A bank may calculate the **CEA** of a number of **SFTs** covered by a master netting agreement with a given counterparty using the approach in section B2.9 of BPR132, provided that the conditions in section B2.8 of that document are satisfied.

Guidance: The simple approach for collateral is not available for calculating the **CEA** of **SFTs** covered by a master netting agreement.

3. A bank must calculate the **CEA** using the methodology in Part D and apply a **CCF** of 100% if–

   a. the bank lends securities under an **SFT**; and

   b. either–

      i. the conditions for recognition of collateral are not satisfied; or

      ii. the transaction is not collateralised.

SUPERSEDED

Part F: Credit Valuation Adjustment (CVA) capital charge

F1 Overview

F1.1 Introduction

1. This Part sets out how a bank must calculate the **Credit Valuation Adjustment** (**CVA**) capital charge on its **derivatives** that are settled bilaterally.

> Guidance: The **CVA** charge covers the risk of mark-to-market losses on the expected counterparty credit exposures arising from the bank's **derivatives**. This is in addition to the capital requirements for the risk of default of any counterparty with which the bank has a **derivative** contract, which are calculated using the **CEA** amounts defined in Part E. The **CVA** charge is a single number calculated from the **CEAs** of the counterparty credit exposure to each of the bank's **derivative** counterparties.

2. A bank must use the methodology in subpart F2 to calculate the **CVA** capital charge across all of its **derivatives**, whether exchange-traded or over-the-counter, except those referred to in subsection (3).

3. The **CVA** capital charge does not apply to **derivatives** settled by means of a **QCCP**, as defined in section G1.2, except in the following situations (which are provided for in Part G):

   a. the bank is a client of a **QCCP** clearing member that enables it to settle a trade across the **QCCP**, and the situation described in subsection G2.2(5) exists, in which case the bank must treat the trade as a bilateral trade with the clearing member; or

   b. the bank is a clearing member of the **QCCP** and enables a client to settle a trade across the **QCCP**, in which case the bank must treat its exposure to the client as a bilateral trade, as provided for in section G2.3.

4. The **CVA** capital charge does not apply to **SFTs** unless the Reserve Bank determines that the loss exposures from **SFTs** are such that it does apply.

5. The **CVA** capital charge applies to a bank whether it is using the standardised approach for **credit risk RWAs** or is approved to use the **IRB approach** and, in each case, the calculations that the bank must use are the same.

6. The bank must add an amount 12.5 x (**CVA** capital charge) to **RWAs**.

SUPERSEDED

F2 Calculation of CVA capital charge

F2.1 CVA capital charge calculation: general case

1. The **CVA** capital charge must be calculated in accordance with the following formula:

$$K = 2.33 \times \sqrt{\left(\sum_i 0.5 w_i \left(M_i D_i CEA_i^{total} - M_i^{hedge} D_i^{hedge} B_i\right) - \sum_j w_j^{ind} M_j^{ind} D_j^{ind} B_j^{ind}\right)^2 + \sum_i 0.75 w_i^2 \left(M_i D_i CEA_i^{total} - M_i^{hedge} D_i^{hedge} B_i\right)^2}$$

where–

i is an index running through all the bank's counterparties on **derivatives** included in the **CVA** charge

w_i is the capital risk weight applicable to counterparty "i". Counterparty "i" must be mapped to one of the six capital risk weights specified in Table F2.4. The weights reflect a counterparty's external credit rating. If a counterparty does not have an external rating, the bank–

a. must, if it uses the standardised approach, use the level 4 rating; or

b. may, if it is accredited to use an **IRB** model to determine an internal rating for the counterparty, either use the level 4 rating, or, subject to the Reserve Bank's approval, map the internal rating of the counterparty to another external rating

CEA_i^{total} is the total **CEA** of exposure to **CCR** arising on **derivatives** with counterparty "i", summed across all netting sets and taking account of collateral. It is calculated in accordance with Part E

B_i is the notional value of eligible purchased single name **credit default swap** (**CDS**) hedges referencing counterparty i (summed if more than one position) and used to hedge **CVA** risk

j is an index running through one or more index **CDSs** that the bank has purchased to hedge **CVA** risk

B_j^{ind} is the full notional value of eligible index **CDS** "j"

w_j^{ind} is the capital risk weight for index hedge "j". The bank must map each index hedge to one of the six capital risk weights in Table F2.4 based on its average spread

M_i is the weighted average of the maturities of all transactions with counterparty 'i' that are included in the calculation, using the notional amount of each transaction as the weight for that transaction

M_i^{hedge} is the maturity of the hedge instrument with notional value Bi (the quantities M_i^{hedge} x B_i are to be summed if these are several positions)

M_j^{ind} is the maturity of index hedge "j"

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Guidance: To avoid doubt, in determining the maturities M_i, M_i^{hedge} and M_j^{ind} above, no one-year floor or five-year cap applies. This is different from the definition of M for the purpose of calculating risk weights for the **IRB** corporate, **sovereign**, and bank exposures class (see subpart C6 of BPR133).

2. In the formula in subsection (1), the discount factors "D" are defined as follows:

$$\boldsymbol{D_i} = \frac{1 - e^{-0.05M_i}}{0.05M_i}$$

$$\boldsymbol{D_j^{ind}} = \frac{1 - e^{-0.05M_j^{ind}}}{0.05M_j^{ind}}$$

$$\boldsymbol{D_i^{hedge}} = \frac{1 - e^{-0.05M_i^{hedge}}}{0.05M_i^{hedge}}$$

3. The benefit of a hedge may only be reflected in the calculation of the **CVA** capital charge set out in subsection (1) if it meets the eligibility conditions in section F2.5.

F2.2 CVA capital charge calculation: no eligible hedges

If a bank has exposures from **derivatives** with more than one counterparty but does not use **CVA** hedges that are eligible under section F2.5, it may calculate the **CVA** risk charge in the following way:

$$K = 2.33 \times \sqrt{0.25\left(\sum_i w_i M_i D_i CEA_i^{total}\right)^2 + 0.75\sum_i \left(w_i M_i D_i CEA_i^{total}\right)^2}$$

where all notations have the same meaning as in section F2.1.

Guidance: This formula is derived from the formula in section F2.1 by setting all the hedge values (B_i and B_j^{ind}) to zero.

F2.3 CVA capital charge calculation: no eligible hedges, only one counterparty

1. If a bank has exposures from **derivatives** with only one counterparty and does not use **CVA** hedges in accordance with section F2.5, it may calculate the **CVA** capital charge using the following formula:

K = 2.33*w*M*D*CEA

where–

w is the capital risk weight applicable to the counterparty in accordance with Table F2.4.

M is the weighted average of the maturities of all transactions with the counterparty, using the notional amount of each transaction as the weight for that transaction.

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Guidance: To avoid doubt, in determining the maturity "**M**", no one year floor or five year cap applies.

CEA is the total **CEA** of exposure to CCR arising on **derivatives** with the counterparty, taking account of collateral. It is calculated in accordance with Part E.

2. In the formula in subsection (1), the discount factor "D" is defined as follows:

$$\boldsymbol{D} = \frac{1 - e^{-0.05M}}{0.05M}$$

Guidance: The formula in subsection F2.3(1) is derived from the formula in section F2.2 when the index number 'i' only takes the value 1.

F2.4 CVA capital charge: risk weights

When calculating the **CVA** capital charge, a bank must use the capital risk weights specified in column 2 of Table F2.4, based on the rating grade of a counterparty or an index hedge specified in column 1 of Table F2.4.

Guidance: The relevant rating grade is the long-term rating grade determined in accordance with the Table B2.3.

Table F2.4

Capital risk weights

Rating grade	Capital risk weighting, w
1	0.7%
2	0.8%
3	1.0%
4 (or unrated)	2.0%
5	3.0%
6	10.0%

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F2.5 CVA capital charge: conditions on hedges

1. Subject to the requirements of this section, a bank may include eligible **CVA** hedges in the calculation of the **CVA** charge, as provided for in the formula in subsection F2.1(1).

2. To qualify as eligible, the hedge must–

   a. be transacted with an external counterparty, used for the purpose of mitigating **CVA** risk, and be managed as such; and

   b. be one of the following:

i. a single-name **CDS** (including a **sovereign CDS**); or

ii. a single-name contingent **CDS**; or

iii. an equivalent hedging instrument referencing the counterparty directly; or

iv. an index **CDS**.

3. A tranched or nth-to-default **CDS**, or an instrument for which the associated payment depends on cross-default, is not eligible as a **CVA** hedge.

4. A hedge that is included in the **CVA** capital charge calculation must not be included in the calculation of the bank's market risk capital requirement (as provided in BPR140). A hedge that is not eligible as a **CVA** hedge or is for another purpose is subject to any applicable regulatory capital requirements provided in the rest of the capital adequacy framework.

5. If the bank uses an index **CDS** to hedge **CCR** and has a counterparty that is a constituent of the reference index for the **CDS**, the bank may, with the Reserve Bank's approval, subtract the notional amount attributable to that single name (in accordance with its reference weight) from the index **CDS** notional amount (B_j^{ind}), and treat that notional amount as a single name eligible hedge (B_i) of the individual counterparty, with maturity based on the maturity of the index.

SUPERSEDED

Part G: Central counterparties (CCPs)

G1 Introduction

G1.1 Exposures arising from trades settled via CCPs

1. This Part sets out the risk-weighting treatment for **CCR** exposures arising from **derivative** transactions and **SFTs** settled via a central counterparty (**CCP**).

2. This treatment–

   a. varies depending whether the **CCP** is qualifying or non-qualifying, as defined in section G1.2; and

   b. applies equally to banks using the standardised approach to **credit risk** and to those banks accredited to use the **IRB approach** to **credit risk**; and

   c. applies equally to **derivatives** that are entered into bilaterally (**OTC derivatives**) and exchange-traded **derivatives**.

G1.2 Meaning of qualifying central counterparty (QCCP)

1. A **qualifying central counterparty** (**QCCP**) is:

   a. A **CCP** that is a designated Financial Market Infrastructure under the Financial Market Infrastructures Act 2021; or

   b. Any other **CCP** determined by the Reserve Bank as complying with the **CPMI**/**IOSCO** Principles for Financial Market Infrastructures.

2. Whether a **CCP** meets those principles is determined by the Reserve Bank.

> Guidance: Where the **CCP** is from a jurisdiction in which the regulator applies the **CPMI**/**IOSCO** principles and determines that the **CCP** complies with those principles, the Reserve Bank will in general consider that the **CCP** is a **QCCP**. However, the Reserve Bank reserves the right to decide otherwise and may require a bank to hold additional capital against its exposures to a **QCCP** if there are material shortcomings in the regulation of that **QCCP**. A **CCP** located in a jurisdiction where the regulator does not apply the **CPMI**/**IOSCO** principles will be treated as non-qualifying unless determined otherwise by the Reserve Bank.

G2 QCCP capital requirements

G2.1 Bank is QCCP clearing member acting on own behalf

1. If a bank is a clearing member of a **QCCP**, it must hold capital for all of its trade exposures to the **QCCP** that arise from the bank acting for its own purposes, and for its exposure to the **QCCP's** default fund.

2. The bank must calculate the **RWA** for its total exposure to a **QCCP** arising in the situation in subsection (1) as follows:

$$Min\{(2\% \times TE + 1250\% \times DF), (20\% \times TE)\}$$

SUPERSEDED

where–

TE is the total of the bank's trade exposures to the **QCCP**, where the value of each trade exposure must be calculated using the method for calculating the **CEA** of **derivatives** and **SFTs**, as set out in Part E.

DF is the bank's pre-funded contribution to the **QCCP's** default fund.

Guidance: The trade exposure definition means that TE does not include the value of any collateral that the bank has posted in connection with the trade. The capital requirements for posted collateral are dealt with separately in section G2.4. If the bank holds any collateral against the trade exposure, that may be recognised in the calculation of TE, as provided for in Part E.

3. Where a default fund is shared between products or types of business that give rise to settlement risk only, and products or types of business that give rise to **CCR**, all of the bank's contribution to the default fund must be incorporated in **RWAs** in accordance with the formula in subsection (2), without apportioning the contribution to different classes or types of business or products.

Guidance: Products with settlement risk only include, for example, equities and bonds. Products that give rise to **CCR** are limited to **OTC derivatives**, exchange-traded **derivatives**, and **SFTs**.

4. However, where the default fund contributions from clearing members are segregated by product type and only accessible for specific product types, the capital requirements for those default fund exposures determined according to the formula in subsection (2) must be calculated for each specific product type giving rise to **CCR**.

G2.2 Bank is client of QCCP clearing member

1. This section sets out the risk-weight calculation a bank must use for its **CCR** exposure when it is a client of a clearing member of a **QCCP** and it clears a contract through the **QCCP**, where either–

   a. the bank clears the contract indirectly, with the clearing member acting as a financial intermediary (that is, the clearing member completes an offsetting transaction with the **QCCP**); or

   b. the bank enters a transaction directly with the **QCCP** and the clearing member guarantees the bank's performance.

2. If the conditions set out in subsection (3) are met, the bank must calculate the **RWA** for the credit exposure arising in the case set out in subsection (1) as follows:

$$\textbf{RWA} = 2\% * TE$$

where–

TE is the bank's trade exposure to the clearing member, calculated using the method for calculating the **CEA** of **derivatives** and **SFTs** set out in Part E.

SUPERSEDED

Guidance: This risk-weighting treatment is the same as for the clearing member's own exposures to the **QCCP**, except that the client does not have credit exposure arising from a contribution to the default fund, "DF". As in the clearing member case, posted collateral is treated separately under section G2.4.

3. The conditions are as follows:

   a. the offsetting transactions are identified by the **QCCP** as client transactions; and the collateral to support those transactions is held by the **QCCP**, the clearing member, or both, under arrangements that prevents any losses to the bank due to–

      i. the default or insolvency of the clearing member; or

      ii. the default or insolvency of any of the clearing member's other clients; or

      iii. the joint default or insolvency of the clearing member and any of its clients; and

   b. the bank must have conducted a sufficient legal review (and undertake such further review as necessary to ensure continuing enforceability) and have a well-founded basis to conclude that, in the event of legal challenge, the relevant courts and administrative authorities would find that the arrangements referred to in paragraph (a) would be legal, valid, binding and enforceable under relevant law, including the law of the jurisdictions of the following:

      i. the bank, the clearing member **bank**, and the **QCCP**; and

      ii. any foreign branches of the bank, clearing member, or **QCCP** involved in the trade; and

      iii. the law that governs the individual transactions and collateral; and

      iv. the law that governs any contract or agreement necessary to meet this condition; and

   c. the relevant laws, regulations, rules, contractual, or administrative arrangements provide that the offsetting transactions with the defaulted or insolvent clearing member are highly likely to continue to be indirectly transacted through the **QCCP**, or by the **QCCP**, should the clearing member default or become insolvent. In such circumstances, the bank's positions and collateral with the **QCCP** will be transferred at market value unless the bank requests to close out the position at market value.

Guidance: Each bank is responsible for assessing and deciding what legal basis would be required by the relevant courts and administrative authorities in all the relevant jurisdictions in the event of a legal challenge on their claim to their clearing intermediary and/or QCCP. To ensure continuing enforceability, further review may be required, for example any time when contracts change or relevant laws or other requirements change in the relevant jurisdictions. If a bank has any

SUPERSEDED

doubt on legal certainty of their arrangements, the bank should not apply the risk weight specified in the subsection (2).

4. Where a bank is not protected from losses in the case that the clearing member and another client of the clearing member jointly default or become jointly insolvent, but all other conditions in subsection (3) are met, the bank must calculate the **RWA** for the situation set out in subsection (1) as follows:

$$\textbf{RWA} = 4\% * TE$$

where TE is the bank's trade exposure to the clearing member.

5. If neither the conditions in subsection (3) nor the conditions in subsection (4) are met, the bank must calculate the **RWA** for an exposure arising in the case set out in subsection (1) as if it were a bilateral trade with the clearing member.

Guidance: Subsection (5) means that a **standardised bank** must calculate the **RWA** by multiplying the **CEA** (as determined under Part E) by the risk weight for the clearing member. A bank using the **IRB approach** for the exposure must add the **CEA** to the total **EAD** in the **RWA** calculation for its exposure to the clearing member. In each case, the **CEA** must also be included in the **CVA** calculation in Part F, as applicable.

G2.3 Bank is QCCP clearing member acting for client

1. This section sets out the capital requirements that apply when the bank is a clearing member of a **QCCP** and enables a client to carry out a trade involving the **QCCP** by either–

   a. acting as intermediary between the client and the **QCCP**; or

   b. guaranteeing the client's trade.

2. The bank must calculate an **RWA** for its counterparty credit exposure to the client using the same approach as for a bilateral trade with the client, except that the bank must multiply the **CEA** of the exposure (calculated in accordance with Part E) by the scalar specified in subsection (3).

3. The scalar is 71%, to recognise the shorter close-out period for cleared transactions.

Guidance: This means that where the bank is using the standardised approach for calculating the **RWA** for the client, the **RWA** is the **CEA** calculated in accordance with Part E, multiplied by the scalar, and then multiplied by the applicable risk-weight for the client from Part C.

Where the bank is using the **IRB approach** for calculating the **RWA** for the client, it must calculate the **RWA** using its accredited **IRB** model and the methodology in BPR133 applicable to the exposure class of the client, with **EAD**

SUPERSEDED

for the calculation being the **CEA** calculated in accordance with Part E and then multiplied by the scalar.

4. The bank must reflect its exposure to the client in its **CVA** capital charge, by including the **CEA** of the exposure (calculated in accordance with Part E) in the applicable formula for calculating the **CVA** capital charge in Part F.

Guidance: Inclusion in the **CVA** calculation is consistent with the exposure being treated as a bilateral trade. For the purpose of the **CVA** calculation, **CEA** is not multiplied by the scalar defined in subsection (3).

G2.4 Treatment of posted collateral

1. This section applies to a bank–
   a. that is either –
      i. a clearing member of a **QCCP**; or
      ii. a client of a clearing member of a **QCCP**; and
   b. has posted assets as collateral (including cash, securities, other pledged assets, and excess initial or variation margin, also called overcollateralisation) in relation to trades carried out across the **QCCP**.
2. A bank to which this section applies must–
   a. in all cases, calculate **RWAs** for the **credit risk** on those assets in accordance with the bank's required capital adequacy treatment of those assets; and
   b. calculate **RWAs** to reflect the risk of default of the entity holding the collateral, in accordance with subsections (3) to (5).
3. If the bank is a clearing member of a **QCCP** and posts collateral in relation to a trade carried out across the **QCCP**, for the purpose of subsection (2)(b)–
   a. the bank may apply a zero risk-weight to all posted collateral that is held by a custodian and is bankruptcy-remote from the **QCCP**; and
   b. the bank must apply a 2% risk-weight to all posted collateral that is held by the **QCCP** and is not bankruptcy-remote from the **QCCP**.
4. If the bank is a client of a clearing member of a **QCCP** and the conditions in one of subsections (a) to (c) are met, it must calculate **RWAs** for the purpose of subsection (2)(b) by multiplying the value of the posted collateral by the risk weight specified in whichever of subsections (a), (b), or (c) applies:
   a. 0%, if the collateral is held by a custodian, and is bankruptcy-remote from the **QCCP**, the clearing member and the clearing member's other clients; or
   b. 2%, if the collateral is held by the **QCCP** on behalf of the client and is not bankruptcy-remote from the **QCCP**, and all of the conditions in subsection G2.2(3) are met; or

SUPERSEDED

c. 4%, if the collateral is held by the **QCCP** on behalf of the client and is not bankruptcy-remote from the **QCCP**, and the conditions in subsection G2.2(4) are met.

Guidance: This means that the conditions for a 2% or 4% risk-weight for the **CCR** on collateral posted by a client mirror the conditions for a 2% or 4% risk-weight of the client's trade exposures under section G2.2.

5. If the bank is a client of a clearing member of a **QCCP** and none of the conditions in subsections (4)(a) to (c) are met, the bank must calculate the **RWA** for the purpose of subsection (2)(b) by including the value of the posted collateral in its risk-weighting approach applicable to the entity holding the collateral.

Guidance: This means that when the standardised approach applies, the bank must calculate the **RWA** as the value of the collateral multiplied by the applicable risk-weight from Part C for the entity holding the collateral. When the **IRB approach** applies, the bank must calculate the **RWA** using its **IRB** model and the BPR133 methodology applicable to the exposure class of the entity holding the collateral, with **EAD** being the value of the collateral.

G3 Non-qualifying CCP capital requirements

G3.1 Requirements for exposures to non-qualifying CCPs

1. A trade exposure to a non-qualifying **CCP** must be treated as a bilateral trade exposure.

2. A bank, whether using the standardised or **IRB approach**, must, for the purposes of subsection (1), calculate the **RWA** for the counterparty default risk by multiplying the standardised risk weight for the **CCP**, determined in accordance with Part C, by the **CEA** of the trade exposure, determined in accordance with Part E.

3. The **CEA** of the trade exposure must also be included in the **CVA** capital charge in accordance with Part F, provided the trade falls within the **CVA** scope specified in section F1.1.

4. If a bank is a clearing member of a non-qualifying **CCP** and is exposed to the **CCP's** default fund, the bank must apply a risk weight of 1250% to that exposure in the following way:

$$\mathbf{RWA} = 1250\% \times DF$$

Where

RWA is the risk weighted assets from the default fund exposure

DF is the bank's contribution to the **CCP's** default fund, determined in accordance with subsection (5).

5. DF must be calculated as the sum of–

   a. the full amount of the bank's pre-funded contribution to the **CCP's** default fund; and

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b. if there is an unfunded contribution, an additional amount to be determined by the Reserve Bank.

6. In subsection (5), **unfunded contribution** means a situation in which the bank has a binding commitment to make additional contributions if the **CCP** requires.

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