Regulation (EU) No 575/2013 of the European Parliament and of the Council of 26 June 2013 on prudential requirements for credit institutions and investment firms and amending Regulation (EU) No 648/2012 (Text with EEA relevance)

[X1 PART THREE

CAPITAL REQUIREMENTS

TITLE II

CAPITAL REQUIREMENTS FOR CREDIT RISK

CHAPTER 6

Counterparty credit risk

[X1 Section 1

Definitions

Article 271

Determination of the exposure value

1 An institution shall determine the exposure value of derivative instruments listed in Annex II in accordance with this Chapter.

2 An institution may determine the exposure value of repurchase transactions, securities or commodities lending or borrowing transactions, long settlement transactions and margin lending transactions in accordance with this Chapter instead of making use of Chapter 4.

Article 272

Definitions

For the purposes of this Chapter and of Title VI of this Part, the following definitions shall apply:

General terms

(1) ‘counterparty credit risk’ or ‘CCR’ means the risk that the counterparty to a transaction could default before the final settlement of the transaction's cash flows;

Transaction types

(2) ‘long settlement transactions’ means transactions where a counterparty undertakes to deliver a security, a commodity, or a foreign exchange amount against cash, other financial instruments, or commodities, or vice versa, at a

settlement or delivery date specified by contract that is later than the market standard for this particular type of transaction or five business days after the date on which the institution enters into the transaction, whichever is earlier;

(3) 'margin lending transactions' means transactions in which an institution extends credit in connection with the purchase, sale, carrying or trading of securities. Margin lending transactions do not include other loans that are secured by collateral in the form of securities;

Netting set, hedging sets, and related terms

(4) 'netting set' means a group of transactions between an institution and a single counterparty that is subject to a legally enforceable bilateral netting arrangement that is recognised under Section 7 and Chapter 4.

Each transaction that is not subject to a legally enforceable bilateral netting arrangement which is recognised under Section 7 shall be treated as its own netting set for the purposes of this Chapter.

Under the Internal Model Method set out in Section 6, all netting sets with a single counterparty may be treated as a single netting set if negative simulated market values of the individual netting sets are set to 0 in the estimation of expected exposure (hereinafter referred to as 'EE');

(5) 'risk position' means a risk number that is assigned to a transaction under the Standardised Method set out in Section5 following a predetermined algorithm;

(6) 'hedging set' means a group of risk positions arising from the transactions within a single netting set, where only the balance of those risk positions is used for determining the exposure value under the Standardised Method set out in Section 5;

(7) 'margin agreement' means an agreement or provisions of an agreement under which one counterparty must supply collateral to a second counterparty when an exposure of that second counterparty to the first counterparty exceeds a specified level;

(8) 'margin threshold' means the largest amount of an exposure that remains outstanding before one party has the right to call for collateral;

(9) 'margin period of risk' means the time period from the most recent exchange of collateral covering a netting set of transactions with a defaulting counterparty until the transactions are closed out and the resulting market risk is re-hedged;

(10) 'effective maturity' under the Internal Model Method for a netting set with maturity greater than one year means the ratio of the sum of expected exposure over the life of the transactions in the netting set discounted at the risk-free rate of return, divided by the sum of expected exposure over one year in the netting set discounted at the risk-free rate.

This effective maturity may be adjusted to reflect rollover risk by replacing expected exposure with effective expected exposure for forecasting horizons under one year;

(11) 'cross-product netting' means the inclusion of transactions of different product categories within the same netting set pursuant to the cross-product netting rules set out in this Chapter;

(12) 'Current Market Value' (hereinafter referred to as 'CMV') for the purposes of Section 5 refers to the net market value of the portfolio of transactions within a netting set, where both positive and negative market values are used in computing the CMV;

Distributions

(13) 'distribution of market values' means the forecast of the probability distribution of net market values of transactions within a netting set for a future date (the forecasting horizon), given the realised market value of those transactions at the date of the forecast;

(14) 'distribution of exposures' means the forecast of the probability distribution of market values that is generated by setting forecast instances of negative net market values equal to zero;

(15) 'risk-neutral distribution' means a distribution of market values or exposures over a future time period where the distribution is calculated using market implied values such as implied volatilities;

(16) 'actual distribution' means a distribution of market values or exposures at a future time period where the distribution is calculated using historic or realised values such as volatilities calculated using past price or rate changes;

Exposure measures and adjustments

(17) 'current exposure' means the larger of zero and the market value of a transaction or portfolio of transactions within a netting set with a counterparty that would be lost upon the default of the counterparty, assuming no recovery on the value of those transactions in insolvency or liquidation;

(18) 'peak exposure' means a high percentile of the distribution of exposures at particular future date before the maturity date of the longest transaction in the netting set;

(19) 'expected exposure' (hereinafter referred to as 'EE') means the average of the distribution of exposures at a particular future date before the longest maturity transaction in the netting set matures;

(20) 'effective expected exposure at a specific date' (hereinafter referred to as 'Effective EE') means the maximum expected exposure that occurs at that date or any prior date. Alternatively, it may be defined for a specific date as the greater of the expected exposure at that date or the effective expected exposure at any prior date;

(21) 'expected positive exposure' (hereinafter referred to as 'EPE') means the weighted average over time of expected exposures, where the weights are the proportion of the entire time period that an individual expected exposure represents.

When calculating the own funds requirement, institutions shall take the average over the first year or, if all the contracts within the netting set mature within less than one year, over the time period until the contract with the longest maturity in the netting set has matured;

(22) ‘effective expected positive exposure’ (hereinafter referred to as ‘Effective EPE’) means the weighted average of effective expected exposure over the first year of a netting set or, if all the contracts within the netting set mature within less than one year, over the time period of the longest maturity contract in the netting set, where the weights are the proportion of the entire time period that an individual expected exposure represents;

CCR related risks

(23) ‘rollover risk’ means the amount by which EPE is understated when future transactions with a counterparty are expected to be conducted on an ongoing basis.

The additional exposure generated by those future transactions is not included in calculation of EPE;

(24) ‘counterparty’ for the purposes of Section 7 means any legal or natural person that enters into a netting agreement, and has the contractual capacity to do so;

(25) ‘contractual cross product netting agreement’ means a bilateral contractual agreement between an institution and a counterparty which creates a single legal obligation (based on netting of covered transactions) covering all bilateral master agreements and transactions belonging to different product categories that are included within the agreement;

For the purposes of this definition, ‘different product categories’ means:

(a) repurchase transactions, securities and commodities lending and borrowing transactions;

(b) margin lending transactions;

(c) the contracts listed in Annex II;

(26) ‘payment leg’ means the payment agreed in an OTC derivative transaction with a linear risk profile which stipulates the exchange of a financial instrument for a payment.

In the case of transactions that stipulate the exchange of payment against payment, those two payment legs shall consist of the contractually agreed gross payments, including the notional amount of the transaction.**]**

Editorial Information

X1 Substituted by Corrigendum to Regulation (EU) No 575/2013 of the European Parliament and of the Council of 26 June 2013 on prudential requirements for credit institutions and investment firms and amending Regulation (EU) No 648/2012 (OJ L 176, 27.6.2013, p. 1).