<u>**Completion Instructions**</u>

**Return of Capital Adequacy Ratio
Part IIId – Risk-weighted Amount for Credit Risk
(Securitization Exposures)
<u>Form MA(BS)3(IIId)</u>**

<u>**Introduction**</u>

1. Form MA(BS)3(IIId) of Part III should be completed by each authorized institution ("AI") incorporated in Hong Kong that has ***securitization exposures***[1] booked in its ***banking book***.

2. This Form contains the following Divisions:

    (a) Division A is a summary table showing the total ***risk-weighted amounts*** ("RWAs") of the securitization exposures of a reporting AI and the capital deduction required in respect of its ***securitization transactions*** or securitization exposures;

    (b) Division B captures securitization exposures (other than ***re-securitization exposures***) that are subject to the ***securitization internal ratings-based approach*** (***SEC-IRBA***);

    (c) Division C1 captures securitization exposures (other than re-securitization exposures) that are subject to the ***securitization external ratings-based approach*** (***SEC-ERBA***) where the risk-weights are determined based on—

        (i) ***long-term ECAI issue specific ratings*** or ***long-term inferred ratings***; or

        (ii) (if the reporting AI has an ***IAA approval*** to use the ***internal assessment approach*** (***IAA***)) ***internal credit ratings*** mapped to equivalent long-term ECAI issue specific ratings;

    (d) Division C2 captures securitization exposures (other than re-securitization exposures) that are subject to the SEC-ERBA where the risk-weights are determined based on—

        (i) ***short-term ECAI issue specific ratings*** or ***short-term inferred ratings***; or

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[1] For example, asset-backed securities, mortgage-backed securities, credit enhancements, liquidity facilities, interest rate or currency swaps, credit derivative contracts, tranched credit protection, and reserve accounts, such as cash collateral accounts, recorded as an asset by the originating institution.

(ii) (if the reporting AI has an IAA approval to use the IAA) internal credit ratings mapped to equivalent short-term ECAI issue specific ratings;

(e) Division D1 captures securitization exposures (other than re-securitization exposures) that are subject to the **securitization standardized approach** (**SEC-SA**);

(f) Division D2 captures re-securitization exposures that are subject to the SEC-SA; and

(g) Division E captures securitization exposures (including re-securitization exposures) that are subject to the **securitization fall-back approach** (**SEC-FBA**).

3. In each of Divisions B, D1, D2 and E, <u>columns (1) to (3)</u> are for reporting of on-balance sheet securitization exposures while <u>columns (4) to (7)</u> are for reporting of off-balance sheet securitization exposures. In Divisions C1 and C2, on-balance sheet securitization exposures and off-balance sheet securitization exposures must be reported in <u>columns (1) to (3a)</u> and <u>columns (4) to (7a)</u> respectively. <u>Columns (3a) and (7a)</u> are subsets of <u>columns (3) and (7)</u>.

4. This Form and its completion instructions should be read in conjunction with the Banking (Capital) Rules ("BCR") and the relevant supervisory policy/guidance related to the capital adequacy framework (in particular, the SPM module CR-G-12 "Credit Risk Transfer Activities" (to the extent related to credit assessments and significant credit risk transfer) and the Q&As on the securitization framework).

<u>Section A: Definitions and General Instructions</u>

In this Form—

5. "Exposure Amount before CRM" means the **exposure amount** of a securitization exposure before taking into account any **Part 7 credit risk mitigation** ("Part 7 CRM") obtained for the exposure, but net of any amounts that are permitted to be deducted from the exposure amount (e.g. **specific provisions**, write-offs and non-refundable purchase price discounts) under section 236(3) of the BCR.

6. "Principal Amount" of an off-balance sheet exposure has the meaning given by paragraph (b) of the definition of **principal amount** in section 227(1) of the BCR. However, if the off-balance sheet exposure concerned is a **default risk exposure** arising from a **derivative contract**, "Principal Amount" means the nominal **notional amount** of the contract, which should not be confused with any effective notional amount or adjusted notional calculated for the contract under Part 6A of the BCR.

7. "Senior exposures" means securitization exposures in **senior tranches** (See **<u>Annex IIId-A</u>** for more information on the determination of seniority).

8. "Non-senior exposures" means securitization exposures in **non-senior tranches**.

9.   "Senior long-term securitization exposures" means senior exposures that have a long-term ECAI issue specific rating or a long-term inferred rating.

10.   "Non-senior long-term securitization exposures" means non-senior exposures that have a long-term ECAI issue specific rating or a long-term inferred rating.

11.   "Senior short-term securitization exposures" means senior exposures that have a short-term ECAI issue specific rating or a short-term inferred rating.

12.   "Non-senior short-term securitization exposures" means non-senior exposures that have a short-term ECAI issue specific rating or a short-term inferred rating.

13.   "Risk-weight" means—

(a)   in the case of a securitization exposure (other than a re-securitization exposure)—the risk-weight applicable to the exposure determined by using the SEC-IRBA, SEC-ERBA, SEC-SA or SEC-FBA—

(i)   after taking into account the risk-weight floor of 15% (see section 240(1) of the BCR) and, if applicable, the risk-weight floor set out in section 240(3) or (4) and the risk-weight cap for senior tranches (see section 241 of the BCR); and

(ii)   without taking into account any Part 7 CRM;

(b)   in the case of a re-securitization exposure—the risk-weight applicable to the exposure determined by using the SEC-SA or SEC-FBA—

(i)   after taking into account the risk-weight floor of 100% (see section 240(2) of the BCR) and if applicable, the risk-weight floor set out in section 240(4) of the BCR; and

(ii)   without taking into account any Part 7 CRM;

(c)   in the case of Part 7 CRM obtained for a securitization exposure—the risk-weight applicable to—

(i)   the *recognized collateral* concerned determined in accordance with Part 4, 6 or 7 and in compliance with Division 5 of Part 7 of the BCR; or

(ii)   the *credit protection provider* of the *recognized guarantee* or *recognized credit derivative contract* concerned, as the case may be, determined in accordance with Part 4 or 6 and in compliance with Division 5 of Part 7 of the BCR;

(d)   in the case of assets held by a *special purpose entity* (*SPE*) in an *eligible synthetic securitization transaction* described in section 230(2A) of the BCR—the weighted-average risk-weight of the assets determined in accordance with Part 4 of the BCR.

A.1 Reporting of underlying exposures of securitization transaction where reporting AI is *originating institution*

14. The AI must report the ***underlying exposures*** of a ***non-eligible securitization transaction*** as follows—

    (a) report the underlying exposures in Form MA(BS)3(IIIa), Form MA(BS)3(IIIb) or Form MA(BS)3(IIIc) (if the underlying exposures are non-securitization exposures) or this Form (if the underlying exposures are securitization exposures), as if the underlying exposures had not been securitized; and

    (b) if the transaction is a ***synthetic securitization transaction***, the underlying exposures must be reported <u>without</u> taking into account the effect of any credit risk mitigation ("CRM") used for transferring the credit risk of the underlying exposures to other parties to the transaction.

15. If the AI has served a notice to the HKMA under section 230(3) of the BCR for applying the treatment set out in section 230(1), (2) or (2A) of the BCR to the underlying exposures of an ***eligible securitization transaction***—

    (a) in the case where the transaction is a ***traditional securitization transaction***, the AI is not required to report the underlying exposures in any of Form MA(BS)3(IIIa), Form MA(BS)3(IIIb), Form MA(BS)3(IIIc) and this Form;

    (b) in the case where the transaction is a synthetic securitization transaction—

        (i) subject to subparagraph (ii), the AI must report the underlying exposures and the effect of the CRM used for transferring the credit risk of the underlying exposures in Form MA(BS)3(IIIa), Form MA(BS)3(IIIb) or Form MA(BS)3(IIIc) (if the underlying exposures are non-securitization exposures) or this Form (if the underlying exposures are securitization exposures);

        (ii) if ***tranched credit protection*** is obtained by the AI for the underlying exposures, the AI must report the underlying exposures and the effect of the CRM used for transferring the credit risk of the underlying exposures in this Form in accordance with paragraphs 16, 17, 34 and 35 below.

A.2 Decomposition of exposures covered by tranched credit protection

16. Subject to paragraph 17, if a securitization exposure or non-securitization exposure is covered by tranched credit protection ("protected exposure"), no matter whether the protection is provided or obtained by the reporting AI, the protected exposure must be decomposed[2] into a protected sub-tranche and an unprotected sub-tranche. The sub-tranches resulted from decomposing a non-

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[2] The sub-tranches resulted from the decomposition are not considered as re-securitization exposures for capital adequacy purposes.

securitization exposure must be treated as securitization exposures for the purposes of calculating their RWAs.

17. When decomposing an exposure for which the AI has obtained tranched credit protection, the decomposition must take into account—

(a) if there is a *maturity mismatch*—the adjustment to the value of the credit protection required under section 246 of the BCR; and

(b) if the tranched credit protection is in the form of recognized collateral and the reporting AI uses the *comprehensive approach* or Formula 19 in Part 6 of the BCR to take into account the credit risk mitigation effect ("CRM effect") of the collateral—the adjustment to the value of the credit protection resulted from any applicable *standard supervisory haircuts* applied to the collateral.

A.3 Reporting of derivative contracts entered into under securitization transactions

18. If a reporting AI's securitization exposure is a default risk exposure arising from a derivative contract and the risk-weight of the exposure is determined by using the SEC-IRBA, SEC-ERBA, SEC-SA or SEC-FBA, the default risk exposure must be reported in this Form.

A.4 Reporting of eligible ABCP exposures risk-weighted by using the IAA

19. A reporting AI with an IAA approval to risk-weight *eligible ABCP exposures* by using the IAA must include the eligible ABCP exposures in the amounts reported in columns (1) to (3) and (4) to (7) of Divisions C1 and C2, and the RWAs of the eligible ABCP exposures must also be reported separately in columns (3a) and (7a) of those Divisions.

A.5 Treatment of default risk and *dilution risk* in respect of purchased receivables under SEC-IRBA

20. For cases where the default and dilution risks are not treated in an aggregated manner, a reporting AI must determine in a prudent manner how the K_{IRB} of the entire pool of the underlying exposures concerned should be calculated in order to adequately reflect the extent to which the AI is exposed to the two risks (see section 252(3) of the BCR). Reporting AIs may refer to paragraphs 99.4 to 99.19 of Chapter CRE99 of the Basel Framework[3] for guidance.

A.6 Tranche maturity of tranche in securitization transaction

21. To avoid doubt, if a reporting AI uses Formula 24 under section 248 of the BCR to calculate the tranche maturity (M_T) of a *tranche* for the purpose of reporting in this Form the RWA of a securitization exposure in the tranche as of a particular position date, the cash flows (CF_t) used in the Formula should be those that are

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[3] https://www.bis.org/basel_framework/chapter/CRE/99.htm?inforce=20230101&published=20200327

contractually payable under the tranche from the position date to the final maturity of the tranche.

Section B: Reporting Arrangements for Division A

22. Column (1) is for reporting the total RWAs of all of a reporting AI's securitization exposures to securitization transactions and the capital deductions required in respect of securitization transactions. If the reporting AI is the originating institution of any of these securitization transactions, it must report the RWAs of its securitization exposures to, and the capital deductions in respect of, the transactions originated by it in Column (2) as a subset of the amounts reported in Column (1).

23. Items *A5(a)* and *(b)* are to be filled in by reporting AIs that are originating institutions. If a reporting AI, which is the originating institution of a securitization transaction (other than a re-securitization transaction), has, in accordance with section 242 of the BCR, taken the maximum capital charge calculated for the transaction under that section as the total capital charge of all the AI's securitization exposures to the transaction, the AI—

   (a) must report the corresponding RWA (i.e. the maximum capital charge times 12.5) in either item *A5(a)* or *(b)* based on the original approach used by the AI for risk-weighting the securitization exposures; and

   (b) must not adjust the RWAs of the securitization exposures reported in any of Divisions B to E to reconcile with the amount reported in item *A5(a)* or *(b)* (in other words, the amounts reported in any of these Divisions must be based on risk-weights without considering the maximum capital charge).

Section C: Reporting Arrangements for Divisions B to E

C.1   Securitization Exposures not covered by Part 7 CRM

24. Subject to paragraph 26, if a reporting AI has not obtained any Part 7 CRM for its securitization exposure—

   (a) the exposure amount before CRM of the exposure must be reported in column (1) or (5), as the case requires;

   (b) if the exposure is an off-balance sheet exposure, its principal amount must be reported in column (4);

   (c) the exposure amount after CRM of the exposure, which is the same amount as the exposure amount before CRM, must be reported in column (2) or (6), as the case requires;

   (d) the RWA of the exposure, which is the product of the amount reported in column (2) or (6) and the risk-weight applicable to the exposure, must be

reported in <u>column (3) or (7)</u> (and, if applicable, <u>column (3a) or (7a)</u> of Division C1 or C2), as the case requires; and

(e)   all the amounts above must be reported in the same row that corresponds to the risk-weight applicable to the exposure.

25.   The reporting arrangements in paragraph 24 also apply to cases where—

(a)   the securitization exposure is a default risk exposure calculated by using the ***SA-CCR approach*** or the ***IMM(CCR) approach***; and

(b)   the collaterals received by the reporting AI for the exposure have already been included in—

(i)   the calculation of haircut value of net collateral held under section 226BJ of the BCR when calculating the default risk exposure under the SA-CCR approach; or

(ii)   the estimation mentioned in section 226H(2)(a) of the BCR when calculating the default risk exposure under the IMM(CCR) approach.

26.   In the case of a securitization exposure arising from <u>credit protection provided by the reporting AI</u>—

(a)   <u>if the credit protection is a full or proportional credit protection provided to another securitization exposure</u> ("protected exposure")—

(i)   for the purpose of paragraphs 24(a) and 24(b), the AI must determine the amount to be reported in <u>column (1)</u> or the amounts to be reported in <u>columns (4) and (5)</u>, as the case requires, as if it directly held that portion of the protected exposure on which it has provided the credit protection; and

(ii)   for the purpose of paragraph 24(e), the risk-weight applicable to the AI's exposure is the risk-weight applicable to the protected exposure; or

(b)   <u>if the credit protection is a tranched credit protection provided to another securitization exposure or a non-securitization exposure</u> ("protected exposure")—

(i)   for the purpose of paragraphs 24(a) and 24(b), the AI must report the amount of the protected sub-tranche of the protected exposure in column (1) or in columns (4) and (5) (see paragraph 16 above on decomposition of the protected exposure); and

(ii)   for the purpose of paragraph 24(e), the risk-weight applicable to the AI's exposure is the risk-weight applicable to the protected sub-tranche determined by using the SEC-IRBA, SEC-ERBA, SEC-SA or SEC-FBA, as the case requires, and in accordance with sections 240, 241 and 249 of the BCR.

C.2 Securitization Exposures covered by Full or Proportional Credit Protection - Reporting Arrangements for Division B

27. If Part 7 CRM is obtained by a reporting AI for its securitization exposure and the exposure is risk-weighted by using the SEC-IRBA, the AI must report the exposure amount before CRM of the exposure in <u>column (1) or (5)</u> of the row corresponding to the risk-weight applicable to the exposure. If the exposure is an off-balance sheet exposure, the principal amount of the exposure must be reported in <u>column (4)</u> of the same row.

28. If the Part 7 CRM is a recognized guarantee or a recognized credit derivative contract, the AI must, after adjusting the value of the credit protection for any maturity mismatch in accordance with section 246 of the BCR—

    (a) report in the row corresponding to the risk-weight applicable to the securitization exposure and—

        (i) in <u>column (2) or (6)</u>—the uncovered portion of the exposure determined in accordance with the *substitution framework* under Part 6 of the BCR; and

        (ii) in <u>column (3) or (7)</u>—the RWA of the uncovered portion; and

    (b) report in the row corresponding to the risk-weight applicable to the credit protection provider concerned and—

        (i) in <u>column (2) or (6)</u>—the covered portion of the exposure determined in accordance with the substitution framework; and

        (ii) in <u>column (3) or (7)</u>—the RWA of the covered portion.

29. If the Part 7 CRM is recognized collateral, the AI must report—

    (a) the net credit exposure (after adjusting the value of the credit protection for any maturity mismatch in accordance with section 246 of the BCR) determined by using Formula 19 in Part 6 of the BCR in <u>column (2) or (6)</u>; and

    (b) the RWA of the net credit exposure in <u>column (3) or (7)</u>.

    All the amounts above must be reported in the same row corresponding to the risk-weight applicable to the securitization exposure.

C.3 Securitization Exposures covered by Full or Proportional Credit Protection - Reporting Arrangements for Divisions C1 to E

30. If Part 7 CRM is obtained by a reporting AI for its securitization exposure and the exposure is risk-weighted by using the SEC-ERBA, SEC-SA or SEC-FBA, the AI must report the exposure amount before CRM of the exposure in <u>column (1) or (5)</u> of the row corresponding to the risk-weight applicable to the exposure.

If the exposure is an off-balance sheet exposure, the principal amount of the exposure must be reported in column (4) of the same row.

31. Reporting of CRM effects of recognized collateral subject to the *simple approach*, recognized guarantees and recognized credit derivative contracts

   (a) If the securitization exposure is an on-balance sheet exposure, a default risk exposure or an exposure arising from the provision of unfunded credit protection, the AI must, after adjusting the value of the credit protection pursuant to Parts 4 and 7 of the BCR (e.g. section 100 for *currency mismatch* and section 246 for maturity mismatch)—

      (i) report the *credit protection uncovered portion* of the exposure in column (2) or (6) of the row corresponding to the risk-weight applicable to the securitization exposure;

      (ii) report the *credit protection covered portion* of the exposure in column (2) or (6) of the row corresponding to the risk-weight applicable to the credit protection provider or collateral concerned; and

      (iii) report—

         (A) the RWA of the credit protection uncovered portion in column (3) or (7) (and, if applicable, column (3a) or (7a) of Division C1 or C2) of the row corresponding to the risk-weight applicable to the securitization exposure; and

         (B) the RWA of the credit protection covered portion in column (3) or (7) of the row corresponding to the risk-weight applicable to the credit protection provider or collateral concerned.

   (b) If the securitization exposure is an off-balance sheet exposure other than one that falls within paragraph (a), the same reporting arrangements in paragraph (a) apply except that—

      (i) the references to "credit protection uncovered portion" in paragraphs (a)(i) and (a)(iii) must be construed to mean the product of the credit protection uncovered portion of the exposure and the factor applicable to the exposure specified in section 235(2)(c) of the BCR; and

      (ii) the references to "credit protection covered portion" in paragraphs (a)(ii) and (a)(iii) must be construed to mean the product of the credit protection covered portion of the exposure and the factor applicable to the exposure specified in section 235(2)(c) of the BCR.

32. Reporting of CRM effect of recognized collateral subject to the comprehensive approach

   (a) The net credit exposure (after adjusting the value of the credit protection for any maturity mismatch in accordance with section 246 of the BCR) calculated under section 87 or 88 of the BCR, as the case requires, must be reported in column (2) or (6).

(b) The RWA of the net credit exposure must be reported in <u>column (3) or (7)</u> (and, if applicable, <u>column (3a) or (7a)</u> of Division C1 or C2).

All the amounts above must be reported in the same row corresponding to the risk-weight applicable to the securitization exposure.

C.4 Securitization Exposure or Non-securitization Exposure covered by Tranched Credit Protection

33. Subject to paragraphs 34 and 35, if tranched credit protection is obtained by a reporting AI for a securitization exposure or non-securitization exposure—

(a) the amounts of the unprotected sub-tranche and protected sub-tranche must be reported in <u>column (1)</u> or in <u>columns (4) and (5)</u>, and in the rows corresponding to the risk-weights applicable to the sub-tranches (i.e. the risk-weights determined by using the SEC-IRBA, SEC-ERBA, SEC-SA or SEC-FBA, as the case requires, and in accordance with sections 240, 241 and 249 of the BCR);

(b) the amount of the unprotected sub-tranche must be reported in <u>column (2) or (6)</u> of the row corresponding to the risk-weight applicable to the unprotected sub-tranche;

(c) the RWA of the unprotected sub-tranche must be reported in <u>column (3) or (7)</u> (and, if applicable, <u>column (3a) or (7a)</u> of Division C1 or C2) of the row corresponding to the risk-weight applicable to the unprotected sub-tranche;

(d) in cases where the tranched credit protection is in the form of—

(i) recognized collateral subject to the simple approach;

(ii) recognized guarantee; or

(iii) recognized credit derivative contract,

the amount of the protected sub-tranche must be reported in <u>column (2) or (6)</u> and the RWA of the protected sub-tranche must be reported in <u>column (3) or (7)</u>. Both of the two amounts must be reported in the row corresponding to the risk-weight applicable to the collateral or credit protection provider concerned.

34. If—

(a) tranched credit protection is obtained by a reporting AI for securitization exposures or non-securitization exposures ("protected exposures") through a *credit-linked note* issued by the AI; and

(b) the credit derivative contract embedded in the credit-linked note is a recognized credit derivative contract[4],

subject to paragraph 17 above, the AI may only treat that amount of the protected exposures which is equivalent to the cash funding received by the AI from the credit-linked note as being fully covered and must treat that portion of the protected exposures covered by the cash funding as a protected sub-tranche collateralized by cash deposit[5]. The reporting arrangements are same as those in paragraph 33.

35.   If—

(a) a reporting AI is the originating institution of an eligible synthetic securitization transaction;

(b) tranched credit protection in the form of recognized guarantee or recognized credit derivative contract is obtained by the AI for the underlying exposures of the eligible synthetic securitization transaction;

(c) the guarantor of the recognized guarantee or the ***protection seller*** of the recognized credit derivative contract, as the case may be, is the SPE in the eligible synthetic securitization transaction;

(d) all the conditions in section 2(a) of Schedule 10 to the BCR are satisfied in respect of the SPE and its assets; and

(e) the AI has served a notice to the HKMA under section 230(3) of the BCR for applying the treatment set out in section 230(2A) of the BCR to the underlying exposures of the eligible synthetic securitization transaction,

the AI must report the underlying exposures and the CRM effect of the recognized guarantee or recognized credit derivative contract as follows—

(f) the amounts of the unprotected sub-tranche and protected sub-tranche of the underlying exposures must be reported in column (1) (and/or columns (4) and (5) if applicable) and in the rows corresponding to the risk-weights applicable to the sub-tranches (i.e. the risk-weights determined by using the SEC-IRBA, SEC-ERBA, SEC-SA or SEC-FBA, as the case requires, and in accordance with sections 240, 241 and 249 of the BCR);

(g) the amount of the unprotected sub-tranche must be reported in column (2) (and/or column (6) if applicable) of the row corresponding to the risk-weight applicable to the unprotected sub-tranche;

(h) the amount of the protected sub-tranche must be reported in column (2) (and/or column (6) if applicable) of the row corresponding to the weighted-average risk-weight of the assets held by the SPE (in other words, the

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[4] For the purpose of determining whether the credit derivative contract qualifies as a recognized credit derivative contract, the AI may consider the condition in section 99(1)(b) to be met.
[5] See section 101(8) of the BCR and paragraph 157 of the completion instructions for Form MA(BS)3 Part IIIc.

weighted-average risk-weight of the SPE's assets is treated as the risk-weight applicable to the SPE (see section 230(2B) of the BCR));

(i) the RWA of the unprotected sub-tranche must be reported in column (3) (and/or column (7) if applicable) of the row corresponding to the risk-weight applicable to the unprotected sub-tranche; and

(j) the RWA of the protected sub-tranche must be reported in column (3) (and/or column (7) if applicable) of the row corresponding to the weighted-average risk-weight of the assets held by the SPE.

Section D: Reporting of overlapping securitization exposures

36. If there is an overlapping portion in a reporting AI's securitization exposures to a securitization transaction and the overlapping is between securitization exposures booked in the banking book and the trading book of the AI, the overlapping portion that is attributed to the exposures booked in the banking book must be reported in this Form. However, if the overlapping portion is attributed to the exposures booked in the trading book, the overlapping portion must be reported in Form MA(BS)3(IV) (see **Annex IIId-B** for illustration).

Hong Kong Monetary Authority

June 2024

Guidance on determining the seniority of tranches

1. If several senior tranches in the same securitization transaction have different maturities and the tranches share pro rata loss allocation, the different maturities shall have no effect on the seniority of these tranches since they benefit from the same level of credit enhancement.

2. In a typical synthetic securitization transaction, a tranche that does not have an ECAI issue specific rating ("relevant tranche") would be treated as a senior tranche, provided that an *inferred rating* can be attributed to the relevant tranche by reference to a *rated* lower tranche that is a senior tranche.

3. In a traditional securitization transaction where all tranches above the *first loss tranche* are rated, the most highly rated position would be treated as a senior tranche. If there are several tranches that share the same rating, only the tranche that is eligible for the highest priority of payment or repayment will be treated as a senior tranche. If there are several senior tranches having different ratings and the different ratings only result from a difference in maturity, all of these tranches should be treated as a senior tranche.

4. A *liquidity facility* supporting an *ABCP programme* may be treated as a senior tranche if—

    (a) the facility is sized to cover all of the outstanding commercial papers and other senior debts supported by the pool of underlying exposures concerned; and

    (b) no cash flows from the pool of underlying exposures can be transferred to creditors (other than the person providing the facility) until the drawn portion of the liquidity facility is repaid in full.

5. If a liquidity facility supporting an ABCP programme does not meet the conditions in paragraphs 4(a) and 4(b), or if for other reasons the facility constitutes a mezzanine position in economic substance rather than a senior position in the pool of underlying exposures concerned, the facility should be treated as a non-senior tranche.

Treatment of Overlapping Securitization Exposures

1.   A reporting AI may determine the amount of the overlapping portion using any of the two different approaches described below.

2.   The first approach is to split its securitization exposures to a securitization transaction into—

   (a)   portions that overlap with another securitization exposure held by it to the same transaction; and

   (b)   other portions that do not overlap with each other.

3.   The second approach is to expand its securitization exposures to a securitization transaction by assuming for capital adequacy purposes that the institution's obligations with respect to one of the securitization exposures are larger than those established contractually. This could be done, say, by expanding the trigger events to exercise a facility and/or the extent of the institution's obligations under the facility. For example, if a liquidity facility provided by an authorized institution to an ABCP programme is not contractually required to cover defaulted assets or will not fund the programme under certain circumstances, the institution may regard the facility overlaps with the commercial papers ("CPs") issued by the ABCP conduit held by the institution as if—

   (a)   its obligations under the facility covered the defaulted assets; or

   (b)   the circumstances concerned were trigger events which, if occur, will allow the facility to be drawn,

such that the facility would preclude all losses on the CPs. In this case, the institution is not required to hold regulatory capital for the CPs. However, the regulatory capital it must hold against the facility must be calculated based on the obligations as expanded in the manner described in paragraph (a) and (b) instead of those established contractually.

Illustrative Examples of the First Approach

4.   An originating institution of an ABCP programme provides a liquidity facility of $10 million to the programme. The institution also holds $2 million of the CPs (rating: A-2) issued under the programme. The overlapping portion of these two exposures is $2 million and the liquidity facility has a higher seniority than the CPs. Other details are as follows:

   (a)   the risk-weight of the liquidity facility ($RW_{facility}$) is 15%;

   (b)   the CCF applicable to the liquidity facility is 100%;

(c)   the risk-weight of the CPs is 50% (RW $_{credit}$);

(d)   the market risk capital charge factor for specific risk of the CPs under the STM approach is 4% which is equivalent to a risk-weight of 50% (RW $_{market}$).

$10 mio – higher repayment priority

$2 mio – lower repayment priority
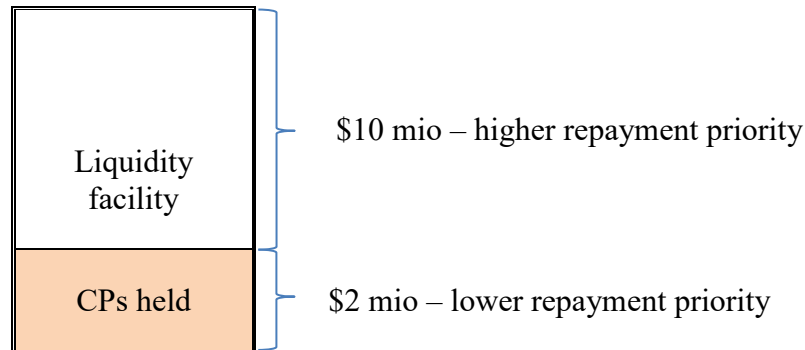
A.   Overlapping within Banking Book (i.e. liquidity facility overlaps with CPs that are held in the banking book)

5.   Since the liquidity facility has a higher seniority, fulfilling the AI's obligations with respect to the CPs by absorbing credit losses on the underlying exposures first will preclude a loss from the facility, the overlapping portion is attributed to the CPs.

(a)   The RWA of the overlapping portion:

= 2 million × RW $_{credit}$

= 2 million × 50%

= 1 million --- (1)

(b)   The RWA of the portion of the liquidity facility that is not the overlapping portion:

= (10 million – 2 million) × CCF × RW $_{liquidity}$

= 8 million × 100% × 15%

= 1.2 million --- (2)

6.   The total RWA of the institution's securitization exposures to the programme:

= (1) + (2)

= 1 million + 1.2 million

= 2.2 million

B.   Overlapping between Banking Book and Trading Book (i.e. liquidity facility overlaps with CPs that are held in the trading book)

7.   If the overlapping portion is attributed to the liquidity facility, RWA of the overlapping portion

= 2 million × CCF × $RW_{liquidity}$

= 2 million × 100% × 15%

= 0.3 million

8.   If the overlapping portion is attributed to the CPs, the RWA of the overlapping portion

= 2 million × RW_{market}

= 2 million × 50 %

= 1 million

9.   The overlapping portion is attributed to the CPs as this results in a higher RWA. Hence, the RWA of 1 million must be reported in Form MA(BS)3(IV).

10.   The RWA of the portion of the liquidity facility that is not the overlapping portion

= (10 million - 2 million) × CCF × $RW_{liquidity}$

= 8 million × 100% × 15%

= 1.2 million   *(To be reported in this Form)*