Federal Reserve System

Section 10 Standardized Measurement Method for Specific Risk

Section 11 Simplified Supervisory Formula Approach

Section 12 Market Risk Disclosures

Section 1. Purpose, Applicability, and Reservation of Authority

(a) Purpose. This appendix establishes risk-based capital requirements for bank holding companies with significant exposure to market risk and provides methods for these bank holding companies to calculate their risk-based capital requirements for market risk. This appendix supplements and adjusts the risk-based capital calculations under Appendix A to this part and establishes public disclosure requirements.

(b) Applicability. (1) This appendix applies to any bank holding company with aggregate trading assets and trading liabilities (as reported in the bank holding company’s most recent quarterly Consolidated Financial Statements for Bank Holding Companies (FR Y-9C)), equal to:

(i) 10 percent or more of quarter-end total assets as reported on the most recent quarter FR Y-9C; or

(ii) $1 billion or more.

(2) The Board may require a bank holding company to hold an amount of capital greater than otherwise required under this appendix if the Board determines that the risk-based capital requirement calculated under this appendix is not commensurate with the market risk of the bank holding company’s covered positions. In making determinations under paragraphs (c)(1) through (c)(3) of this section, the Board will apply notice and response procedures generally in the same manner as the notice and response procedures set forth in [12 CFR 3.12, 12 CFR 223.209, 12 CFR 325.6(c), 12 CFR 567.3(d)].

(c) Reservation of authority. (1) The Board may require a bank holding company to hold an amount of capital greater than otherwise required under this appendix if the Board determines that the bank holding company’s capital requirement for market risk as calculated under this appendix is not commensurate with the market risk of the bank holding company’s covered positions. In making determinations under paragraphs (c)(1) through (c)(3) of this section, the Board will apply notice and response procedures generally in the same manner as the notice and response procedures set forth in [12 CFR 3.12, 12 CFR 223.209, 12 CFR 325.6(c), 12 CFR 567.3(d)].

(2) If the Board determines that the risk-based capital requirement calculated under this appendix by the bank holding company for one or more covered positions or portfolios of covered positions is not commensurate with the risks associated with those positions or portfolios, the Board may require...
the bank holding company to assign a different risk-based capital requirement to the positions or portfolios that more accurately reflects the risk of the positions or portfolios.

(3) The Board may also require a bank holding company to calculate risk-based capital requirements for specific positions or reporting purposes appendix, or under Appendix G to this part or Appendix A to this part, as appropriate, to more accurately reflect the risks of the positions.

(4) Nothing in this appendix limits the authority of the Board under any other provision of law or regulation to take supervisory or enforcement action, including action to address unsafe or unsound practices or conditions, deficient capital levels, or violations of law.

Section 2. Definitions

For purposes of this appendix, the following definitions apply:

Affiliate with respect to a company means any company that controls, is controlled by, or is under common control with, the company.

Backtesting means the comparison of a bank holding company’s internal estimates with actual outcomes during a sample period not used in model development. For purposes of this appendix, backtesting is one form of out-of-sample testing.

Bank holding company is defined in section 2(a) of the Bank Holding Company Act of 1935 (12 U.S.C. 1841(a)).

Commodity position means a position for which price risk arises from changes in the price of a commodity.

Company means a corporation, partnership, limited liability company, depository institution, business trust, special purpose entity, association, or similar organization.

Control means a person or company controls a company if it:

(1) Owns, controls, or holds with power to vote 25 percent or more of a class of voting securities of the company; or

(2) Consolidates the company for financial reporting purposes.

Corporate debt position means a debt position that is an exposure to a company that is not a sovereign entity, the Bank for International Settlements, the European Central Bank, the European Commission, the International Monetary Fund, a multilateral development bank, a depository institution, a foreign bank, a credit union, a public sector entity, a government-sponsored entity, or a securitization.

Country risk classification (CRC) means the consensus CRC published from time to time by the Organization for Economic Cooperation and Development that provides a view of the likelihood that the sovereign entity will service its external debt.

Covered position means the following positions:

(1) A trading asset or trading liability (whether on- or off-balance sheet), as reported on Schedule RC-D of the Call Report or Schedule HC-D of the FR Y-9C, that meets the following conditions:

(i) The position is a trading position or hedges another covered position;

(ii) The position is free of any restrictive covenants on its tradability or the bank holding company is able to hedge the material risk elements of the position in a two-way market;

(iii) Any position that, in form or substance, acts as a liquidity facility that provides support to asset-backed commercial paper;

(2) A foreign exchange or commodity position, regardless of whether the position is a trading asset or trading liability (excluding any structural foreign currency positions that the bank holding company chooses to exclude with prior supervisory approval); and

(3) Notwithstanding paragraphs (1) and (2) of this definition, a covered position does not include:

(i) An intangible asset, including any servicing asset;

(ii) Any hedge of a trading position that the Board or the appropriate Reserve Bank, with concurrence of the Board determines to be outside the scope of the bank holding company’s hedging strategy required in paragraph (a)(2) of section 3 of this appendix;

Correlation trading position means:

(1) A securitization position for which all or substantially all of the value of the underlying exposures is based on the credit quality of a single company for which a two-way market exists, or on commonly traded index securities of the company; or

(2) A position that is not a securitization position and that hedges a position described in paragraph (1) of this definition; and

(3) A correlation trading position does not include:

(i) A resecuritization position;

(ii) A derivative of a securitization position that does not provide a pro rata share in the proceeds of a securitization tranche; and

(iii) A securitization position for which the underlying assets or reference exposures are retail exposures, residential mortgage exposures, or commercial mortgage exposures.

Covenant means the following:

(1) A trading asset or trading liability (whether on- or off-balance sheet), as reported on Schedule RC-D of the Call Report or Schedule HC-D of the FR Y-9C, that meets the following conditions:

(i) The position is a trading position or hedges another covered position;

(ii) The position is free of any restrictive covenants on its tradability or the bank holding company is able to hedge the material risk elements of the position in a two-way market;

(iii) Any position that, in form or substance, acts as a liquidity facility that provides support to asset-backed commercial paper;

(iv) A credit derivative the bank holding company recognizes as a guarantee for risk-
Federal Reserve System

weighted asset amount calculation purposes under Appendix G to this part or Appendix A to this part;

(v) Any equity position that is not publicly traded, other than a derivative that references a publicly traded equity;

(vi) Any position a bank holding company holds with the intent to securitize; or

(vii) Any direct real estate holding.

Credit derivative means a financial contract executed under standard industry documentation that allows one party (the protection purchaser) to transfer the credit risk of one or more exposures (reference exposure(s)) to another party (the protection provider).

Credit union means an insured credit union as defined under the Federal Credit Union Act (12 U.S.C. 1752).

Default by a sovereign entity means noncompliance by the sovereign entity with its external debt service obligations or the inability or unwillingness of a sovereign entity to service an existing obligation according to its original contractual terms, as evidenced by failure to pay principal and interest timely and fully, arrearages, or restructuring.

Debt position means a covered position that is not a securitization position or a correlation trading position and that has a value that reacts primarily to changes in interest rates or credit spreads.

Depository institution is defined in section 3 of the Federal Deposit Insurance Act (12 U.S.C. 1813).

Equity position means a covered position that is not a securitization position or a correlation trading position and that has a value that reacts primarily to changes in equity prices.

Event risk means the risk of loss on equity or hybrid equity positions as a result of a financial event, such as the announcement or occurrence of a company merger, acquisition, spin-off, or dissolution.

Foreign bank means a foreign bank as defined in §211.2 of the Federal Reserve Board’s Regulation K (12 CFR 211.2), other than a depository institution.

Foreign exchange position means a position for which price risk arises from changes in foreign exchange rates.

General market risk means the risk of loss that could result from broad market movements, such as changes in the general level of interest rates, credit spreads, equity prices, foreign exchange rates, or commodity prices.

General obligation means a bond or similar obligation that is guaranteed by the full faith and credit of states or other political subdivisions of a sovereign entity.

Government-sponsored entity (GSE) means an entity established or chartered by the U.S. government to serve public purposes specified by the U.S. Congress but whose debt obligations are not explicitly guaranteed by the full faith and credit of the U.S. government.

Hedge means a position or positions that offset all, or substantially all, of one or more material risk factors of another position.

Idiosyncratic risk means the risk of loss in the value of a position that arises from changes in risk factors unique to that position.

Incremental risk means the default risk and credit migration risk of a position. Default risk means the risk of loss on a position that could result from the failure of an obligor to make timely payments of principal or interest on its debt obligation, and the risk of loss that could result from bankruptcy, insolvency, or similar proceeding. Credit migration risk means the price risk that arises from significant changes in the underlying credit quality of the position.

Investment grade means that the entity to which the bank holding company is exposed through a loan or security, or the reference entity with respect to a credit derivative, has adequate capacity to meet financial commitments for the projected life of the asset or exposure. Such an entity or reference entity has adequate capacity to meet financial commitments if the risk of its default is low and the full and timely repayment of principal and interest is expected.

Market risk means the risk of loss on a position that could result from movements in market prices.

Multilateral development bank means the International Bank for Reconstruction and Development, the Multilateral Investment Guarantee Agency, the International Finance Corporation, the Inter-American Development Bank, the Asian Development Bank, the African Development Bank, the European Bank for Reconstruction and Development, the European Investment Bank, the European Investment Fund, the Nordic Investment Bank, the Caribbean Development Bank, the Islamic Development Bank, the Council of Europe Development Bank, and any other multilateral lending institution or regional development bank in which the U.S. government is a shareholder or contributing member or which the Board determines poses comparable credit risk.

Nth-to-default credit derivative means a credit derivative that provides credit protection only for the nth-defaulting reference exposure in a group of reference exposures.

Over-the-counter (OTC) derivative means a derivative contract that is not traded on an exchange that requires the daily receipt and payment of cash-variation margin.

Public sector entity (PSE) means a state, local authority, or other governmental subdivision below the sovereign entity level.

Publicly traded means traded on:
(1) A transaction on or off the balance sheet of a financial institution or an associated company that is directly or indirectly exposed to credit risk arising from a single or a group of underlying exposures.

(2) Under the law governing the agreement, its rights under the agreement are legal, valid, binding, and enforceable.

Securitization means a securitization in which one or more of the underlying exposures is a securitization position.

Resecuritization means a securitization or resecuritization in which one or more of the underlying exposures is a securitization position.

Revenue obligation means a bond or similar obligation, including loans and leases, that is an obligation of a state or other political subdivision of a sovereign entity, but for which the government entity is committed to repay with revenues from the specific project financed rather than with general tax funds.

SEC means the U.S. Securities and Exchange Commission.

Securitization means a transaction in which:

(1) All or a portion of the credit risk of one or more underlying exposures is transferred to one or more third parties;

(2) The credit risk associated with the underlying exposures has been separated into at least two tranches that reflect different levels of seniority;

(3) Performance of the securitization exposures depends upon the performance of the underlying exposures;

(4) All or substantially all of the underlying exposures are financial exposures (such as loans, commitments, credit derivatives, guarantees, receivables, asset-backed securities, mortgage-backed securities, other debt securities, or equity securities);

(5) For non-synthetic securitizations, the underlying exposures are not owned by an operating company;

(6) The underlying exposures are not owned by a small business investment company described in section 302 of the Small Business Investment Act of 1958 (15 U.S.C. 682); and

(7) The underlying exposures are not owned by a firm an investment in which qualifies as a community development investment under 12 U.S.C. 21 (Eleventh).

(8) The Board may determine that a transaction in which the underlying exposures are owned by an investment firm that exercises substantially unfettered control over the size and composition of its assets, liabilities, and off-balance sheet exposures is not a securitization based on the transaction’s leverage, risk profile, or economic substance.

(9) The Board may deem an exposure to a transaction that meets the definition of a securitization, notwithstanding paragraph (5), (6), or (7) of this definition, to be a securitization based on the transaction’s leverage, risk profile, or economic substance.
Securitization position means a covered position that is:
(1) An on-balance sheet or off-balance sheet credit exposure (including credit-enhancing representations and warranties) that arises from a securitization (including a resecuritization); or
(2) An exposure that directly or indirectly references a securitization exposure described in paragraph (1) of this definition.
Sovereign debt position means a direct exposure to a sovereign entity.
Sovereign entity means a central government (including the U.S. government) or an agency, department, ministry, or central bank of a central government.
Sovereign of incorporation means the country where an entity is incorporated, chartered, or similarly established.
Specific risk means the risk of loss on a position that could result from factors other than broad market movements and includes event risk, default risk, and idiosyncratic risk.
Structural position in a foreign currency means a position that is not a trading position and that is:
(1) Subordinated debt, equity, or minority interest in a consolidated subsidiary that is denominated in a foreign currency;
(2) Capital assigned to foreign branches that is denominated in a foreign currency;
(3) A position related to an unconsolidated subsidiary or another item that is denominated in a foreign currency;
(4) The bank holding company has conducted and documented sufficient legal review to conclude with a well-founded basis that the agreement meets the requirements of paragraph (3) of this definition and is legal, valid, binding, and enforceable under applicable law in the relevant jurisdictions.
Tier 1 capital is defined in Appendix A to this part or Appendix G to this part, as applicable.
Tier 2 capital is defined in Appendix A to this part or Appendix G to this part, as applicable.
Trading position means a position that is:
(a) Trading positions. (1) Identification of trading positions. A bank holding company must have clearly defined policies and procedures for determining which of its trading assets and trading liabilities are trading positions and which of its trading positions are correlation trading positions. These policies and procedures must take into account:
(i) The extent to which a position, or a hedge of its material risks, can be marked-to-market daily and subject to daily margin maintenance requirements;
(ii) The transaction is marked-to-market and sold so that a price reasonably related to the last sales price or current bona fide competitive bid and offer quotations can be determined within one day and settled at that price within a relatively short time frame conforming to trade custom.
Underlying exposure means one or more exposures that have been securitized in a securitization transaction.
Value-at-Risk (VaR) means the estimate of the maximum amount that the value of one or more positions could decline due to market price or rate movements during a fixed holding period within a stated confidence interval.
Section 3. Requirements for Application of the Market Risk Capital Rule
(a) Trading positions. (1) Identification of trading positions. A bank holding company must have clearly defined policies and procedures for determining which of its trading assets and trading liabilities are trading positions and which of its trading positions are correlation trading positions. These policies and procedures must take into account:
(i) The extent to which a position, or a hedge of its material risks, can be marked-to-market daily and subject to daily margin maintenance requirements;
(ii) The transaction is marked-to-market and sold so that a price reasonably related to the last sales price or current bona fide competitive bid and offer quotations can be determined within one day and settled at that price within a relatively short time frame conforming to trade custom.
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(i) The extent to which a position, or a hedge of its material risks, can be marked-to-market daily and subject to daily margin maintenance requirements;
to-market daily by reference to a two-way market; and
(ii) Possible impairments to the liquidity of a position or its hedge.

(2) Trading and hedging strategies. A bank holding company must have clearly defined trading and hedging strategies for its trading positions that are approved by senior management of the holding company:
(i) The trading strategy must articulate the expected holding period of, and the market risk associated with, each portfolio of trading positions.
(ii) The hedging strategy must articulate for each portfolio of trading positions the level of market risk the bank holding company is willing to accept and must detail the instruments, techniques, and strategies the bank holding company will use to hedge the risk of the portfolio.

(b) Management of covered positions. (1) Active management. A bank holding company must have clearly defined policies and procedures for actively managing all covered positions. At a minimum, these policies and procedures must require:
(i) Marking positions to market or to model on a daily basis;
(ii) Daily assessment of the bank holding company’s ability to hedge position and portfolio risks, and of the extent of market liquidity;
(iii) Establishment and daily monitoring of limits on positions by a risk control unit independent of the trading business unit;
(iv) Daily monitoring by senior management of information described in paragraphs (b)(1)(i) through (b)(1)(iii) of this section;
(v) At least annual reassessment of established limits on positions by senior management; and
(vi) At least annual assessments by qualified personnel of the quality of market inputs to the valuation process, the soundness of key assumptions, the reliability of parameter estimation in pricing models, and the stability and accuracy of model calibration under alternative market scenarios.
(2) Valuation of covered positions. The bank holding company must have a process for prudent valuation of its covered positions that includes policies and procedures on the valuation of positions, marking positions to market or to model, independent price verification, and valuation adjustments or reserves. The valuation process must consider, as appropriate, unearned credit spreads, close-out costs, early termination costs, investing and funding costs, liquidity, and model risk.

(c) Requirements for internal models. (1) A bank holding company must obtain the prior written approval of the Board or the appropriate Reserve Bank, with concurrence of the Board, before using any internal model to calculate its risk-based capital requirement under this appendix.
(2) A bank holding company must meet all of the requirements of this section on an ongoing basis. The bank holding company must promptly notify the Board and the appropriate Reserve Bank when:
(i) The bank holding company plans to extend the use of a model that the Board or the appropriate Reserve Bank, with concurrence of the Board, has approved under this appendix to an additional business line or product type;
(ii) The bank holding company makes any change to an internal model approved by the Board or the appropriate Reserve Bank, with concurrence of the Board, under this appendix that would result in a material change in the bank holding company’s risk-weighted asset amount for a portfolio of covered positions;
(iii) The bank holding company makes any material change to its modeling assumptions.
(3) The Board or the appropriate Reserve Bank, with concurrence of the Board, may rescind its approval of the use of any internal model (in whole or in part) or of the determination of the approach under section 9(a)(2)(ii) of this appendix for a bank holding company’s modeled correlation trading positions and determine an appropriate capital requirement for the covered positions to which the model would apply, if the Board or the appropriate Reserve Bank, with concurrence of the Board, determines that the model no longer complies with this appendix or fails to reflect accurately the risks of the bank holding company’s covered positions.

(d) Control, oversight, and validation mechanisms. (1) The bank holding company must have a risk control unit that reports directly to senior management and is independent from the business trading units.
(2) The bank holding company must validate its internal models initially and on an ongoing basis. The bank holding company’s validation process must be independent of the internal models’ development, implementation, and operation, or the validation process must be subjected to an independent review of its adequacy and effectiveness. Validation must include:
(i) An evaluation of the conceptual soundness of (including developmental evidence supporting) the internal models;
(ii) An ongoing monitoring process that includes backtesting. For internal models used to calculate the VaR-based measure, this process must include a comparison of the changes in the bank holding company’s portfolio value that would have occurred were end-of-day positions to remain unchanged.
Section 4. Adjustments to the Risk-Based Capital Ratio Calculations

(a) Risk-based capital ratio denominators. A bank holding company must calculate its general risk-based capital ratio denominator by following the steps described in paragraphs (a)(1) through (a)(4) of this section. A bank holding company subject to Appendix G to this part must use its general risk-based capital ratio denominator for purposes of determining its total risk-based capital ratio and its tier 1 risk-based capital ratio under section 3(a)(2)(i) and section 3(a)(3)(i), respectively, of Appendix G to this part.

(3) The bank holding company must stress test the market risk of its covered positions at a frequency appropriate to each portfolio, and in no case less frequently than quarterly. The stress tests must take into account concentration risk (including but not limited to concentrations in single issuers, industries, sectors, or markets), illiquidity under stressed market conditions, and risks arising from the bank holding company’s trading activities that may not be adequately captured in its internal models.

(4) The bank holding company must have an internal audit function independent of business-line management that at least annually assesses the effectiveness of the controls supporting the bank holding company’s market risk measurement systems, including the activities of the business trading units and independent risk control unit, compliance with policies and procedures, and calculation of the bank holding company’s measures for market risk under this appendix. At least annually, the internal audit function must report its findings to the bank holding company’s board of directors (or a committee thereof).

(e) Internal assessment of capital adequacy. The bank holding company must have a rigorous process for assessing its overall capital adequacy in relation to its market risk. The assessment must take into account risks that may not be captured fully in the VaR-based measure, including concentration and liquidity risk under stressed market conditions.

(1) Documentation. The bank holding company must adequately document all material aspects of its internal models, management and valuation of covered positions, control, oversight, validation and review processes and results, and internal assessment of capital adequacy.

Section 4. Adjustments to the Risk-Based Capital Ratio Calculations

(a) Risk-based capital ratio denominators. A bank holding company must calculate its general risk-based capital ratio denominator by following the steps described in paragraphs (a)(1) through (a)(4) of this section. A bank holding company subject to Appendix G to this part must use its general risk-based capital ratio denominator for purposes of determining its total risk-based capital ratio and its tier 1 risk-based capital ratio under section 3(a)(2)(i) and section 3(a)(3)(i), respectively, of Appendix G to this part.

(b) For a bank holding company subject to Appendix G to this part, advanced adjusted risk-weighted assets, which equal risk-weighted assets as determined in accordance with Appendix A to this part with the adjustments in paragraphs (a)(1)(i) and, if applicable, (a)(1)(ii) of this section; and

(B) For a bank holding company subject to Appendix G to this part, advanced adjusted risk-weighted assets, which equal risk-weighted assets as determined in accordance with Appendix A to this part with the adjustments in paragraphs (a)(1)(i) and, if applicable, (a)(1)(ii) of this section.

(2) For a bank holding company subject to Appendix G to this part, advanced adjusted risk-weighted assets, which equal risk-weighted assets as determined in accordance with Appendix A to this part with the adjustments in paragraphs (a)(1)(i) and, if applicable, (a)(1)(ii) of this section.

(a) General adjusted risk-weighted assets, which equals risk-weighted assets as determined in accordance with Appendix A to this part with the adjustments in paragraphs (a)(1)(i) and, if applicable, (a)(1)(ii) of this section.

B) For a bank holding company subject to Appendix G to this part, advanced adjusted risk-weighted assets, which equal risk-weighted assets as determined in accordance with Appendix A to this part with the adjustments in paragraphs (a)(1)(i) and, if applicable, (a)(1)(ii) of this section.

(i) The...
(i) VaR-based capital requirement. A bank holding company’s VaR-based capital requirement equals the greater of:

(A) The previous day’s VaR-based measure as calculated under section 5 of this appendix; or

(B) The average of the daily VaR-based measures as calculated under section 5 of this appendix for each of the preceding 12 weeks multiplied by three, except as provided in paragraph (b) of this section.

(ii) Stressed VaR-based capital requirement. A bank holding company’s stressed VaR-based capital requirement equals the greater of:

(A) The most recent stressed VaR-based measure as calculated under section 6 of this appendix; or

(B) The average of the stressed VaR-based measures as calculated under section 6 of this appendix for each of the preceding 250 business days multiplied by three, except as provided in paragraph (b) of this section.

(iii) Specific risk add-ons. A bank holding company’s specific risk add-ons equal any specific risk add-ons that are required under section 7 of this appendix and are calculated in accordance with section 10 of this appendix.

(iv) Incremental risk capital requirement. A bank holding company’s incremental risk capital requirement equals any incremental risk capital requirement as calculated under section 8 of this appendix.

(v) Comprehensive risk capital requirement. A bank holding company’s comprehensive risk capital requirement equals any comprehensive risk capital requirement as calculated under section 9 of this appendix.

(vi) Capital requirement for de minimis exposures. A bank holding company’s capital requirement for de minimis exposures equals:

(A) The absolute value of the market value of those de minimis exposures that are not captured in the bank holding company’s VaR-based measure or under paragraph (a)(2)(vi)(B) of this section; and

(B) With the prior written approval of the Board or the appropriate Reserve Bank, with concurrence of the Board, the capital requirement for any de minimis exposures using alternative techniques that appropriately measure the market risk associated with those exposures.

(3) Market risk equivalent assets. The bank holding company must calculate general market risk equivalent assets as the general measure for market risk (as calculated in paragraph (a)(2) of this section) multiplied by 12.5. A bank holding company subject to Appendix G to this part also must calculate advanced market risk equivalent assets as the advanced measure for market risk (as calculated in paragraph (a)(2) of this section) multiplied by 12.5.

(4) Denominator calculation. (i) The bank holding company must add general market risk equivalent assets (as calculated in paragraph (a)(3) of this section) to general adjusted risk-weighted assets (as calculated in paragraph (a)(1)(i) of this section). The resulting sum is the bank holding company’s general risk-based capital ratio denominator.

(ii) A bank holding company subject to Appendix G to this part must add advanced risk equivalent assets (as calculated in paragraph (a)(3) of this section) to advanced adjusted risk-weighted assets (as calculated in paragraph (a)(1)(i) of this section). The resulting sum is the bank holding company’s advanced risk-based capital ratio denominator.

(b) Backtesting. A bank holding company must compare each of its most recent 250 business days’ trading losses (excluding fees, commissions, reserves, net interest income, and intraday trading) with the corresponding daily VaR-based measures calculated in paragraph (a)(3) of this section to determine its VaR-based capital requirement for market risk under paragraph (a)(2)(i) of this section to determine its VaR-based capital requirement for market risk under paragraph (a)(2)(ii) of this section until it obtains the next quarter’s backtesting results, unless the Board or the appropriate Reserve Bank, with the concurrence of the Board notifies the bank holding company in writing that a different adjustment or other action is appropriate.

<table>
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<th>Number of exceptions</th>
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TABLE 1—MULTIPLICATION FACTORS BASED ON RESULTS OF BACKTESTING
Section 5. VaR-Based Measure

(a) General requirement. A bank holding company must use one or more internal models to calculate daily a VaR-based measure of the general market risk of all covered positions. The daily VaR-based measure also may reflect the bank holding company’s specific risk for one or more portfolios of debt and equity positions, if the internal models meet the requirements of paragraph (b)(1) of section 7 of this appendix. The daily VaR-based measure must also reflect the bank holding company’s specific risk for any portfolio of correlation trading positions that is modeled under section 9 of this appendix. A bank holding company may elect to include term repo-style transactions in its VaR-based measure, provided that the bank holding company includes all such term repo-style transactions consistently over time.

(1) The bank holding company’s internal models for calculating its VaR-based measure must use risk factors sufficient to measure the market risk inherent in all covered positions. The market risk categories must include, as appropriate, interest rate risk, credit spread risk, equity price risk, foreign exchange risk, and commodity price risk. For material positions in the major currencies and markets, modeling techniques must incorporate enough segments of the yield curve—in no case less than six—to capture differences in volatility and less than perfect correlation of rates along the yield curve.

(2) The VaR-based measure may incorporate empirical correlations within and across risk categories, provided the bank holding company validates and demonstrates the reasonableness of its process for measuring correlations. If the VaR-based measure does not incorporate empirical correlations across risk categories, the bank holding company must add the separate measures from its internal models used to calculate the VaR-based measure for the appropriate market risk categories (interest rate risk, credit spread risk, equity price risk, foreign exchange rate risk, and/or commodity price risk) to determine its aggregate VaR-based measure.

(3) The VaR-based measure must include the risks arising from the nonlinear price characteristics of options positions or positions with embedded optionality and the sensitivity of the market value of the positions to changes in the volatility of the underlying rates, prices, or other material risk factors. A bank holding company with a large or complex options portfolio must measure the volatility of options positions or positions with embedded optionality by different maturities and/or strike prices, where material.

(4) The bank holding company must be able to justify to the satisfaction of the Board or the appropriate Reserve Bank, with the concurrence of the Board the omission of any risk factors from the calculation of its VaR-based measure that the bank holding company uses in its pricing models.

(5) The bank holding company must demonstrate to the satisfaction of the Board or the appropriate Reserve Bank, with the concurrence of the Board the appropriateness of any proxies used to capture the risks of the bank holding company’s actual positions for which such proxies are used.

(b) Quantitative requirements for VaR-based measure. (1) The VaR-based measure must be calculated on a daily basis using a one-tail, 99.0 percent confidence level, and a holding period equivalent to a 10-business-day movement in underlying risk factors, such as rates, spreads, and prices. To calculate VaR-based measures using a 10-business-day holding period, the bank holding company may calculate 10-business-day measures directly or may convert VaR-based measures using holding periods other than 10 business days to the equivalent of a 10-business-day holding period. A bank holding company that converts its VaR-based measure in such a manner must be able to justify the reasonableness of its approach to the satisfaction of the Board or the appropriate Reserve Bank, with the concurrence of the Board.

(2) The VaR-based measure must be based on a historical observation period of at least one year. Data used to determine the VaR-based measure must be relevant to the bank holding company’s actual exposures and of sufficient quality to support the calculation of risk-based capital requirements. The bank holding company must update data sets at least monthly or more frequently as changes in market conditions or portfolio composition warrant. For a bank holding company that uses a weighting scheme or other method for the historical observation period, the bank holding company must either:

(i) Use an effective observation period of at least one year in which the average time lag of the observations is at least six months; or

(ii) Demonstrate to the Board or the appropriate Reserve Bank, with the concurrence of the Board that its weighting scheme is more effective than a weighting scheme with an average time lag of at least six months representing the volatility of the bank holding company’s trading portfolio over a full business cycle. A bank holding company using
this option must update its data more frequently than monthly and in a manner appropriate for the type of weighting scheme.

(c) A bank holding company must divide its portfolio into a number of significant subportfolios approved by the Board or the appropriate Reserve Bank, with concurrence of the Board, for subportfolio backtesting purposes. These subportfolios must be sufficient to allow the bank holding company and the Board or the appropriate Reserve Bank, with concurrence of the Board, to assess the adequacy of the VaR model at the risk factor level; the Board or the appropriate Reserve Bank, with concurrence of the Board, will evaluate the appropriateness of these subportfolios relative to the value and composition of the bank holding company’s covered positions. The bank holding company must retain and make available to the Board and the appropriate Reserve Bank the following information for each subportfolio for each business day over the previous two years (500 business days), with no more than a 60-day lag:

1. A daily VaR-based measure for the subportfolio calibrated to a one-tail, 99.0 percent confidence level;
2. The daily profit or loss for the subportfolio (that is, the net change in price of the positions held in the portfolio at the end of the previous business day); and
3. The p-value of the profit or loss on each day (that is, the probability of observing a profit that is less than, or a loss that is greater than, the amount reported for purposes of paragraph (c)(2) of this section based on the model used to calculate the VaR-based measure described in paragraph (c)(1) of this section).

Section 6. Stressed VaR-Based Measure

(a) General requirement. At least weekly, a bank holding company must use the same internal model(s) used to calculate its VaR-based measure to calculate a stressed VaR-based measure.

(b) Quantitative requirements for stressed VaR-based measure. (1) A bank holding company must calculate a stressed VaR-based measure for its covered positions using the same model(s) used to calculate the VaR-based measure, subject to the same confidence level and holding period applicable to the VaR-based measure under section 5 of this appendix, but with model inputs calibrated to historical data from a continuous 12-month period that reflects a period of significant financial stress appropriate to the bank holding company’s current portfolio.

2. The stressed VaR-based measure must be calculated at least weekly and be no less than the bank holding company’s VaR-based measure.

3. A bank holding company must have policies and procedures that describe how it determines the period of significant financial stress used to calculate the bank holding company’s stressed VaR-based measure under this section and must be able to provide empirical support for the period used. The bank holding company must obtain the prior approval of the Board or the appropriate Reserve Bank, with concurrence of the Board, for, and notify the Board and the appropriate Reserve Bank if the bank holding company makes any material changes to, these policies and procedures. The policies and procedures must address:

(i) How the bank holding company links the period of significant financial stress used to calculate the stressed VaR-based measure to the composition and directional bias of its current portfolio; and

(ii) The bank holding company’s process for selecting, reviewing, and updating the period of significant financial stress used to calculate the stressed VaR-based measure and for monitoring the appropriateness of the period to the bank holding company’s current portfolio.

4. Nothing in this section prevents the Board or the appropriate Reserve Bank, with concurrence of the Board from requiring a bank holding company to use a different period of significant financial stress in the calculation of the stressed VaR-based measure.

Section 7. Specific Risk

(a) General requirement. A bank holding company must use one of the methods in this section to measure the specific risk for each of its debt, equity, and securitization positions with specific risk.

(b) Modeled specific risk. A bank holding company may use models to measure the specific risk of covered positions as provided in paragraph (a) of section 5 of this appendix (therefore, excluding securitization positions that are not modeled under section 9 of this appendix). A bank holding company must use models to measure the specific risk of correlation trading positions that are modeled under section 9 of this appendix.

1. Requirements for specific risk modeling. (1) If a bank holding company uses internal models to measure the specific risk of a portfolio, the internal models must:

A. Explain the historical price variation in the portfolio;
B. Be responsive to changes in market conditions;
C. Be robust to an adverse environment, including signaling rising risk in an adverse environment; and
D. Capture all material components of specific risk for the debt and equity positions in the portfolio. Specifically, the internal models must:

1. Capture event risk and idiosyncratic risk;
2. Capture and demonstrate sensitivity to material differences between positions that
are similar but not identical and to changes in portfolio composition and concentrations. (ii) If a bank holding company calculates an incremental risk measure for a portfolio of constant positions or securitization positions under section 8 of this appendix, the bank holding company is not required to capture default and credit migration risks in its internal models used to measure the specific risk of those portfolios.

(2) Specific risk fully modeled for one or more portfolios. If the bank holding company’s VaR-based measure captures all material aspects of specific risk for one or more of its portfolios of debt, equity, or correlation trading positions, the bank holding company has no specific risk add-on for those portfolios for purposes of paragraph (a)(2)(iii) of section 4 of this appendix.

(c) Specific risk not modeled. (1) If the bank holding company’s VaR-based measure does not capture all material aspects of specific risk for a portfolio of debt, equity, or correlation trading positions, the bank holding company must calculate a specific-risk add-on for the portfolio under the standardized measurement method as described in section 10 of this appendix. (2) A bank holding company must calculate a specific risk add-on under the standardized measurement method as described in section 10 of this appendix for all of its securitization positions that are not modeled under section 9 of this appendix.

Section 8. Incremental Risk

(a) General requirement. A bank holding company that measures the specific risk of a portfolio of debt positions under section 7(b) of this appendix using internal models must calculate at least weekly an incremental risk measure for that portfolio according to the requirements in this section. The incremental risk measure is the bank holding company’s measure of potential losses due to incremental risk over a one-year time horizon at a one-tail, 99.9 percent confidence level, either under the assumption of a constant level of risk, or under the assumption of constant positions.

(i) Choose to model the rebalancing of the position(s) in a manner consistent with how the bank holding company maintains the position(s) in the portfolio. The bank holding company must determine the frequency of rebalancing in a manner consistent with the liquidity horizons of the positions in the portfolio. The liquidity horizon for a position or set of positions is the time required for a bank holding company to reduce its exposure to, or hedge all of its material risks of, the position(s) in a stressed market. The liquidity horizon for a position or set of positions may not be less than the shorter of three months or the contractual maturity of the position.

(ii) A constant position assumption means that the bank holding company maintains the same set of positions throughout the one-year horizon. If a bank holding company uses this assumption, it must do so consistently across all portfolios.

(iii) A bank holding company’s selection of a constant position or a constant risk assumption must be consistent between the bank holding company’s incremental risk model and its comprehensive risk model described in section 9 of this appendix, if applicable.

(iv) A bank holding company’s treatment of liquidity horizons must be consistent between the bank holding company’s incremental risk model and its comprehensive risk model described in section 9 of this appendix, if applicable.

(v) Recognize the impact of correlations between default and migration events among obligors.

(vi) Recognize the effect that liquidity horizons have on dynamic hedging strategies. In such cases, a bank holding company must:

(i) Choose to model the rebalancing of the hedge consistently over the relevant set of trading positions;

(ii) Demonstrate that the inclusion of rebalancing results in a more appropriate risk measurement;
(iii) Demonstrate that the market for the hedge is sufficiently liquid to permit rebalancing during periods of stress; and
(iv) Capture in the incremental risk model any residual risks arising from such hedging strategies.

(7) Reflect the nonlinear impact of options and other positions with material nonlinear hedging with respect to default and migration changes.

(8) Maintain consistency with the bank holding company’s internal risk management methodologies for identifying, measuring, and managing risk.

(c) Calculation of incremental risk capital requirement. The incremental risk capital requirement is the greater of:
(1) The average of the incremental risk measures over the previous 12 weeks; or
(2) The most recent incremental risk measure.

Section 9. Comprehensive Risk

(a) General requirement. (1) Subject to the prior approval of the Board or the appropriate Reserve Bank, with concurrence of the Board, a bank holding company may use the method in this section to measure comprehensive risk, that is, all price risk, for one or more portfolios of correlation trading positions.

(2) A bank holding company that measures the price risk of a portfolio of correlation trading positions using internal models must calculate at least weekly a comprehensive risk measure that captures all price risk according to the requirements of this section. The comprehensive risk measure is either:
(i) The sum of:
(A) The bank holding company’s modeled measure of all price risk determined according to the requirements in paragraph (b) of this section; and
(B) A surcharge for the bank holding company’s modeled correlation trading positions equal to the total specific risk add-on for such positions as calculated under section 10 of this appendix multiplied by 8.0 percent; or
(ii) With approval of the Board or the appropriate Reserve Bank, with concurrence of the Board and provided the bank holding company has met the requirements of this section for a period of at least one year and can demonstrate the effectiveness of the model through the results of ongoing model validation efforts including robust benchmarking, the greater of:
(A) The bank holding company’s modeled measure of all price risk determined according to the requirements in paragraph (b) of this section; or
(B) The total specific risk add-on that would apply to the bank’s modeled correlation trading positions as calculated under section 10 of this appendix multiplied by 8.0 percent.

(b) Requirements for modeling all price risk. If a bank holding company uses an internal model to measure the price risk of a portfolio of correlation trading positions:
(1) The internal model must measure comprehensive risk over a one-year time horizon at a one-tail, 99.9 percent confidence level, either under the assumption of a constant level of risk, or under the assumption of constant positions.

(2) The model must capture all material price risk, including but not limited to the following:
(i) The risks associated with the contractual structure of cash flows of the position, its issuer, and its underlying exposures;
(ii) Credit spread risk, including nonlinear price risks;
(iii) The volatility of implied correlations, including nonlinear price risks such as the cross-effect between spreads and correlations;
(iv) Basis risk;
(v) Recovery rate volatility as it relates to the propensity for recovery rates to affect tranche prices; and
(vi) To the extent the comprehensive risk measure incorporates the benefits of dynamic hedging, the static nature of the hedge over the liquidity horizon must be recognized. In such cases, a bank holding company must:
(A) Choose to model the rebalancing of the hedge consistently over the relevant set of trading positions;
(B) Demonstrate that the inclusion of rebalancing results in a more appropriate risk measurement;
(C) Demonstrate that the market for the hedge is sufficiently liquid to permit rebalancing during periods of stress; and
(D) Capture in the comprehensive risk model any residual risks arising from such hedging strategies;

(3) The bank holding company must use market data that are relevant in representing the risk profile of the bank holding company’s correlation trading positions in order to ensure that the bank holding company fully captures the material risks of the correlation trading positions in its comprehensive risk measure in accordance with this section; and

(4) The bank holding company must be able to demonstrate that its model is an appropriate representation of comprehensive risk in light of the historical price variation of its correlation trading positions.

(c) Requirements for stress testing.
(1) A bank holding company must at least weekly apply specific, supervisory stress scenarios to its portfolio of correlation trading positions that capture changes in:
(i) Default rates;
(ii) Recovery rates;
(iii) Credit spreads;
Federal Reserve System
Pt. 225, App. E

(iv) Correlations of underlying exposures; and
(v) Correlations of a correlation trading position and its hedge.

(2) Other requirements. (i) A bank holding company must retain and make available to
the Board or the appropriate Reserve Bank, with concurrence of the Board the results of
the supervisory stress testing, including comparisons with the capital requirements
generated by the bank holding company’s comprehensive risk model.
(ii) A bank holding company must report to the Board or the appropriate Reserve
Bank, with concurrence of the Board promptly any instances where the stress
tests indicate any material deficiencies in the comprehensive risk model.

(d) Calculation of comprehensive risk capital requirement. The comprehensive risk capital
requirement is the greater of:

(i) The average of the comprehensive risk measures over the previous 12 weeks; or
(ii) The most recent comprehensive risk measure.

Section 10. Standardized Measurement Method for Specific Risk

(a) General requirement. A bank holding company must calculate a total specific risk
add-on for each portfolio of debt and equity positions for which the bank holding com-
pany’s VaR-based measure does not capture all material aspects of specific risk and for
all securitization positions that are not mod-
ed under section 9 of this appendix. A bank
holding company must calculate each spe-
cific risk add-on in accordance with the re-
quirements of this section. Notwithstanding
any other definition or requirement in this
appendix, a position that would have quali-
fied as a debt position or an equity position
but for the fact that it qualifies as a correla-
tion trading position under paragraph (2) of
the definition of correlation trading posi-
tion, shall be considered a debt position or
an equity position, respectively, for purposes
of this section 10.

(1) The specific risk add-on for an indi-
vidual debt or securitization position that
represents sold credit protection is capped at
the notional amount of the credit derivative
contract. The specific risk add-on for an indi-
vidual debt or securitization position that
represents purchased credit protection is
capped at the current market value of
the transaction plus the absolute value of
the present value of all remaining payments
to the protection seller under the transaction.
This sum is equal to the value of the protec-
tion leg of the transaction.

(2) For debt, equity, or securitization posi-
tions that are derivatives with linear pay-
offs, a bank holding company must assign a
specific risk-weighting factor to the market
value of the effective notional amount of the
underlying instrument or index portfolio, ex-
cept for a securitization position for which the
bank holding company directly cal-
culates a specific risk add-on using the SIFA
in paragraph (b)(2)(vi)(B) of this section. A
swap must be included as an effective no-
tional position in the underlying instrument
or portfolio, with the receiving side treated
as a long position and the paying side treat-
ed as a short position. For debt, equity, or
securitization positions that are derivatives
with nonlinear payoffs, a bank holding com-
pany must risk weight the market value of
the effective notional amount of the under-
lying instrument or portfolio multiplied by
the derivative’s delta.

(3) For debt, equity, or securitization posi-
tions, a bank holding company may net long
and short positions (including derivatives) in
identical issues or identical indices. A bank
holding company may also net positions in
depository receipts against an opposite posi-
tion in an identical equity in different mar-
kets, provided that the bank holding com-
pany includes the costs of conversion.

(4) A set of transactions consisting of ei-
ther a debt position and its credit derivative
hedge or a securitization position and its
credit derivative hedge has a specific risk
add-on of zero if:

(i) The debt or securitization position is
fully hedged by a total return swap (or simi-
lar instrument where there is a matching of
swap payments and changes in market value
of the debt or securitization position);
(ii) There is an exact match between the
reference obligation of the swap and the debt
or securitization position;
(iii) There is an exact match between the
currency of the swap and the debt or
securitization position; and
(iv) There is either an exact match be-
tween the maturity date of the swap and the
maturity date of the debt or securitization
position; or, in cases where a total return
swap references a portfolio of positions with
different maturity dates, the total return
swap maturity date must match the matur-
ity date of the underlying asset in that
portfolio that has the latest maturity date.

(5) The specific risk add-on for a set of
transactions consisting of either a debt posi-
tion and its credit derivative hedge or a
securitization position and its credit deriva-
tive hedge that does not meet the criteria of
paragraph (a)(4) of this section is equal to
20.0 percent of the capital requirement for
the side of the transaction with the higher
specific risk add-on when:

(i) The credit risk of the position is fully
hedged by a credit default swap or similar in-
strument;
(ii) There is an exact match between the
reference obligation of the credit derivative
hedge and the debt or securitization posi-
tion;
(iii) There is an exact match between the currency of the credit derivative hedge and the debt or securitization position; and

(iv) There is either an exact match between the maturity date of the credit derivative hedge and the maturity date of the debt or securitization position; or, in the case where the credit derivative hedge has a standard maturity date:

(A) The maturity date of the credit derivative hedge is within 30 business days of the maturity date of the debt or securitization position; or

(B) For purchased credit protection, the maturity date of the credit derivative hedge is later than the maturity date of the debt or securitization position, but is no later than the standard maturity date for that instrument that immediately follows the maturity date of the debt or securitization position. The maturity date of the credit derivative hedge may not exceed the maturity date of the debt or securitization position by more than 90 calendar days.

(6) The specific risk add-on for a set of transactions consisting of either a debt position and its credit derivative hedge or a securitization position and its credit derivative hedge that does not meet the criteria of either paragraph (a)(4) or (a)(5) of this section, but in which all or substantially all of the price risk has been hedged, is equal to the specific risk add-on for the side of the transaction with the higher specific risk add-on.

(b) Debt and securitization positions. (1) The total specific risk add-on for a portfolio of debt or securitization positions is the sum of the specific risk add-ons for individual debt or securitization positions, as computed under this section. To determine the specific risk add-on for individual debt or securitization positions, a bank holding company must multiply the absolute value of the current market value of each net long or net short debt or securitization position in the portfolio by the appropriate specific risk-weighting factor as set forth in paragraphs (b)(2)(i) through (b)(2)(vii) of this section.

(2) For the purpose of this section, the appropriate specific risk-weighting factors include:

(i) Sovereign debt positions. (A) In general. A bank holding company must assign a specific risk-weighting factor to a sovereign debt position based on the CRC applicable to the sovereign entity and, as applicable, the remaining contractual maturity of the position, in accordance with table 2. Sovereign debt positions that are backed by the full faith and credit of the United States are treated as having a CRC of 0.

<table>
<thead>
<tr>
<th>CRC of Sovereign</th>
<th>Specific risk-weighting factor</th>
<th>Percent</th>
</tr>
</thead>
<tbody>
<tr>
<td>0–1</td>
<td></td>
<td>0.0</td>
</tr>
<tr>
<td>Remaining contractual maturity of 6 months or less.</td>
<td></td>
<td>0.25</td>
</tr>
<tr>
<td>2–3</td>
<td>Remaining contractual maturity of greater than 6 and up to and including 24 months.</td>
<td>1.0</td>
</tr>
<tr>
<td></td>
<td>Remaining contractual maturity exceeds 24 months.</td>
<td>1.6</td>
</tr>
<tr>
<td>4–6</td>
<td>8.0</td>
<td></td>
</tr>
<tr>
<td>7</td>
<td>12.0</td>
<td></td>
</tr>
</tbody>
</table>

(B) Notwithstanding paragraph (b)(2)(i)(A) of this section, a bank holding company may assign to a sovereign debt position a specific risk-weighting factor that is lower than the applicable specific risk-weighting factor in table 2 if:

(i) The position is denominated in the sovereign entity’s currency;

(ii) There is an exact match between the currency of the credit derivative hedge and the debt or securitization position; and

(iii) There is either an exact match between the maturity date of the credit derivative hedge and the maturity date of the debt or securitization position; or, in the case where the credit derivative hedge has a standard maturity date:

(A) The maturity date of the credit derivative hedge is within 30 business days of the maturity date of the debt or securitization position; or

(B) For purchased credit protection, the maturity date of the credit derivative hedge is later than the maturity date of the debt or securitization position, but is no later than the standard maturity date for that instrument that immediately follows the maturity date of the debt or securitization position. The maturity date of the credit derivative hedge may not exceed the maturity date of the debt or securitization position by more than 90 calendar days.

(2) The bank holding company has at least an equivalent amount of liabilities in that currency; and

(3) The sovereign entity allows banks under its jurisdiction to assign the lower specific risk-weighting factor to the same exposures to the sovereign entity.

(C) A bank holding company must assign a 12.0 percent specific risk-weighting factor to

<table>
<thead>
<tr>
<th>Sovereign Debt Positions</th>
<th>Specific risk-weighting factor</th>
</tr>
</thead>
<tbody>
<tr>
<td>Default by the Sovereign Entity</td>
<td>12.0</td>
</tr>
</tbody>
</table>

(2) The bank holding company has at least an equivalent amount of liabilities in that currency; and

(3) The sovereign entity allows banks under its jurisdiction to assign the lower specific risk-weighting factor to the same exposures to the sovereign entity.

(C) A bank holding company must assign a 12.0 percent specific risk-weighting factor to
Federal Reserve System

a sovereign debt position immediately upon determination that a default has occurred; or if a default has occurred within the previous five years.

(D) A bank holding company must assign an 8.0 percent specific risk-weighting factor to a sovereign debt position if the sovereign entity does not have a CRC assigned to it, unless the sovereign debt position must be assigned a higher specific risk-weighting factor under paragraph (b)(2)(i)(C) of this section.

(ii) Certain supranational entity and multilateral development bank debt positions. A bank holding company may assign a 0.0 percent specific risk-weighting factor to a debt position that is an exposure to the Bank for International Settlements, the European Central Bank, the European Commission, the International Monetary Fund, or a MDB.

(iii) GSE debt positions. A bank holding company must assign a 1.6 percent specific risk-weighting factor to a debt position that is an exposure to a GSE. Notwithstanding the foregoing, a bank holding company must assign an 8.0 percent specific risk-weighting factor to preferred stock issued by a GSE.

(iv) Depository institution, foreign bank, and credit union debt positions. (A) Except as provided in paragraph (b)(2)(iv)(B) of this section, a bank holding company must assign a specific risk-weighting factor to a debt position that is an exposure to a depository institution, a foreign bank, or a credit union using the specific risk-weighting factor that corresponds to that entity’s sovereign of incorporation and, as applicable, the remaining contractual maturity of the position, in accordance with table 3.

<table>
<thead>
<tr>
<th>TABLE 3—SPECIFIC RISK-WEIGHTING FACTORS FOR DEPOSITORY INSTITUTION, FOREIGN BANK, AND CREDIT UNION DEBT POSITIONS</th>
</tr>
</thead>
<tbody>
<tr>
<td><strong>CRC of Sovereign</strong></td>
</tr>
<tr>
<td>--------------------</td>
</tr>
<tr>
<td>0–2</td>
</tr>
<tr>
<td></td>
</tr>
<tr>
<td></td>
</tr>
<tr>
<td>3</td>
</tr>
<tr>
<td>4–7</td>
</tr>
<tr>
<td>No CRC</td>
</tr>
<tr>
<td>Default by the Sovereign Entity</td>
</tr>
</tbody>
</table>

(B) A bank holding company must assign a specific risk-weighting factor of 8.0 percent to a debt position that is an exposure to a depository institution or a foreign bank that is includable in the depository institution’s or foreign bank’s regulatory capital and that is not subject to deduction as a reciprocal holding under the [general risk-based capital rules].

(C) A bank holding company must assign a 12.0 percent specific risk-weighting factor to a debt position that is an exposure to a foreign bank immediately upon determination that a default by the foreign bank’s sovereign of incorporation has occurred or if a default by the foreign bank’s sovereign of incorporation has occurred within the previous five years.

(v) PSE debt positions. (A) Except as provided in paragraph (b)(2)(v)(B) of this section, a bank holding company must assign a specific risk-weighting factor to a debt position that is an exposure to a PSE based on the specific risk-weighting factor that corresponds to the PSE’s sovereign of incorporation and to the position’s categorization as a general obligation or revenue obligation and, as applicable, the remaining contractual maturity of the position, as set forth in tables 4 and 5.

(B) A bank holding company may assign a lower specific risk-weighting factor than would otherwise apply under tables 4 and 5 to a debt position that is an exposure to a foreign PSE if:

1. The PSE’s sovereign of incorporation allows banks under its jurisdiction to assign a lower specific risk-weighting factor to such position; and

2. The specific risk-weighting factor is not lower than the risk weight that corresponds
Pt. 225, App. E

12 CFR Ch. II (1–1–14 Edition)

to the PSE’s sovereign of incorporation in accordance with tables 4 and 5.

(C) A bank holding company must assign a 12.0 percent specific risk-weighting factor to a PSE debt position immediately upon determination that a default by the PSE’s sovereign of incorporation has occurred or if a default by the PSE’s sovereign of incorporation has occurred within the previous five years.

**TABLE 4—SPECIFIC RISK-WEIGHTING FACTORS FOR PSE GENERAL OBLIGATION DEBT POSITIONS**

<table>
<thead>
<tr>
<th>CRC of Sovereign</th>
<th>General obligation specific risk-weighting factor</th>
<th>Percent</th>
</tr>
</thead>
<tbody>
<tr>
<td>0–2</td>
<td>Remaining contractual maturity is 6 months or less.</td>
<td>0.25</td>
</tr>
<tr>
<td></td>
<td>Remaining contractual maturity is greater than 6 and up to and including 24 months.</td>
<td>1.0</td>
</tr>
<tr>
<td></td>
<td>Remaining contractual maturity exceeds 24 months.</td>
<td>1.6</td>
</tr>
<tr>
<td>3</td>
<td></td>
<td>8.0</td>
</tr>
<tr>
<td>4–7</td>
<td></td>
<td>12.0</td>
</tr>
</tbody>
</table>

No CRC

Default by the Sovereign Entity

12.0

**TABLE 5—SPECIFIC RISK-WEIGHTING FACTORS FOR PSE REVENUE OBLIGATION DEBT POSITIONS**

<table>
<thead>
<tr>
<th>CRC of Sovereign</th>
<th>General obligation specific risk-weighting factor</th>
<th>Percent</th>
</tr>
</thead>
<tbody>
<tr>
<td>0–1</td>
<td>Remaining contractual maturity is 6 months or less.</td>
<td>0.25</td>
</tr>
<tr>
<td></td>
<td>Remaining contractual maturity is greater than 6 and up to and including 24 months.</td>
<td>1.0</td>
</tr>
<tr>
<td></td>
<td>Remaining contractual maturity exceeds 24 months.</td>
<td>1.6</td>
</tr>
<tr>
<td>2–3</td>
<td></td>
<td>8.0</td>
</tr>
<tr>
<td>4–7</td>
<td></td>
<td>12.0</td>
</tr>
</tbody>
</table>

No CRC

Default by the Sovereign Entity

12.0

(vi) Corporate debt positions. Except as otherwise provided in paragraph (b)(2)(vi)(B), a bank holding company must assign a specific risk-weighting factor to a corporate debt position in accordance with the investment grade methodology in paragraph (b)(2)(vi)(A) of this section.

(A) Investment grade methodology. (1) For corporate debt positions that are exposures to entities that have issued and outstanding

publicly traded instruments, a bank holding company must assign a specific risk-weighting factor based on the category and remaining contractual maturity of the position, in accordance with table 6. For purposes of this paragraph (A), the bank holding company must determine whether the position is in the investment grade or not investment grade category.
A bank holding company must assign an 8.0 percent specific risk-weighting factor for corporate debt positions that are exposures to entities that do not have publicly traded instruments outstanding.

(b) Limitations. (1) A bank holding company must assign a specific risk-weighting factor of at least 8.0 percent to an interest-only mortgage-backed security that is not a securitization position.

(2) A bank holding company shall not assign a corporate debt position a specific risk-weighting factor that is lower than the specific risk-weighting factor that corresponds to the CRC of the issuer’s sovereign of incorporation in table 1.

(vii) Securitization positions. (A) General requirements. (1) A bank holding company that does not use the advanced capital adequacy framework must assign a specific risk-weighting factor to a securitization position using either the simplified supervisory formula approach (SSFA) in accordance with section 11 of this appendix or assign a specific risk-weighting factor of 100 percent to the position.

(2) A bank holding company that uses the advanced capital adequacy framework must calculate a specific risk add-on for a securitization position using the SFA in section 11 of this appendix, the bank holding company must set the specific risk add-on for its position in accordance with paragraph (b)(2)(vii)(B) or assign a specific risk-weighting factor using the SSFA in section 11 of this appendix.

(D) Nth-to-default credit derivatives. A bank holding company must determine a specific risk add-on using the SFA in paragraph (b)(2)(vii)(B), or assign a specific risk-weighting factor using the SSFA in section 11 of this appendix to an nth-to-default credit derivative in accordance with this paragraph (D), irrespective of whether the bank holding company is a net protection buyer or net protection seller. A bank holding company must determine its position in the nth-to-default credit derivative as the largest notional dollar amount of all the underlying exposures.

(1) For purposes of determining the specific risk add-on using the SFA in paragraph (b)(2)(vii)(B) or the specific risk-weighting factor for an nth-to-default credit derivative using the SSFA in section 11 of this appendix, the bank holding company must calculate the attachment point and detachment point of its position as follows:

(i) The attachment point (parameter A) is the ratio of the sum of the notional amounts of all underlying exposures that are subordinated to the bank holding company’s position to the total notional amount of all underlying exposures. For purposes of using the SFA to calculate the specific add-on for its position in an nth-to-default credit derivative, parameter A must be set equal to the credit enhancement level (L) input to the SFA formula. In the case of a first-to-default credit derivative, there are no underlying exposures that are subordinated to the bank holding company’s position.

(ii) In the case of a second-or-subsequent-to-default credit derivative, the smallest (n-1) notional amounts of the underlying exposure(s) are subordinated to the bank holding company’s position.
The absolute value of the current market value of each net long or net short equity position by a specific risk-weighting factor as determined under this paragraph:

1. The sum of the bank holding company’s specific risk add-ons for each net long correlation trading position calculated under this section; or
2. The sum of the bank holding company’s specific risk add-ons for each net short correlation trading position calculated under this section.

2. The sum of the bank holding company’s specific risk add-ons for each net long or net short equity position by a specific risk-weighting factor as determined under this paragraph:

(i) The sum of the bank holding company’s specific risk add-ons for each net long correlation trading position calculated under this section; or
(ii) The sum of the bank holding company’s specific risk add-ons for each net long securitization position calculated under this section.

Equity positions. The total specific risk add-on for a portfolio of equity positions is the sum of the specific risk add-ons of the individual equity positions, as computed under this section. To determine the specific risk add-on of individual equity positions, a bank holding company must multiply the absolute value of the current market value of each net long or net short equity position by the appropriate specific risk-weighting factor as determined under this paragraph:

1. The bank holding company must multiply the absolute value of the current market value of each net long or net short equity position by a specific risk-weighting factor of 8.0 percent. For equity positions that are index contracts comprising a well-diversified portfolio of equity instruments, the absolute value of the current market value of each net long or net short position is multiplied by a specific risk-weighting factor of 2.0 percent.\(^{46}\)

2. For equity positions arising from the following futures-related arbitrage strategies, a bank holding company may apply a 2.0 percent specific risk-weighting factor to one side (long or short) of each position with the opposite side exempt from an additional capital requirement:

(a) Long and short positions in exactly the same index at different dates or in different market centers; or
(b) Long and short positions in index contracts at the same date in different, but similar indices.

3. For futures contracts on main indices that are matched by offsetting positions in a basket of stocks comprising the index, a bank holding company may apply a 2.0 percent specific risk-weighting factor to the futures and stock basket positions (long and short), provided that such trades are deliberately entered into and separately controlled, and that the basket of stocks is comprised of stocks representing at least 90.0 percent of the capitalization of the index. A main index refers to the Standard & Poor’s 500 Index, the FTSE All-World Index, and any other index for which the bank holding company can demonstrate to the satisfaction of the Board or the appropriate Reserve Bank, with concurrence of the Board that the equities represented in the index have liquidity, depth of market, and size of bid-ask spreads comparable to equities in the Standard & Poor’s 500 Index and FTSE All-World Index.

Due diligence requirements. (1) A bank holding company must demonstrate to the satisfaction of the Board or the appropriate Reserve Bank, with concurrence of the Board, a comprehensive understanding of the features of a securitization position that would materially affect the performance of the position by conducting and documenting the analysis set forth in paragraph (f)(2) of this section. The bank holding company’s analysis must be commensurate with the complexity of the securitization position and the materiality of the position in relation to capital.

2. To support the demonstration of its comprehensive understanding, for each securitization position a bank holding company must:

(i) Conduct an analysis of the risk characteristics of a securitization position prior to acquiring the position and document such analysis within three business days after acquiring the position, considering:

\[46\] A portfolio is well-diversified if it contains a large number of individual equity positions, with no single position representing a substantial portion of the portfolio’s total market value.
A Structural features of the securitization that would materially impact
the performance of the position, for example, the contractual cash flow waterfall,
waterfall triggers, credit enhancements, liquidity enhancements, market value trig-
ggers, the performance of organizations that service the position, and deal-specific definition of defaults;
B Relevant information regarding the performance of the underlying credit expo-
sures; for example, the percentage of loans 30, 60, and 90 days past due; default rates; prepayment rates; loans in foreclosure; property types; occupancy; average credit score or other measures of creditworthiness; average loan-to-value ratio; and industry and geographic diversification data on the under-
lying exposures(s);
C Relevant market data of the securitization, for example, bid-ask spreads, most recent sales price and historical price volatility, trading volume, implied market rating, and size, depth and concentration level of the market for the securitization; and
D For resecuritization positions, performance information on the underlying securitization exposures, for example, the issuer name and credit quality, and the characteristics and performance of the exposures underlying the securitization exposures; and
(ii) On an on-going basis (no less frequently than quarterly), evaluate, review, and update as appropriate the analysis required under paragraph (f)(1) of this section for each securitization position.

Section 11. Simplified Supervisory Formula Approach

(a) General requirements. To use the SSFA to determine the specific risk-weighting fac-
tor for a securitization position, a bank holding company must have data that enables it to assign accurately the parameters described in paragraph (b) of this section. Data used to assign the parameters described in paragraph (b) of this section must be the most currently available data and no more than 91 calendar days old. A bank holding company that does not have the appropriate data to assign the parameters described and defined, for purposes of this section, in paragraph (b) of this section must assign a specific risk-weighting factor of 100 percent to the position.

(b) SSFA parameters. To calculate the specific risk-weighting factor for a securitization position using the SSFA, a bank holding company must have accurate information on the five inputs to the SSFA calculation described in paragraphs (b)(1) through (b)(5) of this section:
(1) \( K_A \) is the weighted-average (with unpaid principal used as the weight for each expo-
sure) total capital requirement of the under-
lying exposures calculated using the (general
risk-based capital rules). \( K_A \) is expressed as a decimal value between zero and 1 (that is, an average risk weight of 180 percent represents a value of \( K_A \) equal to .80).
(2) Parameter \( W \) is expressed as a decimal value between zero and one. Parameter \( W \) is the ratio of the sum of the dollar amounts of any underlying exposures within the securitized pool that meet any of the criteria as set forth in paragraphs (i) through (vi) of this paragraph (b)(2) to the ending balance, measured in dollars, of underlying exposures:
(i) Ninety days or more past due;
(ii) Subject to a bankruptcy or insolvency proceeding;
(iii) In the process of foreclosure;
(iv) Held as real estate owned;
(v) Has contractually deferred interest payments for 90 days or more; or
(vi) Is in default.
(3) Parameter \( A \) is the attachment point for the position, which represents the thresh-
hold at which credit losses will first be allo-
cated to the position. Parameter \( A \) equals the ratio of the current dollar amount of under-
lying exposures that are subordinated to the position of the bank holding company to the current dollar amount of underlying ex-
posures. Any reserve account funded by the accumulated cash flows from the underlying exposures that is subordinated to the posi-
tion that contains the bank holding company’s securitization exposure may be in-
cluded in the calculation of parameter \( A \) to the extent that cash is present in the ac-
count. Parameter \( A \) is expressed as a decimal value between zero and one.
(4) Parameter \( D \) is the detachment point for the position, which represents the thresh-
hold at which credit losses of principal allo-
cated to the position would result in a total loss of principal. Parameter \( D \) equals param-
ter \( A \) plus the ratio of the current dollar amount of the securitizations positions that are pari passu with the position (that is, have equal seniority with respect to credit risk) to the current dollar amount of the under-
lying exposures. Parameter \( D \) is expressed as a decimal value between zero and one.
(5) A supervisory calibration parameter, \( p \), is equal to 0.5 for securitization positions that are not resecuritization positions and equal to 1.5 for resecuritization positions.
(c) Mechanics of the SSFA. \( K_A \) and \( W \) are used to calculate \( K_r \), the augmented value of \( K_A \), which reflects the observed credit quality of the underlying pool of exposures. \( K_r \) is defined in paragraph (d) of this section. The values of parameters \( A \) and \( D \), relative to \( K_r \), determine the specific risk-weighting factor assigned to a position as described in this paragraph and paragraph (d) of this section. The specific risk-weighting factor assigned to a securitization position, or portion of a position, as appropriate, is the larger of the specific risk-weighting factor determined in
accordance with this paragraph and paragraph (d) of this section and a specific risk-weighting factor of 1.6 percent.

1) When the detachment point, parameter D, for a securitization position is less than or equal to K_A, the position must be assigned a specific risk-weighting factor of 100 percent.

2) When the attachment point, parameter A, for a securitization position is greater than or equal to K_A, the bank holding company must calculate the specific risk-weighting factor in accordance with paragraph (d) of this section.

3) When A is less than K_A and D is greater than K_A, the specific risk-weighting factor is a weighted-average of 1.00 and K_SSFA, calculated in accordance with paragraph (d) of this section, but with the parameter A revised to be set equal to K_A. For the purpose of this weighted-average calculation:

(i) The weight assigned to 1.00 equals \[
\frac{K_A - A}{D - A}.
\]

(ii) The weight assigned to K_SSFA equals \[
\frac{D - K_A}{D - A}.
\]

The specific risk-weighting factor will be set equal to:

\[
SRWF = 100 \times \left[ \left( \frac{K_A - A}{D - A} \right) \times 1.00 \right] + \left[ \left( \frac{D - K_A}{D - A} \right) \times K_SSFA \right]
\]

(d) SSFA equation. (1) The [bank] must define the following parameters:

\[
K_{\alpha} = (1 - \alpha) \cdot K_D + (0.5 \cdot \alpha)
\]

\[
\alpha = \frac{1}{\rho \cdot K_{\alpha}}
\]

\[
u = D - K_{\alpha}
\]

\[
u = A - K_{\alpha}
\]

\[
u = 2.71828 ,
\]

the base of the natural logarithms.

(2) Then the [bank] must calculate K_SSFA according to the following equation:

\[
K_{SSFA} = \frac{\phi \alpha \cdot u - \phi \alpha \cdot \varphi}{\alpha (u - 1)}
\]

(3) The specific risk-weighting factor for the position (expressed as a percent) is equal to K_SSFA \times 100.
Federal Reserve System

home jurisdiction. A bank holding company must make quantitative disclosures publicly each calendar quarter. If a significant change occurs, such that the most recent reporting amounts are no longer reflective of the bank holding company’s capital adequacy and risk profile, then a brief discussion of this change and its likely impact must be provided as soon as practicable thereafter. Qualitative disclosures that typically do not change each quarter may be disclosed annually, provided any significant changes are disclosed in the interim. If a bank holding company believes that disclosure of specific commercial or financial information would prejudice seriously its position by making public certain information that is either proprietary or confidential in nature, the bank holding company is not required to disclose these specific items, but must disclose more general information about the subject matter of the requirement, together with the fact that, and the reason why, the specific items of information have not been disclosed.

(b) Disclosure policy. The bank holding company must have a formal disclosure policy approved by the board of directors that addresses the bank holding company’s approach for determining its market risk disclosures. The policy must address the associated internal controls and disclosure controls and procedures. The board of directors and senior management must ensure that appropriate verification of the disclosures takes place and that effective internal controls and disclosure controls and procedures are maintained. One or more senior officers of the bank holding company must attest that the disclosures meet the requirements of this appendix, and the board of directors and senior management are responsible for establishing and maintaining an effective internal control structure over financial reporting, including the disclosures required by this section.

(c) Qualitative disclosures.

(1) For each material portfolio of covered positions, the bank holding company must disclose publicly the following information at least quarterly:

(i) The high, low, and mean VaR-based measures over the reporting period and the VaR-based measure at period-end;

(ii) The high, low, and mean stressed VaR-based measures over the reporting period and the stressed VaR-based measure at period-end;

(iii) The high, low, and mean incremental risk capital requirements over the reporting period and the incremental risk capital requirement at period-end;

(iv) The high, low, and mean comprehensive risk capital requirements over the reporting period and the comprehensive risk capital requirement at period-end, with the period-end requirement broken down into appropriate risk classifications (for example, default risk, migration risk, correlation risk);

(v) Separate measures for interest rate risk, credit spread risk, equity price risk, foreign exchange risk, and commodity price risk used to calculate the VaR-based measure; and

(vi) A comparison of VaR-based estimates with actual gains or losses experienced by the bank holding company, with an analysis of important outliers.

(2) In addition, the bank holding company must disclose publicly the following information at least quarterly:

(i) The aggregate amount of on-balance sheet and off-balance sheet securitization positions by exposure type; and

(ii) The aggregate amount of correlation trading positions.

(d) Qualitative disclosures. For each material portfolio of covered positions, the bank holding company must disclose publicly the following information at least annually, or more frequently in the event of material changes for each portfolio:

(1) The composition of material portfolios of covered positions;

(2) The bank holding company’s valuation policies, procedures, and methodologies for covered positions including, for securitization positions, the methods and key assumptions used for valuing such positions, any significant changes since the last reporting period, and the impact of such change;

(3) The characteristics of the internal models used for purposes of this appendix. For the incremental risk capital requirement and the comprehensive risk capital requirement, this must include:

(i) The approach used by the bank holding company to determine liquidity horizons;

(ii) The methodologies used to achieve a capital assessment that is consistent with the required soundness standard; and

(iii) The specific approaches used in the validation of these models;

(4) A description of the approaches used for validating and evaluating the accuracy of internal models and modeling processes for purposes of this appendix;

(5) For each market risk category (that is, interest rate risk, credit spread risk, equity price risk, foreign exchange risk, and commodity price risk), a description of the stress tests applied to the positions subject to the factor;

(6) The results of the comparison of the bank holding company’s internal estimates for purposes of this appendix with actual outcomes during a sample period not used in model development;

(7) The soundness standard on which the bank holding company’s internal capital adequacy assessment under this appendix is
based, including a description of the methodologies used to achieve a capital adequacy assessment that is consistent with the soundness standard;

(b) A description of the bank holding company’s processes for monitoring changes in the credit and market risk of securitization positions, including how those processes differ for resecuritization positions; and

(8) A description of the bank holding company’s policy governing the use of credit risk mitigation to mitigate the risks of securitization and resecuritization positions.

[77 FR 53113, Aug. 30, 2012]

EFFECTIVE DATE NOTES: 1. At 78 FR 62291, Oct. 11, 2013, appendix E was removed and reserved, effective Jan. 1, 2015.

2. At 78 FR 76529, Dec. 18, 2013, appendix E to part 225 was amended in section 2, by revising paragraphs (3)(v) through (vii) and adding paragraph (3)(viii) in the definition of “Covered position”, effective April 1, 2014. For the convenience of the user, the added and revised text is set forth as follows:

APPENDIX E TO PART 225—CAPITAL ADEQUACY GUIDELINES FOR BANK HOLDING COMPANIES: MARKET RISK

SECTION 2. DEFINITIONS

* * * * *

Covered position * * * *

(3) * * *

(v) Any equity position that is not publicly traded, other than a derivative that references a publicly traded equity and other than a position in an investment company as defined in and registered with the SEC under the Investment Company Act of 1940 (15 U.S.C. 80a–1 et seq.), provided that all the underlying equities held by the investment company are publicly traded;

(vi) Any equity position that is not publicly traded, other than a derivative that references a publicly traded equity and other than a position in an entity not domiciled in the United States (or a political subdivision thereof) that is supervised and regulated in a manner similar to entities described in paragraph (3)(v) of this definition;

(vii) Any position a bank holds with the intent to securitize; or

(viii) Any direct real estate holding.

* * * * *

3. At 78 FR 76529, Dec. 18, 2013, appendix E to part 225 was amended in section 10 by revising (b)(2)(i)(A), table 2, and (b)(2)(i)(B), (C), and (D), and adding (b)(2)(i)(E); revising (b)(2)(iv)(A), table 3; (b)(2)(v), table 4, and table 5, effective April 1, 2014. For the convenience of the user, the added and revised text is set forth as follows:

APPENDIX E TO PART 225—CAPITAL ADEQUACY GUIDELINES FOR BANK HOLDING COMPANIES: MARKET RISK

SECTION 10. STANDARDIZED MEASUREMENT METHOD FOR SPECIFIC RISK

(b) Debt and securitization positions. * * *

(1) Sovereign Debt Positions. (A) In accordance with table 2, a bank must assign a specific risk-weighting factor to a sovereign debt position based on the CRC applicable to the sovereign entity and, as applicable, the remaining contractual maturity of the position, or, if there is no CRC applicable to the sovereign entity, based on whether the sovereign entity is a member of the OECD. Notwithstanding any other provision in this Appendix E, sovereign debt positions that are backed by the full faith and credit of the United States are treated as having a CRC of 0.

<table>
<thead>
<tr>
<th>CRC:</th>
<th>Specific risk-weighting factor (in percent)</th>
</tr>
</thead>
<tbody>
<tr>
<td>0–1</td>
<td>0.0</td>
</tr>
<tr>
<td>2–3</td>
<td>0.25</td>
</tr>
<tr>
<td></td>
<td>Remaining contractual maturity of 6 months or less.</td>
</tr>
<tr>
<td></td>
<td>Remaining contractual maturity of greater than 6 and up to and including 24 months.</td>
</tr>
<tr>
<td></td>
<td>Remaining contractual maturity exceeds 24 months.</td>
</tr>
</tbody>
</table>
Federal Reserve System


TABLE 2—SPECIFIC RISK-WEIGHTING FACTORS FOR SOVEREIGN DEBT POSITIONS—Continued

<table>
<thead>
<tr>
<th>Specific risk-weighting factor</th>
<th>(in percent)</th>
</tr>
</thead>
<tbody>
<tr>
<td>4–6</td>
<td>8.0</td>
</tr>
<tr>
<td>7</td>
<td>12.0</td>
</tr>
<tr>
<td>OECD Member with No CRC</td>
<td>0.0</td>
</tr>
<tr>
<td>Non-OECD Member with No CRC</td>
<td>8.0</td>
</tr>
<tr>
<td>Default by the Sovereign Entity</td>
<td>12.0</td>
</tr>
</tbody>
</table>

(B) Notwithstanding paragraph (b)(2)(i)(A) of this section, a bank may assign to a sovereign debt position a specific risk-weighting factor that is lower than the applicable specific risk-weighting factor in table 2 if:

1. The position is denominated in the sovereign entity’s currency;
2. The bank has at least an equivalent amount of liabilities in that currency; and
3. The sovereign entity allows banks under its jurisdiction to assign the lower specific risk-weighting factor to the same exposures to the sovereign entity.

(C) A bank must assign a 12.0 percent specific risk-weighting factor to a sovereign debt position immediately upon determination a default has occurred; or if a default has occurred within the previous five years.

(D) A bank must assign a 0.0 percent specific risk-weighting factor to a sovereign debt position if the sovereign entity is a member of the OECD and does not have a CRC assigned to it, except as provided in paragraph (b)(2)(i)(C) of this section.

(E) A bank must assign an 8.0 percent specific risk-weighting factor to a sovereign debt position if the sovereign entity is not a member of the OECD and does not have a CRC assigned to it, except as provided in paragraph (b)(2)(i)(C) of this section.

(iv) Depository institution, foreign bank, and credit union debt positions. (A) Except as provided in paragraph (b)(2)(iv)(B) of this section, a bank must assign a specific risk-weighting factor to a debt position that is an exposure to a depository institution, a foreign bank, or a credit union in accordance with table 3, based on the CRC that corresponds to that entity’s sovereign of incorporation or the OECD membership status of that entity’s sovereign of incorporation if there is no CRC applicable to the entity’s sovereign of incorporation, and, as applicable, the remaining contractual maturity of the position.

TABLE 3—SPECIFIC RISK-WEIGHTING FACTORS FOR DEPOSITORY INSTITUTION, FOREIGN BANK, AND CREDIT UNION DEBT POSITIONS

<table>
<thead>
<tr>
<th>Specific risk-weighting factor (in percent)</th>
</tr>
</thead>
<tbody>
<tr>
<td>CRC 0–2 or OECD Member with No CRC.</td>
</tr>
<tr>
<td>Remaining contractual maturity of 6 months or less.</td>
</tr>
<tr>
<td>Remaining contractual maturity of greater than 6 and up to and including 24 months.</td>
</tr>
<tr>
<td>Remaining contractual maturity exceeds 24 months.</td>
</tr>
<tr>
<td>CRC 3 ..............................................</td>
</tr>
<tr>
<td>CRC 4–7 ...........................................</td>
</tr>
<tr>
<td>Non-OECD Member with No CRC ..</td>
</tr>
<tr>
<td>Default by the Sovereign Entity ......</td>
</tr>
</tbody>
</table>
(v) **PSE debt positions.** (A) Except as provided in paragraph (b)(2)(v)(B) of this section, a bank must assign a specific risk-weighting factor to a debt position that is an exposure to a PSE in accordance with table 4 and table 5 depending on the position’s categorization as a general obligation or revenue obligation, based on the CRC that corresponds to the PSE’s sovereign of incorporation or the OECD membership status of the PSE’s sovereign of incorporation if there is no CRC applicable to the PSE’s sovereign of incorporation, and, as applicable, the remaining contractual maturity of the position.

(B) A bank may assign a lower specific risk-weighting factor than would otherwise apply under tables 4 and 5 to a debt position that is an exposure to a foreign PSE if:

1. The PSE’s sovereign of incorporation allows banks under its jurisdiction to assign a lower specific risk-weighting factor to such position; and
2. The specific risk-weighting factor is not lower than the risk weight that corresponds to the PSE’s sovereign of incorporation in accordance with tables 4 and 5.

(C) A bank must assign a 12.0 percent specific risk-weighting factor to a PSE debt position immediately upon determination that a default by the PSE’s sovereign of incorporation has occurred or if a default by the PSE’s sovereign of incorporation has occurred within the previous five years.

**TABLE 4—SPECIFIC RISK-WEIGHTING FACTORS FOR PSE GENERAL OBLIGATION DEBT POSITIONS**

<table>
<thead>
<tr>
<th>CRC 0–2 or OECD Member with No CRC.</th>
<th>General obligation specific risk-weighting factor (in percent)</th>
</tr>
</thead>
<tbody>
<tr>
<td></td>
<td>Remaining contractual maturity of 6 months or less.</td>
</tr>
<tr>
<td></td>
<td>Remaining contractual maturity of greater than 6 and up to and including 24 months.</td>
</tr>
<tr>
<td></td>
<td>Remaining contractual maturity exceeds 24 months.</td>
</tr>
<tr>
<td>CRC 3</td>
<td></td>
</tr>
<tr>
<td>CRC 4–7</td>
<td></td>
</tr>
<tr>
<td>Non-OECD Member with No CRC</td>
<td></td>
</tr>
<tr>
<td>Default by the Sovereign Entity</td>
<td></td>
</tr>
</tbody>
</table>

**TABLE 5—SPECIFIC RISK-WEIGHTING FACTORS FOR PSE REVENUE OBLIGATION DEBT POSITIONS**

<table>
<thead>
<tr>
<th>CRC 0–1 or OECD Member with No CRC.</th>
<th>Revenue obligation specific risk-weighting factor (in percent)</th>
</tr>
</thead>
<tbody>
<tr>
<td></td>
<td>Remaining contractual maturity of 6 months or less.</td>
</tr>
<tr>
<td></td>
<td>Remaining contractual maturity of greater than 6 and up to and including 24 months.</td>
</tr>
<tr>
<td></td>
<td>Remaining contractual maturity exceeds 24 months.</td>
</tr>
<tr>
<td>CRC 2–3</td>
<td></td>
</tr>
<tr>
<td>CRC 4–7</td>
<td></td>
</tr>
<tr>
<td>Non-OECD Member with No CRC</td>
<td></td>
</tr>
<tr>
<td>Default by the Sovereign Entity</td>
<td></td>
</tr>
</tbody>
</table>
Federal Reserve System

Pt. 225, App. F

4. At 78 FR 76529, Dec. 18, 2013, appendix E to part 225 was amended in section 11, by revising paragraph (b)(2), effective April 1, 2014. For the convenience of the user, the revised text is set forth as follows:

APPENDIX E TO PART 225—CAPITAL ADEQUACY GUIDELINES FOR BANK HOLDING COMPANIES: MARKET RISK

SECTION 11. SIMPLIFIED SUPERVISORY FORMULA APPROACH

(b) SSFA parameters.

(2) Parameter W is expressed as a decimal value between zero and one. Parameter W is the ratio of the sum of the dollar amounts of any underlying exposures of the securitization that meet any of the criteria as set forth in paragraphs (i) through (vi) of this paragraph (b)(2) to the balance, measured in dollars, of underlying exposures:

(i) Ninety days or more past due;

(ii) Subject to a bankruptcy or insolvency proceeding;

(iii) In the process of foreclosure;

(iv) Held as real estate owned;

(v) Has contractually deferred payments for 90 days or more, other than principal or interest payments deferred on:

(A) Federally-guaranteed student loans, in accordance with the terms of those guarantee programs; or

(B) Consumer loans, including non-federally-guaranteed student loans, provided that such payments are deferred pursuant to provisions included in the contract at the time funds are disbursed that provide for period(s) of deferral that are not initiated based on changes in the creditworthiness of the borrower;

(vi) Is in default.

5. At 78 FR 76529, Dec. 18, 2013, appendix E to part 225 was amended in section 12, by revising (a); (c)(1) introductory text, and (d) introductory text, effective Apr. 1, 2014. For the convenience of the user, the revised text is set forth as follows:

APPENDIX E TO PART 225—CAPITAL ADEQUACY GUIDELINES FOR BANK HOLDING COMPANIES: MARKET RISK

SECTION 12. MARKET RISK DISCLOSURES

(a) Scope. A bank must comply with this section unless it is a consolidated subsidiary of a bank holding company or a depository institution that is subject to these requirements or of a non-U.S. banking organization that is subject to comparable public disclo-