

June 21, 2013

Secretariat of the Basel Committee
on Banking Supervision
Bank for International Settlements
CH-4002 Basel, Switzerland

Dear Basel Committee members:

**Re: CBA¹ Comments on consultative document:
“*Recognising the cost of credit protection purchased*”**

We appreciate the opportunity to review and comment on the Basel Committee's consultative document, *Recognising the cost of credit protection purchased* dated March 2012 ('Consultative Document').

The CBA supports the Basel Committee's objective to limit capital arbitrage opportunities. As Canadian banks are generally not active in these types of transaction – due to both self-discipline and strong regulatory review – actions to curb such practices help to level the international playing field. However, we question the need to have these new requirements included in Pillar I, as opposed to relying on the tools already available to regulators as part of Pillar II. We believe that no Pillar I rules can effectively address all arbitrage opportunities; when such objective is attempted, unintended consequences, like the ones identified in this letter, are unfortunately unavoidable. As such, we believe that it would be simpler and preferable for the Basel Committee to give local supervisors the discretion to review hedges and disqualify those that do not have economic substance. Implementing complex rules that are excessively conservative and that have the outcome of discouraging legitimate hedging is undesirable.

For your consideration, we have provided our comments on some key issues below.

¹ The Canadian Bankers Association works on behalf of 55 domestic banks, foreign bank subsidiaries and foreign bank branches operating in Canada and their 274,000 employees. The CBA advocates for effective public policies that contribute to a sound, successful banking system that benefits Canadians and Canada's economy. The Association also promotes financial literacy to help Canadians make informed financial decisions and works with banks and law enforcement to help protect customers against financial crime and promote fraud awareness. www.cba.ca.

Scope of the Consultative Document

It is not clear from the Consultative Document which transactions are “in-scope” and as such, we recommend that the Consultative Document be more specific in isolating and identifying arbitrage transactions that the Basel Committee seeks to mitigate so that both banks and supervisors are clear as to the scope of the Committee’s proposals.

In this regard, one could interpret that the present value of premiums on all purchased credit protection transactions (assuming the hedged asset has a risk-weight in excess of 150% at the time the credit protection is bought and the PV of the premiums is not recognized in earnings) will attract a 1250% risk-weight. We assume this is not the intent of the Consultative Document in view that the Basel Committee “*recognises that the purchase of credit protection can be an effective risk management tool*”.

Concerning the scope of the Consultative Document:

1. We recognize that the intent of the Consultative Document is to address the potential for capital arbitrage within the credit risk mitigation framework, particularly with respect to securitization transactions where no “true” risk transference has occurred. As such, we believe that the scope of the Consultative Document should be limited to hedges on first loss securitization exposures and assets synthetically securitized into a first loss tranche. All other transactions should be managed as part of the Pillar II supervisory review so as to avoid the unintended consequence of forcing premiums on bona fide hedges (i.e. “true” risk transfer) to be risk-weighted at 1250%.

Further, it is our understanding that the following items will be considered “out of scope”. For greater clarity, we request that the final document explicitly state that the premiums on the following hedges will not attract a 1250% risk-weight:

- **Hedging of trading book exposures (including hedging of Credit Valuation Adjustment (“CVA”)):** Hedging of trading book exposures, including CVA, should be considered “out-of-scope” since both the underlying and the hedge are recorded at fair value for accounting purposes and thus not subject to arbitrage.
- **Hedging of Single-name CDS:** Hedges that cover 100% of the loss exposure profile of a single-name entity (vs. first loss or a tranche of losses) are bona fide hedges that should not be considered within the scope of the consultative document. This includes hedges that take the form of both CDS and guarantees.
- **Exposures guaranteed by government entities.**
- **Trade finance transactions:** In view that the Basel Committee’s objective is to address the potential for capital arbitrage within the credit risk mitigation framework, trade finance transactions (including Letters of Credit, etc.), which often involve guarantees, should be specifically excluded from the scope of the Consultative Document since such transactions are intended to facilitate international trade.

- Any other transactions where at least one of the following is true :
 - i. both the underlying asset and the derivative are marked-to-market for accounting purposes (since no potential arbitrage opportunities can exist);
 - ii. in the case where the hedged asset is not fair-valued for accounting purposes, sufficient accounting provisions have been taken on the asset to offset the gains that have been recognized in earnings from the marketing-to-mark of the CDS;
 - iii. the hedge does not meet the materiality threshold (which we recommend to be modified (see #3 below) to occur when the sum of non-contingent premiums is equal to or below 50% of the book value of the hedged asset(s) as at the relevant reporting date); and
 - iv. the credit spread income of the loan exposure is equal to or greater than the credit spread of the CDS protection at the time the credit protection is bought.
2. With respect to the transactions that the Consultative Document is targeting, we question the necessity of the Consultative Document and encourage the Basel Committee to consider the following factors related to securitization:
- a. **Pillar II:** First loss securitization transactions are already effectively addressed in most markets as part of the Pillar II supervisory review.
 - b. **Revisions to the Basel Securitization Framework:** The sample calculation in the technical guidance of the Consultative Document ignores the potential effects of the recently proposed Basel securitization Framework (*Revisions to the Basel Securitization Framework* – Consultative Document, December 2012). Please refer to Appendix A which demonstrates how the sample calculation in the consultative document shows 122% RWA relief from the first-loss CDS hedge, while a revised calculation based on current market data indicates 60% RWA relief from the first-loss CDS hedge. In considering new rules, we encourage regulators to be mindful of all rules that have been recently implemented or proposed, as the cumulative impact of all new rules can often result in “double-counting”, leading to excessively punitive cumulative capital charges.
- Please also refer to Appendix B which illustrates the high cost of credit protection for a \$1 Billion BBB- average rated securitization transaction under four scenarios: (i) 0 – 7% tranche using SFA calculations, which illustrates capital treatment under existing rules; (ii) 0 – 7% tranche using MSFA calculations, which illustrates capital treatment of existing transactions under proposed MSFA calculations; (iii) 0 – 16% tranche using MSFA calculations, which illustrates potential tranche changes to adapt to MSFA rule changes; and (iv) 0 – 16% tranche using MSFA and HCCP calculations, which illustrates the impact of MSFA and HCCP on potential tranche changes. Notably, under the current proposals in the Consultative Document, the capital impact (after hedging and taking into account the cost of credit protection) in the context of this example is \$42,700,620.
- c. **Legitimate first loss hedging transactions:** Even if there are rare instances where the Consultative Document does prove necessary, the proposed guidance is very penalizing to all first loss transactions. In our view, this is unrealistic and fails to recognize legitimate first loss hedging transactions (please see below for further details and refer to Appendix C).

3. Given the above and in order to better ensure that premiums on bona fide risk management hedges do not attract a 1250% risk-weight, we respectfully request that the materiality threshold be amended from a 150% risk-weight to when the sum of non-contingent premiums is above 50% of the book value of the hedged asset(s) as at the relevant reporting date. As capital arbitrage transactions within the credit risk mitigation framework would involve large non-contingent premiums in relation to the book value of the hedged asset(s), we believe this recommended materiality threshold will better ensure that bona fide risk management hedges are not unjustifiably penalized by the new proposal. While Canadian banks do not hedge a large number of 150% risk weighted exposures, they do hedge some, and the results of this proposed guidance are unreasonable in those instances.

Sample calculations not reflective of Wholesale Banking Hedging Activity

The sample calculations in the technical guidance of the Consultative Document do not appear to be indicative of market conditions and if more realistic inputs were used, the CDS would fail to produce material RWA relief under the Consultative Document. Please refer to Appendix A which illustrates, by way of example, the RWA after protection: (i) as provided in the annex; and (ii) on the basis of revised realistic assumptions. Notably, the sample calculation in the technical guidance shows 143% relief from the single-name CDS hedge, whereas the revised calculation based on current market data indicates no RWA relief from the single-name CDS hedge.

Moreover, the examples in the Consultative Document do not generally reflect typical wholesale banking hedging activity. Please refer to Appendix C which illustrates, by way of example, a typical wholesale loan hedging transaction. As shown in this example, banks predominantly provide revolvers, which tend to be undrawn or partially drawn, and that have very low commitment fees. These fees are much lower than market spreads for the prevailing risk. However, banks are prepared to enter into these revolvers for two reasons:

- bank revolvers typically have a better structure than market instruments and banks use this structure to mitigate downside risk; and
- bank revolvers are critical relationship products that allow banks to generate ancillary revenue which provides more than adequate compensation for the risk they take.

Notably, the examples in the Consultative Document fail to consider future relationship income. In our view, it is unreasonably conservative to recognize future costs of protection without recognizing future revenues as well. For example, first loss tranches arising from securitizations provide high returns. If a bank hedges the credit risk of this receivable through a guarantee/CDS, as the bank must risk weight future premiums on the guarantee/CDS (even though obligor default may result in it not being paid), we believe this risk weighting should be net of the contractual revenue from the underlying (hedged) first loss asset.

Operational complexities

The unique features of CDS (e.g. upfront premium not necessarily equal to rolling premium) make the construction of the present value calculations proposed in the Consultative Document open to various interpretations. Therefore, for transactions that are “in-scope”, we seek the Basel Committee’s clarification with respect to the calculation of premiums.

For example, the standardized CDS contract consists of a standard coupon of a 100 bps or 500 bps and an upfront premium that may be paid or received by the purchasing bank depending on whether the effective cost of protection is above the running coupon (purchaser pays upfront premium) or below (purchaser receives upfront premium). Determining which premium to discount is not obvious. Specifically, should banks:

- Discount the upfront premium (including negative premiums or premiums received) at a different rate than the running coupon or at the same rate?
- Ignore the split of premium and coupon and use a market calculator to determine an effective running premium?
- Use a unique risky rate for each effected CDS hedge to determine the PV of future costs?

While the theoretically correct answer is that banks should discount the effective running premium at a unique risky rate, it is likely too complex for most banks to implement this approach. This highlights one of several operational challenges of the Consultative Document given the uniqueness of CDS contracts. We respectfully request that OSFI consider these operational challenges when finalizing the Consultative Document.

Impact of the “Modified Restructuring” credit event trigger

We note that while the standard European CDS contract includes a “Modified Restructuring” credit event trigger, a standard North American CDS contract does not. This is because a modified restructuring rarely occurs in North America, yet is more frequent in Europe.

While the Basel Committee’s proposals automatically haircut protection by 40%, the European standard contract, due to the inclusion of a “Modified Restructuring” as a structuring event, is not subject to this haircut. In this regard, we are very concerned that the Consultative Document does not differentiate between the European and North American market.

Further and in our view, the proposed 40% haircut appears to be arbitrary without an empirical basis. To add a deduction for the cost of credit protection (on top of this haircut) appears unduly punitive, particularly for standard single-name CDS, in view that most corporate revolvers extend maturity annually. Even for shorter dated revolvers, most banks will use 5 year CDS to hedge in anticipation that revolver maturity will extend annually (please refer to Appendix C).

Conclusion

While we support the Basel Committee’s objective to limit capital arbitrage opportunities, we respectfully request that the final document specify which transactions are “in-scope” so as to avoid forcing premiums on bona fide risk management hedges from being risk-weighted at 1250%. We recommend that only hedges on first loss securitization exposures and assets synthetically securitized into a first loss tranche should be considered “in-scope”. All other transactions should be managed as part of the Pillar II supervisory review so as to mitigate the unintended consequences of discouraging the use of CDS contracts to manage “true” risk. A change in the materiality threshold (i.e. sum of non-contingent premiums greater than 50% of the book value of the hedged asset(s) as at the relevant reporting date) is also warranted in order to ensure that only the capital arbitrage transactions will be captured by the new rules. Finally, in preparing the final document, the Basel Committee should give consideration to the capital impact of the proposed revised securitization framework, the future relationship income component that is prevalent in wholesale loan hedging transactions, the operational complexities that are inherent to CDS contracts, and the existing 40% haircut applied to North American CDS contracts due to the exclusion of a “Modified Restructuring” credit event trigger.

We thank you for taking our comments into consideration and look forward to future discussions on these issues.

Sincerely,

A handwritten signature in black ink, appearing to read "J. Starkes", with a stylized, flowing script.

Attachments:

- Appendix A: BlackRock Sample Calculations – Single Name DS Hedge & First-loss CDS Hedge
- Appendix B: Securitization Example for High Cost of Credit Protection Letter
- Appendix C: Typical Wholesale Loan Hedging Example

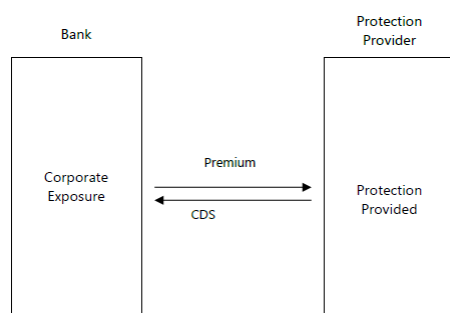
cc:

- Joel Starkes, Director, Securitization and Structured Products, OSFI Capital Division
- Brad Shinn, Director, OSFI Capital Division

Sample Calculation – Single Name CDS Hedge

The sample calculations in the Technical Guidance Annex do not appear to be indicative of market conditions

Example 1 – Single Name CDS hedge



- Bank holds single-name corporate exposure 100 with 5 yrs which is risk weighted at 200%
- Bank hedges with 5-yr CDS from a 0% risk-weight counterparty
- CDS premium is 100bps per annum
- Assumed LGD is 80%
- Risk-free rate is 2%

Implies a B/B+ quality borrower

CDS counterparty is more likely to be a AA rated bank, risk weighted at ~35% (ignoring CVA charges)

CDS premium for a B/B+ industrial name is around ~400bps (~200bps pre-crisis levels) according to Barclays Live Time Series Plotter

Senior, unsecured LGD should be lower, e.g. 50-60% range

5-yr Treasury yields are around 0.8%

Sample calculation in the Technical Guidance Annex of the BCBS proposal shows 143 RWA relief from the single-name CDS hedge

Option 2: Supervisory choice (ii) - risky discount rate [as provided in Annex]

Year	1	2	3	4	5
Position	100	100	100	100	100
Contractual Premium (100bps)	1	1	1	1	1
Risky PV (1%/80% + 2%)	0.97	0.94	0.91	0.88	0.85

Sum Risky PV Premium **4.55**
 RWA before protection **200.00**
 RWA after protection (Risky PV) **56.84** (=4.55 x 1250%)

Revised calculation based on more representative market data indicates no RWA relief from the single-name CDS hedge

Option 2: Supervisory choice (ii) - risky discount rate [with revised assumptions]

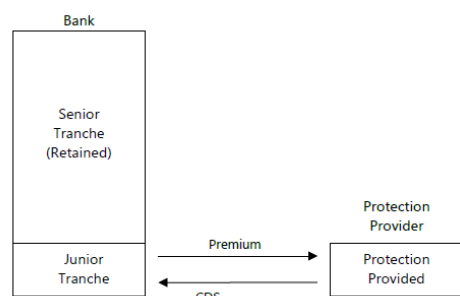
Year	1	2	3	4	5
Position	100	100	100	100	100
Contractual Premium (400bps)	4	4	4	4	4
Risky PV (4%/55% + 0.8%)	0.93	0.86	0.79	0.73	0.68

Sum Risky PV Premium **15.94**
 RWA before protection **200.00**
 RWA after protection (Risky PV) **234.25** (=15.94x1250% + 100x35%)

Sample Calculation – First-loss CDS Hedge

The sample calculation ignores the potential effects of recently proposed Basel Securitization Framework

Example 3 – First-loss CDS hedge



- Bank holds portfolio of corporate exposures booked at 100 with 5 yrs average life and 200 RWA
- Banks hedges 10% of first-losses with 5-yr CDS from a 0% risk-weight counterparty
- Bank retains super-senior 90 tranche, risk weighted at 7%
- Expected loss on the pool is 2%
- CDS premium is 20% per annum
- Assumed LGD is 80%
- Risk-free rate is 2%

Implies B/B+ average credit quality

Reasonable, since these hedges are typically fully collateralized

Consistent with B/B+ quality and 80% LGD

New Basel Securitization proposal will increase 5yr senior tranche risk weight to 50-60% range

Premium would be 30-35% range for 2% EL pool based on 15-20% IRR expectations over 5-yrs

Senior, unsecured LGD should be lower, e.g. 50-60% range

5-yr Treasury yields are around 0.8%

Sample calculation in the Technical Guidance Annex shows 122 RWA relief from the first-loss CDS hedge

Option 2: Supervisory choice (ii) - risky discount rate [as provided in Annex]

Year	1	2	3	4	5
Position	10	10	10	10	10
Contractual Premium (20%)	2	2	2	2	2
Risky PV (20% + 2%)	1.64	1.34	1.10	0.90	0.74

Sum Risky PV Premium **5.73**
 RWA before protection **200.00**
 RWA after protection (Risky PV) **77.89** (=5.73 x 1250% + 90 x 7%)

Revised calculation based on more representative market data combined with potential impact of the recently proposed Revisions to Securitization Framework indicates 60 RWA relief from the first-loss CDS hedge

Option 2: Supervisory choice (ii) - risky discount rate [with revised assumptions]

Year	1	2	3	4	5
Position	10	10	10	10	10
Contractual Premium (30%)	3	3	3	3	3
Risky PV (30% + 0.8%)	2.29	1.75	1.34	1.02	0.78

Sum Risky PV Premium **7.20**
 RWA before protection **200.00**
 RWA after protection (Risky PV) **139.45** (=7.2 x 1250% + 90 x 55%)

Appendix B - Example for High Cost of Credit Protection Letter

	Current Methodology (SFA)	December 2012 Proposals (MSFA) -- No Tranche Changes	December 2012 Proposals (MSFA) -- With Wider Tranche	March 2013 Proposals (High Cost Deduction)
Portfolio & Regulatory Capital Parameters				
Portfolio Notional Amount	1,000,000,000	1,000,000,000	1,000,000,000	1,000,000,000
Average Rating	BBB-	BBB-	BBB-	BBB-
Average PD	0.30%	0.30%	0.30%	0.30%
Hedge Maturity (Y)	5.0	5.0	5.0	5.0
Loan Maturity (Y)	3.5	3.5	3.5	3.5
Exposure at Default	85%	85%	85%	85%
Loss Given Default	45%	45%	45%	45%
Obligors	150	150	150	150
Tranche Structure & Cost				
Junior Attachment Point	0%	0%	0%	0%
Junior Detachment Point	7%	7%	7%	7%
Mezz Attachment Point			7%	7%
Mezz Detachment Point			16%	16%
Libor	1.00%	1.00%	1.00%	1.00%
Junior Tranche Premium (% of tranche)	13.50%	13.50%	13.50%	13.50%
Mezz Tranche Premium (% of tranche)		3.50%	3.50%	3.50%
Premium Cost / Portfolio	1.02%	1.02%	1.42%	1.42%
Capital Before Hedging				
Risk Weight	58.5%	58.5%	58.5%	58.5%
Kirb	4.68%	4.68%	4.68%	4.68%
Unhedged Risk Weighted Assets	584,613,444	584,613,444	584,613,444	584,613,444
Minimum Capital Required	9.00%	9.00%	9.00%	9.00%
Unhedged Capital Requirement	52,615,210	52,615,210	52,615,210	52,615,210
Capital After Hedging				
Counterparty Risk Rating	Cash	Cash	Cash	Cash
Counterparty Risk Weight	0.00%	0.00%	0.00%	0.00%
Junior Tranche Notional Amount	70,000,000	70,000,000	70,000,000	70,000,000
Junior Tranche Counterparty Capital	-	-	-	-
Mezz Tranche Notional Amount	-	-	90,000,000	90,000,000
Mezz Tranche Counterparty Capital	-	-	-	-
Retained Senior Tranche Notional	930,000,000	930,000,000	840,000,000	840,000,000
Retained Senior Tranche Capital Rate	0.56%	2.51%	1.09%	1.09%
Retained Senior Tranche Capital	5,208,000	23,297,711	9,139,200	9,139,200
Capital Requirement after Hedging	5,208,000	23,297,711	9,139,200	9,139,200
Net Capital Saving	47,407,210	29,317,499	43,476,010	43,476,010
-- as a % of unhedged Capital	90.1%	55.7%	82.6%	82.6%
Annual Cost / Capital Saved (no defaults)	19.9%	32.2%	29.0%	29.0%
Portfolio Income				
Loan Utilization Rate	10%	10%	10%	10%
Loan Commitment Fee	0.15%	0.15%	0.15%	0.15%
Loan Drawn Spread	1.00%	1.00%	1.00%	1.00%
Annual Portfolio Income	2,350,000	2,350,000	2,350,000	2,350,000
-- as a % of Portfolio	0.235%	0.235%	0.235%	0.235%
High Cost of Credit Protection Calculation				
Annual Credit Protection Cost -- Junior				9,450,000
Junior Tranche Capital (if held on balance sheet)				61,037,493
Junior Tranche Implied Risk Weight				1089.96%
Annual Credit Protection Cost -- Mezz				1,278,000
Mezz Tranche Capital (if held on balance sheet)				20,895,322
Mezz Tranche Implied Risk Weight				290.21%
Total Annual Credit Protection Cost				10,728,000
-- as a % of Portfolio				1.07%
Aggregate Discount Rate				7.88%
Risk Weight Threshold for PV Calculations				150%
PV of Junior Tranche Protection Cost				37,855,744
PV of Mezz Tranche Protection Cost				5,119,539
PV of Portfolio Income				(9,413,862)
PV of Net Credit Protection Cost				33,561,420
Capital Requirement after Hedging and High Cost Credit Protection Capital Impact				42,700,620
Net Capital Saving				9,914,590
-- as a % of unhedged Capital				18.8%
Annual Cost / Capital Saved (no defaults)				127.1%

Proposed changes to regulatory capital methodology						
		Net Capital		Capital Savings		Annual Cost /
		(€)	% of portfolio	(€)	% of unhedged	Capital Saved
1B Unhedged Portfolio with BBB- Avg. Internal Rating		52,615,210	5.3%	-	-	
Tranche(s) Hedged	Methodology					
0%-7%	SFA	5,208,000	0.5%	47,407,210	90.1%	19.9%
0%-7%	MSFA	23,297,711	2.3%	29,317,499	55.7%	32.2%
0%-16%	MSFA	9,139,200	0.9%	43,476,010	82.6%	29.0%
0%-16%	MSFA & HCCP	42,700,620	4.3%	9,914,590	18.8%	127.1%

Appendix C - Credit Default Swaps – Typical Wholesale Loan Hedging Example

Credit Default Swaps

- A credit default swap (CDS) is a derivative contract in which the protection buyer transfers risk that the reference entity might default through a series of payments to the protection seller. In exchange, the buyer receives a payout if a specified credit event occurs (Bankruptcy or Failure to Pay in N.A; Bankruptcy, Failure to Pay and Modified Restructuring in Europe).
- The CDS specifies a reference obligation that robustly defines the issuing entity, the notional amount of credit risk being transferred, and the seniority. At inception, two cash flows are agreed upon: the upfront amount, and the annual fixed coupon.
- If, during the life of the CDS contract, there is no Credit event, the CDS contract will mature as scheduled. If there is a Credit event (i.e. bankruptcy or failure to pay in N.A.), the Seller will typically pay the buyer a cash settlement (though physical is an option) following an auction administered by ISDA to fix the price of defaulted obligations.

Standardized CDS contract

- Two standardized coupons: 100bps and 500bps in N.A.
- Standardized quarterly maturity and coupon dates (20 March, June, September and December).
- Quoted two ways: i) Running spread paid annually, e.g. 250 bps, or ii) upfront pts + annual coupon, paid quarterly, e.g. 6.75% + 500 bps running. In either case, the CDS contract will have an upfront payment + quarterly coupon payments.
- If quoted spread < coupon, buyer of protection receives from protection seller an upfront payment equal to the PV of the delta between the quoted spread and coupon. Vice versa if quoted spread > coupon.

Typical Wholesale Loan Hedging example: ABC company

- US\$100mm CDS purchased to hedge against a US\$250mm hold in an undrawn \$2.3Bn 5 year revolving Credit facility due Mar 9/18.
- Anticipate loan may extend tenor annually. \$100mm 5yr CDS protection is purchased at a quoted spread of 228bps with a fixed coupon of 500bps.
- Cash flows: i) Upfront payment, Bank receives \$13.3mm, and ii) Bank pays fixed 500bps, or ~ \$1.25mm each quarter.
- The effective unrecognized cost of protection purchased is the PV of 228bps discounted at the risk adjusted spread for ABC: \$10.4mm.
- The Revolver pays a commitment fee of 50bps or \$500k p.a. (L+225bps if drawn).
- Cost of protection exceeds commitment fee income.
- Expected 3yr/5yr ancillary income (IPO, DCM, FX...etc) of \$15/\$25mm exceeds cost of protection.

Marking the CDS

- One month after transaction, market spread on CDS is 190 bps.
- The MTM is negative and taken through income.
- Effective unrecognized cost of credit protection (given MTM loss recognition) is now the PV of 190bp: approx \$8.8mm.
- Conclusion: the unrecognized future cost of credit protection moves every day as the MTM of the CDS changes.

Bloomberg CDSW screen shot- Example- buy \$100mm 5yr CDS at quoted spread of 228bps with a 500bp coupon

- Upfront payment is \$13.3mm from seller of protection to buyer of protection; Total OTL payments of buyer of protection are \$26.7mm, which PV to \$23.7mm; PV of unrecognized cost of protection = \$10.4mm at inception.

GRAB

90 Actions		91 Products		92 View		Credit Default Swap	
Cpty	CDS CNTRPARTY	Client		CCP	OTC	Ticker /	AIG Series Deal#
31) Load		32) Save		33) Share		34) Ticket	
35) Refresh		36) Settings					
Deal				Market			
Buy	Notional	100 MM	USD	Contract	SNAC	Curve Date	05/09/13
REF Entity	International Lease Finance Corp						
Debt Type	Senior	Restructuring	NR				
REF Obligation	US459745GF62	RED Pair Code	49EGB9AE5				
Trade Date	05/09/13	Trd Sprd (bp)	228.0000				
1st Accr Start	03/20/13	Backstop Date	03/10/13				
1st Coupon	06/20/13	Coupon (bp)	500.000				
Pen Coupon	03/20/18	Day Cnt	ACT/360	Freq	Q		
Maturity	5Y 06/20/18	Pay AI	True	Date Gen	I		
Use Curve Recovery Rate	True	Business Days	5D				
Recovery Rate	0.40	Bus Day Adj	1	Amrt	N		
Calculator				ISDA Standard Upfront Model (I)*			
Cash Settled On	05/14/13	Valuation Date	05/09/13				
Cash Calculated On	05/14/13						
Price	112.60148432	Spread DV01	51,530.10				
Principal	-12,601,485	IR DV01	3,224.38				
Accrued (51 Days)	-708,333	Rec Risk (1%)	19,847.00				
Cash Amount	-13,309,818	Def Exposure	72,601,484				
5) View USD ISDA Standard Curve CDS Curve C CMAN Ask 6) View AIG USD Senior Curve (CDSD)							
Recovery Rate		0.40					
Term	Pts Upf	Spread	Prob				
06/20/18	-12.6014	228.0000	0.1788				
View Term Structure							
*This application is based on the ISDA Std Model v1, developed and supported in collaboration with Markit Group Ltd. Australia 61 2 9777 8600 Brazil 5511 3048 4500 Europe 44 20 7330 7500 Germany 49 69 9204 1210 Hong Kong 852 2977 6000 Japan 81 3 3201 8900 Singapore 65 6212 1000 U.S. 1 212 318 2000 Copyright 2013 Bloomberg Finance L.P. SN 655250 6728-964-3 09-May-13 11:49:42 EDT GMT-4:00							

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		Cashflows				Swap
Cpty	CDS					
311						
Deal		Date	Act Cashflow	Disc Factor	Survival Prob	Disc Cashflow
Buy	N	06/20/2013	1,277,777.78	0.99975304	0.9957	1,271,951.82
REF Entity		09/20/2013	1,277,777.78	0.99866285	0.9861	1,258,299.76
Debt Type		12/20/2013	1,263,888.89	0.99695321	0.9767	1,230,627.58
REF Obliga		03/20/2014	1,250,000.00	0.99460152	0.9674	1,202,765.54
		06/20/2014	1,277,777.78	0.99287608	0.9581	1,215,512.74
		09/22/2014	1,305,555.56	0.99281732	0.9486	1,229,616.13
Trade Date		12/22/2014	1,263,888.89	0.99276044	0.9396	1,178,938.88
1st Accr S		03/20/2015	1,222,222.22	0.99270544	0.9309	1,129,481.09
1st Coupou		06/22/2015	1,305,555.56	0.99190524	0.9217	1,193,629.76
Pen Coupo		09/21/2015	1,263,888.89	0.99016375	0.9129	1,142,491.82
		12/21/2015	1,263,888.89	0.98842532	0.9042	1,129,595.68
Maturity		03/21/2016	1,263,888.89	0.98668995	0.8956	1,116,845.10
Use Curve		06/20/2016	1,263,888.89	0.98439617	0.8870	1,103,609.02
Recovery P		09/20/2016	1,277,777.78	0.98129335	0.8785	1,101,483.27
		12/20/2016	1,263,888.89	0.97823387	0.8701	1,075,742.67
Calculator		03/20/2017	1,250,000.00	0.97521740	0.8619	1,050,623.55
Cash Settl		06/20/2017	1,277,777.78	0.97155583	0.8535	1,059,610.03
Cash Calcu		09/20/2017	1,277,777.78	0.96699796	0.8453	1,044,458.41
		Total	26,652,777.78			23,757,910.59
Price		Upfront Premium	10,448,093			
Principal		= Cash Amount(-13,309,818) + Future Discount Cashflows(23,757,911)				
Accrued (\$						
Cash Amou						
*This appli						

Australia 61 2 9777 8600 Brazil 5511 3048 4500 Europe 44 20 7330 7500 Germany 49 69 9204 1210 Hong Kong 852 2977 6000
 Japan 81 3 3201 8900 Singapore 65 6212 1000 U.S. 1 212 318 2000 Copyright 2013 Bloomberg Finance L.P.
 SN 655250 6728-964-3 09-May-13 11:54:02 EDT GMT-4:00

RWA Relief

- Using the above example of a \$250MM 5yr RC, with \$100mm of CDS protection, on a B+ rated credit, 167% Risk-Weighted, assuming ctpy is JPM 2+H, RWA is as follows:

		With MOD-R		Without MOD-R	
		Undrawn	Fully Drawn	Undrawn	Fully Drawn
Auth		250,000,000	250,000,000	250,000,000	250,000,000
OS		-	250,000,000	-	250,000,000
CEE		162,500,000	250,000,000	162,500,000	250,000,000
Hedge		(100,000,000)	(100,000,000)	(100,000,000)	(100,000,000)
Hedge w no MOD-R: 40% haircut		-	-	(40,000,000)	(40,000,000)
Net Hedge		(100,000,000)	(100,000,000)	(60,000,000)	(60,000,000)
Unhedged RWA Long		271,511,427	417,709,888	271,511,427	417,709,888
Hedged					
RWA Long		104,427,472	250,625,933	171,261,054	317,459,515
RWA Counterparty (double default)		21,340,000	21,340,000	21,340,000	21,340,000
Net RWA (existing standards)		125,767,472	271,965,933	192,601,054	338,799,515
RWA Relief (existing standards)		145,743,955	145,743,955	78,910,373	78,910,373
RWA reduction	Cost of Protection	10,400,000	10,400,000	10,400,000	10,400,000
		12.5	12.5	12.5	12.5
		130,000,000	130,000,000	130,000,000	130,000,000
Net RWA proposed		255,767,472	401,965,933	322,601,054	468,799,515
Net RWA Relief (proposed)		15,743,955	15,743,955	(51,089,627)	(51,089,627)