

# Basel Committee on Banking Supervision

LEV

Leverage ratio

LEV30

Exposure measurement

**Version effective as of  
15 Dec 2019**

First version in the format of the consolidated  
framework.



BANK FOR INTERNATIONAL SETTLEMENTS



## **Introduction to the exposure measure**

**30.1** The exposure measure for the leverage ratio should generally follow the accounting value, subject to the following:

- (1) on-balance sheet, non-derivative exposures are included in the exposure measure net of specific provisions or accounting valuation adjustments (eg accounting credit valuation adjustments); and
- (2) netting of loans and deposits is not allowed.

FAQ  
FAQ1

*Are notional and physical cash pooling positions (ie whereby corporate groups combine the credit and debit positions of their various accounts into one account) required to be treated on a gross basis?*

*The Basel III leverage ratio exposure measure treatment of assets that are subject to cash pooling positions (ie whereby corporate groups combine the credit and debit positions of various accounts into one account) must be determined in accordance with the first sentence of [LEV30.1](#). On this basis, the starting point is the exposure value as identified in the applicable accounting framework subject to the additional criteria of [LEV30.1\(2\)](#) and [LEV30.2](#). Hence, the Basel III leverage ratio exposure measure must not be reduced through recognition of collateralisation, guarantees or risk mitigation purchased. Also, possible effects arising from netting of loans and deposits must be reversed, leading to an un-netted (gross) recognition of these exposures in the Basel III leverage ratio exposure measure.*

*“Netting” should, however, be distinguished from physical “settlement”, with the latter referencing the transfer of credit and debit balances into a single account, with the result that these balances are extinguished and transformed into a single balance (ie a single claim on or a single liability to a single legal entity on the basis of a single account). In contrast to “netting”, the criteria of [LEV30.1\(2\)](#) and [LEV30.2](#) do not require the reversal of the effects of physical “settlement”. The resulting single balance as the consequence of physical settlement constitutes the new starting point for establishing the Basel III leverage ratio exposure measure. Note, however, that the condition of “extinguished and transformed into a single balance” is not met when the bank could potentially be held liable for the non-performance of one or multiple participants in the cash pool.*

*To the extent that physical settlement does not extinguish all of the credit and/or debit balances of the participants in the cash pool, in addition to the balance amount in the master account after settlement, banks must include in their Basel III leverage ratio exposure measure any remaining credit balances (ie the “unswept” amounts owed to the institution) in the cash pool on a gross basis.*

*In addition, any off-balance sheet exposures arising from cash pooling products (both notional and physical) must be included in the Basel III leverage ratio exposure measure in accordance with [LEV30.44](#) to [LEV30.53](#).*

**FAQ2** *How should long settlement transactions (LSTs) and failed trades be treated in the Basel III leverage ratio?*

*“Long settlement transactions” (LSTs) and “failed trades” are terms that are in use in [CRE51](#) and [CRE70](#). For the purposes of the Basel III leverage ratio framework, such transactions have to be treated according to their accounting classification. For example, if an LST is classified as a derivative according to the applicable accounting standards, the Basel III leverage ratio exposure measure has to be calculated according to [LEV30.8](#) to [LEV30.32](#). Similarly, if a failed trade is classified as a receivable according to the applicable accounting standards, the exposure measure has to be calculated according to [LEV30.5](#) to [LEV30.7](#) related to “on-balance sheet exposures”. Securities financing transactions that have failed to settle are excluded from the described treatment and their exposure measure must be calculated according to [LEV30.36](#) to [LEV30.43](#) on securities financing transaction exposures.*

- 30.2** Unless specified differently below, banks must not take account of physical or financial collateral, guarantees or other credit risk mitigation techniques to reduce the exposure measure.
- 30.3** With regard to traditional securitisations, an originating bank may exclude securitised exposures from its leverage ratio exposure measure if the securitisation meets the operational requirements for the recognition of risk transference according to [CRE40.24](#). Banks meeting these conditions must include any retained securitisation exposures in their leverage ratio exposure measure. In all other cases, eg traditional securitisations that do not meet the operational requirements for the recognition of risk transference or synthetic securitisations, the securitised exposures must be included in the leverage ratio exposure measure.
- 30.4** At national discretion, and to facilitate the implementation of monetary policies, a jurisdiction may temporarily exempt central bank reserves from the leverage ratio exposure measure in exceptional macroeconomic circumstances. To maintain the same level of resilience provided by the leverage ratio, a jurisdiction applying this discretion must also increase the calibration of the minimum leverage ratio requirement commensurately to offset the impact of exempting central bank reserves. In addition, in order to maintain the comparability and transparency of the Basel III leverage ratio framework, banks will be required to disclose the impact of any temporary exemption alongside ongoing public disclosure of the leverage ratio without application of such exemption.

## On-balance sheet exposures

**30.5** Banks must include all balance sheet assets in their exposure measure, including on-balance sheet derivatives collateral and collateral for securities financing transactions (SFTs), with the exception of on-balance sheet derivative and SFT assets that are covered in [LEV30.8](#) to [LEV30.45](#).<sup>1</sup>

### Footnotes

<sup>1</sup> *Where a bank according to its operative accounting framework recognises fiduciary assets on the balance sheet, these assets can be excluded from the leverage ratio exposure measure provided that the assets meet the IAS 39 criteria for derecognition and, where applicable, IFRS 10 for deconsolidation. When disclosing the leverage ratio, banks must also disclose the extent of such de-recognised fiduciary items as set out in Template LR1 in [DIS80](#).*

### FAQ

**FAQ1** *Where the underlying asset being leased is a tangible asset, should the right-of-use (ROU) asset be included in risk-based capital and leverage ratio denominators?*

*Yes, the ROU asset should be included in the risk-based capital and leverage denominators. The intent of the revisions to the lease accounting standards was to more appropriately reflect the economics of leasing transactions, including both the lessee's obligation to make future lease payments, as well as a ROU asset reflecting the lessee's control over the leased item's economic benefits during the lease term.*

**30.6** However, to ensure consistency, balance sheet assets deducted from Tier 1 capital (as set out in [CAP30](#)) may be deducted from the exposure measure. Two examples follow.

- (1) Where a banking, financial or insurance entity is not included in the regulatory scope of consolidation as set out in [LEV10](#), the amount of any investment in the capital of that entity that is totally or partially deducted from Common Equity Tier 1 (CET1) capital or from Additional Tier 1 capital of the bank following the corresponding deduction approach in [CAP30.29](#) to [CAP30.34](#) may also be deducted from the exposure measure.

- (2) For banks using the internal ratings-based approach to determining capital requirements for credit risk, [CAP30.13](#) requires any shortfall in the stock of eligible provisions relative to expected losses to be deducted from CET1 capital. The same amount may be deducted from the exposure measure.

**30.7** Liability items must not be deducted from the measure of exposure. For example, gains/losses on fair valued liabilities or accounting value adjustments on derivative liabilities due to changes in the bank's own credit risk as described in [CAP30.15](#) must not be deducted from the exposure measure.

## Derivative exposures

**30.8** Derivatives create two types of exposure:

- (1) an exposure arising from the underlying of the derivative contract; and
- (2) a counterparty credit risk (CCR) exposure. The leverage ratio framework uses the method set out below to capture both of these exposure types.

### FAQ

**FAQ1** *Since banks will not encounter CCR with written options under the risk-based capital framework, please clarify whether these kinds of transactions should be included in the Basel III leverage ratio exposure measure.*

*As written options create an exposure, they must be included in the Basel III leverage ratio exposure measure.*

**30.9** Banks must calculate their derivative exposures, including where a bank sells protection using a credit derivative, as the replacement cost (RC)<sup>2</sup> for the current exposure plus an add-on for potential future exposure (PFE), as described in [LEV30.10](#) to [LEV30.11](#). If the derivative exposure is covered by an eligible bilateral netting contract as specified in [LEV30.20](#) to [LEV30.21](#), an alternative treatment may be applied, as set out in [LEV30.23](#) to [LEV30.32](#).<sup>3</sup> Written credit derivatives are subject to an additional treatment, as set out in [LEV30.33](#) to [LEV30.35](#).

## Footnotes

<sup>2</sup> If, under a bank's national accounting standards, there is no accounting measure of exposure for certain derivative instruments because they are held (completely) off-balance sheet, the bank must use the sum of positive fair values of these derivatives as the replacement cost.

<sup>3</sup> Note that cross-product netting is not permitted in determining the leverage ratio exposure measure.

## FAQ

**FAQ1** How should banks perform netting under the leverage ratio for derivatives and SFTs that are included in a cross-product netting agreement?

Consistent with footnote 3 of [LEV30.9](#), netting across product categories (ie derivatives and SFTs) is not permitted for the purpose of determining the Basel III leverage ratio exposure measure. However, where a bank has a cross-product netting agreement in place that meets the eligibility criteria of [LEV30.20](#) to [LEV30.21](#) it may choose to perform netting separately in each product category provided that all other conditions for netting in this product category that are applicable to the Basel III leverage ratio are met.

**30.10** For a single derivative exposure not covered by an eligible bilateral netting contract as specified in [LEV30.20](#) to [LEV30.21](#), the amount to be included in the exposure measure is determined as follows:

$$\text{exposure measure} = \text{replacement cost (RC)} + \text{add on}$$

**30.11** In the formula in [LEV30.10](#):

- (1) "RC" is defined as the replacement cost of the contract (obtained by marking to market), where the contract has a positive value; and
- (2) "add on" is an amount for PFE over the remaining life of the contract calculated by applying an add-on factor to the notional principal amount of the derivative. The add-on factors are included in [LEV30.12](#) and [LEV30.14](#).

**30.12** The following add-on factors apply to financial derivatives, based on residual maturity:



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	Interest rates	Foreign exchange and gold	Equities	Precious metals except gold	Other commodities
One year or less	0.0%	1.0%	6.0%	7.0%	10.0%
Over one year to five years	0.5%	5.0%	8.0%	7.0%	12.0%
Over five years	1.5%	7.5%	10.0%	8.0%	15.0%

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Notes:

1. For contracts with multiple exchanges of principal, the factors are to be multiplied by the number of remaining payments in the contract.
  2. For contracts that are structured to settle outstanding exposures following specified payment dates and where the terms are reset such that the market value of the contract is zero on these specified dates, the residual maturity would be set equal to the time until the next reset date. In the case of interest rate contracts with remaining maturities of more than one year that meet the above criteria, the add-on is subject to a floor of 0.5%.
  3. Forwards, swaps, purchased options and similar derivative contracts not covered by any of the columns in this matrix are to be treated as "other commodities".
  4. No potential future credit exposure would be calculated for single currency floating / floating interest rate swaps; the credit exposure on these contracts would be evaluated solely on the basis of their mark-to-market value.
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**30.13** Supervisors will take care to ensure that add-ons are based on effective rather than apparent notional amounts. In the event that the stated notional amount is leveraged or enhanced by the structure of the transaction, banks must use the effective notional amount when determining PFE.

**30.14** The following add-on factors apply to single-name credit derivatives:

	Protection buyer	Protection seller
<b>Total return swaps</b>		
"Qualifying" reference obligation	5%	5%
"Non-qualifying" reference obligation	10%	10%
<b>Credit default swaps</b>		
"Qualifying" reference obligation	5%	5%**
"Non-qualifying" reference obligation	10%	10%**

There will be no difference depending on residual maturity.

\*\* The protection seller of a credit default swap shall only be subject to the add-on factor where it is subject to closeout upon the insolvency of the protection buyer while the underlying is still solvent. The add-on should then be capped to the amount of unpaid premiums.

## FAQ

**FAQ1** *Single-name credit derivatives have their own add-on factors, as specified in [LEV30.14](#). Should an index credit default swap (CDS) be treated the same or would it be in a different category?*

*For index CDS, banks must use the same PFE add-on factors as they would use for single-name CDS.*

**30.15** Where the credit derivative is a first-to-default transaction, the add-on will be determined by the lowest credit quality underlying the basket, ie if there are any non-qualifying items in the basket, the non-qualifying reference obligation add-on should be used. For second and subsequent nth-to-default transactions, underlying assets should continue to be allocated according to the credit quality, ie the second or, respectively, nth lowest credit quality will determine the add-on for a second-to-default or an nth-to-default transaction, respectively.

**30.16** The "qualifying" category includes securities issued by public sector entities and multilateral development banks, plus other securities that are:

- (1) rated investment grade<sup>4</sup> by at least two credit rating agencies specified by the national authority; or

- (2) rated investment grade by one rating agency and not less than investment grade by any other rating agency specified by the national authority (subject to supervisory oversight); or
- (3) subject to supervisory approval, unrated, but deemed to be or comparable to investment grade credit quality by the reporting bank, and the issuer has securities listed on a recognised exchange.

*Footnotes*

<sup>4</sup> *Eg rated Baa or higher by Moody's and BBB or higher by Standard & Poor's.*

- 30.17** Each supervisory authority will be responsible for monitoring the application of these qualifying criteria, particularly in relation to the last criterion where the initial classification is essentially left to the reporting banks. National authorities will also have discretion to include within the qualifying category debt securities issued by banks in countries which have implemented the current framework, subject to the express understanding that supervisory authorities in such countries undertake prompt remedial action if a bank fails to meet the leverage ratio standards set forth in this framework. Similarly, national authorities will have discretion to include within the qualifying category debt securities issued by securities firms that are subject to equivalent rules.
- 30.18** Furthermore, the "qualifying" category shall include securities issued by institutions that are deemed to be equivalent to investment grade quality and subject to supervisory and regulatory arrangements comparable to those under this framework.
- 30.19** When an eligible bilateral netting contract is in place as specified in [LEV30.20](#) to [LEV30.21](#), the RC for the set of derivative exposures covered by the contract will be the net replacement cost and the add-on will be  $A_{\text{Net}}$  as calculated in [LEV30.22](#) to [LEV30.23](#).
- 30.20** For the purposes of the leverage ratio, the following will apply:
- (1) Banks may net transactions subject to novation under which any obligation between a bank and its counterparty to deliver a given currency on a given value date is automatically amalgamated with all other obligations for the same currency and value date, legally substituting one single amount for the previous gross obligations.

- (2) Banks may also net transactions subject to any legally valid form of bilateral netting not covered in [LEV30.20\(1\)](#), including other forms of novation.
- (3) In both cases [LEV30.20\(1\)](#) and [LEV30.20\(2\)](#), a bank will need to satisfy its national supervisors that it has:
  - (a) a netting contract or agreement with the counterparty that creates a single legal obligation, covering all included transactions, such that the bank would have either a claim to receive or obligation to pay only the net sum of the positive and negative mark-to-market values of included individual transactions in the event a counterparty fails to perform due to any of the following: default, bankruptcy, liquidation or similar circumstances;
  - (b) written and reasoned legal opinions that, in the event of a legal challenge, the relevant courts and administrative authorities would find the bank's exposure to be such a net amount under:
    - (i) the law of the jurisdiction in which the counterparty is chartered and, if the foreign branch of a counterparty is involved, then also under the law of jurisdiction in which the branch is located;
    - (ii) the law that governs the individual transactions; and
    - (iii) the law that governs any contract or agreement necessary to effect the netting. The national supervisor, after consultation when necessary with other relevant supervisors, must be satisfied that the netting is enforceable under the laws of each of the relevant jurisdictions;<sup>5</sup> and
  - (c) procedures in place to ensure that the legal characteristics of netting arrangements are kept under review in the light of possible changes in relevant law.

#### *Footnotes*

<sup>5</sup> *Thus, if any of these supervisors are dissatisfied about enforceability under its laws, the netting contract or agreement will not meet the condition and neither counterparty could obtain supervisory benefit.*

**30.21** Contracts containing walkaway clauses will not be eligible for netting for the purpose of calculating the leverage ratio requirements pursuant to this framework. A walkaway clause is a provision that permits a non-defaulting counterparty to make only limited payments, or no payment at all, to the estate of a defaulter, even if the defaulter is a net creditor.

**30.22** Credit exposure on bilaterally netted forward transactions will be calculated as the sum of the net mark-to-market replacement cost, if positive, plus an add-on based on the notional underlying principal. The add-on for netted transactions ( $A_{Net}$ ) will equal the weighted average of the gross add-on ( $A_{Gross}$ ) and the gross add-on adjusted by the ratio of net current replacement cost to gross current replacement cost (NGR). This is expressed through the following formula:

$$A_{Net} = 0.4 \times A_{Gross} + 0.6 \times NGR \times A_{Gross}$$

**30.23** In the formula in [LEV30.22](#):

- (1) "NGR" is the level of net replacement cost/level of gross replacement cost for transactions subject to legally enforceable netting agreements.<sup>6</sup>
- (2) " $A_{Gross}$ " is the sum of individual add-on amounts (calculated by multiplying the notional principal amount by the appropriate add-on factors set out in [LEV30.12](#) to [LEV30.18](#)) of all transactions subject to legally enforceable netting agreements with one counterparty.

#### Footnotes

<sup>6</sup> National authorities may permit a choice of calculating the NGR on a counterparty by counterparty or on an aggregate basis for all transactions that are subject to legally enforceable netting agreements. If supervisors permit a choice of methods, the method chosen by the institution is to be used consistently. Under the aggregate approach, net negative current exposures to individual counterparties cannot be used to offset net positive current exposures to others, ie for each counterparty the net current exposure used in calculating the NGR is the maximum of the net replacement cost or zero. Note that under the aggregate approach, the NGR is to be applied individually to each legally enforceable netting agreement so that the credit equivalent amount will be assigned to the appropriate counterparty risk weight category.

- 30.24** For the purposes of calculating potential future credit exposure to a netting counterparty for forward foreign exchange contracts and other similar contracts in which the notional principal amount is equivalent to cash flows, the notional principal is defined as the net receipts falling due on each value date in each currency. The reason for this is that offsetting contracts in the same currency maturing on the same date will have lower potential future exposure as well as lower current exposure.
- 30.25** Collateral received in connection with derivative contracts has two countervailing effects on leverage:
- (1) it reduces counterparty exposure; but
  - (2) it can also increase the economic resources at the disposal of the bank, as the bank can use the collateral to leverage itself.
- 30.26** Collateral received in connection with derivative contracts does not necessarily reduce the leverage inherent in a bank's derivatives position, which is generally the case if the settlement exposure arising from the underlying derivative contract is not reduced. As a general rule, collateral received may not be netted against derivative exposures whether or not netting is permitted under the bank's operative accounting or risk-based framework. Hence, when calculating the exposure amount by applying [LEV30.9](#) to [LEV30.23](#), a bank must not reduce the exposure amount by any collateral received from the counterparty.
- 30.27** Similarly, with regard to collateral provided, banks must gross up their exposure measure by the amount of any derivatives collateral provided where the provision of that collateral has reduced the value of their balance sheet assets under their operative accounting framework.
- 30.28** In the treatment of derivative exposures for the purpose of the leverage ratio, the cash portion of variation margin exchanged between counterparties may be viewed as a form of pre-settlement payment, if the following conditions are met:
- (1) For trades not cleared through a qualifying central counterparty (QCCP)<sup>7</sup> the cash received by the recipient counterparty is not segregated.
  - (2) Variation margin is calculated and exchanged on a daily basis based on mark-to-market valuation of derivatives positions.
  - (3) The cash variation margin is received in the same currency as the currency of settlement of the derivative contract.
  - (4) Variation margin exchanged is the full amount that would be necessary to fully extinguish the mark-to-market exposure of the derivative subject to the threshold and minimum transfer amounts applicable to the counterparty.

- (5) Derivatives transactions and variation margins are covered by a single master netting agreement (MNA)<sup>8,9</sup> between the legal entities that are the counterparties in the derivatives transaction. The MNA must explicitly stipulate that the counterparties agree to settle net any payment obligations covered by such a netting agreement, taking into account any variation margin received or provided if a credit event occurs involving either counterparty. The MNA must be legally enforceable and effective in all relevant jurisdictions, including in the event of default and bankruptcy or insolvency.

#### Footnotes

<sup>7</sup> A QCCP is defined as in [CRE50.3](#).

<sup>8</sup> A Master MNA may be deemed to be a single MNA for this purpose.

<sup>9</sup> To the extent that the criteria in this paragraph include the term "master netting agreement", this term should be read as including any "netting agreement" that provides legally enforceable rights of offsets. This is to take account of the fact that for netting agreements employed by central counterparties (CCPs), no standardisation has currently emerged that would be comparable with respect to over-the-counter netting agreements for bilateral trading.

#### FAQ

FAQ1 *What does currency of settlement mean?*

*Currency of settlement means any currency of settlement specified in the derivative contract, governing qualifying MNA, or the credit support annex to the qualifying MNA. In this context, MNA should be read as including any netting agreement that provides legally enforceable rights of offsets. This is to take account of the fact that, for netting agreements employed by CCPs, no standardisation has currently emerged that would be comparable with respect to over-the-counter netting agreements for bilateral trading.*

FAQ2 *What standards are banks expected to meet for MNAs to be legally enforceable and effective?*

*An MNA is deemed to meet this criterion if it satisfies the conditions in [LEV30.20\(3\)](#) and [LEV30.21](#).*

FAQ3 *The condition that cash variation margin must be calculated and exchanged on a daily basis may not be met for certain types of cleared*

*derivatives (eg energy derivatives). Will any exception for the daily calculation/exchange requirement be permitted for these types of transactions?*

*To meet this criterion, derivative positions must be valued daily and cash variation margin must be transferred daily to the counterparty or to the counterparty's account, as appropriate.*

**FAQ4** *In the case where cash variation margin is exchanged the next morning to meet end-of-day market values, would the requirement of [LEV30.28\(4\)](#) still be met?*

*Cash variation margin exchanged on the morning of the subsequent trading day based on the previous, end-of-day market values would meet this criterion, provided that the variation margin exchanged is the full amount that would be necessary to fully extinguish the mark-to-market exposure of the derivative subject to applicable threshold and minimum transfer amounts.*

**FAQ5** *What is meant in [LEV30.28](#) where it states that the cash received by the recipient counterparty is not segregated?*

*Cash variation margin would satisfy the non-segregation criterion if the recipient counterparty has no restrictions on the ability to use the cash received (ie the cash variation margin received is used as its own cash).*

**FAQ6** *Where a bank provides cash variation margin, it would not necessarily have any knowledge of whether its counterparty has segregated the cash or not. What standard would need to be met to fulfil this criterion?*

*This criterion would be met if the cash received by the recipient counterparty is not required to be segregated by law, regulation or any agreement with the counterparty.*

**30.29** If the conditions in [LEV30.28](#) are met, the cash portion of variation margin received may be used to reduce the replacement cost portion of the leverage ratio exposure measure, and the receivables assets from cash variation margin provided may be deducted from the leverage ratio exposure measure as follows:



- (1) In the case of cash variation margin received, the receiving bank may reduce the replacement cost (but not the add-on portion) of the exposure amount of the derivative asset by the amount of cash received if the positive mark-to-market value of the derivative contract(s) has not already been reduced by the same amount of cash variation margin received under the bank's operative accounting standard.
- (2) In the case of cash variation margin provided to a counterparty, the posting bank may deduct the resulting receivable from its leverage ratio exposure measure, where the cash variation margin has been recognised as an asset under the bank's operative accounting framework.

**30.30** Cash variation margin may not be used to reduce the PFE amount (including the calculation of the net-to-gross ratio, or NGR, as defined in [LEV30.23](#)).

FAQ

FAQ1 [LEV30.30](#) mentions that cash variation margin may not be used in the calculation of the NGR. Is this also the case when the conditions of [LEV30.28](#) are met?

*Cash variation margin may not be used to reduce the NGR, even if the conditions in [LEV30.28](#) are fully met. Specifically, in the calculation of the NGR, cash variation margin may not reduce the net replacement cost (ie the numerator of the NGR) nor the gross replacement cost (ie the denominator of the NGR).*

**30.31** Where a bank acting as clearing member (CM)<sup>10</sup> offers clearing services to clients, the clearing member's trade exposures<sup>11</sup> to the central counterparty (CCP) that arise when the CM is obligated to reimburse the client for any losses suffered due to changes in the value of its transactions in the event that the CCP defaults, must be captured by applying the same treatment that applies to any other type of derivatives transactions. However, if the CM, based on the contractual arrangements with the client, is not obligated to reimburse the client for any losses suffered due to changes in the value of its transactions in the event that a QCCP defaults, the CM need not recognise the resulting trade exposures to the QCCP in the leverage ratio exposure measure.

## Footnotes

10 For the purposes of this paragraph, a CM is defined as in [CRE50.4](#).

11 For the purposes of [LEV30.31](#) and [LEV30.32](#), "trade exposures" includes initial margin irrespective of whether or not it is posted in a manner that makes it remote from the insolvency of the CCP.

## FAQ

**FAQ1** Can an entity affiliated to the bank acting as a CM be considered a client in the sense and for the purposes of [LEV30.31](#)?

*An entity affiliated to the bank acting as a CM may be considered a client for the purposes of [LEV30.31](#) if it is outside the relevant scope of regulatory consolidation at the level at which the Basel III leverage ratio is applied. In contrast, if an affiliate entity falls within the regulatory scope of consolidation, the trade between the affiliate entity and the CM is eliminated in the course of consolidation, but the CM still has a trade exposure to the qualifying central counterparty, which will be considered proprietary and the exemption in [LEV30.31](#) no longer applies.*

**30.32** Where a client enters directly into a derivatives transaction with the CCP and the CM guarantees the performance of its clients' derivative trade exposures to the CCP, the bank acting as the clearing member for the client to the CCP must calculate its related leverage ratio exposure resulting from the guarantee as a derivative exposure as set out in [LEV30.9](#) to [LEV30.30](#), as if it had entered directly into the transaction with the client, including with regard to the receipt or provision of cash variation margin.

**30.33** In addition to the CCR exposure arising from the fair value of the contracts, written credit derivatives create a notional credit exposure arising from the creditworthiness of the reference entity. The Committee therefore believes that it is appropriate to treat written credit derivatives consistently with cash instruments (eg loans, bonds) for the purposes of the exposure measure.

**30.34** In order to capture the credit exposure to the underlying reference entity, in addition to the above CCR treatment for derivatives and related collateral, the effective notional amount<sup>12</sup> referenced by a written credit derivative is to be included in the exposure measure. The effective notional amount of a written credit derivative may be reduced by any negative change in fair value amount that has been incorporated into the calculation of Tier 1 capital with respect to

the written credit derivative. The resulting amount may be further reduced by the effective notional amount of a purchased credit derivative on the same reference name,<sup>13,14</sup> provided:

- (1) the credit protection purchased is on a reference obligation which ranks pari passu with or is junior to the underlying reference obligation of the written credit derivative in the case of single name credit derivatives;<sup>15</sup> and
- (2) the remaining maturity of the credit protection purchased is equal to or greater than the remaining maturity of the written credit derivative.

## Footnotes

[12](#)

*The effective notional amount is obtained by adjusting the notional amount to reflect the true exposure of contracts that are leveraged or otherwise enhanced by the structure of the transaction.*

[13](#)

*Two reference names are considered identical only if they refer to the same legal entity. For single-name credit derivatives, protection purchased that references a subordinated position may offset protection sold on a more senior position of the same reference entity as long as a credit event on the senior reference asset would result in a credit event on the subordinated reference asset. Protection purchased on a pool of reference entities may offset protection sold on individual reference names if the protection purchased is economically equivalent to buying protection separately on each of the individual names in the pool (this would, for example, be the case if a bank were to purchase protection on an entire securitisation structure). If a bank purchases protection on a pool of reference names, but the credit protection does not cover the entire pool (ie the protection covers only a subset of the pool, as in the case of an nth-to-default credit derivative or a securitisation tranche), then offsetting is not permitted for the protection sold on individual reference names. However, such purchased protections may offset sold protections on a pool provided the purchased protection covers the entirety of the subset of the pool on which protection has been sold. In other words, offsetting may only be recognised when the pool of reference entities and the level of subordination in both transactions are identical.*

[14](#)

*The effective notional amount of a written credit derivative may be reduced by any negative change in fair value reflected in the bank's Tier 1 capital provided the effective notional amount of the offsetting purchased credit protection is also reduced by any resulting positive change in fair value reflected in Tier 1 capital. Where a bank buys credit protection through a total return swap and records the net payments received as net income, but does not record offsetting deterioration in the value of the written credit derivative (either through reductions in fair value or by an addition to reserves) reflected in Tier 1 capital, the credit protection will not be recognised for the purpose of offsetting the effective notional amounts related to written credit derivatives.*

[15](#)

*For tranching products, the purchased protection must be on a reference obligation with the same level of seniority.*

FAQ  
FAQ1

What is meant by “negative change in fair value”?

*A “negative change in fair value” is meant to refer to a negative fair value of a credit derivative that is recognised in Tier 1 capital. This treatment is consistent with the Committee’s communicated rationale that the effective notional amounts included in the exposure measure may be capped at the level of the maximum potential loss, which means that the maximum potential loss at the reporting date is the notional amount of the credit derivative minus any negative fair value that has already reduced Tier 1 capital.*

*For example, if a written credit derivative had a positive fair value of 20 on one date and has a negative fair value of 10 on a subsequent reporting date, the effective notional amount of the credit derivative may be reduced by 10. The effective notional amount cannot be reduced by 30. However, if at the subsequent reporting date the credit derivative has a positive fair value of 5, the effective notional amount cannot be reduced at all.*

FAQ2 *Does the term “written credit derivative” as used in [LEV30.34](#) apply exclusively to written credit default swaps (CDS) and total return swaps?*

*For the purposes of [LEV30.34](#), the term “written credit derivative” refers to a broad range of credit derivatives through which a bank effectively provides credit protection and is not limited solely to CDS and total return swaps.*

FAQ3 *Please confirm the following interpretations of the first half of [LEV30](#) footnote 14: for the purposes of offsetting, (a) when a purchased credit derivative transaction exists, the effective notional amount of the written credit derivative may be reduced by any negative change in fair value reflected in Tier 1 capital provided that the effective notional amount of the offsetting purchased credit derivative is also reduced by any resulting positive change in fair value reflected in Tier 1 capital; and (b) when a purchased credit derivative transaction exists, and the effective notional amount of the purchased credit derivative has not been reduced by any resulting positive change in fair value reflected in Tier 1 capital, then the effective notional amount of the written credit derivative may only be offset if the effective notional amount of that written credit derivative has not been reduced by any negative change in fair value reflected in Tier 1 capital.*

*The interpretations in the question are correct.*

**FAQ4** *Would tranching junior position hedges through credit derivatives that meet the following criteria be eligible for offsetting: (i) the junior and senior tranches are on the same pool of reference entities; (ii) the level of seniority of the debt of each of the reference entities in the portfolio is the same; (iii) the designated credit events for the credit protection sold on the senior tranche, and purchased on the junior tranche, are the same; and (iv) the anticipated economic recovery on the junior tranching protection purchased is equal to or greater than the anticipated economic loss on the senior tranching protection sold?*

*No. As described in [LEV30](#) footnote 13, credit protection purchased through a credit derivative on a pool of reference assets cannot offset a written credit derivative unless both instruments reference the same pool of reference assets and the level of subordination of both transactions is identical.*

**FAQ5** *If a bank writes credit protection through a credit derivative for a client and enters into a back-to-back trade with a CCP whereby it purchases credit protection through a credit derivative on the same name, may that purchased credit protection be used to offset the written protection for the purposes of the Basel III leverage ratio?*

*Yes. A bank may offset the effective notional amount of a written credit derivative sold to a client by means of a credit derivative on the same underlying name purchased from a CCP provided that the criteria in [LEV30.34](#) are met.*

**30.35** Since written credit derivatives are included in the exposure measure at their effective notional amounts, and are also subject to add-on amounts for PFE, the exposure measure for written credit derivatives may be overstated. Banks may therefore choose to deduct the individual PFE add-on amount relating to a written credit derivative (which is not offset according to [LEV30.34](#) and whose effective notional amount is included in the exposure measure) from their gross add-on in [LEV30.9](#) to [LEV30.23](#).<sup>16</sup>

## Footnotes

[16](#)

*In these cases, where effective bilateral netting contracts are in place, and when calculating  $A_{Net} = 0.4 \cdot A_{Gross} + 0.6 \cdot NGR \cdot A_{Gross}$  as per [LEV30.9](#) to [LEV30.23](#),  $A_{Gross}$  may be reduced by the individual add-on amounts (ie notionals multiplied by the appropriate add-on factors) which relate to written credit derivatives whose notional amounts are included in the leverage ratio exposure measure. However, no adjustments must be made to NGR. Where effective bilateral netting contracts are not in place, the PFE add-on may be set to zero in order to avoid the double-counting described in this paragraph.*

## FAQ

FAQ1

*What does the phrase “which is not offset according to [LEV30.34](#)” in [LEV30.35](#) mean? Does it refer to the case where neither of the two deductions in the effective notional amount from an offsetting purchased credit derivative, detailed in [LEV30.34](#), is included?*

*The condition in [LEV30.35](#) regarding the removal of a PFE add-on associated with a written credit derivative from the Basel III leverage ratio exposure measure refers only to the offset by credit protection purchased through a credit derivative according to [LEV30.34](#) and not to the reduction of the effective notional amount as a result of the negative change in fair value that has reduced Tier 1 capital.*

## Securities financing transaction exposures

**30.36** SFTs<sup>[17](#)</sup> are included in the exposure measure according to the treatment described below. The treatment recognises that secured lending and borrowing in the form of SFTs is an important source of leverage, and ensures consistent international implementation by providing a common measure for dealing with the main differences in the operative accounting frameworks.

## Footnotes

[17](#)

*SFTs are transactions such as repurchase agreements, reverse repurchase agreements, security lending and borrowing, and margin lending transactions, where the value of the transactions depends on market valuations and the transactions are often subject to margin agreements.*

**30.37** For a bank acting as principal, the sum of the amounts below is to be included in the leverage ratio exposure measure.

- (1) Gross SFT assets<sup>18</sup> recognised for accounting purposes (ie with no recognition of accounting netting),<sup>19</sup> adjusted as follows:
  - (a) excluding from the exposure measure the value of any securities received under an SFT, where the bank has recognised the securities as an asset on its balance sheet;<sup>20</sup> and
  - (b) cash payables and cash receivables in SFTs with the same counterparty may be measured net if all the following criteria are met:
    - (i) transactions have the same explicit final settlement date;
    - (ii) the right to set off the amount owed to the counterparty with the amount owed by the counterparty is legally enforceable both currently in the normal course of business and in the event of default, insolvency and bankruptcy; and
    - (iii) the counterparties intend to settle net, settle simultaneously, or the transactions are subject to a settlement mechanism that results in the functional equivalent of net settlement, that is, the cash flows of the transactions are equivalent, in effect, to a single net amount on the settlement date. To achieve such equivalence, both transactions are settled through the same settlement system and the settlement arrangements are supported by cash and/or intraday credit facilities intended to ensure that settlement of both transactions will occur by the end of the business day and the linkages to collateral flows do not result in the unwinding of net cash settlement.<sup>21</sup>



(2) A measure of CCR calculated as the current exposure without an add-on for PFE, calculated as follows:

- (a) Where a qualifying MNA<sup>22</sup> is in place, the current exposure ( $E^*$ ) is the greater of zero and the total fair value of securities and cash lent to a counterparty for all transactions included in the qualifying MNA ( $\sum E_i$ ), less the total fair value of cash and securities received from the counterparty for those transactions ( $\sum C_i$ ). This is illustrated in the following formula:

$$E^* = \max\left(0, \left(\sum E_i - \sum C_i\right)\right)$$

- (b) Where no qualifying MNA is in place, the current exposure for transactions with a counterparty must be calculated on a transaction by transaction basis: that is, each transaction  $i$  is treated as its own netting set, as shown in the following formula:

$$E^* = \max\left(0, \left(E_i - C_i\right)\right)$$

## Footnotes

- [18](#) *For SFT assets subject to novation and cleared through QCCPs, “gross SFT assets recognised for accounting purposes” are replaced by the final contractual exposure, given that pre-existing contracts have been replaced by new legal obligations through the novation process.*
- [19](#) *Gross SFT assets recognised for accounting purposes must not recognise any accounting netting of cash payables against cash receivables (eg as currently permitted under the IFRS and US GAAP accounting frameworks). This regulatory treatment has the benefit of avoiding inconsistencies from netting which may arise across different accounting regimes.*
- [20](#) *This may apply, for example, under US GAAP where securities received under an SFT may be recognised as assets if the recipient has the right to rehypothecate but has not done so.*
- [21](#) *This latter condition ensures that any issues arising from the securities leg of the SFTs do not interfere with the completion of the net settlement of the cash receivables and payables.*
- [22](#) *A “qualifying” MNA is one that meets the requirements under [LEV30.38](#) to [LEV30.39](#).*

FAQ  
FAQ1

LEV30.37(1)(b)(iii) requires that the linkages to collateral flows between a reverse repo and repo settled on the same day not result in the unwinding of net cash settlement. What is meant by this requirement and what is the standard for meeting it? How should one interpret LEV30 footnote 21? Could you provide further clarity on this point, and examples of settlement system facilities that would be acceptable to qualify for netting and any that would not? Can the Basel Committee define in more detail what is meant by "net settlement" as described in LEV30.37(1)(b)(iii)? More specifically, does a transaction that has "failed" impact the ability of that transaction to be netted?

LEV30.37(1)(b)(iii) and footnote 21 set out necessary requirements for settlement mechanisms which are used to settle cash payables and cash receivables in SFTs with the same counterparty in order to offset the cash payables against the cash receivables. Subject to the criteria of LEV30.37(1)(b)(i) and LEV30.37(1)(b)(ii) also being met, the requirements are that the transactions are subject to a settlement mechanism that results in the functional equivalence of net settlement, ie the cash flows of the transactions are equivalent, in effect, to a single net amount on the settlement date. To achieve such equivalence, all transactions must be settled through the same settlement mechanism. The failure of any single securities transaction in the settlement mechanism should delay settlement of only the matching cash leg or create an obligation to the settlement mechanism, supported by an associated credit facility.

Further to the requirements set out in LEV30.37(1)(b)(iii) and footnote 21, if there is a failure of the securities leg of a transaction in such a mechanism at the end of the window for settlement in the settlement mechanism, then this transaction and its matching cash leg must be split out from the netting set and treated gross for the purposes of the Basel III leverage ratio exposure measure.

Specifically, the criteria in LEV30.37(1)(b)(iii) and footnote 21 are not intended to preclude a delivery-versus-payment settlement mechanism or other type of settlement mechanism, provided that the settlement mechanism meets the functional requirements set out in LEV30.37(1)(b)(iii). For example, a settlement mechanism may meet these functional requirements if any failed transaction (that is, the securities that failed to transfer and the related cash receivable or payable) can be re-entered in the settlement mechanism until they are settled.

FAQ2 How should SFTs with no explicit end date but which can be unwound at any time by any counterparty be treated?

*An SFT with no explicit end date but which can be unwound at any time by any counterparty (eg open repos) is not eligible for Basel III leverage ratio netting of SFTs, as it does not meet the condition set out in [LEV30.37\(1\)\(b\)\(i\)](#). This condition requires that, for Basel III leverage ratio netting, transactions must have the same explicit final settlement date.*

**FAQ3** *The Basel III leverage ratio framework refers to the “final contractual exposure” as a replacement for “gross SFT assets recognised for accounting purposes” for SFT assets cleared through QCCPs. Could you please define “final contractual exposure”?*

*“Final contractual exposure” as set out in [LEV30](#) footnote 18 refers to the exposure to the QCCP after the process of novation has been applied. However, banks can only net cash receivables and cash payables with a QCCP if the criteria in [LEV30.37\(1\)](#) are met. Any other netting permitted by the QCCP is not permitted for the purposes of the Basel III leverage ratio.*

**FAQ4** *Please clarify whether [LEV30.37\(1\)\(b\)\(ii\)](#) refers to the default, insolvency and bankruptcy of the counterparty or also of the reporting entity.*

*[LEV30.37\(1\)\(b\)\(ii\)](#) provides that, for the purpose of measuring SFT assets on a net basis, “the right to set off the amount owed to the counterparty with the amount owed by the counterparty is legally enforceable both currently in the normal course of business and in the event of: (i) default; (ii) insolvency; and (iii) bankruptcy”. The references to the events of default, insolvency and bankruptcy apply to such events occurring at the counterparty, not at the reporting entity.*

**FAQ5** *When banks enter into repo transactions with customers, must the securities that banks deposit at triparty repo agents as collateral be considered as “securities lent to a counterparty” and therefore be included in the exposure (E) under [LEV30.37\(2\)](#)?*

*For the purposes of [LEV30.37\(2\)](#), the term “counterparty” includes not only the counterparty of bilateral repo transactions but also triparty repo agents that receive collateral in deposit and manage the collateral in the case of triparty repo transactions. Therefore, securities deposited at triparty repo agents are included in “total value of securities and cash lent to a counterparty” (E) under [LEV30.37\(2\)](#), up to the amount effectively lent to the counterparty in a repo transaction. However, excess collateral that has been deposited at triparty repo agents but*

*has not yet been lent out in specific repo transactions should be excluded.*

**30.38** The effects of bilateral netting agreements for covering SFTs will be recognised on a counterparty by counterparty basis if the agreements are legally enforceable in each relevant jurisdiction upon the occurrence of an event of default and regardless of whether the counterparty is insolvent or bankrupt. In addition, netting agreements must:

- (1) provide the non-defaulting party with the right to terminate and close out in a timely manner all transactions under the agreement upon an event of default, including in the event of insolvency or bankruptcy of the counterparty;
- (2) provide for the netting of gains and losses on transactions (including the value of any collateral) terminated and closed out under it so that a single net amount is owed by one party to the other;
- (3) allow for the prompt liquidation or setoff of collateral upon the event of default; and
- (4) be, together with the rights arising from provisions required in [LEV30.38\(1\)](#) and [LEV30.38\(3\)](#) above, legally enforceable in each relevant jurisdiction upon the occurrence of an event of default regardless of the counterparty's insolvency or bankruptcy.

**30.39** Netting across SFT positions held in the banking book and trading book will only be recognised when the netted transactions fulfil the following conditions:

- (1) all transactions are marked to market daily; and
- (2) the collateral instruments used in the transactions are recognised as eligible financial collateral in the banking book.

**30.40** Leverage may remain with the lender of the security in an SFT whether or not sale accounting is achieved under the operative accounting framework. As such, where sale accounting is achieved for an SFT under the bank's operative accounting framework, the bank must reverse all sales-related accounting entries, and then calculate its exposure as if the SFT had been treated as a financing transaction under the operative accounting framework (ie the bank must include the sum of amounts in [LEV30.37\(1\)](#) and [LEV30.37\(2\)](#) for such an SFT) for the purposes of determining its exposure measure.

**30.41** A bank acting as agent in an SFT generally provides an indemnity or guarantee to only one of the two parties involved, and only for the difference between the

value of the security or cash its customer has lent and the value of collateral the borrower has provided. In this situation, the bank is exposed to the counterparty of its customer for the difference in values rather than to the full exposure to the underlying security or cash of the transaction (as is the case where the bank is one of the principals in the transaction). Where the bank does not own/control the underlying cash or security resource, that resource cannot be leveraged by the bank.

FAQ

FAQ1

*[LEV30.41](#) states that a bank agent generally provides indemnity or guarantee to only one of the two parties involved. Does this mean that the treatments as set out in [LEV30.42](#) and [LEV30.43](#) apply only to this case? If so, what is the treatment for the case where the bank agent provides guarantee to both parties?*

*[LEV30.41](#) to [LEV30.43](#) explains the treatment of SFTs where a bank acts as an agent between two parties of the transaction. It is assumed that an agent bank generally provides an indemnity or guarantee to only one party of the transaction and only for the difference between the cash/securities lent and the collateral borrowed.*

*If an agent bank provides an indemnity or guarantee to both parties involved in an SFT (ie securities lender and securities borrower), it must calculate its Basel III leverage ratio exposure measure in accordance with [LEV30.41](#) to [LEV30.43](#) separately for each party involved in that transaction.*

**30.42** Where a bank acting as agent in an SFT provides an indemnity or guarantee to a customer or counterparty for any difference between the value of the security or cash the customer has lent and the value of collateral the borrower has provided, then the bank will be required to calculate its exposure measure by applying only [LEV30.37\(2\)](#).<sup>23</sup>

## Footnotes

23

*Where, in addition to the conditions in [LEV30.41](#) to [LEV30.43](#), a bank acting as an agent in an SFT does not provide an indemnity or guarantee to any of the involved parties, the bank is not exposed to the SFT and therefore need not recognise those SFTs in its exposure measure.*

- 30.43** A bank acting as agent in an SFT and providing an indemnity or guarantee to a customer or counterparty will be considered eligible for the exceptional treatment set out in [LEV30.42](#) only if the bank's exposure to the transaction is limited to the guaranteed difference between the value of the security or cash its customer has lent and the value of the collateral the borrower has provided. In situations where the bank is further economically exposed (ie beyond the guarantee for the difference) to the underlying security or cash in the transaction, 24 a further exposure equal to the full amount of the security or cash must be included in the exposure measure.

## Footnotes

24

*For example, due to the bank managing collateral received in the bank's name or on its own account rather than on the customer's or borrower's account (eg by on-lending or managing unsegregated collateral, cash or securities).*

## FAQ

FAQ1

*Please clarify the application of [LEV30](#) footnote 24 to omnibus accounts that are used by agent lenders to hold segregated client collateral.*

*Under the condition that the bank calculates the exposure on a client by client basis, for the purposes of the Basel III leverage ratio exposure measure it does not matter how the bank elects to categorise its client collateral provided that client collateral is segregated from the bank's proprietary assets and other relevant criteria, as described in [LEV30.42](#) to [LEV30.43](#), are met. Under those circumstances, [LEV30](#) footnote 24 does not apply to omnibus accounts that are used by agent lenders to hold and manage client collateral segregated from the agent bank's own assets.*

## Off-balance sheet items

- 30.44** This section explains the incorporation of off-balance sheet items as defined in the Basel II framework into the leverage ratio exposure measure. Off-balance sheet items include commitments (including liquidity facilities), whether or not unconditionally cancellable, direct credit substitutes, acceptances, standby letters of credit and trade letters of credit.
- 30.45** For the purpose of determining the exposure amount of off-balance sheet items for the leverage ratio, credit conversion factors (CCFs) set out in [LEV30.46](#) to [LEV30.53](#) must be applied to the notional amount.<sup>25</sup>

### Footnotes

<sup>25</sup>

*These correspond to the CCFs of the standardised approach for credit risk under [CRE20](#), subject to a floor of 10%. The floor of 10% will affect commitments that are unconditionally cancellable at any time by the bank without prior notice, or that effectively provide for automatic cancellation due to deterioration in a borrower's creditworthiness. These may receive a 0% CCF under the risk-based capital framework.*

- 30.46** Commitments other than securitisation liquidity facilities with an original maturity up to one year and commitments with an original maturity over one year will receive a CCF of 20% and 50%, respectively. However, any commitments that are unconditionally cancellable at any time by the bank without prior notice, or that effectively provide for automatic cancellation due to deterioration in a borrower's creditworthiness, will receive a 10% CCF.<sup>26</sup>

### Footnotes

<sup>26</sup>

*In certain countries, retail commitments are considered unconditionally cancellable if the terms permit the bank to cancel them to the full extent allowable under consumer protection and related legislation.*

- 30.47** Direct credit substitutes, eg general guarantees of indebtedness (including standby letters of credit serving as financial guarantees for loans and securities) and acceptances (including endorsements with the character of acceptances) will receive a CCF of 100%.
- 30.48** Forward asset purchases, forward deposits and partly paid shares and securities, which represent commitments with certain drawdown, will receive a CCF of 100%.



## FAQ

### FAQ1

*What is the treatment of forward forward deposits, deliverable bond futures and equity forward purchases under the Basel III leverage ratio framework?*

*[LEV30.44](#) to [LEV30.45](#) provide that off-balance sheet items are included in the Basel III leverage ratio exposure measure using the CCFs as set out in [LEV30.46](#) to [LEV30.53](#), subject to the 10% CCF floor. [LEV30.48](#) provides that forward asset purchases, forward forward deposits and partly paid shares and securities, which represent commitments with certain drawdown, will receive a CCF of 100%.*

*The commitment to place or accept forward forward deposits under the Basel III leverage ratio framework must be treated consistently with the treatment for these commitments under the risk-based capital framework. Specifically, the commitment to place forward forward deposits is subject to a 100% CCF, as provided in [LEV30.48](#), while the commitment to accept forward forward deposits is treated as an interest rate derivative. In addition, deliverable bond futures and over-the-counter equity forward purchases must be treated as derivatives.*

- 30.49** Certain transaction-related contingent items (eg performance bonds, bid bonds, warranties and standby letters of credit related to particular transactions) will receive a CCF of 50%.
- 30.50** Note issuance facilities and revolving underwriting facilities will receive a CCF of 50%.
- 30.51** For short-term self-liquidating trade letters of credit arising from the movement of goods (eg documentary credits collateralised by the underlying shipment), a 20% CCF will be applied to both issuing and confirming banks.
- 30.52** Where there is an undertaking to provide a commitment on an off-balance sheet item, banks are to apply the lower of the two applicable CCFs.
- 30.53** All off-balance sheet securitisation exposures, except an eligible liquidity facility or an eligible servicer cash advance facility as set out below, will receive a CCF of 100%. All eligible liquidity facilities will receive a CCF of 50%. At national discretion, undrawn servicer cash advances or facilities that are unconditionally cancellable without prior notice may be eligible for a 10% CCF.

- (1) Banks are permitted to treat off-balance sheet securitisation exposures as eligible liquidity facilities if the following minimum requirements are satisfied:
  - (a) The facility documentation must clearly identify and limit the circumstances under which it may be drawn. Draws under the facility must be limited to the amount that is likely to be repaid fully from the liquidation of the underlying exposures and any seller-provided credit enhancements. In addition, the facility must not cover any losses incurred in the underlying pool of exposures prior to a draw, or be structured such that draw-down is certain (as indicated by regular or continuous draws);
  - (b) The facility must be subject to an asset quality test that precludes it from being drawn to cover credit risk exposures that are in default as defined in [CRE36.69](#) to [CRE36.76](#). In addition, if the exposures that a liquidity facility is required to fund are externally rated securities, the facility can only be used to fund securities that are externally rated investment grade at the time of funding;
  - (c) The facility cannot be drawn after all applicable (eg transaction-specific and programme-wide) credit enhancements from which the liquidity would benefit have been exhausted; and
  - (d) Repayment of draws on the facility (ie assets acquired under a purchase agreement or loans made under a lending agreement) must not be subordinated to any interests of any note holder in the programme (eg asset-backed commercial paper programme) or subject to deferral or waiver.
- (2) Eligible servicer cash advance facilities: subject to national discretion, if contractually provided for, servicers may advance cash to ensure an uninterrupted flow of payments to investors so long as the servicer is entitled to full reimbursement and this right is senior to other claims on cash flows from the underlying pool of exposures.