

Chapter 4

The IRB approach

4.9 The IRB approach: Securitisation, non-credit obligations assets and CIUs

Application

- 4.9.1 **R** BIPRU 4.9 applies with respect to *securitisation exposures, non credit-obligation assets and exposures to CIUs*.

Securitisation exposures

- 4.9.2 **R** The following must be calculated in accordance with ■ BIPRU 9 (Securitisation):

- (1) *risk-weighted exposure amounts for securitised exposures and for exposures belonging to the IRB exposure class referred to in ■ BIPRU 4.3.2 R (6) (securitisation positions); and*
- (2) *the expected loss amounts for securitised exposures.*

[Note: BCD Article 87(10) and Article 88(3)]

Provision of credit protection

- 4.9.3 **R** Where a *firm* provides credit protection for a number of *exposures* under terms that the *n*th default among the *exposures* shall trigger payment and that this credit event shall terminate the contract, if the product has an external credit assessment from an *eligible ECAI* the *risk weights* set out in ■ BIPRU 9 must be applied. If the product is not rated by an *eligible ECAI*, the *risk weights* of the *exposures* included in the basket must be aggregated, excluding *n-1 exposures* where the sum of the *expected loss* amount multiplied by 12.5 and the *risk weighted exposure amount* must not exceed the nominal amount of the protection provided by the credit derivative multiplied by 12.5. The *n-1 exposures* to be excluded from the aggregation must be determined on the basis that they must include those *exposures* each of which produces a lower *risk weighted exposure amount* than the *risk weighted exposure amount* of any of the *exposures* included in the aggregation.

[Note: BCD Annex VII Part 1 point 9]

Non credit obligation assets: Introduction

- 4.9.4 **R** ■ BIPRU 4.9.5 R-■ BIPRU 4.9.10 R apply to *non credit-obligation assets*.

Non credit obligation assets: Inclusion of residual value of leases

- 4.9.5 **R** The *non credit obligation asset IRB exposure class* includes the residual value of leased properties, if not included in the *lease exposure* as defined in **■ BIPRU 4.4.75 R**.

[Note: BCD Article 86(8)]

Non credit obligation assets: Risk weighted exposure amount

- 4.9.6 **R** The *risk weighted exposure amounts* must be calculated according to the formula:

Risk-weighted exposure amount = 100% * *exposure* value except for when the *exposure* is a residual value of leased properties in which case it must be calculated as follows:

$1/t * 100\% * \textit{exposure}$ value; where *t* is the greater of 1 and the nearest number of whole years of the lease remaining.

[Note: BCD Annex VII Part 1 point 27]

- 4.9.7 **G** *t* should be an integer number reflecting the nearest number of whole years of the lease remaining and should decrease as the lease matures so that the discounted value steps up gradually from a small value to 100% as the end of the lease approaches.

- 4.9.8 **R** Where a *firm* has full recourse in respect of purchased receivables for *default* risk and for *dilution* risk, to the seller of the purchased receivables, **■ BIPRU 4.8.21 R** and **■ BIPRU 4.8.30 R** need not be applied. The *exposure* may instead be treated as a collateralised *exposure*.

[Note: BCD Article 87(2) (part)]

Non credit obligation assets: Exposure value

- 4.9.9 **R** The *exposure* value of *non credit-obligation assets* must be the value presented in the financial statements.

[Note: BCD Annex VII Part 3 point 13]

Non credit obligation assets: Expected loss amounts

- 4.9.10 **R** For *non credit-obligation assets* the *expected loss* amount must be zero.

[Note: BCD Article 88(4)]

Collective investment undertakings

- 4.9.11 **R** (1) Where *exposures* in the form of a *CIU* meet the criteria set out in **■ BIPRU 3.4.121 R** (Conditions for look through treatment under the standardised approach) and the *firm* is aware of all of the underlying *exposures* of the *CIU*, the *firm* must look through to those underlying *exposures* in order to calculate *risk weighted exposure amounts* and *expected loss* amounts in accordance with the methods set out in **■ BIPRU 4.■ BIPRU 4.9.12 R** applies to the part of the underlying *exposures* of the *CIU* of which the *firm* is not aware or could not

reasonably be aware. In particular, ■ BIPRU 4.9.12 R must apply where it would be unduly burdensome for the *firm* to look through the underlying *exposures* in order to calculate *risk weighted exposure amounts* and *expected loss* amounts in accordance with methods set out in this rule.

- (2) Where (1) applies but a *firm* does not meet the conditions for using the methods set out in ■ BIPRU 4 for all or part of the underlying *exposures* of the *CIU*, *risk weighted exposure amounts* and *expected loss* amounts must be calculated in accordance with the following approaches.
- (3) For *equity exposures* the approach set out in ■ BIPRU 4.7.9 R - ■ BIPRU 4.7.12 R (Simple risk weights) must be used. If, for those purposes, the *firm* is unable to differentiate between private equity, exchange-traded and other *equity exposures*, it must treat the *exposures* concerned as other *equity exposures*.
- (4) For all other underlying *exposures*, the *standardised approach* must be used, subject to the following modifications:
 - (a) [deleted]
 - (b) [deleted]
 - (c) for *exposures* subject to a specific *risk weight* for unrated *exposures* or subject to the *credit quality step* yielding the highest *risk weight* for a given exposure class, the *risk weight* must be multiplied by a factor of two, but cannot be higher than 1250%; and
 - (d) for all other *exposures*, the *risk weight* must be multiplied by a factor of 1.1 and subject to a minimum of 5%.

[Note: BCD Article 87(11)]

4.9.12

R

- (1) Where *exposures* in the form of a *CIU* do not meet the criteria set out in ■ BIPRU 3.4.121 R (Conditions for look through treatment under the standardised approach) or the *firm* is not aware of all of the underlying *exposures* of the *CIU*, a *firm* must look through to the underlying *exposures* and calculate *risk weighted exposure amounts* and *expected loss* amounts in accordance with the approach set out in ■ BIPRU 4.7.9 R - ■ BIPRU 4.7.12 R (Simple risk weights). If, for those purposes, the *firm* is unable to differentiate between private equity, exchange-traded and other *equity exposures*, it must treat the *exposures* concerned as other *equity exposures*. For these purposes, non-equity *exposures* must be assigned to one of the classes (private equity, exchange traded equity or other equity) set out in ■ BIPRU 4.7.9 R (Simple risk weight approach) and unknown *exposures* must be assigned to the other equity class.
- (2) Alternatively to the method described in (1), a *firm* may calculate itself or rely on a third party to calculate and report the average *risk weighted exposure amounts* based on the *CIU's* underlying *exposures* and calculated in accordance with the approaches in ■ BIPRU 4.9.11R (3) to ■ BIPRU 4.9.11R (4), provided that the correctness of the calculation and the report is adequately ensured.
- (3) [deleted]

(4) [deleted]

(a) [deleted]

(b) [deleted]

[Note: BCD Article 87(12)]

- 4.9.13** **G** For the purposes of ■ BIPRU 4.9.12 R (1), in the case of non-equity *exposures* a *firm* should look at the risk profile of the underlying *exposures* and map these to an equivalent equity *risk weight*. For example, if the underlying *exposures* are exchange-traded, the *risk weight* of exchange-traded equity *exposures* will apply. If the underlying *exposures* are unknown, the *risk weight* of the other equity class will apply. Only under exceptional circumstances would supervisors expect to see non-equity *exposures* mapped to the diversified private equity *risk weight*.
- 4.9.14** **G** For the purposes of ■ BIPRU 4.9.12 R (2), a *firm* should ensure that any third party relied on for the calculations and report possesses the necessary competence and experience to ensure that the calculations and report are correct.
- 4.9.15** **R** The *expected loss* amounts for *exposures* referred to in ■ BIPRU 4.9.11 R - ■ BIPRU 4.9.12 R must be calculated in accordance with the methods set out in ■ BIPRU 4.4.61 R (Calculation of expected loss for sovereigns, institutions and corporates), ■ BIPRU 4.5.12 R - ■ BIPRU 4.5.14 R (Calculation of expected loss for specialised lending), ■ BIPRU 4.6.47 R - ■ BIPRU 4.6.48 R (Calculation of expected loss for retail exposures), ■ BIPRU 4.7.12 R, ■ BIPRU 4.7.17 R and ■ BIPRU 4.7.26 R (Calculation of expected loss for equity exposures) and ■ BIPRU 4.8.30 R (Dilution risk of purchased receivables).
- [Note: BCD Article 88(6)]