Chapter 1

Commission Delegated Regulation (EU) 2016/101

Article 9 Calculation of market price uncertainty AVA

(1) Market price uncertainty AVAs shall be calculated at valuation exposure level ("individual market price uncertainty AVAs").

(2) The market price uncertainty AVA shall only be assessed to have zero value where both of the following conditions are met:

(a) the institution has firm evidence of a tradable price for a valuation exposure or a price can be determined from reliable data based on a liquid two-way market as described in the second subparagraph of Article 338(1) of Regulation (EU) No 575/2013;

(b) the sources of market data set out in Article 3(2) do not indicate any material valuation uncertainty.

(3) Where a valuation exposure cannot be shown to have a zero AVA, when assessing the market price uncertainty AVA institutions shall use the data sources defined in Article 3. In this case the calculation of the market price uncertainty AVA shall be performed as described in paragraphs 4 and 5.

(4) Institutions shall calculate AVAs on valuation exposures related to each valuation input used in the relevant valuation model.

(a) The granularity at which those AVAs shall be assessed shall be one of the following:

(i) where decomposed, all the valuation inputs required to calculate an exit price for the valuation position;

(ii) the price of the instrument.

(b) Each of the valuation inputs referred to in point (a)(i) shall be treated separately. Where a valuation input consists of a matrix of parameters, AVAs shall be calculated based on the valuation exposures related to each parameter within that matrix. Where a valuation input does not refer to tradable instruments, institutions shall map the valuation input and the related valuation exposure to a set of market tradable instruments. Institutions may reduce the number of parameters of the valuation input for the purpose

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of calculating AVAs using any appropriate methodology provided the reduced parameters satisfy all of the following requirements:

(i) the total value of the reduced valuation exposure is the same as the total value of the original valuation exposure;

(ii) the reduced set of parameters can be mapped to a set of market tradable instruments;

(iii) the ratio of variance measure 2 defined below over variance measure 1 defined below, based on historical data from the most recent 100 trading days, is less than 0,1.

For the purposes of this paragraph, "variance measure 1" shall mean profit and loss variance of the valuation exposure based on the unreduced valuation input and "variance measure 2" shall mean profit and loss variance of the valuation exposure based on the unreduced valuation input minus the valuation exposure based on the reduced valuation input.

(c) Where a reduced number of parameters is used for the purpose of calculating AVAs, the determination that the criteria set out in point (b) are met shall be subject to independent control function review of the netting methodology and internal validation on at least an annual basis.

(5) Market price uncertainty AVAs shall be determined as follows:

(a) where sufficient data exists to construct a range of plausible values for a valuation input:

(i) for a valuation input where the range of plausible values is based on exit prices, institutions shall estimate a point within the range where they are 90 % confident they could exit the valuation exposure at that price or better;

(ii) for a valuation input where the range of plausible values is created from mid prices, institutions shall estimate a point within the range where they are 90 % confident that the mid value they could achieve in exiting the valuation exposure would be at that price or better;

(b) where insufficient data exists to construct a plausible range of values for a valuation input, institutions shall use an expert-based approach using qualitative and quantitative information available to achieve a level of certainty in the prudent value of the valuation input that is equivalent to that targeted under point (a). Institutions shall notify competent authorities of the valuation exposures for which this approach is applied, and the methodology used to determine the AVA;

(c) institutions shall calculate the market price uncertainty AVA based on one of the following approaches:

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(i) they shall apply the difference between the valuation input values estimated according to either point (a) or point (b), and the valuation input values used for calculating fair value to the valuation exposure of each valuation position;

(ii) they shall combine the valuation input values estimated according to either point (a) or point (b) and they shall revalue valuation positions based on those values. Institutions shall then take the difference between the revalued positions and fair-valued positions.

(6) Institutions shall calculate the total category level AVA for market price uncertainty by applying to individual market price uncertainty AVAs the formulae for either Method 1 or Method 2 laid down in the Annex.