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Consultation Paper

Guidelines on the treatment of CVA risk under the supervisory review and evaluation process (SREP)

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1. Responding to this consultation

The EBA invites comments on all proposals put forward in this paper and in particular on the specific questions summarised in 5.2.

Comments are most helpful if they:

- respond to the question stated;
- indicate the specific point to which a comment relates;
- contain a clear rationale;
- provide evidence to support the views expressed/ rationale proposed; and
- describe any alternative regulatory choices the EBA should consider.

Submission of responses

To submit your comments, click on the 'send your comments' button on the consultation page by 12.02.2016. Please note that comments submitted after this deadline, or submitted via other means may not be processed.

Publication of responses

Please clearly indicate in the consultation form if you wish your comments to be disclosed or to be treated as confidential. A confidential response may be requested from us in accordance with the EBA's rules on public access to documents. We may consult you if we receive such a request. Any decision we make not to disclose the response is reviewable by the EBA's Board of Appeal and the European Ombudsman.

Data protection

The protection of individuals with regard to the processing of personal data by the EBA is based on Regulation (EC) N° 45/2001 of the European Parliament and of the Council of 18 December 2000 as implemented by the EBA in its implementing rules adopted by its Management Board. Further information on data protection can be found under the Legal notice section of the EBA website.

2. Executive Summary

These Guidelines should be read together the EBA Guidelines on common procedures and methodologies for SREP[1] and build on the CVA Report published by the EBA in February 2015[2] implementing a number of policy recommendation provided in the report. In particular, the Guidelines establish a proportionate approach to the determination of whether institutions is exposed to a material CVA risk and to the assessment of how an institution manages such risk and reflects it in the own funds requirements.

The Guidelines provide a common European approach to (1) assessing the materiality of CVA risk, (2) its assessment under the supervisory review and evaluation process (SREP), and (3) determination of additional own funds requirements, where the risk is not adequately covered by the minimum own funds requirements, in particular due to the exemptions in the EU legislative framework. Building on the CVA Report, the Guidelines also broadly implement the EBA view on how the CVA framework should be improved and re-dimensioned until the review of the international regulatory framework (Fundamental Review of the Trading Book by the Basel Committee on Banking Supervision) is completed.

The approach provided for the assessment of adequacy of own funds and determination of additional own funds requirements for CVA risk, where it is assessed as material, is built around re-inclusion of certain exemptions into the perimeter of calculation of own fund requirements (EU and non-EU non-financial counterparties, sovereign, pension funds, and intra-group transactions), and comparing such hypothetical own funds requirements for CVA risk with actual minimum own funds requirements calculated pursuant to Title VI of Regulation (EU) No 575/2013. In addition, in case of institutions applying the advanced method to calculating minimum own funds requirements for CVA risk, they would be expected to implement certain technical recommendations of the CVA Report.

As already stated in the CVA Report, when developing the approach provided in these Guidelines as well as calibrating the threshold values that will be provided in the accompanying EBA recommendation, the EBA is mindful that the additional own funds requirements imposed pursuant to Article 104(1)(a) of Directive 2013/36/EU following the SREP assessment of CVA risk should not simply replicate in full or in substantive part the international standards that have not been implemented into EU legislation (i.e. additional own funds requirements should not compensate on one-to-one basis exemptions from the minimum own funds requirements).

[1] EBA/GL/2014/13 of 19 December 2014

[2] EBA Report on Credit Valuation Adjustments (CVA) under Article 456(2) of Regulation (EU) No 575/2013 and EBA Review on the application of CVA charges to non-financial counterparties established in a third country under Article 382(5) of regulation (EU) No 575/2013, published on 25 February 2015

Next steps

The Guidelines will be finalised following the completion of the public consultation and the accompanying Quantitative Impact Study (QIS). The feedback received during the consultation and data provided by institutions for QIS purposes will be used to assess the impact of the proposed common approach and calibrate the threshold values for the formulas set out in these Guidelines.

The threshold values for the formulas provided in the Guidelines will be provided by the EBA by means of the recommendation issued pursuant to Article 16 of Regulation (EU) 1093/2010 which will apply together with the Guidelines. The EBA will be monitoring the level of CVA risk and associated own funds requirements, including additional own fund requirements imposed by competent authorities, where relevant, on an annual basis, and may amend the threshold values, if necessary.

The Guidelines will be translated into the official EU languages and published on the EBA website. The deadline for competent authorities to report whether they comply with the guidelines will be two months after the publication of the translations.

3. Background and rationale

1. Article 456(2) of Regulation (EU) No 575/2013 mandates the EBA to monitor the own funds requirements for Credit Value Adjustment (CVA) risk and report to the European Commission its assessment *inter alia* of the treatment of CVA risk charge and the calculation of capital requirements of CVA risk. The EBA has discharged its task performing a comprehensive analysis of the CVA framework, and published the report in February 2015 ('CVA Report')[3]. The CVA report provides a detailed analysis of the practices applied by institutions and of the regulatory frameworks applicable to CVA risk, quantifying the impact of including in the calculations of own funds requirements transaction currently exempted under Article 382 of Regulation (EU) No 575/2013.

2. In particular, in the CVA Report the EBA notes that the CVA risk generated by the counterparties exempted from the calculation of minimum own funds requirements pursuant to Article 382(4) of Regulation (EU) No 575/2013 is considered to be substantial and therefore needs to be captured prudentially. Therefore, based on the outcomes of the analysis of current industry and supervisory practices and considering the actual financial risk associated with CVA, the EBA recommends defining a coordinated approach for the annual monitoring of the impact of transactions exempted from the minimum own fund requirements for CVA risk, and for defining situations constituting a presumption of excessive (or material) CVA risk that should be considered by the competent authorities under the supervisory review and evaluation process (SREP) (Policy Recommendation 4 of CVA Report).

3. This coordinated approach should be followed by competent authorities at least until the Basel Committee on Banking Supervision ('BCBS') completes its relevant work on the review of trading book and CVA frameworks and the relevant BCBS principles have been implemented into the EU legislation.

4. These Guidelines provide, also on the basis of the CVA Report (Recommendation 4), a coordinated approach to:

    a. the determination of materiality of the CVA risk;

    b. the SREP assessment of material CVA risk, including the assessment of risk exposures, risk management, measurement and control;

    c. the SREP assessment of the adequacy of own funds to cover material CVA risk; and

    d. the determination of additional own funds requirements imposed under Article 104(1)(a) of Directive 2013/36/EU to cover for such risk.

[3] EBA Report on Credit Valuation Adjustments (CVA) under Article 456(2) of Regulation (EU) No 575/2013 and EBA Review on the application of CVA charges to non-financial counterparties established in a third country under Article 382(5) of regulation (EU) No 575/2013, published on 25 February 2015

5. More specifically, Title VI of Regulation (EU) No 575/2013 requires that institutions hold own funds to cover CVA risk; Article 382 (4) of that Regulation excludes certain transaction from the scope of that calculation.

6. Further, Article 73 of Directive 2013/36/EU provides that institutions should, when performing their Internal Capital Adequacy Assessment Process ('ICAAP') ensure that they maintain adequate internal capital to cover all elements and levels of risks to which they are or might be exposed to.

7. Likewise, Article 97 of Directive 2013/36/EU provides that competent authorities should , under their Supervisory Review and Evaluation Process ('SREP'), determine whether the arrangements, strategies, processes and mechanisms implemented by institutions and the own funds and liquidity held by them ensure a sound management and coverage of the risks they are or might be exposed to. Such assessment should be performed in accordance with the EBA Guidelines on common procedures and methodologies for SREP ('SREP Guidelines')[4].

8. Thus, when assessing ICAAP as part of the SREP assessment, competent authorities should expect an institution to identify all material risks it is or might be exposed to, and provide adequate capital for such risks, including for CVA risk, if determined as material.

9. Following the requirements of SREP Guidelines, generally, competent authorities would usually assess CVA risk as a sub-category of market risk. However, depending on the materiality of risk, competent authorities may decide to assess and score sub-categories of risk on an individual basis. Also on the basis of CVA Report (Policy Recommendation 4), these Guidelines provide guidance for determining the materiality of CVA risk and specify the calculation method and the materiality threshold. Should an institution meet the materiality threshold as provided in these Guidelines, it should be considered to be exposed to material CVA risk that needs to be assessed and scored individually by competent authorities in the SREP.

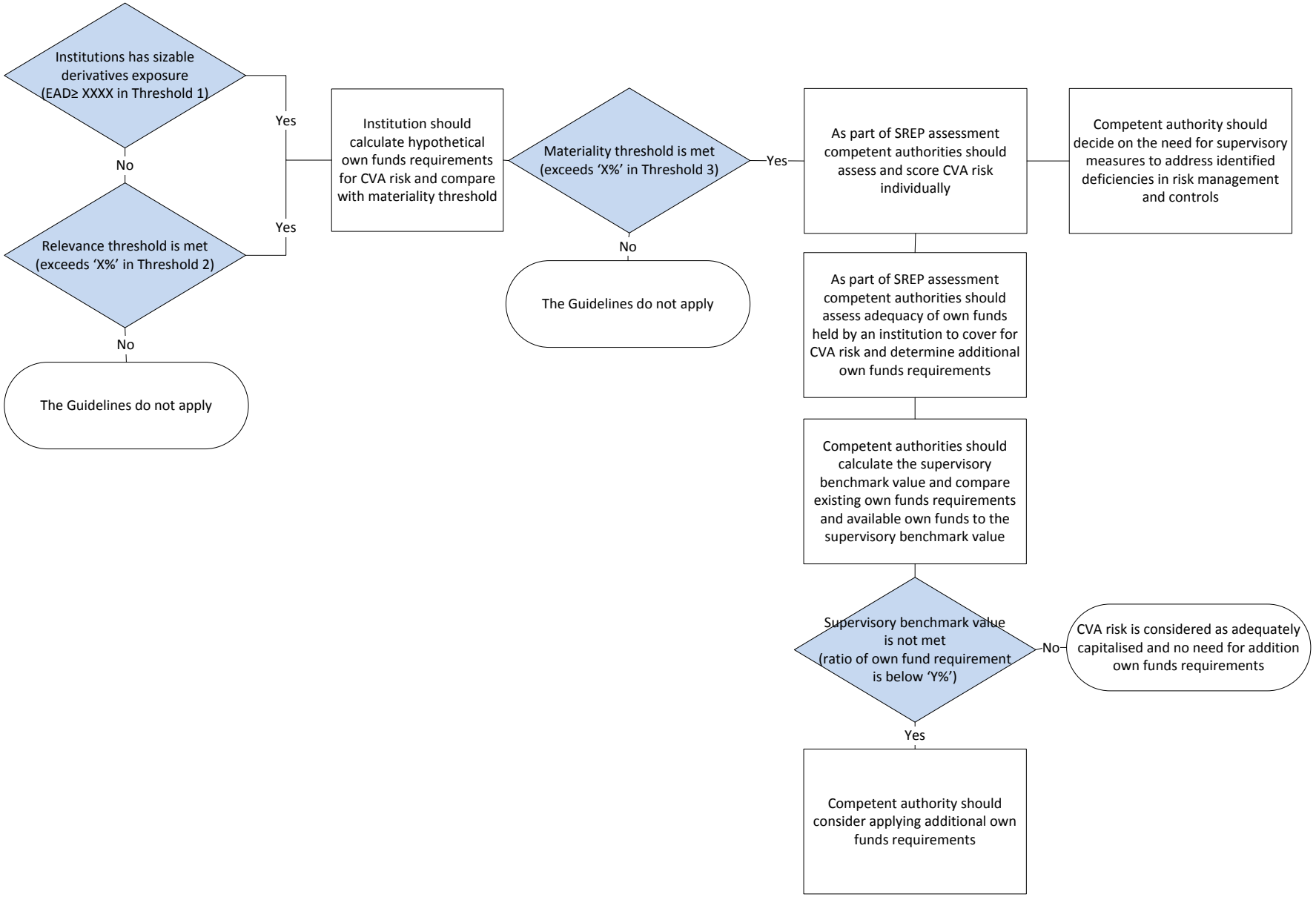
10. Besides, the institutions within their ICAAPs should consider the relevance and the materiality threshold applying the calculation methods provided in these Guidelines to determine the materiality of their exposure to CVA risk. In particular, competent authorities should expect an institution to identify whether they are exposed to material CVA risk using the thresholds and calculation methods proved. Wherever an institution meets the relevance and materiality thresholds, they should assume to be exposed to material CVA risk, and competent authorities should expect the institutions to reflect this risk in their ICAAP.

11. Competent authorities should assess CVA risk that is identified as material as part of the assessment of risks to capital within the SREP as well as review the treatment of CVA risk in the institution's ICAAP.

12. Where, as part of the outcome of the SREP assessment, competent authorities determine that the arrangements, strategies, processes and mechanisms to identify, quantify and manage CVA risk implemented by an institution are inadequate and/or that minimum own funds requirements are insufficient to cover CVA risk, then competent authorities should impose appropriate measures under Article 104 of Directive 2013/36/EU to address these deficiencies, including requiring an institution to hold additional own funds.

[4] EBA/GL/2014/13 of 19 December 2014

13. The process of determination of materiality of CVA risk and its supervisory assessment provided in these Guidelines is shown below:


Institutions has sizable derivatives exposure (EAD≥ XXXX in Threshold 1)
Yes
No
Relevance threshold is met (exceeds 'X%' in Threshold 2)
Yes
No
The Guidelines do not apply
Institution should calculate hypothetical own funds requirements for CVA risk and compare with materiality threshold
Materiality threshold is met (exceeds 'X%' in Threshold 3)
Yes
No
The Guidelines do not apply
As part of SREP assessment competent authorities should assess and score CVA risk individually
Competent authority should decide on the need for supervisory measures to address identified deficiencies in risk management and controls
As part of SREP assessment competent authorities should assess adequacy of own funds held by an institution to cover for CVA risk and determine additional own funds requirements
Competent authorities should calculate the supervisory benchmark value and compare existing own funds requirements and available own funds to the supervisory benchmark value
Supervisory benchmark value is not met (ratio of own fund requirement is below 'Y%')
No
CVA risk is considered as adequately capitalised and no need for addition own funds requirements
Yes
Competent authority should consider applying additional own funds requirements

14. The Guidelines fully recognise the principle of proportionality and aim at focusing the assessment of competent authorities on the CVA risk that can be considered as material. This is implemented through a 'relevance' and 'materiality' thresholds: (1) institutions should have a significant derivatives portfolio (the exposure value for derivatives is larger than the amount specified by the EBA) or their current own funds requirements for CVA risk should exceed a pre-defined share of their current total risk exposure amount (relevance threshold); (2) only those institutions meeting the above criteria will be required to calculate the materiality threshold using the methods provided in these Guidelines. If both thresholds are met, institutions would be assumed to have material CVA risk that will need to be capitalised for by institutions, and assessed by competent authorities under SREP.

15. The approach provided in the Guidelines as well as calculation methods for the thresholds and supervisory benchmarks will be supplemented by the EBA recommendation issued pursuant to Article 16 of Regulation (EU) 1093/2010 which will apply together with the Guidelines. In its recommendation, the EBA will advise competent authorities and institutions on the common approach to the implementation of these Guidelines by setting threshold values for all formulas provided in these Guidelines.

16. In developing the approach provided in these Guidelines and in calibrating the threshold values that will be provided in the accompanying recommendation, the EBA is mindful that the additional own funds requirements imposed pursuant to Article 104(1)(a) of Directive 2013/36/EU following the SREP assessment of CVA risk should not simply replicate in full or in substantive part the international standards that have not been implemented into EU legislation (i.e. additional own funds requirements should not compensate on one-to-one basis exemptions from the minimum own funds requirements).

17. The approach set forward in these Guidelines aims also at addressing several shortcomings of the current CVA framework already identified in the CVA Report. Specifically, institutions using the advanced method for the calculation of minimum own funds requirements for CVA risk should use the proxy spread, and the LGD_MKT parameters (see also Policy Recommendations 7 and 8 in the CVA Report). These technical repairs in the calculation of the advanced method are particularly suited for the exempted transactions due to the nature of the associated counterparties (non-financials, sovereigns) which often do not have CDS spreads quoted on the market (therefore requiring the use of the proxy spread methodology) or for which the seniority of derivative transactions may differ from the usual convention used to compute LGD_MKT.

18. The Guidelines also include provisions for the annual monitoring of the level of excessive CVA risk and associated own funds requirements by competent authorities. This data will be also provided to the EBA in order to allow for the ongoing assessment of the relevance of the threshold levels set in the recommendation, and their update, if necessary.

4. Draft guidelines

In between the text of the draft Guidelines advice that follows, further explanations on specific aspects of the proposed text are occasionally provided, which either offer examples or provide the rationale behind a provision, or set out specific questions for the consultation process. Where this is the case, this explanatory text appears in a framed text box.

EBA/GL-REC/20XX/XX

DD Month YYYY

Draft Guidelines

on the treatment of CVA risk under the supervisory review and evaluation process (SREP)

1. Compliance and reporting obligations

Status of these guidelines

1. This document contains guidelines issued pursuant to Article 16 of Regulation (EU) No 1093/2010[5]. In accordance with Article 16(3) of Regulation (EU) No 1093/2010, competent authorities and financial institutions must make every effort to comply with the guidelines.

2. Guidelines set the EBA view of appropriate supervisory practices within the European System of Financial Supervision or of how Union law should be applied in a particular area. Competent authorities as defined in Article 4(2) of Regulation (EU) No 1093/2010 to whom guidelines apply should comply by incorporating them into their practices as appropriate (e.g. by amending their legal framework or their supervisory processes), including where guidelines are directed primarily at institutions.

Reporting requirements

3. According to Article 16(3) of Regulation (EU) No 1093/2010, competent authorities must notify the EBA as to whether they comply or intend to comply with these guidelines, or otherwise with reasons for non-compliance, by ([dd.mm.yyyy] *two months after publication of all language versions of the guidelines*). In the absence of any notification by this deadline, competent authorities will be considered by the EBA to be non-compliant. Notifications should be sent by submitting the form available on the EBA website to compliance@eba.europa.eu with the reference 'EBA/GL/201x/xx'. Notifications should be submitted by persons with appropriate authority to report compliance on behalf of their competent authorities. Any change in the status of compliance must also be reported to EBA.

4. Notifications will be published on the EBA website, in line with Article 16(3).

[5] Regulation (EU) No 1093/2010 of the European Parliament and of the Council of 24 November 2010 establishing a European Supervisory Authority (European Banking Authority), amending Decision No 716/2009/EC and repealing Commission Decision 2009/78/EC, (OJ L 331, 15.12.2010, p.12).

2. Subject matter, scope and definitions

Subject matter

5. These Guidelines aim at ensuring convergence of supervisory practices for the assessment of CVA risk by institutions under the internal capital adequacy assessment process ('ICAAP') and by competent authorities under the supervisory review and examination process ('SREP') performed in accordance with Articles 73 and 97 of Directive 2013/36/EU respectively and the EBA Guidelines on common procedures and methodologies for SREP[6] ('SREP Guidelines').

6. The Guidelines provide to the competent authorities methods, principles and criteria with a view to enable them:

    a. determining the materiality of CVA risk;

    b. assessing material CVA risk including risk stemming from derivative transactions exempted from the calculation of minimum own funds requirements pursuant to Article 382(4) of regulation (EU) No 575/2013;

    c. assessing the arrangements, strategies, processes and mechanisms that institutions implement to identify and manage their exposure to CVA risk; and

    d. assessing the adequacy of own funds held by an institution to cover CVA risk and the determination of additional own funds requirements to cover for such risk in accordance with Article 104(1)(a) of Directive 2013/36/EU.

7. The Guidelines provide to institutions methods, principles and criteria with a view to enable them to assess, during their internal capital adequacy assessment process ('ICAAP') carried out pursuant to Article 73 of Directive 2013/36/EU, material CVA risk not covered by Article 1 of Regulation (EU) No 575/2013 including due to application of Article 382(4) of that regulation.

Addressees

8. These Guidelines are addressed to competent authorities as defined in point (i) of Article 4(2) of Regulation (EU) No 1093/2010 and to financial institutions as defined in Article 4(1) of Regulation No 1093/2010.

[6] EBA/GL/2014/13 of 19 December 2014

Scope

9. Competent authorities and institutions should apply these Guidelines in accordance with the levels of application of ICAAP and SREP set out in Articles 108 to 110 of Directive 2013/36/EU.

3. Implementation

Date of application

10. These guidelines apply from dd.mm.yyyy

4. Assessment of CVA risk under SREP

4.1 Determination of relevance for the calculation of CVA Risk

11. All institutions should perform the following calculation to determine the relevance of their CVA risk. In particular, institutions should determine their CVA risk as relevant if:

    a. the exposure value for derivatives transactions, excluding derivative transactions with a qualifying central counterparty, as calculated following the requirements of Part 3, Title 2, Chapter 6 of the Regulation (EU) 575/2013 exceeds the value specified by the EBA (Threshold 1); or

Explanatory text for consultation purposes

The appropriate level of the threshold will be determined and set in the EBA recommendation following performance of impact assessment based on the outcomes of quantitative impact study taking place in parallel with the public consultation.

The EBA is considering the following policy options regarding the value of Threshold 1: 10; 50; 100; 150 mln EUR (or equivalent in other reporting currency).

Question 1: Do you agree with determining relevance of CVA risk by means of assessing the size of an institution's derivative business using the exposure value for non-QCCP cleared derivatives transactions?

Question 2: What are your views on how Threshold 1 should be calibrated?

    b. the ratio of minimum own funds requirements for CVA risk as calculated pursuant to Title VI of Regulation (EU) No 575/2013 to total risk exposure amount as calculated following the requirements of Article 92(3) of Regulation (EU) No 575/2013 exceeds the value of x% specified by the EBA (Threshold 2).

$$\frac{Own\ funds\ requirements\ for\ CVA\ risks\ as\ reported}{Total\ risk\ exposure\ amount} \geq x\%\ (Threshold\ 2)$$

4.2 Determination of materiality of CVA risk

12. Institutions with a relevant CVA risk determined in accordance with Section 4.1. of these Guidelines should determine whether they meet the materiality threshold and therefore are assumed to be exposed to material CVA risk. For this purpose institutions should calculate the

hypothetical own funds requirement for CVA risk as a ratio of the hypothetical total risk exposure amount (see Formula 1 below).

$$\frac{Hypothetical\ own\ funds\ requirements\ for\ CVA\ risks\ including\ exempted\ transactions}{Hypothetical\ total\ risk\ exposure\ amount} \geq x\%\ (Threshold\ 3)$$

Formula 1. Determination of materiality of CVA risk

13. If the ratio equals or exceeds a pre-determined threshold 'x%', whose value should be provided by the EBA, CVA risk for the institution should be presumed to be material and the need of additional own funds for CVA risk of the exempted transactions should be further investigated by the competent authorities under SREP. Otherwise, CVA risk for the institution would be considered as non- material and it would not fall under the scope of the assessment methodology and potential additional own funds requirements as provided in these Guidelines.

14. Institutions should provide the results of calculation referred to in paragraph 12 of these Guidelines to competent authorities as specified in Section 6 of these Guidelines.

Explanatory text for consultation purposes

The appropriate level of the threshold 'x%' will be determined and set in the EBA recommendation following performance of impact assessment based on the outcomes of quantitative impact study taking place in parallel with the public consultation.

The EBA is considering the following policy options regarding the value of Thresholds 2 and 3: x = 0.5; 1; 2; 3; 4%.

Question 3: Do you agree with determining relevance of CVA risk by means of assessing the share of own funds requirements for CVA risk to the total risk exposure amount?

Question 4: Do you agree with the approach provided for the determination of materiality of CVA risk?

Question 5: What are your views on how 'x%' (Thresholds 2 and 3) should be calibrated?

4.2.1 Calculating hypothetical own funds requirement for CVA risk

15. The hypothetical own funds requirement for CVA risk referred to in paragraph 12 and Formula 1 should be calculated for the scope of transactions specified in paragraph 17 of these Guidelines based on the available calculation methods of Part 3, Title VI of Regulation (EU) No 575/2013. Institutions applying the advanced method set out in Article 383 of Regulation (EU) No 575/2013 should perform the following:

    a. institutions may use alternative approaches to proxy the spread of those counterparties for which no time series of credit spreads are available, nor for any of their peers, due to their very nature, provided that such alternative approaches duly documented and based on a more fundamental analysis of credit risk. The use of alternative approaches should be justified by the use of similar approaches to proxy the spreads of the same counterparty for CVA accounting purposes. In addition, institutions should be allowed to use single name proxy spreads to the case of a parent and a subsidiary, which share at least either the same industry or the same region; and

    b. institutions should reflect the seniority of the netting set in the first LGD_MKT parameter of the regulatory formula set out in Article 383 of Regulation (EU) No 575/2013, provided that they can document all the instances where this parameter is different from the LGD_MKT parameter in the formula used for implying probabilities of default from credit spreads.

16. The hypothetical total risk exposure amount referred to in Paragraph 12 and Formula 1 of these Guidelines should be the total risk exposure amount calculated in accordance with Article 92(3) of Regulation (EU) No 575/2013, where the risk exposure amount determined as per Article 92(3)(d) of that regulation is replaced by the hypothetical own funds requirement for CVA risk calculated according to the provisions of these Guidelines.

17. For the purposes of calculation of the hypothetical own funds requirements for CVA risk in Formula 1, institutions should include all OTC derivative transactions within the scope of Article 382 of Regulation (EU) No 575/2013, except derivative transactions excluded in accordance with Article 382(3) of that Regulation. In particular, the following derivative transactions should be included in the calculation of the hypothetical own funds requirements for CVA risk in Formula 2 that have been exempted from the calculation of minimum own funds requirements based on Article 382(4) of Regulation (EU) No 575/2013:

    a. transactions with non-financial counterparties as referred to in Article 382(4)(a);

    b. transactions with sovereign counterparties as referred to in Article 382(4)(d);

    c. transactions with pension scheme arrangements as referred to in Article 382(4)(c); and,

d. intra-group transactions as referred to in Article 382(4)(b).

Question 6: Do you agree with the scope of derivative transactions to be included into the calculation of hypothetical own funds requirements for CVA risk?

Question 7: Do you agree that intra-group derivatives transactions should be explicitly included into the scope of calculation? If not, what do you think could be a credible alternative treatment of the CVA risk of intragroup transactions?

4.3 Assessing and scoring CVA risk

18. Competent authorities should consider that an institution meeting the materiality threshold as specified in Section 4.2 of these Guidelines is exposed to a material CVA risk. Thus they should assess the CVA risk independently from market risk, and assess the level of risk exposure as well as risk management and controls.

19. When assessing the CVA risk, competent authorities should apply the principles set forward in Section 6 of SREP Guidelines: in particular they should assess the following:

    a. types of counterparties;

    b. for institutions using advanced approaches, VaR and Stressed VaR for CVA, and their evolution over time;

    c. the degree of concentration of counterparties and specific products;

    d. the strategies, processes and mechanisms of measuring and managing CVA risk of exempted transactions, including the allocation of internal capital.

20. When assessing CVA risk management and controls, competent authorities should consider them as part of the risk management and controls for market risk in general and not only for CVA risk separately, i.e. the assessment of the risk management and controls should be based on the requirements stipulated in Section 6.3.3 of SREP Guidelines.

21. Following the assessment of the CVA risk as above and taking into account their assessment of overall market risk management and controls of the institution, competent authorities should form a view on the institution's overall CVA risk. This view should be reflected in the summary of findings, accompanied by a risk score. The risk score should be based on the definitions and considerations provided in Section 6.3.4 of SREP Guidelines.

5. Application of supervisory measures to address CVA risk

22. Following the assessment of the CVA risk and its management and controls as provided in these Guidelines, in case competent authorities identify deficiencies in the institution's arrangements, strategies, processes and mechanisms to identify, quantify and manage CVA risk, they should consider applying supervisory measures as provided in Article 104 of Directive 2013/36/EU to address the deficiencies.

23. Pursuant to requirements of Section 10 of SREP Guidelines, competent authorities should apply the most appropriate supervisory measures based on the deficiencies identified. Such measures may include capital (e.g. requiring institutions to hold additional own funds) and other supervisory measures that should be applied considering the outcomes of the assessment of all SREP elements and overall SREP assessment as provided in the SREP Guidelines.

24. In particular, competent authorities may, on the basis of the vulnerabilities and deficiencies identified in the SREP assessment of CVA risk, impose supervisory measures including:

    a. requiring the institution in accordance with Article 104(1)(b) of Directive 2013/36/EU to enhance the performance of the institution's internal approaches, or of stress-testing capacity, enhancing the quality and frequency of the market risk reporting to the institution's senior management; and/or requiring more frequent and in-depth internal audits of market activity:

    b. requiring the institution in accordance Article 104(1)(e) of Directive 2013/36/EU to restrict investment in certain products when the institution's policies and procedures do not ensure that the risk from those products will be adequately covered and controlled, or to divest financial products when the valuation processes of the institution do not produce conservative valuations that comply with the standards of Regulation (EU) No 575/2013;

    c. requiring the institution in accordance with Article 104(1)(f) of Directive 2013/36/EU to reduce the level of CVA risk when significant shortcomings have been found in the institution's measurement systems, or to increase the amount of derivatives settled through qualifying central counterparties (QCCPs);

    d. requiring the institution to use net profits to strengthen own funds in accordance with Article 104(1)(h) of Directive 2013/36/EU;

    e. restricting or prohibiting distributions or interest payments by the institution to shareholders, members or holders of Additional Tier 1 instruments where such

prohibition does not constitute an event of default of the institution in accordance with Article 104(1)(i) of Directive 2013/36/EU; and/or

f. requiring the institution to apply a specific treatment of assets in terms of own funds requirements in accordance with Article 104(1)(d) of Directive 2013/36/EU.

25. Notwithstanding the requirements regarding the application of supervisory measures in the case of the identified vulnerabilities or deficiencies as stipulated in the paragraphs above, competent authorities should assess whether an institution has adequate own funds to cover for material CVA risk and decide on the application of additional own funds requirements as specified in Section 5.1 below.

5.1 Determination of additional own funds requirements for material CVA risk

26. Competent authorities should assess how an institution is taking material CVA risk into account in its ICAAP and, provided the outcome of the overall assessment of the reliability of ICAAP performed under SREP (see Sections 5.6 and 7.2.1 of SREP Guidelines), consider relevant internal estimates as an input to the determination of possible additional own funds requirements for CVA risk.

27. In order to determine possible additional own funds requirements for material CVA risk, competent authorities should also take into account the following:

a. the value and evolution of hypothetical own funs requirements for CVA risk calculated based on the requirements of these Guidelines in relation to the thresholds set by the EBA in its recommendation for the implementation of these Guidelines;

b. the value of supervisory benchmarks, where developed by competent authorities pursuant to the requirements of SREP Guidelines and considering the requirements of these Guidelines and EBA recommendation for the implementation of these Guidelines;

c. the level of concentration of CVA risk, in particular single-name, sectoral, geographical and product concentrations;

d. the processes and procedures that institution has put in place in order to manage and mitigate CVA risk; and

e. other relevant elements, including outcomes of peer-group comparisons, risk-specific stress testing, inputs from macroprudential (designated) authorities and outcomes from the dialogue with an institution.

28. The competent authorities should set the composition (quality) of the additional own funds requirements for CVA risk applying Section 7.4 of SREP Guidelines.

29. The additional own funds requirements for material CVA risk should form a part of TSCR as determined and articulated following the requirements set out in Section 7 of SREP Guidelines.

5.1.1 Determination and use of supervisory benchmark

30. For the purposes of determining additional own funds requirements for risks not covered by minimum own funds requirements (material CVA risk in the context of these Guidelines) the competent authorities should determine a value of supervisory benchmark as the proportion of the hypothetical own funds requirements for CVA risk specified in these Guidelines, calculated using the threshold value provided by the EBA (see Formula 2).

$$Hypothetical\ own\ funds\ requirements\ for\ CVA\ risk\ including\ exempted\ transactions * y\%\ (Threshold\ 4)$$

Formula 2. Determination of supervisory benchmark for additional own funds requirements

Explanatory text for consultation purposes

The appropriate level of the 'y%' threshold will be determined and set in the EBA recommendation following performance of impact assessment based on the outcomes of quantitative impact study taking place in parallel with the public consultation.

The EBA is considering the following policy options regarding the value of Threshold 4: y = 40; 50; 60; 70%.

Question 8: Do you agree with the approach provided for the determination of supervisory benchmark for material CVA risk?

Question 9: What are your views on how 'y%' (Threshold 4) should be calibrated?

31. The value of supervisory benchmark should indicate an appropriate coverage of CVA risk by own funds requirements (minimum or additional). In particular, the value of supervisory benchmark is set to a portion 'y%', which value should be provided by the EBA, of the hypothetical own funds requirement for CVA (which includes the CVA risk for the exempted transactions in the scope of these Guidelines).

32. To assess the adequacy of own funds held to cover material CVA risk and determine potential additional own funds requirements, competent authorities should compare actual own funds requirements for CVA risk with the value of supervisory benchmark as determined using Formula 2 above.

33. When the ratio between the actual own funds requirements for CVA risk and the hypothetical own funds requirements for CVA risk is above 'y%', competent authorities may conclude that the material CVA risk is already adequately covered by the institution by own funds and the competent authority would generally not impose additional own funds requirements for CVA risk.

34. When the ratio between the actual own funds requirements for CVA risk and the hypothetical own funds requirements for CVA risk determined as specified in these Guidelines is below 'y%' specified by the EBA, competent authorities may conclude that material CVA risk is not adequately covered by own funds, and the competent authority should consider applying additional own funds requirements using Formula 3.

$$(Hypothetical\ own\ funds\ requirements\ for\ CVA\ risk\ including\ exempted\ transactions * y\%) - Own\ funds\ requirements\ for\ CVA\ risk\ as\ reported = potential\ additional\ own\ funds\ requirements$$

Formula 3. Determination of potential additional own funds requirements using the supervisory benchmark

35. In both cases above the supervisory response should not be based solely on the outcome of the calculation of supervisory benchmark, and competent authorities when deciding on the application of additional own funds requirements and the size and composition of such requirement should also take into consideration all factors set out in these Guidelines, including the outcome of the supervisory assessment of CVA risk and assessment of institution's ICAAP.

36. Additional own funds requirements for material CVA risk imposed following the requirements of these Guidelines should be included into the determination of total SREP Capital Requirements ('TSCR') as outlined in Section 7 of SREP Guidelines.

6. Monitoring of the CVA risk by competent authorities and the EBA

37. In order to facilitate the assessment of CVA risk, its materiality and own funds requirements based on the approach provided in these Guidelines, institutions should regularly calculate the materiality criteria, including where relevant calculating hypothetical own funds requirements for CVA risk as specified in these Guidelines (see Section 4.2), and provide to the respective competent authorities the following information:

a. exposure value for derivatives transactions, excluding derivative transactions with a qualifying central counterparty, calculated in accordance with Part 3, Title 2, Chapter 6 of the Regulation (EU) 575/2013;

b. own funds requirements for CVA risk calculated in accordance with Title VI of Regulation (EU) No 575/2013;

c. total risk exposure amount calculated in accordance with Article 92(3) of Regulation (EU) 575/2013;

d. hypothetical own funds requirement for CVA risk calculated in accordance with Section 4.2 of these Guidelines;

e. hypothetical total risk exposure amount calculated in accordance with Paragraph 16 of these Guidelines;

f. additional own funds requirements for material CVA risk applied in accordance with these Guidelines and contributing to TSCR in accordance with SREP Guidelines.

38. Institutions meeting the materiality criteria set out Section 4.2 of these Guidelines should provide to the competent authorities the information referred to paragraph 37 at least four times per year as of the end of each quarter (four values). This information should be provided along with information submitted to the competent authorities on the institution's ICAAP. Each competent authority should define the process and procedures to be followed by institutions when submitting such information.

39. Competent authorities should use the information received for the purposes of the assessment of material CVA risk as set out in Section 4.3 these Guidelines and assessment of capital adequacy and determination of additional own funds requirements as set out in Section 5.1 of these Guidelines.

40. Competent authorities should provide information regarding values of hypothetical own funds requirements for CVA risk to the EBA. Competent authorities should provide such information to the EBA for all institutions within the scope of these Guidelines by no later than 30 April of each calendar year.

Explanatory text for consultation purposes

The monitoring of CVA risk and associated own funds requirements is important part of EBA mandate on CVA risk. The informational specified in this section that will be provided to the EBA would also allow to monitor how supervisory benchmark provided in Section 5.1.1 of these Guidelines is applied in practice and would allow recalibration of threshold values, where necessary.

Question 10: Do you agree with the approach provided monitoring of CVA risk by competent authorities and EBA and data to be provided to competent authorities for this monitoring?

For institutions using the CVA advanced method, the computation of hypothetical own funds requirement for CVA risk in accordance with Section 4.2 of these Guidelines will require, in order to be consistent with the figures reported under COREP, to be performed at the same frequency as the computation of the regulatory CVA VaR and Stressed VaR figures, and taking into account the average over 3 months.

Question 11: What is your view regarding the potential burden of computing hypothetical own funds requirement for CVA risk at the same frequency as the regulatory CVA VaR and Stressed VaR figures?

5. Accompanying documents

5.1 Draft impact assessment

a. Problem identification

The CVA Report, published in February 2015, denotes that there is evidence that CVA risk, generated by the counterparties exempted from the calculation of minimum own funds requirements pursuant to Article 382(4) of Regulation (EU) No 575/2013, is substantial and therefore should be captured prudentially. Therefore, considering the substantial CVA risk generated by EU exempted counterparties, the EBA recommends the determination of a coordinated approach for annual monitoring of the impact of transactions exempted from the minimum own fund requirements for CVA risk, and for defining situations constituting a presumption of excessive (or material) CVA risk that should be considered by the competent authorities under the supervisory review and evaluation process (SREP) (Policy Recommendation 4 of CVA Report).

In anticipation of the Fundamental Review of Trading Book of the BCBS, including the CVA framework, the coordinated approach should be in place until the BCBS standards are implemented into the EU legislation. In the interim period, the EBA should develop a temporary guidance which addresses the following issues:

- to apply, in principle, to all institutions subject to SREP; and,
- following the principle of proportionality in the implementation of EBA guidance, to apply only to EU institutions with excessive CVA risk; thus, exclude small non-complex EU institutions which does not exhibit excessive CVA risk.

b. Policy objectives

The policy objective of the current Guidelines aim to implement the Policy Recommendation 4 (PR4) of the CVA Report and frame the coordinated approach in order to:

a. Determine the materiality (excessiveness) of CVA risk;

b. SREP assessment of material (excessive) CVA risk, including risk stemming from the derivative transactions that are exempted from the calculation of minimum own funds requirements pursuant to Article 382(4) of Regulation (EU) No 575/2013, and its management, measurement and control;

c. SREP assessment of adequacy of own funds to cover material CVA risk; and,

d. the determination of additional own funds requirements to cover for such risk based on the provision of Article 104(1)(a) of Directive 2013/36/EU.

The policy objective set above is considered to be achieved with the following specific operational objectives:

- set out a materiality threshold on the Total Credit Counterparty Risk (CCR) exposure value for derivatives according to which credit institutions would be excluded from the EBA guidance;
- set out a relative materiality threshold by comparing the hypothetical own funds requirements for CVA risk to total own funds requirements; and,
- should the hypothetical own funds requirements for CVA risk exceed the threshold, set out a supervisory benchmark for the additional own funds requirements for the excessive CVA risk.

c. Baseline

The Guidelines fully recognise the principle of proportionality and aim to focus the assessment of competent authorities on the CVA risk that can be considered as material. This is implemented through a double-materiality threshold: (1) institutions should have a significant derivatives portfolio (exposure value for derivatives, excluding transactions with a qualifying central counterparty (QCCP), is larger than the amount specified by the EBA) or their current own funds requirements for CVA risk should exceed a pre-defined share of their current total risk exposure amount; (2) only those institutions meeting the above criteria will be required to calculate the materiality threshold using the methods provided in these Guidelines. If both sets of criteria are met, institutions would be assumed to have material CVA risk that will need to be capitalised for by institutions, and assessed by competent authorities under SREP.

The current GLs suggest the framework to establish procedures for the identification of excessive CVA risks and the adequate capitalisation of the excessive risk. This procedure involves the estimation of specific thresholds which have not yet been set. Thus, the baseline for the assessment of the options of different levels of thresholds is the set formulas for their calculation. Once this framework is in place, there will be a separate assessment of the different levels of the threshold (see next session).

When converting the above principles into quantitative expressions, one has to consider data that could be used to access whether institutions have a ***significant derivatives portfolio*** (EAD for derivatives) and find the appropriate threshold that could be set by the EBA, above which the derivatives EAD would be deemed significant.

The ***identification of excessive CVA risks can be identified by comparing*** the *'credit institution's hypothetical own funds requirement for CVA risks under CRR'*, i.e. including all the exempted

transactions in the scope of EBA guidance, to *'total hypothetical own funds requirement under Pillar 1'*.

$$\frac{\begin{pmatrix} Hypothetical\ own\ funds\ requirements\ for\ CVA\ risks \\ including\ exempted\ transactions \end{pmatrix}}{Hypothetical\ total\ own\ funds\ requirements} > x\%$$

This ratio should be first calculated (Step 1) and then assessed accordingly (Step 2). Should the ratio be above a threshold x% (to be specified), then CVA risks are considered to be 'excessive' and should be investigated further (Step 2). If not, then there are no additional own funds requirements expected under the EBA coordinated approach.

According to Step 2 (SREP), there should be additional assessment of CVA risk, independently from market risk, and assessment of the level of risk exposure as well as risk management and control systems.

The GLs also suggest that there is a supervisory benchmark for additional own funds which ensure that excessive CVA risks are sufficiently capitalised and help competent authorities to assess credit institutions' own ICAAP calculations (Step 3). This supervisory benchmark is expressed as

$$y\% * \begin{pmatrix} Hypothetical\ own\ funds\ requirements\ for\ CVA\ risks \\ including\ exempted\ transactions \end{pmatrix}$$

The additional amount required to adequately capitalise of hypothetical own funds requirement for CVA risks including exempted transactions in scope of EBA guidance:

$$max\ [\ y\% * \begin{pmatrix} Hypothetical\ own\ funds\ requirements\ for\ CVA\ risks \\ including\ exempted\ transactions \end{pmatrix}$$

$$- Actual\ own\ funds\ requirements\ for\ CVA\ risks;\ 0\ ]$$

The level of y% threshold needs to be calibrated at a level which represents an acceptable CVA risk charge, consistent with high-level requirements agreed as part of CVA report. Namely, the level of y% should not materially reverse the effect of exemptions enshrined in EU regulation and be broadly consistent with other PR, in particular PR15 (e.g. sum of VaR and Stressed VaR should be dropped), of the CVA Report.

d. Options considered

The scope of the impact assessment is limited as it constitutes a screening IA based on a limited sample which submitted data to be included in the CVA Report. Thus, it only considers the impact from the implementation of alternative combinations of thresholds regarding the materiality for the identification of excessive CVA risks (x%) and the level of risk charge (y%) for the excessive

CVA risk. Nonetheless, this IA does not examine the impact of EBA imposing a threshold on exposure value for derivatives due to the lack of data.

During the consultation on these GLs, the EBA will launch a process for collecting additional data for an extended sample of banks to produce a QIS which in turn will set the exact thresholds for:

- The exposure value for derivatives, excluding transactions with a QCCP;
- The identification of excessive CVA risks according to 'own funds requirements for CVA risk in relation to the total risk exposure amount' (x%); and,
- The risk charge for the excessive CVA risk (y%).

Assessment of the 'significant derivatives portfolio (exposure value of derivatives)' threshold

In the effort to set a quantitative threshold for the exposure value of derivatives, the EBA considered data for 180 banks in the ITS (COREP) reporting templates as of December 2014. The data showed that derivatives exposures, measured as the exposure value computed in accordance with the requirements of Part 3, Title 2, Chapter 6 of the CRR including derivative transactions with a QCCP, vary from zero to approximately EUR 140 billion. The analysis of the data showed that the distribution of banks' exposures follows the following pattern (Table 1):

Table 1: Q-Q analysis for the distribution of exposures

Quantile	Estimate (in EUR)
Maximum value	139,606,000,000
90%	32,353,900,000
75% (3rd quartile)	4,519,640,000
66%	2,109,301,000
50% (median)	990,329,000
33%	338,752,000
25% (1st quartile)	157,847,000
10%	9,924,000

The consideration of a threshold that would exclude 25% of the EU banks participating in the sample would lead to its quantification at EUR 157.847 million. The threshold at this precise level would be significantly lower than the maximum exposure (0.11% of the maximum exposure), which enables the capture of medium and large exposures, while at the same time the representation of the member states in the part of the sample which was not excluded remains high (21 out of 28 member states are represented [not shown in the Tables / Figures). However, for the sake of simplicity, it is proposed the threshold to be set at either EUR 150 million or EUR 200 million. As observed in Table 2, a threshold at EUR 200 million would capture 73% of the sample (27% will be excluded), while a threshold at EUR 150 million would capture 75% of the sample.

It is also observed that there is only one additional bank, in the sample used, that is captured (in total 76% of the sample) by a threshold of EUR 100 million in relation to setting the threshold at EUR 150 million. Thus, the first three options examined seem to be broadly equivalent when considering the specific sample.

However, the sample used mainly consists of large EU banks. This implies that the quantiles shown above could be lower should a more representative sample, with balanced participation of large, medium and small EU banks, be used. If small and medium banks are included, the exposure values are expected to drop, setting the quartiles in Table 1, and thus the candidate thresholds, at lower levels.

Thus, there is need for additional QIS, based on an expanded sample, to not only examine the alternative thresholds of the current analysis (EUR 100 million, EUR 150 million, EUR 200 million) above but also the usefulness of lower thresholds, possibly at the area of EUR 50 million or EUR 10 million (currently 10th quantile of the sample used).

Table 2: Distribution of exposures-at-default for derivatives as of December 2014

Range of exposures	Number of banks
up to EUR 10 mn	20
from EUR 10 mnmn to EUR 50 mn	16
from EUR 50 mn to EUR 100 mn	8
from EUR 100 mn to EUR 150 mn	1
from EUR 150 mn to EUR 200 mn	4
from EUR 200 mn to EUR 500 mn	22
from EUR 500 mn to EUR 1 bn	20
from EUR 1 bn to EUR 50 bn	77
from EUR 50 bn to EUR 140 bn	12
Total	180

Assessment of the threshold of 'own funds requirements for CVA risk in relation to the total risk exposure amount'

The main materiality threshold, i.e. threshold for hypothetical own funds requirements for CVA risk to the hypothetical total risk exposure amount, is examined separately from the 'exposure value of derivatives' threshold due to the absence of common ITS sample. The different composition of samples does not allow the joint evaluation of the two materiality thresholds, something which will be carried out in an extensive QIS study, during the consultation period if these Guidelines. This QIS will collect information for a common sample for both materiality thresholds and will jointly assess them to come up with the final threshold values.

The alternative combinations of thresholds that have been examined include all the combinations taken from a set of four different materiality threshold (x%) values {0.5%, 1%, 2%, 3%, 4%} and a set of four different capital charge (y%) values {40%, 50%, 60%, 70%}. This results to 20 different

combinations of materiality threshold / capital charge. The principle for the selection of those variables was the x% to be on the low side to include as more credit institutions as possible for the SREP assessment and the y% to be sufficiently high to adequately address the excessive risks while at the same time be significantly less than 1-to-1 risk change of the excessive risk, as the last would cancel out in practice the exemptions of the existing Regulation.

Table 3: Percentage of the sample affected by the rules for excessive CVA risk

Materiality threshold (x%)	CVA capital charge (y%)			
	y = 40%	y = 50%	y = 60%	y = 70%
x = 0.5%	46%	54%	69%	73%
x = 1%	46%	54%	65%	69%
x = 2%	46%	54%	65%	69%
x = 3%	42%	50%	62%	65%
x = 4%	38%	46%	54%	54%

The data for the analysis derive from the CVA report and rely on a much smaller sample of banks (32 banks) than the analysis for the 'exposure value of derivatives' threshold (180 banks). Out of the 32 banks which submitted data, only 26 banks were included in the analysis due to data quality issues. 12 of these institutions use the standardised CVA approach while 14 use the advanced CVA approach. Under the most conservative scenario, approximately 27% of the sample (8 out of the 26 participating banks) remained unaffected.

The size of the sample captured by the materiality threshold remained stable for the three lowest materiality thresholds (0.5%, 1%, 2%) while it decreases when 3% and 4% materiality thresholds are considered. This pattern appears in all levels of additional CVA capital charge, i.e. 40%, 50%, 60% and 70% (see Table 3).

Table 4: Additional CVA exposure in relation to the current actual total RWA for CVA risks (in %), all banks for different combinations of x% and y%

Materiality threshold (x%)	CVA capital charge (y%)			
	y = 40%	y = 50%	y = 60%	y = 70%
x = 0.5%	21.23%	32.93%	47.05%	64.73%
x = 1%	21.23%	32.93%	47.05%	64.71%
x = 2%	21.23%	32.93%	47.05%	64.71%
x = 3%	18.83%	29.55%	42.70%	59.39%
x = 4%	18.60%	29.22%	41.97%	56.38%

The additional CVA exposure, in relation to the current actual total RWA for CVA risks (Table 4), increase monotonically for different levels of y% values when considering the same x% values.

The largest change in capital charges is observed between y=50% and y=60% for all levels of materiality thresholds.

When the sample is split into banks subject to Advanced CVA (A-CVA) approach and those subject to Standardised CVA (S-CVA) approach for the calculation of the CVA capital charge, the results show that the A-CVA are affected on average less than the S-CVA banks (see Table 5 and

Table 6) for all four alternative capital charge values (y%), despite the fact that this sub-sample is highly influenced by an outlier (see Figure 1 and Figure 2).

Table 5: Additional CVA exposure in relation to the current actual total RWA for CVA risks (in %), A-CVA banks, for different combinations of x% and y%

Materiality threshold (x%)	CVA capital charge (y%)			
	y = 40%	y = 50%	y = 60%	y = 70%
x = 0.5%	20.33%	32.37%	47.31%	65.57%
x = 1%	20.33%	32.37%	47.31%	65.57%
x = 2%	20.33%	32.37%	47.31%	65.57%
x = 3%	16.84%	27.46%	40.99%	57.83%
x = 4%	16.84%	27.46%	40.99%	55.48%

Table 6: Additional CVA exposure in relation to the current actual total RWA for CVA risks (in %), S-CVA banks, for different combinations of x% and y%

Materiality threshold (x%)	CVA capital charge (y%)			
	y = 40%	y = 50%	y = 60%	y = 70%
x = 0.5%	23.19%	34.16%	46.48%	62.87%
x = 1%	23.19%	34.16%	46.48%	62.82%
x = 2%	23.19%	34.16%	46.48%	62.82%
x = 3%	23.19%	34.16%	46.48%	62.82%
x = 4%	22.45%	33.10%	44.13%	58.36%

The bank-by-bank analysis below presents the impact of implementing the materiality thresholds of x=2% and x=3% for all alternative capital charges (40%, 50%, 60%, 70%). The reason for selecting only these materiality thresholds is the fact that they exhibit the largest differences between them while options x=0.5% and x=1% are identical with x=2% and the option x=4% is almost identical with x=3%.

The impact of the combination of the two thresholds on individual banks is shown in Figure 1 and Figure 2 below. As mentioned above, there is a notable outlier in A-CVA sub-sample which is highly impacted by the proposed thresholds.

Figure 1: Additional CVA exposure in relation to the current actual total RWA for CVA risks (in %), per bank, for x= 2% and different levels of y%

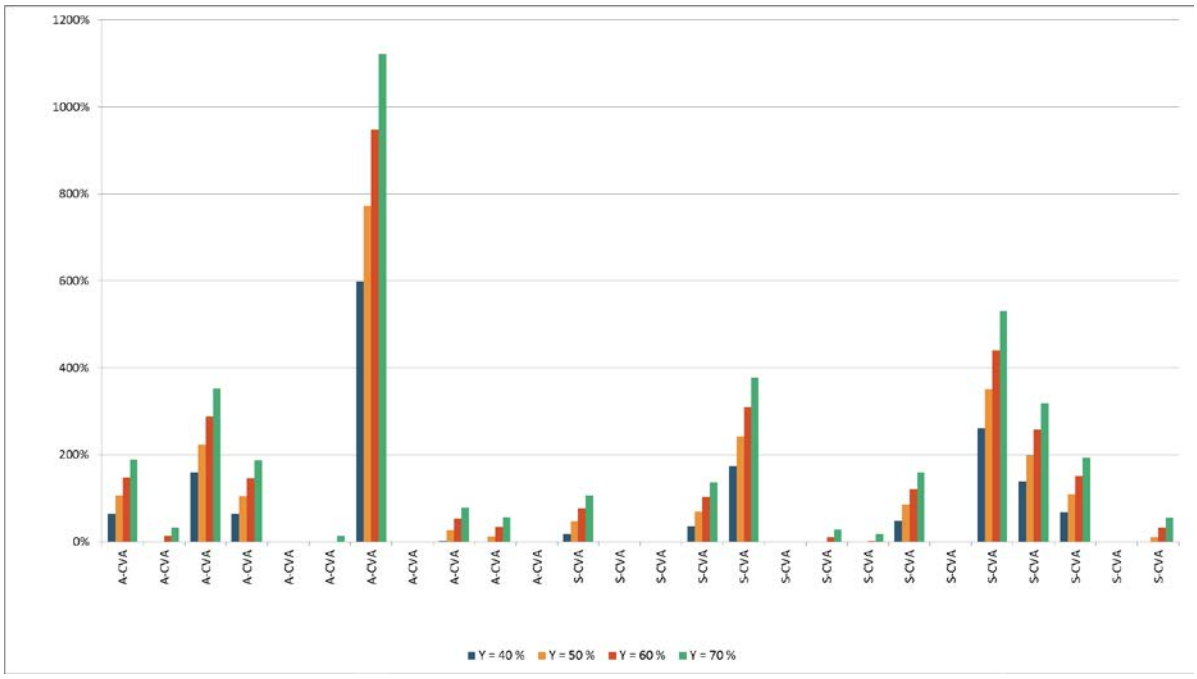
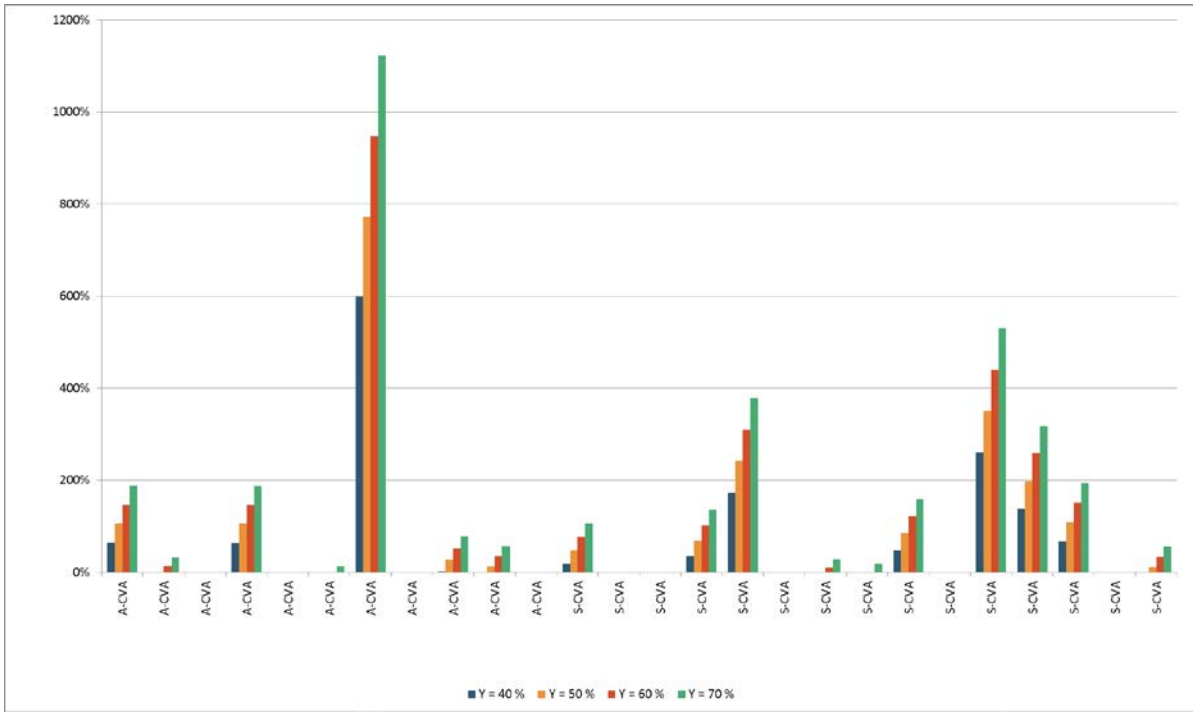


Figure 2: Additional CVA exposure in relation to the current actual total RWA for CVA risks (in %), per bank, for x= 3% and different levels of y%



By raising the threshold of materiality from x=2% to x=3% renders one bank is excluded from the SREP assessment and the additional capital requirements for the excessive CVA exposures for derivatives.

e. Preferred options prior to QIS results

The analysis above separately assessed the implementation of two materiality thresholds, i.e. the threshold of 'significant derivatives portfolio (EAD for derivatives)' (Threshold A) and the threshold of 'own funds requirements for CVA risk in relation to the total risk exposure amount' (Threshold B). The breach of these thresholds would consequently lead to an additional evaluation of the excessive CVA risks and to additional capital charges.

Due to the lack of data for a consistent sample, the assessment of the two materiality thresholds was conducted separately. The data relevant to Threshold A indicate that the 25th quantile of the sample would be at approximately EUR 158 million. Based on the sample used, this level would ensure that the representation of the member states is broad enough and at the same time not many banks would be excluded from the additional assessment and the capital charge for excessive CVA risks.

As to the Threshold B, it is observed that there is a substantial cliff effect for combinations of high x% and high y% values (fewer banks are expected to be subject to much higher add-on). The summary statistics show that the A-CVA banks are affected less than S-CVA banks, despite they are highly influenced by an outlier. Nonetheless, it is observed that the three lower values of the examined materiality threshold for Threshold B (x=0.5%, x=1% or x=2%) capture the same number of banks while x=3% and x=4% capture less banks. Thus, based on the available data, the EBA proposes the selection of either of the three lower materiality thresholds for Threshold B (x%).

As to the capital charge (y%), which would be applied should a bank is considered to have excessive CVA risk, this should be sufficiently high to adequately address the excessive risks while at the same time be significantly less than 1-to-1 capital change of the excessive exposure. Since a high capital charge of the excessive derivatives exposures would cancel out in practice the exemptions set out in the Regulation, it is proposed that the lowest of the examined values to be applied in practice, i.e. y=40% and y=50%.

All in all, the present IA can only be considered as a preliminary 'screening' assessment, in view of a more detailed QIS study. Although the available data provided useful evidence, the representation and size of the sample do not allow for safe conclusions. Moreover, the differences in size and composition of the samples, used for the analyses of Threshold A and B, do not allow for a joint analysis of the two suggested thresholds. Thus, the final conclusions on the assessment of impact and calibration of thresholds should be finalised based on evidence from the QIS, to be conducted during the consultation period of the current Guidelines.

5.2 Overview of questions for consultation

Question 1: Do you agree with determining relevance of CVA risk by means of assessing the size of an institution's derivative business using the exposure value for non-QCCP cleared derivatives transactions?

Question 2: What are your views on how Threshold 1 should be calibrated?

Question 3: Do you agree with determining relevance of CVA risk by means of assessing the share of own funds requirements for CVA risk to the total risk exposure amount?

Question 4: Do you agree with the approach provided for the determination of materiality of CVA risk?

Question 5: What are your views on how 'x%' (Thresholds 2 and 3) should be calibrated?

Question 6: Do you agree with the scope of derivative transactions to be included into the calculation of hypothetical own funds requirements for CVA risk?

Question 7: Do you agree that intra-group derivatives transactions should be explicitly included into the scope of calculation? If not, what do you think could be a credible alternative treatment of the CVA risk of intragroup transactions?

Question 8: Do you agree with the approach provided for the determination of supervisory benchmark for material CVA risk?

Question 9: What are your views on how 'y%' (Threshold 4) should be calibrated?

Question 10: Do you agree with the approach provided monitoring of CVA risk by competent authorities and EBA and data to be provided to competent authorities for this monitoring?

Question 11: What is your view regarding the potential burden of computing hypothetical own funds requirement for CVA risk at the same frequency as the regulatory CVA VaR and Stressed VaR figures?