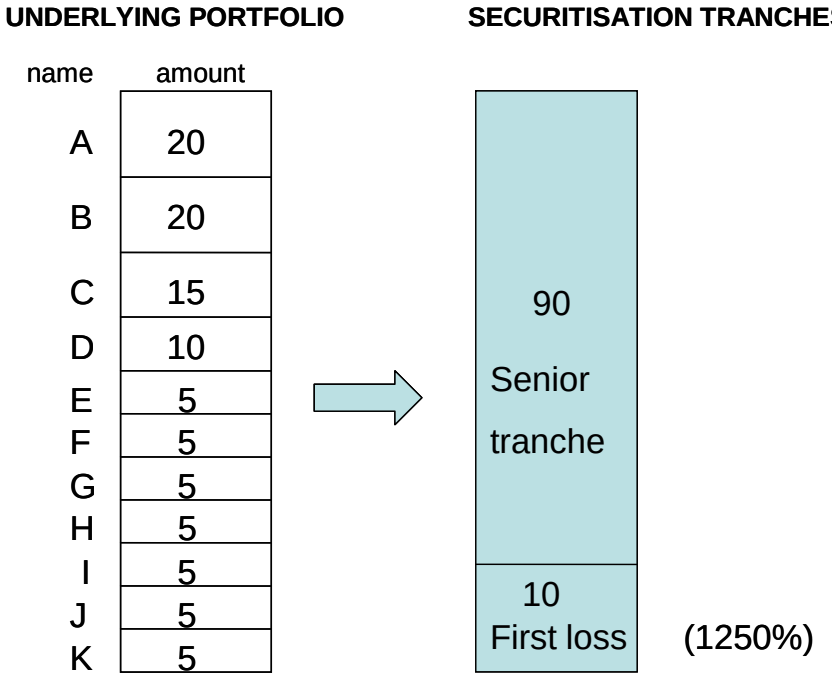
Corrigendum[1] to the examples on pages 26-29 of the CEBS Guidelines on the implementation of the revised large exposure regime published on 11 December 2009.

EXAMPLE 1

A. FULL LOOK-THROUGH (this example illustrates the case where the look-through is applied)

The structure of the product is as follows:



Assuming that:

Institution 1 has invested 90 in the senior tranche; and

Institution 2 has invested 10 in the first loss tranche.

The treatment for large exposures purposes should be the following:

Institution 1, on the senior tranche, must recognise:

0 with debtors D to K

[1] The amendments refer to the large exposure treatment of tranched products. The changes made to examples 1c, 2, 2a and 3 are of technical nature and have no impact on the substance of the above mentioned guidelines. The amended examples replace the respective examples of the CEBS Guidelines on the implementation of the revised large exposure regime on the date of their publication.

5 with debtor C

10 with debtors A and B

Institution 2, on the first loss tranche, must recognise:

5 with debtors E to K

10 with debtors A to D

Assuming that in the next period counterparty K defaults and a loss of 5 is registered, then, once this loss is known, institutions 1 and 2 must reassess their exposures. Therefore, just after the default:

Institution 1, on the senior tranche, must recognise:

0 with debtors E to J

5 with debtor D

10 with debtor C

15 with debtors A and B

Institution 2, on the first loss tranche, must recognise:

5 with debtors A to J

B. PARTIAL LOOK-THROUGH

This example assumes that only the names A and B are known, whereas for the rest, the institutions only know that the maximum amount invested is 20.

The treatment for large exposures purposes should be the following:

Institution 1, on the senior tranche, must recognise:

10 with debtors A and B

10 to add to the rest of the unknown exposures

Institution 2, on the first loss tranche, must recognise:

10 with debtors A and B

10 to add to the rest of the unknown exposures.

C. STRUCTURE-BASED APPROACH

This example assumes that no names are known; institutions only know that the maximum amount which can be invested in each counterparty is 20, counterparties can only belong to the UK pharmaceutical sector, and the institution has no other direct or indirect investments in that sector.

The treatment for large exposures purposes should be the following:

Institution 1, on the senior tranche, must recognise:

90 to the scheme (no effect because an exposure to the scheme of 90 is already recognised)

Institution 2, on the first loss tranche, must recognise:

10 to the scheme (no effect because an exposure to the scheme of 10 is already recognised)

D. RESIDUAL APPROACH

This example assumes that no names are known and the institutions do not know the maximum amount invested in each counterparty nor have any idea as to the nature (structure) of the investments.

The treatment for large exposures purposes should be the following:

Institution 1, on the senior tranche, must recognise:

90 to add to the unknown exposures

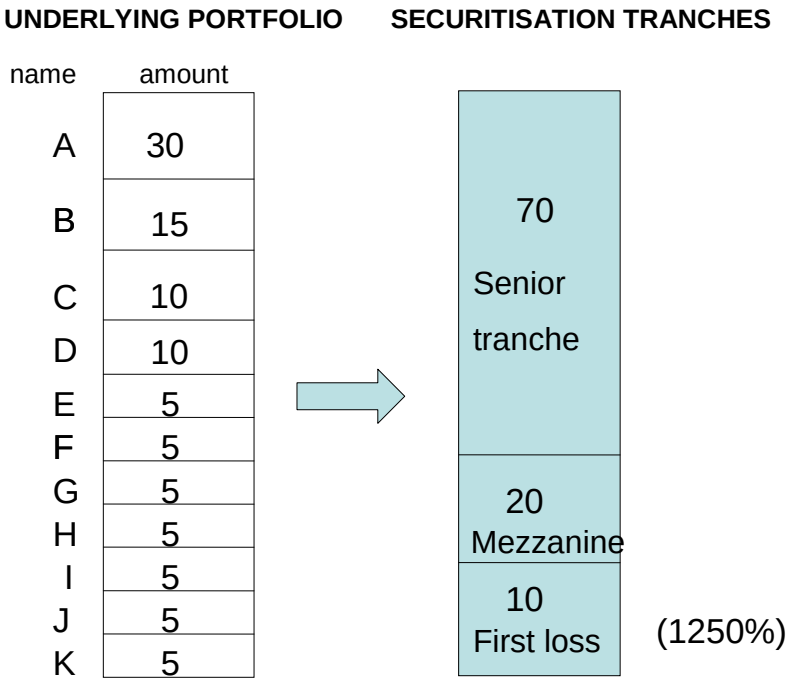
Institution 2, on the first loss tranche, must recognise:

10 to add to the unknown exposures

More examples on how the full look-through approach could be implemented for more complex structures are provided below:

EXAMPLE 2

In this example, a mezzanine tranche is added to the structure.



Assuming that:

Institution 1 has invested 70 in the senior tranche;

Institution 2 has invested 20 in the mezzanine tranche; and

Institution 3 has invested 10 in the first loss tranche.

The treatment for large exposures purposes should be the following:

Institution 1, on the senior tranche, must recognise:

0 with debtors A to K

Institution 2, on mezzanine tranche, must recognise:

0 with debtors C to K

5 with debtor B

20 with debtor A

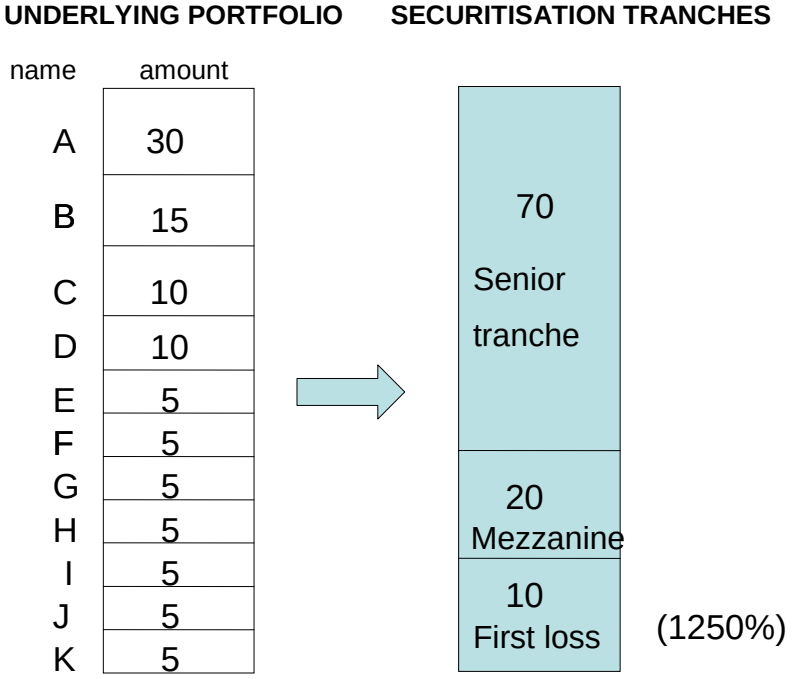
Institution 3 on first loss tranche:

5 with debtors E to K

10 with debtors A to D

EXAMPLE 2a

This example is to illustrate the effect of a haircut, in this case 50 % for the first loss tranche. Since CEBS is not in a position to recommend the use of a haircut (see point 86 and footnote 18 of the main document), the haircut used in this example is simply an illustration of how a haircut could be used, but of course the haircut in each specific case should depend on the risks outlined above: 1) lags in the reassessment and 2) losses that can stem from the required re-composition of the portfolio once the first loss tranche is exhausted, given the sudden emergence of large exposures breaches.



Assuming that:

Institution 1 has invested 70 in the senior tranche;

Institution 2 has invested 20 in the mezzanine tranche; and

Institution 3 has invested 10 in the first loss tranche.

The treatment for large exposures purposes should be the following:

Institution 1, on the senior tranche, must recognise:

0 with debtors B to K

5 with debtor A

Institution 2 on mezzanine tranche:

0 with debtors E to K

5 with debtors C and D

10 with debtor B

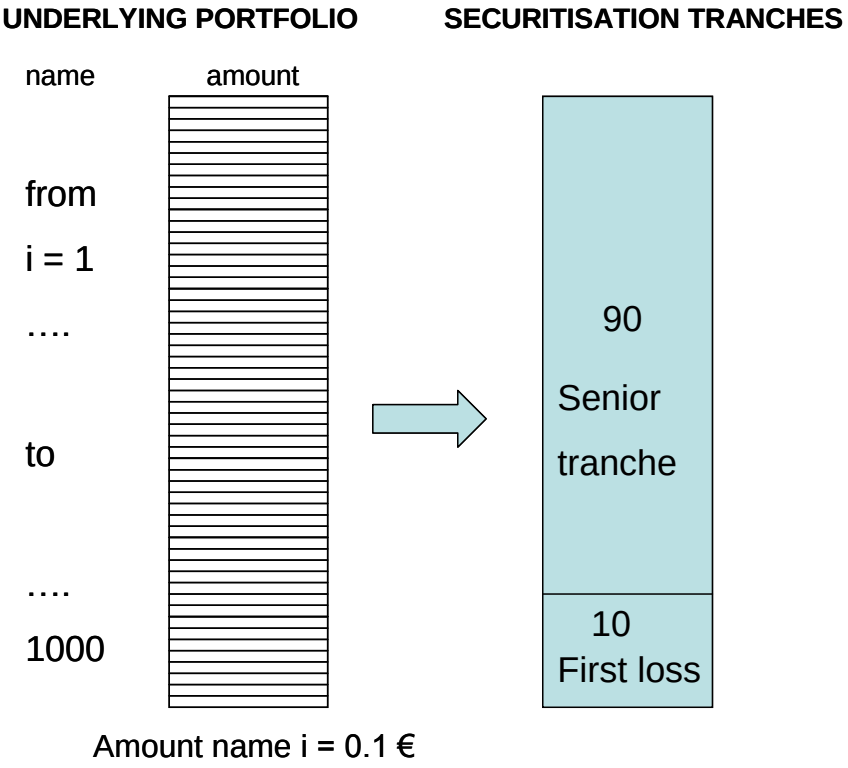
20 with debtor A

Institution 3, on first loss tranche, must recognise:

5 with debtors E to K

10 with debtors A to D

EXAMPLE 3



Assuming that:

Institution 1 has invested 90 in the senior tranche; and

Institution 2 has invested 10 in the first loss tranche.

The treatment for large exposures purposes should be the following:

Institution 1, on the senior tranche, must recognise:

0 with debtors i = 1 to 1000

Institution 2, on the first loss tranche, must recognise:

0.1 with debtors i = 1 to 1000

1. CEBS recognises that the variety and diversity of structured finance/structured finance vehicles can be large and therefore the details of individual cases should be properly accounted for when implementing these principles. However, CEBS firmly believes that common application of the principles stated in this paper will be a valuable contribution to the effectiveness of the prudential framework.