§ 217.37 Collateralized transactions.

(a) General. (1) To recognize the risk-mitigating effects of financial collateral, a Board-regulated institution may use:

(i) The simple approach in paragraph (b) of this section for any exposure; or

(ii) The collateral haircut approach in paragraph (c) of this section for repo-style transactions, eligible margin loans, collateralized derivative contracts, and single-product netting sets of such transactions.

(2) A Board-regulated institution may use any approach described in this section that is valid for a particular type of exposure or transaction; however, it must use the same approach for similar exposures or transactions.

(b) The simple approach—(1) General requirements. (i) A Board-regulated institution may recognize the credit risk mitigation benefits of financial collateral that secures any exposure.

(ii) To qualify for the simple approach, the financial collateral must meet the following requirements:

(A) The collateral must be subject to a collateral agreement for at least the life of the exposure;

(B) The collateral must be revalued at least every six months; and

(C) The collateral haircut approach must be used for determining the effective notional amount of the guarantee or credit derivative.
(C) The collateral (other than gold) and the exposure must be denominated in the same currency.

(2) Risk weight substitution. (i) A Board-regulated institution may apply a risk weight to the portion of an exposure that is secured by the fair value of financial collateral (that meets the requirements of paragraph (b)(1) of this section) based on the risk weight assigned to the collateral under §217.32. For repurchase agreements, reverse repurchase agreements, and securities lending and borrowing transactions, the collateral is the instruments, gold, and cash that the Board-regulated institution has borrowed, purchased subject to resale, or taken as collateral from the counterparty under the transaction. Except as provided in paragraph (b)(3) of this section, the risk weight assigned to the collateralized portion of the exposure may not be less than 20 percent.

(ii) A Board-regulated institution must apply a risk weight to the unsecured portion of the exposure based on the risk weight applicable to the exposure under this subpart.

(3) Exceptions to the 20 percent risk-weight floor and other requirements. Notwithstanding paragraph (b)(2)(i) of this section:

(i) A Board-regulated institution may assign a zero percent risk weight to an exposure to an OTC derivative contract that is marked-to-market on a daily basis and subject to a daily margin maintenance requirement, to the extent the contract is collateralized by cash on deposit.

(ii) A Board-regulated institution may assign a 10 percent risk weight to an exposure to an OTC derivative contract that is marked-to-market daily and subject to a daily margin maintenance requirement, to the extent that the contract is collateralized by an exposure to a sovereign that qualifies for a zero percent risk weight under §217.32.

(iii) A Board-regulated institution may assign a zero percent risk weight to the collateralized portion of an exposure where:

(A) The financial collateral is cash on deposit; or

(B) The financial collateral is an exposure to a sovereign that qualifies for a zero percent risk weight under §217.32, and the Board-regulated institution has discounted the fair value of the collateral by 20 percent.

(c) Collateral haircut approach—(1) General. A Board-regulated institution may recognize the credit risk mitigation benefits of financial collateral that secures an eligible margin loan, repo-style transaction, collateralized derivative contract, or single-product netting set of such transactions, and of any collateral that secures a repo-style transaction that is included in the Board-regulated institution’s VaR-based measure under subpart F of this part by using the collateral haircut approach in this section. A Board-regulated institution may use the standard supervisory haircuts in paragraph (c)(3) of this section or, with prior written approval of the Board, its own estimates of haircuts according to paragraph (c)(4) of this section.

(2) Exposure amount equation. A Board-regulated institution must determine the exposure amount for an eligible margin loan, repo-style transaction, collateralized derivative contract, or a single-product netting set of such transactions by setting the exposure amount equal to max \{0, \left[\Sigma E - \Sigma C + \Sigma (E x Hs) + \Sigma (Efx x Hfx)\right]\}, where:

(i)(A) For eligible margin loans and repo-style transactions and netting sets thereof, \(\Sigma E\) equals the value of the exposure (the sum of the current fair values of all instruments, gold, and cash the Board-regulated institution has lent, sold subject to repurchase, or posted as collateral to the counterparty under the transaction (or netting set)); and

(B) For collateralized derivative contracts and netting sets thereof, \(\Sigma E\) equals the exposure amount of the OTC derivative contract (or netting set) calculated under §217.34 (a)(1) or (2).

(ii) \(\Sigma C\) equals the value of the collateral (the sum of the current fair values of all instruments, gold and cash the Board-regulated institution has borrowed, purchased subject to resale, or taken as collateral from the counterparty under the transaction (or netting set));

(iii) \(E\) equals the absolute value of the net position in a given instrument or in gold (where the net position in
§ 217.37  the instrument or gold equals the sum of the current fair values of the instrument or gold the Board-regulated institution has lent, sold subject to repurchase, or posted as collateral to the counterparty minus the sum of the current fair values of that same instrument or gold the Board-regulated institution has borrowed, purchased subject to resale, or taken as collateral from the counterparty;  

(iv) $H_s$ equals the market price volatility haircut appropriate to the instrument or gold referenced in $E_s$;  

(v) $E_{fx}$ equals the absolute value of the net position of instruments and cash in a currency that is different from the settlement currency (where the net position in a given currency equals the sum of the current fair values of any instruments or cash in the currency the Board-regulated institution has lent, sold subject to repurchase, or posted as collateral to the counterparty minus the sum of the current fair values of any instruments or cash in the currency the Board-regulated institution has borrowed, purchased subject to resale, or taken as collateral from the counterparty); and  

(vi) $H_{fx}$ equals the haircut appropriate to the mismatch between the currency referenced in $E_{fx}$ and the settlement currency.

(3) Standard supervisory haircuts. (i) A Board-regulated institution must use the haircuts for market price volatility ($H_s$) provided in Table 1 to §217.37, as adjusted in certain circumstances in accordance with the requirements of paragraphs (c)(3)(iii) and (iv) of this section.

<table>
<thead>
<tr>
<th>Residual maturity</th>
<th>Haircut (in percent) assigned based on:</th>
<th>Investment grade securitization exposures (in percent)</th>
</tr>
</thead>
<tbody>
<tr>
<td>Less than or equal to 1 year</td>
<td>Zero 20 or 50 100 20 50 100</td>
<td></td>
</tr>
<tr>
<td>Greater than 1 year and less than or equal to 5 years</td>
<td>2.0 3.0 15.0 4.0 6.0 8.0 12.0</td>
<td></td>
</tr>
<tr>
<td>Greater than 5 years</td>
<td>4.0 6.0 15.0 8.0 12.0 16.0 24.0</td>
<td></td>
</tr>
<tr>
<td>Main index equities (including convertible bonds) and gold</td>
<td>15.0</td>
<td></td>
</tr>
<tr>
<td>Other publicly traded equities (including convertible bonds)</td>
<td>25.0</td>
<td></td>
</tr>
<tr>
<td>Mutual funds</td>
<td>Highest haircut applicable to any security in which the fund can invest</td>
<td></td>
</tr>
<tr>
<td>Cash collateral held</td>
<td>Zero</td>
<td></td>
</tr>
<tr>
<td>Other exposure types</td>
<td>25.0</td>
<td></td>
</tr>
</tbody>
</table>

1 The market price volatility haircuts in Table 1 to §217.37 are based on a 10 business-day holding period.

2 Includes a foreign PSE that receives a zero percent risk weight.

(ii) For currency mismatches, a Board-regulated institution must use a haircut for foreign exchange rate volatility ($H_{fx}$) of 8.0 percent, as adjusted in certain circumstances under paragraphs (c)(3)(iii) and (iv) of this section.

(iii) For repo-style transactions, a Board-regulated institution may multiply the standard supervisory haircuts provided in paragraphs (c)(3)(i) and (ii) of this section by the square root of $\frac{1}{2}$ (which equals 0.707107).

(iv) If the number of trades in a netting set exceeds 5,000 at any time during a quarter, a Board-regulated institution must adjust the supervisory haircuts provided in paragraphs (c)(3)(i) and (ii) of this section upward on the basis of a holding period of twenty business days for the following quarter except in the calculation of the exposure amount for purposes of §217.35. If a netting set contains one or more trades involving illiquid collateral or an OTC derivative that cannot be easily replaced, a Board-regulated institution must adjust the supervisory haircuts upward on the basis of a holding period of twenty business days. If
over the two previous quarters more than two margin disputes on a netting set have occurred that lasted more than the holding period, then the Board-regulated institution must adjust the supervisory haircuts upward for that netting set on the basis of a holding period that is at least two times the minimum holding period for that netting set. A Board-regulated institution must adjust the standard supervisory haircuts upward using the following formula:

\[ H_A = H_S \sqrt{\frac{T_M}{T_S}} \], where

(A) \( T_M \) equals a holding period of longer than 10 business days for eligible margin loans and derivative contracts or longer than 5 business days for repo-style transactions;

(B) \( H_S \) equals the standard supervisory haircut; and

(C) \( T_S \) equals 10 business days for eligible margin loans and derivative contracts or 5 business days for repo-style transactions.

(v) If the instrument a Board-regulated institution has lent, sold subject to repurchase, or posted as collateral does not meet the definition of financial collateral, the Board-regulated institution must use a 25.0 percent haircut for market price volatility (\( H_L \)).

(4) **Own internal estimates for haircuts.** With the prior written approval of the Board, a Board-regulated institution may calculate haircuts (\( H_S \) and \( H_F \)) using its own internal estimates of the volatilities of market prices and foreign exchange rates:

(i) To receive Board approval to use its own internal estimates, a Board-regulated institution must satisfy the following minimum standards:

(A) A Board-regulated institution must use a 99th percentile one-tailed confidence interval.

(B) The minimum holding period for a repo-style transaction is five business days and for an eligible margin loan is ten business days except for transactions or netting sets for which paragraph (c)(4)(i)(C) of this section applies. When a Board-regulated institution calculates an own-estimates haircut on a \( T_N \)-day holding period, which is different from the minimum holding period for the transaction type, the applicable haircut (\( H_M \)) is calculated using the following square root of time formula:

\[ H_M = H_N \sqrt{\frac{T_M}{T_N}} \], where

(1) \( T_M \) equals 5 for repo-style transactions and 10 for eligible margin loans;

(2) \( T_N \) equals the holding period used by the Board-regulated institution to derive \( H_N \); and

(3) \( H_N \) equals the haircut based on the holding period \( T_N \).

(C) If the number of trades in a netting set exceeds 5,000 at any time during a quarter, a Board-regulated institution must calculate the haircut using a minimum holding period of twenty business days for the following quarter except in the calculation of the exposure amount for purposes of §217.35. If a netting set contains one or more trades involving illiquid collateral or an OTC derivative that cannot be easily replaced, a Board-regulated institution must calculate the haircut using a minimum holding period of twenty business days. If over the two
§ 217.38  Unsettled transactions.

(a) Definitions. For purposes of this section:

(1) Delivery-versus-payment (DvP) transaction means a securities or commodities transaction in which the buyer is obligated to make payment only if the seller has made delivery of the securities or commodities and the seller is obligated to deliver the securities or commodities only if the buyer has made payment.

(2) Payment-versus-payment (PvP) transaction means a foreign exchange transaction in which each counterparty is obligated to make a final transfer of one or more currencies only if the other counterparty has made a final transfer of one or more currencies.