

Content of question:

Is it possible to interpret the provisions of Annex 16, II, 3, h, 3 to Decree No. 123/2007 Coll. in the sense that even collateral not meeting the general eligibility criteria can be recognised in the case of repurchase transactions or securities lending or borrowing transactions, and that only a stricter volatility adjustment will apply, namely the volatility adjustment for non-main index equities listed on a recognised stock exchange?

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Approved by: **Pavel Vacek**

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Piece of law	Decree No. 123/2007 Coll. (as amended)
Provision	Articles 103 and 104 Annexes 15 and 16
Explanation	<p>The liable entity must always evaluate first whether a given credit risk mitigation technique meets the basic eligibility prerequisites pursuant to Article 103 of the Decree; furthermore, in the case of financial collateral it must also assess the conditions pursuant to Annex 15, A, I, 2. Only after the conclusion that all eligibility prerequisites and conditions are met is reached, it may proceed pursuant to Article 104 and Annex 16 to the Decree.</p> <p>Consequently, the provision of Annex 16, II, 3, h), 3 needs to be understood in the above-mentioned context. Therefore, ineligible financial collateral cannot be reflected in the calculation of the capital requirement.</p> <p>In the case of a security sold or provided as collateral under a repurchase transaction or lent under a securities lending transaction a capital requirement to cover the risk of the counterparty to the repurchase or the lending transaction is determined, in addition to the capital requirement for the credit risk of the security's issuer. Pursuant to Article 87, 2, or to Annex 13, IV, 1, i) the exposure amount corresponding to the securities is increased using the appropriate volatility adjustment pursuant to Annex 16. The above mentioned provision of Annex 16, II, 3, h), 3 is related to the very instances of repurchase transactions or securities or commodities lending or borrowing transactions where the relevant volatility adjustment is applied to the amount of the exposure (not the collateral), and only in those cases where the exposure takes the form of an ineligible security. This is also the reason why the wording of the Decree says "securities or commodities lent or sold" and not "securities received as financial collateral".</p>