

Content of question:

A liable entity intends to estimate conversion factors for off-balance sheet retail exposures within the IRB Approach by estimating first the value of the exposure at default, i.e. value E, by means of the model and determining subsequently the conversion factor in a manner utilising the previously calculated value of E. Is this procedure in keeping with the Decree?

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Approved by: **Pavel Vacek**

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Piece of law	Decree No. 123/2007 Coll.
Provision	Annex 10, B Annex 13, IV, 1, k)
Explanation	<p>Decree No. 123/2007 Coll. requires that the liable entity use the conversion factor as one of the risk parameters within the IRB Approach and in the calculation of risk-weighted exposure amounts and expected credit losses. The values of this parameter are laid down in Annex 13, IV, 1, k) and the requirements for quantifying conversion factors are laid down in Annex 10, B, or specifically in Annex 10, B, p). These requirements must be met, they relate, for example, to the length of time series, the margin of conservatism where appropriate, factoring all relevant information into the estimates, regular updating, taking account of an economic downturn.</p> <p>The suggested procedure is not in contradiction with the Decree. Let us also mention the provision of Annex 10, B, d) which allows for the liable entity to estimate first the expected loss rate and base the breakdown into factors determining the values of risk parameters on it.</p> <p>However, the liable entity must always be able to distinguish conversion factors related to individual transaction grades and pools of exposures based on its calculations and, inter alia, to apply them to corresponding (off-balance sheet) exposures in relevant regulatory reports.</p>