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NATIONAL BANK OF MOLDOVA

D E C I S I O N
on the approval of the Regulation on the treatment of Credit Valuation Adjustment risk for banks

No 103 of 16.04.2020
(in force as of 01.01.2021)

Official Monitor of the Republic of Moldova No 118-123 Art. 465 of 22.05.2020

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REGISTERED:
by the Ministry of Justice
of the Republic of Moldova
No 1564 of May 8, 2020

Pursuant to Art.27 paragraph (1) point c) of the Law No 548/1995 on the National Bank of Moldova (republished in the Official Monitor of the Republic of Moldova, 2015, No 297-300, Art.544), with subsequent amendments, Art.60 paragraph (4) and Art.73 of the Law No 202/2017 on the activity of banks (Official Monitor of the Republic of Moldova, 2017, No 434-439, Art.727), the Executive Board of the National Bank of Moldova

DECIDES:

1. The Regulation on the treatment of credit valuation adjustment risk for banks is approved (attached).

2. This Decision is published in the Official Monitor of the Republic of Moldova and enters into force starting from 01.01.2021.

CHAIRMAN
OF THE EXECUTIVE BOARD **Octavian ARMAŞU**

No 103. Chişinău, April 16, 2020.

Approved
by the Decision of the Executive Board
of the National Bank of Moldova
No 103 of April 16, 2020

REGULATION
on the treatment of Credit Valuation Adjustment risk for banks

This Regulation transposes Articles 381, 382, 384, 385, 386 paragraph (1) point (a), paragraph (2) and (3) of Regulation (EU) No 575/2013 of the European Parliament and of the Council of June 26, 2013 on prudential requirements for credit institutions and investment firms and amending Regulation (EU) No 648 /2012 (Text with EEA relevance), published in the Official Journal of the European Union No L 176 of June 27, 2013, as last amended by Delegated Regulation (EU) 2015/62 of the Commission of October 10, 2014.

Chapter I
GENERAL PROVISIONS

1. This Regulation establishes methodologies for determining own funds requirements to cover credit valuation adjustment risk (CVA risk) and the conditions that banks must comply with for the use of those methodologies.

2. This Regulation shall apply to banks headquartered in the Republic of Moldova, as well as to branches in the Republic of Moldova of banks from other states, which are licensed by the National Bank of Moldova, hereinafter referred to as banks.

Chapter II
CREDIT VALUATION ADJUSTMENT

3. For the purposes of this Regulation, Credit Valuation Adjustment (CVA) shall mean an adjustment to the market average rate of the portfolio of transactions concluded with a counterparty.

4. The CVA reflects the current market value of the credit risk that the counterparty represents to the bank but does not reflect the current market value of the credit risk that the bank represents to the counterparty.**5.** Banks shall report the exposure to credit valuation adjustment risk in accordance with the requirements set out in the Instruction on the submission by banks of COREP reports for supervisory purposes, approved by HCE No 117/2018.

Chapter III
OWN FUNDS REQUIREMENTS FOR CVA RISK

6. A bank shall calculate the own funds requirements for CVA risk in accordance with this Regulation for all OTC derivatives in respect of all of its activities, other than credit derivatives recognized for the purpose of reducing risk-weighted exposure amounts for credit risk.

7. A bank shall include securities financing transactions in the calculation of own funds requirements as provided in point 6, if the bank's exposures to CVA risk arising from these transactions represent 5% of eligible capital.

8. Transactions with a qualified central counterparty (QCCP, which means a central counterparty as defined in point 3 of the Regulation on the treatment of counterparty credit risk for banks and is authorized in an EU member state) and transactions between a client and a clearing member where the clearing member acts as an intermediary between the client and a QCCP, and where the transactions give rise to an exposure of the clearing member to the QCCP, are excluded from the application of own funds requirements for CVA risk.

9. The following transactions are excluded from the application of own funds requirements for CVA risk:

1) transactions with the National Bank of Moldova and the Ministry of Finance of the Republic of Moldova;

2) transactions with multilateral development banks listed in Chapter IV, Section 4 of the Regulation on the treatment of credit risk for banks according to the standardized method, approved by Decision of the Executive Board of the National Bank of Moldova No 111/2018;

3) transactions with the counterparties referred to in Chapter IV, Section 1 and Section 2 of Regulation No 111/2018 on the treatment of credit risk for banks under the standardized method;

4) transactions with public sector entities referred to in Chapter IV, Section 3 of Regulation No 111/2018 on the treatment of credit risk for banks under the standardized method;

5) transactions within the group. For the purposes of this point, an intragroup transaction is a transaction based on an OTC derivative contract entered into by a bank from the Republic of Moldova with another counterparty from the Republic of Moldova which are part of the same group where both counterparties are fully included in the same consolidation and are subject to appropriate risk assessment, measurement and control procedures.

Chapter IV
STANDARDIZED METHOD AND ALTERNATIVE TO THE STANDARDIZED METHOD

10. A bank shall calculate a portfolio own funds requirements for CVA risk for each counterparty in accordance with the formula below, taking into account CVA hedges that are eligible in accordance with Chapter V:

$$K = 2.33 \cdot \sqrt{h} \cdot \sqrt{\left(\sum_i 0.5 \cdot w_i \cdot \left(M_i \cdot EAD_i^{total} - M_i^{hedge} B_i\right) - \sum_{ind} w_{ind} \cdot M_{ind} \cdot B_{ind}\right)^2 + \sum_i 0.75 \cdot w_i^2 \cdot \left(M_i \cdot EAD_i^{total} - M_i^{hedge} B_i\right)^2}$$

where:

1) h = one-year risk horizon (in units of a year); h = 1;

2) w_i = the weight applicable to counterparty 'i' as follows:

a) counterparty 'i' shall be mapped to one of the six weights wi based on an external credit assessment carried out by a designated external credit assessment institution (ECAI), as provided in Table 1.

Table 1

Credit quality step	1	2	3	4	5	6
Weight w_i	0,7%	0,8%	1,0%	2,0%	3,0%	10,0%

b) in the case of a counterparty for which a credit assessment by a nominated ECAI is not available, a bank shall assign to that counterparty the weight wi=1.0%. However, if a bank applies Chapter IV Section 15 of Regulation No 111/2018 on the treatment of credit risk for banks under the standardized method for credit risk exposures of this counterparty, risk-weighted, the weight wi=3.0 % is assigned;

3) M_i = the actual maturity of the transactions with counterparty 'i';

4) EAD_i^{total} = the total counterparty credit risk exposure value of counterparty 'i' (summed across its netting sets), including the effect of collateral in accordance with the methods set out in Chapters III to V of the Regulation on the treatment of counterparty credit risk for banks, applicable to the calculation of own funds requirements for counterparty credit risk for that counterparty.

The bank applying one of the methods provided in Chapters III and IV of the Regulation on the treatment of counterparty credit risk for banks shall use as EADitotal the fully adjusted exposure value in accordance with point 92 of the Regulation on credit risk mitigation techniques used by banks, approved by Decision of the Executive Board of the National Bank of Moldova No 112/2018.

The exposure is discounted by applying the following factor:

$$\frac{1 - e^{-0.05 \cdot M_i}}{0.05 \cdot M_i}$$

5) M_i^{hedge} = the maturity of the hedge instrument with notional B_i (the quantities M_i^{hedge} B_i are to be summed, if these are several positions);

6) B_i = the notional amount of single name credit default swap hedges purchased (summed if more than one position), referencing to counterparty 'i' and used to hedge CVA risk. That notional amount shall be discounted by applying the following factor:

$$\frac{1 - e^{-0.05 \cdot M_i^{hedge}}}{0.05 \cdot M_i^{hedge}}$$

7) w_{ind} = the weight applicable to index hedges, according to table 1;

8) M_{ind} = the maturity of the index hedge

9) B_{ind} = is the full notional of one or more index credit default swap of purchased protection used to hedge CVA risk. That notional amount shall be discounted by applying the following factor:

$$\frac{1 - e^{-0.05 \cdot M_{ind}}}{0.05 \cdot M_{ind}}$$

11. Banks calculate own funds requirements for CVA risk for their counterparties using the standardized method.

12. As an alternative to the standardized method, for the instruments set out in Chapter III and subject to the prior approval granted by the National Bank of Moldova, banks using the initial exposure method set out in Chapter IV of the Regulation on the treatment of counterparty credit risk for banks may apply a multiplication factor equal to 10 to the resulting risk-weighted exposure amounts for the counterparty credit risk of these exposures, instead of calculating the own funds requirements for CVA risk.

13. For the purpose of applying the provisions of point 14, the bank will request prior approval from the National Bank of Moldova by submitting a request containing information that includes arguments regarding the appropriateness of using the alternative method to the standardized method and its impact on the size of own funds. The request is submitted to the National Bank of Moldova in Romanian and signed by the person authorized by the bank.

14. The National Bank of Moldova shall give a written decision on the request referred to in point 13, no later than 30 days from the date of its registration, regarding the approval or refusal of the use of the alternative method to the standardized method, informing the bank in writing of its decision. The National Bank of Moldova may set a longer deadline for the submission of the application for prior approval, which shall not exceed 90 days, under the conditions of the Administrative Code, with notification to the bank.

15. If the information referred to in point 13 is insufficient to make a decision on the application for prior approval, the National Bank of Moldova shall be entitled to request the submission of additional information.

16. The Bank shall be obliged to submit additional information within the deadline specified by the National Bank of Moldova, during which period the deadline referred to in point 14 shall be suspended.

17. In case of rejection of the application for prior approval, the grounds on which the application is rejected shall be indicated. The following shall be considered as grounds for refusal of the application for prior approval by the National Bank of Moldova:

1) submission to the National Bank of Moldova of erroneous, inauthentic and/or contradictory information.

2) based on the information provided, it is found that the use/application of the respective method may lead to an unjustified increase in own funds.

18. The Bank shall be entitled to apply the alternative method to the standardized method from the date of issuance of the prior approval by the National Bank of Moldova.

Chapter V
ELIGIBLE HEDGES AGAINST RISK

19. Risk hedges are eligible hedges for the purposes of calculating own funds requirements for CVA risk in accordance with Chapter IV only if they are used for the purpose of mitigating CVA risk and are effectively managed. They are also credit default swap instruments, or other equivalent hedging instruments that directly refer to the counterparty.

20. A bank does not reflect other types of counterparty risk hedges when calculating own funds requirements for CVA risk. In particular, credit default swap instruments of the type „nth-to-default" or divided into tranches and credit linked notes are not eligible hedges for the purpose of calculating own funds requirements for CVA risk.

21. Eligible hedges that are included in the calculation of own funds requirements for CVA risk shall not be included in the calculation of own funds requirements for specific risk set out in

Regulation No 114/2018 on the treatment of market risk under the standardized method and shall not be treated as a reduction of credit risk except for the credit risk of the counterparty within the same trading portfolio.