DECREE
of the National Bank of Slovakia
of 3 January 2012,

amending Decree No 4/2007 of the National Bank of Slovakia on banks' own funds of financing and banks' capital requirements and on securities dealers' own funds of financing and securities dealers' capital requirements as amended

In accordance with Article 30(8), Article 31(5), Article 32(11), Article 33(25), Article 33a(8), Article 33b(9), Article 33c(5) and (6), Article 33d(10), Article 33e(12), Article 39(15) and Article 48(8) of Act No 483/2001 Coll. on banks and on amendments to certain laws as amended, and in accordance with Article 74(9), Article 74a(10) and Article 139(9) of Act No 566/2001 Coll. on securities and investment services and on amendments to certain laws (the Securities Act) as amended, the National Bank of Slovakia stipulates as follows:

Article 1

Decree of National Bank of Slovakia of 13 March 2007 No 4/2007 on banks' own funds of financing and banks' capital requirements and on securities dealers' own funds of financing and securities dealers' capital requirements (Notification No 121/2007 Coll.) as amended by Decree No 10/2007 (Notification No 420/2007 Coll.), Decree No 17/2008 (Notification No 443/2008 Coll.), Decree No 12/2010 (Notification No 279/2010 Coll.) and Decree No 3/2011 (Notification No 145/2011 Coll.) shall be amended as follows:

1. Paragraph (6) shall be added to Article 3 that shall read:
"(6) Assets valued at fair value shall be subject to the procedure referred to in Article 154. Any adjustment to the valuation shall be deducted from the amount of the bank's own funds.".

2. In Article 6(1)(d), the following words shall be added at the end:
"and the amount of securitization positions in the trading book which have received a risk weight of 1,250% if they are recorded in the banking book".

3. In Article 6(4), the following words shall be added at the end:
"including the calculation of own funds requirement to cover the specific and general risks of capital instruments and the calculation of own funds requirement to cover the risks in accordance with Article 30(5)(b) and (c) of the Banking Act".

4. In Article 19(1), the number "4" shall be replaced with the number "5".

5. In Article 19(1), the following words shall be added at the end of the second sentence:
"(5), (6) and (10)".

6. Paragraph (5) shall be added to Article 19 that shall read:
"(5) Exposures to higher territorial units or municipalities of a Member State denominated and funded in the domestic currency of that Member State shall be assigned a risk weight of 20%.".

7. In Article 27(1), the words "(2) to (4)" shall be replaced with the words "(2) and (3)".

8. In Article 35 paragraph (2), subparagraph (c) shall be added that shall read:

“(c) The credit assessment shall not be based or partly based on unfunded support provided by the bank itself; in such case, the relevant position shall be considered as if it were not rated and the relevant treatment of unrated positions shall be applied as set out in Article 33b(8) of the Banking Act and Article 140(7), Article 143(3) and (4) and Article 145(1) and (2).”.

9. In Article 139, subparagraphs (u) and (v) shall be added that shall read:
“(u) “re-securitisation” means a securitisation where the risk associated with an underlying pool of exposures is tranched and at least one of the underlying exposures is a securitisation position;
v) “re-securitisation position” means an exposure to a re-securitisation.”.

10. In Article 140(6), the following sentences shall be added at the end:
“Alternatively, such overlap between the specific risk amount corresponding with capital charges for positions in the trading book and the amount corresponding with capital charges for positions in the banking book may also be recognised, provided that it is possible to calculate and compare the capital charges for the relevant positions. Where Article 35(2)(c) applies to positions in the ABCP, the bank may, subject to the approval from the National Bank of Slovakia, use the risk-weight assigned to a liquidity facility in order to calculate the risk-weighted exposure amount for the ABCP if the liquidity facility ranks pari passu with the ABCP so that they form overlapping positions and 100% of the ABCP issued by the programme is covered by liquidity facilities.”.

11. In Article 141, paragraph (12) shall read:
“(12) Where an originator bank or sponsor bank, in respect of a securitisation, proceeded pursuant to paragraphs (1) to (3) in the calculation of risk-weighted exposure amounts or has sold instruments from its trading book to a securitisation special purpose entity, due to which it is no longer required to hold own funds for the risks of those instruments, this bank shall not, with a view to reducing potential or actual losses of investors, provide support to the securitisation beyond its contractual obligations.”.

12. In Article 143, paragraph (1) shall read:
“(1) Subject to paragraph (3), the risk-weighted exposure amount of a rated securitisation position or re-securitisation position shall be calculated by applying to the exposure value the risk weight associated with the credit quality step to which the National Bank of Slovakia has assigned the external rating in accordance with respective provisions of the Banking Act concerning the securitisation positions pursuant to Table 23.

Table 23

Credit quality step	1	2	3	4 (only for other than short-term credit assessments)	All other credit quality steps
Securitisation positions	20%	50%	100%	350%	1,250%
Re-securitisation positions	40%	100%	225%	650%	1,250%

”.

13. In Article 146, paragraph (1) shall read:
“(1) Under the ratings based method, the risk-weighted exposure amount of a rated securitisation or re-securitisation position shall be calculated by applying to the exposure value the risk weight associated with the credit quality step to which the rating was assigned by the National Bank of Slovakia in accordance with the respective provisions of the Banking Act for securitisation positions pursuant to Table 26, multiplied by 1.06.

Table 26

Credit quality step		Risk weightings for securitisation positions			Risk weightings for re-securitisation positions	
Other than short term credit assessments	**Short term credit assessments**	A	B	C	D	E
1	1	7%	12%	20%	20%	30%
2		8%	15%	25%	25%	40%
3		10%	18%	35%	35%	50%
4	2	12%	20%		40%	65%
5		20%	35%		60%	100%
6		35%	50%		100%	150%
7	3	60%	75%		150%	225%
8		100%			200%	350%
9		250%			300%	500%
10		425%			500%	650%
11		650%			750%	850%
All other ratings and unrated		1,250%				

”.

14. In article 146, paragraph (2) shall read:

“(2) The risk weightings in column C of table 26 shall be applied where the securitisation position is not a re-securitisation position and where the effective number of exposures securitised is less than six. For the remainder of the securitisation positions that are not re-securitisation positions, the weightings in column B shall be applied unless the position is in the most senior tranche of a securitisation, in which case the weightings in column A shall be applied. For re-securitisation positions, the weightings in column E shall be applied unless the re-securitisation position is in the most senior tranche of the re-securitisation and none of the underlying exposures are themselves re-securitisation exposures, in which case column D shall be applied. When determining whether a securitisation tranche is the most senior, it is not required to take into consideration amounts due on the interest rate or currency derivative contracts, fees due, or other similar payments.”.

15. In article 146(3), the third sentence shall be deleted.

16. In article 147(1), the introductory sentence shall read:

“(1) The value corresponding to the risk weight applicable to a securitisation position under the supervisory formula method set out in this Decree shall be calculated in accordance with the following formula and it shall be no less than 20% for re-securitisation positions and no less than 7% for all other securitisation positions:”.

17. In article 147(1), the words “Article 146(4)” shall be replaced with the words “Article 146(3); In the case of re-securitisations, the number of securitisation exposures in the pool shall be taken into account and not the number of underlying exposures in the original pools from which the underlying securitisation exposures stem.”.

18. In Article 152(2), subparagraph (a) shall be deleted. The present subparagraphs (b) to (e) shall become subparagraphs (a) to (d).

19. In Article 154(1)(a), the words “guidelines for the use of unobservable inputs reflecting the bank’s assumptions of what market participants would use in pricing the positions“ shall be added after the words „verifying their appropriateness”.

20. In Article 154(2), a new first sentence shall be added at the beginning that shall read:
“Bank’s positions shall be marked to market whenever possible.”.

21. In Article 154(4), the first sentence shall read:
“Where marking to market under paragraph (3) is not possible, the bank shall conservatively mark to model its positions or sets of positions before calculating the respective capital requirement for covering risks from positions recorded in the trading book.”.

22. In Article 154(5)(a), the words “or of other fair-valued positions” shall be added after the words “the items of the trading book”.

23. In Article 154(7), the words “or creating special reserves” shall be deleted.

24. In Article 154(8), a new second sentence and a new third sentence shall be added after the first sentence that shall read:
“A bank shall establish and maintain procedures for calculating an adjustment to the current valuation of less liquid positions. Such adjustments shall be designed to reflect the reduced liquidity of the positions and shall be in addition to any changes to the value of the position required for the financial reporting purposes.”.

25. In Article 154(8), the following sentence shall be added at the end:
“With regard to complex products including mainly securitisation exposures and n-th-to-default credit derivatives, the need for valuation adjustments shall be explicitly assessed to reflect the model risk associated with using a possibly incorrect valuation methodology and the model risk associated with using unobservable and possibly incorrect calibration parameters in the valuation model.”.

26. The title of Article 156 including Article 156 itself shall be deleted.

27. In Article 157(3)(b), the following words shall be added at the end:
“in which case the figure for potential future credit exposure of the institution shall be limited to the amount of premiums which are not yet paid by the entity to the bank;”.

28. In Article 159, paragraph (1) shall read:

“(1) For the purposes of calculating capital requirements for the specific debt instrument risk, the net interest-rate positions in instruments that are not securitisation positions shall be assigned to categories on the basis of their issuer/obligor, external or internal credit assessment and residual maturity, and then multiplied by the coefficients shown in Table 28. The capital requirement for specific debt instrument risk for positions that are securitisation positions shall be calculated in accordance with Article 159(7). For the purposes of this provision the bank may cap the product of the weight and the net position at the maximum possible default-risk related loss. For a short position, that limit may be calculated as a change in value due to the underlying instruments immediately becoming risk-free, in case of default.”.

29. In Article 159, paragraphs (6) to (11) shall be added that shall read:

“(6) By way of derogation from paragraphs (1) to (4) a bank may determine the larger of the following amounts as the specific risk capital charge for the correlation trading portfolio:

(a) the total specific risk capital charges that would apply just to the net long positions of the correlation trading portfolio;
(b) the total specific risk capital charges that would apply just to the net short positions of the correlation trading portfolio.

(7) The correlation trading portfolio shall consist of the securitisation positions and the n-th-to-default credit derivatives that meet the following criteria:
(a) the positions are neither re-securitisation positions, nor options on a securitisation tranche, nor any other derivatives of securitisation exposures that do not provide a pro-rata share in the proceeds of a securitisation tranche;
(b) all reference instruments are either single-name instruments, including single-name credit derivatives for which a liquid two-way market exists, or commonly-traded indices based on those reference entities.

(8) Positions which reference either of the following shall not be part of the correlation trading portfolio:
(a) an underlying instrument that is capable of being assigned to the exposure classes referred to in Article 31(1)(h) and (i) of the Banking Act in the banking book or
(b) a claim against a special purpose entity.

(9) The correlation trading portfolio may include positions which are neither securitisation positions nor n-th-to-default credit derivatives but which hedge other positions of that portfolio, provided that a liquid two-way market exists for this instrument or its underlying instruments. A two-way market is deemed to exist where there are independent bona fide offers to buy and sell so that a price reasonably related to the last sales price or current bona fide competitive bid and offer quotations can be determined within 1 day and settled at such price within a relatively short time conforming to the trade custom.

(10) For instruments in the trading book that are securitisation positions, the bank's net positions shall be weighted as follows:
(a) for securitisation positions that would be subject to the Standardised Approach for credit risk in the same bank's banking book, 8% of the risk weight under the Standardised Approach as set out in Article 143;
(b) for securitisation positions that would be subject to the Internal Ratings Based Approach in the same bank's non-trading book, 8% of the risk weight under the Internal Ratings Based Approach as set out in Articles 145 to 150.

(11) For the purposes of paragraph (10), the Supervisory Formula Method under Article 147 may be used with prior consent by the National Bank of Slovakia only by a bank other than an originator bank that may apply it for the same securitisation position in its banking book. The PD and LGD estimates as inputs to the Supervisory Formula Method under Article 147 may be determined in accordance with the Internal Ratings Based Approach referred to in Article 33 of the Banking Act, or - subject to prior consent by the National Bank of Slovakia - may be based on estimates that are derived from an approach set out in Article 187(4) and that are in line with the quantitative standards for the Internal Ratings Based Approach. Notwithstanding paragraph (10), for securitisation positions that would be subject to a risk weight in accordance with Article 150a, provided they were in the same bank's banking book, 8% of the risk weight in accordance with that Article shall be applied. For the purposes of calculating the specific risk capital charge, the weighted positions resulting from the application of paragraphs (10) and (11) shall be added together.".

30. In Article 164(2), a new second sentence shall be added after the first sentence that shall read: “The notional value may be replaced by the notional value, minus any market value changes of the credit derivative since trade inception.”.

31. In Article 164(11), the following sentence shall be added at the end:
“Where a default credit derivative is rated by an ECAI, the specific risk capital charge shall be calculated using the rating of the default credit derivative and the respective securitisation risk weights shall be applied as appropriate.”.

32. In Article 167(1), the number “0.04” shall be replaced with the number “0.08”.

33. In Article 169(1)(c) and (d), the words “Article 156” shall be replaced with the words “Article 178a”.

34. In Article 170(3)(c), the words “Article 156” shall be replaced with the words “Article 178a”.

35. In the title of Chapter Three, the words “risk, settlement risk” shall be added after the word “foreign-exchange”.

36. In Article 171(1), the following sentence shall be added at the end:
“The capital requirement for the settlement risk shall be calculated from position values booked in the trading book and banking book.”.

37. Article 178a shall be added after Article 178 that shall read:

“Article 178a

(1) Where transactions in financial instruments or commodities, with the exception of repo trades and reverse repo trades, securities or commodities lending and securities or commodities borrowing are not settled within four working days following delivery of the financial instruments or commodities, the capital requirement for settlement risk shall be calculated.

(2) The capital requirement for settlement risk shall be calculated as the sum of the price differences of unsettled transactions multiplied by the conversion figures in paragraph (3), provided these differences would mean a loss for the bank. Price differences shall be determined as the difference between the agreed settlement price and the price of the financial instruments or commodities identified for the evaluation under Article 154 and valid for the reporting date.

(3) The conversion figure for calculating the capital requirement for settlement risk shall be
(a) 0.08 where 5 to 15 working days have elapsed since the settlement date;
(b) 0.50 where 16 to 30 working days have elapsed since the settlement date;
(c) 0.75 where 31 to 45 working days have elapsed since the settlement date;
(d) 1.00 where more than 45 working days have elapsed since the settlement date.

(4) In the case of the delivery of financial instruments or commodities in advance, the capital requirements under paragraph (5) shall be calculated, if:
(a) the bank has paid for the financial instruments or commodities before receiving them or it has already delivered the financial instruments or commodities before receiving payment for them; and
(b) in the case of cross-border transactions, one day or more has elapsed since the bank made that payment or delivery.

(5) From the moment of the transfer of the first contractual payment or delivery leg up to four working days after the second contractual payment or delivery leg, the claim shall be treated as an exposure in the banking book. From five working days after the second contractual payment or delivery leg until the expiry of the transaction, the claim shall be deducted from own funds.

(6) In applying a risk weight to claims treated as exposures in the banking book, a bank using the internal ratings based approach may assign PDs (probability of default) to counterparties towards which it has no other banking book exposure, on the basis of the counterparty's external credit assessment. Where own estimates of loss given defaults ("LGDs") are used the LGD set out in paragraph 50(2) may be applied to claims treated as exposures in the banking book provided that they are applied to all such exposures. Alternatively, where the internal ratings based approach is used the risk weights under the provisions on the standardised approach of credit risk may be applied provided that they are applied to all such exposures, or a 100% risk weight may be applied to all such exposures. If the amount of a positive exposure resulting from transactions under this paragraph is not material, a risk weight of 100% may be applied to these exposures.

(7) In the case of a system-wide failure of a settlement or clearing system the requirements under paragraphs (1) to (6) shall not be calculated until the situation is rectified. In this case the non settlement of a transaction by counterparty shall not be deemed as default for the purposes of credit risk.".

38. In Article 185(1), the introductory sentence shall read:
"(1) The criteria for the specification of risk factors in the calculation of the capital charge for market risk using an internal market risk model shall be deemed fulfilled if this calculation is influenced by the risk factors in terms of the bank's operations in individual markets and the nature of these markets, if the bank is able to justify that a risk factor is incorporated into the bank's pricing model but not into the risk-measurement model, if the risk-measurement model captures non-linearities for options and other products as well as correlation risk and basis risk, if the bank, when proxies for risk factors are used, is able to show a good track record for the given position held, and if it is true that at least…".

39. In Article 186, subparagraph (e) shall read:
"(e) data sets are renewed at least once a month;".

40. In Article 186, subparagraph (h) shall be deleted. The present subparagraphs (i) to (l) shall be marked as (h) to (k).

41. In Article 186, subparagraphs (h) to (j) shall read:
" (h) the minimum multiplication factor is 3; the value of the multiplication factor is increased by the value of the plus factor stated in Table 33, depending on the number of over-shootings in the course of the last 250 working days, where an over-shooting represents a one-day change in the value of a portfolio higher than the value-at-risk generated by the internal market risk model; where it is demonstrated that the multiplication factor increased by the value of the plus factor stated in Table 33 is not justified, the National Bank of Slovakia may waive this requirement in its prior approval of the own model for market risk calculation;
(i) for the purposes of determining the plus factor, the number of over-shootings under subparagraph (h) are assessed at least quarterly, the number of over-shootings shall be evidenced by the back-testing of the value-at-risk measure on the basis of hypothetical and actual changes in the portfolio's value and the number of over-shootings shall be equal to the higher of the number of over-shootings under hypothetical and actual changes in the value of the portfolio;

j) the accuracy and operation of the internal market risk model are monitored daily with the aid of a back-testing programme; for each working day, using back-testing, a comparison is generated of the one day-value-at-risk calculated by the internal market risk model with the difference of the actual value of the bank's portfolio for the following day and with the actual value of the bank's portfolio for the respective day (back-testing on actual changes in the portfolio's value), or with the difference of the theoretical value of the bank's portfolio for the following day and the actual value of the bank's portfolio for the respective day, assuming unchanged positions (back-testing on hypothetical changes in the portfolio's value).".

42. After Article 186, Article 186a shall be added that shall read:

„Article 186a

(1) In addition to the requirements under Article 186, the internal market risk model determining the value-at-risk shall also fulfil the following requirements:

(a) a "stressed value-at-risk" shall be calculated based on the value-at-risk measure of the current portfolio for the 10-day period or a shorter period, but corrected to the equivalent of 10 days, and with a one-tailed confidence interval of 99%, where value-at-risk model inputs are calibrated to historical data from a continuous minimum 12-month period of significant financial stress relevant to the bank's portfolio; the historical data shall be subject to approval by the National Bank of Slovakia in accordance with Article 33c(1) of the Banking Act; and shall be reviewed at least annually while the stressed value-at-risk shall be calculated at least weekly;

(b) a capital requirement shall be met on a daily basis, expressed as the sum of the following values:

1. the higher value of:

1a. its previous day's value-at-risk number calculated in accordance with Article 186(a) to (e) (VaR t-1);

1b. an average of the daily value-at-risk measures in accordance with Article 186(a) to (e) on each of the preceding sixty working days (VaR avg), multiplied by the multiplication factor;

2. the higher value of:

2a. the bank's latest available stressed value-at-risk figure in accordance with point (a) (sVaRt-1);

2b. an average of the stressed value-at-risk figures calculated in the manner and frequency specified in point (a) during the preceding sixty working days (sVaR avg), multiplied by the multiplication factor;

(c) when the internal model is used to calculate the specific risk capital charge, the capital charge shall be calculated as the sum of the following values:

1. the capital charge value calculated in accordance with Articles 158 to 168 for the position risks of securitisation positions and the nth-to-default credit derivatives in the trading book with the exception of those incorporated in the capital charge in accordance with Article 187(15);

2. the higher value of:

2a. the most recent measure of incremental default and migration risk;

2b. the 12 weeks average measure of incremental default and migration risk in accordance with Article 187(4);

3. or, where applicable, the higher value of:

3a. the most recent measure of all price volatility risks;

3b. 12-week-average measure of all price volatility risks in accordance with Article 187(15);

(d) reverse stress tests shall also be carried out.

(2) A reverse stress test means a stress test carried out in a reverse order to determine, based on a pre-defined hypothetical impact of a monitored phenomenon in the future, which stress scenarios might occur with regard to the pre-defined impact and the resulting effects of the monitored phenomenon.”.

43. Article 187 shall read:

“Article 187

(1) For the purposes of calculating the specific risk capital charge for debt instruments and the specific risk capital charge for capital instruments, an internal market risk model shall be deemed to fulfil sufficient quantitative requirements provided that
(a) it explains the historical price variation in the portfolio;
(b) it is sensitive to changes in the structure of the bank’s portfolio and determines a higher risk value for a portfolio with increased asset exposure (concentration);
(c) it is robust to all adverse influences;
(d) its operation is validated through back-testing aimed at assessing whether specific risks are accurately estimated;
(e) it accurately estimates for debt and capital securities how big are the risks that a significant change in the real price of a financial instrument will occur in consequence of an unexpected event and that the issuer will not meet its commitments.

(2) When calculating the specific risk capital charge for debt instruments and the specific risk capital charge for capital instruments using an internal market risk model, a bank may exclude those positions in securitisations or n-th-to-default credit derivatives for which it meets the capital requirement for specific debt instrument risk, general debt instrument risk, specific capital instrument risk and general capital instrument risk, with the exception of those positions that are subject to the approach set out in paragraph (15).

(3) A bank shall not be required to capture incremental default and migration risks for traded debt instruments in its internal model where it is capturing those risks through the requirements set out in paragraphs (4) to (14).

(4) The bank subject to paragraphs (1) to (3) shall have an approach in place to capture, in the calculation of their capital requirements, the default and migration risks of its trading book positions that are incremental to the risks captured by the value-at-risk measure as specified in paragraphs (1) to (3). The approach shall meet soundness standards comparable to the approach set out in Article 33 of the Banking Act under the assumption of a constant level of risk, and adjusted where appropriate to reflect the impact of liquidity, concentrations, hedging and optionality.

(5) The approach to capture the incremental default and migration risks shall cover all positions subject to capital charge for specific interest rate risk but shall not cover the securitisation positions and the n-th-to-default credit derivatives. Subject to a prior approval in accordance with Article 33c of the Banking Act, the bank may consistently include all listed equity positions and derivatives positions based on listed equities for which such inclusion is consistent with the bank's method of internal measurement and management of risks. The approach shall reflect the impact of correlations between default and migration events. The impact of diversification between the default and migration events on the one hand and other market risk factors on the other hand shall not be reflected.

(6) The approach to capture the incremental default and migration risks shall measure losses due to default and losses due to internal or external ratings migration, at the confidence interval of

99.9% over a capital horizon of one year. Correlation assumptions shall be supported by the analysis of objective data in a conceptually sound framework. The approach to capture the incremental default and migration risks shall appropriately reflect issuer concentrations. Concentrations that can arise within and across product classes under stressed conditions shall also be reflected. The approach to capture the incremental default and migration risks shall be based on the assumption of a constant level of risk over the one-year capital horizon, implying that given individual trading book positions or sets of positions that have experienced default or migration over their liquidity horizon are re-balanced at the end of their liquidity horizon to attain the initial level of risk. Alternatively, a bank may consistently use the assumption of a one-year constant position.

(7) The liquidity horizons shall be set according to the time required to sell the position or to hedge all material relevant price risks in a stressed market, having particular regard to the size of the position. Liquidity horizons shall reflect the actual practice and experience during periods of both systematic and idiosyncratic stresses. The liquidity horizon shall be measured under conservative assumptions and shall be sufficiently long to ensure that the act of selling or hedging, in itself, does not materially affect the price at which the selling or hedging is executed. The appropriate liquidity horizon for a position or set of positions is at least three months. The determination of the appropriate liquidity horizon for a position or set of positions shall take into account the bank's internal policies relating to valuation adjustments and the management of stale positions. When the bank determines liquidity horizons for sets of positions rather than for individual positions, the criteria for defining sets of positions shall be defined in a way that meaningfully reflects differences in liquidity. The liquidity horizons shall be greater for positions that are concentrated, reflecting the longer period needed to liquidate such positions. The liquidity horizon for a securitisation warehouse shall reflect the time to build, sell and securitise the assets, or to hedge the material risk factors, under stressed market conditions.

(8) Hedges may be incorporated into the bank's approach to capture the incremental default and migration risks. Positions may be netted when long and short positions refer to the same financial instrument. Hedging or diversification effects associated with long and short positions involving different instruments or different securities of the same obligor, as well as long and short positions in different issuers, may only be recognised by explicitly modelling gross long and short positions in the different instruments. The bank shall reflect the impact of material risks that could occur during the interval between the hedge's maturity and the liquidity horizon, as well as the potential for significant basis risks in the hedging strategies by product, seniority in the capital structure, internal or external rating, maturity, vintage and other differences in the instruments. The bank shall reflect a hedge only where it can be maintained even if the obligor approaches a credit or other event. For trading book positions that are hedged via dynamic hedging strategies, a rebalancing of the hedge within the liquidity horizon of the hedged position may be recognised provided that the bank

(a) chooses to model rebalancing of the hedge consistently over the relevant set of trading book positions;
(b) demonstrates that the inclusion of rebalancing results in a better risk measurement;
(c) demonstrates that the markets for the instruments serving as hedges are liquid enough to allow for such rebalancing even during periods of stress; any residual risks resulting from dynamic hedging strategies must be reflected in the capital charge.

(9) The approach to capture the incremental default and migration risks shall reflect the nonlinear impact of options, structured credit derivatives and other positions with material nonlinear behaviour with respect to price changes. The bank shall also have due regard to the amount of model risk inherent in the valuation and estimation of price risks associated with such products.

(10) The approach to capture the incremental default and migration risks shall be based on data that are objective and up-to-date.

(11) The approach to capture the incremental default and migration risks shall be consistent with the bank's internal risk management methodologies for identifying, measuring, and managing trading risks. As part of the independent review of its risk measurement system and the validation of its internal market risk models, the bank shall, with a view to the approach to capture incremental default and migration risks, in particular

(a) validate that its modelling approach for correlations and price changes is appropriate for its portfolio, including the choice and weights of its systematic risk factors;
(b) perform a variety of stress tests, including sensitivity analysis and scenario analysis, to assess the qualitative and quantitative reasonableness of the approach, particularly with regard to the treatment of concentrations; such tests shall not be limited to the range of events experienced historically;
(c) apply appropriate quantitative validation including relevant internal modelling benchmarks.

(12) A bank shall document its approach to the capturing of incremental default and migration risks so that its correlation and other modelling assumptions are transparent.

(13) If the bank uses such an approach to the capturing of incremental default and migration risks that does not comply with all requirements under Article 187 but that is consistent with the bank's internal methodologies for identifying, measuring and managing risks, the bank shall be able to demonstrate that its approach results in a capital requirement that is at least as high as if it was based on an approach in full compliance with the requirements under Article 187. The compliance with this provision shall be reviewed by the National Bank of Slovakia at least annually.

(14) A bank shall perform the calculations required under its chosen approach to capture the incremental default and migration risks on a weekly basis at a minimum.

(15) A bank may use an internal approach to capture the incremental default and migration risks for calculating the capital charge instead of the specific risk capital charge for the correlation trading portfolio in accordance with Article 159(6) to (11), if

(a) such an internal approach adequately captures all price risks at the confidence interval of 99.9% over a capital horizon of one year under the assumption of a constant level of risk, and is adjusted where appropriate to reflect the impact of liquidity, concentrations, hedging and optionality; the bank may incorporate any positions in the approach that are jointly managed with positions of the correlation trading portfolio, and may then exclude those positions from the approach required under paragraph (4);
(b) the amount of the capital charge for all price risks is not less than 8% of the capital charge that would be calculated in accordance with Article 159(6) to (11) for all positions incorporated in the charge for all price risks;
(c) in particular, the following risks are adequately captured:
    1. the cumulative risk arising from multiple defaults, including the ordering of defaults, in tranched products;
    2. credit spread risk, including the gamma and cross-gamma effects;
    3. volatility of implied correlations, including the cross effect between spreads and correlations;
    4. basis risk, including
        4a. the basis between the spread of an index and the those of its constituent single names;

4b. the basis between the implied correlation of an index and that of bespoke portfolios;
5. recovery rate volatility, as it relates to the propensity for recovery rates to affect tranche prices;
6. to the extent the comprehensive risk measure incorporates benefits from dynamic hedging, the risk of hedge slippage and the potential costs of rebalancing such hedges;

(d) a bank shall have sufficient market data to ensure that it fully captures the salient risks of those exposures in the bank's internal approach; through back testing or other appropriate means it is demonstrated that the bank's risk measures can appropriately explain the historical price variation of those products; the bank is able to separate the positions for which it holds approval in order to incorporate them in the capital charge from those positions for which it does not hold such approval;

(e) with regard to portfolios subject to this paragraph, the bank regularly applies a set of specific, predetermined stress scenarios; such stress scenarios shall examine the effects of stress to default rates, recovery rates, credit spreads, and correlations on the profit and loss of the correlation trading desk; the bank shall apply such stress scenarios at least weekly and report at least quarterly to the National Bank of Slovakia the results, including comparisons with the bank's capital charge in accordance with this paragraph; any instances where the stress tests indicate a material shortfall of this capital charge shall be reported to the National Bank of Slovakia in a timely manner; based on those stress testing results, the National Bank of Slovakia shall consider a specific capital charge against the correlation trading portfolio as set out in Article 50(13) of the Banking Act;

(f) a bank shall calculate the capital charge to capture all price risks at least on a weekly basis.".

44. After Article 227c, Article 227d shall be added that shall read:

"Article 227d

In calculating the specific risk capital charge for debt instruments in accordance with Article 159(7), the weighted net long positions and the weighted net short positions shall be summed separately up to 31 December 2013. The larger of those sums shall constitute the specific risk capital requirement for debt instruments. The total sum of the bank's weighted net long and net short positions, broken down by types of underlying assets shall be reported to the National Bank of Slovakia.".

Article 2

This Decree shall enter into force on 31 January 2012.

Jozef Makúch v. r.
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