

بِسْمِ اللَّهِ الرَّحْمَنِ الرَّحِيمِ

مؤسسة النقد العربي السعودي

المركز الرئيسي

إدارة السياسات البنكية



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المحترمون

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السلام عليكم ورحمة الله وبركاته.

الموضوع: تحديث تعليمات التعرضات الكبيرة (LEX).

إحافاً لتعليمات المؤسسة الخاصة بالتعرضات الكبيرة الصادرة بتعميم المؤسسة رقم
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المتضمن التحديث على التعليمات.

نفيدكم بإجراء تحديثات على هذه التعليمات (مرفق) لتتوافق مع أفضل الممارسات
الدولية. وتؤكد المؤسسة على كافة البنوك والمصارف الالتزام بهذه التعليمات المحدثة اعتباراً من
تاريخه.

وتقبلوا تحياتي،

مركز

سليمان

فهد بن إبراهيم الشثري
وكيل المحافظ للرقابة

نطاق التوزيع:

البنوك والمصارف العاملة في المملكة



مؤسسة النقد العربي السعودي
Saudi Arabian Monetary Authority

Rules on Large Exposures of Banks

General Department Of Banking Control
Banking Policy Department

June 2018

أحمد



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Rules on Large Exposures of Banks

1. General Requirements:

1.1. Introduction:

These Rules are issued by SAMA in exercise of the powers vested upon it under its Charter issued by the Royal Decree No.23 on 23-05-1377H (15 December 1957G) and the Banking Control Law issued by the Royal Decree No. M/5 on 22-02-1386H (11 June 1966G) and the rules for Enforcing its Provisions issued by Ministerial Decision No 3/2149 on 14/10/1406H.

These Rules sets out the minimum requirements on large exposures including the limits on a bank's exposures to a single counterparty, groups of connected counterparties and related counterparties as well as the types of exposures to be included in or excluded from those limits, and the regulatory reporting requirements for large and connected exposures.

These Rules shall supersede the existing SAMA rules regarding Limits on Credit Exposures issued vide SAMA Circular of June 1994.

1.2. Definitions:

The following terms and phrases, where used in these Rules, shall have the corresponding meanings, unless the context requires otherwise:

- i. SAMA:* the Saudi Arabian Monetary Agency.
- ii. Rules:* Rules for Large Exposures of banks.
- iii. Subsidiary:* include a subsidiary where a bank owns more than 50% of its shareholding.
- iv. Exposure:* include both on and off-balance sheet exposures included in either the banking or trading books, and instruments with counterparty credit risk under the Basel risk-based capital framework. Banking and trading books have the same meaning as under the Basel risk-based capital framework.



- v. **Large Exposure:** if the sum of all exposures values of a bank to a single counterparty or to a *Group of Connected Counterparties* is equal to or above 10% of the bank's eligible capital base. The exposures values have to be measured and eligible capital base calculated as per requirements set out under these Rules.
- vi. **Eligible Capital Base:** is the effective amount of Common Equity Tier 1 capital fulfilling the criteria defined in Part 1 of the Basel III framework.
- vii. **Control Relationship:** Control relationship will be deemed to exist automatically if one entity owns more than 50% of the voting rights of another entity. In addition, banks must assess connectedness between counterparties based on control, using the following criteria:
 - a. Voting agreements (e.g. control of a majority of voting rights pursuant to an agreement with other shareholders);
 - b. Significant influence on the appointment or dismissal of an entity's administrative, management or supervisory body, such as the right to appoint or remove a majority of members in those bodies, or a majority of members have been appointed solely as a result of the exercise of an individual entity's voting rights;
 - c. Significant influence on senior management, e.g. an entity has the power, pursuant to a contract or otherwise, to exercise a controlling influence over the management or policies of another person (e.g. through consent rights over key decisions);

Banks are also expected to refer to criteria specified in appropriate internationally recognized accounting standards (The International Accounting Standards – IAS and International Financial Reporting Standards - IFRS are applied to all banks in KSA) for further qualitatively based guidance when determining control.

Where control has been established based on any of these criteria, a bank may still demonstrate to SAMA in exceptional cases, e.g. due to the existence of corporate



governance safeguards, that such control does not necessarily result in the entities concerned constituting a group of connected counterparties.

viii. ***Economic Interdependence:*** In establishing connectedness based on economic interdependence, banks must consider, at a minimum, the following qualitative criteria:

- a. Where 50% or more of one counterparty's gross receipts or gross expenditures (on an annual basis) is derived from transactions with the other counterparty (eg the owner of a residential/commercial property and the tenant who pays a significant part of the rent);
- b. Where one counterparty has fully or partly guaranteed the exposure of the other counterparty, or is liable by other means, and the exposure is so significant that the guarantor is likely to default if a claim occurs;
- c. Where a significant part of one counterparty's production/output is sold to another counterparty, which cannot easily be replaced by other customers;
- d. When the expected source of funds to repay each loan of both counterparties is the same and neither counterparty has another independent source of income from which the loan may be serviced and fully repaid (as amended by BCBS via its FAQ issued on September 29, 2016);
- e. Where it is likely that the financial problems of one counterparty would cause difficulties for the other counterparties in terms of full and timely repayment of liabilities;
- f. Where the insolvency or default of one counterparty is likely to be associated with the insolvency or default of the other(s);
- g. When two or more counterparties rely on the same source for the majority of their funding and, in the event of the common provider's default, an alternate provider cannot be found. In this case, the funding problems of one counterparty are likely to spread to another due to a one-way or two-way dependence on the same main funding source.

Banks will be required to demonstrate to SAMA that a counterparty who is economically closely related to another counterparty may overcome financial difficulties or even the second counterparty's default by finding alternative



business partners or funding sources within an appropriate time period, and thus the bank does not need to combine these counterparties to form a group of connected counterparties despite meeting some of the above criteria.

There are cases where a thorough investigation of economic interdependencies will not be proportionate to the size of the exposures. Therefore, banks are expected to identify possible connected counterparties on the basis of economic interdependence in all cases where the sum of all exposures (including guarantors) to one individual counterparty or a group of connected counterparties exceeds 5% of the eligible capital base.

ix. ***Group of Connected Counterparties:***

In some cases, a bank may have exposures to a group of counterparties with specific relationships or dependencies such that, were one of the counterparties to fail, all of the counterparties would very likely fail. A group of this sort, referred to in this framework as a group of connected counterparties, must be treated as a single counterparty. In this case, the sum of the bank's exposures to all the individual entities included within a group of connected counterparties is subject to the large exposure limit and to the regulatory reporting requirements.¹

Two or more natural or legal persons shall be deemed a group of connected counterparties if at least one of the following criteria is satisfied:

- a. *The existence of a control relationship; or*
- b. *The existence of Economic interdependence.*

The bank shall assess the relationship amongst counterparties with reference to (a) and (b) above in order to properly assess the existence and the extent of a group of connected counterparties.

Where control has been established based on any of these criteria, a bank may still demonstrate to SAMA in exceptional cases, e.g. due to the existence of specific circumstances and corporate governance safeguards, that such control does not necessarily result in the entities concerned constituting a group of connected counterparties.

¹ See section 7. Regulatory Reporting of this circular



- x. **Related Party:** any party that the bank exerts control over or that exerts control over the bank, including, inter-alia, the following:
- a. Members of Board of Directors, Members of Shariah Committees or Boards, Key Executives/members of Senior Management, Major Shareholders and External Auditors of the Bank and their dependent family members;
 - b. Un-incorporated establishments in which any Director, Members of Shariah Committees or Boards, External Auditor, Major Shareholder, or Key Executive/member of Senior Management of the Bank or any of their dependent family members is a partner or manager or has a direct financial interest or is a guarantor;
 - c. Affiliated or Associated companies and partnerships: These include establishments that are connected to the Bank by a common parent or a controlling shareholder.

Where dependence criteria for family members has been identified based on a and b above, a bank may still demonstrate to SAMA in exceptional cases, that the family members clearly operate all business activities independent of each other with no economic inter dependence, financial support or shareholding from the other family member.

- xi. **Major Shareholder:** a person who directly or indirectly owns, controls or has power to vote more than 5% of the voting shares of the bank granting the facility
- xii. **Entities Connected with Saudi Government:** includes public sector entities treated as sovereigns under the Basel risk-based capital framework. However, any commercial undertakings majority owned by Saudi Government will be treated as normal commercial entities and therefore be subject to the exposure limits under these Rules.
- xiii. **Dependent Family Members:** means first-degree relatives including parents, spouse and offspring.

1.3. Objectives of the Rules:

The main objectives of these Rules are to enable banks:

- i. To contain the maximum loss a bank could face in the event of a sudden default or failure of a counterparty;



- ii. To manage credit concentration risk emanating from concentrated exposures to single counterparties or groups of connected counterparties, through diversification of credit portfolio;
- iii. To put in place a large exposures framework which complements and serves as a backstop to the risk-based capital requirements;
- iv. To deal effectively with large exposures so as to contribute to the stability of the financial system; and
- v. To ensure broader access to credit for the economic development of the Kingdom.

2. Scope and Level of Application:

2.1. Institutional Coverage:

These rules² shall be applicable to the following institutions:

- i) All locally incorporated banks licensed and operating in the Kingdom of Saudi Arabia;
- ii) All majority owned subsidiary (ies) of locally incorporated banks operating in the financial sector
- iii) All foreign branches of locally incorporated banks
- iv) Branches of foreign banks operating in the Kingdom

While applying the rules to their subsidiaries and branches, the banks shall also take into account the legal and regulatory requirements of the concerned regulatory authorities.

When implementing the Rules, Branches of foreign banks operating in the Kingdom are only required to put in place internal policies to ensure reasonable diversification of their exposures, and to report their 50 largest exposures as per reporting requirements under Section 7 of these Rules.

2.2. Level of Application:

These rules shall be applicable on a consolidated as well as standalone basis. They apply at the same level as the risk-based capital requirements are required to be applied following SAMA's Detailed Guidance Document relating to Pillar 1, June 2006,³ i.e. at every tier within a banking group. While applying the rules at a consolidated level, a bank must

² SAMA may consider differentiated applicability of these rules for any category of Banks that do not fall under the Basel framework

³ See "Basel II - SAMA's Detailed Guidance Document relating to Pillar 1, June 2006"



consider all exposures to third parties across the relevant regulatory consolidation group and compare the aggregate of those exposures with the group's eligible capital base.

2.3. Scope of counterparties:

A bank must consider exposures to any counterparty to comply with the exposure limits unless a specific exemption to any exposure is granted under these Rules. The only exposures to certain counterparties that are exempted from the application of these Rules are exposures to Saudi government, SAMA and entities connected with Saudi Government, GCC and central governments and their central banks, intra-group and intraday interbank exposures which are exempted to the extent specified under Section 4.6 of these Rules

3. Maximum Exposure Limits:

3.1. Exposure Limits:

All banks are required to ensure compliance of the following exposure limits:

- i. ***Single Counterparty:*** Single counterparty: The sum of all exposures values a bank has to a single non-bank counterparty (excluding individuals and sole proprietorships) must not be higher than 15% of the banks available eligible capital base at all times. However, the banks will regularize their existing exposures to meet this requirement within the following transition period:

<i>Effective From:</i>	<i>Existing Exposure to be reduced to:</i>
1 st January 2016	23% of eligible capital base
1 st January 2017	21% of eligible capital base
1 st January 2018	18% of eligible capital base
1 st January 2019	15% of eligible capital base

- ii. ***Group of Connected Counterparties:*** The sum of all exposures values a bank has to a group of connected non-bank counterparties must not be higher than 15% of the bank's available eligible capital base at all times. Where an individual/sole proprietorship/partnership is included within a Group of Connected Counterparties, the exposure limit specified under Section 3.1.iii below shall also be applicable, in



addition to the overall group exposure limit. However, the banks will regularize their existing exposures to meet these requirements as per the transition period prescribed under Section 3.1.i above and Section 3.1.iii below.

Furthermore, the sum of a banks exposures to the entities included within a group of connected counterparties will also be subject to the regulatory reporting requirements as specified under Section 7 of these Rules.

- iii. **Individual/Sole proprietor:** The sum of all the exposures values a bank has to an individual or a sole proprietorship or a partnership must not be higher than 5% of the banks available eligible capital base at all times. However, the banks will regularize their existing exposures to meet this requirement within the following transition period;

<i>Effective From:</i>	<i>Existing Exposure to be reduced to:</i>
1 st January 2016	16% of eligible capital base
1 st January 2017	12% of eligible capital base
1 st January 2018	8% of eligible capital base
1 st January 2019	5% of eligible capital base

- iv. **Banks:** The sum of all the exposures values a bank has to another bank must not be higher than 25% of the lending bank's available eligible capital base at all times, subject to the following
- If the lending bank and the counterparty bank are both designated by SAMA as Domestically – Systemically Important Banks (D-SIBs), as defined in Appendix VI, then the sum of all exposures of the lending Bank to its counterparty bank cannot exceed 15% of the lending bank's available eligible capital base at all times
 - If the lending bank is not a D-SIB and the counterparty bank is a D-SIB or G-SIB (as defined in Appendix VI), then the sum of all exposures of the lending Bank to its counterparty bank cannot exceed 15% of the lending bank's available eligible capital base at all times



- c. If the lending bank is a D-SIB and the counterparty bank is a G-SIB, then the sum of all exposures of the lending Bank to its counterparty bank cannot exceed 15% of the lending bank's available eligible capital base at all times
- v. **Related Counterparty:** The sum of all exposures values a bank has to a non-bank related counterparty must not be higher than 10% of the bank's available eligible capital base at all times. However, a bank may have exposure to its non-banking subsidiary in financial sector of up to 25% of the banks eligible capital. Any existing exposures in excess of this limit of 25% will be proportionately reduced by one-fourth every calendar year over the next four years so as to fully regularize the position by 31st December 2018. Furthermore, a cumulative limit on all exposures to non-bank related counterparties shall be 50% of the banks eligible capital;
- vi. **Aggregate Large Exposures:** The aggregate of all Large Exposures shall not exceed 6 times of the bank's eligible capital.

3.2. Measurement of Exposures and Capital Base:

The exposures must be measured as specified in Section 4 of these Rules. The eligible capital base is the effective amount of Common Equity Tier 1 capital fulfilling the criteria defined in Section A of the "Finalized Guidance Document Concerning the Implementation of Basel III"⁴.

3.3. Breaches of Limits:

Any breaches of the exposure limits, which must stay exceptional events, must be communicated immediately to SAMA and must be rapidly rectified. Furthermore, any such breaches may attract punitive supervisory action depending upon their materiality.

4. Measurement of Exposures Values:

4.1. General Measurement Principles:

Banks shall adhere to the following principles in measuring the values of exposures:

- i. The exposure values to be considered for identifying large exposures to a counterparty are all those exposures defined under the risk-based capital framework. Accordingly, banks must consider both on and off-balance sheet exposures included

⁴ The above mentioned guidelines is available at the following link on SAMA's website: http://www.sama.gov.sa/en-US/Laws/Pages/SAMA_Basel_Program_Sec2.aspx



- in either the banking or trading books, and instruments with counterparty credit risk under the risk-based capital framework;
- ii. In case the counterparty is part of a *Group of Connected Counterparties*, the values of exposures to all individual counterparties within a group of connected counterparties must be aggregated.
 - iii. An exposure amount to a counterparty that is deducted from capital must not be added to other exposures to that counterparty for the purpose of the large exposures limit. This general approach does not apply where an exposure is 1,250% risk-weighted. When this is the case, this exposure must be added to any other exposures to the same counterparty and the sum subject to the large exposures limit, except if this exposure is specifically exempted for other reasons.

4.2. Eligible credit risk mitigation (CRM) techniques:

Eligible credit risk mitigation techniques for large exposures purposes are those that meet the minimum requirements and eligibility criteria for the recognition of unfunded credit protection⁵ and financial collateral that qualify as eligible financial collateral under the standardised approach for risk-based capital requirement purposes. (Note: SAMA does not consider equities, including convertible bonds and Undertakings for Collective Investments in Transferable Securities as eligible CRM mitigants)

Other forms of collateral that are only eligible under the Internal-ratings based (IRB) approach in accordance with Paragraph 31, Basel III IRB Approaches Prudential Returns And Guidance Notes, 2014 (Only Equities for margin lending exposures has been allowed in the aforementioned paragraph, as eligible CRM, SAMA does not recognize any IRB collaterals i.e. Financial Receivable, Residential Real Estate, Commercial Real Estate, Physical Cards, etc., under the IRB approach) are not eligible to reduce exposure values for large exposures purposes.

⁵ Unfunded credit protection refers collectively to guarantees and credit derivatives the treatment of which is described in Section 6, Basel II – SAMA's Detailed Guidance Document relating to Pillar 1, June 2006, and GN 2 of Basel II Package of Bank Prudential Returns and Guidance Notes Concerning Standardized Approach, 2007.



A bank must recognize an eligible CRM technique in the calculation of an exposure whenever it has used this technique to calculate the risk-based capital requirements, and provided it meets the conditions for recognition under the large exposures framework;

i. Treatment of maturity mismatches in CRM

- a. In accordance with provisions set out in the risk-based capital framework⁶, hedges with maturity mismatches are recognised only when their original maturities are equal to or greater than one year and the residual maturity of a hedge is not less than three months.
- b. If there is a maturity mismatch in respect of credit risk mitigants (collateral, on-balance sheet netting, guarantees and credit derivatives) recognised in the risk-based capital requirement, the adjustment of the credit protection for the purpose of calculating large exposures is determined using the same approach as in the risk-based capital requirement.⁷

ii. On-balance sheet netting⁸

- a. Where a bank has in place legally enforceable netting arrangements for loans and deposits, it may calculate the exposure values for large exposures purposes according to the calculation it uses for capital requirements purposes – i.e. on the basis of net credit exposures subject to the conditions set out in the approach to on-balance sheet netting in the risk-based capital requirement.⁹

⁶ See, Credit Risk Mitigation – Chapter 6.5 Pages 164/165, Basel II - SAMA's Detailed Guidance Document, 2006 and GN 2, Pages No.12/13, Basel II, Package Of Bank Prudential Returns And Guidance Notes Concerning Standardized Approach, 2007.

⁷ See Credit Risk Mitigation – Chapter 6.5 Page 164/165, Basel II - SAMA's Detailed Guidance Document, 2006.

⁸ This should not be currently applied to exposures based in KSA as netting is not currently permitted within the legal framework.

⁹ See Credit Risk Mitigation – Chapter 6.2 Page 158 and 159, Basel II - SAMA's Detailed Guidance Document, 2006.



4.3. *Recognition of CRM techniques in reduction of original exposure*

A bank must reduce the value of the exposure to the original counterparty by the amount of the eligible CRM technique recognised for risk-based capital requirements purposes. This recognised amount is:

- the value of the protected portion in the case of unfunded credit protection;
- the value of the portion of claim collateralised by the market value of the recognised financial collateral when the bank uses the simple approach for risk-based capital requirements purposes;
- the value of the collateral adjusted after applying the required haircuts, in the case of financial collateral when the bank applies the comprehensive approach. The haircuts used to reduce the collateral amount are the supervisory haircuts under the comprehensive approach.¹⁰ Internally modelled haircuts must not be used.
- the value of the collateral as recognized in the calculation of the counterparty credit risk exposure value for any instruments with counterparty credit risk, such as OTC derivatives;

4.4. *Recognition of exposures to CRM providers*

Whenever a bank is required to recognise a reduction of the exposure to the original counterparty due to an eligible CRM technique, it must also recognise an exposure to the CRM provider. The amount assigned to the CRM provider is the amount by which the exposure to the original counterparty is reduced (except in the cases where credit protection takes the form of a CDS and either the CDS provider or the referenced entity is not a financial entity, the amount to be assigned to the credit protection provider is not the amount by which the exposure to the original counterparty is reduced but, instead, the counterparty credit risk exposure value calculated according to the SA-CCR)¹¹

For the purposes of this section, financial entities comprise:

- Regulated financial institutions, defined as a parent and its subsidiaries where any substantial legal entity in the consolidated group is supervised by a regulator that imposes prudential requirements consistent with international norms. These include,

¹⁰ GN 2, Page 14, of Basel II Package of Bank Prudential Returns and Guidance Notes Concerning Standardized Approach, 2007 and Chapter 6.1, Page 157, Basel II - SAMA's Detailed Guidance Document, 2006.

¹¹ See SAMA Circular No. 351000095021, 21 May 2014, Basel Committee on Banking Supervision Document of March 2014 regarding the Standardized Approach for Measuring Counterparty Credit Risk Exposures



but are not limited to, prudentially regulated insurance companies, broker/dealers, banks, thrifts and futures commission merchants; and

- Unregulated financial institutions, defined as legal entities whose main business includes: the management of financial assets, lending, factoring, leasing, provision of credit enhancements, securitisation, investments, financial custody, central counterparty services, proprietary trading and other financial services activities identified by supervisors.

4.5. Treatment of Specific Measurement Issues:

While determining the exposure values for the purposes of these Rules, the following specific issues will be dealt with as per the guidance provided in the BCBS Document titled “Supervisory Framework for measuring and controlling large exposures” issued in April 2014 (available at <https://www.bis.org/publ/bcbs283.pdf>) and FAQs (available at <https://www.bis.org/bcbs/publ/d384.pdf>) issued in Sept 2016. Please note that these have also been reproduced in Appendix VII-XI, for ready reference.

- i. Definition of exposure values: (Refer Appendix VII):
 - a. Banking book on-balance sheet non-derivative assets;
 - b. Banking book and trading book OTC derivatives (and any other instrument with counterparty credit risk);
 - c. Securities financing transactions;
 - d. Banking book “traditional” off balance sheet commitments;
- ii. Trading Book Positions (Refer Appendix VIII):
 - a. Calculation of exposure value for trading book positions;
 - b. Offsetting long and short positions in the trading book;
- iii. Covered bonds; (Refer Appendix IX)
- iv. Collective investment undertakings, securitizations vehicles and other structures; (Refer Appendix X)
- v. Exposures to central counterparties (Refer Appendix XI)

4.6. Exposures Exempted from Exposure Limits:

The following exposures shall be exempt from the large exposure limits specified under these Rules:

- i. ***Sovereign exposures and entities connected with the Saudi Government:***



Banks' exposures to the Saudi Government, SAMA, Entities Connected with the Saudi Government, GCC and their central banks will be exempt from exposure limits as under:

- a. Any exposure directly taken to Saudi Government, SAMA and any of the Entities Connected with the Saudi Government;
- b. Any portion of an exposure guaranteed, or secured by the financial instruments issued by Saudi government or SAMA to the extent that the eligibility criteria for recognition of the credit risk mitigation are met;
- c. Any exposure to the GCC and central governments and their central banks;
- d. Any entity falling within the scope of the above sovereign exemption will not be taken into account when determining whether two (or more) entities that are in scope must be connected to form a Group of Connected Counterparties (i.e. if two entities that are in scope of the framework, which are otherwise not connected, are controlled by or economically dependent through an exempted entity they need not be connected);
- e. Any exposure to an exempted entity which is hedged by a credit derivative, will be recognized as an exposure to the counterparty providing the credit protection notwithstanding the fact that the original exposure is exempted. In addition, if a bank has an exposure to an exempted entity which is hedged by a credit derivative, the bank will have to recognize an exposure to the counterparty providing the credit protection as prescribed in Section 4.4 of this guideline, notwithstanding the fact that the original exposure is exempted. Hence the credit protection provider would still be subject to the large exposure guidelines;
- f. All exposures that are subject to the sovereign exemption under this Section must be reported under the regulatory reporting requirements if these exposures meet the minimum reporting threshold.

ii. Interbank exposures: All intra-day interbank exposures will not be subject to the large exposures limits, neither for reporting purposes nor for application of the large exposure limits. However, all non-intraday interbank exposures will be subject to the large exposure limits.

In addition, under stressed and exceptional circumstances, SAMA (under its discretion) may accept a breach of an interbank limit ex post, in order to help ensure stability in the interbank market;



- iii. Intra-group exposures:* All exposures to intra-group entities of the concerned bank will not be subject to the large exposures limits provided that such entities are included in the scope of accounting consolidation of the banking group. However, the non-banking subsidiaries in the financial sector will be subject to the exposure limit of 25% of the banks eligible capital as specified under Section 3.1(v) of these Rules.

All other exposures of a bank, not specifically listed above as exempted, must be fully subject to the large exposure limits.

5. Exposure to Related Counterparties:

Banks shall ensure compliance of the following requirements while taking any exposure to related parties:

- i. Exposures to related parties shall only be considered on arms length basis and without any preferential treatment. Furthermore, any such credit exposures should also be strictly in line with the bank's credit policy and procedures;
- ii. Any exposure to a related party should be approved at the level of Board of Directors. While considering any proposal of lending to a Board member or any of his connected party, the Board of Directors shall ensure that the concerned Board member would neither participate in the discussion nor influence such a decision;
- iii. Banks should institute procedures to prevent the beneficiaries of any credit exposure being part of the processing or approval of such exposure;
- iv. Any facilities granted by a bank to its key executives/members of senior management as a part of their employment contract/compensation package shall be exempt from the application of these rules.

6. Additional Requirements:

While ensuring compliance with the exposure limits under these Rules, the banks shall also meet the following additional requirements:

- i. The exposure limits under these Rules shall be calculated based on the eligible capital base as disclosed in the latest published quarterly financial statements of the bank;



- ii. The exposure limits specified under these Rules are the maximum and within such limits, each bank can set lower exposure limits as a part of its Credit Policy. Banks are required to introduce adequate internal systems and controls to closely monitor on a daily basis all large exposures and ensure compliance with the specified limits;
- iii. Banks shall include appropriate clauses in their respective credit Policies on the management and control of large exposures;
- iv. For the purpose of compliance with exposure limits under these Rules, banks shall measure, monitor, and report all exposures net of amounts reduced by eligible CRM techniques.

7. Regulatory Reporting:

Banks are required to submit to SAMA the following information on their exposures before and after application of the credit risk mitigation techniques, on a quarterly basis:

- i) All Large Exposures as defined in the BCBS "Supervisory Framework for measuring and controlling large exposures" issued in April 2014" (before application of the credit risk mitigation techniques) along-with the ratio of the aggregate of all such large exposures with the banks eligible capital, on the prescribed format attached as Appendix-I;
- ii) All Large Exposures (after application of the credit risk mitigation techniques) along-with the ratio of the aggregate of all such large exposures with the banks eligible capital, on the prescribed format attached as Appendix-II;
- iii) All the exempted exposures with values equal to or above 10% of the banks eligible capital, on the prescribed format attached as per Appendix-I & II;
- iv) The largest 50 exposures to counterparties, irrespective of the values of these exposures relative to the banks eligible capital base, on the prescribed format attached as per Appendix-III;
- v) All exposures that exceeded the exposure limits specified under these Rules during the reporting quarter even if regularized subsequently, on the prescribed format attached as per Appendix-IV;
- vi) All exposures to related counterparties that exceeded 5% of the banks eligible capital base on the reporting date, on the prescribed format attached as per Appendix-V.



The above information shall be submitted to SAMA starting from the quarter ending 30th September, 2015 and each calendar quarter thereafter, within 30 calendar days of the end of each quarter.

8. Implementation:

All banks are required to institute necessary policies and procedures to ensure compliance of these Rules. SAMA will monitor compliance of these Rules through its off-site monitoring and on-site inspection process.

9. Sanctions

Where an offence has occurred, SAMA can impose any one or more of the sanctions stipulated in Article (22) and (23) of the Banking Control Law.

10. Effective Date

These revised Rules shall come into force with effect immediately. Banks are required to ensure compliance of these Rules while taking any new exposure or renewing existing exposures after the effective date. Furthermore, the information required under Section 7 of these Rules shall be submitted to the Agency starting from the quarter ending 30th September, 2015 and each quarter thereafter, within 30 days of the end of each calendar quarter. In case there are any practical issues in implementation of these Rules, banks should approach SAMA to seek further guidance on addressing such issues.



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Appendix-I

Name of the Bank: _____
Statement for the Month ended _____

M-18A

**Statement Showing Large Exposures to Single and Group of Connected Counterparties
(before application of the credit risk mitigation techniques)**

(All amounts are in SR thousands)

SR. No.	Name and Location of Borrower	Total value of Gross Exposure			Ratio of Gross Exposure to Bank's Eligible Capital	Whether exempted from Exposure Limits (Yes or No)	In Case of Exempted Exposures, State Reasons for Exemption	Remarks (if any)
		On Bal. Sheet	Off Bal. Sheet	Total				
1	2	3	4	5 (=3+4)	6	7	8	9
A. Aggregate of all Large Exposures								
B. Aggregate of Exempted Large Exposures								
C. Net Large Exposures (A - B)								
D. Ratio of Net Large Exposures to Bank's Eligible Capital								



Appendix-II

Name of the Bank: _____
Statement for the Month ended _____

M-18B

**Statement Showing Large Exposures to Single and Group of Connected Counterparties
(after application of the credit risk mitigation techniques)**

(All amounts are in SR thousands)

SR. No.	Name and Location of Borrower	Total value of Gross Exposure	Value of Eligible Credit Risk Mitigates (CRM)			Net Value of Exposure	Ratio of Net Exposure to Bank's Eligible Capital	Whether exempted from Exposure Limits (Yes or No)	In Case of Exempted Exposures, State Reasons for Exemption	Remarks (if any)
			Cash Margins	Other Eligible CRM	Total					
1	2	3	4	5	6 (=4+5)	7	8	9	10	
A. Aggregate of all Net Large Exposures										
B. Aggregate of Exempted Net Large Exposures										
C. Aggregate of Large Exposures Net of CRM (A - B)										
D. Ratio of Aggregate Large Exposures net of CRM to Bank's Eligible Capital										



Appendix-III

Name of the Bank: _____
Statement for the Month ended _____

M-18C

Statement Showing Largest 50 Exposures to Counterparties

(All amounts are in SR thousands)

SR. No.	Name and Location of Borrower	Total Amount of Gross Exposure			Value of Eligible Credit Risk Mitigates(CRM)	Net Exposure	Ratio of Net Exposure to Bank's Eligible Capital	In Case of Exempted Exposures, State Reasons for Exemption
		On Bal. Sheet	Off Bal. Sheet	Total				
1	2	3	4	5 (=3+4)	6	7 (=5-6)	8	9
Total								
A. Aggregate of all Largest 20 Exposures								
B. Ratio of Aggregate Largest 20 Exposures to Bank's Eligible Capital								



Appendix-IV

Name of the Bank: _____
Statement for the Month ended _____

M-19A

Statement Showing Exposures that Exceeded the Specified Exposure Limits during the Reporting Month

(All amounts are in SR thousands)

SR. No.	Name and Location of Borrower	Total Value of Gross Exposure On Reporting Date			Total Value of Exposure on Date of Breach	Original Date of Breach	Date of Regularization	Reasons for Breach	Remarks (if any)
		On Bal. Sheet	Off Bal. Sheet	Total					
1	2	3	4	5 (=3+4)	6	7	8	9	10
Total									



Appendix-V

Name of the Bank: _____

Statement for the Month ended _____

M-190

Statement Showing Exposures to Related Counterparties that Exceeded 5% of Bank's Eligible Capital Base

(All amounts are in SR thousands)

Sr. No.	Name and Location of Borrower	Total Amount of Gross Exposure			Value of Eligible Credit Risk Mitigates(CRM)	Net Exposure	Ratio of Net Exposure to Bank's Eligible Capital	Related Party's Relationship with Bank
		On Bal. Sheet	Off Bal. Sheet	Total				
1		3	4	5 (=3+4)	6	7 (=5-6)	8	9
Total								
A. Aggregate of all Exposures to Related Parties (Incl. the above Exposures)								
B. Ratio of Aggregate Related Parties Exposures to Bank's Eligible Capital								

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Appendix VI

The Financial Stability Board (FSB) defines Systemically Important Financial Institutions (SIFI's) as "financial institutions whose distress or disorderly failure because of their size, complexity and systematic interconnectedness, would cause significant disruption to the wider financial system and economic activity"

At the international level, the Basel Committee on Banking Supervision has developed a methodology for identifying G-SIB's, and a set of principles to guide national authorities in the identification of domestic systematically important banks (D-SIB's). G-SIB status is determined using five main criteria: cross-jurisdictional activity; interconnectedness; size; substitutability and complexity. The methodology (issued via SAMA circular no. 107018 dated 10 July 2013) is also used to rank a G-SIB's level of systemic importance relative to other G-SIB's. The list of G-SIB's is reviewed annually, and banks can move in or out of G-SIB classification or be re-classified at a different level of systemic importance.

The 2017 list of G-SIBs are available on FSB website as below:
<http://www.fsb.org/wp-content/uploads/P211117-1.pdf>

Updated G-SIB list should be received from the website below:
<http://www.fsb.org/>

Domestic Systematically Important Bank (D-SIB):

A D-SIB is a bank whose distress or disorderly failure could have a serious detrimental impact on either the financial system or the real economy within the country in which the bank operates. The BCBS has published a framework for developing a D-SIB assessment methodology (issued via SAMA circular no. 351000138356 dated 7 September 2014 and circular no. 371000091395 dated 24/05/2016). In connection with identifying and notifying banks with respect to the D-SIB designation, SAMA is required to:

- Take into consideration size; interconnectedness; substitutability; and complexity (including additional complexities caused by cross-border activity) within the domestic economy;



- Produce a D-SIB list (issued via SAMA circulars nos. 391000089191 dated 03/05/2018, 381000082448 dated 02/05/2017 and 371000091395 dated 24/05/2016) , and review it on an annual basis; and
- Publicly disclose D-SIB assessment methodology (issued via SAMA circular no. 371000091395 dated 24/05/2016)

Updated D-SIB list should be received from the SAMA website.

The relationship between G-SIB's and D-SIB's:

- Banks can be classified as D-SIB at the consolidated group level or subsidiary or a branch level by the bank's supervisory authorities.
- A bank identified as a G-SIB can also be classified as a D-SIB in any of the countries depending on the nature of operations.
- A bank with large global operations identified as G-SIB that does not have significant operations in any individual country can also be classified as a G-SIB



Appendix VII

Definition of exposure value¹²

Banking book on-balance sheet non-derivative assets:

The exposure value must be defined as the accounting value of the exposure i.e. Net of specific provisions and value adjustments. As an alternative, a bank may consider the exposure value gross of specific provisions and value adjustments.

Banking book and trading book OTC derivatives (and any other instrument with counterparty credit risk):

The exposure value for instruments that give rise to counterparty credit risk and are not securities financing transactions must be the exposure at default according to the standardised approach for counterparty credit risk (SA-CCR – (See SAMA Circular No 351000095021, 21 May 2014 and circular no. 371000101120 dated 20 June 2016, Basel Committee on Banking Supervision Document of March 2014 regarding the Standardized Approach for Measuring Counterparty Credit Risk Exposures).

Securities financing transactions:

BCBS has revised Standardized approach for measuring counterparty credit risk in March 2014 implemented by SAMA via. Circular no. 371000101120 dated 20 June 2016. In addition, BCBS has revised the comprehensive approach used for the measurement of Securities Financing Transaction (SFT) exposures in December 2017 which SAMA will apply in future. All banks must use the revised comprehensive approach with supervisory haircuts or equivalent non-internal model method for large exposure purposes. However, until SAMA issues these revised rules, banks would be allowed to use the method they currently use for calculating their risk-based capital requirements against SFTs (i.e. GN 2, Page 14, of Basle II Package of Bank Prudential Returns and Guidance Notes Concerning Standardized Approach, 2007 and Chapter 6.1, Page 157, Basel II - SAMA's Detailed Guidance Document)

¹² Paragraphs 32-35 of BCBS "Supervisory framework for measuring and controlling large exposures" April 2014

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Banking book “traditional” off-balance sheet commitments:

For the purpose of the large exposures framework, off-balance sheet items will be converted into credit exposure equivalents through the use of credit conversion factors (CCFs) by applying the CCFs set out for the standardised approach for credit risk for risk-based capital requirements, with a floor of 10%.



Appendix VIII

Calculation of exposure value for trading book positions¹³

A bank must add any exposures to a single counterparty arising in the trading book to any other exposures to that counterparty that lie in the banking book to calculate its total exposure to that counterparty.

Scope of large exposure limits in the trading book:

The exposures considered in this section correspond to concentration risk associated with the default of a single counterparty for exposures included in the trading book (See note below). Therefore, positions in financial instruments such as bonds and equities must be constrained by the large exposure limit, but concentrations in a particular commodity or currency need not be.

Note (SAMA recognizes that the risk from large exposures to single counterparties or groups of connected counterparties is not the only type of concentration risk that could undermine a bank's resilience. Other types include both sectoral and geographical concentrations of asset exposures; reliance on concentrated funding sources; and also a significant net short position in securities, because the bank may incur severe losses if the price of these securities increases. SAMA has decided to focus this framework on losses incurred due to default of a single counterparty or a group of connected counterparties and not to take into account any other type of concentration risk.)

Calculation of exposure value for trading book positions:

The exposure value of straight debt instruments and equities must be defined as the accounting value of the exposure (i.e. the market value of the respective instruments).

Instruments such as swaps, futures, forwards and credit derivatives must be converted into positions following the risk-based capital requirements. (See paragraph 718 (x - xii), Page 89, Basel II.5 SAMA's Guidance Document Concerning Implementation, 2012). These instruments are decomposed into their individual legs. Only transaction legs representing exposures in the scope of the large exposures framework need be considered (see note below)

¹³ Paragraphs 44-59 of BCBS "Supervisory framework for measuring and controlling large exposures" April 2014



Note: A future on stock X, for example, is decomposed into a long position in stock X and a short position in a risk-free interest rate exposure in the respective funding currency, or a typical interest rate swap is represented by a long position in a fixed and a short position in a floating interest rate exposure or vice versa.

In the case of credit derivatives that represent sold protection, the exposure to the referenced name must be the amount due in the case that the respective referenced name triggers the instrument, minus the absolute value of the credit protection. (see note below) For credit-linked notes, the protection seller needs to consider positions both in the bond of the note issuer and in the underlying referenced by the note. For positions hedged by credit derivatives, refer to "Offsetting long and short positions in the trading book" section below (paragraphs 3 to 6).

Note: In the case that the market value of the credit derivative is positive from the perspective of the protection seller, such a positive market value would also have to be added to the exposure of the protection seller to the protection buyer (counterparty credit risk; refer to "Banking book and trading book OTC derivatives section in Appendix VII above). Such a situation could typically occur if the present value of already agreed but not yet paid periodic premiums exceeds the absolute market value of the credit protection.

The measures of exposure values of options under this framework differ from the exposure value used for risk-based capital requirements. The exposure value must be based on the change(s) in option prices that would result from a default of the respective underlying instrument. The exposure value for a simple long call option would therefore be its market value and for a short put option would be equal to the strike price of the option minus its market value. In the case of short call or long put options, a default of the underlying would lead to a profit (i.e. a negative exposure) instead of a loss, resulting in an exposure of the option's market value in the former case and equal the strike price of the option minus its market value in the latter case. The resulting positions will in all cases be aggregated with those from other exposures. After aggregation, negative net exposures must be set to zero.

Exposure values of banks' investments in transactions (i.e. index positions, securitizations, hedge funds or investment funds) must be calculated applying the same rules as for similar instruments in the banking book (refer to Appendix X). Hence, the amount invested in a particular structure may be assigned to the structure itself, defined as a distinct counterparty, to the counterparties corresponding to the underlying assets,



or to the unknown client, following the rules described in Appendix X paragraphs 1 to 5).

Offsetting long and short positions in the trading book

Offsetting between long and short positions in the same issue:

Banks may offset long and short positions in the same issue (two issues are defined as the same if the issuer, coupon, currency and maturity are identical). Consequently, banks may consider a net position in a specific issue for the purpose of calculating a bank's exposure to a particular counterparty.

Offsetting between long and short positions in different issues:

Positions in different issues from the same counterparty may be offset only when the short position is junior to the long position, or if the positions are of the same seniority.

Similarly, for positions hedged by credit derivatives, the hedge may be recognised provided the underlying of the hedge and the position hedged fulfil the provision mentioned in the previous paragraph (the short position is junior or of equivalent security to the long position).

In order to determine the relative seniority of positions, securities may be allocated into broad buckets of degrees of seniority (for example, "Equity", "Subordinated Debt" and "Senior Debt").

For those banks that find it excessively burdensome to allocate securities to different buckets based on relative seniority, they may recognise no offsetting of long and short positions in different issues relating to the same counterparty in calculating exposures.

In addition, in the case of positions hedged by credit derivatives, any reduction in exposure to the original counterparty will correspond to a new exposure to the credit protection provider, following the principles underlying the substitution approach stated in section 4.4 "Recognition of exposures to CRM providers", except in the case described in the next paragraph.

When the credit protection takes the form of a CDS and either the CDS provider or the referenced entity is not a financial entity, the amount to be assigned to the credit protection provider is not the amount by which the exposure to the original counterparty is reduced but, instead, the counterparty credit risk exposure value calculated according to the SA-CCR. (See SAMA Circular No 351000095021, 21 May 2014, Basel

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Committee on Banking Supervision Document of March 2014 regarding the Standardized Approach for Measuring Counterparty Credit Risk Exposures) For the purposes of this paragraph, financial entities comprise:

- regulated financial institutions, defined as a parent and its subsidiaries where any substantial legal entity in the consolidated group is supervised by a regulator that imposes prudential requirements consistent with international norms. These include, but are not limited to, prudentially regulated insurance companies, broker/dealers, banks, thrifts and futures commission merchants; and
- unregulated financial institutions, defined as legal entities whose main business includes: the management of financial assets, lending, factoring, leasing, provision of credit enhancements, securitisation, investments, financial custody, central counterparty services, proprietary trading and other financial services activities identified by supervisors

Offsetting short positions in the trading book against long positions in the banking book:

Netting across the banking and trading books is not permitted.

Net short positions after offsetting:

When the result of the offsetting is a net short position with a single counterparty, this net exposure need not be considered as an exposure for large exposure purposes (refer to "Scope of large exposure limits in the trading book" section in this Appendix).

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Appendix IX

Covered bonds¹⁴

Covered bonds are bonds issued by a bank or mortgage institution and are subject by law to special public supervision designed to protect bond holders. Proceeds deriving from the issue of these bonds must be invested in conformity with the law in assets which, during the whole period of the validity of the bonds, are capable of covering claims attached to the bonds and which, in the event of the failure of the issuer, would be used on a priority basis for the reimbursement of the principal and payment of the accrued interest.

A covered bond satisfying the conditions set out in the next paragraph may be assigned an exposure value of no less than 20% of the nominal value of the bank's covered bond holding. Other covered bonds must be assigned an exposure value equal to 100% of the nominal value of the bank's covered bond holding. The counterparty to which the exposure value is assigned is the issuing bank.

To be eligible to be assigned an exposure value of less than 100%, a covered bond must satisfy all the following conditions:

- It must meet the general definition set out in the first paragraph of this appendix;
- The pool of underlying assets must exclusively consist of:
 - claims on, or guaranteed by, sovereigns, their central banks, public sector entities or multilateral development banks;
 - claims secured by mortgages on residential real estate that would qualify for a 35% or lower risk weight under the Basel II Standardised Approach (SAMAs local guidelines in connection therewith are Basel II Package of Bank Prudential Returns and Guidance Notes Concerning Standardized Approach, 2007 and Basel II - SAMA's Detailed Guidance Document, 2006) for credit risk and have a loan-to-value ratio of 80% or lower (Note: Currently SAMA does not utilize 35% or lower RWA for mortgages on residential real estate); and/or
 - claims secured by commercial real estate that would qualify for the 100% or lower risk-weight under the Basel II Standardised Approach for credit risk (SAMAs local guidelines in connection therewith are Basel II Package of Bank

¹⁴ Paragraphs 68-71 of BCBS "Supervisory framework for measuring and controlling large exposures" April 2014



Prudential Returns and Guidance Notes Concerning Standardized Approach, 2007 and Basel II - SAMA's Detailed Guidance Document, 2006)and with a loan-to-value of 60% or lower;

- The nominal value of the pool of assets assigned to the covered bond instrument(s) by its issuer should exceed its nominal outstanding value by at least 10%. The value of the pool of assets for this purpose does not need to be that required by the legislative framework. However, if the legislative framework does not stipulate a requirement of at least 10%, the issuing bank needs to publicly disclose on a regular basis that their cover pool meets the 10% requirement in practice. In addition to the primary assets listed in the previous paragraph, the additional collateral may include substitution assets (cash or short term liquid and secure assets held in substitution of the primary assets to top up the cover pool for management purposes) and derivatives entered into for the purposes of hedging the risks arising in the covered bond program.

In order to calculate the required maximum loan-to-value for residential real estate (RRE) and commercial real estate (CRE) referred to in the third of this appendix, the operational requirements regarding the objective market value of collateral and the frequent revaluation in the BCBS Basel II framework included in the next paragraph of must be used. The conditions set out in the third paragraph of this appendix must be satisfied at the inception of the covered bond and throughout its remaining maturity.

Operational requirements for eligible CRE/RRE¹⁵

CRE and RRE will be eligible for recognition as collateral for corporate claims only if all of the following operational requirements are met:

- Legal enforceability: any claim on a collateral taken must be legally enforceable in all relevant jurisdictions, and any claim on collateral must be properly filed on a timely basis. Collateral interests must reflect a perfected lien (ie all legal requirements for establishing the claim have been fulfilled). Furthermore, the collateral agreement and the legal process underpinning it must be such that they provide for the bank to realise the value of the collateral within a reasonable timeframe.
- Objective market value of collateral: the collateral must be valued at or less than the current fair value under which the property could be sold under private contract between a willing seller and an arm's-length buyer on the date of valuation.

¹⁵ Paragraphs 509 of BCBS Basel II Framework



- Frequent revaluation: the bank is expected to monitor the value of the collateral on a frequent basis and at a minimum once every year. More frequent monitoring is suggested where the market is subject to significant changes in conditions. Statistical methods of evaluation (eg reference to house price indices, sampling) may be used to update estimates or to identify collateral that may have declined in value and that may need re-appraisal. A qualified professional must evaluate the property when information indicates that the value of the collateral may have declined materially relative to general market prices or when a credit event, such as default, occurs.
- Junior liens may be taken into account where there is no doubt that the claim for collateral is legally enforceable and constitutes an efficient credit risk mitigant.

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Appendix X

Collective investment undertakings, securitization vehicles and other structures¹⁶

Banks must consider exposures even when a structure lies between the bank and the exposures, that is, even when the bank invests in structures through an entity which itself has exposures to assets (hereafter referred to as the “underlying assets”). Banks must assign the exposure amount, ie the amount invested in a particular structure, to specific counterparties following the approach described below. Such structures include funds, securitizations and other structures with underlying assets.

Determination of the relevant counterparties to be considered:

A bank may assign the exposure amount to the structure itself, defined as a distinct counterparty, if it can demonstrate that the bank’s exposure amount to each underlying asset of the structure is smaller than 0.25% of its eligible capital base, considering only those exposures to underlying assets that result from the investment in the structure itself and using the exposure value calculated according to sections titled “Any structure where all investors rank pari passu” and “Any structure with different seniority levels among investors” below in this appendix. (By definition, this required test will be passed if the bank’s whole investment in a structure is below 0.25% of its eligible capital base.) In this case, a bank is not required to look through the structure to identify the underlying assets.

A bank must look through the structure to identify those underlying assets for which the underlying exposure value is equal to or above 0.25% of its eligible capital base. In this case, the counterparty corresponding to each of the underlying assets must be identified so that these underlying exposures can be added to any other direct or indirect exposure to the same counterparty. The bank’s exposure amount to the underlying assets that are below 0.25% of the bank’s eligible capital base may be assigned to the structure itself (ie partial look-through is permitted).

If a bank is unable to identify the underlying assets of a structure:

¹⁶ Paragraphs 72-83 of BCBS “Supervisory framework for measuring and controlling large exposures” April 2014



- Where the total amount of its exposure does not exceed 0.25% of its eligible capital base, the bank must assign the total exposure amount of its investment to the structure;
- Otherwise, it must assign this total exposure amount to the unknown client.

The bank must aggregate all unknown exposures as if they related to a single counterparty (the unknown client), to which the large exposure limit would apply.

When the look-through approach (LTA) is not required according to the criteria mentioned in the second paragraph of this appendix, a bank must nevertheless be able to demonstrate that regulatory arbitrage considerations have not influenced the decision whether to look through or not – eg that the bank has not circumvented the large exposure limit by investing in several individually immaterial transactions with identical underlying assets.

Calculation of underlying exposures - bank's exposure amount to underlying assets:

If the LTA need not be applied, a bank's exposure to the structure must be the nominal amount it invests in the structure.

Any structure where all investors rank pari passu (eg CIU):

When the LTA is required according to the paragraphs above, the exposure value assigned to a counterparty is equal to the pro rata share that the bank holds in the structure multiplied by the value of the underlying asset in the structure. Thus, a bank holding a 1% share of a structure that invests in 20 assets each with a value of 5 must assign an exposure of 0.05 to each of the counterparties. An exposure to a counterparty must be added to any other direct or indirect exposures the bank has to that counterparty.

Any structure with different seniority levels among investors (eg securitization vehicles)

When the LTA is required according to the paragraphs above, the exposure value to a counterparty is measured for each tranche within the structure, assuming a pro rata distribution of losses amongst investors in a single tranche. To compute the exposure value to the underlying asset, a bank must:

- First, consider the lower of the value of the tranche in which the bank invests and the nominal value of each underlying asset included in the underlying portfolio of assets



- Second, apply the pro rata share of the bank's investment in the tranche to the value determined in the first step above.

Identification of additional risks:

Banks must identify third parties that may constitute an additional risk factor inherent in a structure itself rather than in the underlying assets. Such a third party could be a risk factor for more than one structure that a bank invests in. Examples of roles played by third parties include originator, fund manager, liquidity provider and credit protection provider.

The identification of an additional risk factor has two implications:

- The first implication is that banks must connect their investments in those structures with a common risk factor to form a group of connected counterparties. In such cases, the manager would be regarded as a distinct counterparty so that the sum of a bank's investments in all of the funds managed by this manager would be subject to the large exposure limit, with the exposure value being the total value of the different investments. But in other cases, the identity of the manager may not comprise an additional risk factor – for example, if the legal framework governing the regulation of particular funds requires separation between the legal entity that manages the fund and the legal entity that has custody of the fund's assets. In the case of structured finance products, the liquidity provider or sponsor of short-term programs (asset-backed commercial paper – ABCP – conduits and structured investment vehicles – SIVs) may warrant consideration as an additional risk factor (with the exposure value being the amount invested). Similarly, in synthetic deals, the protection providers (sellers of protection by means of CDS/guarantees) may be an additional source of risk and a common factor for interconnecting different structures (in this case, the exposure value would correspond to the percentage value of the underlying portfolio).
- The second implication is that banks may add their investments in a set of structures associated with a third party that constitutes a common risk factor to other exposures (such as a loan) it has to that third party. Whether the exposures to such structures must be added to any other exposures to the third party would again depend on a case-by-case consideration of the specific features of the structure and on the role of the third party. In the example of the fund manager, adding together the exposures may not be necessary because potentially fraudulent behavior may not necessarily affect



the repayment of a loan. The assessment may be different where the risk to the value of investments underlying the structures arises in the event of a third-party default. For example, in the case of a credit protection provider, the source of the additional risk for the bank investing in a structure is the default of the credit protection provider. The bank must add the investment in the structure to the direct exposures to the credit protection provider since both exposures might crystallize into losses in the event that the protection provider defaults (ignoring the covered part of the exposures may lead to the undesirable situation of a high concentration risk exposure to issuers of collateral or providers of credit protection).

It is conceivable that a bank may consider multiple third parties to be potential drivers of additional risk. In this case, the bank must assign the exposure resulting from the investment in the relevant structures to each of the third parties.

The requirement set out in section "Calculation of underlying exposures - bank's exposure amount to underlying assets" in this appendix to recognise a structural risk inherent in the structure instead of the risk stemming from the underlying exposures is independent of whatever the general assessment of additional risks concludes.



Appendix XI

Exposures to central counterparties¹⁷

Banks' exposures to qualifying central counterparties (QCCPs – see note below) related to clearing activities are exempted from the large exposures limits. However, these exposures will be subject to the regulatory reporting requirements as defined in the table below, and the SAMA will monitor the need for this exemption

Note: The definition of QCCP for large exposures purposes is the same as that used for risk-based capital requirement purposes. A qualifying central counterparty (QCCP) is an entity that is licensed to operate as a CCP (including a license granted by way of confirming an exemption), and is permitted by the appropriate regulator/overseer to operate as such with respect to the products offered. This is subject to the provision that the CCP is based and prudentially supervised in a jurisdiction where the relevant regulator/overseer has established, and publicly indicated that it applies to the CCP on an ongoing basis, domestic rules and regulations that are consistent with the CPSS-IOSCO Principles for Financial Market Infrastructures.

In the case of non-QCCPs, banks must measure their exposure as a sum of both the clearing exposures described in sections titled "Calculation of exposures related to clearing activities" and "Other exposures" below, and must respect the general large exposure limit of 25% of the eligible capital base.

The concept of connected counterparties as described in Section 1.2, of these guidelines, does not apply in the context of exposures to CCPs that are specifically related to clearing activities.

Calculation of exposures related to clearing activities:

Banks must identify exposures to a CCP related to clearing activities and sum together these exposures. Exposures related to clearing activities are listed in the table below together with the exposure value to be used:

¹⁷ Paragraphs 84-89 of BCBS "Supervisory framework for measuring and controlling large exposures" April 2014, and FAQs issued in September 2016.



<u>Trade exposures</u>	<u>The exposure value of trade exposures must be calculated using the exposure measures prescribed in other parts of this framework for the respective type of exposures (eg using the SA-CCR for derivative exposures as per SAMA circular no 351000095021 dated 21 May 2014 and circular no. 371000101120 dated 20 June 2016).</u>
<u>Segregated initial margin</u>	<u>The exposure value is 0.- Note A</u>
<u>Non-segregated initial margin</u>	<u>The exposure value is the nominal amount of initial margin posted.</u>
<u>Pre-funded default fund contributions</u>	<u>Nominal amount of the funded contribution. Note B</u>
<u>Unfunded default fund contributions</u>	<u>The exposure value is 0.</u>
<u>Equity stakes</u>	<u>The exposure value is the nominal amount. Note C</u>

Note A: When the initial margin (IM) posted is bankruptcy-remote from the CCP – in the sense that it is segregated from the CCP's own accounts, eg when the IM is held by a third-party custodian – this amount cannot be lost by the bank if the CCP defaults; therefore, the IM posted by the bank can be exempted from the large exposure limit.

Note B: The exposure value for pre-funded default fund contributions may need to be revised if applied to QCCPs and not only to non QCCPs.

Note C: If equity stakes are deducted from the level of capital on which the large exposure limit is based, such exposures must be excluded from the definition of an exposure to a CCP



Regarding exposures subject to clearing services (the bank acting as a clearing member or being a client of a clearing member), the bank must determine the counterparty to which exposures must be assigned by applying the provisions of the risk-based capital requirements. (Refer to circular no. 351000095018 dated 21 May 2014, Basel Committee on Banking Supervision Document regarding Capital Requirements for bank exposures to central counterparties of April 2014)

Other exposures:

Other types of exposures that are not directly related to clearing services provided by the CCP, such as funding facilities, credit facilities, guarantees etc., must be measured according to the rules set out in Sections IV of this guidelines, as for any other type of counterparty. These exposures will be added together and be subjected to the large exposure limit.