



# Decision memo

DATE: 5 October 2012  
DEPARTMENT: Asset Management Department  
REFERENCE: Jan Schüllerqvist

SVERIGES RIKSBANK  
SE-103 37 Stockholm  
(Brunkebergstorg 11)

Tel +46 8 787 00 00  
Fax +46 8 21 05 31  
registratorn@riksbank.se  
www.riksbank.se

---

DNR 2011-399-KAP

## ■ Principles for the rules for collateral for credit pursuant to the Terms and Conditions for RIX and monetary policy instruments

### Proposed decision

The Head of the Asset Management Department proposes

- to determine principles for the rules for collateral for credit pursuant to the Terms and Conditions for RIX and monetary policy instruments (Terms and Conditions) in accordance with [Appendix 1](#), and
- to assign the Head of the RIX Division to prepare a proposal for revised Terms and Conditions in accordance with these principles.

### Background

In light of developments such as the measures adopted during the financial crisis 2008–2010, the Riksbank has carried out a review of the rules for collateral for credit provided in accordance with the Terms and Conditions.

On 16 May 2011, the Riksbank submitted proposed principles for the rules for collateral for credit pursuant to the Terms and Conditions ([Appendix 2](#)) for consultation to the Riksbank's counterparties, the Swedish Bankers' Association and the Swedish Securities Dealers Association. The Riksbank received feedback on the proposal from five companies and organisations ([Appendix 3A-E](#)).

### Considerations

#### Concentration limit

Proposal for consultation: The value of the collateral for certain types of securities may together comprise at the most 40 per cent of a counterparty's total collateral value. The securities encompassed are (i) securities with a credit rating less than AA-, (ii) all securities issued by a counterparty or a company with which the counterparty has close links, regardless of the type of security and credit rating, and (iii) all Asset-Backed Securities.

Feedback from consultation: No feedback was submitted.

■ The proposal for consultation should be adopted. However, the introduction of this limit may restrict the counterparties' possibilities of utilising existing collateral. To limit these immediate effects, the introduction of the limit should take place successively. Consequently, in 2013, the securities encompassed by the limit will be allowed to amount to 100 per cent of a counterparty's total collateral value (i.e. no change), during the first six months of 2014 the securities encompassed by the limit will be allowed to amount to 70 per cent of a counterparty's total collateral value and thereafter the limit will be reduced to 40 per cent of a counterparty's total collateral value.

### **Own covered bonds**

Proposal for consultation: Covered bonds issued by the counterparty or a related company (own covered bonds) that fulfil the requirements of the UCITS Directive<sup>1</sup>, and with creditworthiness equal to at least AA-, will be accepted as collateral, but their use will be limited. The total collateral value of own covered bonds and other types of security also covered by the concentration limit may, at the most, comprise 40 per cent of a counterparty's total collateral value.

Feedback from consultation: The *Association of Swedish Covered Bond Issuers* (ASCB) points out that covered bonds have a special status in the Swedish bond market and among credit institutions' securities as they are covered by special legislation. The ASCB therefore considers that they cannot be compared with other securities issued by the Riksbank's counterparties and therefore suggests that the applicable rules be kept unamended. *Skandinaviska Enskilda Banken* points out that the use of own covered bonds should not be limited in such a way that the counterparties' freedom of action is also limited. The bank also points out that the existence of an extra haircut for own covered securities already forms a negative incentive for these securities.

Like most lenders, the Riksbank does not accept, in principle, that a counterparty provides collateral that the counterparty itself or a company with close links to the counterparty has issued. However, the Riksbank shares the opinion that covered bonds and other covered securities have a special status. It is therefore proposed that covered securities issued by the counterparty itself will be accepted also in the future, however, to a limited extent.

As a principle, the Riksbank endeavours to achieve a diversification of risk towards individual counterparties. This kind of diversification will not be achieved if a counterparty uses covered bonds issued by the counterparty itself or a closely related company without any restrictions. Consequently, there are reasons to limit the use of own covered bonds by introducing a quantitative limit. The potentially higher risk related to an institution using its own securities as collateral also motivates a minor extra haircut.

The proposal for consultation should be adopted for own covered securities.

---

<sup>1</sup> Article 52.4 of Directive 2009/65/EC of the European Parliament and of the Council of 13 July 2009 on the coordination of laws, regulations and administrative provisions relating to undertakings for collective investment in transferable securities (UCITS)

## ■ Haircuts

Proposal for consultation: The haircuts are based on the observed price change over the estimated time it took to liquidate different types of collateral in the period 1 September 2008 – 31 August 2010.

Feedback from consultation: *Skandinaviska Enskilda Banken* notes that the proposed haircuts exceed those currently required by the Eurosystem, while the Riksbank's current haircuts show great similarities to those of the Eurosystem. The bank therefore points out that the proposal goes too far, as it is difficult to argue that the price changes should be significantly higher for the securities accepted by the Riksbank, compared with those accepted by the Eurosystem.

The Riksbank's starting point in the calculation of haircuts is that the haircuts should reflect the real price risk over the time it takes to liquidate the collateral. The haircuts should also cover the risk in periods of stress. The Riksbank's assessment is that the proposed haircuts fulfil these requirements better than the current haircuts.

The proposal for consultation should be adopted for haircuts.

## Asset-Backed Securities

Proposal for consultation: The proposal entailed a continued acceptance of Asset-Backed Securities (ABSs). At the same time, it showed that the Riksbank was considering the possibility of no longer accepting ABSs, due to risk aspects as well as practical aspects. In conjunction with the proposal, reasons for continuing to accept ABSs were requested.

The proposal for consultation meant that ABSs will be required to have had a creditworthiness equal to AAA at issue and thereafter always a creditworthiness of at least AA-. Furthermore, the creditworthiness will be verified by ratings from at least two external credit rating agencies. It was proposed that ABSs not be used without limit, but the total collateral value of ABSs and other types of security also covered by the concentration limit may, at the most, comprise 40 per cent of a counterparty's total collateral value. In addition, there are already existing special requirements for the acquisition of assets, assets in the form of credit derivatives, seniority, and currency protection and liquidity arrangements.

Feedback from consultation: *Citibank* points out that the Riksbank should at least accept the best types of ABS, such as those with the credit rating AAA, those holding loans with collateral in housing as underlying asset and those issued recently.

*Skandinaviska Enskilda Banken* points out that ABSs form a class of asset that will probably increase in significance as an important source of funding for the banking system, not least considering the introduction of Basel III. The bank considers that the limitations proposed by the Riksbank (if ABSs continue to be accepted) should be enough to limit the Riksbank's risk, and so the Riksbank should continue to accept ABSs. *Svensk Exportkredit* points out that the Eurosystem accepts ABSs and that the view of ABSs should be harmonised within the EU. Furthermore, during the financial crisis, many banks encountered problems due to their dependence on borrowing in foreign currency, and there remains a degree of uncertainty, with the market being sensitive to negative events. For this reason, the disqualification of ABSs as approved collateral should be postponed. In addition, investments in ABSs have successively decreased in Sweden, and so *Svensk Exportkredit* deems it would be more appropriate for the Riksbank to stop accepting ABSs as of 2014.

■ The Riksbank may only grant credit against adequate collateral but should not unnecessarily limit the stock of eligible collateral. Accepting ABSs would mean that the counterparties, not least in a crisis situation, would have access to more eligible collateral and therefore have easier access to liquidity from the Riksbank. Accepting ABSs could also contribute to further diversification of the eligible assets. However, it should be noted that the possibility of using ABSs as collateral did not play a vital role in the most recent financial crisis and, at present, ABSs only account for slightly less than 2 per cent of the stock of collateral that has been pledged.

ABSs are often complex products that are structured in order to limit the investor's risk, but without the special arrangements characterising covered bonds. The complexity result in amongst other things not only that the examination of the single securities but also the credit approval process becomes more extensive and therefore subject to larger operational risks. Data from the most recent financial crisis indicate also that liquidity, measured in different ways, has been significantly lower for other securitised products than covered bonds. This can entail potential risks for the Riksbank. Therefore, there is reason to no longer accept ABS. A decision to not accept ABS is deemed not to entail that counterparties meet incentives which from the Riksbank's perspective can be deemed to be negative. In this context, it can be noted that ABS are not considered highly liquid according to Basel III.

Against this background, ABS should not be included in the stock of eligible collateral.

However, to give the counterparties the possibility of adjusting their holdings of collateral, ABSs should continue to be accepted during a transition phase throughout 2013. During this transition phase the requirements specified in the proposal for consultation should be fulfilled.

### **Other issues**

Proposal for consultation: See [Appendix 2](#).

Feedback from consultation: Some omitted details and verbal comments have been pointed out by *Euroclear Sweden*. Those comments have mainly been taken into consideration. Otherwise, it is proposed that the proposal for consultation be adopted.

### **Entry into force**

The proposal for consultation stated that the Terms and Conditions with the new principles were intended to enter into force on 2 January 2012, about six months after the conclusion of the period of consultation. The same time period should apply now, and the new rules should thus enter into force on 15 April 2013.

Transitional rules apply to the concentration limit, to the effect that this limit will come into effect first on 1 January 2014. Until 30 June 2014 the affected securities may amount to 70 per cent of a counterparty's total collateral value. For ABSs, transitional rules will be applied in 2013 as described above.

The Riksbank deems that there is no reason to continue to approve securities as collateral if these securities can only be used for a short period. Consequently, after 31 December 2012, the Riksbank should not approve new securities that do not comply with the new principles. However, during the period in which ABSs are accepted, new securities of this type should be approved.

- The Financial Stability Department, the Monetary Policy Department and the Risk Division of the General Secretariat have been consulted in this matter. Information has been provided to the Executive Board.