WAC 208-512A-300 Credit exposure arising from derivative transactions. (1) This section sets forth the rules for calculating the credit exposure arising from a derivative transaction entered into by a bank for purposes of determining the bank's lending limit pursuant to RCW 30A.04.111 and this chapter.

(2) Subject to the direction of the division, a bank shall calculate the credit exposure to a counterparty arising from a derivative transaction by means of:

(a) The internal model method;

(b) The conversion factor matrix method;

(c) The remaining maturity method; or

(d) The current exposure method.

(3) Except as otherwise required by the division, a bank shall use the same method for calculating counterparty credit exposure arising from all of its derivative transactions.

(4) The division may require a bank to use the internal model method, the conversion factor matrix method, or the remaining maturity method to calculate the credit exposure of derivative transactions if it finds that such method is necessary to promote the safety and soundness of the bank.

(5) The requirements for using the internal model method are as follows:

(a) The credit exposure of a derivative transaction under the internal model method shall equal the sum of the current credit exposure of the derivative transaction and the potential future credit exposure of the derivative transaction.

(b) A bank shall determine its current credit exposure by the mark-to-market value of the derivative contract. If the mark-to-market value is positive, then the current credit exposure equals that mark-to-market value. If the mark-to-market value is zero or negative, than the current credit exposure is zero.

(c) A bank may not use the internal model method in its calculation of potential credit exposure to a derivative transaction unless the bank obtains prior approval of the division or unless it is already using the internal model method, as of January 21, 2013, and the division thereafter determines that the bank's internal model method is safe and sound and that bank's management is competent to administer its derivative investment program using such internal model method.

(d) A bank that calculates its credit exposure by using the internal model method may net credit exposures of derivative transactions arising under the same qualifying master netting agreement.

(6) The credit exposure arising from a derivative transaction under the conversion factor matrix method shall equal and remain fixed at the potential future credit exposure of the derivative transaction as determined at the execution of the transaction by reference to Table 1 below.

Table 1 - Conversion Factor Matrix
for Calculating Potential Future
Credit Exposure[1]

Original Maturity[2]	Interest Rate	Foreign Exchange Rate and Gold	Equity	Other[3] (includes commodities and precious metals except gold)
1 year or less	0.015	0.015	0.20	0.06
Over 1 to 3 years	0.030	0.030	0.20	0.18
Over 3 to 5 years	0.060	0.060	0.20	0.30
Over 5 to 10 years	0.120	0.120	0.20	0.60
Over ten years	0.300	0.300	0.20	1.00

1 For an OTC derivative contract with multiple exchanges of principal, the conversion factor is multiplied by the number of remaining payments in the derivative contract.

2 For an OTC derivative contract that is structured such that on specified dates any outstanding exposure is settled and the terms are reset so that the market value of the contract is zero, the remaining maturity equals the time until the next reset date. For an interest rate derivative contract with a remaining maturity of greater than one year that meets these criteria, the minimum conversion factor is 0.005.

3 Transactions not explicitly covered by any other column in Table 1 are to be treated as "Other."

(7) The credit exposure arising from a derivative transaction under the remaining maturity method shall equal the greater of zero or the sum of the current mark-to-market value of the derivative transaction added to the product of the notional amount of the transaction, the remaining maturity in years of the transaction, and a fixed multiplicative factor determined by reference to Table 2 below.

Table 2 - Remaining Maturity Factor for Calculating Credit Exposure

	Interest Rate	Foreign Exchange Rate and Gold	Equity	Other[1] (includes commodities and precious metals except gold)
Multiplicative Factor	1.5%	1.5%	6%	6%

1 Transactions not explicitly covered by any other column in Table 2 are to be treated as "Other."

(8) The credit exposure arising from a derivative transaction under the current exposure method shall be calculated pursuant to the Office of the Comptroller of the Currency regulations, 12 C.F.R. Part 32, at Sec. 9 (b)(iii).

(9) Notwithstanding any other provision of this section, a bank that uses the conversion factor matrix method or remaining maturity method, or that uses the internal model method without entering an effective margining arrangement, shall calculate the counterparty credit exposure arising from credit derivatives entered by the bank by adding the net notional value of all protection purchased from the counterparty on each reference entity.

(10) A bank shall calculate the credit exposure to a reference entity arising from credit derivatives entered by the bank by adding the notional value of all protection sold on the reference entity. However, the bank may reduce its exposure to a reference entity by the amount of any eligible credit derivative purchased on that reference entity from an eligible protection provider.

[Statutory Authority: RCW 43.320.040, 43.320.050, 30A.04.030, 30A.04.111, 30A.04.215, 30A.08.140, 32.08.157 and section 939A of the Dodd-Frank Act. WSR 17-24-053, § 208-512A-300, filed 12/1/17, effective 1/1/18. Statutory Authority: RCW 30.04.030, 30.04.111, 30.04.215, 30.08.140, 32.08.157, 43.320.040, and 43.320.050 and Section 611 of the Dodd-Frank Wall Street Reform and Consumer Protection Act (codified as section 18(y) of the Federal Deposit Insurance Act, 12 U.S.C. §1828(y)), which takes effect January 21, 2013. WSR 13-03-037, § 208-512A-300, filed 1/8/13, effective 2/8/13.]