[F1 ANNEX VII

COMMODITIES RISK

Textual Amendments

F1 Inserted by Directive 98/31/EC of the European Parliament and of the Council of 22 June 1998 amending Council Directive 93/6/EEC on the capital adequacy of investment firms and credit institutions.

1. Each position in commodities or commodity derivatives shall be expressed in terms of the standard unit of measurement. The spot price in each commodity shall be expressed in the reporting currency.

2. Positions in gold or gold derivatives shall be considered as being subject to foreign-exchange risk and treated according to Annex III or Annex VIII, as appropriate, for the purpose of calculating market risk.

3. For the purposes of this Annex, positions which are purely stock financing may be excluded from the commodities risk calculation only.

4. The interest-rate and foreign-exchange risks not covered by other provisions of this Annex shall be included in the calculation of general risk for traded debt instruments and in the calculation of foreign-exchange risk.

5. When the short position falls due before the long position, institutions shall also guard against the risk of a shortage of liquidity which may exist in some markets.

6. For the purpose of paragraph 19, the excess of an institution's long (short) positions over its short (long) positions in the same commodity and identical commodity futures, options and warrants shall be its net position in each commodity. The competent authorities shall allow positions in derivative instruments to be treated, as laid down in paragraphs 8, 9 and 10, as positions in the underlying commodity.

7. The competent authorities may regard the following positions as positions in the same commodity:

— positions in different sub-categories of commodities in cases where the sub-categories are deliverable against each other,

and

— positions in similar commodities if they are close substitutes and if a minimum correlation of 0,9 between price movements can be clearly established over a minimum period of one year.

Particular instruments

8. Commodity futures and forward commitments to buy or sell individual commodities shall be incorporated in the measurement system as notional amounts in terms of the standard unit of measurement and assigned a maturity with reference to expiry date. The competent authorities may allow the capital requirement for an exchange-traded future to be equal to the margin required by the exchange if they are fully satisfied that it provides an accurate measure of the risk associated with the future and that it is at least equal to the capital requirement for a future that would result from a calculation made using the method set out in the remainder of this Annex or applying

the internal models method described in Annex VIII. Until 31 December 2006 the competent authorities may also allow the capital requirement for an OTC commodity derivatives contract of the type referred to in this paragraph cleared by a clearing house recognised by them to be equal to the margin required by the clearing house if they are fully satisfied that it provides an accurate measure of the risk associated with the derivatives contract and that it is at least equal to the capital requirement for the contract in question that would result from a calculation made using the method set out in the remainder of this Annex or applying the internal models method described in Annex VIII.

9. Commodity swaps where one side of the transaction is a fixed price and the other the current market price shall be incorporated into the maturity ladder approach as a series of positions equal to the notional amount of the contract, with one position corresponding with each payment on the swap and slotted into the maturity ladder set out in the table appearing in paragraph 13. The positions would be long positions if the institution is paying a fixed price and receiving a floating price and short positions if the institution is receiving a fixed price and paying a floating price.

Commodity swaps where the sides of the transaction are in different commodities are to be reported in the relevant reporting ladder for the maturity ladder approach.

10. Options on commodities or on commodity derivatives shall be treated as if they were positions equal in value to the amount of the underlying to which the option refers, multiplied by its delta for the purposes of this Annex. The latter positions may be netted off against any offsetting positions in the identical underlying commodity or commodity derivative. The delta used shall be that of the exchange concerned, that calculated by the competent authorities or, where none of those is available or for OTC options, that calculated by the institution itself, subject to the competent authorities being satisfied that the model used by the institution is reasonable.

However, the competent authorities may also prescribe that institutions calculate their deltas using a methodology specified by the competent authorities.

The competent authorities shall require that the other risks, apart from the delta risk, associated with commodity options are safeguarded against. The competent authorities may allow the requirement for a written exchange-traded commodity option to be equal to the margin required by the exchange if they are fully satisfied that it provides an accurate measure of the risk associated with the option and that it is at least equal to the capital requirement against an option that would result from a calculation made using the method set out in the remainder of this Annex or applying the internal models method described in Annex VIII. Until 31 December 2006 the competent authorities may also allow the capital requirement for an OTC commodity option cleared by a clearing house recognised by them to be equal to the margin required by the clearing house if they are fully satisfied that it provides an accurate measure of the risk associated with the option and that it is at least equal to the capital requirement for an OTC option that would result from a calculation made using the method set out in the remainder of this Annex or applying the internal models method described in Annex VIII. In addition they may allow the requirement on a bought exchange-traded or OTC commodity option to be the same as that for the commodity underlying it, subject to the constraint that the resulting requirement does not exceed the market value of the option. The requirement for a written OTC option shall be set in relation to the commodity underlying it.

11. Warrants relating to commodities shall be treated in the same way as commodity options under paragraph 10.

12. The transferor of commodities or guaranteed rights relating to title to commodities in a repurchase agreement and the lender of commodities in a commodities lending agreement shall include such commodities in the calculation of its capital requirement under this Annex.

(a) Maturity ladder approach

13. The institution shall use a separate maturity ladder in line with the following table for each commodity. All positions in that commodity and all positions which are regarded as positions in the same commodity pursuant to paragraph 7 shall be assigned to the appropriate maturity bands. Physical stocks shall be assigned to the first maturity band.

Maurity band(1)	Spread rate(in %)(2)
0 ≤ 1 month	1,5
> 1 ≤ 3 months	1,5
> 3 ≤ 6 months	1,5
> 6 ≤ 12 months	1,5
> 1 ≤ 2 years	1,5
> 2 ≤ 3 years	1,5
> 3 years	1,5

14. Competent authorities may allow positions which are, or are regarded pursuant to paragraph 7 as, positions in the same commodity to be offset and assigned to the appropriate maturity bands on a net basis for:

— positions in contracts maturing on the same date,

and

— positions in contracts maturing within 10 days of each other if the contracts are traded on markets which have daily delivery dates.

15. The institution shall then work out the sum of the long positions and the sum of the short positions in each maturity band. The amount of the former (latter) which are matched by the latter (former) in a given maturity band shall be the matched positions in that band, while the residual long or short position shall be the unmatched position for the same band.

16. That part of the unmatched long (short) position for a given maturity band that is matched by the unmatched short (long) position for a maturity band further out shall be the matched position between two maturity bands. That part of the unmatched long or unmatched short position that cannot be thus matched shall be the unmatched position.

17. The institution's capital requirement for each commodity shall be calculated on the basis of the relevant maturity ladder as the sum of the following:

(i) the sum of the matched long and short positions, multiplied by the appropriate spread rate as indicated in the second column of the table appearing in paragraph 13 for each maturity band and by the spot price for the commodity;

(ii) the matched position between two maturity bands for each maturity band into which an unmatched position is carried forward, multiplied by 0,6 % (carry rate) and by the spot price for the commodity;

(iii) the residual unmatched positions, multiplied by 15 % (outright rate) and by the spot price for the commodity.

18. The institution's overall capital requirement for commodities risk shall be calculated as the sum of the capital requirements calculated for each commodity according to paragraph 17.

(b) Simplified approach

19. The institution's capital requirement for each commodity shall be calculated as the sum of:

(i) 15 % of the net position, long or short, multiplied by the spot price for the commodity;

(ii) 3 % of the gross position, long plus short, multiplied by the spot price for the commodity.

20. The institution's overall capital requirement for commodities risk shall be calculated as the sum of the capital requirements calculated for each commodity according to paragraph 19.**]**