

## Visual Comparison Chart: U.S. Supplementary Leverage Ratio (SLR) vs. Basel III Leverage Ratio

Posted on April 9, 2014, by **Luigi L. De Ghenghi** and **Andrew S. Fei**

Advanced Approaches, Basel Committee, Basel III - International, Basel III - US, FDIC, Federal Reserve, Final Rules, G-SIB, Leverage Ratios, OCC, Visuals.

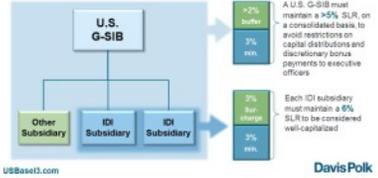
We have prepared a chart that compares the U.S. banking agencies' *proposed* revisions to the U.S. Basel III Supplementary Leverage Ratio (“**SLR**”) with the Basel Committee’s January 2014 revisions to the Basel III leverage ratio. While the revised SLR proposed by the U.S. banking agencies is similar to the revised Basel III leverage ratio in many respects, there are some important differences between the two ratios.

Our visual summary of the SLR denominator proposal and U.S. G-SIB leverage surcharge final rule is available [here](#). Our visual memo of the revised Basel III leverage ratio is [here](#).

### Supplementary Leverage Ratio vs. Basel III Leverage Ratio

[Click on images to enlarge them]

Topic	Revised Basel III Leverage Ratio (Jan. 2014)	Supplementary Leverage Ratio (SLR) (including Apr. 2014 proposed denominator revisions)
<b>Level of the ratio</b>	<ul style="list-style-type: none"> <li>• 3% minimum</li> <li>• Applies to “internationally active banks”</li> <li>• Basel Committee Chairman <b>stated</b> in February 2014: “Only now that we have an agreed [measure of leverage exposure] can the Committee begin to turn to the issue of calibration, and the relationship of the leverage ratio to the risk-based framework. We have quite a bit of work to do to get this balance right.”</li> </ul>	<ul style="list-style-type: none"> <li>• 3% minimum for advanced approaches banking organizations and advanced approaches U.S. intermediate holding companies (“<b>IHCs</b>”) of foreign banks</li> <li>• Surcharge for 8 U.S. global systemically important banks (“<b>G-SIBs</b>”) and their U.S. insured depository institutions (“<b>IDI</b>”) subsidiaries (&gt;5% for consolidated group and 6% for IDI subsidiaries)</li> </ul>

Topic	Revised Basel III Leverage Ratio (Jan. 2014)	Supplementary Leverage Ratio (SLR) (including Apr. 2014 proposed denominator revisions)
	$\text{Basel III Leverage Ratio} = \frac{\text{Tier 1 Capital}}{\text{Exposure Measure}}$	 <p>The diagram illustrates the structure of a U.S. G-SIB and its subsidiaries. At the top is the U.S. G-SIB, which has three subsidiaries: Other Subsidiary, IDI Subsidiary, and IDI Subsidiary. Arrows point from each subsidiary to a box indicating its SLR requirement: Other Subsidiary (no requirement), IDI Subsidiary (6% min.), and IDI Subsidiary (6% min.). A separate box indicates that the U.S. G-SIB must maintain a &gt;5% SLR. Text notes that a U.S. G-SIB must maintain a &gt;5% SLR on a consolidated basis to avoid restrictions on capital distributions and discretionary bonus payments to executive officers, and that each IDI subsidiary must maintain a 6% SLR to be considered well-capitalized.</p> $\text{SLR} = \frac{\text{Tier 1 Capital}}{\text{Total Leverage Exposure}}$
<b>Numerator</b>	<ul style="list-style-type: none"> <li>Tier 1 capital as defined in Basel III, taking into account transitional arrangements</li> <li>Basel Committee will “track the impact” of using either Common Equity Tier 1 capital or total capital as the numerator</li> </ul>	<ul style="list-style-type: none"> <li>Tier 1 capital as defined in the U.S. Basel III final rule, taking into account transitional arrangements</li> </ul>
<b>Denominator</b>	<ul style="list-style-type: none"> <li><b>Exposure Measure</b> (components discussed below)</li> </ul>	<ul style="list-style-type: none"> <li><b>Total Leverage Exposure</b> (components discussed below)</li> </ul>
<b>Frequency of calculation</b>	<ul style="list-style-type: none"> <li>Not specifically addressed in January 2014 revisions</li> <li>July 2013 consultative document: “The basis of calculation is the average of the three month-end leverage ratios over a quarter.”</li> </ul>	<ul style="list-style-type: none"> <li>Tier 1 capital (numerator) is calculated as of the last day of each reporting quarter</li> <li>Total Leverage Exposure (denominator) is calculated as the arithmetic mean of the Total Leverage Exposure calculated <b>each day</b> of the reporting quarter</li> </ul>
<b>Compliance timing</b>	<ul style="list-style-type: none"> <li><b>January 1, 2018:</b> Becomes a minimum requirement after any final calibration and adjustments</li> <li><b>January 1, 2015:</b> Public disclosure begins</li> </ul>	<ul style="list-style-type: none"> <li><b>January 1, 2018:</b> SLR becomes a minimum requirement and SLR surcharge for U.S. G-SIBs becomes effective</li> <li><b>January 1, 2015:</b> Public disclosure begins</li> </ul>

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<p><b>Public disclosures</b></p>	<ul style="list-style-type: none"> <li>Prescribes detailed Pillar 3 disclosure templates and tables</li> </ul> 	<ul style="list-style-type: none"> <li>Prescribes detailed Pillar 3 disclosure table focusing on (1) comparison of accounting assets with Total Leverage Exposure; (2) components of Total Leverage Exposure; and (3) explanation of key drivers of material changes in SLR from quarter to quarter</li> </ul> 
<p><b>Components of denominator</b></p>		
<p><b>1. On-balance sheet assets</b></p>	<ul style="list-style-type: none"> <li>A banking organization must include <b>all</b> balance sheet assets in its Exposure Measure</li> <li><b>Include</b> any on-balance sheet collateral relating to derivatives and repo-style transactions</li> </ul>	<ul style="list-style-type: none"> <li>Balance sheet carrying value of all on-balance sheet assets</li> <li><b>Plus</b> the value of securities sold under a repo-style arrangement that are not included on balance sheet</li> </ul>

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	<ul style="list-style-type: none"> <li>• <b>Exclude</b> on-balance sheet derivative and repo-style transaction assets that are addressed separately below</li> <li>• If a banking organization recognizes fiduciary assets on the balance sheet under applicable accounting standards, these assets can be <b>excluded</b> from the Exposure Measure if the assets meet the IAS 39 criteria for derecognition and, if applicable, IFRS 10 for deconsolidation</li> <li>• Balance sheet assets deducted from Tier 1 capital under Basel III should be <b>excluded</b> from the Exposure Measure</li> <li>• Liability items may <b>not</b> be deducted from the Exposure Measure. <i>E.g.</i>, netting of loans and deposits is not permitted.</li> <li>• A banking organization generally may <b>not</b> take into account of physical or financial collateral, guarantees or other credit risk mitigation techniques to reduce the Exposure Measure.</li> </ul>	<ul style="list-style-type: none"> <li>• <b>Less</b> amounts deducted from Tier 1 capital</li> <li>• <b>Less</b> the value of securities received in security-for-security repo-style transactions, where the banking organization acts as a securities lender and includes the securities received in its on-balance sheet assets but has <b>not</b> sold or re-hypothecated the securities received. If the securities lender sells or re-hypothecates the security, the securities lender would include the amount of cash received or, in the case of re-hypothecation, the value of the security pledged as collateral in Total Leverage Exposure.</li> </ul>
<p><b><u>2. Derivatives – general</u></b></p>	<ul style="list-style-type: none"> <li>• <b>Exposure Measure = replacement cost (RC) + potential future exposure (PFE) +/- adjustments for certain collateral</b></li> <li>• RC + PFE formulation is based on the Current Exposure Method (“<b>CEM</b>”)</li> <li>• In the risk-based capital framework, the Basel Committee has replaced the CEM with a new standardized approach for measuring counterparty credit risk exposures (“<b>SA-CCR</b>”) – Davis Polk overview <a href="#">here</a>. The Basel Committee will consider</li> </ul>	<ul style="list-style-type: none"> <li>• “<b>On-balance sheet assets</b>” already includes the U.S. GAAP on-balance sheet carrying value of a banking organization’s derivatives</li> <li>• For purposes of determining the carrying value of derivative contracts, U.S. GAAP provide a banking organization the option to reduce any positive mark-to-fair value of a derivative contract by the amount of any cash collateral received from the counterparty, provided the relevant U.S. GAAP criteria for offsetting are met (the “<b>U.S. GAAP offset option</b>”).</li> </ul>

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	<p>whether to incorporate SA-CCR into the Basel III leverage ratio framework.</p> <ul style="list-style-type: none"> <li>• There are different calculation methodologies for:</li> <li>• A single derivative transaction that is <b>not</b> subject to an eligible bilateral netting contract</li> <li>• Multiple derivatives subject to an eligible bilateral netting contract</li> <li>• Collateral received and provided by a bank, including cash variation margin</li> <li>• Cleared derivatives</li> <li>• Sold credit protection</li> </ul>	<ul style="list-style-type: none"> <li>• Similarly, under the U.S. GAAP offset option, a banking organization has the option to offset the negative mark-to-fair value of a derivative contract with a counterparty by the amount of any cash collateral posted to the counterparty.</li> <li>• In addition, regardless of whether a banking organization uses the U.S. GAAP offset option to calculate the on-balance sheet amount of derivatives contracts, the banking organization includes the amount of cash collateral received from the counterparty in its on-balance sheet assets, and thus in its Total Leverage Exposure.</li> <li>• <b>PFE:</b> Include PFE amount for each derivative transaction or each single-product netting set of derivative transactions calculated using the CEM <u>without</u> regard to rules that provide for the recognition of eligible collateral</li> <li>• Specifically, there are different calculation methodologies for:               <ul style="list-style-type: none"> <li>• Cash variation margin</li> <li>• Cleared derivatives</li> <li>• Sold credit protection</li> </ul> </li> </ul>
<p><b>2.A Single derivative transaction that is not subject to an eligible bilateral netting contract</b></p>	<ul style="list-style-type: none"> <li>• <b>RC</b> = greater of mark-to-market value and zero</li> <li>• <b>PFE</b> = effective notional principal amount (<i>i.e.</i>, the apparent or stated notional principal amount multiplied by any multiplier in the derivative contract) x add-on factor</li> </ul>	<ul style="list-style-type: none"> <li>• <b>RC</b> = greater of mark-to-market value and zero</li> <li>• <b>PFE</b> = effective notional principal amount x add-on factor</li> <li>• PFE add-on factors (ranging from 0% to 15%) depend on reference asset and remaining maturity of the</li> </ul>

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	<ul style="list-style-type: none"> <li>PFE add-on factors (ranging from 0% to 15%) depend on reference asset and remaining maturity of the derivative</li> </ul> <p style="text-align: center;">PFE Add-on Factors <span style="float: right;">USBasel3.com   DavisPolk</span></p> <table border="1" style="width: 100%; border-collapse: collapse;"> <thead> <tr> <th>Remaining maturity</th> <th>Interest rate</th> <th>FX and gold</th> <th>Credit (qualifying)</th> <th>Credit (non-qualifying)</th> <th>Equity</th> <th>Precious metals (except gold)</th> <th>Other commodities</th> </tr> </thead> <tbody> <tr> <td>≤ 1 year</td> <td>0%</td> <td>1%</td> <td>5%</td> <td>10%</td> <td>6%</td> <td>7%</td> <td>10%</td> </tr> <tr> <td>&gt; 1 year and ≤ 5 years</td> <td>0.5%</td> <td>5%</td> <td>5%</td> <td>10%</td> <td>8%</td> <td>7%</td> <td>12%</td> </tr> <tr> <td>&gt; 5 years</td> <td>1.5%</td> <td>7.5%</td> <td>5%</td> <td>10%</td> <td>10%</td> <td>8%</td> <td>15%</td> </tr> </tbody> </table>	Remaining maturity	Interest rate	FX and gold	Credit (qualifying)	Credit (non-qualifying)	Equity	Precious metals (except gold)	Other commodities	≤ 1 year	0%	1%	5%	10%	6%	7%	10%	> 1 year and ≤ 5 years	0.5%	5%	5%	10%	8%	7%	12%	> 5 years	1.5%	7.5%	5%	10%	10%	8%	15%	<p>derivative.</p> <ul style="list-style-type: none"> <li>PFE add-on factors are broadly similar to those used in the Basel III leverage ratio context</li> </ul> <p style="text-align: center;">PFE Add-on Factors <span style="float: right;">USBasel3.com   DavisPolk</span></p> <table border="1" style="width: 100%; border-collapse: collapse;"> <thead> <tr> <th>Remaining maturity</th> <th>Interest rate</th> <th>FX and gold</th> <th>Credit (qualifying)</th> <th>Credit (non-qualifying)</th> <th>Equity</th> <th>Precious metals (except gold)</th> <th>Other commodities</th> </tr> </thead> <tbody> <tr> <td>≤ 1 year</td> <td>0%</td> <td>1%</td> <td>5%</td> <td>10%</td> <td>6%</td> <td>7%</td> <td>10%</td> </tr> <tr> <td>&gt; 1 year and ≤ 5 years</td> <td>0.5%</td> <td>5%</td> <td>5%</td> <td>10%</td> <td>8%</td> <td>7%</td> <td>12%</td> </tr> <tr> <td>&gt; 5 years</td> <td>1.5%</td> <td>7.5%</td> <td>5%</td> <td>10%</td> <td>10%</td> <td>8%</td> <td>15%</td> </tr> </tbody> </table>	Remaining maturity	Interest rate	FX and gold	Credit (qualifying)	Credit (non-qualifying)	Equity	Precious metals (except gold)	Other commodities	≤ 1 year	0%	1%	5%	10%	6%	7%	10%	> 1 year and ≤ 5 years	0.5%	5%	5%	10%	8%	7%	12%	> 5 years	1.5%	7.5%	5%	10%	10%	8%	15%
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<p><b>2.B Multiple derivatives subject to an eligible bilateral netting contract</b></p>	<ul style="list-style-type: none"> <li><b>Exposure Measure</b> = Net RC + <math>A_{net}</math> +/- Adjustments for Certain Collateral</li> <li><b>Net RC</b> = greater of net mark-to-market replacement cost and zero</li> <li><math>A_{net}</math> = adjusted sum of the PFE amounts of all derivative transactions subject to the same eligible bilateral netting contract</li> <li><math>A_{net}</math> is determined using the following formula, which provides for limited recognition of the benefits of bilateral netting:</li> <li><math>A_{net} = (0.4 \times A_{gross}) + (0.6 \times NGR \times A_{gross})</math></li> <li><math>A_{gross}</math> = sum of individual PFEs (calculated by multiplying the notional principal amount by the appropriate PFE add-on factor) of all transactions subject to the same eligible bilateral netting contract</li> <li><b>NGR</b> = net to gross ratio, which is the ratio of net</li> </ul>	<ul style="list-style-type: none"> <li>Method for calculating the adjusted sum of the PFE amounts (<math>A_{net}</math>) is broadly similar to Basel III leverage ratio.</li> <li><math>A_{net} = (0.4 \times A_{gross}) + (0.6 \times NGR \times A_{gross})</math></li> <li>Cross-product netting may not be used to determine Total Leverage Exposure</li> </ul>																																																																

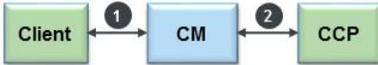
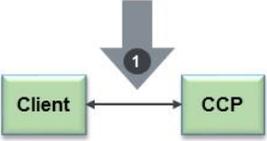
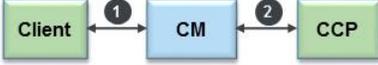
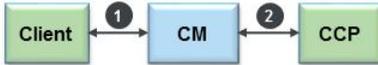
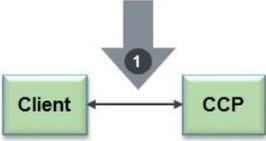
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	<p>RC to gross RC for transactions subject to the same eligible bilateral netting contract (on counterparty by counterparty or aggregate basis, but no netting across counterparties)</p> <ul style="list-style-type: none"> <li>• Cross-product netting may not be used to determine the Exposure Measure</li> </ul>	
<p><b>2.C Definition of eligible bilateral netting contract</b></p>	<p>An <b>eligible bilateral netting contract</b> is a netting contract or agreement with a counterparty:</p> <ul style="list-style-type: none"> <li>• That creates a single legal obligation, covering all included transactions, resulting in either a right to receive or an obligation to pay only the <i>net</i> sum of the positive and negative mark-to-market values of included individual transactions in the event a counterparty fails to perform due to any default, bankruptcy, liquidation or similar circumstances</li> <li>• With respect to which the banking organization has written and reasoned legal opinions concluding and satisfying national supervisor (if necessary after consultation with other relevant supervisors) that, in the event of a legal challenge, the relevant courts and administrative authorities would find the banking organization’s exposure to be the net amount described above under:</li> <li>• The law of the jurisdiction in which the counterparty is chartered and, if the foreign branch of a counterparty is involved, also under the law of jurisdiction in which the branch is located</li> <li>• The law governing the individual transactions</li> </ul>	<p>A <b>qualifying master netting agreement</b> means a written, legally enforceable agreement provided that:</p> <ul style="list-style-type: none"> <li>• The agreement creates a single legal obligation for all individual transactions covered by the agreement upon an event of default, including upon an event of receivership, insolvency, liquidation, or similar proceeding, of the counterparty</li> <li>• The agreement provides the banking organization the right to accelerate, terminate, and close-out on a net basis all transactions under the agreement and to liquidate or set-off collateral promptly upon an event of default, including upon an event of receivership, insolvency, liquidation, or similar proceeding, of the counterparty, provided that, in any such case, any exercise of rights under the agreement will not be stayed or avoided under applicable law in the relevant jurisdictions, other than in receivership, conservatorship, resolution under the Federal Deposit Insurance Act, Title II of the Dodd-Frank Act, or under any similar insolvency law applicable to government sponsored enterprises (“<b>GSEs</b>”)</li> <li>• The agreement does not contain a walkaway clause (that is, a provision that permits a non-defaulting</li> </ul>

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	<ul style="list-style-type: none"> <li>The law governing the netting contract or agreement</li> <li>With respect to which the banking organization has procedures to ensure that the legal characteristics of netting arrangements are reviewed in light of possible changes in relevant law</li> <li>That does not contain a walkaway clause, which is a provision that permits a non-defaulting counterparty to make only limited payments, or no payment at all, to the estate of a defaulter, even if the defaulter is a net creditor</li> </ul>	<p>counterparty to make a lower payment than it otherwise would make under the agreement, or no payment at all, to a defaulter or the estate of a defaulter, even if the defaulter or the estate of the defaulter is a net creditor under the agreement)</p> <ul style="list-style-type: none"> <li>In order to recognize an agreement as a qualifying master netting agreement, a banking organization must comply with the operational requirements for counterparty credit risk with respect to that agreement</li> </ul>
<p><b>2.D Treatment of collateral and cash variation margin</b></p>	<ul style="list-style-type: none"> <li>A banking organization generally <b>cannot</b> reduce the Exposure Measure by any collateral <b>received</b> from the counterparty (regardless of permissibility of netting under applicable accounting standards or risk-based capital framework)</li> <li><b>Exception</b> for cash variation margin that meets certain conditions</li> <li>A banking organization generally must <b>gross up</b> its Exposure Measure by the amount of any derivatives collateral <b>provided</b> where the provision of that collateral has reduced the value of its balance sheet assets under applicable accounting standards</li> <li><b>Exception</b> for cash variation margin that meets certain conditions</li> </ul> <p>If all of the <b>conditions for cash variation margin</b></p>	<ul style="list-style-type: none"> <li>SLR generally does <b>not</b> permit collateral to reduce Total Leverage Exposure</li> <li>If a banking organization reduces the positive mark-to-fair value of a derivative contract with a counterparty as permitted under the U.S. GAAP offset option, but the cash collateral received does <b>not</b> meet the <b>conditions for cash variation margin</b> in the proposal, the banking organization would be required to include the positive mark-to-fair value of the derivative contract <b>gross</b> of any cash collateral in its Total Leverage Exposure</li> <li>Similarly, if a banking organization offsets the net negative mark-to-fair value of derivative contracts with a counterparty by the amount of any cash collateral posted to the counterparty, and does not include that cash collateral posted to the counterparty in its on-balance sheet assets, as permitted under the U.S. GAAP offset option, but the cash collateral posted does <b>not</b> meet the <b>conditions for cash variation margin</b> in</li> </ul>

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	<p>are met, cash variation margin may be treated as follows:</p> <ul style="list-style-type: none"> <li>The banking organization may <b>reduce</b> the RC portion of the Exposure Measure by the amount of cash variation margin received <b>if</b> the positive mark-to-market value of the derivative contract(s) has not already been reduced by the same amount under applicable accounting standards</li> <li>The banking organization may <b>deduct</b> the resulting receivable from the Exposure Measure, <b>if</b> the cash variation margin provided is recognized as an asset under applicable accounting standards</li> <li>Cash variation margin may <b>not</b> be used to reduce the PFE portion of the Exposure Measure</li> </ul>	<p>the proposal, the banking organization would be required to include such cash collateral in its Total Leverage Exposure</p> <ul style="list-style-type: none"> <li>In other words, a banking organization that applies the U.S. GAAP offset option to cash collateral exchanged between it and its counterparty to a derivative contract must <b>reverse</b> the effect of the U.S. GAAP offset for purposes of determining Total Leverage Exposure, <b><u>unless all of the conditions for cash variation margin are met</u></b></li> <li>Cash variation margin may <b>not</b> be used to reduce the PFE portion of the Total Leverage Exposure</li> </ul>
<p><b>2.E Conditions for cash variation margin</b></p>	<ul style="list-style-type: none"> <li>For trades not cleared through a qualifying central counterparty (“<b>QCCP</b>”), the cash received by the recipient counterparty is not segregated</li> <li>Variation margin is calculated and exchanged on a daily basis based on mark-to-market valuation of derivatives positions</li> <li>The cash variation margin is received in the <b>same currency</b> as the settlement currency of the derivative contract</li> <li>Variation margin exchanged is the full amount necessary to fully extinguish the mark-to-market exposure of the derivative subject to the threshold and minimum transfer amounts applicable to the</li> </ul>	<ul style="list-style-type: none"> <li>For derivative contracts that are not cleared through a QCCP, the cash collateral received by the recipient counterparty is not segregated</li> <li>Variation margin is calculated and transferred on a daily basis based on the mark-to-fair value of the derivative contract</li> <li>The variation margin is in the form of cash in the <b>same currency</b> as the currency of settlement set forth in the derivative contract, provided that for the purposes of this paragraph, currency of settlement means any currency for settlement specified in the governing qualifying master netting agreement, the credit support annex to the qualifying master netting agreement, or in the governing rules for a cleared transaction</li> </ul>

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	<p>counterparty</p> <ul style="list-style-type: none"> <li>The derivatives transactions and variation margins are covered by a single master netting agreement between the legal entities that are the counterparties in the derivatives transaction</li> <li>The master netting agreement must explicitly stipulate that the counterparties agree to settle net any payment obligations covered by such a netting agreement, taking into account any variation margin received or provided if a credit event occurs involving either counterparty</li> <li>The master netting agreement must be legally enforceable and effective in all relevant jurisdictions, including in the event of default and bankruptcy or insolvency</li> </ul>	<ul style="list-style-type: none"> <li>The variation margin transferred under the derivative contract or the governing rules for a cleared transaction is the full amount that is necessary to fully extinguish the net current credit exposure to the counterparty of the derivative contracts, subject to the threshold and minimum transfer amounts applicable to the counterparty under the terms of the derivative contract or the governing rules for a cleared transaction</li> <li>The derivative contract and the variation margin are governed by a qualifying master netting agreement (defined above) between the legal entities that are the counterparties to the derivative contract or by the governing rules for a cleared transaction. The qualifying master netting agreement or the governing rules for a cleared transaction must explicitly stipulate that the counterparties agree to settle any payment obligations on a net basis, taking into account any variation margin received or provided under the contract if a credit event involving either counterparty occurs</li> </ul>
<p><b><u>3. Cleared transactions</u></b></p>	<ul style="list-style-type: none"> <li><b>CM guarantees <u>CCP's</u> performance to client:</b> If a clearing member banking organization (“<b>CM</b>”) is contractually obligated to reimburse the client for any losses suffered due to changes in the value of the client’s transactions in the event that the CCP defaults, the CM’s trade exposures to the CCP must be included in the Exposure Measure and treated like any other type of derivative transaction. Trade exposures include initial margin posted irrespective of whether it is bankruptcy remote vis-à-vis the CCP.</li> <li><b>CM does <u>not</u> guarantee CCP’s performance to</b></li> </ul>	<ul style="list-style-type: none"> <li><b>CM guarantees <u>CCP's</u> performance to client:</b> A CM that guarantees the performance of a CCP with respect to a transaction cleared on behalf of a client must treat its exposure to the CCP as a derivative contract for purposes of determining its Total Leverage Exposure</li> <li><b>CM does <u>not</u> guarantee CCP’s performance to client:</b> A CM that does <b>not</b> guarantee the performance of a CCP with respect to a transaction cleared on behalf of a client may <b>exclude</b> its exposure to the CCP for purposes of determining its Total Leverage Exposure</li> <li><b>CM guarantees <u>client's</u> performance to CCP:</b> A CM that guarantees the performance of a client with respect</li> </ul>

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	<p><b>client:</b> If the CM is not contractually obligated to reimburse the client for any losses suffered due to changes in the value of the client's transactions in the event that the CCP defaults, the CM's trade exposures to the CCP should <b>not</b> be included in the Exposure Measure</p> <ul style="list-style-type: none"> <li>• <b>CM guarantees <u>client's</u> performance to CCP:</b> Where a client directly enters into a derivative transaction with the CCP and the CM guarantees its client's performance to the CCP, the CM must treat the guarantee as a derivative transaction that it has entered into with its client, including with respect to the treatment of cash variation margin</li> </ul>	<p>to a cleared transaction must treat its exposure to the client as a derivative contract for purposes of determining its Total Leverage Exposure</p>

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	<p style="text-align: center;"><b>CM Guarantees CCP's Performance to Client</b></p>  <p style="text-align: center;">Include both derivative ① and derivative ② in denominator</p> <p style="text-align: center;"><b>CM Does <u>Not</u> Guarantee CCP's Performance to Client</b></p>  <p style="text-align: center;">Include <u>only</u> derivative ① in denominator</p> <p style="text-align: center;"><b>CM Guarantees Client's Performance to CCP</b></p>  <p style="text-align: center;">Include guarantee ① in denominator as a derivative transaction with the client</p> <p style="text-align: center;">USBasel3.com <b>DavisPolk</b></p>	<p style="text-align: center;"><b>CM Guarantees CCP's Performance to Client</b></p>  <p style="text-align: center;">Include both derivative ① and derivative ② in denominator</p> <p style="text-align: center;"><b>CM Does <u>Not</u> Guarantee CCP's Performance to Client</b></p>  <p style="text-align: center;">Include <u>only</u> derivative ① in denominator</p> <p style="text-align: center;"><b>CM Guarantees Client's Performance to CCP</b></p>  <p style="text-align: center;">Include guarantee ① in denominator as a derivative transaction with the client</p> <p style="text-align: center;">USBasel3.com <b>DavisPolk</b></p>

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<p><b>4. Sold credit protection</b> (credit derivatives and other similar instruments through which a banking organization provides credit protection)</p>	<ul style="list-style-type: none"> <li>• Include in the Exposure Measure the effective notional amount of sold credit protection</li> <li>• The effective notional amount of sold credit protection may be <b>reduced</b> by any negative change in fair value reflected in the banking organization's Tier 1 capital, <u>provided</u> the effective notional amount of the offsetting purchased credit protection is also reduced by any resulting positive change in fair value reflected in Tier 1 capital</li> </ul>	<ul style="list-style-type: none"> <li>• Include the effective notional principal amount of sold credit protection</li> <li>• The effective notional amount of sold credit protection may be <b>reduced</b> by any reduction in the mark-to-fair value of the sold credit protection if the reduction is recognized in Common Equity Tier 1 capital, <u>provided</u> the banking organization also reduces the effective notional principal amount of purchased credit protection used to offset the sold credit protection by the amount of any increase in the mark-to-fair value of the purchased credit protection that is recognized in Common Equity Tier 1 capital</li> </ul>
<p><b>4.A Taking into account certain purchased credit protection</b></p>	<p>The effective notional amount of sold credit protection may be <b>reduced</b> by the effective notional amount of <b>purchased</b> credit protection on the <b>same reference name</b> provided:</p> <ul style="list-style-type: none"> <li>• Remaining maturity of purchased credit protection is <math>\geq</math> remaining maturity of sold credit protection</li> <li>• The purchased credit protection is on a reference obligation that ranks <i>pari passu</i> with <b>or</b> is junior to the underlying reference obligation of the sold credit protection in the case of single-name credit derivatives.</li> <li>• For tranching products, the purchased protection must be on a reference obligation with the same level of seniority.</li> <li>• Where a bank buys credit protection through a total return swap and records the net payments received as net income, but does not record offsetting</li> </ul>	<p>The effective notional amount of sold credit protection may be <b>reduced</b> by the effective notional amount of <b>purchased</b> credit protection provided:</p> <ul style="list-style-type: none"> <li>• Remaining maturity of purchased credit protection is <math>\geq</math> remaining maturity of sold credit protection.</li> <li>• With respect to a credit derivative that references a single exposure, the reference exposure of the purchased credit derivative is to the <b>same legal entity</b> and ranks <i>pari passu</i> with, <b>or</b> is junior to, the reference exposure of the sold credit protection.</li> <li>• With respect to a credit derivative that references multiple exposures, such as securitization exposures, the reference exposures of the purchased credit protection are to the same legal entities and rank <i>pari passu</i> with the reference exposures of the sold credit protection, and the level of seniority of the purchased credit protection ranks <i>pari passu</i> to the level of seniority</li> </ul>

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	<p>deterioration in the value of the written credit derivative (either through reductions in fair value or by an addition to reserves) reflected in Tier 1 capital, the credit protection may <b>not</b> be recognized for the purpose of offsetting the effective notional amounts of sold credit protection</p> <p>Two reference names are considered the same only if they refer to the <b>same legal entity</b></p> <ul style="list-style-type: none"> <li>• For single-name credit derivatives, protection purchased that references a subordinated position may offset protection sold on a more senior position of the same reference entity as long as a credit event on the senior reference asset would result in a credit event on the subordinated reference asset</li> <li>• Protection purchased on a pool of reference entities may offset protection sold on individual reference names if the protection purchased is economically equivalent to buying protection separately on each of the individual names in the pool (<i>e.g.</i>, if a banking organization purchases protection on an entire securitization structure)</li> <li>• If a banking organization purchases protection on a pool of reference names, but the credit protection does not cover the entire pool (<i>i.e.</i>, the protection covers only a subset of the pool, as in the case of an <math>n^{\text{th}}</math>-to-default credit derivative or a securitization tranche), offsetting is <b>not</b> permitted for the protection sold on individual reference names</li> <li>• However, purchased credit protection may offset</li> </ul>	<p>of the sold credit protection</p> <ul style="list-style-type: none"> <li>• A banking organization may reduce the effective notional principal amount of sold credit protection that references a single reference exposure by a purchased credit protection that references multiple exposures if the purchased credit protection is economically equivalent to buying credit protection separately on each of the individual reference exposures of the sold credit protection. <i>E.g.</i>, if a banking organization purchases credit protection on an entire securitization structure or on an entire index that includes the reference exposure of the sold credit protection.</li> <li>• However, if a banking organization purchases credit protection that references multiple exposures, but the purchased credit protection does not cover all of the sold credit protection's reference exposures (<i>i.e.</i>, the purchased credit protection covers only a subset of the sold credit protection's reference exposures, as in the case of an <math>n^{\text{th}}</math>-to-default credit derivative or a tranche of a securitization), the banking organization may <b>not</b> reduce the effective notional principal amount of the sold credit protection that references a single exposure.</li> <li>• If a banking organization purchases credit protection through a total return swap and records the net payments received as net income but does not record offsetting deterioration in the mark-to-fair value of the sold credit protection on the reference exposure (either through reductions in fair value or by additions to reserves) in Common Equity Tier 1 capital, the banking organization may <b>not</b> reduce the effective notional principal amount of the sold credit protection</li> </ul>

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	<p>sold credit protection on a pool if the purchased protection covers the entire subset of the pool on which protection has been sold</p>	
<p><b>4.B Adjustments to PFE to avoid double counting of sold credit protection</b></p>	<ul style="list-style-type: none"> <li>To avoid double-counting of the notional amount, a banking organization may adjust the PFE for sold credit protection</li> <li>If an eligible bilateral netting contract is <u>not</u> in place, a <b>PFE of zero</b> is assigned to sold credit protection whose effective notional amount is already included in the Exposure Measure</li> <li>If an eligible bilateral netting contract is in place, <math>A_{\text{gross}}</math> may be reduced by the individual PFEs of sold credit protection whose notional amounts are already included in the Exposure Measure. However, <b>no</b> adjustments may be made to NGR.</li> </ul>	<ul style="list-style-type: none"> <li>To avoid double-counting of the notional amount, a banking organization may adjust the PFE for sold credit protection</li> <li>For example, if sold credit protection is governed by a qualifying master netting agreement, a banking organization may adjust the PFE for sold credit protection covered by the qualifying master netting agreement</li> <li>A banking organization that makes such election must do so consistently over time for the calculation of PFE for all sold credit protection. However, <b>no</b> adjustments may be made to NGR.</li> </ul>
<p><b>5. Repo-style transactions</b> (including securities lending, securities borrowing, repurchase and reverse repurchase transactions)</p>	<ul style="list-style-type: none"> <li><b>Exposure Measure = Adjusted Repo-Style Transaction Assets + Counterparty Credit Exposure</b></li> <li><b>Adjusted Repo-Style Transaction Assets =</b> <u>Gross</u> repo-style transaction assets recognized for accounting purposes (<i>i.e.</i>, with no recognition of <i>accounting</i> netting), but adjusted as follows: <ul style="list-style-type: none"> <li><b>Exclude</b> from the Exposure Measure the value of any securities <b>received</b> under a repo-style transaction if the banking organization has recognized the securities as an asset on its balance sheet. This may apply, for example, under certain accounting regimes where securities</li> </ul> </li> </ul>	<ul style="list-style-type: none"> <li><b>“On-balance sheet assets”</b> already includes the U.S. GAAP on-balance sheet carrying value of a banking organization’s repo-style transactions</li> <li><b>Exclude</b> from carrying value of on-balance sheet assets the value of securities received in security-for-security repo-style transactions, where the banking organization acts as a securities lender and includes the securities received in its on-balance sheet assets but has <b>not</b> sold or re-hypothecated the securities received. If the securities lender sells or re-hypothecates the security, the securities lender would include the amount of cash received or, in the case of re-hypothecation, the value of the security pledged as collateral in Total Leverage Exposure.</li> </ul>

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	<p>received under a repo-style transaction may be recognized as assets if the recipient has the right to rehypothecate but has not done so</p> <ul style="list-style-type: none"> <li>• Cash payables and cash receivables in repo-style transactions with the same counterparty may be netted if the <b>conditions for netting of repo-style transaction</b> are satisfied</li> <li>• In other words, although <i>accounting</i> netting is not recognized, regulatory netting is permissible if the <b>conditions for netting of repo-style transaction</b> are satisfied</li> </ul>	<ul style="list-style-type: none"> <li>• For the purpose of determining the on-balance sheet carrying value of a repo-style transaction with a counterparty, U.S. GAAP permits the offset of gross values of receivables due from a counterparty under reverse repurchase agreements by the amount of the payments due to the counterparty (<i>i.e.</i>, amounts recognized as payables to the same counterparty under repurchase agreements), provided the relevant accounting criteria are met (“<b>U.S. GAAP offset for repo-style transactions</b>”)</li> <li>• Where a banking organization acting as a principal has more than one repo-style transaction with the same counterparty and has applied the U.S. GAAP offset for repo-style transactions, but the <b>conditions for netting of repo-style transactions</b> are not satisfied, it must include the gross value of receivables associated with the repo-style transactions less any on-balance sheet receivables amount associated with these repo-style transactions</li> <li>• In other words, a banking organization that applies the U.S. GAAP offset for repo-style transactions must <b>reverse</b> the effect of the U.S. GAAP offset for purposes of determining Total Leverage Exposure, <b>unless all of the conditions for netting of repo-style transactions are met.</b></li> </ul>
<p><b>5.A Conditions for netting of repo-style transactions</b></p>	<ul style="list-style-type: none"> <li>• The repo-style transactions are with the same counterparty</li> <li>• The repo-style transactions have the same explicit final settlement date</li> <li>• The right to set off the amount owed to the</li> </ul>	<ul style="list-style-type: none"> <li>• The offsetting transactions have the same explicit final settlement date under their governing agreements</li> <li>• The right to offset the amount owed to the counterparty with the amount owed by the counterparty is legally enforceable in the normal course of business and in the event of receivership, insolvency, liquidation, or similar</li> </ul>

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	<p>counterparty with the amount owed by the counterparty is legally enforceable both in the normal course of business and in the event of default; insolvency; and bankruptcy</p> <ul style="list-style-type: none"> <li>The counterparties intend to settle net, settle simultaneously, or the transactions are subject to a settlement mechanism that results in the functional equivalent of net settlement, <i>i.e.</i>, the cash flows of the transactions are equivalent, in effect, to a single net amount on the settlement date</li> <li>To achieve such equivalence, both transactions are settled through the same settlement system and the settlement arrangements are supported by cash and/or intraday credit facilities intended to ensure that settlement of both transactions will occur by the end of the business day and the linkages to collateral flows do not result in the unwinding of net cash settlement</li> </ul>	<p>proceeding</p> <ul style="list-style-type: none"> <li>Under the governing agreements, the counterparties intend to settle net, settle simultaneously, or settle according to a process that is the functional equivalent of net settlement. That is, the cash flows of the transactions are equivalent, in effect, to a single net amount on the settlement date</li> <li>To achieve this result, both transactions must be settled through the same settlement system and the settlement arrangements must be supported by cash or intraday credit facilities intended to ensure that settlement of both transactions will occur by the end of the business day, and the settlement of the underlying securities does not interfere with the net cash settlement</li> </ul>
<p><b>5.B Counterparty credit exposure for repo-style transactions</b></p>	<ul style="list-style-type: none"> <li>If a qualifying master netting agreement is in place, <b>Counterparty Credit Exposure = max {0, [<math>\sum E_i - \sum C_i</math>]}</b></li> <li>If a qualifying master netting agreement is <u>not</u> in place, <b>Counterparty Credit Exposure = max {0, [<math>E_i - C_i</math>]}</b></li> <li><math>\sum E_i</math> = total fair value of securities and cash lent to a counterparty for all transactions included in the qualifying master netting agreement</li> <li><math>\sum C_i</math> = total fair value of cash and securities received from the counterparty for all transactions</li> </ul>	<p>The counterparty credit exposure of a repo-style transaction, including where the banking organization acts as an agent for a repo-style transaction, is calculated in a manner that is broadly consistent with methods in the Basel III leverage ratio:</p> <ul style="list-style-type: none"> <li>If a qualifying master netting agreement is in place, <b>Counterparty Credit Exposure = max {0, [<math>\sum E_i - \sum C_i</math>]}</b></li> <li>If a qualifying master netting agreement is <u>not</u> in place, <b>Counterparty Credit Exposure = max {0, [<math>E_i - C_i</math>]}</b></li> <li><math>\sum E_i</math> = total fair value of instruments, gold, or cash that the banking organization has lent, sold subject to</li> </ul>

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	<p>included in the qualifying master netting agreement</p> <ul style="list-style-type: none"> <li>If a qualifying master netting agreement is <b>not</b> in place, Counterparty Credit Exposure is calculated on a transaction by transaction basis, <i>i.e.</i>, each transaction <i>i</i> is treated as its own netting set</li> </ul>	<p>repurchase or provided as collateral to a counterparty for all transactions included in the qualifying master netting agreement</p> <ul style="list-style-type: none"> <li><math>\Sigma C_i</math> = total fair value of the instruments, gold, or cash that the banking organization borrowed, purchased subject to resale or received as collateral from the counterparty for all transactions included in the qualifying master netting agreement</li> <li>If a qualifying master netting agreement is <b>not</b> in place, Counterparty Credit Exposure is calculated on a transaction by transaction basis, <i>i.e.</i>, each transaction <i>i</i> is treated as its own netting set.</li> </ul>
<p><b>5.C Acting as agent in repo-style transactions and providing an indemnity to a counterparty</b></p>	<ul style="list-style-type: none"> <li>If a banking organization acting as agent in a repo-style transaction provides an indemnity or guarantee to a customer or counterparty for any <b>difference</b> between the value of the security or cash the customer has lent and the value of collateral the borrower has provided, the banking organization should include in its Exposure Measure <b>only</b> the measure for Counterparty Credit Exposure and <b>not</b> Adjusted Repo-Style Transaction Assets</li> <li>If a qualifying master netting agreement is in place, <b>Counterparty Credit Exposure</b> = <math>\max \{0, [\Sigma E_i - \Sigma C_i]\}</math></li> <li>If a qualifying master netting agreement is <u>not</u> in place, <b>Counterparty Credit Exposure</b> = <math>\max \{0, [E_i - C_i]\}</math></li> <li><b>Further economic exposure:</b> If a banking</li> </ul>	<ul style="list-style-type: none"> <li>Where a banking organization acts as agent for a repo-style transaction and provides a guarantee (indemnity) to a customer with regard to the performance of the customer's counterparty that is <b>greater</b> than the difference between the fair value of the security or cash lent and the fair value of the security or cash borrowed, the banking organization must <b>include</b> the amount of the guarantee that is greater than this difference in its Total Leverage Exposure.</li> </ul>

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	<p>organization is further economically exposed (<i>i.e.</i>, beyond the guarantee for the difference between the value of the security or cash its customer has lent and the value of the collateral the borrower has provided) to the underlying security or cash in the repo-style transaction, the banking organization must calculate its Exposure Measure as if it were acting as principal, <i>i.e.</i>, by including both Adjusted Repo-Style Transaction Assets and the measure for Counterparty Credit Exposure.</p> <ul style="list-style-type: none"> <li>• <b>No guarantee or indemnity:</b> Where a banking organization acting as an agent in a repo-style transaction does <b>not</b> provide an indemnity or guarantee to any of the involved parties, the banking organization is not exposed to the repo-style transaction and should <u>not</u> include the transaction in its Exposure Measure.</li> </ul>	
<p><b><u>5.D Reversing sales-related accounting entries</u></b></p>	<p>Where sale accounting is used for a repo-style transaction under applicable accounting standards, the banking organization must:</p> <ul style="list-style-type: none"> <li>• <b>Reverse</b> all sales-related accounting entries; and</li> <li>• Calculate its Exposure Measure as if the repo-style transaction had been treated as a financing transaction under applicable accounting standards.</li> </ul>	<ul style="list-style-type: none"> <li>• If a banking organization sells securities under a repo-style transaction and the transaction is treated as a sale (rather than a secured borrowing) for accounting purposes, the banking organization is required to add the value of such securities to its Total Leverage Exposure for as long as the repo-style arrangement is outstanding</li> </ul>
<p><b><u>6. Other off-balance sheet items</u></b></p>	<ul style="list-style-type: none"> <li>• <b>10%</b> credit conversion factor (“<b>CCF</b>”) for commitments that are unconditionally cancelable at any time by the banking organization without prior notice, or that effectively provide for automatic cancellation due to deterioration in a borrower’s</li> </ul>	<ul style="list-style-type: none"> <li>• <b>10%</b> CCF for a commitment that is unconditionally cancelable by the banking organization</li> <li>• <b>20%</b> CCF for the amount of a commitment with an original maturity of <math>\leq 1</math> year that is not unconditionally</li> </ul>

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	<p>creditworthiness</p> <ul style="list-style-type: none"> <li>• <b>10%</b> CCF for undrawn servicer cash advances or facilities that are unconditionally cancelable without prior notice (at national discretion)</li> <li>• <b>20%</b> CCF for short-term self-liquidating trade letters of credit arising from the movement of goods (e.g., documentary credits collateralized by the underlying shipment) – for both issuing and confirming banking organizations</li> <li>• <b>20%</b> CCF for commitments other than securitization liquidity facilities with an original maturity of <math>\leq 1</math> year</li> <li>• <b>50%</b> CCF for commitments with an original maturity of <math>&gt; 1</math> year</li> <li>• <b>50%</b> CCF for note issuance facilities (“<b>NIFs</b>”)</li> <li>• <b>50%</b> CCF for revolving underwriting facilities (“<b>RUFs</b>”)</li> <li>• <b>50%</b> CCF for certain transaction-related contingent items (e.g., performance bonds, bid bonds, warranties and standby letters of credit related to particular transactions)</li> <li>• <b>50%</b> CCF for all eligible liquidity facilities</li> <li>• <b>100%</b> CCF for all off-balance sheet securitization exposures, except an eligible liquidity facility or an eligible servicer cash advance facility</li> <li>• <b>100%</b> CCF for direct credit substitutes, e.g., general guarantees of indebtedness (including</li> </ul>	<p>cancelable by the banking organization</p> <ul style="list-style-type: none"> <li>• <b>20%</b> CCF for self-liquidating trade-related contingent items with an original maturity of <math>\leq 1</math> year</li> <li>• <b>50%</b> CCF for the amount of a commitment with an original maturity of <math>&gt; 1</math> year that is not unconditionally cancelable by the banking organization</li> <li>• <b>50%</b> CCF for transaction-related contingent items (performance bonds, bid bonds, warranties, and standby letters of credit)</li> <li>• <b>100%</b> CCF for guarantees, credit-enhancing representations and warranties that are not securitization exposures, financial standby letters of credit and forward agreements</li> </ul>

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	<p>standby letters of credit serving as financial guarantees for loans and securities) and acceptances (including endorsements with the character of acceptances)</p> <ul style="list-style-type: none"> <li>• <b>100%</b> CCF for forward asset purchases, forward forward deposits and partly paid shares and securities, which represent commitments with certain drawdown</li> <li>• A banking organization may apply the lower of the two applicable CCFs to an undertaking to provide a commitment on an off-balance sheet item</li> </ul>	