

## Guidance for Completing the Exit Costs Template (Template A)

### Overview

The purpose of this template is to assist in the analysis and review of exit cost projections and of trade exit-related liquidity flow projections. The template breaks down the total exit cost by driver, timeframe and by segment, with associated liquidity flow and portfolio information. This data is expected to be a product of the management information system used to communicate key quantitative information to internal decision-makers (i.e. in the TWD firm) and external decision-makers (i.e. at the Bank).

As described in the SS 4.33, the first important step in modelling exit costs is to segment the balance sheet into sub-portfolios (or segments), reflecting the disposal strategy and position characteristics that materially impact the method and cost of exit. The segments used for completing this template should be at least as granular as the segmentation used for modelling exit costs. Further subdivisions should be provided where they are useful for review, analysis or planning purposes.

Some exit cost elements captured in the template may not apply at the segment level (e.g. whole portfolio level hedging costs, the tear-up and replacement costs of intra-Group hedges, FVA and PVA reporting). Such items should be reported at the level at which they are calculated for internal management information, using additional segment identifiers (field 1 below). The “hedging” exit strategy (field 34) should be selected in these cases.

In addition to populating the template, firms should produce a narrative report to accompany the completed template, which would as a minimum:

- List and explain key features and assumptions of their approach to calculating the cost and other projections;
- Provide commentary on and analysis of the projections.

### Detailed Template Description & Guidance

*Please note: Unless otherwise stated, enter all currency amounts in the template in: your reporting currency; the units of your internal MI (e.g. if your MI is calculated to the nearest \$ then report in this unit and do not round to the nearest \$1000 or \$1million).*

The template is divided into six sections (colour coded in the Excel file) as follows:

1. *Segment Description;*
2. *Segment Metrics;*
3. *Exit Strategy;*
4. *Exit Costs - Hedging Costs;*
5. *Exit Costs - Exit Discounts; and*
6. *Timing of Exit Costs and Liquidity Flows.*

Each of these sections will now be considered in greater detail.

## 1. Segment Description

The aim of this section is to provide a description of the contents of each segment, using trade attributes that commonly drive portfolio segmentation. Some of the fields contain characteristics that may not be relevant to a particular TWD firm's methodology, in which case it may be appropriate to leave these blank or complete with generic categories rather than complete lists. For example, if a derivatives sub-portfolio contains trades with a variety of counterparty types, but this differentiation in counterparty type has no impact on the method or cost of exit, then a single segment may be sufficient and a generic description of the counterparty types within the segment can be provided.

### Field Definitions

1: Unique Segment Identifier (USI): Free format alphanumeric field. Each segment line should have a unique identifier. TWD firms may choose a simple integer approach (1, 2, 3, 4...), or use decimals (1.1, 1.2, 2.1, 2.2...) or alphanumerics (R1, R2, R3, E1, E2...) to provide a hierarchical structure.

2: Group ID: Free format alphanumeric with similar approach options to the USI. Grouping should be used where multiple segment lines need to be linked together to represent a single exit strategy (not to be confused with corporate grouping of entities). A common example is a hedged portfolio of intra-group (this time in the corporate group sense) and 3<sup>rd</sup>-party trades, where the intra-group trades have to be replaced prior to the sale of the package.

3/4: Business Area and Sub-Business Area: Free format text fields that provide a two level breakdown of a TWD firm's balance sheet. TWD firms may use these fields as they think best, although it may be common for the business area to be an asset class (e.g. Rates) and the sub-business area to represent a product set and region combination (e.g. 'EMEA Flow Derivatives').

5: Asset Class: Asset class of the business selected from the following list:

- Commodities;
- Credit;
- Equities;
- Financing;
- FX;
- Multi-Asset;
- Rates;
- Other.

6: Products: Free format text field. A description of the products included in the exit segment. This should focus on product attributes and market context that are relevant to the chosen exit strategy e.g. complexity, level of market standardisation, existence / non-existence of 2-way flow. Where possible, this information should be integrated into the product taxonomy used for business as usual purposes.

7: Currencies: A list of all currencies included in the segment, using standard currency codes. This should not only consider the settlement currency, but also all underlying asset currencies for derivatives (e.g. if a segment included equity basket options, then the currency list should cover the currencies of all stocks in the baskets).

8: Maturities: Free format text. Range of product maturities covered by the exit segment (e.g. less than 20 years, 20-30 years, etc.). “All” is not permissible (the full range should be provided), although maturity may not be applicable (e.g. as for a simple stock portfolio), in which case “N/A” may be used.

9: Counterparty Types: Free format text listing the counterparty types for positions within the segment (e.g. broker-dealers, banks, insurance companies, pension funds, hedge funds, large corporates, internal, etc.). The descriptions used should identify any counterparty characteristics that impact the method and cost of exit.

10: Collateralisation: List of collateralisation types included in the segment taken from the following list (where ‘Other’ is used, this should be explained in the free format description of the exit segment):

- Clearing House Margin;
- Single Currency Cash CSA;
- Multi-Currency Cash CSA;
- Bond CSA (Super Green Assets);
- Bond CSA (Other);
- Mixed Cash and Securities CSA;
- None;
- Other.

11: Description of Exit Segment: An additional free format description of the exit segment that summarises the nature of the segment and explains why it can be considered a homogeneous unit for the purpose of disposal. An explanation of any “Other” counterparties or types of collateralisation should be included.

## **2. Segment Metrics**

The purpose of this section is to present various metrics that are likely to be useful in indicating the scale of segments as a reference for review and analysis. They also help TWD firms to demonstrate completeness by showing that totals can be reconciled to regulatory or internal reporting.

With the exception of hedging costs, Fair Value Adjustment (FVA) offset and Prudent Valuation Adjustment (PVA) fields, all the portfolio metrics should be self-explanatory and available at the same level of granularity as the segmentation. Concentration and loss of market maker exemption-related bid-offer PVA are separated from other elements of the PVA, as they potentially overlap with the exit costs.

When hedging costs, FVA or PVA are calculated at a higher level of portfolio granularity than the exit segmentation (i.e. it is less granular), a separate segment line should be included for the component that cannot be disaggregated. The Group ID (potentially multiple groups) and segment descriptions should be used to explain which exit segments the component covers.

### **Field Definitions**

12: 3<sup>rd</sup> Party No. of Trades: Numeric field capturing the number of trades with 3<sup>rd</sup> parties in the exit segment. Positions in securities and listed derivatives should be considered a single position.

13: 3<sup>rd</sup> Party No. of Counterparties: Numeric field capturing the number of 3<sup>rd</sup> party counterparties in the exit segment.

14: 3<sup>rd</sup> Party Long Book Value: Numeric field capturing the long book value (i.e. gross assets) with 3<sup>rd</sup> parties, in reporting currency. Netting is only permitted for securities and exchange traded derivatives.

15: 3<sup>rd</sup> Party Short Book Value: Numeric field capturing the short book value (i.e. gross liabilities) with 3<sup>rd</sup> parties, in reporting currency. Netting is only permitted for securities and exchange-traded derivatives.

16: Intra-Group No. of Trades: Numeric field capturing the number of trades with intra-group entities in the exit segment. Positions in securities and listed derivatives should be considered a single trade.

17: Intra-Group No. of Counterparties: Numeric field capturing the number of intra-Group counterparties in the exit segment.

18: Intra-Group Long Book Value: Numeric field capturing the long book value (i.e. gross assets) with intra-group entities, in reporting currency. Netting is only permitted for securities and exchange traded derivatives.

19: Intra-Group Short Book Value: Numeric field capturing the short book value (i.e. gross liabilities) with intra-group entities, in reporting currency. Netting is only permitted for securities and listed derivatives.

20: Appropriate Risk Metric and Units: We encourage TWD firms to use this and the following two fields where they help characterise the segment. They are particularly relevant where segments contain unhedgeable risks that drive the cost of exit. For example, correlation might be the relevant risk metric for many exotic derivative portfolios. The relevant risk metric field is a free format text field that should describe the risk metric chosen as the most relevant (possibly most illiquid) in terms of exit considerations, and the reporting units (e.g. reporting currency millions per basis point change in interest rate).

21: Long Risk: Numeric field showing the sum of long risks in the portfolio. Netting should ideally follow that used for market value.

22: Short Risk: Numeric field showing the sum of short risks in the portfolio. Netting should ideally follow that used for market value.

23: Capital Usage Metric: Numeric field providing a measure of the future capital usage of the segment assuming it runs to contractual maturity, such as present value of RWAs.

24: Close-out cost FVAs: Bid-offer reserves applied to reflect bid-mid or mid-offer spread that would be charged on exit, where position values are marked to mid-market price.

25: Credit Valuation Adjustment: Numeric field showing the sum of adjustments applied in fair value to cover expected losses due to counterparty default.

26: Debit Valuation Adjustment: Numeric field showing the sum of adjustments applied in fair value to reflect the risk of the TWD firm's own default.

27: Funding Valuation Adjustment: Numeric field showing the sum of adjustments applied in the institution's fair value, to reflect the funding cost that market participants would factor into the exit price for a position or portfolio.

28: Other non-XVA FVAs: Numeric field showing the sum of other fair value adjustments included in fair value, e.g. model risk, price uncertainty, concentrated positions, future administrative costs, early termination risk etc.

29: Other XVAs: Numeric field, e.g. margin valuation adjustment, replacement valuation adjustment, capital valuation adjustment.

30: Concentration AVA (Additional Valuation Adjustment): Numeric field capturing the concentration element of PVA relating to the exit segment in reporting currency. Concentration AVA is risk- or position-specific, so should normally be available at the same level as the exit segment. If this is not possible, a separate segment line should be included for the PVA using the Group ID and/or the segment description, to explain which exit segments it relates to.

31: Loss of Market Maker Exemption AVA: Numeric field capturing the portion of Bid-Offer related AVA for the exit segment, in reporting currency, net of any diversification applied, that is due to removal of the market maker exemption. Where this element of PVA is calculated at a portfolio level, which does not allow it to be broken down at the exit segment level, a separate segment line should be included for this element of PVA. The Group ID and/or the segment description should be used to explain which exit segments it relates to.

32: Other Overlapping PVA: Numeric field capturing the remaining PVA in reporting currency that the TWD firm considers overlapping with exit costs (e.g. where the exit cost and the PVA taken together would bring the valuation below a theoretical floor), net of any diversification benefit applied, for the exit segment. Where this element of PVA is calculated at a portfolio level, which does not allow it to be broken down at the exit segment level, a separate segment line should be included for this element of PVA. The Group ID and/or the segment description should be used to explain which exit segments the PVA relates to. The other overlapping PVA can be broken down into multiple lines if the additional granularity increases the transparency of the data.

33: Other Non-Overlapping PVA: Numeric field capturing the remaining PVA in reporting currency, that the TWD firm does not consider overlaps with the exit discounts (e.g. fair value uncertainty that should be combined with any exit discounts to establish the exit price to a 90<sup>th</sup> percentile degree of confidence, per the Prudent Valuation RTS), net of any diversification applied, for the exit segment. Where this element of PVA is calculated at a portfolio level that does not allow it to be broken down at the exit segment level, a separate segment line should be included for this element of PVA. The Group ID and/or the segment description should be used to explain which exit segments it relates to. The residual PVA can be broken down into multiple lines if the additional granularity aids the transparency of the data.

C1: Total PVA (This is a calculated field that should not be populated): Numeric calculated field which is the sum of the concentration, loss of market maker and other PVA fields for the specific exit segment. Across the entire balance sheet this should reconcile to the reported post-diversification PVA for the reference date.

### 3. Exit Strategy

This section of the template is used to identify the planned exit method. The exit strategy “Hedging” in field 34 should be used to cover hedging costs that cannot be allocated down to the exit segment level.

#### Field Definitions

34: Exit Strategy: Text field identifying the expected exit strategy. The following list provides expected principal exit strategies, categorised to a level within which the exit cost calculation methodology is likely to be affected by similar considerations and therefore fairly homogenous. It is not exhaustive and TWD firms should add other categories if they are useful.

- Contractually matures within wind-down period (3rd party trades);
- Contractually matures within wind-down period (intra-group trades);
- Cash security sale or buyback;
- Exchange traded derivative closeout;
- Cleared derivative closeout;
- Trade Compression;
- Package and sell;
- Exercise contractual option to terminate (potential loss due to out of the money exercise and loss of option time value);
- Negotiate closeout (close out of single counterparty portfolios by negotiation with the counterparty);
- Intra-group trade tear-up;
- Hedging; to be used for costs and measures that cannot be allocated to a segment level (see 3A overview section above);
- Client exercises option to terminate arising due to credit down grade triggers;
- Client exercises option to terminate – other;
- Securitisation;
- Contractually forced exit due to credit downgrade triggers;
- Discretionary Rump;
- Non-Discretionary Rump - Client Not Expected to Provide Consent;
- Non-Discretionary Rump - Collateralisation (Uncollateralised or Non-Standard);
- Non-Discretionary Rump - Insufficient Market Capacity;
- Non-Discretionary Rump - Legal or Regulatory Restrictions;
- Non-Discretionary Rump - Subject to Ongoing Litigation;
- Non-Discretionary Rump - Unable to Identify or Contact End Client(s);
- Non-Discretionary Rump - Other (Please Specify);
- Positions held to support non-discretionary rump - Cash, HQLA or Other Liquid Structural Rump Assets;
- Positions held to support non-discretionary rump - Hedges to Other Rump Positions;
- Positions held to support non-discretionary rump - Issued Debt, Structural Funding Liabilities or Equity;
- Positions held to support non-discretionary rump - Other (Please Specify); and

- Not in scope of TWD option – (Trading Book positions not wound down under partial wind-down plans).

Exit cost estimates should be included for discretionary rump positions.

35: Type of Buyer/Counterparty: Text field selected from the list below identifying the expected type of buyer for the segment:

- Broker-Dealer;
- Bank;
- Hedge Fund;
- Pension Fund;
- Mutual Fund;
- Insurance Company;
- Corporate; and
- Other.

36: Estimated Number of Disposal Packages: Numeric field showing the number of trades / components into which the exit segment is expected to be broken down when novating or selling to other parties. This may commonly be '1' for segments that are 'small' as compared with the size of the market, but it is possible that a relatively homogeneous segment may still need to be sold in multiple pieces.

#### **4. Exit Costs – Hedging Costs**

This section separates out the different hedging elements of the wind-down. Hedging of the portfolio of trading activities as at the reference date is expected to occur in two stages, the first immediately after the initiation of the wind-down during the period of systemic stress, with potentially further hedging later in the wind-down period when normal market liquidity returns. The section aims to capture the extent of hedging, along with the expected bid-offer costs. Where intra-group hedges replacement can be allocated at the exit segment level, then these costs can be captured in the same line as the rest of the costs for that exit strategy (typically a package and sell line). However, if intra-group hedge replacement is taking place at a portfolio level across a range of exit segments, then the replacement cost may still be shown as a separate exit segment line using the “intra-group trade tear-up” exit strategy.

All hedging costs amounts should be the excess of projected cost in the scenario over that already recognised in fair value (i.e. net of release of fair value adjustments).

#### **Field Definitions**

##### **Systemic Stress Hedging**

37: Initial Open Risk Hedged: This field describes the level of hedging undertaken during the systemic stress. A narrative description should be selected from the list below:

- None;
- High-level macro hedging;
- Detailed first order risk hedging;
- Significantly hedged but with material open risks;

- Fully hedged except for residual inter-time bucket risk; and
- Fully hedged.

Trader judgement should be used when completing this field.

38: Systemic Stress Hedging Phase Length (Days): The period over which the stress-period hedging process is expected to take place (e.g. days 0-10) with 0 representing the start of the wind-down period (i.e. the reference date). The period should take into account the size of the positions to be hedged, given the level of market liquidity associated with the systemic stress.

39: Hedging Costs: The expected hedging costs in reporting currency incurred during the systemic stress. This is bid-offer cost only and does not need to capture potential market price movements during the hedging window.

### **Hedging in Normal Market Conditions**

40: Open Risk Hedged following resumption of normal market conditions: This field describes the level of hedging undertaken following resumption of normal market conditions. If no material further hedging is anticipated once normal market conditions resume, then this field should match field 37. As for 37, a narrative description should be selected from the list below to characterise the overall level of hedging achieved:

- None;
- High level macro hedging;
- Detailed first order risk hedging;
- Significantly hedged but with material open risks;
- Fully hedged except for residual inter-time bucket risk; and
- Fully hedged.

Trader judgement should be used when completing this field.

41: Unstressed Phase Hedging Period (Days): The period over which the hedging process in field 40 is expected to take place (e.g. days 200-210) with 0 representing the start of the wind-down period. The period should take into account the size of the positions to be hedged given the level of market liquidity associated with normal market conditions.

42: Unhedged Risks after Hedging: Free format text field to list the types of risk that will remain unhedged up to the point of final exit (e.g. FX-LIBOR correlation, single stock – index basis). This will provide additional understanding of portfolios that are to be packaged and sold with material risks so should tie in with the choice of exit strategy.

43: Hedging Costs: The expected hedging costs incurred following resumption of normal market conditions. This is bid-offer cost only and does not need to capture potential market price movements during the hedging window.

### **Tear Up & Replacement of Intra-Group Hedges**

44: Intra-Group Hedged Risk Replaced: This field describes how much of intra-group hedged risk is replaced by 3<sup>rd</sup> party hedges prior to exit of the associated portfolio. The appropriate narrative description should be selected from the list below. If the original intra-group hedges were simple vanilla trades that can be replaced on a like for like basis, this will be “fully

hedged” but if, for example, they were exotic back-to-back trades that can only be replaced with first order hedges then this would be “detailed first order risk hedging”.

- None;
- High level macro hedging;
- Detailed first order risk hedging;
- Significantly hedged but with material open risks;
- Fully hedged except for residual inter-time bucket risk; and
- Fully hedged.

Trader judgement should be used and the approach should be documented

45: Close-Out Window Intra-Group Hedge Replacement (Days): The period over which the initial hedging process is expected to take place (e.g. days 0-10) with 0 representing the start of the wind-down period. The period should take into account the size of the positions to be hedged, given the level of market liquidity associated with normal market conditions.

46: Unhedged Risks Resulting from Hedge Replacement: Free format text field to list the types of risk that will remain unhedged up to the point of final exit (e.g. FX-LIBOR correlation, single stock – index basis). This will provide additional understanding of portfolios that are to be packaged and sold with material risks and so should tie in with the choice of exit strategy.

47: Hedging Costs: The expected cost of tearing up intra-group hedges (where no contractual right to tear up at mid) plus the cost of replacing the resultant risk costs in. This is bid-offer cost only and does not need to capture potential market price movements during the hedging window.

### **Portfolio Rebalancing**

48. Portfolio Rebalancing Bid Offer Costs (if available): An estimate of the bid offer spread costs that will be incurred, as a result of re-hedging due to position exits (contractual and non-contractual) over the wind-down period.

C2: Net Hedging Costs (This is a calculated field and should not be submitted): Calculated numeric field equalling the total hedging costs.

## **5. Exit Costs - Exit Discount**

This section breaks down of the exit cost discount vs. fair value by the main commonly cited drivers of the book-to-exit value gaps. Where a discount to book value is anticipated, it should be allocated between the listed drivers, but it is not expected that all drivers will apply to every exit segment. A single exit segment may require a combination of factors to explain the total book-to-exit value gap e.g. an additional bid-offer cost beyond fair value to neutralise outside market risks plus a required return on capital (KVA)-style discount to reflect the likely discount on auction of the resultant risk-neutral portfolio. In some cases two or more of the listed drivers may be covered by a single calculation methodology and the allocation of the calculated number may not be readily apparent. TWD firms should nevertheless use judgement to disaggregate the cost between those drivers.

All exit discounts should be the excess of projected cost in the scenario over that already recognised in the fair value (i.e. net of release of fair value adjustments).

## Field Definitions

49: Return on Capital Discounts (KVA): Charges that would be levied to reflect the required return on capital of the replacement risk-provider over the remaining life of the position or portfolio.

50: Operational Cost Discounts: Discounts reflecting the marginal operational costs that counterparties would incur. Including due diligence over portfolio composition, initial booking and modelling costs, and ongoing administration and risk management of trades taken on.

51: Bid-Offer Charges on Disposal Packages: Cost of new trades done to remove risk on disposal packages or spread charged on risky disposal packages.

52: Loss of Market Maker Exemption: Additional bid-offer FVA arising from TWD firm's loss of market maker status in the scenario – affecting ability to close-out without incurring bid-offer spreads.

53: Concentration and Market Capacity: Size discounts for large positions within disposal packages. Additional charges anticipated due to the constraints on TWD firm's ability to construct novation packages that are within the risk appetite or operational capacity of potential step-in counterparty in a timely manner. Examples might include illiquid one-way market in which market peers are already at capacity in terms of ability to absorb more risk.

54: Incentivisation of Existing Counterparties: Compensation required to incentivise exiting counterparties to be novated to another counterparty.

55: Loss of beneficial pricing components: Components of fair value that are positive from the TWD firm's point of view but not expected to be recoverable in a negotiation of an unwind price. Examples include the value of CSA terms that are favourable to the TWD firm relative to standard terms.

56: Discount for Franchise Value: Franchise value expected to be factored into the pricing for portfolio novations.

57: Other Exit Discounts: Discounts attributed to other drivers.

58: Net Cash and Securities Flows on Trade Exit: The net cash and securities flow from trade exit or final maturity. This should reconcile to the Trade Exit Flows in the Liquidity Template (Template E in Appendix E) (should not include cash flows from derivative hedges, or pre-maturity contractual flows).

## **Total Exit Costs**

C3: Total TWD firm Costs including Hedging (This is a calculated field that should not be submitted): Calculated numeric field in reporting currency that sums the net hedging costs with the discount from each of the different exit discount drivers.

## **6. Timing of Exit Costs and Liquidity Flows**

This section captures the timing of P&L impacts and cash and securities flows associated with the disposal of the each segment.

## **Field Definitions**

Odd number columns 59 to 105: Month x Exit Cost: Exit cost impact associated with exit segment in each time bucket (disaggregation of field C3 above).

Even number columns 60 to 106: month x Cash and Securities Flows on Exit: cash and securities flow associated with trade exit in each time bucket (disaggregation of field 58 above).