

3 Collateral

3.1 Agreements concerning collateral

3.1.1 Deed of pledge

3.1.2 Pledge agreement concerning credit claims

3.2 Rules on collateral management

3.2.1 Eligible assets

3.2.1.1 Requirement for adequate collateral

3.2.1.2 Eligibility criteria for marketable assets

3.2.1.3 Eligibility criteria for non-marketable assets

3.2.1.4 Additional requirements for the use of collateral

3.2.1.5 Requirement on high credit standards for eligible assets

3.2.1.6 Establishment of high credit standards for marketable assets

3.2.1.7 Establishment of high credit standards for non-marketable assets

3.2.1.8 Marketable assets without a public credit assessment

3.2.1.9 Acceptance criteria for credit assessment systems

3.2.1.10 Performance monitoring of credit assessment systems

3.2.2 Collateral management

3.2.2.1 Collateral held in the pooling system

3.2.2.2 Domestic marketable assets

3.2.2.3 Foreign marketable assets

3.2.2.4 Domestic non-marketable assets

3.2.2.5 Foreign non-marketable assets

3.2.2.6 Margin calls (based on valuation) in a pooling system

3.2.2.7 Exceptional procedures for foreign assets

3.2.2.8 Collateral management fees

3.2.3 Collateral related risk control and sanctions

3.2.3.1 Introduction

3.2.3.2 Risk control measures for marketable assets

3.2.3.3 Risk control measures for non-marketable assets

3.2.3.4 Pricing and valuation principles for collateral

3.2.3.5 Sanctions

3.2.4 Acceptance of non-euro-denominated collateral in contingencies

Annex 1. Websites of euro area central banks

Annex 2. External credit risk assessment institutions used by the Eurosystem

Annex 3. Collateral Management opening hours and deadlines

Annex 4. Collateral management messages – marketable assets

**Notification of a change in the amount of collateral held in an Euroclear
Finland Ltd account/the overdraft limit**

Notification of the use of foreign assets

Annex 5 Notification of pledge concerning credit claims

**Annex 6. Bank of Finland's Terms and Conditions: Use of non-marketable assets
via correspondent central banking model**

**Annex 7. Example: Calculation of a collateral requirement and valuation of
collateral asset**

Annex 8. Collateral Management contact persons



3.1.1 Deed of pledge

Pledger: XX Bank

Pledge:

1. Book-entry account No yyy in the sub-register of XX Bank [NN Bank] and any book-entry securities in this account or monetary amounts accumulated on such book-entry securities. Any monetary amounts replacing the capital of the pledged book-entries upon maturity or sale shall be kept separate on behalf of the pledger in the payment transfer account of the Finnish Central Securities Depository Ltd. with the Bank of Finland.
2. Book-entry account ååå of XX Bank to be used in the event of a realization and kept in the sub-register of the Bank of Finland and any book-entry securities in this account or monetary amounts accumulated upon their maturity.
3. Securities deposited on behalf of the pledger in central securities depositories abroad.

Amount of debt:

The amount of the debt shall be the sum of the amounts in items 1, 2 and 3 below:

1. The intraday credit given to XX Bank in TARGET2- Suomen Pankki.
2. Any possible debit balance in the PM account at the end of a business day, specified as a liquidity credit in accordance with the terms stated by the Bank of Finland and/or any liquidity credit granted in order to fulfil the minimum reserve requirement in accordance with the terms stated by the Bank of Finland.
3. Any monetary amounts deriving from monetary policy operations executed as collateralized loans or from margin requirements in repurchase agreements.

Pledgee: The Bank of Finland

Terms of the pledge:

The pledge shall be registered in the book-entry account, No yyy, which is a collateral management account, the information in respect of which includes the collateral requirement for the account and the eligibility terms for the acceptance of book-entry securities as collateral. The Bank of Finland shall determine the calculation rule for the value of the collateral. Any value of book-entry securities in excess of the collateral requirement may be transferred from the account without separate consent of the pledgee. XX Bank shall be liable for its registrations in the pledged account in accordance with the agreement made between it and the Finnish Central Securities Depository Ltd. and the law governing book-entry securities.

The Bank of Finland shall not have the right to repledge a pledge deposited as collateral.

Pledged collateral located abroad shall be governed by the provisions on the establishment of a binding pledge in the concerned foreign law.

Rights pertaining to the account:

The Bank of Finland shall have debiting and restricted viewing rights to the book-entry securities in the pledged account and to any monetary amounts replacing them.

The Bank of Finland shall have the right to change the collateral requirement concerning the account, the collateral eligibility terms and the calculation rule for the collateral value.

The Finnish Central Securities Depository Ltd. shall have viewing and technical debiting rights pertaining to the activation of the account.

Costs:

XX Bank shall be liable for all expenses deriving from the pledged accounts.

Realization of a pledge:

If XX Bank in any respect fails to fulfil the obligation for which the collateral has been pledged, the Bank of Finland shall have the right; without hearing the pledger, without applying for a judgment or a decision, without complying with the formalities prescribed in the law, and without announcing the sale of the pledge; to convert the pledge into a monetary amount in such manner as to protect the interests of the parties.

On the basis of its debiting right, the Bank of Finland shall have the right to have book-entry securities registered in the account transferred to its possession for the purpose of realization. The book-entry securities shall be registered in book-entry account ååå opened in the name of XX Bank and pledged to the Bank of Finland.

On the basis of the pledge, the Bank of Finland shall have the right to have the monetary amounts deposited in place of pledged book-entry securities transferred to itself.

Pledged securities located in a foreign country shall be realized in the manner applicable in the concerned country.

The Bank of Finland shall have the right to use monetary amounts obtained from realization to fulfil outstanding obligations. If the yield from the conversion of a pledge into a monetary amount exceeds the liabilities of XX Bank in accordance with this obligation, the Bank of Finland shall repay the surplus to XX Bank.

If there is more than one pledge, the Bank of Finland shall have the right to decide the order in which the pledges shall be converted into monetary amounts and their application in fulfilling the obligations.

The Bank of Finland shall without undue delay and if possible prior to converting the pledged assets into cash inform XX Bank in writing to the address provided by the pledger.

Force majeure:

The Counterparties shall not be liable for damages incurred by actions taken by another domestic or foreign authority, by war or threat of war, or by civil disturbance; or by a disturbance that is not attributable to the Counterparty and that essentially disrupts its operations in respect of automatic data processing, information transmission, postal services and telecommunications, or the supply of electricity; or by interruptions or delays in its operations or actions due to a fire or other similar catastrophe; or by an industrial action that essentially affects the Counterparty's operations, whether applying to all or only some of the employees of the Counterparty; or by unreasonable difficulties in the operations of the Counterparty due to some other comparable incident of force majeure or similar cause.

Commitment:

XX Bank shall pledge the above-mentioned collateral to the Bank of Finland as collateral for credit granted by the Bank of Finland as determined above, the initial margin, the valua-



tion margin, the interest calculated thereon and any collection costs.

The pledger undertakes to ensure that the collateral requirement corresponding to the amount of the debt is fulfilled at all times. The pledger undertakes to retain the rights pertaining to the account with the Bank of Finland and to comply with the rules for collateral valuation determined by the Bank of Finland.

The Bank of Finland agrees that any value of book-entry securities in excess of the collateral requirement may be transferred from the account without the separate consent of the pledgee.

Governing law:

This agreement shall be governed by Finnish law.

Pledging of securities located abroad shall be governed by the provisions on establishment of a right of pledge and realization of pledged securities of the concerned foreign law.

The Agreement has been concluded in two identical copies, one for each party. A copy of the Agreement shall be submitted to the Finnish Central Securities Depository Ltd.

Date

3.1.2 Pledge agreement concerning credit claims

1 Pledger

XX Bank

2 Pledge

Non-marketable credit claims granted by the pledger which meet the eligibility and other legal requirements defined in the Bank of Finland's collateral management rules and on which the pledger has submitted the required information to the Bank of Finland, using the form 'notification of pledge concerning credit claims' or the specified electronic format. The pledged credit claims, including their terms and conditions, shall be governed by Finnish law.

3 Amount of debt

1. The intraday credit given to XX Bank in TARGET2- Suomen Pankki.
2. Any possible debit balance in the PM account at the end of a business day, specified as marginal lending in accordance with the Bank of Finland monetary policy rules and/or any marginal lending granted in order to fulfil the minimum reserve requirement.
3. Any monetary amounts relating to monetary policy operations executed as collateralised loans or margin requirements in repurchase agreements.

4 Pledgee

Bank of Finland

5 Commitment

XX Bank shall pledge the above-mentioned collateral to the Bank of Finland as security for credit granted by the Bank of Finland as determined above, the interest calculated on the credit and any collection charges. *(Amendment 1 January 2011)*

6 Terms of the pledge

The pledger shall make a separate endorsement on negotiable promissory notes subject to section 11 of the Act on Promissory Notes (622/47) and deliver a copy of such an endorsement to the Bank of Finland. The pledger shall preserve the credit claims pledged by it in accordance with section 22.2 of the Act on Promissory Notes. *(Amendment 1 January 2011)*

The pledger shall provide the debtor with an ex ante notification of using ordinary promissory notes subject to section 26 of the Act on Promissory Notes for collateral purposes. The pledger undertakes to submit the notification in compliance with procedures agreed with the debtor and to send a copy to the Bank of Finland.

The pledger undertakes to comply with the operative procedures for use of credit claims as collateral, as defined in the Bank of Finland's collateral management rules. If the relationship between pledger and debtor changes so as to affect the eligibility of the pledged assets, the pledger shall notify the Bank of Finland immediately; in no case later than the following banking day. Such changes are, for instance, early, partial or full repayment of a credit claim, changes in the debtor's credit standards or material changes in credit claim conditions.

The pledger shall continue to receive from the debtor payments of interest and principal on the pledged credit claim, unless otherwise specifically notified by the Bank of Finland.

7 Administration of the pledge

The pledger undertakes to preserve, with due diligence and due care, any promissory notes pledged to the benefit of the Bank of Finland, including attached collateral and other documentation. (*Amendment 1 January 2011*)

8 The Bank of Finland's right to take verification measures and disclose information to the Eurosystem

In order to verify the existence of credit claims pledged to the Bank of Finland and the accuracy of their details, the Bank of Finland shall have the right to undertake verifications on the pledger's premises, or commission a financial supervision authority or external auditor to carry out such verifications. If the pledger employs an Internal Ratings Based (IRB) approach for credit risk – in addition to assessing credit claims – to ascertain the eligibility of negotiable debt instruments that are not publicly rated, the right of verification shall also apply to information on the issuers of such debt instruments.

The Bank of Finland shall have the right to disclose information on pledged credit claims to Eurosystem central banks. If the pledger assesses its credit claims and/or some of its negotiable debt instruments for collateral purposes employing an IRB approach for credit risk, the Bank of Finland shall have the right to disclose information on the approach and resulting assessments to Eurosystem central banks.

The Bank of Finland shall have the right to disclose information on an IRB approach for credit risk to be used/used for assessing credit claims, and on the accuracy of assessments generated by such an approach, to the financial supervision authority of the EU country which has given permission to employ the approach for capital adequacy calculations.

The pledger undertakes to ensure that, under any circumstances, the Bank of Finland shall have the right to disclose any information referred to in this section.

9 Realisation of a pledge

If XX Bank in any respect fails to fulfil the obligation for which the collateral has been pledged, the Bank of Finland shall have the right, without hearing the pledger, to convert the pledge into a monetary amount in such manner as to protect the interests of the parties involved.

XX Bank undertakes to provide the Bank of Finland with all documents needed for realisation of the pledge.

10 Force majeure

A party to this agreement shall not be liable for damages incurred by unreasonable difficulties in the operations of the party due to an incident of force majeure or similar cause. A party to this agreement shall be obligated to notify the other party of an incident of force majeure as soon as possible.

11 Place of jurisdiction and governing law

Any disputes arising from this pledge shall be settled at the Helsinki district court. This agreement shall be governed by Finnish law.

Date

Bank of Finland

XX Bank

3.2 Bank of Finland rules on collateral management

3.2.1 Eligible assets

3.2.1.1 Requirement for adequate collateral

The Statute of the ESCB requires all Eurosystem credit operations to be based on adequate collateral. Consequently, all Bank of Finland liquidity-providing open market operations¹, marginal lending and intraday credits are based on underlying assets provided by the counterparties. Acceptable collateral consists of marketable and non-marketable assets as defined by the Eurosystem.

The Eurosystem has developed a single framework for eligible assets common to all Eurosystem credit operations. On 1 January 2007, this single framework (also referred to as the 'Single List') replaced the two-tier system that had been in place since the start of stage three of economic and monetary union.

The single framework comprises two distinct asset classes – marketable assets and non-marketable assets. The eligibility criteria for the two asset classes are uniform across the euro area² and are set out in Sections 3.2.1.2–3.2.1.4. To ensure that the two asset classes comply with the same credit standards, a Eurosystem credit assessment framework (ECAAF) has been set up, which relies on different credit assessment sources (see Sections 3.2.1.5–3.2.1.10).

The procedures and rules applicable to the use of collateral by banks based in Finland are outlined in Section 3.2.2. Instructions are given on the use as collateral of assets located in Finland and abroad.

The risk control measures and sanctions on collateral and counterparties agreed jointly in the Eurosystem and applied by the Bank of Finland are set out in Section 3.2.3.

The European Central Bank (ECB) daily posts on its website a list of eligible marketable assets. See at https://mfi-assets.ecb.int/query_EA.htm or https://mfi-assets.ecb.int/dla_EA.htm.

Non-marketable assets and marketable assets without rating by a public credit assessment institution listed on the ECB website are accepted as collateral on a case-by-case basis for each counterparty bank (see Sections 3.2.1.3 and 3.2.1.8). Information is not published on such assets.

The Bank of Finland shall only provide counterparties with advice regarding eligibility as collateral if already issued marketable assets or outstanding non-marketable assets are submitted to the Bank of Finland as collateral. There shall thus be no pre-issuance advice.

Because the Eurosystem has harmonised the eligibility criteria and risk management procedures for collateral, the rules on collateral management conform in this respect to the contents of the Guideline of the European Central Bank on monetary policy instruments and procedures of the Eurosystem.³ (*Amendment 10 October 2010*)

¹ The central bank can increase liquidity by purchasing certain assets if such operations are executed only for
² During the interim period until 2013 for a specific asset class of the non-marketable assets, credit claims, a limited number of eligibility and operational criteria may diverge across the euro area. (*Amendment 1 January 2012*)

³ Guideline of the European Central Bank of 31 August 2000 on monetary policy instruments and procedures of the Eurosystem (OJ L 310 of 11 December 2000, p. 1), as amended. The publication can be accessed on the ECB's website under Legal framework (<http://www.ecb.int/ecb/legal/1002/1014/html/index.en.html>) (*Amendment 10 October 2010*).

3.2.1.2 Eligibility criteria for marketable assets

The Bank of Finland accepts as collateral in its credit operations marketable debt instruments that fulfil the eligibility criteria laid down in this section.

Debt certificates issued by the ECB and all debt certificates issued by national central banks of the Eurosystem prior to euro adoption in the respective member states are eligible.

To determine the eligibility of other marketable assets, the following eligibility criteria are applied:

Type of asset

It must be a *debt instrument* having:

- (a) a fixed, unconditional principal amount;⁴ and
- (b) a coupon that cannot result in a negative cash flow. In addition, the coupon should be one of the following: (i) a zero coupon; (ii) a fixed rate coupon; or (iii) a floating rate coupon linked to an interest rate reference. The coupon may be linked to a change in the assessment of the issuer itself. Furthermore, inflation-indexed bonds are also eligible.

These features must be maintained until the redemption of the obligation. Debt instruments may not afford rights to the principal and/or the interest that are subordinated to the rights of holders of other debt instruments of the same issuer.

Requirement (a) does not apply to *asset-backed securities*, with the exception of bonds issued by credit institutions in accordance with the criteria set out in Article 22 (4) of the UCITS Directive⁵ (referred to as 'covered bank bonds'). The Eurosystem assesses the eligibility of asset-backed securities other than covered bank bonds against the following criteria:

The cash flow-generating assets backing the asset-backed securities must fulfil the following requirements:

- (a) the acquisition of such assets must be governed by the law of an EU Member State;
- (b) they must be acquired from the lender, ie the originator or from an intermediary by the securitisation special-purpose vehicle in a manner which the Eurosystem considers to be a 'true sale' that is enforceable against any third party, and be beyond the reach of the originator and its creditors, or the intermediary and its creditors, including in the event of the originator's or the intermediary's insolvency; (*Amendment 10 October 2010*)
- (c) they must be originated and sold to the issuer by an originator or, if applicable, an intermediary incorporated in the EEA;
- (d) they must not consist, in whole or in part, actually or potentially, of tranches of other asset-backed securities⁶. In addition, they must not consist, in whole or in part, actually or potentially, of credit-linked notes, swaps or other derivatives instruments,⁷ or synthetic securities;⁸ (*Amendment 10 October 2010*) and

⁴ Bonds with warrants or other similar rights attached are not eligible

⁵ Council Directive 85/611/EEC of 20 December 1985 on the coordination of laws, regulations and administrative provisions relating to undertakings for collective investment in transferable securities (UCITS) (OJ L 375 of 31 December 1985, page 3), as last amended by Directive 2005/1/EC (OJ L 79 of 24 March 2005, page 9).

⁶ This requirement does not exclude asset-backed securities where the issuance structure includes two special purpose vehicles and the 'true sale' requirement is met in respect of those special-purpose vehicles so that the debt instruments issued by the second special-purpose vehicle are directly or indirectly backed by the original pool of assets and all cash flows from the cash flow generating assets are transferred from the first to the second special-purpose vehicle.

⁷ This restriction does not encompass swaps used in asset-backed securities transactions strictly for hedging purposes.

⁸ Asset-backed securities which are on the list of eligible marketable assets as of 10 October 2010 are exempted from this requirement and remain eligible until 9 October 2011.

(e) if they are credit claims, the obligors and the creditors must be incorporated (or, if natural persons, resident) in the EEA and, if relevant, the related security must be located in the EEA. The law governing those credit claims must be the law of an EEA country. If they are bonds, the issuers must be incorporated in the EEA, they must be issued in an EEA country under the law of an EEA country and any related security must be located in the EEA.⁹ *(Amendment 10 October 2010)*

In cases where originators or, if applicable, intermediaries were incorporated in the euro area, or in the United Kingdom, the Eurosystem has verified that there were no severe claw back provisions in those jurisdictions. If the originator or, if applicable, the intermediary, is incorporated in another EEA country, the asset-backed securities can only be considered eligible if the Eurosystem ascertains that its rights would be protected in an appropriate manner against claw back provisions considered relevant by the Eurosystem under the law of the relevant EEA country. For this purpose, an independent legal assessment in a form acceptable to the Eurosystem must be submitted setting out the applicable claw back rules in the country, before the asset-backed securities can be considered eligible.⁹ To decide whether its rights are adequately protected against claw back rules, the Eurosystem may require other documents, including a solvency certificate from the transferee, for the suspect period. Claw back rules which the Eurosystem considers to be severe and therefore not acceptable include rules whereby the sale of underlying assets can be invalidated by the liquidator solely on the basis that it was concluded within a certain period (suspect period) before the declaration of insolvency of the seller (originator/intermediary), or where such invalidation can only be prevented by the transferee if they can prove that they were not aware of the insolvency of the seller (originator/intermediary) at the time of the sale. *(Amendment 10 October 2010)*

Within a structured issue, in order to be eligible, a tranche (or sub-tranche) may not be subordinated to other tranches of the same issue. A tranche (or sub-tranche) is considered to be non-subordinated vis-à-vis other tranches (or sub-tranches) of the same issue if, in accordance with the priority of payment applicable after the delivery of an enforcement notice, as set out in the prospectus, no other tranche (or sub-tranche) is given priority over that tranche or sub-tranche in respect of receiving payment (principal and interest), and thereby such tranche (or sub-tranche) is last in incurring losses among the different tranches or sub-tranches of a structured issue. For structured issues where the prospectus provides for the delivery of an acceleration and an enforcement notice, non-subordination of a tranche (or sub-tranche) must be ensured under both acceleration and enforcement notice-related priority of payments. *(Amendment 10 October 2010)*

The Bank of Finland reserves the right to request from any relevant third party (such as the issuer, the originator or the manager) any clarification and/or legal confirmation that it considers necessary to assess the eligibility of asset-backed securities.

Credit standards

The debt instrument must meet the high credit standards specified in the ECAF rules for marketable assets, as set out in Section 3.2.1.6.

Place of issue

The debt instrument must be deposited/ registered (issued) in the EEA with a central bank or with a central securities depository (CSD) which fulfils the minimum standards established by the ECB.¹⁰ In case a marketable debt instrument is issued by a non-financial cor-

⁹ Asset-backed securities which are on the list of eligible marketable assets as of 10 October 2010 are exempted from this requirement and remain eligible until 9 October 2011.

¹⁰ International debt securities in global bearer form issued on or after 1 January 2007, through the ICSDs Euroclear Bank (Belgium) and Clearstream Banking Luxembourg must, in order to be eligible, be issued in the form of new global notes and must be deposited with a common safekeeper which is an ICSD or, if applicable, a CSD that fulfils the minimum standards established by the ECB. International debt securities in global bearer form that were issued in the form of classical global notes prior to 1 January 2007 and fungible securities issued under the same ISIN code on or after that date remain eligible until maturity. International debt securities issued in global registered form through the ICSDs Euroclear Bank (Belgium) and Clearstream Banking Luxembourg after 30 September 2010 must, in order to be eligible, be issued under the new safekeeping structure for international debt securities. International debt securities in global registered form issued before or on that date remain eligible until their maturity. International debt securities in individual note form will cease to be eli-

poration¹¹ that is not assessed by an accepted external credit assessment institution (ECAI), the place of issue must be the euro area.

Settlement procedures

The debt instrument must be transferable in book-entry form. It must be held and settled in the euro area through an account with the Eurosystem or with an SSS that fulfils the standards established by the ECB, so that perfection and realisation are subject to the law of an EU Member State.

If the CSD where the asset is issued and the SSS where it is held are not identical, then the two institutions have to be connected by a link approved by the ECB.¹²

Acceptable markets

The debt instrument must be admitted to trading on a regulated market as defined in the Directive 2004/39/EC of the European Parliament and of the Council of 21 April 2004 on markets in financial instruments,¹³ or traded on certain non-regulated markets as specified by the ECB.¹⁴

The assessment of non-regulated markets by the Eurosystem is based on three principles – safety, transparency and accessibility. 'Safety', 'transparency' and 'accessibility' are defined by the Eurosystem exclusively in terms of the performance of the Eurosystem's collateral management function. The selection process is not aimed at assessing the intrinsic quality of the various markets. The principles are to be understood as follows. *Safety* is taken to mean certainty with regard to transactions, in particular certainty on the validity and enforceability of transactions. *Transparency* is taken to mean unimpeded access to information on the market's rules of procedure and operation, the financial features of the assets, the price formation mechanism, and the relevant prices and quantities (quotes, interest rates, trading volumes, outstanding amounts, etc.). *Accessibility* refers to the Eurosystem's ability to take part in and have access to the market; a market is accessible for collateral management purposes if its rules of procedure and operation allow the Eurosystem to obtain information and conduct transactions when needed for these purposes.¹⁵

Type of issuer/guarantor

The debt instrument may be issued or guaranteed by central banks of the EU Member States, public sector entities, private sector entities, or international or supranational institutions. Moreover, an issuer of eligible debt instruments lacking ECAI rating and accepted as bank-specific collateral cannot be from the financial and insurance sector. (*Amendment 1 January 2012*)

gible if issued after 30 September 2010. International debt securities in individual note form issued before or on that date remain eligible until their maturity. (*Amendment 10 October 2010*)

¹¹ Non-financial corporations are defined as in the European System of Accounts 1995 (ESA 95), see Statistics Finland's Classification of Sectors 2000 on http://www.stat.fi/meta/luokitukset/sectoriluokitus/001-2000/index_en.html

¹² The description of the standards for the use of eligible SSSs in the euro area and an updated list of the eligible links between these systems can be found on the ECB's website (www.ecb.europa.eu).

¹³ OJ L 145 of 30 April 2004, page 1.

¹⁴ A list of acceptable non-regulated markets is published on the ECB's website (www.ecb.europa.eu) and updated at least once a year.

¹⁵ Marketable assets, which were accepted as tier two assets, have been issued prior to 31 May 2007 and are traded on non-regulated markets that currently fulfil the Eurosystem's requirements for safety and accessibility, but not for transparency, remain eligible until 31 December 2010, provided they fulfil the other eligibility criteria, and become ineligible after that date. This does not apply to uncovered marketable assets issued by credit institutions that were accepted as tier two assets and became ineligible on 31 May 2007.

Place of establishment of the issuer/guarantor

The issuer must be established in the EEA or in one of the non-EEA G10 countries.¹⁶ In the latter case, the debt instruments can only be considered eligible if the Eurosystem ascertains that its rights would be protected in an appropriate manner, as determined by the Eurosystem, under the laws of the respective non-EEA G10 country. For this purpose, a legal assessment in a form and with substance acceptable to the Eurosystem will have to be submitted to the Bank of Finland before the assets can be considered eligible. In the case of an asset-backed security, the issuer must be established in the EEA.

The guarantor must be established in the EEA, unless a guarantee is not needed to establish the high credit standards for marketable assets, as set out in Section 3.2.1.6. (*Amendment 10 October 2010*)

International or supranational institutions are eligible issuers/guarantors irrespective of their place of establishment. In case a marketable debt instrument is issued by a non-financial corporation that is not assessed by an ECAI, the issuer/guarantor must be established in the euro area.

Currency of denomination

The debt instrument must be denominated in euro.¹⁷

3.2.1.3 Eligibility criteria for non-marketable assets

The Bank of Finland accepts as collateral in its credit operations such fixed-term deposits from eligible counterparties as defined in Section 1.2.3.5 of the Rules, non-marketable credit claims (bank loans)¹⁸ and non-marketable retail mortgage-backed debt instruments. Currently Irish non-marketable mortgage-backed promissory notes are the only instruments in this asset class. Non-marketable assets are accepted as collateral on a case-by-case basis for each counterparty bank. (*Amendment 1 January 2011*)

To be eligible, a credit claim has to fulfil the following *eligibility criteria*:

- *Type of asset*: It must be a credit claim which is a debt obligation of a debtor vis-à-vis a Eurosystem counterparty. Credit claims that have a 'reducing balance' (ie where the principal and interest are paid off according to a pre-agreed schedule) are also eligible. Undrawn credit lines (eg undrawn facilities of revolving credit claims), current account overdrafts and letters of credit (which authorise the use of credit but are not credit claims per se) are not eligible. The share of a syndicate member institution in a syndicated loan is considered an eligible type of credit claim. Credit claims may not afford rights to the principal and/or the interest that are subordinated to the rights of holders of other credit claims (or other tranches or sub-tranches in the same syndicated loan) or debt instruments of the same issuer.

The credit claim must have (a) a fixed, unconditional principal amount and (b) an interest rate that cannot result in a negative cash flow. In addition, the interest rate should be one of the following: 1) zero coupon-style; 2) fixed; or 3) floating linked to another interest rate reference. Furthermore, inflation-indexed bonds are also eligible. These features must be maintained until the redemption of the obligation.

- *Type of debtor/guarantor*: Eligible debtors and guarantors are non-financial corpora-

¹⁶ Non-EEA G10 countries currently include the United States, Canada, Japan and Switzerland. Marketable assets issued before 1 January 2007 by an entity not established in the EEA or in one of the non-EEA G10 countries, but guaranteed by an entity established in the EEA, remain eligible until 31 December 2011, provided they fulfil the other eligibility criteria and the requirements applicable to guarantees and become ineligible after that date.

¹⁷ Expressed as such or in the national denominations of the euro.

¹⁸ Between 2007 and 2013, an intermediate regime will be in place for credit claims, allowing each national central bank to choose the minimum threshold for the size of credit claims eligible for collateral purposes (apart from crossborder use) and whether a handling fee should be applied. In the course of 2013 a fully unified regime will be in place.

tions, 19 public sector entities and international or supranational institutions. Each debtor is individually and severally liable for the full repayment of the credit claim in question (co-debtors jointly liable for individual credit claims are excluded).

- *Place of establishment of the debtor and guarantor:* The debtor must be established in the euro area. The guarantor must also be established in the euro area, unless a guarantee is not needed to establish the high credit standards for non-marketable assets, as set out in section 3.2.1.7. This requirement does not apply to international or supranational institutions. (*Amendment 10 October 2010*)
- *Credit standards:* The quality of credit claims is assessed through the underlying creditworthiness of the debtor or guarantor. Credit claims must meet the high credit standards specified in the ECAF rules for non-marketable assets, as set out in Section 3.2.1.7.
- *Minimum size:* At the time of submission for use as collateral by the counterparty, the credit claim must meet a minimum size threshold. Each national central bank may apply a minimum size of its choice for domestic credit claims. The Bank of Finland has decided to apply a minimum of EUR 500,000, the amount agreed to apply as soon as practicable in the course of 2013 for the whole Eurosystem. For cross-border use, a common minimum threshold of EUR 500,000 is applicable in the interim period. The minimum threshold applies to the remaining amount of an individual credit claim at the moment it is accepted as collateral. (*Amendment 1 January 2012*)
- *Handling procedures:* The credit claim must be handled according to the procedures defined in Section 3.2.2.
- *Governing laws:* The credit claim agreement and the agreement between the counterparty and the Bank of Finland on using the credit claim as collateral must both be governed by the law of a member state belonging to the euro area, including Finland. Furthermore, the total number of different governing laws that are applicable to 1) the counterparty, 2) the creditor, 3) the debtor, 4) the guarantor (if relevant), 5) the credit claim agreement and 6) the agreement on using the credit claim as collateral may not exceed two.
- *Currency of denomination:* The credit claim must be denominated in euro.²⁰

Non-marketable retail mortgage-backed debt instruments (RMBD) cannot be implemented in Finland. They are subject to the following eligibility criteria:

- *Type of asset:* It must be a debt instrument (a promissory note or a bill of exchange) that is secured by collateralised residential real estate loans held by the issuer of the debt instrument and that falls short of full securitisation. Substitution of assets in the underlying pool must be possible and a mechanism needs to be in place to ensure that the Eurosystem enjoys priority over creditors other than those exempted for public policy reasons. (*Amendment 1 January 2011*)

The RMBD must have (a) a fixed, unconditional principal amount and (b) an interest rate that cannot result in a negative cash flow.

- *Credit standards:* The RMBD must meet high credit standards, which are assessed through the part of the ECAF that addresses RMBDs.
- *Type of issuer:* Eligible issuers are credit institutions that are eligible counterparties.
- *Place of establishment of the issuer:* The issuer must be located in the euro area.

¹⁹ As defined in the European System of Accounts 1995 (ESA 95), see Statistics Finland's Classification of Sectors 2000 on http://www.stat.fi/meta/luokitukset/sectoriluokitus/001-2000/index_en.html
²⁰ In euro or in its national sub-units.

- *Handling procedures:* The RMBD must be handled according to the Eurosystem procedures, particularly those of the Irish central bank. Further information can be obtained from the Irish central bank.
- *Currency of denomination:* The RMBD must be denominated in euro.²¹

3.2.1.4 Additional requirements for the use of collateral

Conditions for the use of marketable and non-marketable assets

Marketable assets can be used for all monetary policy operations ie reverse and outright open market transactions and the marginal lending facility. Non-marketable assets can be used as underlying assets for reverse transactions and the marginal lending facility, but not for outright transactions. All marketable and non-marketable assets can also be used as underlying assets for intraday credit.

Irrespective of the fact that a marketable or non-marketable asset fulfils all eligibility criteria, a counterparty may not submit as collateral any asset for which it, or any other entity with which it has close links, is the issuer, debtor or guarantor.²²

'Close links' means a situation in which the counterparty is linked to an issuer/debtor/guarantor of eligible assets by reason of the fact that:

- (i) the counterparty owns directly, or indirectly, through one or more other undertakings, 20% or more of the capital of the issuer/debtor/guarantor; or
- (ii) the issuer/debtor/guarantor owns directly, or indirectly through one or more other undertakings, 20% or more of the capital of the counterparty; or
- (iii) a third party owns more than 20% of the capital of the counterparty and more than 20% of the capital of the issuer/debtor/guarantor, either directly or indirectly, through one or more undertakings.

For monetary policy implementation purposes, in particular for the monitoring of compliance with the rules for the use of eligible assets concerning close links, the Eurosystem internally shares information on capital holdings provided by supervisory authorities for such purposes. The information is subject to the same secrecy standards as applied by supervisory authorities. (*Amendment 10 October 2010*)

The above provisions concerning close links do not apply to: (a) close links between the counterparty and an EEA public sector entity which has the right to levy taxes, or in the case where a debt instrument is guaranteed by an EEA public sector entity which has the right to levy taxes; (b) covered bank bonds issued in accordance with the criteria set out in Article 22(4) of the UCITS Directive; or (c) cases in which debt instruments are protected by specific legal safeguards comparable to those instruments given under (b) such as in the case of (i) non-marketable retail mortgage-backed debt instruments (RMBDs) which are not securities; or (ii) residential real estate loan-backed structured bank bonds covered by residential real estate loans or commercial mortgage loans, ie certain covered bonds not declared UCITS compliant by the European Commission that fulfil all the criteria that apply to asset-backed securities, as set out in Sections 3.2.1.5 and 3.2.1.6 and the following additional criteria: (*Amendment 1 February 2011*)

In the case of residential real estate loan-backed structured covered bank bonds, the close links provisions do not apply, provided that the following conditions are met²³ (*Amendment 1 February 2011*):

²¹ In euro or in its national sub-units.

²² In the event of a counterparty using assets that, owing to an identity with the issuer/debtor/guarantor or the existence of close links, it may not or no longer use to secure an outstanding credit, it is obliged to immediately notify the Bank of Finland thereof. The assets are valued at zero on the next valuation date and a margin call may be triggered. In addition, the counterparty has to remove the asset on the earliest possible date.

²³ Residential real estate loan-backed structured covered bank bonds submitted before 10 October 2010 that do not comply with these criteria can continue to be used until 31 March 2011. Commercial mortgage loan-backed structured covered bank bonds submitted before 1 February 2011 that do not comply with these criteria can continue to be used until 31 March 2011.

- Any residential real estate loans underlying the structured covered bank bonds must be denominated in euro; the issuer (and the debtor and guarantor, if they are legal persons), must be incorporated in a Member State, their underlying assets must be located in a Member State, and the law governing the loan must be that of a Member State. *(Amendment 1 February 2011)*
- Residential real estate loans are eligible for the cover pool of relevant structured covered bank bonds, if they are guaranteed by an eligible guarantee or secured by a mortgage. An eligible guarantee must be payable within 24 months upon default. Eligible guarantees for the purposes of such guaranteed loans can be provided in different contractual formats, including contracts of insurance, provided that they are granted by a public sector entity or a financial institution subject to public supervision. The guarantor for the purposes of such guaranteed loans must not have close links to the issuer of the covered bonds, and must be rated at least A+/A1/AH by an accepted ECAI over the life of the transaction. *(Amendment 1 February 2011)*
- High quality substitute collateral up to 10% of the cover pool is accepted. This threshold can only be exceeded after an in-depth review by the relevant NCB.
- The maximum portion of each individual eligible loan that can be funded through the structured covered bank bond issuance is 80% loan-to-value (LTV). The LTV calculation must be based on a conservative market valuation. *(Amendment 1 February 2011)*
- The minimum mandatory over-collateralisation is 8%.
- The maximum loan amount for a residential real estate loan is EUR 1 million.
- The stand-alone credit assessment of the cover pool must correspond to an annual PD level of 10 basis points in line with the 'single A' threshold (see Section 3.2.1.5.).
- A long-term minimum threshold of 'single A' ('A-' by Fitch or Standard & Poor's, or 'A3' by Moody's, or 'AL' by DBRS) must be applied to the issuer and related entities which are part of or relevant to the transaction relating to the structured covered bank bond. *(Amendment 1 February 2011)*

In the case of commercial mortgage loan-backed structured covered bank bonds, the provisions on close links do not apply, provided that the following conditions are met: *(Amendment 1 February 2011)*

- Any commercial mortgage loans underlying the structured covered bank bonds must be denominated in euro; the issuer (and the debtor and guarantor, if they are legal persons) must be incorporated in a Member State, their underlying assets must be located in a Member State, and the law governing the loan must be that of a Member State. *(Amendment 1 February 2011)*
- High quality substitute collateral up to 10% of the cover pool is accepted. This threshold can only be exceeded after an in-depth review by the relevant national central bank. *(Amendment 1 February 2011)*
- The maximum portion of each individual eligible loan that can be funded through the structured covered bank bond issuance is 60% LTV. The LTV calculation must be based on a conservative market valuation. *(Amendment 1 February 2011)*
- The minimum mandatory over-collateralisation is 10%. *(Amendment 1 February 2011)*
- The share of each borrower in the cover pool, after aggregating all individual loan amounts outstanding from a given borrower, must not exceed 5% of the cover pool's total. *(Amendment 1 February 2011)*
- The stand-alone credit assessment of the cover pool must correspond to credit

quality step 1 in line with the Eurosystem rating scale (see Section 3.2.1.5).

(Amendment 1 February 2011)

- Credit quality step 2 must be applied to the issuer and related entities which are part of or relevant to the transaction relating to the structured covered bank bond.
(Amendment 1 February 2011)
- All underlying commercial mortgage loans need to be revalued at least on an annual basis. Price decreases of properties must be fully reflected in the revaluation. In the case of price increases, a 15% haircut is applied. Loans that do not fulfil the LTV threshold requirement must be replaced by new loans, or must be over-collateralised, subject to the approval of the relevant national central bank. The primary valuation methodology to be applied is the market value, i.e. the estimated price that would be obtained if the assets were sold on the market using reasonable efforts. This estimation must be based on the most conservative assumption. Statistical methods can also be applied but only as a secondary valuation methodology. *(Amendment 1 February 2011)*
- Liquidity cushion in the form of cash in euro deposited with an eligible counterparty must be maintained at all times to cover all interest payments related to covered bank bonds for the subsequent six-month period. *(Amendment 1 February 2011)*
- Whenever the short-term credit rating of the borrower of an underlying commercial mortgage loan falls below credit quality step 2 in the 9 months before a hard bullet covered bank bond matures, such borrower must post an amount of cash in euro sufficient to cover the relevant part of the covered bank bond principal payment as well as related expenses scheduled to be paid by the issuer under the covered bank bond to the liquidity cushion. *(Amendment 1 February 2011)*
- In case of liquidity stress, the original maturity date can be extended up to 12 months to compensate for maturity mismatches between the amortising loans in the cover pool and the bullet redemption of the covered bank bond. However, the covered bank bond will become ineligible for own use after the original maturity date. *(Amendment 1 February 2011)*

Furthermore, in the case of bank bonds covered by residential real estate loans or commercial mortgage loans, counterparties have to provide legal confirmation from a reputable law firm confirming the fulfilment of the following conditions: *(Amendment 1 February 2011)*

- The issuer of the covered bank bonds is a credit institution incorporated in an EU Member State, and is not a special-purpose vehicle, even if such bonds are guaranteed by a credit institution incorporated in an EU Member State. *(Amendment 1 February 2011)*
- The issuer/issue of the covered bank bonds is subject, by the law of the Member State where the issuer is incorporated or where the bonds were issued, to special public supervision designed to protect bondholders. *(Amendment 1 February 2011)*
- In the event of the insolvency of the issuer of the covered bank bonds, bondholders have priority as regards reimbursement of the principal and payment of interest deriving from the (underlying) eligible assets. *(Amendment 1 February 2011)*
- Sums deriving from the issue of the covered bank bonds must be invested (according to the investment rules set out by the bond documentation) in conformity with the relevant national covered bond legislation or other legislation applicable to the assets in question. *(Amendment 1 February 2011)*

Moreover, a counterparty may not submit as collateral any asset-backed security if the counterparty (or any third party with which it has close links) provides a currency hedge to the asset-backed security by entering into a currency hedge transaction with the issuer as a hedge counterparty or provides liquidity support for 20% or more of the outstanding

amount of the asset-backed security.

All eligible marketable and non-marketable assets must be usable in a cross-border context throughout the euro area. This implies that all Eurosystem counterparties must be able to use eligible assets either through links with their domestic SSSs in the case of marketable assets or through other eligible arrangements to receive credit from the national central bank of the Member state in which the counterparty is established (see Section 3.2.2).

Additional legal requirements for credit claims

In order to ensure that a valid security is created over credit claims (bank loans) and that the credit claim can be swiftly realised in the event of a counterparty default, additional legal requirements have to be met. These legal requirements relate to:

- *Verification of the existence of credit claims:* As a minimum, the Bank of Finland shall use the following measures to verify the existence of credit claims submitted as collateral: 1) self-certification and commitment by the counterparty to the Bank of Finland, at least every quarter, with respect to the existence of the credit claims submitted as collateral, 2) one-off verification by the Bank of Finland, or a financial supervision authority on authority of the Bank of Finland, or by an external auditor of the counterparty's procedures for submitting information on the existence of credit claims to the Bank of Finland; and 3) random checks by the Bank of Finland, or a financial supervision authority on authority of the Bank of Finland, or by an external auditor of the quality and accuracy of the self-certification.

The quarterly self-certification and commitment under 1) above includes the requirement that Bank of Finland counterparties perform the following in writing:

- confirm and warrant compliance of credit claims pledged to the Bank of Finland with the eligibility criteria applied by the Eurosystem;
- confirm and warrant that no credit claim submitted as an underlying asset is being simultaneously used as collateral to the benefit of any third party and undertake that the counterparty shall not use any credit claim as collateral to any third party; and
- confirm and warrant to notify the Bank of Finland immediately, but no later than the next business day, of any event which materially affects the actual contractual relationship between the counterparty and the Bank of Finland, in particular early, partial or total repayments, downgrades or material changes in the conditions of the credit claim.

In order for such checks to take place as described in 2) and 3) above (one-off verifications and random checks), the Bank of Finland, a financial supervision authority or external auditors must be authorised to carry out such investigation in accordance with the applicable national requirements or, if necessary, under contract.

The Bank of Finland's operative procedures in respect of the implementation of 1), 2) and 3) above are described in Section 3.2.2.

- *Submission of a notice of transfer to the debtor or endorsement:* Finnish legislation prescribes that prior notification must be submitted to debtors and possible guarantors of the use of ordinary credit claims as collateral (notice of transfer) before they can be used for such purpose. Bank of Finland counterparties must submit a prior notification to debtors or possible guarantors of the use of ordinary credit claims as collateral to the Bank of Finland. Prior notification need not be made to debtors or possible guarantors of the use as collateral of negotiable credit claims, but credit documents must be validated with a separate endorsement. In the event of insolvency of the counterparty or its failure to fulfil the obligations for which the credit claim has been used as collateral, the Bank of Finland shall submit to the debtor and possible guarantor notices of transfer, which specify use of the credit claim as collateral for the behalf of the Bank of Finland and issues new payment instructions.

- *Absence of restrictions related to banking secrecy and confidentiality:* The counterparty shall not be obliged to obtain the debtor's approval for disclosure of information about the credit claim and the debtor that are required by the Bank of Finland for the purpose of ensuring that a valid security is created over credit claims and that the credit claims can be swiftly realised in the event of a counterparty default. If bank secrecy regulations prevent disclosure of information, the counterparty and the debtor shall agree contractually that the debtor unconditionally consents to the disclosure of such details about the credit claim and the debtor to the Eurosystem.
- *Absence of restrictions on the use of the credit claim:* Counterparties shall ensure that credit claims are fully transferable and can be used, without restriction, as collateral for the benefit of the Bank of Finland. There should not be any restrictive stipulation in the credit claim agreement or in other contractual arrangements between the counterparty and the debtor in respect of the use of the credit claim as collateral.
- *Absence of restrictions on the realisation of the credit claim:* The credit claim agreement or other contractual arrangements between the counterparty and the debtor should not contain any restrictions regarding the realisation of the credit claim used as collateral, including any form, time or other requirement with regard to realisation.

3.2.1.5 Requirement on high credit standards for eligible assets

The Eurosystem and the Bank of Finland as part of the Eurosystem require that high credit standards be applied for all eligible assets used as collateral. This means that credit assessment of a marketable credit instrument or its issuer or of a debtor of a credit claim must meet high credit standards. Other potential factors that may improve investors' security, such as guarantees, are also taken into account.

In the assessment of the credit standard of eligible assets, the Eurosystem takes into account credit assessment information from credit assessment systems belonging to one of the four following sources:

- external credit assessment institutions (ECAIs)
- counterparties' internal ratings based (IRB) systems
- third-party providers' rating tools (RTs)
- NCB's in-house credit assessment systems (ICASs, currently employed in the central banks of France, Germany, Austria and Spain).

With regard to the ECAI source, the assessment must be based on a public rating. (*Amendment 10 October 2010*)

The Eurosystem reserves the right to request any clarification that it considers necessary. (*Amendment 10 October 2010*)

For asset-backed securities, ratings must be explained in a publicly available credit rating report, namely a detailed pre-sale or new issue report, including, inter alia, a comprehensive analysis of structural and legal aspects, a detailed collateral pool assessment, an analysis of the transaction participants, as well as an analysis of any other relevant particularities of a transaction. Moreover ECAIs must publish regular surveillance reports for asset-backed securities. The publication of these reports should be in line with the frequency and timing of coupon payments. These reports should at least contain an update of the key transaction data (eg composition of the collateral pool, transaction participants, capital structure), as well as performance data. (*Amendment 10 October 2010*)

The Eurosystem's benchmark for establishing its minimum requirement for high credit standards (its 'credit quality threshold') is defined in terms of a credit assessment of credit quality step 3 in the Eurosystem's harmonised rating scale.²⁴ The Eurosystem considers a

²⁴ The Eurosystem harmonised rating scale is published on the ECB's website (www.ecb.europa.eu). A credit

PD over a one-year horizon of 0.40% as equivalent to a credit assessment of credit quality step 3, subject to regular review. The ECAF follows the definition of a default event given in the Capital Requirements Directive.²⁵ The Eurosystem publishes the lowest rating grade meeting the required credit quality threshold for each accepted ECAI, without assuming any responsibility for its assessment of the ECAI, again subject to regular review. With regard to asset-backed securities, the Eurosystem's benchmark for establishing its minimum requirements for high credit standards is defined in terms of a 'triple A' credit assessment²⁶ at issuance. Over the lifetime of the asset-backed security, the Eurosystem's minimum threshold of credit quality step 2 of the Eurosystem's harmonised rating scale ('single A')²⁷ must be retained. The Eurosystem considers a PD over a one-year horizon of 0.10% as equivalent to a credit assessment of credit quality step 2, subject to regular review.

(Amendment 1 January 2011)

The Eurosystem, including the Bank of Finland, reserves the right to determine whether an issue, issuer, debtor or guarantor fulfils their requirements for high credit standards on the basis of any information it may consider relevant. The Bank of Finland may reject, limit the use of assets or apply supplementary haircuts on such grounds if required to ensure adequate risk protection of the Eurosystem in line with Article 18.1 of the Statute of the ESCB. Such measures can also be applied to specific counterparties, in particular if the credit quality of the counterparty appears to exhibit a high correlation with the credit quality of the collateral assets submitted by the counterparty. In case such a rejection is based on prudential information, the use of any such information transmitted either by counterparties or by supervisors shall be strictly commensurate with, and necessary for, the performance of the Eurosystem's tasks of conducting monetary policy.

Assets issued or guaranteed by entities subject to a freezing of funds and/or other measures imposed by the EU under Article 75 of the Treaty on the Functioning of the European Union or by an EU Member State restricting the use of their funds, or in respect of which the ECB's Governing Council has issued a decision suspending or excluding their access to open market operations or the Eurosystem's standing facilities, may be excluded from the list of eligible assets. *(Amendment 10 October 2010)*

In the case of marketable credit instruments, fulfilment of the credit standards is primarily assessed on the basis of assessments made by the ECAI. Issues that fulfil the minimum credit standards (and other eligibility criteria) are published on the ECB website.

The credit assessment source for credit claims (bank loans) is selected by the counterparty ie the provider of the collateral. This selection is based on certain rules (more details in Section 3.2.1.7). If marketable credit instruments do not have an ECAI credit assessment, the credit assessment source can be selected on the basis of the same criteria as the source for credit claims (see Section 3.2.1.8).

quality step 3 credit assessment means a minimum long-term rating of 'BBB-' by Fitch or Standard & Poor's, of 'Baa3' by Moody's, or of 'BBB' by DBRS.

²⁵ The CRD comprises Directive 2006/48/EC of the European Parliament and of the Council of 14 June 2006 relating to the taking up and pursuit of the business of credit institutions (recast) (OJ L177 of 30 June 2006, p. 1) and Directive 2006/49/EC of the European Parliament and of the Council of 14 June 2006 on the capital adequacy of investment firms and credit institutions (recast) (OJ L177 of 30 June 2006, p. 201).

²⁶ 'Triple A' means a minimum long-term rating of 'AAA' by Fitch, Standard & Poor's or DBRS or 'Aaa' by Moody's or, if this is not available, a short-term rating of 'F1+' by Fitch, or 'A-1+' by Standard & Poor's, or 'R-1H' by DBRS.

²⁷ 'Single A' means a minimum long-term rating of 'A-' by Fitch or Standard & Poor's, or 'A3' by Moody's, or 'AL' by DBRS.

3.2.1.6 Establishment of high credit standards for marketable assets

Marketable assets are considered to fulfil high credit standards when the following conditions are met:

- *ECAI credit assessment:* At least one credit assessment from an accepted ECAI (as set out in Section 3.2.1.9) for the issue (or, in its absence, for the issuer) must comply with the Eurosystem's credit quality threshold.^{28, 29} The ECB publishes the credit quality threshold for any accepted ECAI.³⁰
- *ECAI credit assessment of asset-backed securities:* For asset-backed securities issued on or after 1 March 2010, the Eurosystem requires at least two credit assessments from any accepted ECAs for the issue. To determine the eligibility of these asset-backed securities, the 'second-best rule' shall be applied, which means that not only the best, but also the second-best available ECAI credit assessment must comply with the credit quality threshold for asset-backed securities. Based on this rule, the Eurosystem requires for both credit assessments an 'AAA'/Aaa' level at issuance and a 'single A' level over the life of the security in order for the securities to be eligible.

(Amendment 1 March 2010.)

From 1 March 2011 all asset-backed securities, regardless of their date of issuance, shall have at least two credit assessments from any accepted ECAs for the issue, and the second-best rule shall be met in order for the securities to remain eligible. *(Amendment 1 March 2010.)*

In case of asset-backed securities issued before 1 March 2010 that have only one credit assessment, a second credit assessment shall be additionally obtained before 1 March 2011. For asset-backed securities issued before 1 March 2009 both credit assessments must comply with the 'single A' level over the life of the security. For asset-backed securities issued between 1 March 2009 and 28 February 2010, the first credit assessment must comply with the 'AAA/Aaa' level at issuance and the 'single A' over the life of the security, while the second credit assessment must comply with the 'single A' level both at issuance³¹ and over the life of the security. *(Amendment 1 March 2010.)*

Fungible tap issuances of asset-backed securities are considered to be new issuances of asset-backed securities. All asset-backed securities issued under the same ISIN code must comply with the eligibility criteria in place at the date of the latest fungible tap issuance. For fungible tap issues of asset-backed securities which are not compliant with the eligibility criteria in place at the date of the latest fungible tap issuance, all the asset-backed securities issued under the same ISIN code are considered ineligible. This rule shall not apply in the case of fungible tap issuances of asset-backed securities which were on the Eurosystem list of eligible assets on 10 October 2010 if the latest tap issuance occurred before that date. Non-fungible tap issuances are considered to be different asset-backed securities. *(Amendment 10 October 2010)*

The ECB publishes the credit quality threshold for any accepted ECAs.³² *(Amendment 1 March 2010.)*

- *Guarantees:* In the absence of an (acceptable) ECAI credit assessment of the issuer,

²⁸ If multiple and possibly conflicting ECAI assessments are available for the same issuer/debtor or guarantor, the first-best rule (ie the best available ECAI credit assessment) is applied.

²⁹ The high credit standards for covered bank bonds issued from 1 January 2008 are assessed on the basis of the above-listed set of criteria. Covered bank bonds issued prior to 1 January 2008 are deemed to fulfil high credit standards if they comply strictly with the criteria set out in Article 22 (4) of the UCITS Directive.

³⁰ This information is published on the ECB's website (www.ecb.europa.eu).

³¹ In respect of the required second ECAI rating for those ABS 'credit assessment at issuance' refers to the credit assessment when first issued or published by the ECAI.

³² This information is published on the ECB's website (www.ecb.europa.eu).

high credit standards can be established on the basis of guarantees provided by financially sound guarantors. The financial soundness of the guarantor is assessed on the basis of ECAI credit assessments meeting the Eurosystem's credit quality threshold.

The guarantee must meet the following requirements:

- A guarantee is deemed acceptable if the guarantor has unconditionally and irrevocably guaranteed the obligations of the issuer in relation to the payment of principal, interest and any other amounts due under the debt instruments to the holders thereof until they are discharged in full.
- The guarantee has to be payable on first demand (independently from the underlying debt obligation). Guarantees given by public entities entitled to levy taxes should either be payable on first demand or otherwise provide for prompt and punctual payment following default. The obligations of the guarantor under the guarantee need to rank at least equally and rateably (*pari passu*) with all other unsecured obligations of the guarantor.
- The guarantee must be governed by the law of an EU Member State and be legally valid, and binding and enforceable against the guarantor. (*Amendment 10 October 2010*)
- The Bank of Finland will, if necessary, specifically request a copy of the guarantee for approval purposes.
- A legal confirmation concerning the legal validity, binding effect and enforceability of the guarantee must be submitted to the Bank of Finland, unless the guarantee has been given for a debt instrument with an individual asset rating or if the guarantor is a public entity entitled to levy taxes.
- The legal confirmation will have to be submitted in a form and with substance acceptable to the Eurosystem before the asset supported by the guarantee can be considered eligible. Further information as to legal confirmation in accordance with Finnish legislation can be obtained from the Bank of Finland. If the guarantor is established in a jurisdiction other than the one of the law governing the guarantee, the legal confirmation must also confirm that the guarantee is valid and enforceable under the law governing the establishment of the guarantor. The legal confirmation should be submitted for review to the national central bank that is responsible for reporting a certain asset supported by a guarantee for inclusion in the list of eligible assets.³³ The requirement of enforceability is subject to any insolvency or bankruptcy laws, general principles of fairness and other similar laws and principles applicable to the guarantor and generally affecting creditors' rights against the guarantor.

In the absence of an ECAI credit assessment the issue, issuer or guarantor, the high credit standards are established as follows:

- *Euro area public sector issuers or guarantors*: If a marketable asset is issued or guaranteed by a regional government, local authority or public sector entity (PSE) located in the euro area as defined in the CRD, the following procedure applies:
 - The issuer or guarantor is allocated to one of three classes in accordance with the CRD as explained in Table 1.³⁴
 - An implicit credit assessment for issuers or guarantors belonging to classes 1 and 2 is derived from the ECAI credit assessment of the central government of the country where the issuer or guarantor is established. This implicit credit assess-

³³ The national central bank reporting a certain asset is normally the national central bank of the country in which the asset will be admitted to trading/traded on an acceptable market. In the event that an asset is admitted to trading/traded on multiple markets, any queries should be addressed to the ECB's Eligible Assets Hotline (Eligible-Assets.hotline@europa.eu).

³⁴ Lists of entities belonging to the three classes, as well as the criteria for classifying issuers, debtors or guarantors into the three classes, are expected to be made available, together with links to the relevant websites of the national supervisory authorities, on the website of the Committee of European Banking Supervisors (CEBS): http://www.c-ebis.org/SD/Rules_AdditionalInformation.htm. The website will also have links to the websites of national financial supervisory authorities.

ment has to meet the Eurosystem credit quality threshold. No implicit credit assessment is derived for issuers/guarantors belonging to class 3.

- *Euro area non-financial corporate issuers or guarantors*: If the high credit standards for marketable assets which are issued/guaranteed by non-financial corporations³⁵ established in the euro area cannot be established on the basis of an ECAI credit assessment for the issue, issuer or guarantor, the ECAF rules for credit claims will be applicable and counterparties are allowed to make use eg of their own IRB system or third-party rating tools. The non-rated marketable debt instruments issued by non-financial corporations are not included in the public list of eligible marketable assets.

Table 1. Implicit credit assessments for euro area regional government, local authority and public sector entity¹ issuers, debtors or guarantors without an ECAI credit assessment

	Allocation of issuers, debtors or guarantors following the CRD	ECAF derivation of the implicit credit assessment of the issuer, debtor or guarantor belonging to the corresponding class
Class 1	Regional governments, local authorities and PSEs that, according to competent supervisory authorities, can be treated equally to the central government for capital requirements purposes	Allocated the ECAI credit assessment of the central government of the country in which it is established
Class 2	Regional governments, local authorities and PSEs that, according to competent supervisory authorities, can be treated equally to [credit] institutions for capital requirements purposes	Allocated a credit assessment one credit quality step ¹⁾ below the ECAI credit assessment of the central government of the country in which it is established
Class 3	Other PSEs	Treated like private sector issuers or debtors

¹⁾ Public sector entities are defined in the European System of Accounts 1995 (ESA 95), see Statistics Finland's Classification of Sectors 2000 on http://www.stat.fi/meta/luokitukset/sektoriluokitus/001-2000/index_en.html

²⁾ Information on the credit quality steps is published on the ECB's website (www.ecb.europa.eu).

3.2.1.7 Establishment of high credit standards for non-marketable assets

Credit claims

In order to establish the requirement for high credit standards for the debtors or guarantors of credit claims, counterparties have to select one main credit assessment source from among those that are available and accepted by the Eurosystem. A counterparty will select one *system* from an available credit assessment *source*, except in the case of ECAIs, where all accepted ECAI systems may be used. Alternative credit assessment sources are listed in Section 3.2.1.9. Details on individual accepted credit assessment systems, excluding counterparties' own systems, are published on the ECB website (www.ecb.europa.eu).

Counterparties must notify the Bank of Finland of the credit assessment system they intend to use. The application procedure for using counterparties' internal ratings-based systems is described in Section 3.2.1.9. The notification concerning intended use of assessments by ECAIs and the derived implicit credit assessments for the public sector (see iii in the list below) shall be submitted using a specific form obtainable from the Bank of Finland. The Bank of Finland's contact details are in Annex 8.

³⁵ The definition for a non-financial corporation is the same as in the European System of Accounts 1995 (ESA 95), see Statistics Finland's Classification of Sectors 2000 on http://www.stat.fi/meta/luokitukset/sektoriluokitus/001-2000/index_en.html.

Counterparties have to stick to the selected source for a minimum period of one year so as to preclude 'hopping' between credit assessments (ie looking for the best credit assessment that guarantees eligibility among all available sources or systems on a debtor-by-debtor basis). Counterparties wishing to change credit assessment sources after the minimum period of one year have to submit a reasoned request to the Bank of Finland.

Counterparties may be allowed to use more than one system or source upon submission of a reasoned request to the Bank of Finland. The main credit assessment source chosen is expected to cover the largest number of submitted debtors by the counterparty. The required reasoning could stem from a lack of sufficient coverage of the primary credit assessment source or system.

Counterparties must inform the Bank of Finland promptly of any credit event, including a delay of payments by the submitted debtors, that is known to the counterparty and, if necessary, withdraw or replace the assets. Furthermore, counterparties are responsible for ensuring that they use the most recent credit assessment updates available from their selected credit assessment system or source for the debtors³⁶ or guarantors of submitted assets.

Credit assessments of debtors/guarantors: The high credit standards of the debtors or guarantors of credit claims are established according to rules differentiating between public sector and non-financial corporate debtors/guarantors:

- *Public sector debtors or guarantors:* The following rules are applied in a sequential order:
 - (i) A credit assessment from the system or source selected by the counterparty exists and is used to establish whether the public sector debtor or guarantor meets the credit quality threshold.
 - (ii) In the absence of a credit assessment under (i), an ECAI credit assessment of the debtor or guarantor is used.³⁷
 - (iii) If no credit assessment is available under either (i) or (ii), the same procedure as for marketable assets applies:
 - The debtor or guarantor is allocated to one of three classes in accordance with the CRD³⁸ as explained in Table 1.
 - An implicit credit assessment for debtors or guarantors belonging to classes 1 and 2 is derived from the ECAI credit assessment of the central government of the country where the debtor or guarantor is established. This implicit assessment has to meet the Eurosystem credit quality threshold.

If a credit assessment from the system or source selected by the counterparty (or from an ECAI in case (ii) for public sector debtors or guarantors) exists but is below the credit quality threshold, the debtor or guarantor is ineligible.

- *Non-financial corporate debtors or guarantors:* If the source selected by the counterparty provides a credit assessment equal to or exceeding the credit quality threshold, the debtor or guarantor is eligible.^{39, 40}

³⁶ In the case of marketable assets issued by non-financial corporations but not assessed by an accepted ECAI, this requirement applies to the credit assessment of issuers.

³⁷ If multiple and possibly conflicting ECAI assessments are available for the same issuer/debtor or guarantor, the first-best rule (ie the best available ECAI credit assessment) is applied.

³⁸ Lists of entities belonging to the three classes, as well as the criteria for classifying issuers, debtors or guarantors into the three classes, are intended to be made available, together with links to the relevant websites of the national supervisory authorities, on the website of the Committee of European Banking Supervisors (CEBS): <http://www.eba.europa.eu>

³⁹ If the counterparty has chosen an ECAI as a credit assessment source, it may use the first-best rule.

⁴⁰ For specific credit assessment systems, the credit quality threshold can be adjusted following the performance monitoring process (see Section 3.2.1.10).

If a credit assessment from the system or source selected by the counterparty exists but is below the credit quality threshold, the debtor or guarantor is ineligible. If no credit assessment is available to establish the credit standards, the debtor or guarantor is considered ineligible.

Guarantees: Guarantees must meet the following requirements

- A guarantee is deemed acceptable if the guarantor has unconditionally and irrevocably guaranteed the obligations of the debtor in relation to the payment of principal, interest and any other amounts due under the credit claim to the holder thereof until they are discharged in full. In this regard, a guarantee deemed acceptable does not need to be specific to the credit claim but might apply to the debtor only, provided that it also covers the credit claim in question.
- The guarantee has to be payable on first demand (independently from the underlying credit claim). Guarantees given by public entities entitled to levy taxes should either be payable on first demand or otherwise provide for prompt and punctual payment following default. The obligations of the guarantor under the guarantee need to rank at least equally and rateably (*pari passu*) with all other unsecured obligations of the guarantor.
- The guarantee must be governed by the law of an EU Member State and be legally valid, and binding and enforceable against the guarantor. (*Amendment 10 October 2010*)
- A copy of the guarantee must be submitted to the Bank of Finland in advance to determine the eligibility of the credit claim in the event that the guarantor is a public entity entitled to levy taxes.
- In the event that the guarantor is not a public entity entitled to levy taxes, a legal confirmation concerning the legal validity, binding effect and enforceability of the collateral must be submitted to the Bank of Finland.
- The legal confirmation will have to be submitted in a form and with substance acceptable to the Eurosystem before the asset supported by the guarantee can be considered eligible. Further information on the legal confirmation that conforms to Finnish legislation can be obtained from the Bank of Finland. The legal confirmation should also state that the guarantee is not a personal one, only enforceable by the creditor of the credit claim. If the guarantor is established in a jurisdiction other than the one of the law governing the guarantee, the legal confirmation must also confirm that the guarantee is valid and enforceable under the law governing the establishment of the guarantor.

The legal confirmation should be submitted for review to the national central bank in the jurisdiction of the law governing the credit claim. The requirement of enforceability is subject to any insolvency or bankruptcy laws, general principles of equity and other similar laws and principles applicable to the guarantor and generally affecting creditors' rights against the guarantor.

Non-marketable retail mortgage-backed debt instruments

The high credit standards for non-marketable RMBDs must be in line with a credit assessment of credit quality step 2 of the Eurosystem's harmonised rating scale.⁴¹ (*Amendment 1 January 2011*)

⁴¹ See the Eurosystem's harmonised rating scale, published on the ECB's website (www.ecb.europa.eu).

3.2.1.8 Marketable assets without a public credit assessment

In the absence of an acceptable ECAI credit assessment for marketable assets, ie bonds and commercial paper, or a comparable indicator of fulfilment of high credit standards as specified in Section 3.2.1.6, high credit standards can be established on a case-by-case basis and accepted as collateral for each counterparty bank. First, these assets must fulfil the eligibility criteria for marketable assets (see Section 3.2.1.2), except for the issuer's sector and place of establishment. They are subject to the following rules: issues by companies operating in the financial and insurance sectors are not accepted and the place of establishment of the issuer must be the euro area. Second, they must fulfil the same high credit standard criteria as non-marketable assets (see Section 3.2.1.7).

If the counterparty bank has selected in advance an internal ratings-based (IRB) system as their source of credit assessment information and has used it in assessing the issuer's fulfilment of eligibility criteria, it must contact the Bank of Finland to establish the eligibility of each issue. The Bank of Finland's contact information can be found in Annex 8.

The Bank of Finland must be contacted before counterparty banks use their preferred credit assessment source (IRB or RTs, third-party providers' rating tools) in the assessment of credit claims and marketable assets that do not have an ECAI credit assessment. The application procedure concerning the introduction of IRB systems is described in Section 3.2.1.9. The use of RTs is also subject to assessment and approval by the Eurosystem of the respective system concerned.

Counterparties are obliged to notify the Bank of Finland, without delay, of changes in the issuer's credit assessment, based on either IRB or RTs. In the event that a counterparty chooses to discontinue the use of the issues in question as collateral for a longer period of time and so does not wish to notify the Bank of Finland of changes in assessments, the Bank of Finland must be informed of the discontinuation accordingly.

3.2.1.9 Acceptance criteria for credit assessment systems

The ECAF builds on credit assessment information from four sources. Under each source, there might be a set of credit assessment systems. The sources are external credit assessment institutions (ECAIs), counterparties' internal ratings-based (IRB) systems, third-party providers' rating tools (RTs) and national central banks' in-house credit assessment systems. Assessment systems include individual operators' systems, such as the system of a single ECAI or a single bank's internal ratings-based system.

The accepted ECAIs, ICASs and third-party RTs and their providers are listed on the ECB's website (www.ecb.europa.eu).⁴² The Bank of Finland does not have an in-house credit assessment system. However, all the counterparties of the Eurosystem may select an ICAS based outside its home country for the credit assessment of collateral according to the selection rules set out in Section 3.2.1.7. Further information on the use of in-house credit assessment systems can be found on the websites of the respective central banks (see Annex 1).

External credit assessment institution source

The ECAI source encompasses those institutions whose credit assessments may be used by credit institutions for determining the risk weight of exposures according to the CRD.

⁴² The Eurosystem only publishes the information in conjunction with its Eurosystem credit operations and does not assume any responsibility for its evaluation of the accepted credit assessment systems.

For the purposes of the ECAF, the general acceptance criteria for ECAIs are the following:

- ECAIs must be formally recognised by the relevant EU supervisory authority for the euro area countries in which they will be used, in line with the CRD.
- ECAIs must fulfil operational criteria and provide relevant coverage so as to ensure the efficient implementation of the ECAF. In particular, the use of their credit assessments is subject to the availability to the Eurosystem of information on these assessments, as well as information for the comparison and the assignment (mapping) of the assessments with the ECAF credit quality steps and the credit quality threshold and for the implementation of performance monitoring (see Section 3.2.1.10).

The Eurosystem reserves the right to decide whether it accepts an ECAI for its lending operations, making use, among other factors, of its performance monitoring process.

The ECAIs used by the Eurosystem are listed in Annex 2.

Counterparties must notify the Bank of Finland in advance of their intention to use ECAI assessments in assessing the risk of credit claims offered as collateral. The relevant form can be obtained from the Bank of Finland (contact details in Annex 8).

Internal ratings-based system source

Counterparties intending to use an IRB system to assess the credit quality of the debtors or guarantors of credit claims (or issuers without an ECAI rating) must obtain prior permission from the Bank of Finland. For this purpose, they must file a request, which can be obtained from the Bank of Finland (contact details in Annex 8), together with the following documents.⁴³

- A copy of the decision of the relevant banking supervisory authority within the EU authorising the counterparty to use its IRB system for capital requirements purposes on a consolidated or unconsolidated basis, together with any specific conditions for such use. Such a copy is not requested when such information is transmitted directly by the relevant supervisory authority to the Bank of Finland.
- Information on its approach to assigning probabilities of default to debtors, as well as data on the rating grades and associated one-year probabilities of default used to determine eligible rating grades.
- A copy of the Pillar 3 (market discipline) information that the counterparty is required to publish on a regular basis in accordance with the requirements on market discipline under Pillar 3 of the Basel II framework and the CRD.
- The name and the address of both the competent supervisory authority and the external auditor.

The request has to be signed by the counterparty's chief executive officer (CEO), chief financial officer (CFO) or a manager of similar seniority, or by an authorised signatory on behalf of one of them.

The above provisions apply to all counterparties regardless of their status – parent, subsidiary or branch – and regardless of whether the endorsement of the IRB system comes from the supervisor in the same country (for a parent company and possibly for subsidiaries) or from a supervisor in the home country of the parent (for branches and possibly for subsidiaries).

Any branch or subsidiary of a counterparty may rely on the IRB system of its parent if the Bank of Finland has accepted the use of the IRB system for ECAF purposes.

⁴³ If necessary, the listed documentation should be translated in a working language of the home national central bank.

Counterparties using an IRB system as described above are also subject to the Bank of Finland performance monitoring process (see Section 3.2.1.10). In addition to the information requirements for this process, counterparties are under an obligation to communicate to the Bank of Finland the following information on an annual basis (or as and when required by the Bank of Finland) unless such information is transmitted directly by the relevant supervisory authority:

- a copy of the most up-to-date assessment of the counterparty's IRB system by the counterparty's supervisory authority translated in a working language of the home national central bank;
- any changes to the counterparty's IRB system recommended or required by the supervisory authority, together with the deadline by which such changes must be implemented;
- the annual update of the Pillar 3 (market discipline) information that the counterparty is required to publish on a regular basis in accordance with the requirements of the Basel II framework and the CRD.
- contact information of the competent supervisory authority and the external auditor.

This yearly communication has to be signed by the counterparty's CEO, CFO or a manager of similar seniority, or by an authorised signatory on behalf of one of them. The relevant supervisory authority and, where applicable, the external auditor of the counterparty receive a copy of this letter from the Bank of Finland.

Third-party rating tool source

The RT source consists of entities that assess the credit quality of debtors by using primarily quantitative models in a systematic and mechanical manner, relying among other information on audited accounts, and whose credit assessments are not intended for general public disclosure. An RT provider, established in Finland, wishing to participate in the ECAF has to submit a request to the Bank of Finland, using the template provided by the Eurosystem, supplemented by additional documentation as specified in the template. Counterparties wishing to use a specific RT provider for ECAF purposes that is not accepted by the Eurosystem have to submit a request to the Bank of Finland, using the template provided by the Eurosystem, supplemented by additional documentation as specified in the template. The template can be obtained from the Bank of Finland (contact details in Annex 8). The Eurosystem decides whether to accept the RT provider based on evaluation of compliance with the acceptance criteria set by the Eurosystem.⁴⁴ (*Amendment 10 October 2010*)

Furthermore, the counterparty must inform the RT provider of any credit event that is known only to the counterparty, including a delay of payments by the submitted debtors.

The RT provider participating in the ECAF needs to subject itself by agreement to the Eurosystem performance monitoring process⁴⁵ (see Section 3.2.1.10). The RT provider must allow for the Bank of Finland to monitor the so-called static pool. The static pool has to be in line with the general requirements on performance monitoring under the ECAF. The RT provider has to undertake to inform the Bank of Finland of the results of the performance evaluation as soon as it has been carried out by the RT provider. Therefore, RT providers prepare a report on the RT's static pool performance. They have to undertake to keep internal records of static pools and default details for five years.

⁴⁴ The acceptance criteria are listed on the ECB's website (www.ecb.europa.eu).

⁴⁵ The counterparty must inform the RT provider promptly about any credit event that may indicate a deterioration of the credit quality.

3.2.1.10 Performance monitoring of credit assessment systems

The ECAF performance monitoring process carried out by the Bank of Finland as part of the Eurosystem consists of an annual ex post comparison of the observed default rate for the set of all eligible debtors (the static pool) and the credit quality threshold of the Eurosystem, given by the benchmark PD. It aims to ensure that the results from credit assessments are comparable across systems and sources. The monitoring process takes place one year after the date on which the static pool was defined.

The first element of the process is the annual compilation by the credit assessment system provider of the static pools of eligible debtors, ie pools consisting of all corporate and public debtors, receiving a credit assessment from the system satisfying one of the following conditions (PD=probability of default within a year, i = debtor and t = time):

$PD(i, t) \leq 0.10\%$, which is equivalent to credit quality steps 1 and 2 of the Eurosystem's rating scale, or

$0.10\% < PD(i,t) \leq 0.40\%$, which is equivalent to credit quality step 3 of the Eurosystem's rating scale.

All debtors fulfilling one of these conditions at the beginning of period t constitute the corresponding static pool at time t, divided into two categories as specified in the conditions. At the end of the foreseen 12-month period, the realised default rate for the static pools of debtors at time t is computed. On an annual basis, the rating system provider has to agree to submit to the Bank of Finland/Eurosystem the number of eligible debtors contained in the static pools at time t and the number of those debtors in the static pool (t) that defaulted in the subsequent 12-month period. (*Amendment 1 January 2011*)

The realised default rate of the static pool of a credit assessment system recorded over a one-year horizon serves as input to the ECAF performance monitoring process which comprises an annual rule and a multi-period assessment. In case of a significant deviation between the observed default rate of the static pool and the credit quality threshold over an annual and/or a multi-annual period, the Eurosystem consults the rating system provider to analyse the reasons for that deviation. This procedure may result in a correction of the credit quality threshold applicable to the system in question.

The Eurosystem may decide to suspend or exclude the credit assessment system in cases where no improvement in performance is observed over a number of years. In addition, in the event of an infringement of the rules governing the ECAF, the credit assessment system will be excluded from the ECAF.

3.2.2 Collateral management

3.2.2.1 Collateral held in the pooling system

In its collateral management, the Bank of Finland primarily uses a pooling system. This means that the Bank of Finland collects all of a counterparty's eligible domestic and foreign assets into a pool that covers the counterparty's total collateral requirement.

A counterparty's total collateral requirement consists of the combined requirements for open market operations transacted with the Bank of Finland and the marginal lending facility, including interest thereon; and the intraday overdraft limit on its PM account at the Bank of Finland. Individual collateral assets are not linked to specific credit operations; rather the asset pool serves as collateral for all credits received and the PM account limit. The Bank of Finland grants a credit to a counterparty or raises its PM account limit provided that the subsequent total value of the counterparty's pool of assets is at least equal to the total collateral requirement.

A pool consists of domestic and foreign assets. These collateral assets may be marketable debt instruments or non-marketable credit claims (bank loans).¹ Domestic marketable assets are processed in the automatic collateral management system of the Euroclear Finland Ltd, and domestic non-marketable credit claims are handled according to the Bank of Finland's own procedures. In contrast, foreign assets are processed using the CCBM system or links between central securities depositories, as approved by the ECB.

In calculating the total collateral value of its pool, a Bank of Finland counterparty must take account of applicable valuation haircuts, which depend on residual maturity, coupon structure and liquidity of underlying assets.

Legally, the procedure constitutes collateralised lending, with the collateral being pledged to the Bank of Finland. This requires conclusion of a pledge agreement with the Bank of Finland. When foreign collateral assets are used, it may be necessary to apply other procedures if pledging is not possible.

3.2.2.2 Domestic marketable assets

Automatic collateral management accounts at the Euroclear Finland Ltd

The Bank of Finland administers domestic marketable assets in a counterparty's pool using the counterparty's automatic collateral management account at the Euroclear Finland Ltd. A counterparty may open such an account in its own book-entry register or in that of another registrar, but not in the Bank of Finland's book-entry register.

If a collateral management account has been opened in another registrar's book-entry register, the registrar and the Bank of Finland must conclude an agreement on the operation of the account.

The Euroclear Finland Ltd records in the collateral management accounts the eligibility criteria and asset valuation data as specified by the Bank of Finland. The eligibility criteria determine which debt instruments registered with the Euroclear Finland Ltd may, or may not, be used as collateral. Instruments related to the account holder through close links or defined as having bank-specific eligibility to the benefit of another bank (debt instruments without public credit rating) may not be used as collateral. Notwithstanding separately specified quality requirements for collateral assets, cash may be temporarily accepted as collateral for holding in the account on an intraday basis.

The Bank of Finland records in a counterparty's collateral management account the collateral requirement as notified in writing by the counterparty, which amount cannot exceed the collateral value of the account. The Euroclear Finland Ltd's automatic collateral management system calculates daily the collateral value of assets held in each collateral manage-

¹ Non-marketable retail mortgage-backed debt instruments are defined as assets eligible for inclusion in the Single List. Currently, instruments in this asset class are only used in Ireland.

ment account and prevents a transfer of assets from an account whenever the collateral value of the account would fall below the collateral requirement. Otherwise, the counterparty can freely transfer collateral held in the account.

The counterparty may reduce the collateral requirement at the Euroclear Finland Ltd, provided that the total collateral requirement remains fully covered after the reduction. If the collateral value of the Euroclear Finland Ltd account (in a daily valuation) falls below the collateral requirement, the counterparty must correct the situation without delay, by either supplying additional collateral or lowering the PM account limit if it is not being fully used.

3.2.2.3 Foreign marketable assets

Correspondent central banking model²

The national central banks and the ECB have developed a mechanism to ensure that eligible marketable assets issued in other Member States can be used to collateralise open market operations, marginal lending facilities and intraday credits. The mechanism is called the correspondent central banking model (CCBM). Under the CCBM, national central banks act as correspondents and custodians for each other.

In delivering eligible marketable assets issued in another euro area Member State for its pool at the Bank of Finland in accord with the CCBM, the counterparty must specify the assets in writing by indicating their ISIN or other identifying codes, their quantity and the foreign custodian used by the counterparty. At the same time, the counterparty must also instruct its foreign custodian to transfer the assets to the appropriate correspondent central bank as soon as possible, for holding on the Bank of Finland's account.

The counterparty may at any time during the opening hours of the CCBM transfer foreign marketable assets to a correspondent central bank for holding in the Bank of Finland's account. Once the Bank of Finland is informed by the correspondent central bank that a transfer has been completed and that all requirements of a legally valid pledge have been met, the assets can be considered pledged to the Bank of Finland and added to the pool of the counterparty.

If the counterparty wishes to withdraw foreign marketable assets from its pool or replace such assets by others, it must so inform the Bank of Finland in writing and instruct its custodian to take the necessary action. The Bank of Finland transfers the assets to the custodian indicated by the counterparty. However, such withdrawal or replacement shall not result in a collateral deficit in the counterparty's pool.

Foreign marketable assets are valued by the Bank of Finland daily by 12 noon on the basis of price data received from correspondent central banks and the calculation rules based on current risk control systems. If the valuation results in a collateral deficit in a counterparty's pool, the counterparty must cover the deficit without delay after being so informed by the Bank of Finland.

Any redemptions and coupon payments related to foreign marketable assets pledged to the Bank of Finland will be paid to the counterparty, provided that such payment does not result in a collateral deficit in the counterparty's pool.

² A more detailed description of the correspondent central banking model can be found on the ECB's website, in the document 'Correspondent central banking model (CCBM), Procedures for Eurosystem counterparties' (Amendment 10 October 2010)

Links between central securities depositories

Eligible marketable assets held with a central securities depository located in another Eurosystem country can be transferred to a central securities depository in a counterparty's home country via a link approved by the ECB, without requiring that the counterparty be a member of the concerned foreign central securities depository. A list of links approved by the ECB is available from the ECB's website (www.ecb.europa.eu/paym/coll/coll/html/sss.en.html).

The Euroclear Finland Ltd has opened such links with the German Clearstream Banking Frankfurt and the French Euroclear France.

Account holders may deliver foreign marketable assets to their automatic collateral management accounts with the Euroclear Finland Ltd for inclusion in their respective collateral pools via the link between the Euroclear Finland Ltd and Clearstream Banking Frankfurt. Presently, the only transferable assets that are eligible for use as collateral with same-day value are bonds issued by the German government. If a counterparty wishes to transfer other eligible assets issued in Clearstream Banking Frankfurt for its collateral management account, the counterparty must contact the Bank of Finland and the Euroclear Finland Ltd for further instructions.

Assets delivered via the link are handled in the counterparty's automatic collateral management account in the same manner as domestic marketable assets.

If an account holder wishes to transfer marketable assets held with Euroclear France for use as collateral in its automatic collateral management account with the Euroclear Finland Ltd, the account holder must contact the Bank of Finland and the Euroclear Finland Ltd for further instructions.

3.2.2.4 Domestic non-marketable assets

3.2.2.4.1 Principles for the use of domestic credit claims (bank loans) as collateral

All Eurosystem national central banks have developed procedures for managing domestic credit claims, in accordance with the requirements of its national legislation and operating environment. A detailed description of required measures for using credit claims subject to Finnish law as collateral is provided in subsection 3.2.2.4.2 'Bank of Finland's operative procedures for use of credit claims as collateral'.

Prior to the use of credit claims as collateral, Bank of Finland counterparties must ensure that they fulfil such technical and operative requirements as are listed in subsection 3.2.2.4.2 for use of credit claims as collateral and that all credit claims that they submit as collateral meet the legal and other requirements stated in section 3.2.1.

In order to use credit claims as collateral, a counterparty must provide details of each credit claim it uses as collateral to the Bank of Finland, which manages such credit claims in its own systems. The counterparty undertakes to provide timely information on credit claims it submits as collateral and to observe the instructions in subsection 3.2.2.4.2 for addition of credit claims to the counterparty's pool of assets, update of previously supplied details of credit claims and for withdrawal of credit claims from the pool.

In order to pledge credit claims, a counterparty must, under Finnish law, either give the debtor an ex ante notification of the use of a credit claim as collateral and inform the Bank of Finland accordingly if the credit claim qualifies as an ordinary promissory note, or make a separate endorsement on the credit document if the credit claim qualifies as a negotiable promissory note. (*Amendment 1 January 2011*)

During the time when credit claims are being used as collateral, they constitute part of the counterparty's pool, in the manner of marketable eligible assets. For administrative reasons, the handling of credit claims may be slower than that of marketable eligible assets. Counterparties must therefore be prepared to submit other collateral assets, if necessary, to cover

any collateral deficits that may arise from the use of credit claims.

The Bank of Finland applies to credit claims the eligibility and other criteria stated in section 3.2.1, as well as the risk control measures described in section 3.2.3. National central banks are obliged to take certain ex post verification measures because of the use of credit claims as collateral. (*Amendment 1 January 2011*)

3.2.2.4.2 Bank of Finland's operative procedures for use of credit claims as collateral

In submitting credit claims subject to Finnish law as collateral, counterparties must comply with the following procedures defined by the Bank of Finland.

Measures prior to the use of credit claims as collateral

The use of claims as collateral requires that the following technical and operative measures have been taken.

The counterparty has

- signed a separate pledge agreement on credit claims with the Bank of Finland
- obtained approval from the Bank of Finland for the system(s) it uses to assess debtors' creditworthiness
- submitted to the Bank of Finland a description of the procedures by which the counterparty intends to provide the Bank of Finland with details of credit claims used as collateral and of the procedures by which the counterparty intends to preserve credit claims pledged to the Bank of Finland (*Amendment 1 January 2011*)
- submitted to the Bank of Finland the required specimen signatures for the following operative measures: i) sending of a notification of pledge, ii) signing of endorsements of credit claims for transfer to the benefit of the Bank of Finland as pledge (in respect of negotiable promissory notes) and iii) signing of ex ante notifications to debtors (in respect of ordinary promissory notes), as well as iv) signing of quarterly certifications (*Amendment 1 January 2011*)
- submitted to the Bank of Finland information on the static pool of eligible debtors (see section 3.2.1.10), if the counterparty intends to use an internal ratings based assessment method
- undertaken the necessary testing with the Bank of Finland.

Use of credit claims as collateral

In order to use credit claims as collateral, a counterparty must provide details of such credit claims to the Bank of Finland, which manages them in its own systems. The form used for submitting credit claim details ('notification of pledge concerning credit claims') is provided in Annex 5. The form specifies the information required on each credit claim. In addition to the required information, the counterparty must indicate on the form the measures taken regarding the credit claims: addition of a new credit claim to the counterparty's pool of assets, update of previously supplied credit claim details or withdrawal of credit claims from the pool.

When the counterparty provides details of a new credit claim to the Bank of Finland *in order to use the credit claim as collateral*, the Bank of Finland will enter the information in its own registers. Prior to addition of the credit claim to the counterparty's pool, the measures related to its pledging must have been duly completed (see subsection 'Pledge of credit claims and unwinding of pledge').

The counterparty must *update the details of credit claims in its collateral pool* whenever changes occur eg due to early, partial or full repayment of a credit claim or because of changes in debtors' creditworthiness or material changes in the conditions of credit claims. The Bank of Finland must be immediately notified of such changes, using the form 'notification of pledge concerning credit claims'; in no case later than the next banking day. If a change in the details of a credit claim leads to ineligibility of a claim, the counterparty must, instead of submitting updated details, request withdrawal of the claim from its pool of assets. If a change concerning one debtor affects more than one credit claim used as collateral, the

counterparty must update the details of all such credit claims. If changes made to the conditions of a credit claim are so fundamental that the credit claim can no longer be considered the same claim, the old credit claim must first be withdrawn from the counterparty's pool and a new pledge signed in respect of the new credit claim.

If the counterparty wishes to *withdraw a credit claim from its collateral pool*, it must inform the Bank of Finland, using the form 'notification of pledge concerning credit claims' and choosing 'unwinding of pledge' as the measure to be taken. This will initiate the withdrawal of the credit claim from the counterparty's pool, after which the credit claim no longer serves as collateral. After this, the counterparty must take due measures related to the unwinding of the pledge (see subsection 'Pledge of credit claims and unwinding of pledge').

In withdrawing credit claims from its pool of assets or sending updated details of credit claims that reduce the collateral value of credit claims, the counterparty must ensure that such measures do not lead to a collateral deficit in its pool.

The counterparty may send the form required for submission of credit claim details to the Bank of Finland by fax. Alternatively, counterparties may provide the required information via SWIFTNet FileAct using an electronic template/format message specified by the Bank of Finland in separate instructions. The counterparty may request further instructions for the introduction of the template/format message from the Bank of Finland. If the template/format message does not comply with the current Bank of Finland specifications, the Bank of Finland shall not be liable for any possible damages arising therefrom.

The counterparty may send credit claim details to the Bank of Finland during the opening hours of TARGET2- Suomen Pankki; but data to be updated on the same day must be delivered by 17.00 Finnish time (16.00 CET). The Bank of Finland updates information on credit claims already serving as collateral and withdraws credit claims from the counterparty's pool, per the counterparty's instructions, on the day the instructions arrive at the Bank of Finland. Normally, additions of new credit claims to a counterparty's pool of assets are also made during the same day. However, additions of credit claims require, in addition to submission of credit claim information, finalisation of the pledging procedure. If, for administrative reasons, the handling of a new credit claim requires more time and the Bank of Finland is unable to add the new credit claim to the counterparty's pool on the day of submission of credit claim information, the Bank of Finland will inform the counterparty thereof and the addition will be made as soon as possible. (*Amendment 1 January 2011*)

Pledge of credit claims and unwinding of pledge

Under Finnish legislation, the measures required for pledging credit claims depend on the juridical type of the underlying promissory notes.

The precondition for using *ordinary promissory notes* as collateral is that the debtor (and guarantor, if any) has been notified in advance of their use as collateral (*ex ante notification*). The counterparty must submit the notification to the debtor in a manner agreed with the debtor. The notification must state that payments of interest and principal will continue to be made to the counterparty. The counterparty must submit a copy of the notification to the Bank of Finland after the notification has become effective according to the time limits agreed between counterparty and debtor. The credit claim can be added to the counterparty's pool of assets as soon as the Bank of Finland has received a copy of the notification. Similarly, when the counterparty notifies the Bank of Finland of withdrawal of a credit claim from its pool and the pledge between the parties concerned is considered to be terminated, the Bank of Finland will give written permission to the counterparty to notify the debtor (and guarantor, if any) of termination of the pledge.

The precondition for using *negotiable promissory notes* as collateral is that the counterparty makes a separate endorsement on the original credit documents to the benefit of the Bank of Finland. A copy of the endorsement must be delivered to the Bank of Finland. (*Amendment 1 January 2011*)

Upon termination of the pledge, the original endorsement must be delivered by mail, as a registered letter, to the Bank of Finland, who, in turn, transfers the credit documentation back to the counterparty. After this, the Bank of Finland delivers the original endorsement by mail back to the counterparty. *(Amendment 1 January 2011)*

Counterparties must preserve credit documents and endorsements on their premises with due diligence and due care. *(Amendment 1 January 2011)*

Despite pledging, the customer relationship between counterparty and debtor remains unchanged, that is, the debtor continues to make payments of interest and principal to the counterparty. In the event of a counterparty default or failure to fulfil an obligation for which the credit claim serves as collateral, the Bank of Finland will deliver an ex post notification to the debtor, indicating the use of the credit claim as collateral to the benefit of the Bank of Finland and requesting the debtor to make future payments of interest and principal on the credit claim to the Bank of Finland. In such a case, the counterparty must deliver all necessary documents to the Bank of Finland. *(Amendment 1 January 2011)*

If a credit claim is secured by collateral that requires a particular management agreement, the counterparty must contact the Bank of Finland well in advance in order to agree on the matter separately. *(Amendment 1 January 2011)*

Verification of the existence and details of credit claims

The Bank of Finland will verify the existence and details of credit claims submitted as collateral, in accordance with Eurosystem rules as follows:

- Prior to using credit claims as collateral, the counterparty must submit to the Bank of Finland, for verification purposes, a description of the procedures the counterparty intends to apply when providing the Bank of Finland with details of credit claims submitted as collateral and of the procedures according to which the counterparty intends to preserve credit claims pledged to the Bank of Finland. *(Amendment 1 January 2011)*
- The Bank of Finland will send to the counterparty a quarterly summary of credit claims it has submitted as collateral. The counterparty must check the information, sign the accompanying certification and return it to the Bank of Finland.
- The Bank of Finland will from time to time verify, through random checks, the accuracy and timeliness of details of credit claims submitted as collateral. In general, the Bank of Finland will notify the counterparty in advance of such investigation visits and of the date for which credit claim details will be verified.

3.2.2.5 Foreign non-marketable assets

Bank of Finland counterparties may also use as collateral such non-marketable assets as are governed by the law of a euro area Member State other than Finland. These foreign credit claims (and in principle, also non-marketable retail mortgage-backed debt instruments³) may be used as collateral according to the correspondent central banking model (CCBM) described in section 3.2.2.3. The central bank of the country whose legislation is applied to the credit claims will act as correspondent central bank.

The general CCBM principles apply to the use of foreign credit claims as collateral, but the detailed procedures applied in each particular country are defined by the correspondent central bank in compliance with the country's legal requirements. If Bank of Finland counterparties use such foreign credit claims as collateral, they must deliver the information required for their use as collateral to the relevant correspondent central bank and ensure a legally valid pledge of the credit claims, according to instructions from the correspondent central bank.

Bank of Finland counterparties must also take into account that if credit claims – even if they are credit claims subject to Finnish law – have been granted to foreign debtors, their use as collateral may require specific measures under foreign legislation. In such cases, the central bank of the country where the debtor is located acts as an assisting central bank and provides, as necessary, information on additional measures that may be required under the legislation of the country concerned.

Each Eurosystem national central bank has issued Terms and Conditions to be observed by foreign counterparties whenever such central bank assumes the role of a correspondent central bank or assisting central bank. In order to use as collateral credit claims that are governed by the law of a euro area Member State other than Finland or credit claims that have been granted to debtors located in euro area Member States other than Finland, Bank of Finland counterparties can access the Terms and Conditions published by the correspondent central banks on their respective websites.

Similarly, should any counterparties located in a euro area Member State other than Finland wish to use as collateral credit claims that are governed by the law of Finland or credit claims that have been granted to debtors located in Finland, the counterparties must observe the Terms and Conditions defined by the Bank of Finland. The Bank of Finland's Terms and Conditions are provided in Annex 6.

3.2.2.6 Margin calls (based on valuation) in a pooling system

A counterparty's total collateral requirement (PM account limit + credits, incl. interest) depends on the types of its open market operations, its marginal lending facilities and any changes to the PM account limit, as well as on daily fluctuations in the value of assets supplied by the counterparty. The Bank of Finland ensures, via its own collateral management system, that a counterparty cannot make changes to its commitments without adequate collateral. The daily valuation of assets (including partial or full repayments of credit claims) may, however, result in a collateral deficit in the counterparty's pool. If so, the counterparty must cover the deficit without delay, eg by:

- a) Increasing the amount pledged in the collateral management account at the Euroclear Finland Ltd and, if necessary, depositing additional domestic collateral in the account.
- b) Lowering the PM account limit if it is not being fully used.
- c) Supplying foreign marketable assets in accord with the CCBM procedure or a link. This arrangement may, however, be so time-consuming that, in practice, it cannot be considered suitable for handling collateral deficits that require prompt action. Thus, when a counterparty wishes to use foreign assets as collateral, the counterparty must always

³ Currently, non-marketable retail mortgage-backed debt instruments are only used in Ireland.

see to it that an adequate margin exists between the total collateral requirement and the collateral value of the asset pool.

- d) Supplying credit claims as collateral. Submission of both domestic and foreign credit claims for use as collateral may, however, be so time-consuming that, in practice, it cannot be considered suitable for handling collateral deficits that require prompt action. Thus, when a counterparty wishes to use credit claims as collateral, the counterparty must always see to it that an adequate margin exists between the total collateral requirement and the collateral value of the asset pool.

3.2.2.7 Exceptional procedures for foreign assets

3.2.2.7.1 Taxation of foreign marketable debt instruments and related corporate actions

The counterparty is responsible for knowing the taxation principles applicable to foreign debt instruments used as collateral. If the counterparty uses as collateral under the correspondent central banking model (CCBM) debt instruments on which the interest income is subject to withholding tax, the counterparty must be able to prove its tax status. The correspondent central bank involved may, prior to the coupon detachment date, request that the Bank of Finland provide it with documentation certifying the tax status. The Bank of Finland will forward the request to the counterparty, which should deliver the documentation to the Bank of Finland by the specified deadline.

The Bank of Finland will forward the documentation required for taxation purposes to the correspondent central bank to the best of its ability, consistent with due diligence. If, despite this, damage is caused or the counterparty fails to submit the required documentation or there are defects in the documentation submitted, the Bank of Finland shall not assume responsibility for any tax withholding or tax reimbursement consequences.

The Bank of Finland recommends that, at the time of coupon maturity, counterparties avoid the use of collateral assets for which the coupon payments comprise interest income subject to withholding tax.

The Bank of Finland will forward notices of corporate actions from the correspondent central bank to the counterparty. If the counterparty wishes to be party to the corporate action, the Bank of Finland shall forward the documentation received from the counterparty to the correspondent central bank to the best of its ability, consistent with due diligence.

3.2.2.7.2 Taxation concerning marketable debt instruments issued by entities established in non-EEA G-10 countries and related corporate actions

In addition to what is provided in section 3.2.2.7.1 above concerning taxation procedures related to foreign marketable debt instruments, the counterparty must take account of any particular tax-related matters concerning debt instruments issued by entities established in non-EEA G-10 countries. If the counterparty uses debt instruments on which the interest income is subject to withholding tax, the Bank of Finland must be provided with documentation certifying the counterparty's own tax status in sufficiently good time prior to the use of such debt instruments as collateral. The counterparty must also ensure that the submitted documentation is up-to-date. In order to ensure smooth functioning of operational processes, the counterparty may use only such collateral assets in respect of which the counterparty is itself the beneficial owner or in respect of which it acts as Qualified Intermediary (the latter option concerns only US issues).⁴

Counterparties that intend to use as collateral debt instruments issued by entities established in non-EEA G-10 countries are requested to contact the Bank of Finland in good time for further instructions.

The Bank of Finland will forward notices of corporate actions from the correspondent central bank to the counterparty. If the counterparty wishes to be party to the corporate action, the

⁴ The Bank of Finland reserves the right to deviate from this principle on the basis of a separate application by the counterparty.

Bank of Finland shall forward the documentation received from the counterparty to the correspondent central bank to the best of its ability, consistent with due diligence.

3.2.2.7.3 Earmarked repo transactions or collateral using assignment or floating charge

When using foreign assets, certain special procedures may have to be applied in order to create a legally valid security interest in the assets. Under the CCBM system, when using marketable assets, an exceptional situation may arise where pledging is not possible and it is therefore necessary to conduct an earmarked repo transaction. Similarly, in connection with foreign non-marketable assets, it may be necessary to apply procedures known as assignment or floating charge. These methods are not applicable to domestic assets.

If foreign marketable assets originate from a jurisdiction where pledging of the assets is problematic from a legal viewpoint, the Bank of Finland may exceptionally conduct an earmarked repo transaction in which the ownership right to the marketable assets is transferred. In this case, the value of the underlying assets must be at least equal to the exact amount agreed with the counterparty in the relevant tender operation.

Earmarked assets are processed largely in the same manner as in connection with the supply of pledged foreign assets to a pool administered by the Bank of Finland, ie in accord with the CCBM. The counterparty requests its foreign custodian to transfer the assets to the appropriate correspondent central bank for holding in the Bank of Finland's account. After the correspondent central bank has informed the Bank of Finland that it has received the assets in question, the Bank of Finland may transfer the funds to the counterparty's PM account.

In the Bank of Finland's collateral management system, each earmarked repo transaction is processed separately and these assets are not included in counterparties' pools of assets. Earmarked assets are valued in the same manner as pledged assets. If a daily valuation of the assets results in a collateral deficit, the deficit can be covered from the counterparty's pool. The underlying assets of an earmarked repo transaction can be replaced. The counterparty is responsible for ensuring that the replacement will not result in a collateral deficit at any time during the transaction.

When using foreign non-marketable assets that cannot be pledged, it may be necessary to resort to assignment or floating charge. Further information on the practical implementation of these methods can be obtained from the central bank of the country whose legislation is applied to such non-marketable assets.

3.2.2.8 Collateral management fees

The Euroclear Finland Ltd charges the account holder for expenses arising from the operation of the collateral management account related to the pool of collateral, according to its own fee schedule. The Bank of Finland does not charge for expenses in respect of collateral assets handled in collateral management accounts at the Euroclear Finland Ltd.

The Bank of Finland collects the following fees, as determined by the ECB, in respect of collateral (marketable and non-marketable assets) delivered via the CCBM system:

- A service fee of 0.0069% p.a. of the average nominal value of collateral.⁵
- A transaction fee of EUR 30 for each addition to the pool, per collateral asset.

National tariffs determined by each Eurosystem Member State will be applied to domestic non-marketable assets during the period 2007–2011. The Bank of Finland charges a handling fee for using domestic credit claims, amounting to 0.0020% p.a. of the collateral value of bank loans serving as collateral.

The Bank of Finland invoices counterparties for the fees monthly in arrears.

⁵ Pool factor adjusted nominal value for certain ABS and MBS-type collateral assets.

3.2.3 Collateral-related risk control and sanctions

3.2.3.1 Introduction

Risk control measures are applied to the assets underlying Eurosystem credit operations in order to protect the Eurosystem against the risk of financial loss if underlying assets have to be realised owing to the default of a counterparty.

The Eurosystem, including the Bank of Finland, applies different types of risk control measures depending on the type of assets submitted by the counterparty. The risk control measures are broadly harmonised across the euro area¹ and ought to ensure consistent, transparent and non-discriminatory conditions for any type of eligible asset across the euro area.

Valuation haircuts

The Eurosystem applies 'valuation haircuts' in the valuation of underlying assets. This implies that the value of the underlying asset is calculated as the market value of the asset less a certain percentage (haircut). (*Amendment 10 October 2010*)

Limits in relation to the use of unsecured debt instruments

The Bank of Finland, as part of the Eurosystem, applies limits to the use of unsecured debt instruments, as described in section 3.2.3.2. (*Amendment 10 October 2010*)

The Bank of Finland, as part of the Eurosystem, reserves the right to apply additional risk control measures if required to ensure an adequate risk protection of the Eurosystem in line with Article 18.1 of the Statute of the ESCB. Such risk control measures, which must be applied in a consistent, transparent and non-discriminatory manner, can also be applied at the level of individual counterparties if required to ensure such protection.

Other risk management methods

- Initial margins

The Eurosystem may apply initial margins in its liquidity-providing reverse transactions. This means that counterparties would need to provide underlying assets with a value at least equal to the liquidity provided by the Eurosystem plus the value of the initial margin. (*Amendment 10 October 2010*)

- Limits in relation to issuers/debtors or guarantors

The Eurosystem may apply additional limits, other than those applied to the use of unsecured debt instruments, to the exposure vis-à-vis issuers/debtors or guarantors. Such limits can also be applied to specific counterparties, in particular if the credit quality of the counterparty appears to exhibit a high correlation with the credit quality of the collateral submitted by the counterparty.

- Application of supplementary haircuts

The Eurosystem may apply supplementary haircuts if required to ensure adequate risk protection of the Eurosystem in line with Article 18.1 of the Statute of the ESCB.

(*Amendment 10 October 2010*)

¹ Owing to operational differences across Member States, some differences in terms of risk control measures may prevail. For instance, in respect of the procedures for counterparties' delivery of underlying assets to the NCBs (in the form of a pool of collateral pledged with the NCB or as repurchase agreements based on individual assets specified for each transaction), minor differences may occur with regard to the timing of the valuation and other operational features of the risk control framework. Furthermore, in the case of non-marketable assets, the precision of valuation techniques may differ, which is reflected in the overall level of haircuts (see Section 3.2.3.3).

- Additional guarantees

The Eurosystem may require additional guarantees from financially sound entities in order to accept certain assets.

- Exclusion

The Eurosystem may exclude certain assets from use in its monetary policy operations. Such exclusion may also be applied to specific counterparties, in particular if the credit quality of the counterparty appears to exhibit a high correlation with the credit quality of the collateral submitted by the counterparty. *(Amendment 10 October 2010)*

3.2.3.2 Risk control measures for marketable assets

Marketable assets are subject to haircuts and uncovered bank bonds are furthermore subject to limits.

Eligible marketable assets are allocated to one of five liquidity categories², based on issuer classification and asset type. The liquidity categories (in decreasing order) are I, II, III, IV and V. The haircuts applied to debt instruments included in categories I to IV differ according to the residual maturity and coupon structure of the debt instruments. Haircuts applied to category V do not account for maturity or coupon structure. *(Amendment 1 January 2011)*

Category I

- Central government debt instruments
- Debt instruments issued by central banks³

Category II

- Local and regional government debt instruments
- Jumbo covered bank bonds⁴
- Agency debt instruments⁵
- Supranational debt instruments

Category III

- Traditional covered bank bonds
- Debt instruments issued by corporate and other issuers⁵
- Other covered bank bonds⁶ *(Amendment 1 January 2011)*

Category IV

- Credit institution debt instruments (unsecured)
- Debt instruments issued by financial corporations other than credit institutions (unsecured) *(Amendment 1 January 2011)*

Category V

- Asset-backed securities

² In general, the issuer classification determines the liquidity category. However, all asset-backed securities are included in category V, regardless of the classification of the issuer, and jumbo covered bank bonds are included in category II, while traditional covered bank bonds, other covered bank bonds and other debt instruments issued by credit institutions are included in category III and IV.

³ Debt certificates issued by the ECB and debt instruments issued by the NCBs prior to the adoption of the euro in their respective Member State are included in liquidity category I.

⁴ Only instruments with an issuing volume of at least €1 billion, for which at least three market-makers provide regular bid and ask quotes, fall into the asset class of jumbo covered bank bonds.

⁵ Only marketable assets issued by issuers that have been classified as agencies by the ECB are included in liquidity category II. Marketable assets issued by other agencies are included in liquidity category III or IV, depending on the issuer and asset type.

⁶ Non-UCITS compliant covered bonds, including both structured covered bonds and multi-issuer covered bonds are included in liquidity category III.

The valuation haircuts applied to fixed coupon and zero coupon debt instruments as well as asset-backed securities are assigned in Table 1.

The valuation haircut levels applied to fixed coupon debt instruments included in categories I to IV are also applicable to debt instruments, the coupon of which is linked to a change in the rating of the issuer itself or to inflation-indexed bonds.

The haircut applied to debt instruments included in categories I to IV with variable rate coupons is that applied to the zero-to-one-year maturity bucket of fixed coupon instruments in Table 1. A coupon payment is considered a variable rate payment if the coupon is linked to a reference interest rate and if the resetting period corresponding to this coupon is no longer than one year. (*Amendment 1 January 2011*)

The haircut applied to debt instruments included in categories I to IV with variable rate coupons, for which the resetting period is longer than one year, is that applied to fixed coupon instruments in Table 1 according to the remaining life of the instrument.

Individual debt instruments included in category V are subject to a unique haircut of 16% regardless of maturity or coupon structure. Individual asset-backed securities, covered bank bonds (jumbo covered bank bonds, traditional covered bank bonds and other covered bank bonds) and unsecured credit institution debt instruments that are theoretically valued are subject to an additional valuation haircut. This haircut is directly applied at the level of theoretical valuation of the individual debt instrument in the form of a valuation markdown of 5%. (*Amendment 1 January 2011*)

The haircuts applied to marketable inverse floating rate debt instruments included in categories I to IV are described in Table 2.

The haircuts applied to marketable instruments included in categories I to IV with more than one type of coupon payment depend only on the coupon payments during the remaining life of the instrument. The valuation haircut applied to such an instrument is set equal to the highest of the haircuts applicable to debt instruments with the same residual maturity, and coupon payments of any one of the types occurring in the remaining life of the instrument are considered.

Table 1. Levels of valuation haircuts applied to eligible marketable fixed coupon and zero coupon instruments (Categories I-IV) and asset-backed securities (Category V) (Amendment 1 January 2011)

Credit quality	Residual maturity (years)	Liquidity categories								Category V ⁷
		Category I		Category II ⁷		Category III ⁷		Category IV ⁷		
		fixed coupon	zero coupon	fixed coupon	zero coupon	fixed coupon	zero coupon	fixed coupon	zero coupon	
Steps 1 and 2 (AAA–A-) ⁸	0-1	0.5	0.5	1.0	1.0	1.5	1.5	6.5	6.5	16
	1-3	1.5	1.5	2.5	2.5	3.0	3.0	8.5	9.0	
	3-5	2.5	3.0	3.5	4.0	5.0	5.5	11.0	11.5	
	5-7	3.0	3.5	4.5	5.0	6.5	7.5	12.5	13.5	
	7-10	4.0	4.5	5.5	6.5	8.5	9.5	14.0	15.5	
	>10	5.5	8.5	7.5	12.0	11.0	16.5	17.0	22.5	
<i>Liquidity categories</i>										
Credit quality	Residual maturity (years)	Category I		Category II ⁷		Category III ⁷		Category IV ⁷		Category V ⁷
Step 3 (BBB+–BBB-) ⁸	0-1	5.5	5.5	6.0	6.0	8.0	8.0	15.0	15.0	Not eligible
	1-3	6.5	6.5	10.5	11.5	18.0	19.5	27.5	29.5	
	3-5	7.5	8.0	15.5	17.0	25.5	28.0	36.5	39.5	
	5-7	8.0	8.5	18.0	20.5	28.0	31.5	38.5	43.0	
	7-10	9.0	9.5	19.5	22.5	29.0	33.5	39.0	44.5	
	>10	10.5	13.5	20.0	29.0	29.5	38.0	39.5	46.0	

⁷ Individual asset-backed securities, covered bank bonds (jumbo covered bank bonds, traditional covered bank bonds and other covered bank bonds) and uncovered bank bonds that are theoretically valued in accordance with 3.2.3.4. are subject to an additional valuation haircut. Ratings as specified in the Eurosystem's harmonised rating scale are published on the ECB's website (www.ecb.europa.eu). This haircut is directly applied at the level of the theoretical valuation of the individual debt instrument in the form of a valuation markdown of 5%.

⁸ Ratings as specified in the Eurosystem's harmonised rating scale are published on the ECB's website (www.ecb.europa.eu).

Table 2. Levels of valuation haircuts applied to eligible marketable inverse floating rate debt instruments included in categories I to IV (*Amendment 1 January 2011*)

Credit quality	Residual maturity (years)	Inverse floater coupon
Steps 1 and 2 (AAA–A–)	0-1	7.5
	1-3	11.5
	3-5	16.0
	5-7	19.5
	7-10	22.5
	>10	28.0
Credit quality	Residual maturity (years)	Inverse floater coupon
Step 3 (BBB+– BBB–)	0-1	21.0
	1-3	46.5
	3-5	63.5
	5-7	68.0
	7-10	69.0
	>10	69.5

The instrument-specific valuation haircuts applied to securities accepted on the public list of collateral for marketable assets are available on the ECB's website at the following addresses: https://mfi-assets.ecb.int/query_EA.htm or https://mfi-assets.ecb.int/dla_EA.htm.

The Bank of Finland, as part of the Eurosystem, limits the use of unsecured debt instruments issued by a credit institution or by any other entity with which the credit institution has close links as defined in Section 3.2.1.4. Such assets may only be used as collateral by a counterparty to the extent that the value assigned to that collateral by the Eurosystem after the application of haircuts does not exceed 5 % of the total value of the collateral submitted by that counterparty after the haircuts. This limit does not apply to such assets that are guaranteed by a public sector entity which has the right to levy taxes, or if the value after haircuts of the assets does not exceed EUR 50 million. In the event of a merger between two or more issuers of such assets or the establishment of a close link between such issuers, these issuers are treated as one issuer group, in the context of this limitation, only up until one year after the date of the merger or the establishment of the close link. (*Amendment 1 January 2012*)

3.2.3.3 Risk control measures for non-marketable assets

The risk control framework for eligible credit claims includes the following main elements:

- Individual credit claims are subject to specific valuation haircuts. The haircuts differ according to the residual maturity, type of interest payment (fixed or variable), the credit quality category and the valuation methodology applied by the national central bank, as described in Table 3.⁹ The methodology applied by the Bank of Finland is based on the outstanding amount.
- The valuation haircuts applicable to credit claims with fixed rate interest payments may also be applied to credit claims the interest payments of which are linked to the inflation rate.
- The haircut applied to credit claims with variable rate interest payments is that applied to the credit claims with fixed interest payments classified in the zero-to-one-year maturity bucket in Table 3. An interest payment is considered a variable rate payment if it is linked to a reference interest rate and if the resetting period corresponding to this payment is no longer than one year.
- Interest payments for which the resetting period is longer than one year are treated as fixed rate payments in Table 3, with the relevant maturity for the haircut being the residual maturity of the credit claim.
- The risk control measures applied to a credit claim with more than one type of interest payment depend only on the interest payments during the remaining life of the credit claim. If there is more than one type of interest payment during the remaining life of the credit claim, the remaining interest payments are treated as fixed rate payments, with the relevant maturity for the haircut being the residual maturity of the credit claim.

(Amendment 1 January 2011)

⁹ The valuation haircuts applied to credit claims with fixed rate interest payments are also applicable to credit claims, the interest payments of which are linked to the inflation rate.

Table 3. Levels of valuation haircuts applied to credit claims with fixed interest payments (*Amendment 1 January 2011*)

Credit quality	Residual maturity (years)	Valuation methodology	
		Fixed interest payment and valuation based on a theoretical price assigned by the NCB	Fixed interest payment and valuation based on the outstanding amount assigned by the NCB
Steps 1 and 2 (AAA–A-)	0-1	8.0	10.0
	1-3	11.5	17.5
	3-5	15.0	24.0
	5-7	17.0	29.0
	7-10	18.5	34.5
	>10	20.5	44.5
Step 3 (BBB+–BBB-)	0-1	15.5	17.5
	1-3	28.0	34.0
	3-5	37.0	46.0
	5-7	39.0	51.0
	7-10	39.5	55.5
	>10	40.5	64.5

Non-marketable retail mortgage-backed debt instruments are subject to a valuation haircut of 24%. (*Amendment 1 January 2011*)

Fixed-term deposits

Fixed term deposits are not subject to any valuation haircut. (*Amendment 1 January 2011*)

3.2.3.4 Pricing and valuation principles for collateral

Marketable assets

The Bank of Finland calculates the value of marketable assets on the basis of the price quoted at 12.00 noon on the business day preceding the valuation date. In this calculation, the following principles are applied:

- For each eligible marketable asset, central banks define one reference market place to be used for the calculation of the market value. If securities are listed, quoted or traded on more than one market place, the lowest quotation (normally the bid price) is used for the calculation of the price.
- Central banks define the most representative price of each market place to be used in the calculation of the market value.
- The value of a marketable asset is calculated on the basis of the most representative price of the market place on the business day preceding the valuation date.
- In the absence of a representative price for a particular asset on the business day preceding the valuation date, the last trading price is used. If the trading price is not available or if the reference price obtained is older than five days or if it has not changed in the last five days, a theoretical price is defined.
- The market or theoretical value of a debt instrument is calculated including accrued interest.
- The income flows on assets pledged to the Bank of Finland are transferred to the counterparty if permitted by the collateral coverage of the counterparty. *(Amendment 10 October 2010)*

Non-marketable assets

Non-marketable assets are assigned a value corresponding either to the theoretical price or to the outstanding amount. The latter method is used by the Bank of Finland.

If the national central bank opts for the valuation corresponding to the outstanding amount, the non-marketable assets may be subject to higher haircuts (see Section 3.2.3.2, Table 3).

3.2.3.5 Sanctions

If the counterparty uses ineligible assets as collateral or assets where the issuer, debtor or guarantor is the counterparty itself or an entity with which it has close links (see the definition of close links in Section 3.2.1.4), the Bank of Finland has the right to order the counterparty to pay additional interest equivalent to the interest for the marginal lending rate plus 2.5 percentage points. The following rules shall also be applied where the information provided by a counterparty on, for example, the outstanding amount of the underlying credit claim proves erroneous or outdated or reduces the collateral value. *(Amendment 10 October 2010)*

For the first and second time within a 12-month period that the counterparty uses as collateral assets that are not eligible or assets that the counterparty may not use as collateral, the additional interest shall be computed for the total amount of ineligible assets provided that the collateral has not been replaced with eligible assets within 20 banking days from the date when they became ineligible to the counterparty in question or from the date when the counterparty could no longer use them as collateral. The coefficient used in the computation is 1/360. In the event of repeated use of three times or more of assets deemed ineligible, the counterparty in question may be excluded from the next open market operation in addition to the application of the additional interest. In exceptional cases where the infringement of rules can be considered serious, the counterparty in question may be excluded from all open market operations for the period of three months in addition to the application of the additional interest.

Counterparties are obliged to inform the Bank of Finland of possible close ties emerging between the issuer, debtor or guarantor of an eligible asset pledged by the counterparty to the Bank of Finland¹⁰. Counterparties must also inform the Bank of Finland of transfers of such assets to their automatic collateral management account at the Central Securities Depository. Only one notification is needed for each asset. The phone numbers of Bank of Finland contact persons are listed in Annex 8.

If infringements by the counterparty give rise to several types of sanctions, only one sanction shall be applied, which will generally be the most severe one.

An example of an infringement of rules concerning collateral

An inspection carried out by a national central bank reveals that counterparty X has collateral issued by an entity with close ties to the counterparty, and the counterparty has not replaced this collateral within 20 days from the date when close ties were formed. The collateral is valued at EUR 27 million¹¹. The rate for the marginal lending facility at the time of inspection is 4.5%.

Solution: additional interest applicable to X is

$$27\,000\,000 \times \frac{4.5 + 2.5}{100} \times \frac{1}{360} = 5\,250$$

¹⁰ In this case, the collateral value of an underlying asset is computed as zero on the next valuation day, and the central bank may have to ask for additional collateral.

¹¹ For marketable assets, this is the market value. For non-marketable assets, the value is the collateral value of the assets in monetary policy operations after the application of risk management methods (valuation haircuts).

3.2.4 Acceptance of non-euro-denominated collateral in contingencies

In certain situations the Governing Council may decide to accept as eligible collateral certain marketable debt instruments issued by one or more non euro area G10 central governments in their domestic currency. Upon such decision the applicable criteria shall be clarified and the procedures to be applied for the selection and mobilisation of foreign collateral, including the sources and principles of valuation, the risk control measures and the settlement procedures shall also be communicated to counterparties.

Notwithstanding the provisions of section 3.2.1.2, such assets may be deposited/registered (issued), held and settled outside the EEA and, as stated above, may be denominated in currencies other than the euro. Any such assets used by a counterparty must be owned by the counterparty.

Counterparties that are branches of credit institutions incorporated outside the EEA or Switzerland cannot use such assets as collateral. (*Amendment 10 October 2010*)

Annex 1

WEBSITES OF EURO AREA CENTRAL BANKS

European Central Bank	www.ecb.europa.eu
Nationale Bank van België/Banque Nationale de Belgique	www.nbb.be or www.bnb.be
Deutsche Bundesbank	www.bundesbank.de
Eesti Pank	www.eestipank.ee
Banc Ceannais na hÉireann/Central Bank of Ireland	www.centralbank.ie
Bank of Greece	www.bankofgreece.gr
Banco de España	www.bde.es
Banque de France	www.banque-france.fr
Banca d'Italia	www.bancaditalia.it
Central Bank of Cyprus	www.centralbank.gov.cy
Banque centrale du Luxembourg	www.bcl.lu
Bank Ċentrali ta` Malta / Central Bank of Malta	www.centralbankmalta.org
De Nederlandsche Bank	www.dnb.nl
Oesterreichische Nationalbank	www.oenb.at
Banco de Portugal	www.bportugal.pt
Národná banka Slovenska	www.nbs.sk
Banka Slovenije	www.bsi.si
Suomen Pankki	www.bof.fi



Annex 2

External credit risk assessment institutions used by the Eurosystem

The following external credit risk assessment institutions (ECAIs) are used by the Eurosystem in assessing the eligibility of assets as collateral:

DBRS

Fitch Ratings

Moody's Investors Service

Standard & Poor's

Annex 3

Collateral Management opening hours and deadlines

Opening hours

The Bank of Finland's Collateral Management observes the opening hours of TARGET2-Suomen Pankki.

Marketable collateral administered via collateral management accounts at the Euroclear Finland Ltd may be increased or decreased during the opening hours of the Euroclear Finland Ltd.

Foreign collateral may be increased or decreased in accord with the correspondent central banking model (CCBM). This system opens for business at 10.00 am and closes at 5.00 pm, but requests for receipt of collateral with same day value must be received by the Bank of Finland's Collateral Management Service Desk no later than 4.30 pm on the desired value date.

Transfers of foreign marketable collateral via eligible links with same day value must be recorded in the Euroclear Finland Ltd's system by 4.00 pm at the latest.

Details on domestic credit claims can be transmitted to the Bank of Finland during the opening hours of TARGET2- Suomen Pankki, but details intended to be updated on the same day must be received by the Bank of Finland by 5.00 pm.

Deadlines

Collateral assets are valued by the Bank of Finland daily by 12 noon at the latest on the basis of market prices for the preceding day. Account holders' collateral positions are verified at the same time.

Annex 4

Collateral management messages – marketable assets

I Use of domestic marketable assets

When a Bank of Finland counterparty wishes to make changes in the amount of collateral in its collateral management account administered at the Euroclear Finland Ltd and pledged to the Bank of Finland, the counterparty must inform the Bank of Finland's Collateral Management Customer Service by phone (+358 10 831 2171) and confirm such change either by SWIFT or fax (+358 10 831 2920).

II Use of foreign marketable assets

When a counterparty of the Bank of Finland wishes to increase or decrease the foreign marketable assets held in a pool of assets at the Bank of Finland by using the CCBM, the counterparty must so inform the Bank of Finland by phone (+358 10 831 2171), providing details of the assets serving as collateral to the Bank of Finland's Collateral Management Customer Service by fax (+358 10 831 2920) or SWIFT, in accord with the enclosed instructions (Annex 4, page 3).

The counterparty must simultaneously contact the foreign custodian for such assets, requesting the custodian to transfer the assets to the account of the central bank of the country where the custodian is located in favour of the Bank of Finland. On the other hand, if collateral assets are withdrawn from the pool, the counterparty must inform the custodian of receipt of assets.

Once the Bank of Finland receives a confirmation of the final transfer of assets from the central bank of the concerned country, the value of the assets will be added to the pool of the counterparty.

When the counterparty wishes to withdraw foreign assets from its pool, the value of the assets will be deducted from the pool account immediately upon receipt by the Bank of Finland of the counterparty's written confirmation.

When a counterparty of the Bank of Finland wishes to deliver collateral assets to its automatic collateral management account with the Euroclear Finland Ltd by making use of links, the counterparty must request its foreign custodian to deliver the assets via an appropriate central securities depository to its account with the Euroclear Finland Ltd. Assets delivered via links are administered at the Euroclear Finland Ltd and the Bank of Finland in the same manner as domestic assets.



Receiver

Bank of Finland

Tel: + 358 10 831 2171

TARGET/Collateral Management Customer Service

Fax: + 358 10 831 2920

NOTIFICATION OF A CHANGE IN THE AMOUNT OF COLLATERAL HELD IN AN EUROCLEAR FINLAND LTD ACCOUNT/THE OVERDRAFT LIMIT

Bank name: _____

Sender telephone number: _____

Sender name: _____

Date: _____

Change in the amount of collateral held in an Euroclear Finland Ltd account	
Collateral management account number:	
Value date of change:	
Existing amount (EUR):	
Change (EUR):	
New amount (EUR):	

Change in overdraft limit (RTGS limit)	
Value date of change:	
Existing amount (EUR):	
Change (EUR):	
New amount (EUR):	

Confirm the arrival of the fax by calling TARGET/Collateral Management Customer Service.

Signature

Signature

Name in block letters

Name in block letters



Receiver

Bank of Finland

TARGET/Collateral Management Customer Service

Tel: + 358 10 831 2171

Fax: + 358 10 831 2920

NOTIFICATION OF THE USE OF FOREIGN ASSETS

Bank name: _____

Sender telephone number: _____

Sender name: _____

Date: _____

Use of foreign assets	
Increase of assets <input type="checkbox"/> Return of assets <input type="checkbox"/>	
Trade date	
Settlement date	
ISIN code	
Issuer	
Nominal value of securities	
Maturity date	
Next interest payment date	
BIC code and account number of sender	
BIC code of custodian	
Securities settlement system (SSS)	

Confirm the arrival of the fax by calling TARGET/Collateral Management
Customer Service

Signature

Signature

Name in block letters

Name in block letters



Annex 5

Notification of pledge concerning credit claims

In the event that a counterparty wishes to add a new credit claim to the pool of assets, update previously supplied credit claim details or withdraw a credit claim from the pool of assets, the Bank of Finland Collateral Management Customer Service must be informed by telephone on +358 10 831 2171 and by telefax on +358 10 831 2920, using the notification of pledge below.

Alternatively, counterparties may provide the information via SWIFTNet FileAct using an electronic template/format message specified by the Bank of Finland in separate instructions. The counterparty may request further instructions for the introduction of the template/format message from the Bank of Finland. If the template/format message sent does not comply with the current Bank of Finland specifications, the Bank of Finland shall not be liable for any possible damages arising therefrom.



NOTIFICATION OF PLEDGE CONCERNING CREDIT CLAIMS

Recipient

Bank of Finland
TARGET/Collateral
Management Customer Service

Tel: +358 10 831 2171
Fax: +358 10 831 2920

SENDER DETAILS

Name	
Bank	
Telephone	
Fax	

SUBMISSION OF CREDIT CLAIM DETAILS

Credit claim ID			
Action	<input type="checkbox"/> New pledge	<input type="checkbox"/> Data update	<input type="checkbox"/> Unwinding of pledge
Submission date			

CREDIT CLAIM DETAILS

Date of signing of agreement			
Date of maturity			
Outstanding amount	EUR		
Legal nature of the credit claim in Finnish legislation	<input type="checkbox"/> Ordinary promissory note	<input type="checkbox"/> Negotiable promissory note	
Coupon type	<input type="checkbox"/> Fixed or zero rate	<input type="checkbox"/> Floating rate	
Resetting period in the case of floating rate	<input type="checkbox"/> ≤ 1 year	<input type="checkbox"/> > 1 year	

DEBTOR DETAILS

Name						
Business ID						
Country of location						
Sector of business	<input type="checkbox"/> Central government	<input type="checkbox"/> Other general govt.	<input type="checkbox"/> Corporation (non-financial, non-insurance)			
Credit risk assessment source	<input type="checkbox"/> Internal ratings-based system (IRBA)	<input type="checkbox"/> Moody's	<input type="checkbox"/> S&P	<input type="checkbox"/> Fitch	<input type="checkbox"/> DBRS	
	<input type="checkbox"/> General govt. class (PSE) 1	<input type="checkbox"/> General govt. class (PSE) 2	<input type="checkbox"/> Third-party rating tool (RT)			
PD% / credit rating						
IRB credit assessment date						



GUARANTOR DETAILS

Name						
Business ID						
Country of location						
Sector of business	<input type="checkbox"/> Central government	<input type="checkbox"/> Other general govt.	<input type="checkbox"/> Corporation (non-financial, non-insurance)			
Credit risk assessment source	<input type="checkbox"/> Internal ratings-based system (IRBA)	<input type="checkbox"/> Moody's	<input type="checkbox"/> S&P	<input type="checkbox"/> Fitch	<input type="checkbox"/> DBRS	
	<input type="checkbox"/> General govt. class (PSE) 1	<input type="checkbox"/> General govt. class (PSE) 2	<input type="checkbox"/> Third-party rating tool (RT)			
PD% / credit rating						
IRB credit assessment date						

SIGNATURES (signature and blocked letters)

--	--

INSTRUCTIONS FOR COMPLETING THE NOTIFICATION OF PLEDGE CONCERNING CREDIT CLAIMS

All compulsory fields must be filled in every time.

Sender details

Name, telephone and telefax number of the person and bank submitting the notification of pledge are compulsory fields.

Submission of credit claim details

All fields concerning the delivery of credit claim are compulsory.

Credit claim ID: Identification code, which must remain the same and be known to the bank and debtor.

Action: New pledge = addition of a new credit claim to the pool of assets; Data update = updating of information due to changes in credit details; Unwinding of pledge = removal of credit claim from the pool of assets

Submission date: Date when notification of pledge was sent to the Bank of Finland

Credit claim details

All fields concerning the credit claim details are compulsory.

Date of signing of agreement: The date of signing of the promissory note. Note that the credit claim is eligible as collateral only after it is drawn.

Date of maturity: Date when the last instalment of the credit claim falls due in accordance with the valid payment plan.

Outstanding amount: The amount of the loan still due, EUR XXX. At the time of submission for use as collateral, the outstanding amount of a credit claim must amount to EUR 500 000 at a minimum.

Legal nature of the credit claim in Finnish legislation: Indicate whether the promissory note is ordinary or negotiable. This determines the measures needed for pledging of the credit claim.

Coupon type: Indicate whether the rate is fixed or floating.

Resetting period in the case of floating rate: For loans with a floating rate, specify whether the coupon rate is determined more or less frequently than once a year.

Debtor details

The following fields are always compulsory: 'Name', 'Business identity code', 'Country of location' and 'Sector of business'. The business identity code consists of seven digits, a hyphen

and an inspection number, eg 1234567-8. The country of location is a two-letter country code¹.

The fields 'Credit risk assessment source', 'PD% / credit rating' and 'IRB credit assessment date' can be left empty if the counterparty is accepting the loan as collateral on the basis of the credit worthiness of the guarantor rather than the debtor.

Credit risk assessment source: Indicate the relevant credit risk assessment source, which

¹ The ISO codes of the countries belonging to the euro area are the following: BE, CY, DE, GR, ES, FR, IE, IT, LU, MT, NL, AT, PT, SI, and FI.

must have prior approval from the Bank of Finland. General government entities without a public credit rating and having the same FIN-FSA capital adequacy risk value as central government or (credit) institutions, are assigned General government classes 1 and 2.

PD% / credit rating: Fill in the default probability of debtor with accuracy of three decimals, eg 0.100%, or give the credit rating of an external credit assessment institution, such as A3 or A-. The PD% or credit rating is not needed if the credit assessment source is General government class 1 or 2.

IRB credit assessment date: If the credit assessment source is an internal ratings-based system, the date of the credit assessment must be given. If the source is of other type, this field can be left empty.

Guarantor details

If the loan has a guarantor, the following fields are always compulsory: 'Name', 'Business identity code', 'Country of location' and 'Sector of business'. The business identity code consists of seven digits, a hyphen and an inspection number, eg 1234567-8. The country of location is a two-letter country code.

The fields 'Credit risk assessment source', 'PD% / credit rating' and 'IRB credit assessment date' are compulsory, if the eligibility of the loan is determined on the basis of the credit worthiness of the guarantor. In this case, the counterparty must submit to the Bank of Finland in advance a guarantee and/or a legal confirmation of a form and content acceptable to the Eurosystem.

Credit risk assessment source: Indicate the relevant source. Note that prior acceptance for use of the source must be obtained from the Bank of Finland.

PD% / credit rating: Fill in the default probability of debtor with accuracy of three decimals, eg 0.100%, or give the credit rating of an external credit assessment institution, such as A3 or A-. The PD% or credit rating is not needed if the credit assessment source is General government class 1 or 2.

IRB assessment date: If the credit assessment source is an internal ratings-based system, the date of the credit assessment must be given. If the source is of other type, this field can be left empty.

Annex 6

Bank of Finland's Terms and Conditions: Use of non-marketable assets via correspondent central banking model

Terms & Conditions of Bank of Finland, when acting as CCB

Counterparties may use credit claims to collateralise Eurosystem credit operations on a cross-border basis (ie counterparties may obtain funds from their respective home central bank (HCB) – the national central bank of the Member State where they are located – by making use of credit claims governed by a law other than the national law of the HCB). The national central bank of the country whose law governs the credit claim acts as correspondent central bank (CCB).

The following provisions apply when the Bank of Finland acts as CCB. Some of these provisions may not apply to all NCBs.

Eurosystem counterparties that wish to use, as collateral in credit operations with other Eurosystem NCBs, credit claims governed by Finnish law have to comply with the following provisions, which complement the terms and conditions currently applicable between counterparties and their respective HCB.

When the HCB provides interface services between its counterparties and the CCB, the HCB is purely acting as the messenger for the counterparty without taking any responsibility. The obligation to comply with the requirements – in particular the legal requirements – remains with the counterparty.

1. Legal requirements

- a) The legal technique used for the creation of a security interest is pledge.
- b) Depending on the juridical type of the credit claim, different legal arrangements are needed in order to create a valid pledge. Notification of the debtor (and the guarantor) prior to the mobilisation of the credit claims is required in case of ordinary promissory notes. However, notification is not required if negotiable promissory notes are used as collateral.
- c) When another NCB (which is not the CCB) plays the role of HCB, notification/registration may also be required, in accordance with the requirements of the conflict of law rules of the HCB and/or the CCB. Registration/notification will be performed according to the rules of the jurisdiction that requires registration/notification.
- d) Notification to the debtor after the mobilisation of the credit claim is required following certain events (eg event of default and similar events).
- e) To fulfil the requirements regarding the enforcement of the security interest, in case of negotiable promissory notes, an endorsement of the original credit claim have to be done on behalf of the HCB.
- f) The rules that have to be observed regarding the management of the collateral are presented in the Bank of Finland rules for counterparties and account holders.
- g) The credit claim agreement needs to fulfil the general requirements set out in the Bank of Finland rules for counterparties and account holders.
- h) The other requirements that need to be fulfilled for the purpose of creating valid and enforceable security interest over the credit claim are presented in the Bank of Finland rules for counterparties and account holders.

2. Operational requirements

- a) The counterparty has to submit to the Bank of Finland a list of authorised signatures directly/via the HCB.
- b) The counterparty has to indicate to the Bank of Finland the ECAF sources/system used for assessing credit claims, when sending the information on credit claims to the Bank of Finland.
- c) To use credit claims on a cross-border basis, the counterparty has to send to the Bank of Finland the credit claim information according to the template/format message presented in the Bank of Finland rules for counterparties and account holders.
- d) The template/format message has to be sent via fax / SWIFTNet FileAct by 16.00 CET.
- e) The counterparty undertakes to preserve with due diligence and in a safe custody any credit claims pledged to the benefit of the HCB, including attached collateral and other documentation.
- f) Each credit claim and debtor/guarantor has to be assigned a standard identification number. This is assigned by the Bank of Finland on the basis of the credit claim identification number/business identity code used by the counterparty.
- g) Credit claims will be accepted once their eligibility has been checked and notification/endorsement of the credit claim documentation is confirmed.
- h) By the end of the business day following the acceptance, counterparties will receive confirmation about the value assigned to the accepted claims from the CCB/HCB, which will then be available for use as collateral in credit operations with the respective HCB.
- i) Counterparties have to promptly communicate to the Bank of Finland any change which affects the eligibility and valuation of the credit claim. This update can be done by sending via fax/SWIFTNet FileAct the template/format message presented in the Bank of Finland rules for counterparties and account holders.
- j) To ensure that credit claim details are continuously updated, counterparties have to re-submit the full set of details on the credit claims every time that any change occurs by using the procedure explained in point (c) above.
- k) Counterparties will receive from the relevant HCB/CCB periodical reporting about the outstanding amount of collateral deposited and available for further use.
- l) In case of withdrawal of credit claims, the counterparty must instruct the Bank of Finland. Furthermore, in order to unwind the pledge, a new notification needs to be sent to the debtor/ the endorsement needs to be done by the HCB.

In addition to these Terms and Conditions, the foreign counterparties wishing to use as collateral credit claims governed by the Finnish law have to follow the detailed instructions and templates described in the publication "Bank of Finland rules for counterparties and account holders" (http://www.bof.fi/eng/6_julkaisut/6.1_SPh_julkaisut/6.1.8_Ohjeet_ja_saannot/index.stm) that applies to the domestic counterparties as well.

Terms & Conditions of Bank of Finland, when acting as Assisting NCB

The following provisions apply when Bank of Finland acts as Assisting NCB (ACB), ie in those situations where the debtor/guarantor/creditor is located in Finland, but the credit claim agreement is governed by the law of another country.

These provisions complement the terms and conditions currently applicable between counterparties and their respective home central bank (HCB).

- a) Notification of the debtor (and the guarantor) prior to the mobilisation of the credit claims is required, if the credit claim qualifies as an ordinary promissory note according to the Finnish legislation. Notification can be performed following the procedures agreed between the counterparty and its home central bank.
- b) When another NCB plays the role of HCB, notification/registration may also be required, in accordance with the requirements of the conflict of law rules of the HCB and/or the ACB. Registration/notification will be performed according to the rules of the jurisdiction that requires registration/notification.
- c) Notification to the debtor after the mobilisation of the credit claim is required following certain events (eg event of default and similar events).

Annex 7

Example: Calculation of a collateral requirement and valuation of collateral assets

I Calculation of total collateral requirement

Intraday total collateral requirement:

A Bank of Finland counterparty is granted an overdraft limit of EUR 1,000, 000 on its PM account and a credit of EUR 1,000,000 in connection with a tender at an interest rate of 3.5%. The maturity of the credit is 14 days.

Intraday overdraft limit	1,000,000.00
Credit	1,000,000.00
Interest on the credit, 1 million x 14/360 x 3.5% =	1,361.10

Total collateral requirement **2,001,361.10**

II Valuation of collateral assets

Both domestic and foreign assets are valued daily by 12 noon at the latest on the basis of market prices for the preceding day. The value of collateral assets must always cover the total collateral requirement.

15 January 1999

1) The amount of collateral held in an Euroclear Finland Ltd collateral management account and pledged to the Bank of Finland, valued at market prices, in respect of which the Euroclear Finland Ltd automatically takes into account valuation haircuts defined by the ECB 2,000,000

2) Market value of foreign assets ² according to prices quoted on 14 January	1,863,000
Valuation haircut ³ subtracted	-162,000
	<u>1,701,000</u>

Total collateral value of assets on 15 January (1 + 2) **3,701,000**

² That is the total amount of foreign assets held by the counterparty in a pool of assets with the Bank of Finland.
³ The sum of valuation haircuts applied to all assets in the pool.

16 January 1999

- 1) The amount of collateral held on an Euroclear Finland Ltd collateral management account and pledged to the Bank of Finland, valued at market prices, in respect of which the Euroclear Finland Ltd automatically takes into account valuation haircuts defined by the

ECB 2,000,000

- 2) Market value of foreign assets

according to prices quoted on 15 January

1,843,000

Valuation haircut

-159,000

1,684,000

Total collateral value of assets on 16 January (1 + 2)

3,684,000



Annex 8

Collateral management contact persons

Collateral Management Customer Service

tel. +358 10 831 2171

fax +358 10 831 2920

Email addresses:

Collateral Management Customer Service

t2service@bof.fi

Enquiries regarding eligibility

eligibleassets@bof.fi

Legal matters: Eija Brusila

tel. +358 10 831 2786