UNDERWRITING RISK

Introduction

1. A credit institution which is involved in the underwriting of debt, and/or equity, and/or other securities issues may take significant direct exposures, to the issuer and to the market place, which in the normal course of events can be expected to reduce quickly through sales, or by obtaining underwriting commitments from other firms. Underwriting is therefore to be included within the trading book.

2. The underwriting process, whether of bonds, equities or other securities, normally has a common set of events:

    Announcement Date
    Launch Date
    Commitment Date
    Allotment Date
    Subscription Date
    Closing Date
    Payment Date

    These events may occur with different time gaps between them depending upon particular aspects of the underwriting mechanism. For example the gap between the Announcement Date and the Launch Date may be negligible for a bond underwriting, but may be several days for an equity underwriting.

Underwriting

3. In the case of the underwriting of debt and equity instruments, the authority may allow an institution to use the following procedure in calculating its capital requirements. Firstly, it shall calculate the net positions by deducting the underwriting positions which are subscribed or sub-underwritten by third parties on the basis of formal agreements. Secondly, it shall reduce the net positions by the reduction factors in Table 1.

Table 1

working day 0:	100%
working day 1:	90%
working days 2 to 3:	75%
working day 4:	50%
working day 5:	25%
after working day 5:	0%

'Working day zero' shall be the working day on which the institution becomes unconditionally committed to accepting a known quantity of securities at an agreed price.

Thirdly, it shall calculate its capital requirements using the reduced underwriting positions.

The authority shall ensure that the institution holds sufficient capital against the risk of loss which exists between the time of the initial commitment and working day 1.

Credit institutions shall set up systems to monitor and control their underwriting exposures between the time of the initial commitment and working day one in the light of the nature o the risks incurred in the markets in question.