

Feedback on Tri Party Discussion Paper on Basel III, issued September 2012

1 Summary

- 1.1 Responses received from all Jersey incorporated banks except:
 - 1.1.1 A small number of banks where the operation is very small
 - 1.1.2 A small number of banks that were planning to cease operations in the near future
- 1.2 One response was received from an industry body but this has been excluded as it did not respond to the questions raised, instead expressing concern regarding the implementation of Basel III by consolidating supervisors and seeking changes in Basel III in respect of liquidity requirements.

2 LIQUIDITY

3.7.1 Do you expect to be part of a group that is subject to consolidated supervision of liquidity by a supervisor that has adopted the Basel III liquidity standard? If so, are there any specific aspects that should be considered locally?

- 2.1 Most highlighted the fact that their groups would be subject to CRD IV reporting and that consistency with CRD IV was most important.
- 2.2 A minority of respondents said that the core Basel III measures should apply at the consolidated level only.
- 2.3 A smaller number said that their group view was that Basel III should be implemented at entity level (referred to later in this paper as “**entity level adopters**”).
- 2.4 The remainder expressed no opinion.

3.7.2 Would further alignment of the liquidity regimes across the CDs be beneficial to banks?

- 2.5 Many favoured greater consistency, principally in respect to reporting procedures and definitions. A minority called for this to go further – aligning behavioural adjustments, say – in order to avoid regulatory arbitrage and one called for a consolidated, pan island approach as being the ideal.
- 2.6 Some banks also called for alignment with either the FSA or CRD IV, again focussing on reporting and definitions.

3.7.3 Are there any specific changes to the current regime that you would like to see?

- 2.7 Entity level adopters called for close alignment with Basel III/CRD IV.

2.8 A small number expressed concern regarding the treatment of intermediated deposits, where adjustments had either not been allowed currently (as they were considered to be wholesale) or would be disallowed under Basel III (as they might not be deemed operational deposits). One bank perhaps summed this up best by calling for a clearer, more transparent and hence possibly leveller treatment of intermediary deposits.

2.9 The matter of maturity term in relation to residual vs original maturity was raised – surprisingly as it does not affect liquidity.

4.3.1 For Guernsey and Jersey incorporated banks only, what issues would arise for your bank if the local requirement for the one month liquidity mismatch was amended to remove the allowance of a small net outflow to one month, in line with Basel III and IOMFSC?

2.10 Respondents were almost evenly split between those saying that the impact would be minimal and those saying it would impact on profitability, as more liquidity would need to be held. In particular, it was noted that the impact would be larger if the liquidity had to be held locally in the form of low yielding liquid assets.

4.4.1 Do you envisage using marketable assets as part of liquidity management?

2.11 Around half did now or intended to, including both currently independent banks and a minority who felt that group would require this.

2.12 The remainder intended to rely on group, some pointing out that their group managed liquidity centrally. These stressed the impact of a change, without providing details.

4.4.2 If so, please consider whether these would meet the criteria set out in Basel III. Please also explain the criteria that you currently use to determine marketability, including any restrictions in respect of concentration risk.

2.13 Only one bank said that it held a low level of ineligible assets.

2.14 Several banks highlighted the importance of concentration risk but this was principally in respect of their centrally held portfolios – i.e. asserting that these could be more strictly managed. One bank also set out other criteria – such as central bank repo access – but, again, these appeared to relate to its group’s portfolio requirements, not any local rules.

4.7.1 Do you consider that deposit behaviour should be assessed centrally or on a bank by bank basis?

2.15 General consensus was that behaviour should be assessed on a bank by bank basis.

2.16 Respondents differed regarding the degree of flexibility ideally permitted though, with some favouring a Pillar 1 plus Pillar 2 type approach (i.e. with standard adjustments as a starting point) whilst other favoured the current (Pillar 2 only) approach.

4.7.2 Do you consider that there are specific criteria that should be established (beyond the generic designation of retail and corporate deposits) to identify “sticky” deposits, such as size and nature of relationship? If so, should these be established across the CDs, by each supervisor or on a bank-by-bank basis?

2.17 There was a broad agreement that more guidelines were required, particularly to ensure a consistent approach across the CDs. There was not much of a consensus on what the guidelines should be or on how detailed they should be, with small numbers of banks mentioning ideas such as: increased granularity (assumed to mean defining different types of sticky and less sticky deposits) and clearer definitions of the relevant criteria. Several banks opposed the Basel III criteria around the definition of operational deposits.

4.7.3 *Would the Basel III LCR measure be appropriate for your bank?*

2.18 Only entity level adopters favoured adoption, with the rest (a clear majority) stating that the LCR was inappropriate at a solo level. Some of these specified that the main issue was that liquidity would be captured at a local level – i.e. principally, the objection was to the liquid asset requirement, not the calculation.

5.4.1 *Do you use similar liquidity ratio calculations within your current approach to longer term liquidity management? If so, please provide a brief summary and highlight key differences to the NSFR standard.*

2.19 Entity level adopters were the only banks with positive responses and these said, unsurprisingly, that they were working towards NSFR adoption in due course and provided limited details on current metrics – simpler ratios of customer loans to customer deposit.

2.20 The majority did not report and opposed reporting at solo level.

6.2.1 *Would it be helpful if reporting requirements were closely aligned across the CDs?*

2.21 No opposition and some very positive responses.

6.2.2 *Would it be useful to align the reporting of liquidity data / metrics more closely to the Basel III liquidity standard requirements and/or to requirements specified by other bodies?*

2.22 The majority supported close alignment to ease consolidated reporting or because they would need to comply with group reporting standards. A small number opposed on cost ground.

6.2.3 *Would a requirement to provide data on liquid assets present any specific issues?*

2.23 No opposition (though a couple re-iterated their opposition to there being a requirement).

6.2.4 *Would reporting data on a currency by currency basis be problematic? If so, how could this be limited to provide data on material liquidity mismatches whilst minimising the cost of implementation?*

2.24 All felt they could implement with a significant number saying that a materiality cut-off would reduce costs, with a small number saying that materiality cut-offs would not work. Other than the cost of implementation, no problems were cited.

6.2.5 *What problems would a move to require that banks be able to make more regular submission of liquidity data present (for specific reports and only where considered to be necessary)? In particular, does your current daily internal reporting provide sufficient data to enable completion of the current regulatory templates?*

2.25 Respondents divided into those that could do this now, those that considered that this could be done in due course and those that either could not do this or considered that the cost would be disproportionate.

2.26 Several, including those opposed, said that group plans might ease this over the course of the next few years provided that requirements could be aligned.

3 CAPITAL

7.5.1 *Do you expect to be part of a group that is subject to consolidated supervision of capital requirements by a supervisor that has adopted the Basel III capital standard? If so, are there any specific aspects that should be considered locally?*

3.1 All would be part of groups that expected to be regulated to Basel III standard at consolidated level, with a, similarly to liquidity, many mentioning CRD IV.

3.2 Several mentioned that the SIFI requirements would not extend and several also said that specifics were uncertain, including how this might impact on entities locally.

7.5.2 *Would further alignment of the regimes in the CDs be beneficial and, if so, in which areas?*

3.3 Most favoured alignment either for practical or regulatory arbitrage reasons, with none opposed.

3.4 One bank requested further alignment with the UK/EU – although it is inferred, given other responses, that this primarily relates to the treatment of residual maturity for bank exposures.

7.5.3 *Are there any specific changes to current local capital adequacy requirements that you would like to see?*

3.5 A small number re-raised the issue of the treatment of residual maturity for bank exposures.

3.6 Other banks raised entity specific issues, which mainly relate to Pillar 2 matters.

3.7 A small number either called for the minimum to be aligned or for buffers to be treated more flexibly.

8.5.1 *Would the application of CET1 capital stated in the Basel III capital standard have a significant impact on your current capital or on capital planning (also see section 9, capital minima)?*

3.8 Most considered that this would present no material issues. One stated that it still opposed the introduction, as the added complexity was not warranted. Two banks said there might be issues with existing capital (preference shares and tier 2 capital), without expressing a high degree of concern over this issue as both issued the capital internally.

8.8.1 Would the specifications of additional issued Tier 1 and Tier 2 capital stated in the Basel III capital standard have a significant impact on your bank's total available regulatory capital or on capital planning?

3.9 All felt that any impact would be either negligible or could be managed, for example by re-issuing internal capital so that it was compliant.

8.8.2 Would the removal of Tier 3 capital have a significant impact on your bank's total available regulatory capital or on capital planning?

3.10 Only one bank impacted, which did not envisage any significant impact.

8.8.3 Are there any impediments, legal or otherwise, to issuing capital that meets the criteria set in the Capital FAQ?

3.11 Nothing identified

8.9.1 Would implementation locally within these timeframes present a problem?

3.12 No objections identified, with one proviso (from one bank) that minima are not increased at the same time.

8.9.2 Would a simpler transitional framework be appropriate, particularly where no such instruments currently exist?

3.13 Excluding those unaffected, the majority favoured following Basel III or CRD IV, with a minority favouring a simpler approach.

9.14.1 Would you support a move to using a single CET1 ratio for Pillar 1, instead of a framework of minima and buffers? If so, what level do you consider would be appropriate?

3.14 In general, there was support, with most agreeing with the arguments put forward.

3.15 Only one bank opposed the idea, instead suggesting that no changes be made, given existing regime already allowed for additional capital to be required.

3.16 Of those banks that developed the idea further, several favoured a level in line with current levels or explicitly stated that 10% would be appropriate. One stated that a level of 7%, in line with the minimum for Basel III (excluding conservation buffers, G-SIFI requirements and D-SIFI requirements).

3.17 One bank raised the issue that CFC regulations that have already been introduced in the UK appear to target offshore banks with a higher tier 1 capital than their UK parent and seeking a cap to limit the impact of this.

9.14.2 What timescale would provide sufficient time to enable a smooth transition?

3.18 Some respondents saw no need for a transition, whilst others favoured timescales running from 12-18 months to the CRD IV timeline.

3.19 Two banks responded along the lines that it depended on the exact details but that time should be allowed for banks to meet any actual increases that were a consequence of any changes made.

4 Trading Book and other RWA related changes

10.1.1 If you currently have a trading book or plan to do so, please provide a brief summary of your home supervisor's communicated plans.

4.1 One bank outlined the FSA's established plan, which only addresses the part of the plans that relate to its, relatively simple, operations.

11.2.1 Do you have, or plan to have, any re-securitisation exposure or exposure to central clearing parties? If so, please comment on the desirability and impact of these changes.

4.2 No exposures identified or envisaged.

11.6.1 Would you support the removal of the simplified standardised approach in the CDs, over the medium term, once it is no longer in use or do you believe that it remains appropriate for some types of bank?

4.3 The majority supported removal, citing its risk insensitivity, with a minority either expressing no opinion or favouring retention (no reasons given).

5 Leverage ratio

12.5.1 Are there any obstacles to reporting the leverage ratio?

5.1 No obstacles were identified. A small number of banks noted concerns regarding the leverage ratio concept, mainly either citing concern about the general concept (still subject to consultation at Basel Committee/EU level) or about its applicability at an entity level. One suggested that upstreaming not be included.

12.5.2 If a minimum leverage ratio was set at 3% of (adjusted) assets, in line with the current Basel III proposal, do you consider that adhering to this would have any adverse impacts on your bank?

5.2 Most had no concerns but a larger minority cited concerns that this would constrain business, be inappropriate at an entity level or should exclude upstreaming.

12.5.3 Do you consider that there are any aspects of the leverage ratio that should be amended for subsidiary banks even where a consolidated ratio is seen to be appropriate?

5.3 A similar response to the above.

6 Provisioning

13.7.1 Do your bank's accounting practices regarding credit provisioning only require provisions to be raised where losses are incurred (as opposed to the expected loss approach outlined by the Basel Committee)?

6.1 Most agreed. One said it used an expected loss approach and one said that it only provided for specific risks (which may be missing the point). Several banks favoured a move to an expected loss approach, although some of these noted that additional guidance would be required.

13.7.2 If you do not currently use IFRS, what is the reason for this?

6.2 All respondents said they use IFRS

7 PILLAR 2

14.2.1 Are there any specific areas of Pillar 2 where you consider that a common approach across the CDs would assist banks?

7.1 A small number favoured more alignment generally or even consolidated ICAAP production but equally some opposed this directly, favouring an individual entity/regulator approach.

7.2 Two banks specifically mentioned particular risk areas where more/common guidance might help – pensions and structural foreign exchange. No details were provided.

7.3 Taken together, the responses suggest that looking at key areas, such as pensions and structural FX, jointly might be appropriate but otherwise banks seem content with the separate processes. This could be achieved by sharing thoughts and issuing guidelines separately or, more comprehensively, by issuing joint guidance on these risks.