



**Jersey Financial
Services Commission**

› **Feedback on Consultation Paper No. 8 2015**

› **Basel III: Capital Adequacy and Leverage**

Feedback on responses to the consultation paper on the implementation of revised Basel Committee standards relating to capital adequacy and leverage.

› Consultation Feedback

Please note that terms in *italics* are defined in the Glossary of Terms.

This paper reports on responses received by the *Commission* regarding the *CP*.

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› Glossary of Terms

Basel Committee	Basel Committee on Banking Supervision
Basel II	<i>“International Convergence of Capital Measurement and Capital Standards”</i> , re-issued in comprehensive form in June 2006 by the Basel Committee
Basel III	collectively, a series of documents issued by the Basel Committee that either revise Basel II or establish new international standards regarding the financial management of international banks
Commission	Jersey Financial Services Commission
Commission Law	Financial Services Commission (Jersey) Law 1998
CP	Consultation Paper No. 8 2015 <i>“Basel III: Capital Adequacy and Leverage”</i>

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1 Executive Summary

1.1 Overview

- 1.1.1 This paper addresses certain capital adequacy elements of the “**Basel III**” package of new and revised international standards issued by the Basel Committee on Banking Supervision (“**Basel Committee**”). These revise the prior international standard set out in the document “*International Convergence of Capital Measurement and Capital Standards*” (“**Basel II**”), issued in 2006 by the Basel Committee, which has been implemented previously in Jersey.
- 1.1.2 In July 2015, the *Commission* issued Consultation Paper No. 8 2015: “*Basel III: Capital Adequacy and Leverage*” (the “**CP**”), to seek views on the implementation of revised *Basel Committee* standards relating to capital adequacy and leverage, following on from the publication of Discussion Papers on these subjects.
- 1.1.3 The purpose of this paper is to provide feedback on the responses received regarding the *CP*.

1.2 Feedback received

- 1.2.1 The consultation period closed on 23 October 2015. Four responses were received directly by the *Commission*.
- 1.2.2 Section 2 of this Feedback Paper presents a summary of the substantive comments received and the *Commission’s* response to each.
- 1.2.3 The *Commission* is grateful to respondents for taking the time to consider and comment on the proposals.

1.3 Next Steps

- 1.3.1 In the light of the overwhelmingly positive responses received, it is proposed to implement the plans set out in the *CP* for:
 - 1.3.1.1 new definitions for regulatory capital (Core Equity Tier 1, Tier 1 and total capital, in line with *Basel III*), with minima established for each (8.5%, 8.5% and 10% respectively) that are consistent with the current minimum of 10%; and
 - 1.3.1.2 a new leverage ratio reporting requirement, consistent with the metric established in *Basel III*, but with no minimum established at this time.
- 1.3.2 It is intended to complete the introduction of these changes by the end of 2017.

2 Summary of responses to the CP

2.1 Structure of this section

2.1.1 This section summarises the comments received in response to the CP and the Commission's responses to those comments.

2.1.2 The CP asked twelve questions, as set out below.

2.2 Question 1

- › Would a 1 January 2017 deadline provide sufficient time to replace affected instruments? If not, please provide an alternative.

2.2.1 No respondent expressed any concerns.

Commission response

2.2.2 In line with the plan described in the CP, it is intended to develop reporting systems and completion guidance in 2016 and commence reporting during 2017 with test submissions, with the aim of fully transitioning by the end of 2017.

2.3 Question 2

- › Does your bank provide any funding to non-bank holding companies that directly or indirectly hold capital instruments issued by your bank? If so, please comment on the impact of these proposals and steps that you can take to mitigate the impact.

2.3.1 No respondent suggested any changes to the proposals in the CP.

Commission response

2.3.2 The proposals in the CP will be implemented unchanged.

2.4 Question 3

- › Are the proposed contractual conversion trigger levels for AT1 and Tier 2 instruments reasonable? If not, please propose an alternative.

2.4.1 Respondents either did not plan to issue relevant instruments or supported the proposals.

Commission response

2.4.2 The proposals in the CP will be implemented unchanged.

Question 4

- › Does the extended timeline for implementation (to 2017) provide sufficient time to replace or amend any capital issuance that does not meet the proposed standards for regulatory capital?

2.4.4 Respondents either had not issued relevant instruments or supported the proposals.

Commission response

2.4.5 The proposals in the *CP* will be implemented unchanged.

2.5 Question 5

- › Is the detailed guidance in Appendices B, C and D sufficiently clear? If not, please outline which areas you consider not to be so and any suggestions as to how this should be resolved.

2.5.1 No issues identified by respondents.

Commission response

2.5.2 The proposals in the *CP* will be implemented unchanged.

2.6 Question 6

- › Is the guidance in Appendix E sufficiently clear? If not, please detail areas where you consider that not to be the case and any suggestions you have as to how this should be resolved.

2.6.1 No issues identified by respondents.

Commission response

2.6.2 The proposals in the *CP* will be implemented unchanged.

2.7 Question 7

- › Is the detailed guidance in Appendix F sufficiently clear? If not, please detail areas where you consider that not to be the case and any suggestions you have as to how this should be resolved.

2.7.1 No issues identified by respondents.

Commission response

2.7.2 The proposals in the *CP* will be implemented unchanged.

2.8 Question 8

- › Is the detailed guidance in Appendix G sufficiently clear? If not, please detail areas where you consider that not to be the case and any suggestions you have as to how this should be resolved.

2.8.1 No respondents queried the guidance in Appendix G of the *CP*, regarding the reporting of a leverage ratio.

2.8.2 Some respondents queried whether any plans had been formed to establish a minimum for the leverage ratio, noting that a 3% minimum applied under the international standard.

Commission response

2.8.3 The Commission has no plans to establish a minimum for the leverage ratio. However, it is anticipated that this will be reviewed once: (1) the *Basel Committee* has finalised the international standard for the leverage ratio and (2) data is available (being that reported under these proposals), in order to determine if there is a case for any local implementation and the form that might take.

2.8.4 Any implementation would be the subject of further consultation. This reflects the fact that the proposed leverage ratio standard applies on a consolidated basis and hence does not apply to local subsidiaries on a standalone basis.

2.9 Question 9

- › Is the period to 2017 sufficient to manage any impact arising from the change to using Tier 1 capital for the purpose of determining the capital base for Large Exposures?

2.9.1 No respondent expressed concerns about this change, which is in line with the revised international standard contained within “*Supervisory framework for measuring and controlling large exposures*”, issued in April 2014 by the *Basel Committee*.

Commission response

2.9.2 The proposals in the *CP* will be implemented unchanged.

2.10 Question 10

- › Have you any views as to which of the remaining elements of Basel III should either (1) be introduced at the earliest opportunity or (2) not be introduced locally?

2.10.1 One respondent queried whether a capital conservation buffer would be implemented in Jersey.

2.10.2 Respondents noted that proposals impacting credit risk would have the highest potential impact locally and hence should be circulated at the earliest opportunity.

Commission response

2.10.3 The absence of any proposal in the *CP* to impose Pillar 1 buffers (capital conservation, counter-cyclical or those for globally systemic banks) reflects the fact that the Commission considers that consolidated application, as required by *Basel III*, is appropriate and sufficient, and that therefore local implementation is not necessary.

2.10.4 Pillar 2 will be used on a case-by-case basis where local risks are identified that warrant further capital being set aside, in-line with existing practice, which will be minimally revised

in due course to reflect the move from a single minimum ratio for total regulatory capital to three capital minima.

2.10.5 A Discussion Paper will be issued in 2016 on the recent *Basel Committee* proposals regarding the standardised approach for credit risk and other capital adequacy elements of *Basel III*.

2.11 Question 11

- › In order to gauge better the potential impact of new international standards regarding derivatives, could respondents indicate: (1) whether or not their bank has significant volumes of derivatives contracts and (2) the extent these are already centrally cleared or margined.

2.11.1 No respondent reported significant derivative exposures. One respondent noted that certain of its derivatives were standardised and margined.

Commission response

2.11.2 In light of the low level of exposure and the need to address Basel Committee proposals regarding credit risk and operational risk, it is not planned to address the revised standards relating to derivatives in the next two years. Indicative plans will be commented on in the Discussion Paper referred to above.

2.12 Question 12

- › Are there any specific measures that should be considered that would either increase the benefits of the proposals or reduce any of the associated costs of implementation?

2.12.1 No specific measures were identified.

Commission response

2.12.2 The proposals in the *CP* will be implemented unchanged.

Appendix A

List of respondents to the consultation paper.

- HSBC Bank International Limited
- SG Hambros Bank (Channel Islands) Limited
- Standard Bank Jersey Limited
- The Royal Bank of Scotland International Limited