1 August 2012

Secretariat of the Basel Committee on Banking Supervision
Bank for International Settlements
CH-4002 Basel, Switzerland

Re: Consultative document: A framework for dealing with domestic systemically important banks

Dear Secretariat,

The Global Financial Markets Association[1] welcomes the opportunity to provide comment on the recent consultative paper, *A framework for dealing with domestic systemically important banks* (the D-SIB framework). A number of banks that required government intervention in recent years were large on a regional or national stage, but not the global stage, and it is important that regulators agree to ensure adequate loss absorbency at banks that present systemic risk to their national economies.

As noted in the proposal, individual jurisdictions have authority to impose additional capital charges on institutions over and above Basel III minima. Many are in the process of strengthening their approach to this; for example, the EU, the UK, and the US are developing required processes under which supervisors will establish additional buffers. In addition, many host supervisors assign foreign institutions incremental capital requirements on a case-by-case basis. Our main concern with the D-SIB framework is that the proposed higher loss absorbency (HLA) requirement appears to conflict with, or at best confuse, these vital national and regional initiatives. Before the BCBS adopts a D-SIB capital buffer requirement, it should perform a peer review of the various policies and processes member jurisdictions utilize to establish capital buffer requirements above the Basel III minima. It may then determine that imposing the additional HLA requirement is not necessary, or at a minimum, it can clarify how the HLA fits in to the various national regimes.

If and when the BCBS decides to proceed with a D-SIB framework including a capital component, we agree with taking a principles-based approach in reaching international agreement on this issue. As noted above, one of our most significant concerns is to ensure the framework does not confuse

[1] The Global Financial Markets Association (GFMA) brings together three of the world's leading financial trade associations to address the increasingly important global regulatory agenda and to promote coordinated advocacy efforts. The Association for Financial Markets in Europe (AFME) in London and Brussels, the Asia Securities Industry & Financial Markets Association (ASIFMA) in Hong Kong and the Securities Industry and Financial Markets Association (SIFMA) in New York and Washington are, respectively, the European, Asian and North American members of GFMA. For more information, please visit http://www.gfma.org.

or conflict with what various supervisors are already doing to address systemic and other risks through capital. Another key concern is to ensure that the G-SIB framework remain the ceiling of any systemic capital buffer imposed on a banking organization. Other concerns include striking a balance between the principles-based approach and achieving international consistency, ensuring home and host supervisors coordinate on both the identification of D-SIBs and the allocation of capital within a group, and the consistency between the D-SIB framework and recovery and resolution planning requirements. We elaborate on these and other issues below.

G-SIB Capital Surcharge

The G-SIB capital surcharge reflects the amount of additional loss absorbency that should be required of each firm, based on its global systemic footprint. While the D-SIB proposal acknowledges that the two frameworks should not be additive, it is quite confusing as to how the two frameworks would interact. Principle 10, as well as paragraph 38, seems to imply that the D-SIB surcharges for individual subsidiaries of a G-SIB may add up to more than its G-SIB surcharge. The same sections also seem to imply that a home supervisor would potentially assign a D-SIB surcharge to a G-SIB, although the purpose of this is not clear. It makes no sense to structure the D-SIB framework such that additional systemic buffers would be imposed on a G-SIB that would result in a larger overall capital surcharge at the consolidated level. Even more perversely, the proposal could result in a D-SIB that is not a G-SIB having a higher systemic capital requirement than the highest G-SIB capital surcharge bucket.

We believe that no G-SIB should have to hold, for purposes of a systemic buffer, an amount of capital higher than its G-SIB surcharge would require, regardless of whether its subsidiaries have been assigned D-SIB surcharges. Similarly, no D-SIB should have to hold, as a systemic buffer, an amount of capital that is higher than what would result from its home supervisor's HLA requirement. An institution's supervisory college should work together to ensure the consolidated company's systemic surcharge is no higher than its parent company has been assigned.

Identifying D-SIBs

The criteria for assessing a D-SIB's systemic footprint are sensible. However, while some parts of the proposal suggest that supervisors should incorporate qualitative judgment into their assessments, in other parts of the framework there seems to be an implicit assumption that the application of the criteria will be applied in a more scientific manner than is actually possible or advisable. For example, paragraphs 34 and 36 both suggest that there will be a numerical score for each D-SIB. We agree that supervisors should have discretion to factor in policy judgments relative to national circumstances in identifying D-SIBs, and suggest that the language regarding international consistency in identifying D-SIBs be recast so as not to imply it is a scorecard exercise.

We believe that where appropriate, and in particular in the case of D-SIBs that are part of G-SIBs, there should be coordination between home and host authorities in the identification of D-SIBs. We would suggest relevant BCBS guidance on home-host coordination be revised to reflect the importance of such coordination.

Consistency of Higher Loss Absorbency Requirements

It will be difficult to evaluate cross border consistency regarding the size of the D-SIB surcharge. One problem is that there will be a lack of clarity as to how each jurisdiction defines "higher loss absorbency", because the reference capital standard will not necessarily be the same. Even for internationally active banks that follow Basel III, many jurisdictions add buffers above the Basel III minima based on stress testing, ICAAP, or other factors. For non-internationally-active banks, jurisdictions often have their own capital regimes. Evaluating the consistency of approaches would be challenging at best, but more important, expecting a consistent surcharge on top of an inconsistent capital regime makes little sense. We think it is essential not to duplicate existing or emerging capital buffer requirements, including duplication with any systemic buffers under Pillar 2 processes. National authorities should be encouraged to integrate, where warranted, a systemic buffer into their own capital regimes.

Nonetheless, if the Basel Committee establishes a D-SIB capital framework, it should monitor its implementation, to ensure it understands – and publicizes – each jurisdiction's approach to determining the amount of capital D-SIBs need to hold as a systemic surcharge. As part of this process, we recommend that the Basel Committee continue to survey the numerous developing national capital regimes that add buffers to the Basel III minima to understand holistically how jurisdictions are regulating capital for systemic and other risks.

Recovery and Resolution Plan Requirements

We are pleased to see a recognition that resolution regimes and recovery and resolution plans (RRPs) in place at D-SIBs should be taken into account in setting any capital surcharges. Clearly both the impact *and* probability of a firm's failure would be affected by its plans for recovery and crisis management, as well as its resolvability. In fact, to underscore the importance of this linkage, we believe that it would make sense to raise it in Principle 8 so that it is clear that any D-SIB's resolvability is relevant in determining its capital surcharge, not just those subject to home-host coordination.

It is also critical to promote consistency between the requirements of the RRPs and the D-SIB framework. In particular, there should be consistency between what supervisors consider systemic activities in the context of RRPs, and how they assess D-SIBs' systemic footprints.

Other Comments

The second part of Principle 12 states that national authorities should put in place any additional requirements and other policy measures they consider appropriate to address the risks posed by D-SIBs. This is somewhat concerning, because the paper states the scope of this proposal to be assessment of, and higher loss absorbency requirements for, D-SIBS. Yet this statement seems to go well beyond capital, even within a principle that pertains to common equity. We would appreciate some clarification on this point.

Finally, we recommend that the D-SIB framework clarify that cross-border branches are outside its scope.

***

Thank you for the opportunity to comment on the D-SIB proposed framework. We would be happy to answer any further questions and hope we can be helpful in putting in place a sensible approach to addressing the systemic risk of D-SIBs.

Sincerely,

Simon Lewis
CEO, GFMA