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Basel Committee on Banking Supervision
Via email: baselcommittee@bis.org

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Subject: NVB reaction to bcbs 190 - Capitalisation of bank exposures to central counterparties

Dear Sir, Madam,

On behalf of the Dutch Banking Association[1] (NVB), I would like to thank you for giving us the opportunity to provide you with our feedback on consultation paper 190, *'Capitalisation of bank exposures to central counterparties',* which is a follow up on the December 2009 paper '*Strengthening the resilience of the banking sector*'. The consultation paper bcbs 190 is looking to introduce capital requirements for **currently listed derivatives** which - at the moment - are under a zero solvency regime. This reflects the additional systemic risk that will result from the changing incentives to clear bilateral OTC transactions via CCPs.

We welcome that the Basel Committee is looking at ways to address and mitigate the systemic risk that is associated with the increased incentives to use CCPs and the consequences this will have on the resilience of the banking sector. We would also like to take this opportunity to provide you with our views, alternative approaches, as well as questions we have regarding the paper. We hope you will find our feedback helpful and constructive. In case you have any questions or remarks, please feel free to contact me at your convenience.

Kind regards,

Onno Steins
Advisor Risk Management

[1] The Nederlandse Vereniging van Banken (NVB) is the representative voice of the Dutch banking community with over 90 member firms, large and small, domestic and international, carrying out business in the Dutch market and overseas. The NVB strives towards a strong, healthy and internationally competitive banking industry in the Netherlands, whilst working towards wider single market aims in Europe.

Detailed feedback and additional solutions

In our view, some important considerations relating to CCPs were not yet taken on board sufficiently in the consultative paper. In this section, we will provide you with the details regarding these considerations.

1. *Transparency of netting in case of a CCP default*

The new regulation creates an opportunity to increase the clarity and transparency with regards to the application of netting in case of a CCP default.

The language of the consultation document clearly reflects the way OTC transactions are regulated and contracted. For the CCP industry, however, this does not apply. The way transactions are netted in case of a default is not uniformly specified and might therefore not always be clear. This creates uncertainty and may limit the extent to which netting may reduce the capital charge, consequently increasing the burden on the industry.

Increasing the transparency regarding netting policies will positively affect the predictability of the behaviour of CCPs in the unlikely event of a default. The two main questions in this regard are:

-How will exposures / transactions on CCPs be settled?
-How will trades be 'kept alive' in case there are offsetting positions with different clients when a CCP defaults?

Having adequate answers to these two questions, will allow stakeholders to more effectively manage their positions in case of a default and will create opportunities to limit the impact of the default.

2. *Regulation and supervision of CCPs*

In relation to the systemic risk associated with as well as the capitalisation levels of CCPs, the proposal requires banks to hold additional capital for exposures on CCPs. We feel this will not remove the systemic risks that are related to the vulnerabilities of an undercapitalised CCP, as two important elements of the construction of CCPs were not included in the analysis. Taking these characteristics on board in the final guidance would provide a better and more workable solution, which in turn will result in added resilience. The two elements we suggest to incorporate in the final guidance are:

-Clients of a CCP will have offsetting positions. By charging the individual banks based on their exposures, the aggregate charge to the financial system will be higher than is warranted by the underlying risks. Leveraging off the dependencies between the CCP members will be more effective and also creates a clear opportunity to increase the transparency of netting practices in this industry.
-As banks and clearing institutions do not guarantee the exposures towards their clients, it is actually *the capitalisation level of the clients* that impacts the resilience of the system. In the event of a default, the actual clients will be affected as a result of the way the system is constructed.

The above implies that it could be more effective to strengthen the resilience of the system by:

- Strengthening the supervision on CCPs.
- Ensuring that CCPs are adequately capitalised.
- Imposing procedures and regulations that specify how transactions and exposures are settled in case of a CCP default. This should into account that all transactions have counter transactions and that most clients have an interest in keeping these transactions 'alive'.

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3. CEM method for CCPs

The use of various modelling approaches should be reconsidered, when it comes to calculating the exposures to and from the CCP. With regards to the modelling approaches that can be used by CCPs, we note that the CEM method does not provide the required flexibility to recognize netting and daily margining for all product types. In the case of options for example, the CEM formulas are too conservative. As CCPs are required to use sophisticated models to calculate their margining requirements, it does not seem entirely fair to impose the use of only the CEM method. The possibility should remain to use modelling approaches that better fit the characteristics of the actual products, such as IMM models. For other clearing institutions (non CCPs) other models should also be recognized. The QIS currently requires banks to use the CEM method, which implies that this might also be the case in the final guidance. We reiterate, however, that imposing capital requirements on banks and clearing members is not the optimal solution.

Additional questions and remarks:

Next to the general feedback we provided, we would also like to highlight a number of questions and remarks:

- With regards to the marging period, guidance was already given in 'Strengthening the resilience of the banking sector'. This paper mentions that, in certain cases, the marging period should be increased. In this regard, the consultation document does not provide additional details as to the intended approach for CCPs. We request the Basel Committee to elaborate on the treatment of this issue in its final guidance.

- The present freedom CCPs have regarding their use of a netting logic, as well as the liberty they have to specify these in their contracts or not, creates an array of different treatments. This clearly presents an opportunity to achieve a higher degree of uniformity and clarity by standardizing the netting practices and definitions used by CCPs. ISDA might be able to provide assistance in this area.

- On page three the Basel Committee asks: "*The Committee invites comments on whether CCPs, CCP overseers, clearing members, transaction repositories or other sources of information and expertise are best equipped to assemble and manage the necessary information and to complete this calculation.*"

  We feel this information should be sent either via the CCP or the CCP overseers.