1 August 2012

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

Email: baselcommittee@bis.org

Dear Basel Secretariat,

This is in reference to the June 2012 Consultative Document (CD) titled "A framework for dealing with domestic systemically important banks." We have summarized our thoughts below, and have attached detailed comments to this letter.

Overall, we believe that the proposed regime is appropriately designed to address the negative externalities associated with D-SIBs. The CD clearly delineates the rationale underlying the policy approach towards the Domestically Systemically Important Banks (D-SIBs) and the need for the policies to play a complementary role to that played by G-SIB framework. We appreciate the fact that the CP has duly highlighted the possibility of D-SIBs having cross-border externalities, even if they are not global in their business scope. We appreciate the flexibility provided in terms of an appropriate degree of national discretion in the assessment methodology, given the need to accommodate the specific characteristics of individual jurisdictions.

We believe that mitigating the risk of impact through capital augmentation might have unintended consequences for systemically important, but non-complex, banking operations. We also believe that intensive supervision is a strong risk mitigants; similar to higher loss absorbency measures. We also recognize that intensive supervision techniques are much more difficult to benchmark around the globe as compared with higher loss absorbency measures. The document focuses on domestic banks, which include subsidiaries of cross-border banking groups. The document appears to be silent on branches of cross-border banking groups, where the branch (as a stand-alone entity) would be systemically important. This is further complicated as most deposit insurance schemes do not cross borders. Obviously, branches cannot have capital allocation through higher loss absorbency, but the document might emphasize more cooperation with the home country supervisor in achieving proper risk mitigants to achieve a level, domestic playing field.

Sincerely,

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Treatment of Cross-Border Branches as a D-SIB

The document appropriately focuses on domestic, systemically important, banks. This definition, of course, includes subsidiaries of cross-border banking groups. The document appears to be silent on branches of cross-border banking groups, where the bank branch (if viewed as a stand-alone entity) would be systemically important to the domestic economy. This is further complicated as safety nets such as deposit insurance schemes -- which play an important role in fostering financial stability -- rarely cross borders. Obviously, branches cannot have capital allocation through higher loss absorbency, and we recognize that every country must decide whether a branch is appropriate for its domestic economy, particularly when the branch is a significant market participant in the retail sector. However, we believe the document might emphasize more cooperation with the home country supervisor, when branches are allowed, in developing proper risk mitigants to achieve a level, domestic playing field.

Suggest More Emphasis on Probability of Failure

The fundamental approach to the D-SIB assessment methodology, as outlined under principle 2 and its associated guidance, relies on measures reflecting "impact of failure". While we agree that the criteria for impact of failure are relevant and appropriate, we also believe that certain factors impacting the probability of failure -- business model, complexity of products, governance structures, remuneration structures, etc. -- should also play a role in the risk mitigants. This is particularly the case in emerging markets, where banks are often dominated by a few market participants, but the business model and product line is relatively non-complex.

If, for example, a D-SIB with a low probability risk profile will be required to hold more capital merely as a result of its size, an unintended consequence might be for that institution to assume more risk or increase its complexity to achieve more return. This unintended result might be a low-risk D-SIB transforming to a higher-risk D-SIB, as a result of an additional capital charge.

We recognise that the national discretion described in paragraph 23 of the CD allows for building in some element of flexibility in the design of the assessment methodology by permitting changes in relative weights of different factors. We also believe that the flexibility in the methodology should be driven by a fundamental analysis and identification of the risk drivers and their relative importance to the designation of the bank as a D-SIB. The assessment methodology should also facilitate identification of the main drivers of the "impact of failure" which cause a bank to be designated as D-SIB, so that the mitigating measures can be customised to effectively address those specific determining factors.

We suggest that the overall emphasis on HLA requirements in the principles in Part B be tempered with a higher share of emphasis on measures which address the "risk of failure". This is likely to provide the right incentives for banks to lower their business risk, and improve the effectiveness of their risk management and governance frameworks. Reducing reliance on HLA requirements also precludes unintended consequences like higher cost of banking services for customers of simple commercial banks or better-run banks, which might be designated as D-SIBs on account of their impact factors.

Principle 3 states that the reference systems for assessing the impact of failure should be the domestic economy. This should be extended to include relevant markets outside the domestic

economy in determining the reference system for assessing the impact. This is required to address the needs of jurisdictions wherein the banks do a material amount of their business in markets outside the domestic economy and consequently have impact on interconnectedness, size and complexity considerations.

We agree with the importance of the requirement for public disclosure of the methodology for assessment of systemic importance of banks. In addition to the benefits of this transparency requirement outlined in paragraph 27 of the CD, we also believe that transparency around the assessment methodology will put pressure on regulators to maintain a high level of objectivity in their assessment processes and refrain from employing soft treatment for their domestic banks. Availability of information on the methodology will enable the market participants and multilateral institutions to assess the effectiveness with which the methodology is being employed in a particular country. This requirement will facilitate effective implementation of the strong peer reviews as proposed in the CD by BCBS.

Measures to Address Externalities and Risks Posed by D-SIBs

The CD, in paragraphs 6 & 7, has emphasised the importance and utility of other policy tools like intensive supervision, apart from the HLA to deal with the risks and externalities posed by D-SIBs. We appreciate the intention to allow for wider national discretion to accommodate specific characteristics of national markets in designing measures to mitigate risks and externalities posed by D-SIBs. However, we find that the principles under Part B are heavily focussed on HLA requirement.

The focus on identifying specific risk and impact drivers which are determinants of D-SIB status for a bank will be far more effective when used in combination with wider range of tools and flexibility to use such policy tools or tool mixes. More importantly, the availability of wider range of tools will enable the regulators to address the risks of D-SIBs while precluding unintended consequences of the types described above. The flexibility to use non-HLA measures will be more attractive in cases where HLA might not be used effectively, such as cases where cross-border branch of a bank qualifies as a D-SIB in the host country.

Specifically, we believe that intensive supervision can be an effective policy tool to address the risks and negative externalities of D-SIBs, with or without the use of HLA requirements. For example, in many instances the negative externalities imposed by a D-SIB retail or commercial bank, can be better addressed by business model changes, more intensive supervision or other policy tools apart from HLA requirement, depending on the specific risk or impact factors which determine that bank as a D-SIB.

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