Chaire Desjardins en gestion du développement durable
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Comments on the consultative document :
" A framework for dealing with domestic systematically important banks "

Presented to the Basel Committee on Banking Supervision

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1. Foreword

We welcome the opportunity provided by the Basel Committee on Banking Supervision (BCBS) to comment on its June 2012 Consultative document entitled : “A framework for dealing with domestic systematically important banks”. Members of the Desjardins chair in managing sustainable development believe that improving the framework to regulate and supervise domestic systematically important banks represents an important step to help ensure financial stability and provides a positive contribution to sustainable economic growth. This comment letter is structured into four additional parts. First, a brief introduction is presented. Next, general comments are formulated on the BCBS consultative document. Then, more specific comments and suggestions are formulated, especially on the consultative document’s approach for dealing with domestic systematically important banks. In the fifth and final part, a discussion of our analysis is presented, and the final conclusions to this comment letter are drawn.

2. Introduction

The present BCBS (June 2012) consultative document sets forth a framework for dealing with domestic systematically important banks (D-SIBs) which represents a welcomed extension to its (November 2011) publication of : “Global systematically important banks (G-SIBs): assessment methodology and the additional loss absorbency requirement”. In a recent speech, Caruena (June 2012) outlined progress and challenges in financial reform. Ingves (May 2012) discussed the need for special regulation for the big players; recently, he (June 2012) examined and discussed financial crises and the need to formulate more appropriate financial regulation. In addition, several other senior regulators and supervisors have recently reiterated the importance of improving the regulatory and supervisory framework of D-SIBs: Tarullo (June 2012) for the US, Honohan (June 2012) for Ireland, Lowe (July 2012) for Australia, Visco (July 2012) for Italy, Ingves (June 2012) for Sweden, as well as Noyer (June 2012) for France and EU countries.

3. General comments

We agree and support the BCBS position, see page 1- paragraph 4, that a D-SIB framework should be based on the assessment conducted by the local

authorities who are best placed to evaluate the impact of failure on the local financial system and the local economy. As explained in paragraph 5, by contrast with the prescriptive approach in the G-SIB framework, the D-SIB framework should establish a minimum set of principles, which ensures that it is complementary with the G-SIB framework, addresses adequately cross-border externalities and promotes a level-playing field. We also support the BCBS position expressed in paragraph 6 that would allow for appropriate national discretion to accommodate structural characteristics of the domestic financial system, which we believe, should also include differences between different types of financial institutions such as banks and quasi-banks like financial cooperatives and mutuals. In paragraph 7, in addition to higher loss absorbency (HLA) requirements for D-SIBs, we emphasise that other policy tools like liquidity adequacy requirements, regulatory leverage requirements, and more intensive supervision can also play an important role in dealing with D-SIBs in particular, but with all banks in general. Naturally, we also concur with the Committee's position, see paragraph 8, and intent to add the D-SIB framework to the scope of the Basel III regulatory consistency assessment programme. In paragraph 9, it is stated given that the D-SIB framework complements the G-SIB framework, the Committee considers that it would be appropriate if banks, and we would add if quasi-banks (financial cooperatives and mutuals), identified as D-SIBs by their national authorities are required by those national authorities to comply with the principles in line with phase-in arrangements for the G-SIB framework, ie from January 2016.

4. Specific comments

On page 3, Principle 1 states that national authorities should establish a methodology for assessing the degree to which domestic banks are systematically important in a domestic context. We suggest, that this relative importance of a D-SIB in a domestic context should be calibrated, at the least, as being either below average (low), average, or above average (high) in comparison with a D-SIB peer group. On page 3, the formulation of Principle 3 could be made more precise by writing that the reference system for assessing the impact of failure of a D-SIB should be the domestic economy and its financial system. On page 3, we suggest that the formulation of Principle 5 should be assessed having regard to bank specific factors (a), (b), (c), (d), and (e) thus taking into account the noted differences between banks and quasi-banks like financial cooperatives and mutuals. We also suggest that Principle 12 which states that the HLA requirements should be met fully by D-SIBs (banks) with CET1, and by other D-SIBs (quasi-banks) with CET1 equivalent forms of permanent and loss absorbing capital. On page 5 in paragraph 16, the formulation would be made more precise by stating that : " Correspondingly a process for assessing systematic importance in a domestic context should focus

on addressing the externalities that a bank's or a quasi-bank's failure generates at a domestic level. On page 6 in paragraph 24, we suggest that changes be made in order to respect Basel III – Pillar 3 financial disclosure considerations: "It is expected and considered equitable that the names and buckets of all designated D-SIBs and the data used to produce the scores will be promptly disclosed". Finally, on page 10 in paragraph 43 discussing principle 12, we suggest to add that the additional loss absorbency requirements for G-SIBs is also to be met by banks and quasi-banks designated by national authorities as being D-SIBs, respectively by CET1, and CET 1 - equivalent forms of permanent and loss absorbing capital. In addition, we suggest to add that national authorities should put in place any additional requirements, like capital, liquidity and regulatory leverage, as well as other policy measures they consider to be appropriate to address the risks posed by a D-SIB.

5. Conclusion and discussion

Quite recently, the BCBS (June 2012) reported to G20 leaders that progress made on Basel III implementation was not found to be uniform so far across various countries and economic regions. In addition, Noyer (June 2012) reiterated the same findings. At a recent Conference, Préfontaine (June 2012) discussed some of the weaknesses uncovered so far in gradual Basel III implementation by G-SIBs. We believe that most of the caveats present in the G-SIB prescriptive approach including relatively slow and heterogeneous gradual implementation are better answered in the BCBS proposed and simplified D-SIBs principles-based approach. In our analysis of this approach, we noted that in order to promote a more level playing field, and to enhance competition between banks and non-banks some of the proposed D-SIB principles had to be slightly modified in order to be more inclusive and to better respect national specificities. Following Acharya, Mehran, Schuermann and Thakor (2012) for banks, we also made CET1 equivalent suggestions for quasi-banks in order to foster the acceptance of more robust capital elements and regulation.

References

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