Comments

on the Basel Committee for Banking Supervision’s Consultative document “Supervisory guidance for managing risks associated with the settlement of foreign Exchange transactions”

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*The **German Banking Industry Committee** is the joint committee operated by the central associations of the German banking industry. These associations are the Bundesverband der Deutschen Volksbanken und Raiffeisenbanken (BVR), for the cooperative banks, the Bundesverband deutscher Banken (BdB), for the private commercial banks, the Bundesverband Öffentlicher Banken Deutschlands (VÖB), for the public-sector banks, the Deutscher Sparkassen- und Giroverband (DSGV), for the savings banks finance group, and the Verband deutscher Pfandbriefbanken (vdp), for the Pfandbrief banks. Collectively, they represent more than 2,200 banks.*

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The German Banking Industry Committee (GBIC) would like to thank the Basel Committee for Banking Supervision (BCBS) for the opportunity to comment on the consultative document "Supervisory guidance for managing risks associated with the settlement of foreign exchange transactions". We welcome the update of the last supervisory guidance. We particularly appreciate the organisation into individual "Guidelines" as well as the breakdown of the content into framework conditions and individual risk types. We see this as an improvement over the version published in the year 2000. Please find our individual comments below.

I. Guideline 2

The pivotal approach envisaged under the consultative document consists in a risk management approach concerning material risks stemming from FX-transactions which is based on pari passu settlement systems (PVP, Payment-versus-Payment). In the consultative document the handling is realised by means of two different approaches. On the one hand, the current proposals seem to suggest that PVP – whenever applicable – should be used on a mandatory basis and that this approach should also be proactively pushed by the supervisors (point 2.7 ff., Guideline 2). On the other hand, PVP use is encouraged by means of appropriate incentives during the capital allocation (Guideline 7).

This two-tier approach seems to be redundant. *In lieu* of this we would advocate in favour of a single approach which is consistent with the existing Pillar 2 provisions concerning capital allocation. Any regime which stipulates the mandatory use of certain settlement systems exceeds the usual regulatory scope of Pillar 2 minimum requirements and interferes with entrepreneurial freedom as well as the principle of the free choice of processes and methods. Hence, there should be a specific clarification that banks shall remain free to use approaches which are, qualitatively speaking, *on a par* with the PVP approach.

Furthermore, key consideration 3 could be interpreted as a clear requirement to reduce principal risk. However, risk management also involves the potential acceptance of risks in the form of a deliberate decision beyond the criterion "practicable". Hence, instead of the expression "reduce" we recommend gearing this requirement towards a responsible management (by way of analogy cf. key consideration 1 of Guideline 3). Furthermore, any other persisting risks are addressed by virtue of Guideline 7.

II. Guideline 3

Similar to our comments on Guideline 2, we perceive a slight ambiguity also in this context: Potentially, Guideline 3 could be understood that netting agreements and collateralisation will be required on a mandatory basis. In line with our presentations concerning Guideline 2, we would like to reiterate that, here, too, it would be correct to admit other equivalent methods (on a non-discriminatory basis) and that, in this respect the principle of the freedom of processes or methods ought to be applied.

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III. Guideline 4

Key consideration 2 uses the expression "each currency". In order to clarify that the wording "… taking into consideration the size, nature, complexity and risk profile of their banks' FX activities …" shall be equally applicable in this context, the term "material" currencies should be used. Generally, also in the framework of liquidity risks, only "material" currencies are taken into consideration.

IV. Guideline 7

We would like to reiterate our aforementioned preliminary understanding that the consultative document constitutes an update of the year 2000 version. Under the Basel agreement, said document was explicitly viewed as a part of Pillar 2 (SRP). We suggest a clarification that there has not been any change in terms of this categorisation. Particularly the wording and presentation of Guideline 7 gives rise to certain ambiguities in this respect thus resulting in the impression that there was a link to the capital requirements under Pillar 1.

Yours faithfully,
on behalf of the German Banking Industry Committee
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by proxy

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