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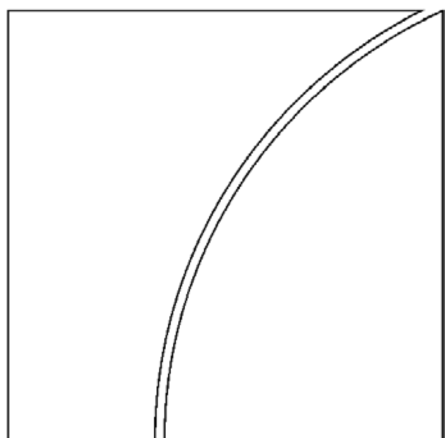
Basel Committee
on Banking Supervision



Report to G20 Finance Ministers and Central Bank Governors on Basel III implementation

October 2012

BANK FOR INTERNATIONAL SETTLEMENTS

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Report to G20 Finance Ministers and Central Bank Governors on Basel III implementation

Introduction and summary

The G20 Leaders met in Los Cabos in June 2012. At this Summit, they endorsed the work of the Basel Committee on Banking Supervision in monitoring the global implementation of its standards, and urged jurisdictions to meet their commitments.

> *"We welcome progress in implementing Basel II, 2.5 and III and urge jurisdictions to fully implement the standards according to the agreed timelines."*[1]

This report updates the G20 Finance Ministers and Central Bank Governors on the progress made by Basel Committee member jurisdictions[2] in implementing the Basel III standards (including Basel II and Basel 2.5, which now form integral parts of Basel III). It also highlights specific areas that require attention if the goal of achieving timely and consistent implementation is to be achieved. The Basel Committee believes that full, timely and consistent implementation of Basel III by its members is essential for restoring confidence in the regulatory framework for banks and to help ensure a safe and stable global banking system.

The transitional phase for implementing the Basel III package commences on 1 January 2013, by when all jurisdictions should have in place the necessary regulations. At the time of this report, eight of the 27 member jurisdictions of the Basel Committee have issued their final set of Basel III related regulations, 17 members have published draft regulations, and two members are currently in the process of drafting regulations but have not yet published them. Given their commitment, and the fact that the transitional date is a publically announced one, it is especially important that member jurisdictions that are home to global systemically important banks (G-SIBs) make every effort to issue final regulations as soon as possible in order to meet the transition period deadline.

To facilitate proper implementation and follow up, the Basel Committee has begun to assess the consistency of these regulations and progress with implementation against 14 core elements of the Basel framework. As a first step, the Committee conducted detailed assessments of the content and substance of the final regulations implementing the Basel III package in Japan, and the draft regulations in the European Union and the United States.[3] While noting implementation progress in all three jurisdictions, the assessments have identified areas of divergence from the globally agreed Basel standards. In the case of Japan, no material deviations were observed and the jurisdiction is assessed overall as

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[1] Los Cabos G20 Leaders Declaration, available at www.g20.org.

[2] The Basel Committee on Banking Supervision consists of senior representatives of bank supervisory authorities and central banks from Argentina, Australia, Belgium, Brazil, Canada, China, France, Germany, Hong Kong SAR, India, Indonesia, Italy, Japan, Korea, Luxembourg, Mexico, the Netherlands, Russia, Saudi Arabia, Singapore, South Africa, Spain, Sweden, Switzerland, Turkey, the United Kingdom and the United States. The Committee's governing body is the Group of Central Bank Governors and Heads of Supervision, which is comprised of central bank governors and (non-central bank) heads of supervision from member countries. The Committee usually meets at the Bank for International Settlements (BIS) in Basel, Switzerland, where its permanent Secretariat is located.

[3] Follow-up assessments in the European Union and United States will be conducted once final regulations are available.

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"compliant." In the European Union and the United States,[4] there were a few deviations in the draft regulations that were assessed to be of a material nature (for securitisation related regulations in the United States, and for regulations covering the definition of capital and the internal ratings-based (IRB) approach in the European Union). All other elements in both jurisdictions were either "compliant" or "largely compliant."

Given the importance of making the banking system more resilient, it is essential that the Basel framework is implemented consistently and according to the globally-agreed timelines. The Basel Committee therefore urges the G20 Finance Ministers and Central Bank Governors to call on (i) all Basel Committee jurisdictions to meet the globally agreed deadline; (ii) the European and United States authorities, and others who undergo a Basel Committee regulatory consistency assessment, to close any identified gaps between their regulations and Basel III and; (iii) all jurisdictions to ensure their implementation of Basel III remains timely and consistent with the internationally agreed package of reforms.

The Basel Committee also continues to perform detailed analysis of the variations in risk-weighted assets across banks, across jurisdictions and over time, both for assets in the banking book and in the trading book. This report includes preliminary conclusions of this analysis. More detailed assessment reports, potentially including policy recommendations, where appropriate, will be considered by the Committee later in 2012 and in early 2013.

[4] The US assessment report also notes the overarching issue of prolonged "parallel run" (under which US banks calculate capital requirements according to both Basel I and Basel II rules). This means that while final Basel II regulations are in place in the United States, the legally binding minimum capital requirements for internationally active banks in the United States are still the 1988 Basel Capital Accord (Basel I). However, as the Basel rules text does not contain explicit rules regarding the length of the parallel run, this finding was not taken into account in the Level 2 grading of the United States.

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Basel standards

In June 2004, a package of reforms known as Basel II introduced more risk-sensitive minimum capital requirements for banks, including an enhanced measurement of credit risk, and capture of operational risk. Basel II also reinforced the requirements by setting out principles for banks to assess the adequacy of their capital and for supervisors to review such assessments to ensure banks have the necessary capital to support their risks. It also strengthened market discipline by enhancing disclosure requirements. The deadline for implementation of the Basel II framework by member jurisdictions was the end of 2006.[5]

In July 2009, the Committee introduced enhancements to the Basel II framework in response to lessons from the financial crisis. These reforms, referred to as Basel 2.5, relate to the measurement of risks for calculating regulatory capital for securitisation and trading book exposures (Pillar 1), risk management and supervisory review (Pillar 2) and disclosure (Pillar 3). A deadline for implementing these reforms was set for end 2011.

In December 2010, the Basel Committee published Basel III, a comprehensive set of reforms to raise the resilience of banks, supplementing Basel II and 2.5 in a number of dimensions. Basel III addresses both firm-specific and broader, systemic risks by:

- Raising the *quality* of capital, with a focus on common equity, and the *quantity* of capital to ensure banks are better able to absorb losses;
- Enhancing the coverage of risk, in particular for capital market activities;
- Introducing capital buffers which should be built up in good times so that they can be drawn down during periods of stress;
- Introducing an internationally harmonised leverage ratio to serve as a backstop to the risk-based capital measure and to contain the build-up of excessive leverage in the system;
- Introducing minimum global liquidity standards to improve banks' resilience to acute short term stress and to improve longer term funding; and
- Introducing additional capital buffers for the most systemically important institutions to address the issue of "too big to fail."

The implementation period for Basel III capital requirements starts from 1 January 2013 and includes transitional arrangements until 1 January 2019. The transitional arrangements are available to give banks time to meet the higher standards, while still supporting lending to the economy.

The liquidity requirements, leverage ratio and systemic surcharges come into force in a phased approach starting from 2015. The implementation of these rules will, therefore, be assessed later[6] and are not covered in this report.

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[5] With the exception of the most advanced approaches which were expected to be made available from the end of 2007.

[6] To be included after the Committee concludes its review on any revisions or final adjustments.

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Design of the Committee's Basel III Implementation Review Programme

In January 2012, the Group of Central Bank Governors and Heads of Supervision (GHOS), the Basel Committee's oversight body, endorsed the comprehensive process proposed by the Committee to monitor members' implementation of Basel III. The process consists of the following three levels of review:

- Level 1: ensuring the **timely** adoption of Basel III;
- Level 2: ensuring **regulatory consistency** with Basel III; and
- Level 3: ensuring consistency of **outcomes** (initially focusing on risk-weighted assets).

The Basel Committee has published three "Level 1" progress reports.[7] It has completed a "Level 2" review of Japan, and has released preliminary reports on the European Union and the United States. In addition, it has commenced an assessment of Singapore. The Committee's "Level 3" reviews are conducting detailed assessments of banks' models to compute capital charges for the banking and trading book, based on test portfolios, information obtained from questionnaires and visits to individual banks.

The Basel Committee has worked in close collaboration with the Financial Stability Board, (FSB) given the FSB's role in coordinating the monitoring of implementation of regulatory reforms. The Committee designed its programme to be consistent with the FSB's Coordination Framework for Monitoring the Implementation of Financial Reforms (CFIM) agreed by the G20.

The objectives and the process of each of the three levels of review are as follows.

Level 1: Timely adoption of Basel III

The objective of the "Level 1" assessment is to ensure that Basel III is transformed into domestic regulations according to the agreed international timelines. It does not include the review of the content or substance of the domestic rules. Each Basel Committee member jurisdiction's status is reported in a simple table.

Separately, the Financial Stability Institute (FSI) of the Bank for International Settlements is surveying non-Basel Committee member countries and has published the results.[8]

Level 2: Regulatory consistency

The objective of the "Level 2" assessments is to ensure compliance of domestic regulations with the international minimum requirements. The Level 2 assessments are conducted by teams of 6-7 specialists with a diverse range of technical skills from independent jurisdictions. The reviews take place over a period of six months and include a detailed self-assessment, on-site visits and an assessment of the materiality of divergences. Multiple layers of cross-checking and peer review exist to ensure a fair and rigorous process and consistent treatment across reviews.

[7] *Progress report on Basel III implementation*, October 2011, April 2012 and October 2012 www.bis.org/publ/bcbs203.htm, www.bis.org/publ/bcbs215.htm, http://www.bis.org/publ/bcbs232.htm

[8] *Financial Stability Institute Survey: Basel II, 2.5 and III implementation*, July 2012, www.bis.org/fsi/fsiop2012.pdf

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All Basel Committee members will be assessed over time. The Committee decided to prioritise its reviews, focusing first on the home jurisdictions of global systemically important banks (G-SIBs). The first three reviews of the draft regulations in the European Union and the United States, and final rules in Japan have been concluded in September and the reports are available on the BIS website.[9]

A summary of the process for the Level 2 reviews is included in Appendix 2 of this report.

Level 3: Risk-weighted assets consistency

The objective of the "Level 3" assessments is to ensure that the outcomes of the rules are in line with the intended policy objectives in practice across banks and jurisdictions. It extends the scope of Levels 1 and 2, both of which focus on national rules and regulations, to supervisory implementation at the bank level.

The Committee has established two expert groups, one for the banking book and one for the trading book. These groups are identifying and analysing areas of material variability and inconsistencies in the calculation of risk-weighted assets[10] (RWAs, or the denominator of the Basel capital ratio). Depending on the outcome, the work may result in policy recommendations to address identified inconsistencies.

Progress and findings to date

Level 1

The tables in Appendix 1 show member jurisdictions' implementation status as of October 2012 including summary information about the next steps and the implementation plans being considered. Separate tables are produced for each of Basel II, Basel 2.5 and Basel III.

Basel II, which was due to come into force from end 2006, has been implemented in full by three-quarters of member jurisdictions. Of the five countries that have not yet fully implemented Basel II, two are home countries of G-SIBs – China and the United States. Both countries are in the process of assessing their banks' progress toward meeting all the qualifying criteria for the advanced approaches. The other countries that are still in the process of implementing Basel II are Argentina, Indonesia and Russia.

Basel 2.5, which was due to be implemented by Basel Committee members by end 2011, has been implemented by 20 of the 27 member jurisdictions. China, Saudi Arabia and the United States have issued final regulations for Basel 2.5 that come into effect from 1 January 2013.

Basel III regulations are due to come into effect from 1 January 2013. While progress can be observed, only eight of the 27 Basel Committee member jurisdictions have thus far issued final regulations – Australia, China, Hong Kong SAR, India, Japan, Saudi Arabia, Singapore and Switzerland. This means there is now a high probability that just six of the 29 global

9 The reports are available at www.bis.org/bcbs/implementation/l2.htm.

10 For purposes of the trading book, the work is reviewing banks' calculation of capital requirements.

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systemically important banks identified by the FSB in November 2011[11] will be subject to Basel III regulations from the globally agreed start date.

Level 2

The assessment of the European Union analysed the 5th Danish compromise versions of the Capital Requirements Regulation (CRR) and Capital Requirements Directive (CRD4). The assessment judged 12 of the 14 key components as either "compliant" or "largely compliant" (see Appendix 3 for the overview tables of compliance gradings). A "materially non-compliant" rating was assigned in two areas: Definition of capital and internal ratings-based (IRB) approach to credit risk. The review identified a number of areas of material (or potentially material) deviation in the draft regulations relating to the definition of capital, which are described in more detail in the report. For IRB credit risk, the material finding relates to the "permanent partial use" which allows IRB banks to risk-weight sovereign exposures according to the standardised approach (eg subject those claims denominated and funded in local currency to a 0% risk weight). A subsequent review will take place on the final regulations once available. It should be noted that the European Commission disagrees with these conclusions and believes that the findings overstate the degree of divergence from the Basel standards and that the section gradings have not been assigned consistently across jurisdictions.

The assessment of Japan was based on final regulations that will come into force from end March 2013 in line with the end of the fiscal year in Japan. Each of the 13 key components was assessed as either "compliant" or "largely compliant." For capital buffers (capital conservation and countercyclical), the domestic rules are not yet in place and hence the finding is "not yet assessed." The Japanese authorities plan to issue the rules by 2015, ie one year before the 2016 deadline. The overall grade of "compliant" is based on three facts/observations (i) the number of gaps is relatively low, (ii) gaps were found to be non-material, both in isolation and in aggregate, and (iii) the review recognised secondary legislation as generally binding.

The assessment of the United States was based on final rules implementing advanced approaches, the final rule on market risk and three notices of proposed rulemaking (NPRs) issued in June 2012. The assessment has highlighted the overarching issue of prolonged parallel run for banks on the advanced IRB and the advanced measurement approach (AMA), the only available options for credit and operational risk in the United States. At the time of the report, none of the core US banks had received permission to exit the transitional parallel run. As a result, US banks continue to determine their capital requirements based primarily on the Basel I framework, and the review noted there is little incentive for some core banks to move onto the more advanced approaches.

The US assessment team judged 12 of the 13 key components as "compliant" or "largely compliant". A "materially non-compliant" rating was assigned to securitisation exposures. It was noted that the US regulatory agencies' proposed implementation must conform with the prohibition on the use of external credit ratings, as required by the Dodd-Frank Act. The US authorities were unable to demonstrate that their alternative formulation of the rules would not result in weaker capital requirements than the Basel requirements. This will be subject to further follow-up analysis once final rules are in place. The US authorities believe that the US implementation of securitisation is likely to be at least as robust as the Basel standards.

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[11] *Policy measures to address Systemically Important Financial Institutions*, FSB, November 2011, available at www.financialstabilityboard.org/publications/r_111104bb.pdf.

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Level 3

Analysis of risk-weighted assets in the banking book

The Committee is also evaluating sources of material differences in risk-weighted assets (RWAs) across banks in the banking book. The Committee is assessing the extent to which differences in credit risk parameters based on the IRB approach for credit risk are driven by differences in risk levels or differences in practices – in the latter case the Committee will discuss whether the variations are consistent with relevant Basel standards.

Review of existing studies

The Committee has reviewed a wide range of existing analyses of RWAs across banks and countries to assess methodologies and identify possible drivers of RWA differences. The various studies highlighted many potential drivers, most of which suggested that RWA differences are driven by both risk-based[12] and practice-based[13] factors, although the relative focus on different drivers vary and no study could pinpoint the definitive causes of RWA differences. The review highlighted important lessons for the Committee's own analytical work:

- There is a need to carry out both top-down and bottom-up analyses while recognising the limitations of each method;
- Better analysis would be facilitated by using more complete (including non-public) data sources, and by collecting new and better data directly from selected banks; and
- An assessment of differences in specific practices by banks, national supervisors, and other sources such as accounting standards authorities can help better identify and understand ultimate drivers of RWA differences.

Top-down analysis

Drawing on these lessons, the Committee is undertaking further top-down analysis using supervisory data collected by the Committee as part of ongoing capital monitoring. The analysis covers 56 large, internationally active banking organisations and 44 non-internationally active banking organisations in 15 jurisdictions.

Preliminary findings indicate that corporate and retail exposures are the largest contributors to credit RWA and show the greatest variability in portfolio risk-weights across banks and countries. Risk-weights for bank and sovereign exposures may vary significantly across banks as well, but these asset classes are less significant contributors to credit RWA variations because of their low absolute risk-weights. Probability of default (PD) appears to be a significant source of RWA variability for the corporate, bank and sovereign asset classes. Loss given default (LGD) appears to be the more important risk parameter for the retail asset class, although LGD also is an important contributor to RWA variability for corporates.

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[12] Risk-based drivers are those that stem from differences in underlying risk at the exposure/portfolio level and in business models/strategies, including asset class mix.

[13] Practice-based drivers include differences in bank practices (eg approaches to risk management and measurement) and in the regulatory environment (eg supervisory practices, implementing laws and regulations including national discretion, accounting standards).

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Bottom-up portfolio benchmarking

The Committee is also conducting a bottom-up portfolio benchmarking exercise using a test portfolio of common exposures to supplement its top-down analysis. Thirty-three banks from 13 jurisdictions participated in the exercise by reporting PD and LGD estimates for a set of sovereign, bank, and corporate exposures. The data submitted by the banks is being reviewed to assess the variability of PD and LGD estimates across banks for common obligors and exposures.

Range of practices and on-site visits

Recognising the importance of overlaying the analytical work with an assessment of differences in bank and regulatory practices, the Committee has developed a list of potentially important practice-based drivers of RWA differences. This work draws on existing supervisory knowledge and judgement of the significance and prevalence of different practices. Based on this initial list of drivers and taking into account the preliminary findings from the top-down analysis, the Committee has identified certain risk measures (like probability of default) as areas where thematic reviews would be fruitful.

Depending on the results of these thematic reviews as well as the top-down and bottom-up analytical work, there may be a need to conduct more focused reviews of practices through on-site visits to banks in 2013.

Future direction

In early 2013, the Committee expects a final report summarising all findings regarding the relative importance of various sources and drivers of RWA variation, as well as the extent to which RWA differences do or do not reflect underlying differences in risk. Based on the conclusions of the work, the Committee may consider changes related to reporting and disclosure, as well as possible narrowing of the range of practices in some areas. Finally, the Committee will consider recommendations or options for ongoing monitoring and supervisory activities to foster RWA consistency in the future.

Analysis of risk-weighted assets in the trading book

The Committee is working on completing the analysis of variability of market risk measures across banks. The analysis is primarily based on publicly available information, but also considers the variability of supervisory data. Furthermore a test portfolio exercise has been undertaken, in which 15 large, internationally active banks participated.[14] The Committee expects to publish some results of this analysis by the end of this year.

Publicly available information and supervisory data

The analysis based on publicly available information so far reveals material differences in the ratio of the regulatory measure of market risk (market-risk RWA or mRWA) to total trading assets across the selected sample.[15] To the extent that such differences are driven by differences in risk taking – for example as a result of differences in business models or trading strategies – the variation should not be a cause for concern. An analysis of the

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[14] It should be noted that there is some overlap between the sample of banks used in the analysis based on public data and the test portfolio exercise; however, it is not one for one. The test portfolio exercise was conducted based on the condition of anonymity of the participating banks and therefore no cross-references can be made between the participating banks in both analyses.

[15] The ratio of mRWA-to-total trading assets has been adjusted for the effect of differences in accounting standards that banks apply across different jurisdictions. See also the June 2012 report of the Basel Committee to the G20 Leaders, available at www.bis.org/publ/bcbs220.pdf.

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composition of trading assets provides some support to this view, as it shows that banks with a higher ratio of mRWA to total trading assets typically have a greater proportion of risky trading assets on the balance sheet, including distressed debt and illiquid equity. However, even after addressing these factors, there remains material unexplained variation in mRWA across banks. Other possible factors that might explain such a variation are:

- differences in supervisory approaches (such as the timing of Basel 2.5 adoption);
- differences in the use of capital add-ons or multipliers;
- methodological choices; or
- the degree of reliance of banks on internal model approaches versus standardised approaches.

A key finding is that data available in public information generally does not appear sufficient to fully explain the variation in mRWA across banks, nor to explain the variation in mRWA for a single bank over time. Limits to the detail of public disclosure can be explained by banks' desire to keep their trading strategies and positions private for competitive reasons. However these shortcomings in disclosure make cross-bank comparison difficult. Some banks provide more detailed and useful disclosures than others and minimal guidance across jurisdictions adds to inconsistencies in content. In some jurisdictions, Basel II Pillar 3 reports were not available for the analysis.

The Committee is therefore considering broadening its analysis to investigate the utility of consistent supervisory data in explaining differences in mRWA. An initial finding is that supervisory data collection, while consistent within jurisdictions, is not consistent across jurisdictions. Some jurisdictions collect only limited additional data for supervisory purposes. It must be noted, however, that in some jurisdictions efforts are underway to improve the regulatory data collection related to banks' trading books. These supervisory efforts may suggest options for more consistent patterns of disclosure across banks.

Test portfolio exercise

To further examine the modelling choices that potentially drive differences in mRWA, the Committee conducted a test portfolio exercise. The test portfolios and accompanying questionnaires were designed to cover a range of trading portfolios and trading strategies, which closely represented but were generally less complex than banks' actual portfolios and trading strategies. A total of 15 large, internationally active banks from nine jurisdictions participated in the exercise. The participating banks calculated for each hypothetical test portfolio the outcome of their internally modelled risk measures and provided detailed information regarding their modelling assumptions through supplemental questionnaires. This allowed the Committee to identify modelling choices that drive potential variation in mRWA.

To investigate the results in more detail, a programme of on-site visits was initiated in which 9 participating banks were visited by international teams of supervisors. The objective of the visits was to gain further understanding of the market risk models that the banks use and to investigate in more detail the causes of variability identified across banks.

The initial results from the test portfolio exercise suggest there is generally less variability observed for internal models that have been in use for a long time. In addition, the variability is generally less for models where there are more regulatory constraints.

Next steps

The Committee will further elaborate on the initial findings and possible policy options. Regarding the analysis of public data, one expectation of the outcome of this exercise could

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be suggestions related to improvements in public disclosures for mRWA calculations. With regard to the analysis of the test portfolio exercise, a final quantification of the level of variability of each internal model for each portfolio in the exercise is expected. The findings will also serve as input for the Committee's current fundamental review of the trading book.[16]

The analysis suggests that there is a direct relationship between complexity of risk metric/product and the associated variability of the metric across banks. The current test portfolio exercise was based on a set of plain vanilla portfolios and excluded the most complex market risk models that are used by banks. The Committee believes it is important to consider more complex products and models in a future exercise. A follow-up test portfolio exercise including more complex portfolios is therefore being considered for 2013.

Further work

Level 1

The Committee will continue to publish progress reports every six months. The next report will be published in April 2013 showing the position as at end March 2013.

Level 2

A Level 2 assessment of Singapore is underway and the report will be published in April 2013. A review of Switzerland will commence in early 2013 followed by China in the second quarter. Reviews of Australia, Brazil and Canada will commence in the second half of 2013. Follow-up reviews of the European Union and the United States will commence after final regulations are published and will cover the final rules in their entirety. The reviews will assess whether identified gaps have been rectified but will also check for issues that were not present in the draft regulations.

At present, the Committee is conducting a "lessons learnt" review to reflect on the experience of the first three Level 2 reviews.

Level 3

Findings of the Level 3 assessments for the banking book and trading book will be reported to the Committee around the end of 2012 or early 2013. Further analysis will be conducted in 2013, and, subject to decisions at a later stage, will continue on an ongoing basis. Further policy development work may be necessary to address the findings.

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[16] *Fundamental review of the trading book - consultative document,* May 2012, www.bis.org/publ/bcbs219.htm.

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Appendix 1

Level 1 charts

Status of Basel II adoption (October 2012)

Jurisdiction	Basel II	Next steps – Implementation plans
Argentina	1, 4	(1) On-going work to assess the migration from Basel I to the Basel II standardised approach for credit risk. (4) Final rules for operational risk published and came into force on 30 April 2012
Australia	4	
Belgium	4	
Brazil	4	
Canada	4	
China	4	New capital regulation that combines Basel II, 2.5 and III was released in June 2012 and will be effective on 1 January 2013. The new capital regulation will be applied to all banking institutions supervised by the CBRC.
France	4	
Germany	4	
Hong Kong SAR	4	
India	4	
Indonesia	3, 4	(3) Pillar 2 and Pillar 3 to be implemented from December 2012. (4) Pillar 1 (all elements based on standardised approaches) implemented.
Italy	4	
Japan	4	
Korea	4	
Luxembourg	4	
Mexico	4	
The Netherlands	4	
Russia	1, 4	(1) Pillar 2 expected to be implemented not earlier than 2014. Pillar 3 expected to be implemented not earlier than 2013. (4) Simplified standardised approach for credit risk, simplified approach for market risk and the Basic Indicator Approach for operational risk implemented.
Saudi Arabia	4	
Singapore	4	

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South Africa	4	
Spain	4	
Sweden	4	
Switzerland	4	
Turkey	4	
United Kingdom	4	
United States	4	Parallel run on-going – All Basel II mandatory institutions are required to implement the advanced approaches to credit risk and operational risk. Banks have made significant progress in implementation efforts and those institutions in parallel run are reporting both Basel I and Basel II regulatory capital ratios to supervisors on a quarterly basis. US institutions in parallel run remain subject to Basel I capital requirements.
European Union	4	

Number and colour code: 1 = draft regulation not published; 2 = draft regulation published; 3 = final rule published; 4 = final rule in force. Green = implementation completed; Yellow = implementation in process; Red = no implementation.

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Status of Basel 2.5 adoption (October 2012)

Jurisdiction	Basel 2.5	Next steps – Implementation plans
Argentina	1	On-going work to draft preliminary documents.
Australia	4	
Belgium	4	
Brazil	4	
Canada	4	
China	4	New capital regulation that combines Basel II, 2.5 and III was released in June 2012 and will be effective on 1 January 2013. The new capital regulation will be applied to all banking institutions supervised by the CBRC.
France	4	
Germany	4	
Hong Kong SAR	4	
India	4	
Indonesia	1	Securitisation exposures in Indonesia are currently insignificant and prospects remain highly subdued for any material issuance. However, the regulation concerning Prudential Requirement on Asset securitisation for banks has been issued since 2005. No bank has adopted the internal model approach (IMA) for market risk capital charge although the relevant regulation has been issued since 2007.
Italy	4	
Japan	4	
Korea	4	
Luxembourg	4	
Mexico	1	Pillar 2 provisions are partially implemented. The remaining aspects will be implemented during 2012 and 2013, as well as the requirements under Pillar 3.
The Netherlands	4	
Russia	1, 2	(1) Pillar 2 expected to be implemented not earlier than 2014. (2) Final regulation (revision to the simplified approach for market risk) adopted and signed by the Governor (Regulation as of 28.9.2012 No. 387-P) and expected to be published in October, and come into force on 1 February 2013.
Saudi Arabia	3	Final regulations will be enforced by 31 December 2012.
Singapore	4	
South Africa	4	
Spain	4	
Sweden	4	(4) Final rules for the Basel 2.5 agreement are in force, including liquidity management and remuneration. The supplementary Pillar 2 guidance is in use. However a new national ICAAP guideline is still under development.

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Switzerland	4	
Turkey	4	
United Kingdom	4	
United States	2, 3	(3) Final market risk capital requirements which incorporate Basel 2.5, as well as restrictions on the use of credit ratings as set forth in the Dodd-Frank regulatory reform legislation approved in June 2012. Market risk requirements are effective as of 1 January 2013. (2) Other Basel 2.5 revisions included as part of the proposed Basel III rule approved in June 2012. The US banking agencies intend to finalise the rule after consideration of public comments.
European Union	4	Final date for full transposition by member states of the European directive implementing Basel 2.5: 31 December 2011.

Number and colour code: 1 = draft regulation not published; 2 = draft regulation published; 3 = final rule published; 4 = final rule in force. Green = implementation completed; Yellow = implementation in process; Red = no implementation.

A revised version of this document was published in April 2013. http://www.bis.org/publ/bcbs249.htm

Status of Basel III adoption (October 2012)

Jurisdiction	Basel III	Next steps – Implementation plans
Argentina	1	On-going work to draft preliminary documents.
Australia	3, 2	(3) Final rules for capital requirements issued on 28 September 2012. Draft rules to implement liquidity requirements issued in November 2011. (2) Draft rules for counterparty credit risk issued on 10 August 2012
Belgium	(2)	(Follow EU process)
Brazil	2	Draft regulation published. Consultation process is over and final adjustments are being made.
Canada	2	On 1 February 2011, banks were directed to meet the 7% CET1 standard as of January 2013. Regulations for (i) non-viability contingent capital and (ii) transitioning for non-qualifying instruments published August and October 2011 respectively. Comprehensive capital regulation (CAR Guideline) issued for public comment on 7 August 2012.
China	3	New capital regulation that combines Basel II, 2.5 and III was released in June 2012 and will be effective on 1 January 2013. The new capital regulation will be applied to all banking institutions supervised by the CBRC.
France	(2)	(Follow EU process)
Germany	(2)	(Follow EU process)
Hong Kong SAR	3	Final rules for capital standards issued on 19 October 2012 and will come into force on 1 January 2013.
India	3	Final capital regulations issued on 2 May 2012 which come into force from 1 January 2013. Draft guidelines on liquidity standards issued in February 2012.
Indonesia	2	Consultative paper on Basel III, which contains draft regulation released in June 2012 for industry comments.
Italy	(2)	(Follow EU process)
Japan	3	Final rules published on 30 March 2012 – Implementation of final rules (end of March 2013 – In Japan, the fiscal year for banks starts in April and ends in March). Rules covering capital conservation buffer and the counter-cyclical buffer not yet issued. Draft regulations expected in 2014/15.
Korea	2	Draft regulation published on 27 September 2012.
Luxembourg	(2)	(Follow EU process)
Mexico	2	Draft rules published on 31 May 2012.
The Netherlands	(2)	(Follow EU process)
Russia	2	Draft regulations for capital definition and capital adequacy ratios published for public consultation in September 2012.

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		Draft regulations for leverage ratio to be published by November 2012.
Saudi Arabia	3	Final regulation issued to banks.
Singapore	3	Final rules published on 14 September 2012.
South Africa	2	Draft amendments to legislation issued on 28 September 2012 for final review.
Spain	(2)	(Follow EU process)
Sweden	(2)	(Follow EU process)
Switzerland	3	Final regulation on Basel III (incl SIFI) published. Minor amendments on final rule text expected before end 2012 (also to implement latest Basel III rules updates as published by BCBS in July 2012). Started LCR test-reporting beginning of 2012. Public consultation on draft regulation of Basel III liquidity reporting requirements starting in August 2012. Decision on final rules by Federal Council in Q4 2012. Enactment on final rule by beginning of 2013.
Turkey	1	Draft regulation expected to be published in the second half of 2012.
United Kingdom	(2)	(Follow EU process)
United States	2	Joint notice of proposed rulemaking approved in June 2012. The US agencies intend to finalise the rule after consideration of public comments. Basel 2.5 and Basel III rulemakings in the United States must be coordinated with applicable work on implementation of the Dodd-Frank regulatory reform legislation.
European Union	2	5th Council Presidency's compromise proposal agreed on 15 May 2012; Draft European Parliament Legislative Resolution agreed on 14 May 2012; The European Parliament, Council and the Commission currently in discussions to agree on a final text.

Number code: 1 = draft regulation not published; 2 = draft regulation published; 3 = final rule published; 4 = final rule in force.

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Appendix 2

Level 2 process

1. Assessment framework

Background and objectives

Full, timely and consistent implementation of Basel III is fundamental to raising the resilience of the global banking system, in maintaining market confidence in regulatory ratios, and in providing a level playing field.

Reflecting the importance of implementation, the Committee has agreed to establish a programme to assess its members' implementation of Basel III. The implementation assessment programme is comprised of three levels of review:

- Level 1: ensuring the timely adoption of Basel III;
- Level 2: ensuring regulatory consistency with Basel III; and
- Level 3: ensuring consistency of risk-weighted asset outcomes.

This document describes the Level 2 review process, which assesses the compliance of domestic regulations implementing Basel III with the international minimum requirements defined by the Basel Committee. By identifying domestic regulations and provisions that are not consistent with the rules agreed by the Committee and by assessing their impact on financial stability and on the international level playing field, this process will promote full and consistent implementation of Basel III. It will also facilitate an effective dialogue among members and provide peer pressure if needed. The conclusions following each jurisdiction's assessment will be published by the Committee.

This assessment programme supports the Financial Stability Board's monitoring of the implementation of the agreed G20/FSB financial reforms and is fully consistent with the "*Coordination Framework for Monitoring the Implementation of Agreed G20/FSB Financial Reforms*" put in place by the FSB.[17]

The Basel Committee's implementation assessment programme and the Financial Sector Assessment Program (FSAP), which is conducted by the International Monetary Fund and the World Bank (and which assesses jurisdictions' compliance with the Basel Committee's Core Principles for Effective Banking Supervision), have different scopes and focuses and will complement each other. In particular, the Basel III Level 2 assessment programme described in this document provides a narrower but deeper focus on the regulatory consistency with Basel III, while the assessment of the Core Principles considers the full range of the regulatory framework and supervisory practices.

[17] Available at www.financialstabilityboard.org/publications/r_111017.pdf.

Scope of the assessments

Basel III builds upon and enhances the regulatory framework provided by Basel II and Basel 2.5 (ie the July 2009 enhancements to Basel II), which now form integral parts of the Basel III framework. The assessments will thus cover the full set of components, including those introduced by Basel II and 2.5 (see the annex for the detailed scope). This full set of requirements is referred to as "Basel III" in this document.

Basel III's liquidity ratios and the leverage ratio along with the additional loss absorbency requirement for global systemically important banks (G-SIBs) will be included in the assessments after the Committee concludes its review on any revisions or final adjustments, consistent with the agreed phase-in arrangements.

Certain jurisdictions, given their economic and development situation, that choose not to adopt some or all of the advanced approaches of Basel III for the measurement of risks will not be considered non-compliant when their compliance with the relevant provisions of Basel III is assessed; these provisions will be considered as non-applicable, in line with the approach adopted by the Committee when developing Basel II.[18]

Schedule of the assessments

All Basel Committee member countries will be assessed following the process presented in this document, with the first reviews commencing in 2012. Given the resources available and the intensity of the assessments planned, the Committee will not be able to review all countries at the same time and will do a limited number of reviews per year, with initial priority given to countries with G-SIBs. Nevertheless, it is intended that all jurisdictions will be covered over a multi-year timetable.

Given the limited discretion available for EU member countries, the focus of the review for the EU and its member countries will be the EU level regulations. A report on the European Union will be supplemented with a summary of the discretions exercised at the country level by each EU member country, but country specific reports will not be prepared.

Particularly in the early phases of the assessment programme, some assessments (or parts of them) might be based on draft or proposed domestic regulations. The part of any assessments based on non-final and non-binding documents will only be regarded as preliminary assessments and will be supplemented at a later stage by a follow-up assessment of the final domestic regulation. Preliminary assessments based on draft or proposed domestic regulations will be clearly distinguished from the assessments based on the final and complete regulations.

2. Assessment methodology

General approach

The objective of the assessment is to ensure that domestic regulations implementing Basel III comply with the agreed international minimum requirements. Although this document refers to "regulations", the term is used solely for simplicity: the Committee is aware that

[18] Paragraph 7 of the Basel II document and its Simplified Standardised Approach in Annex 11 show the Committee's intention to provide a range of options to allow supervisors to select approaches that are most appropriate for their financial market infrastructure.

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Basel III can be implemented by different means depending on the legal and regulatory framework within a given jurisdiction. For the purpose of assessing compliance, the Committee will consider all binding documents that effectively implement Basel III.

The Level 2 assessment will focus on reviewing the **content** of domestic regulations (the extent to which Basel III is effectively enforced by supervisors or whether firms are actually complying with the rules of the Basel III framework will be assessed as part of the Level 3 assessment process). The assessment of compliance with the international rules will primarily be factual and will be based on two aspects:

- a comparison of domestic regulations with the international agreements to identify if all the required provisions of Basel III have been adopted (completeness of the regulation); and
- independent of the form of the requirements, whether there are any differences in substance between the domestic regulation and the international agreement (consistency of the regulation).

When a gap or a difference is identified, a key driver for assessing compliance will be its materiality and impact. To the extent possible, the materiality and impact will be quantified using all available data, including those submitted by the jurisdiction being assessed. The assessment will, in particular, seek to measure the significance of any identified difference(s) for internationally active banks or certain types of firms or businesses. The assessment will consider the current impact and consequences, but also its potential impact in the future.

The assessment will also seek to clarify the rationale for any identified gaps and differences between the domestic provisions and the corresponding international rules, with a view to ensuring a firm understanding of the specificities and drivers of local implementation. However, these elements will not be taken into account when assessing compliance: local specificities will not be seen as mitigants for going beyond the scope of national discretion specified within Basel III.

Domestic measures that strengthen the minimum requirements are fully in line with the nature of the international agreements, which are intended to set minimum requirements, and will therefore be considered as compliant. However, they will not be considered to compensate for inconsistencies or gaps identified elsewhere, unless they fully and directly address the identified inconsistencies or gaps.

Compliance scale

All assessments will be summarised using a four-grade scale: compliant, largely compliant, materially non-compliant and non-compliant.[19]

- Regulatory framework is *compliant* with Basel III: A regulation will be considered compliant with Basel III if all minimum provisions of the international framework have been satisfied and if no material differences have been identified which would give rise to prudential concerns or provide a competitive advantage to internationally active banks.

[19] This four-grade scale is consistent with the approach used for assessing countries' compliance with the Basel Committee's Core Principles for Effective Banking Supervision. The actual definition of the four grades has however been adjusted to take into account the different nature of the two exercises In addition, and as noted above, components of Basel III that are not relevant to an individual jurisdiction may be assessed as non-applicable.

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- Regulatory framework is *largely compliant* with Basel III: A regulation will be considered largely compliant with Basel III if only minor provisions of the international framework have not been satisfied and if only differences that have a limited impact on financial stability or the international level playing field have been identified.
- Regulatory framework is *materially non-compliant* with Basel III: A regulation will be considered materially non-compliant with Basel III if key provisions of Basel III have not been satisfied or if differences that could materially impact financial stability or the international level playing field have been identified.
- Regulation is *non-compliant* with Basel III. A regulation will be considered non-compliant with Basel III if Basel III has not been adopted or if differences that could severely impact financial stability or the international level playing field have been identified.

The outcome of the assessment process is expected to take the form of an overall assessment of the compliance of the jurisdiction's regulation with Basel III and assessments of the compliance of the jurisdiction's regulation for each of the key components of the capital framework as listed in the annex.

3. Assessment process

Each assessment will be based on peer review, and have three main steps: a preparatory phase, the assessment phase itself, and the review phase that will result in the approval of the conclusions of the assessment. A follow-up phase will also occur at a later point in time.

Phase 1: Preparatory phase

The preparatory phase will be used to establish the assessment team and to collect the relevant material.

(a) Establishment of assessment teams

Ad-hoc assessment teams will be established to conduct the assessment of individual jurisdictions. A typical team will involve 5-7 persons, comprising:

- a team leader with seniority and/or experience equivalent to those of a Committee member
- selected experts from member authorities; and
- member(s) of the Basel Committee Secretariat.

(b) Collection of Information and data

The preparatory phase will be used to collect the information needed for supporting the assessment. Jurisdictions will be requested to answer a detailed self-assessment questionnaire, using a standardised template, and to provide all components of the domestic regulation that implement Basel III at the domestic level. Relevant background documents should also be communicated, including in particular copies of the most recent FSAPs or other external assessments which cover capital adequacy regulation. The jurisdiction should also transmit any other document that could usefully inform the assessment.

Phase 2: Assessment phase

The assessment phase will rely on a combination of off-site and on-site assessments.

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(a) Off-site assessment

The assessment team will analyse the compliance of the domestic regulations using all the information provided by the jurisdiction, as well as other relevant information available to the Basel Committee. The assessment team may choose to consult the authorities within the jurisdiction being assessed during this period to seek additional information or clarification, or might consult relevant expert groups of the Basel Committee for an indicative view on certain technical issues. This phase should primarily seek to identify the issues that will need to be explored and discussed in more detail during the on-site review.

(b) On-site assessment

As a general principle, on-site reviews are expected to be conducted as part of the assessment process. On-site reviews will provide the best opportunity to ensure the correct understanding of issues related to the adoption and implementation of Basel III identified during the off-site review, by having exchanges with relevant experts and the senior authorities responsible for the transposition of Basel III into domestic regulations. The length and content of each on-site review will be set based on the complexity of the domestic implementation and on the materiality of the issue identified.

Domestic banking regulators and supervisors are expected to be the key counterparts of the assessment team during the on-site reviews, but meetings with other relevant parties (including the finance ministry or treasury, industry representatives, accounting representatives, analysts) may also take place to ensure that the assessment team collects a broad range of views and develops a sound understanding of local regulatory requirements. If scheduled, meetings with the private sector are expected to take place without the participation of representatives of the domestic authorities.

(c) Drafting of the assessment report

The information collected during the off-site and the on-site assessments will be used to prepare an assessment report. Jurisdictions being assessed will be given an opportunity to comment on the draft report before it is presented for the review phase.

Phase 3: Review phase

The review phase corresponds to the review of the assessment by a broader set of peers, the finalisation and approval of the report, and its subsequent publication.

(a) Review by the Standards Implementation Group

The substantive review by a broader set of peers will take place in the Standards Implementation Group (SIG) of the Basel Committee. The key objectives of the SIG's review of the assessment report are to (i) agree on the conclusions of the assessment and on the content of the report and (ii) to ensure that the assessment is consistent with the agreed methodology and the other assessments already performed. As part of this process, the jurisdiction being assessed will have the opportunity to present its views on the findings of the assessment report to the SIG.

(b) Approval by the Basel Committee

The Basel Committee has the final responsibility for approving the assessment report. The assessments will be approved by consensus. The representatives of the jurisdiction assessed will not take part in the decision making but their views will be reflected in a separate section of the report if needed. If full consensus cannot be reached during the Committee meeting to which the report is presented, minority views will be footnoted in the report.

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(c) Publication and communication of the assessments

After having been formally approved by the Committee, the report, including if applicable the separate views from the assessed jurisdiction, will be published on the Committee's website. The Committee member assessed will also be invited to publish the report in their home jurisdiction.

The report will also be transmitted to the FSB, consistent with its "*Coordination Framework for Monitoring the Implementation of Agreed G20/FSB Financial Reforms.*"

The main conclusions of the assessments will be periodically summarised and reflected in updates of the Committee's *Progress report on Basel III implementation*, to provide a comprehensive view of the situation across member countries.

Phase 4: Follow-up

The Committee will continue to monitor whether its members are updating their domestic regulations or introducing new regulations that could impact the assessments already performed. Where substantial regulatory developments or changes that could have a material impact on existing assessments take place, the Committee will take steps to update these assessments in a reasonable timeframe. The Committee may also update assessments when it concludes its review on any revisions or final adjustments of certain components of Basel III.

While the main objective of the assessment process is to ensure a full and consistent implementation of Basel III across countries, the process is also expected to usefully inform the Committee about implementation challenges or difficulties that countries may have faced or are facing when adopting Basel III. The process is also expected to contribute to identify potential gaps or interpretative issues within the Basel III framework. These elements, in combination with the outcome of its quantitative monitoring of Basel III impact, will be taken into account by the Basel Committee when determining its policy agenda and might result in issuing additional guidance or updating the rules if needed.

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Scope of the assessment

Key components of the Basel framework	Inclusion in the assessments
Capital requirements	
Scope of application	Included
Transitional arrangements	Included
Definition of capital	Included
Pillar 1: Minimum capital requirements	
Credit Risk: Standardised Approach	Included
Credit risk: Internal Ratings-Based approach	Included if adopted
Credit risk: securitisation framework	Included
Counterparty credit risk rules	Included
Market risk: standardised measurement method	Included
Market risk: internal models approach	Included if adopted
Operational risk: Basic Indicator Approach and Standardised Approach	Included
Operational risk: advanced measurement approaches	Included if adopted
Capital buffers (conservation and countercyclical)	Included
G-SIB additional loss absorbency requirements	Included if relevant (1)
Pillar 2: Supervisory Review Process	
Legal and regulatory framework for the Supervisory Review Process and for taking supervisory actions	Included
Pillar 3: Market Discipline	
Disclosure requirements	Included
Liquidity standards	
Scope of application	Included (1)
Transitional arrangements	Included (1)
Liquidity Coverage Ratio	Included (1)
Net Stable Funding Ratio	Included (1)
Leverage ratio	
Leverage ratio	Included (1)

(1) To be included after the Committee concludes its review on any revisions or final adjustments.

A revised version of this document was published in April 2013. http://www.bis.org/publ/bcbs249.htm

Appendix 3

Overview table of compliance grading (European Union)

Key components of the Basel framework	Grade
Overall Grade	Not yet assigned given the preliminary nature of the findings
Capital requirements	
Scope of application	(C)
Transitional arrangements	(C)
Definition of capital	(MNC)
Pillar 1: Minimum capital requirements	
Credit Risk: Standardised Approach	(LC)
Credit risk: Internal Ratings-Based approach	(MNC)
Credit risk: securitisation framework	(C)
Counterparty credit risk rules	(LC)
Market risk: standardised measurement method	(LC)
Market risk: internal models approach	(C)
Operational risk: Basic Indicator Approach and Standardised Approach	(LC)
Operational risk: advanced measurement approaches	(LC)
Capital buffers (conservation and countercyclical)	(C)
G-SIB additional loss absorbency requirements	(1)
Pillar 2: Supervisory Review Process	
Legal and regulatory framework for the Supervisory Review Process and for taking supervisory actions	(C)
Pillar 3: Market Discipline	
Disclosure requirements	(C)
Liquidity standards	
Scope of application	(1)
Liquidity Coverage Ratio	(1)
Net Stable Funding Ratio	(1)
Leverage ratio	
Leverage ratio	(1)

Compliance assessment scale: C (compliant), LC (largely compliant), MNC (materially non-compliant) and NC (non-compliant). Definitions of the compliance scale are found in the foreword of the full document. Ratings that are based on draft or proposed rules are indicated within parentheses. Ratings based on final rules are indicated without parentheses. (1) To be assessed after the Committee concludes its review on any revisions or final adjustments of these elements of Basel III.

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Overview table of compliance grading (Japan)

Key components of the Basel framework (and number of elements)	Grade
Overall Grade:	C
Capital requirements	
Scope of application	C
Transitional arrangements	C
Definition of capital	(LC)
Pillar 1: Minimum capital requirements	
Credit Risk: Standardised Approach	C
Credit risk: Internal Ratings-Based approach	C
Credit risk: securitisation framework	LC
Counterparty credit risk rules	C
Market risk: standardised measurement method	LC
Market risk: internal models approach	C
Operational risk: Basic Indicator Approach and Standardised Approach	C
Operational risk: advanced measurement approaches	C
Capital buffers (conservation and countercyclical)	"Not yet assessed"
G-SIB additional loss absorbency requirements	(1)
Pillar 2: Supervisory Review Process	
Legal and regulatory framework for the Supervisory Review Process and for taking supervisory actions	C
Pillar 3: Market Discipline	
Disclosure requirements	C
Liquidity standards	
Scope of application	(1)
Transitional arrangements	(1)
Liquidity Coverage Ratio	(1)
Net Stable Funding Ratio	(1)
Leverage ratio	
Leverage ratio	(1)

Compliance assessment scale (See foreword of full document for more information): C (compliant), LC (largely compliant), MNC (materially non-compliant) and NC (non-compliant). (1) To be assessed after the Committee concludes its review on any revisions or final adjustments of these elements of Basel III. Ratings that are based on draft or proposed rules are indicated within parentheses. Ratings based on final rules are indicated without parentheses.

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Overview table of compliance grading (United States)

Key components of the Basel framework	Grade
Overall Grade:	Not yet assigned given preliminary nature of findings
Capital requirements	
Scope of application	C
Transitional arrangements	(C)
Definition of capital	(LC)
Pillar 1: Minimum capital requirements	
Credit Risk: Standardised Approach	(LC)
Credit risk: Internal Ratings-Based approach	(LC)
Credit risk: securitisation framework	(MNC)
Counterparty credit risk rules	(LC)
Market risk: standardised measurement method	C
Market risk: internal models approach	C
Operational risk: Basic Indicator Approach and Standardised Approach	N/A*
Operational risk: advanced measurement approaches	LC
Capital buffers (conservation and countercyclical)	(C)
G-SIB additional loss absorbency requirements	(1)
Pillar 2: Supervisory Review Process	
Legal and regulatory framework for the Supervisory Review Process and for taking supervisory actions	C
Pillar 3: Market Discipline	
Disclosure requirements	(C)
Liquidity standards	
Scope of application	(1)
Liquidity Coverage Ratio	(1)
Net Stable Funding Ratio	(1)
Leverage ratio	
Leverage ratio	(1)

Compliance assessment scale: C (compliant), LC (largely compliant), MNC (materially non-compliant) and NC (non-compliant). Definitions of the compliance scale are found in the Foreword of the full document. Ratings that are based on draft or proposed rules are indicated within parentheses. Ratings based on final rules are indicated without parentheses. (1) To be assessed after the Committee concludes its review on any revisions or final adjustments of these elements of Basel III.

* The Basel standards do not explicitly require implementation of standardised approaches in addition to the advanced measurement approach