Comments on the Supervisory Framework for Measuring and Controlling Large Exposures – 28 June 2013

Submitted by: Standard Bank Group (SBG)

Reference to paper	**Comment**
Introductory remarks	
General	• In isolation certain individual components of the large exposure framework appear to be reasonable. • However, when considered in totality, it appears overly cumbersome and impractical.
Introduction	
Objective of the large exposures framework	
General	None
Overall design of a prudential framework for large exposures	
Definition of large exposures	
1. The Committee welcomes views on the proposed definition of large exposures and on the proposal for reporting.	The reporting threshold of 5% may result in an operational burden issue • The conservative measures of exposure that are proposed to be used would lead to more counterparties being included in reporting • Banks would be forced to monitor the exposures of a wider population of counterparties, even those below the 5% threshold, to make sure that a counterparty is reported once it reaches the threshold. • A bank cannot monitor ALL counterparties (e.g. retail customers) individually

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	The reporting of >5% may prove rather burdensome and the hard limits “in the context of interbank exposures in a small market with few dominant players, and i.t.o. the impact of liquidity” could be problematic.
Definition of connected counterparties	
2. The Committee welcomes views on the criteria proposed for the identification of connected counterparties when they pose a single risk.	• Guidelines / rules re interconnectedness may be useful. • Instead of a Pillar 1 approach to connected counterparties based on economic interdependence the Basel framework should require banks to have auditable credit risk management policies in place to monitor and manage connected relationships that result in material exposures.
Definition and calculation of the large exposure limit	
Capital measure – definition of eligible capital	
3. The Committee welcomes views and quantitative information on whether the limit should be based on CET1 or Tier 1.	Noted
Exposure measure – definition of exposure	
4. The Committee welcomes views on the extent and nature of the use of internal models (when they have received supervisory approval for being used for Pillar 1 capital requirements purposes) to measure large exposures.	• To the extent that internal models are used to capture risk, these should be used in the large exposure framework as well. • Model Risk - All approaches have some degree of model/estimation risk. Simple models are likely to be conservative, which means that transactions may be excluded solely due to the conservatism arising from the election of a simple measure over a more accurate one. • For banks to create an entirely separate process for large exposures that would neither be used for risk nor for regulatory purposes would be costly and could lead to increased operational risk since it is not fully integrated into firms’ existing processes.

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OTC derivatives	
5. The Committee welcomes views on the proposal to calculate exposure value of banks' investments in OTC derivatives.	• If a bank has been approved by its regulator to use the IMM, then it should be allowed to use it for large exposure purposes as well.
Securities Financing Transactions	
6. The Committee welcomes views on the proposal for how the exposure values of banks' investments in securities financing transactions should be calculated, in particular on the need to deviate from the risk-based capital requirement rules given the objectives of a large exposures framework.	• There are alternative approaches for measuring exposure that address model risk while ensuring appropriate exposure measures are achieved. Regulators, for example, could prescribe inputs relating to volatility and correlation, as well as confidence levels, which could be used in banks' internal models.
Traditional off-balance sheet items	
7. The Committee welcomes views on the proposal to generally apply a 100% CCF for "traditional" off-balance sheet commitments.	• If the use of supervisory CCFs is applied, they should be aligned with the CCFs under Basel II.
Credit risk mitigation techniques	
8. The Committee welcomes views on the proposed hybrid approach for banks that apply the "comprehensive approach" to financial collaterals.	• If a bank has purchased single-name protection on a diversified portfolio of counterparty exposures, it is inconceivable that all underliers and protection providers would default simultaneously with no recovery as is implied by the proposed requirement. • There is implicit assumption of double default in the proposed substitution approach for the covered position of a collateralized or credit protected exposure. Absent wrong-way risk resulting from a strong correlation between the protection provider or collateral issuer and the underlier or counterparty exposure, the likelihood of double default, or simultaneous failure of both the protection provider and the underlier or counterparty, is low.

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Calculation of exposure value for trading book positions	
9. The Committee welcomes views on whether the approach proposed for calculating exposure values for trading book positions raises specific issues.	Noted
10. The Committee welcomes views on the proposals for offsetting long and short positions, in particular when these positions are in different issues.	Noted
Treatment of specific exposure types	
Interbank exposures	
11. The Committee welcomes comments on the proposal regarding interbank exposures and in particular in which cases specific exemptions would be warranted.	Noted
Exposures to CCPs	
12. The Committee welcomes comments on the calibration of the granularity threshold and whether the mandatory application of the look-through approach to the transaction where an underlying exposure may exceed the granularity threshold will raise specific issues.	• The 1% threshold for determining whether LTA should be reconsidered and potentially increased. • The underlying investments in many managed funds are accounted for on a mark-to-market basis. Consequently, investment volatilities could mean that a fund could move quickly from being “granular” to “non-granular”. If bank funding is conditional on these reporting requirements being met in the event a fund becomes “non-granular” and this triggers early repayment, this could have a material adverse impact on the financial position and liquidity of the fund.
13. The Committee welcomes comments on the proposals for the treatment of the identified additional risks in the large exposures framework.	Noted
14. The Committee welcomes views on the options for the treatment of banks’ exposures to CCPs.	Noted

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Exposures to funds and securitization vehicles	
	• We suggest that the most senior securitization tranches be exempted from the large exposure regime. This is to recognize the structural features of securitizations that reduce both loss probabilities and loss severity for the most senior tranches.
Large exposures rules for global systemically important banks	
General	• Large exposure limit applied to a G-SIB's exposure to another G-SIB should be between 10% and 15% of CET1 or Tier 1 - concerned about the proposed lower limit for inter G-SIBs exposures. • This would particularly be a concern if local regulator applies this rule to D-SIBS.
Transitional arrangements	
General	Noted