Standard Bank

Comments on the Revised Basel III Leverage Ratio framework – 20 September 2013

Submitted by: Standard Bank Group (SBG)

Reference to paper	Comment
Introductory remarks	
General	• With the leverage ratio framework being more of an accounting measure than a regulatory measure it is likely that both these frameworks can result in restrictions at different points in time. The risk sensitive capital adequacy ratio should be the primary focus with leverage as the secondary focus. • The proposal introduces a move towards a risk adjusted view of the exposure measure (somewhere between regulatory and accounting) which in turn results in further complexity. Is it still the intention for this ratio to be a simple non-risk sensitive backstop ratio? • We propose that BIS keep pillar 1 leverage ratio requirement low and any specific bank concerns based on portfolio be addressed under Pillar 2 and any bank specific jurisdictional adjustments be addressed. • Certain aspects of the proposed framework could have an adverse effect on the availability and affordability of trade finance and could result in reduced global trade flows at a time when they are essential to support economic recovery (refer to detailed comments). • The inclusion of off-balance sheet exposure in the leverage ratio could dramatically impede the flow of financing to importers and exporters - particularly in emerging markets. • Banks are increasingly making balance sheet decisions now on what types of financing to conduct and the denominator of the leverage ratio, as currently constructed, will influence

<table>
<tr><th>Reference to paper</th><th>Comment</th></tr>
<tr><td></td><td>those decisions and could harm economic growth and international trade in order to optimize return.</td></tr>
<tr><td colspan="2">Exposure Measure</td></tr>
<tr><td colspan="2">General measurement principles</td></tr>
<tr><td>The proposed framework states that physical or financial collateral, guarantees or credit risk mitigation purchased are not allowed to reduce on-balance sheet exposures</td><td>It is proposed that when netting is legally allowed from an accounting measure of exposure perspective then the same should be applied for the denominator of the leverage ratio, (the exposure measure), i.e. if the carrying value on balance sheet is a net value then the net position should be used.
The definition of exposure needs to be explicit to avoid inconsistency.
In addition to this it is proposed that regulatory netting also be applied to the exposure measure.</td></tr>
<tr><td colspan="2">Derivative Exposures - collateral</td></tr>
<tr><td>Collateral received in connection with derivative contracts does not reduce the economic leverage inherent in a bank's derivatives position. In particular, the exposure arising from the contract underlying is not reduced.
As such, collateral received (cash or non-cash) may not be netted against derivatives exposures whether or not netting is permitted under the bank's operative accounting or risk-based framework</td><td>In calculating the exposure measure, derivative exposures should be reduced by the value of high quality collateral. This should broadly align to the capital rules, i.e. link to the CEM approach.
This treatment disincentives banks for using cash collateral in their trade finance operations and has the potential to limit the ability of a bank to undertake certain trade financing transactions.</td></tr>
<tr><td colspan="2">Written credit derivatives</td></tr>
<tr><td>The effective notional amount of a written credit derivative may be reduced by the effective notional amount of a purchased credit derivative on the same reference name and level of seniority if the remaining maturity of the purchased credit derivative is equal to or greater than the remaining maturity of the written credit derivative.</td><td>More flexibility is required in calculating the notional amount for written credit derivatives –a broader range (tenor mismatch) of offsetting purchased credit derivatives required.</td></tr>
<tr><td colspan="2">Securities financing Transactions</td></tr>
<tr><td>General treatment (bank acting as principal): the sum of the amounts in (i) and (ii) below are to be included in Total</td><td>Regarding securities financing transactions (SFTs) a new methodology is being proposed which is different to both the</td></tr>
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Exposures: (i) Gross SFT assets recognised for accounting purposes (ie with no recognition of accounting netting). Remove the value of securities received in an SFT and recognised as an asset by the transferor if the transferor has the right to hypothecate but has not done so (eg under US GAAP). (ii) A measure of counterparty credit risk calculated as current exposure without an add-on for potential future exposure (PFE).	accounting view and the regulatory view. This creates yet another measure and is overly cumbersome. • It must be clearly indicated which SFTs fall in the off balance sheet and which in the on balance sheet bucket.
Other off-balance sheet exposures	
• The Committee recognises that these OBS items are a source of potentially significant leverage. Therefore, banks should include the above OBS items in the Exposure Measure by applying a uniform 100% credit conversion factor (CCF).	• The application of a 100% CCF for trade finance off-balance sheet (OBS) exposures would be inappropriate and detrimental to the provision of international trade. • Recommend use of the Basel Standardized Approach CCFs of 20% for trade related contingencies and 50% for transaction related guarantees rather than a flat 100% CCF. • These values reflect both the low-risk nature of trade finance and the fact that not all OBS trade exposures will necessarily convert to on-balance sheet exposures. • The lower CCF for trade finance should be applied across all jurisdictions to ensure cross border trade flows, particularly in emerging market economies, are not affected.
Other	
Treatment of CCPs	• The appropriate treatment of exposures to CCPs for the leverage ratio must be determined. Moving from an off-balance sheet to an on-balance sheet position could unnecessarily negatively impact the banks from a calculation perspective with regards to the appropriate treatment of collateral and netting. For example the initial margin will carry full leverage exposure by moving on-balance sheet.
Leverage ratio and liquid asset buffer	• It should be evaluated whether the leverage ratio will be negatively affected by the assets held on-balance sheet for

Reference to paper	Comment
	the liquid asset buffer requirements.
Reference to Leverage Ratio in Non-internal model method paper	
• The new proposal on the non-internal model method for capitalising counterparty credit risk exposures proposes that the leverage ratio will be calculated using the non-internal model method (NIMM) for counterparty credit risk going forward.	• This will in effect result in the leverage ratio moving towards a regulatory quasi-risk metric and moves even further away from the accounting measure. This is not aligned with the original intention of the leverage ratio being a simple backstop measure. In addition to this, for an IMM (internal model method) bank, calculating the NIMM for the leverage ratio would result in a potential burden.