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Secretariat of the Basel Committee on Banking Supervision
Bank for International Settlements
CH-4002 Basel
Switzerland

Submitted to baselcommittee@bis.org

Dear Sir/Madam:

Markit¹ is pleased to submit the following comments to the Bank of International Settlements (the "**BIS**") in response to its Discussion Paper on the *Regulatory framework: balancing risk sensitivity, simplicity and comparability* (the "**Discussion Paper**" or the "**DP**").²

Introduction

Markit is a provider of financial information services to the global financial markets, offering risk analytics, independent data, valuations, and related services across regions, asset classes and financial instruments. Our products and services are used by a large number of market participants to reduce risk, increase transparency, and improve the operational efficiency in their financial markets activities.

Markit Analytics delivers a suite of integrated, scalable and efficient solutions for enterprise-wide risk management across a broad range of asset classes. Its fully interactive interface allows for dynamic, ad hoc risk reports as well as for the ability to analyze the results in great detail. The service supports the highly variable computational demands of financial institutions by leveraging its software over a server grid. Markit Analytics services support a number of banks (including those that have received or are expecting to receive IMM approval) with the calculation of their regulatory capital requirements, including measures such as PFE, IMM EAD, IRC, CRM, and the CVA Capital VaR charge.³ Based on our expertise in these areas, we have also been approached by various institutions to help them address upcoming challenges

¹Markit is a financial information services company with over 3,000 employees in Europe, North America and Asia Pacific. The company provides independent data and valuations for financial products across all asset classes in order to reduce risk and improve operational efficiency. Please see www.markit.com for additional information.

² BIS Discussion Paper: The regulatory framework: balancing risk sensitivity, simplicity and comparability. July 2013.

³ CVA = Counterparty Value Adjustment, PFE = Potential Future Exposure, IMM EAD = Internal Model Method Exposure At Default, IRC = Incremental Risk Charge, and CRM = Comprehensive Risk Measure.

related to the calculation of initial margin and variation margin for their portfolios of cleared and uncleared derivatives transactions.

Markit is actively and constructively engaged in the discussion regarding regulatory reform of the financial markets. We regularly provide regulatory authorities with our insights on current market practice, for example in relation to valuation methodologies, the provision of scenario analysis, the use of reliable and secure means to provide daily marks, and the use of pre-trade credit checks to ensure clearing certainty. We have also advised regulatory bodies on potential approaches to enable the timely and cost-effective implementation of newly established requirements, for example through the use of multi-layered phase-in or by providing participants with a choice of means for satisfying regulatory requirements. Over the last several years, we have submitted over 90 comment letters⁴ to regulatory authorities around the world and participated in numerous stakeholder meetings.

We welcome the publication of the Discussion Paper and we appreciate the opportunity to provide the BIS with our comments.

Specific Comments

Q1: Does the current framework, with its reliance on the risk-based capital at its core, appropriately balance the objectives set out in paragraph 29?

Q2: Are there other objectives that should be considered in reviewing the international capital adequacy framework?

Our experience in supporting banks with the calculation of their regulatory capital requirements has shown that many of them have made very significant investments in their risk management capabilities over the course of implementing Basel II. Such investments have yielded substantially improved, firm specific risk measurement and management capabilities.

We understand the BIS's concern that, "in pursuit of greater risk sensitivity, parts of the Basel capital adequacy framework have become very complex."⁵ However, we believe that any initiative that focused solely or predominantly on simplifying the capital requirements regime⁶ might threaten the advances that have been made and could disincentivize banks from further developing their risk management capabilities. We are concerned that the benefits of the idiosyncratic risk measurement frameworks that have

⁴ This number includes responses that have been submitted by MarkitSERV, a now fully-owned subsidiary of Markit Group.

⁵ BIS DP, par. 48.

⁶ BIS DP, par. 48.

been developed in dialogue between regulators and banks could be lost in a broad brush “simplification” initiative.

In contrast, we believe that the preferred approach to addressing this challenge would be to focus on the *efficacy* of the regulatory regime, i.e. weighing the costs and benefits and optimizing around a more effective policy mix, rather than solely aiming for simplicity. In practice, the elements of the Basel II implementations that do not yield adequate returns in relation to the effort/spend required could potentially be reconsidered on that basis. We therefore believe that the BIS should focus on striking the right balance between cost and benefit, not just pursue a “simplification” strategy.

Q3: To what extent does the current capital framework strike the right balance between simplicity, comparability and risk sensitivity, given the costs and benefits that greater risk sensitivity brings?

Q4: Which of the potential ideas outlined in Section 5 offer the greatest potential benefit in terms of improving the balance between the simplicity, comparability and risk sensitivity of the capital adequacy framework?

Q5: Are there other ideas and approaches that the Committee should consider?

We appreciate the BIS’s stated objectives to simplify the capital regime and to increase comparability across regions and firms in order to ensure a reasonable level-playing field across firms.⁷

Based on our experience in supporting major financial firms with the implementation of risk-based capital calculations, we agree that the BIS framework is complex in nature. In addition to the high degree of complexity, the comparability of capital calculations between firms is reduced by the fact that the implementation of such calculations is subject to interpretation, both by national regulatory authorities and by the individual firms. We agree that, while the use of “national discretion” can provide benefits,⁸ it also

⁷ “Thus, the remainder of this paper discusses ideas that could be pursued to simplify and improve the comparability of bank capital requirements in the light of concerns that, in its current form, the capital adequacy framework may be too complex and that, as a result, comparability is being hindered.” BIS DP par. 29.

⁸ “The use of national discretion allows international standards to be better tailored to reflect local conditions. In theory, this should improve comparability and the evenness of the playing field, as the treatment of dissimilar risks is not forced into a “one size fits all” template. National discretions can, for example, smooth the way for global standards to be suitably applied to advanced and emerging economies, taking into account differences in the structure and development of financial systems. In practice, however, the use of national discretions can also impair the comparability of risk-weighted assets across jurisdictions, if supervisors fail to determine the use of national conditions with the same degree of conservatism in mind.” BIS DP par. 67.

tends to result in risk-weighted capital calculations that are inconsistent between jurisdictions and firms, sometimes to a significant extent.

The BIS proposed several potential approaches to improving both the simplicity and the comparability of risk-weighted capital calculations.⁹ These ideas included explicitly recognizing simplicity as an additional objective,¹⁰ enhancing disclosure for investors about changes in risk-weighted assets, especially those affecting risk-weighted assets derived from internal models,¹¹ using additional metrics,¹² ensuring the effectiveness of the leverage ratio,¹³ utilizing added floors and benchmarks to mitigate the consequences of complexity,¹⁴ reconsidering the linkage between internal and regulatory models,¹⁵ reviewing, making transparent, and potentially limiting, the use of national discretion,¹⁶ improving the accessibility of the Basel Committee documents,¹⁷ and addressing factors that are driving complexity in a more fundamental manner.¹⁸

We believe that many of these proposals have merit and could be useful if they were implemented in a sensible manner. That said, we believe that the BIS should also actively consider specific measures that could help to directly quantify and visualize the actual differences in risk-based capital calculations between jurisdictions and firms. This information could then be used to reduce national and the firms' discretion where such differences are most pronounced, herewith directly targeting an increase in the comparability of risk-based capital calculations.¹⁹

We believe that such approach could be implemented via the launch of a global risk-based capital benchmarking exercise. Such initiative could be operated similar to a consensus pricing exercise²⁰ and would consist of the following steps:

- The relevant firms (be it the firms in a specific jurisdiction or, ideally, across several jurisdictions) would be provided with a number of sample portfolios of

⁹ BIS DP, Section 5.

¹⁰ BIS DP, par. 48.

¹¹ BIS DP, par. 50.

¹² BIS DP, par. 55.

¹³ BIS DP, par. 59.

¹⁴ BIS DP, par. 61.

¹⁵ BIS DP, par. 66.

¹⁶ BIS DP, par. 68.

¹⁷ BIS DP, par. 70.

¹⁸ "The Committee is currently reviewing the framework to assess whether the balance between simplicity, comparability and risk sensitivity can be improved. The complete framework is always likely to be – at least in parts – complex, and comparability will always be subject to certain limits." BIS DP, par. 71.

¹⁹ BIS DP, Annex 1.

²⁰ For example, the Markit Totem service collects prices for a range of standardized products from market makers that form the basis for providing consensus market prices back to them that they will use for the purpose of Independent Price Verification. The service covers a broad range of asset classes and enables market-makers to independently check their book valuations.

- financial instruments, as defined by the BIS, that broadly represent different categories of existing risk exposures.
- The firms would then be tasked to individually compute their risk-based capital for the given portfolios.
 - The BIS would collect the results of these calculations across jurisdictions and compare them.

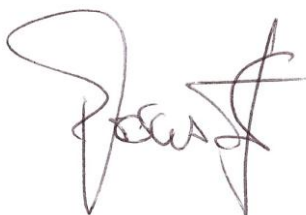
On that basis, the BIS would be in a strong position to identify, either in a specific jurisdiction or for individual firms, those calibrations that result in unusually high or low capital requirements and it could provide appropriate feedback to the relevant national banking supervisors.

As an alternative approach, firms could be provided with several sample portfolios and a given result (in form of a capital requirement) which they would then use to calibrate their models. We believe that either of these approaches could be helpful in creating transparency around divergences in the calibration of models and actively guiding regulators and firms towards an increased harmonization and comparability of capital calculations across jurisdictions and firms.

* * * * *

Markit appreciates the opportunity to comment on BIS's Discussion Paper on the *Regulatory Framework: balancing risk sensitivity, simplicity and comparability*. We would be happy to elaborate or further discuss any of the points addressed above. In the event you may have any questions, please do not hesitate to contact the undersigned or Justin Forrest at justin.forrest@markit.com.

Yours sincerely,

A handwritten signature in dark ink, appearing to read 'Schuler', with a stylized flourish extending from the end.

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