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Dear Sir

Re: Comments on consultative document: Basel III - The Net Stable Funding Ratio

The Banking Association of South Africa ("BASA") and its members appreciate this opportunity to comment on the Basel Committee on Banking Supervision (The Committee) January 2014 consultative document, the Net Stable Funding Ratio ("NSFR").

We welcome the changes incorporated in the 2014 consultative document and are supportive of the principle changes proposed by The Committee to adjust the NSFR to a structural funding measurement from a stress risk measurement.

We are particularly pleased with the changes made with respect to:

- The increase in the ASF factor for demand and term deposits provided by retail and SME customers from an 80% ASF factor to a 90% ASF factor;
- Recognition and alignment to the liquidity coverage ratio for operational deposits;
- Unencumbered loans with a residual maturity of less than 1 year to retail and small business customers lowered from an 85% RSF factor to a 50% RSF factor;
- RSF factor for performing loans and non-high quality liquid assets encumbered for a period of 1 year or more reduced from a 100% RSF factor to an 85% RSF factor;
- The recognition of the 6 month to 1 year time bucket;
- Greater consistency with the Liquidity Coverage Ratio ("LCR"); and
- The adjustments to the RSF factors for level 2 A and B high quality liquid assets have reduced the NSFR shortfall for our bank significantly.

Whilst we welcome these modifications, the reality is that South African banks will still find it difficult to raise the required funding to meet the objective of the NSFR ratio.

Preliminarily calculations indicate a South African industry shortfall of R280bn[1] as at December 2013. This does not take any cyclical buffers into consideration.

[1] Aggregation of individual bank feedback

Our response paper is broken down into 5 sections covering:

1. Background structure of the South African financial markets.
2. Critical recommendations for consideration by The Committee that will assist South African banks' ability to comply with the NSFR;
3. Other recommendations for consideration;
4. Comments related to the 2014 NSFR consultative document; and
5. Request for clarification on specific items in the consultative document and in the QIS.

1. Background structure of the South African markets

1.1 A contained Rand system

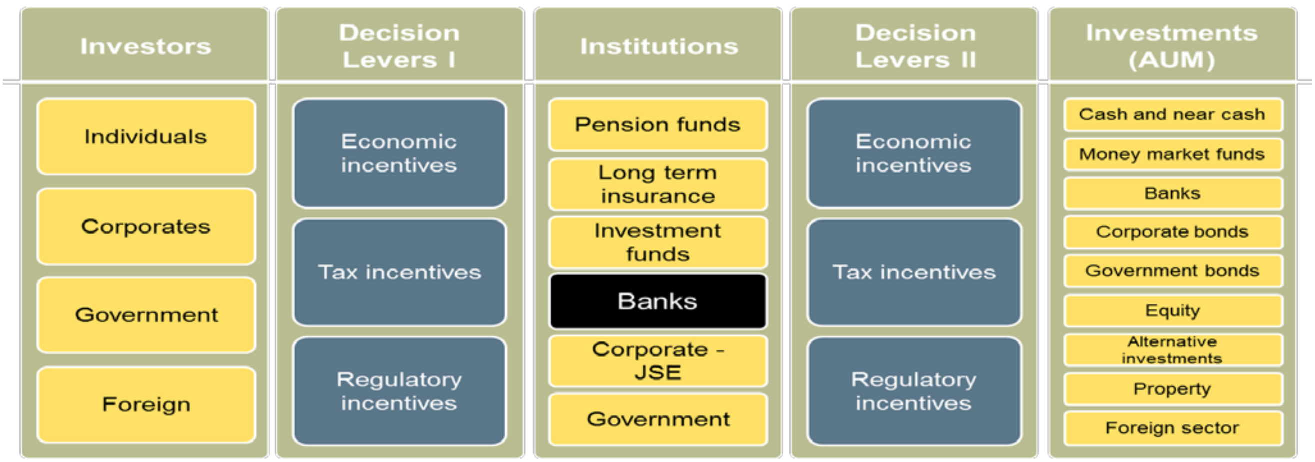
The systemic protection afforded by a contained currency system is not considered in the proposed Basel III liquidity ratios. The contained currency system ensures that all liquidity remains on shore and thus is either placed in the banking system or held at the Central Bank. Exchange Control[2] and Prudential Regulations in South Africa limit the outflow of funds. The liquidity stability afforded by a contained Rand system was evident during the 2008/2009 financial crisis, where the South African banks were relatively unscathed.

The contained Rand system mitigates Rand liquidity risk as funds cannot leave the jurisdiction in a flight to quality.

1.2 Composition of the South African funding base and treatment of wholesale funding by Basel III

In its current economic development stage, South Africa has a low discretionary savings rate and a higher degree of contractual savings that are captured by institutions such as pension funds, provident funds and asset management services.

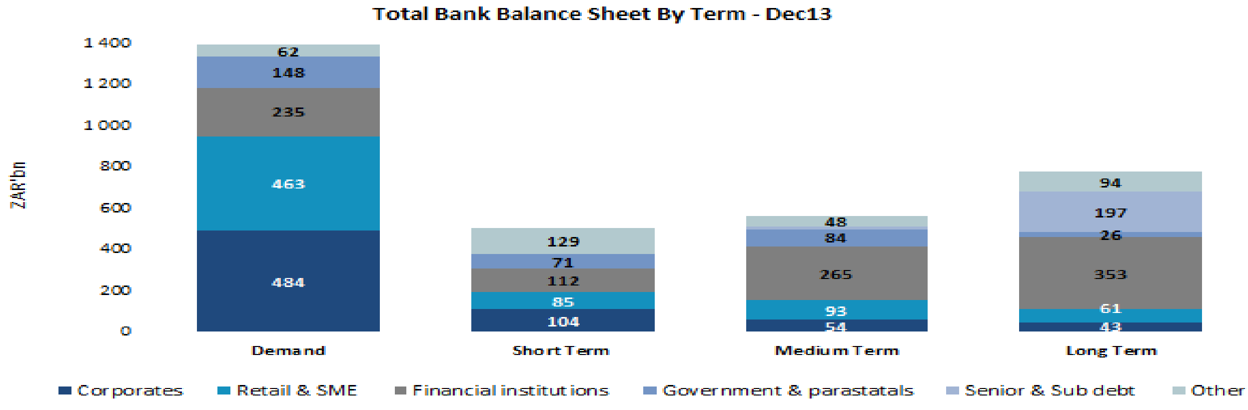
The table[3] below is an illustrative overview of the drivers for savings flows to various platforms within the South African context.



Banks are one of many platforms that attract savings flows in South Africa.

[2] One settlement account, one clearing account and one Sovereign account
[3] National Treasury Structural Liquidity & Funding Task Group

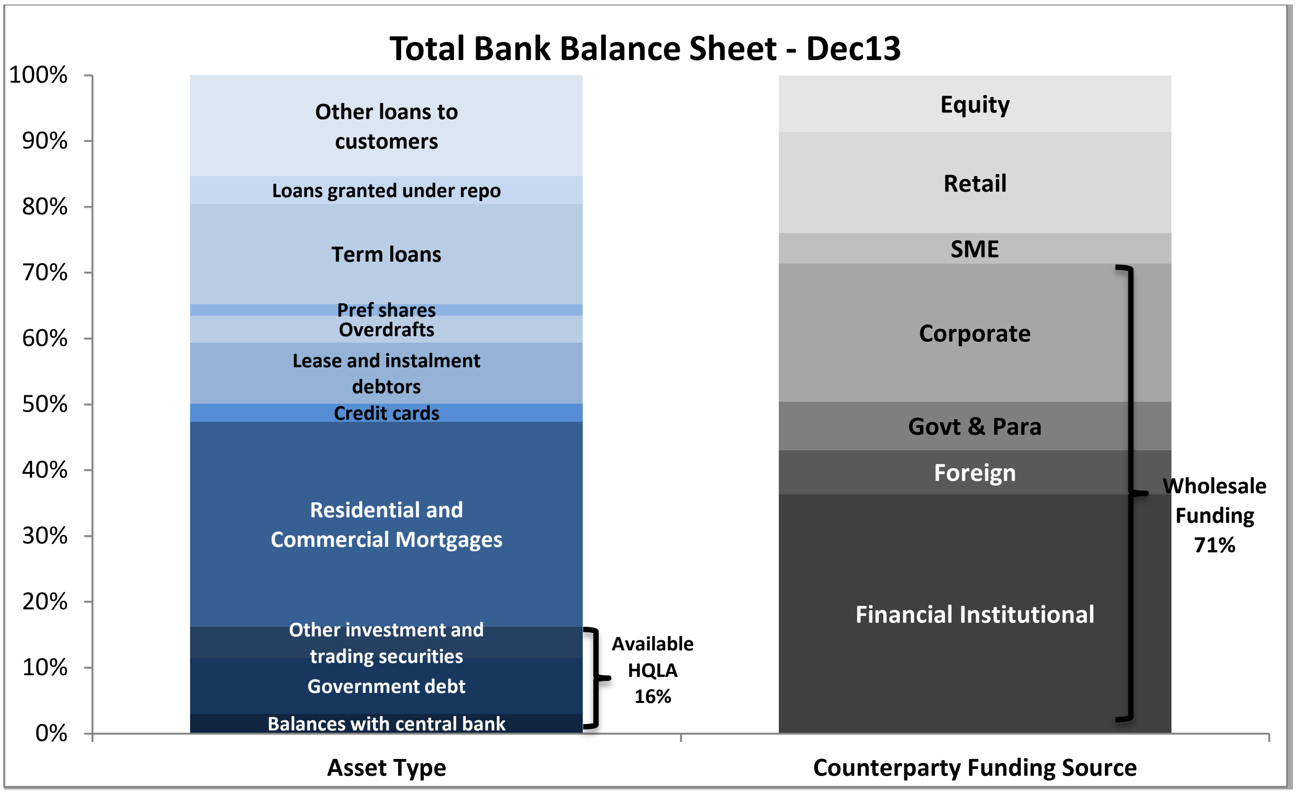
The graph below illustrates the total equity and liabilities of the South African banking industry as at 31 December 2013, broken up by counterparty and remaining contractual maturity date.



Source: SARB BA 900

Long term in this illustration can be defined as liabilities and equity (hereafter referred to as funding) with a remaining maturity of 6 months and greater. Based on January 2014 industry data, only ***24% of South Africa's funding had a maturity date of greater than 6 months***, with the majority of total funding provided by financial institutions (39%). Funding from individuals and SME's contribute to approximately 25% of total funding, however 78% of these funds are either placed with banks on demand or mature within one month. When considering the composition of the South African deposit base, there is a predominant reliance on *wholesale* sources of funding rather than retail deposits. South African consumers tend to invest more wealth in asset managers and insurers compared to other G20 countries thereby causing disintermediation of banks due to high penetration of institutional savings.

The graph below indicates that wholesale funding makes up over **70%** of local bank funding with 25% being contributed by retail & SME funding.



The local banking industry remains reliant on a concentrated funding pool whose investment decisions can change day to day and although we do acknowledge that this is a liquidity risk, the idiosyncrasies of the South African market will need to change before we are able to develop a diversified funding base to mitigate this risk.

Basel III has been drafted based on the lessons learned from the behaviour of the wholesale depositor in the more sophisticated economies during the international economic crisis and although the South African economy and banking system has its own structural peculiarities, proposals arising from the aftermath of the crisis cannot simply be replicated without careful consideration of the implications.

The framework does not appropriately consider local circumstances where the domestic currency is *not freely transferable* across national boundaries (i.e. taking account of the contained Rand system) or the fact that the South African financial system has a high reliance on *wholesale* funding which, in the South African context, is essentially recycled contractual savings and money market funds, as there is not many places the cash can go and it almost always ends up back at the local banks.

Our banks support the objectives and principals which initiated these reforms and it is these objectives that should remain the focus. We believe that should regional circumstances be left unaddressed, they will cause unintended consequences for the provision of finance supporting the import and export of goods and services. This could ultimately lead to damaging development effects in emerging market economies and these outcomes are fundamentally at odds with the sensible risk management and pro-growth economic policies espoused by the Basel Committee and the G-20 and therefore our recommendations below are aligned and contained at enhancing the South African liquidly risk market structure, in addition to improving the appropriate risk measurements.

2. Critical recommendations for consideration by The Committee that will assist South African banks' ability to comply with the NSFR

2.1 Committed Liquidity Facility ("CLF")

As noted in section 1.2, the South African financial market is characterised by high contractual savings, disintermediating savers from banks via professional money managers and has limited availability of high quality liquid assets (HQLA) in particular level 2 assets to mitigate the liquidity risk posed by concentrated financial institutional funding.

During 2012, the South African Reserve Bank ("SARB") approved the provision of the CLF in order to assist local banks in meeting the requirement of the LCR, given the structural aspects of the South African market. The facility will be granted on an annual basis, with eligible collateral defined and ring-fenced under the following characteristics:

(i) It has to be unencumbered;
(ii) Securitised asset pools have to be audited on an annual basis; and
(iii) Collateral shall have an outstanding maturity of more than one year

The facility is legally binding and attracts a commitment fee, payable to SARB on an annual basis to ensure this facility is available to draw on, and hence, we believe this source of funding can be deemed as a stable form of funding.

By reclassifying this asset (we would now hold a marketable security albeit a self-securitised note for which there is liquidity), the asset would move from a 65% RSF

factor or greater, to a 5% RSF factor analogous to a Level 1, or at the very worst, a 15% RSF factor analogous to a Level 2A.

As South Africa operates in a closed Rand system (which traps Rand within the jurisdiction and financial market), the provision of an item of national discretion would facilitate individual bank funding risk mitigation, via the development of market liquidity attributes in assets and being able to access cash trapped either at SARB or held by other banks.

Recommendation

We propose that either the CLF eligible collateral be included with a RSF factor similar to level 2A, or the CLF be included as an available stable source of funding in the NSFR under an item of national discretion.

Inclusion of the CLF asset also aligns to the recovery and resolution regime and improving the stability of the South African financial system.

2.2 Unencumbered holdings of self-securitised RMBS

Under the 2014 proposal, unencumbered holdings of self-securitised RMBS with a rating of least AA don't qualify for a 50% RSF factor that applies to other RMBS with a rating of least AA, as per paragraph 32(a), for the sole reason that, being self-securitised, they don't qualify as Level 2B HQLA. They are therefore assigned an 85% RSF factor.

We understand the reason for this; as applied to the LCR because under a severe crisis the bank may not be able get its own paper to market within 30 days. However applying the same principle to the NSFR is contradictory to the stated intent of the RSF factor in paragraph 25 of the proposal: "The RSF factors assigned to various types of assets are parameters intended to approximate the amount of a particular asset that would have to be funded, either because it will be rolled over, or because it could not be monetised through sale or used as collateral in a secured borrowing transaction over the course of one year without significant expense. Under the standard, such amounts are expected to be supported by stable funding."

In doing the self-securisation, the bank has already done the work and incurred the expense of identifying suitable assets, packaging them in an insolvency-remote SPV, and obtaining external ratings for tranches of debt collaterised by those assets, resulting in a balance sheet that is sturdier for both recovery and resolution.

For such tranches of paper with a rating of at least AA, all that remains is to take them to market, which can surely be done "over the course of one year without significant expense". To count only 15% of this towards stable funding seems overly conservative and provides no reward to the bank for improving its stable funding by converting illiquid assets into marketable securities.

Recommendation

We recommend that unencumbered holdings of self-securitised RMBS with an external rating of at least AA should qualify for an RSF factor that reflects an improved liquidity compared to its underlying mortgages.

2.3 Factors applicable to Residential Mortgages

Under the new rule set, a 50% RSF factor is now applicable to Residential Mortgages up to 1 year, regardless of the risk weight under the Basel II standardised approach for credit risk. Residential Mortgages with a risk weight of less than 35% with a remaining maturity of greater than 1 year still attracts a beneficial RSF factor of 65% compared to the other asset classes.

This differential treatment of the asset class is justified when considering the role Residential Mortgage Backed Securities plays in the South African debt capital markets. As illustrated in the table below[4], total outstanding listed debt (including securitisation) as at 31 December 2013 was ZAR 1.8 trillion, of which South African Government debt accounted for ZAR 1.1 trillion. The remaining outstanding corporate and securitisation debt amounts to ZAR 692 billion.

Issuer Type	1Q13	2Q13	3Q13	4Q13
ABCP	29.04	30.72	30.06	27.79
Banks / Financials	207.10	206.22	212.99	217.92
CLN	40.57	38.13	39.11	38.70
Corporates	95.16	99.82	97.69	103.14
Municipal	14.07	16.31	16.31	16.28
Other / Structured	15.13	14.61	15.64	15.27
Securitisations	50.62	51.34	48.01	47.94
SOEs	205.91	213.69	217.63	225.66
Sovereign	979.04	1,010.34	1,057.72	1,105.54
Grand Total	***1,636.63***	***1,681.18***	***1,735.16***	***1,798.23***

Residential Mortgage Backed Securities make up the overall majority of issuance. These securitised transactions do provide originators with an alternative means of financing that contributes to the diversification of their funding sources, which is becoming increasingly important given the challenges with the implementation of the NSFR in South Africa. RMBS, in particular, is one of the few possible sources of liquid assets in South Africa that can be included in the assessment of the LCR.

In addition to the above, residential mortgage portfolios as highlighted in the table below[5] also has a lower credit loss experience in comparison to unsecured lending types thereby justifying a lower RSF factor.

South African Industry				
Credit Loss Ratio	**2013**	**2012**	**2011**	**2010**
Home Loans	0.52%	0.66%	0.90%	1.24%
Card	3.48%	1.92%	1.63%	3.54%
VAF	1.06%	0.95%	1.27%	2.06%
Personal unsecured lending	7.23%	8.17%	4.36%	5.81%

Recommendation

Based on the above, we acknowledge the need for differential treatment of this asset type and welcome the reduction to 50% applicable to residential mortgages with maturities up to 1 year. Given the high demand in emerging markets for housing and the socio economic demands to house the nation relative to other developed economies, we concur with the beneficial treatment of residential mortgages with a risk weighting of less than 35%. We therefore recommend that the RSF factor for residential mortgages with a risk weighting of less than 35% and a remaining maturity of greater than 1 year be placed as an item of national discretion in order to prevent significant pull back on residential lending in emerging markets.

[4] Johannesburg Stock Exchange & Rand Merchant Bank Global Markets
[5] Aggregated and sourced from annual financial statements

3. Other recommendations for consideration

3.1 Operational Deposits

The recognition of Operational Deposits for NSFR purposes is a positive development, and is consistent with the purposes and rationale of the revised NSFR. The ASF factor amount under the NSFR is measured based on the broad characteristics of the relative stability of an institution's funding sources, including the contractual maturity of its liabilities and the differences in the propensity of different types of funding providers to withdraw their funding. We are concerned that experience, even in the most difficult periods of 2008-2012, does not bear out the conservative 50% ASF factor run-off assumption or take into consideration the high stability of these deposits and hence is not consistent with the stability principles of Paragraph 12 of the BIS document.

The LCR assigns a 25% run-off rate to deposits arising from operational accounts. This lower LCR outflow factor recognises the highly stable nature of cash balances linked to operational accounts. The LCR recognizes the stickiness of these deposits and the substantive dependency on the incumbent provider during a 30 day stress scenario. We do feel that greater stability in funding is derived from the operational account deposits that are anchored by clearing, custody and cash management activities. The qualification criteria for Operational Deposits presumably would apply the same as under the LCR. Analysis conducted by individual banks has shown greater stability with the corporate and commercial transactional accounts than the financial and public sector operational accounts.

Under the NSFR "business as usual" approach, the same characteristics which bind these account deposits should apply. While we understand the motivation of the Basel Committee to ensure a conservative approach to liquidity risk management, the current proposed ASF factor may discourage a bank from attracting the kind of client bank deposits that are reliable even in times of stress. A highly operational banking relationship leads to reliable core deposits even when stress situations occur.

Any remaining concerns about Operational Deposits are likely to be supervisory issues arising from the need to be sure that the qualification criteria are applied appropriately and consistently; however, the need for assurance of compliance should not influence the calibration of NSFR calculations. Supervisors in any case will be examining Operational Deposit determinations for LCR purposes, from January 2015.

Recommendation

An ASF factor set at 65%-75% level, regardless of counterparty, would be consistent with the application of the LCR criteria to define stable Operational Deposits under business-as-usual conditions. This proposal would be consistent with the approach adopted for retail deposits, where the ASF factors are congruent with those specified for the LCR.

3.2 Treatment of Repos & Reverse Repos.

3.2.1. The SARB creates a money market shortage (through cash reserves and liquidity draining open-market operations) in order to force banks to borrow funds from the SARB (through a refinancing mechanism) at the official repo rate. A change in the official rate is immediately transmitted to other short-term wholesale money market instruments which then steers the economy towards achieving monetary policy objectives. In order to drain liquidity (so as to create a shortage), the SARB (as part of their open market operations) requires banks to bid in their debenture auctions. Banks then need to repo these or other qualifying assets (typically Level 1 assets) with the SARB in order to achieve a fully funded position.

Given that these secured borrowing activities (in the form of repo transactions) with the SARB forms an integral part of the monetary policy transmission system it is anticipated that there is an extremely high probability of these repos being rolled and hence having an ASF factor closer to 100%.

Assigning a 0% ASF factor to repos with the SARB, backed by level 1 Sovereign or SARB assets is problematic for the following reasons:

(i) In terms of the LCR, Level 1 assets are deemed to be easily convertible into cash liquidity and therefore assigned a 100% weighting. A 100% LCR HQLA weighting should be equivalent to a 100% ASF factor i.e. Repos with the SARB backed by Level 1 assets should be assigned an ASF factor of 100%

(ii) The SARB structurally engineers the money-market shortage in order to effect monetary policy by forcing banks to enter into repo transactions with them at the official Repo rate. This being the case it does not follow that the SARB would not continue to provide funding through the refinancing mechanism and therefore a 100% ASF should apply to Repos with Central Banks

It is evident from the table below that asymmetry exists between repo and reverse repo transactions associated with non-bank FI's and central banks (maturity less than 6 months). A repo with these counterparties results in an ASF factor of 0% whereas a reverse repo requires stable funding of 50%. It should be noted that these asymmetries could culminate in market making banks having less appetite to perform market making functions in sovereign debt.

Maturity less than 6 months					
	Repo: Banks (47) **Reverse Repo:** Bank (88)	**Repo**: Non-Bank FI (47) **Reverse Repo**: Non-Bank F1 (98)	**Repo**: Central Bank (45) **Reverse Repo**: Central Bank (158)	**Repo**: Non-financial Corporates (44) **Reverse Repo**: Non-financial Corporates (148)	**Repo**: Sovereigns / PSEs / MDBs / NDBs (46) **Reverse Repo**: PSE/Sovereign (168)
Repo **ASF** Factor	0%	0%	0%	50%	50%
Reverse Repo **RSF** Factor	0%	50%	50%	50%	50%

Previously both repos and reverse repos in the less than 6 month space did not require stable funding as per our comment above. Under the revised rule set, short term reverse repos require 50% stable funding. This implies that short term reverse repos from central clearing counterparties, broker-dealers and secured lenders for the matched trading book and cash trading businesses which require reverse repos to cover shorts now require 50% stable funding regardless of the underlying collateral type.

3.2.2. The revised document assumes that the probability of secured borrowing activities (such as repo transactions) being rolled are directly linked to the counterparty client type i.e. it is assumed that non-financial corporates, sovereigns and PSE's will roll repo transactions 50% of the time while financial corporates and financial institutions will roll repo transactions 0% of the time during the course of one whole year. Empirical market data would suggest that while the specific counterparty may differ from transaction to transaction, the probability of funding being received is more closely aligned with the quality of the underlying asset as opposed to the counterparty client type i.e. there is a high probability of a bank receiving full funding via a repo of a government backed instrument than the bank receiving full funding from a credit based asset, which is dependent on a counterparty's risk exposure appetite. To assume that specific counterparties such as financial corporates and

financial institutions will roll repo transactions 0% of the time during the course of one whole year within the NSFR scenario is to assume a very severe systemic event. It is our understanding that the primary objective of the NSFR is to measure the structural stability of funding in relation to the bank's assets as opposed to performing acute stress testing which is the objective of the LCR. Furthermore the LCR / NSFR standards indicate that the intention is to prepare banks for idiosyncratic stress scenarios.

Assuming a 0% ASF factor for repos with financial corporates and financial institutions is to exceed the idiosyncratic stress testing objective by introducing severe systemic scenarios.

3.2.3. Secured funding transactions have 2 sources of liquidity related to them;

(i) there is the final transfer of cash for security;
(ii) in the interim the asset can also be used for other transactions or sold.

Taking into consideration the quality of the collateral used in these transactions takes into consideration the liquidity characteristics of the collateral and aligned to this the likely ease of using this collateral to raise additional funding.

3.2.4. As stated earlier South Africa has a shortage of high quality liquidity assets, in addition the South African interbank market operates on a bilateral unsecured basis. To develop a more robust financial market aligned with the objectives of the recovery and resolution regime and to increase the availability of level 2 assets, an active repo market is required to be available to all market participants. The asymmetrical treatment of secured financing in the current text prohibits the development of a high quality liquid asset market.

Recommendations

In the context of the South African Banking system, we propose the available funding factors for secured borrowings be amended to capture the underlying collateral and not to solely rely on the counterparty classification. The counterparty classification in its current state affects monetary policy market execution in South Africa by penalising secured funding interaction with the Central Bank. Additionally it impedes market development of high quality liquids asset by creating an unequal playing field for accessibility to assets for specific market participants such as financial institutions versus non-financial corporates.

We accept that funding lower credit quality assets on a short term secured basis is not appropriate within the context of a resilient structural funding plan and recommend that secured funding factors be assigned against the instrument's credit quality and market liquidity attributes to the Basel high quality liquid asset text.

As such; we propose secured transactions backed by Level 1 assets should carry 100% ASF factor irrespective of counterparty and the RSF factor should be zero. This reflects the liquidity of these assets and the importance of protecting a liquid market in high quality sovereign debt.

For secured transactions backed by non-level 1 assets, we believe that the RSF factor should be lower than if these assets were held outright reflecting the ability for the assets to be funded on a secured vs an unsecured basis. We propose that the ASF factor and RSF factors for secured funding should be aligned in treatment to ensure no asymmetries continue to exist. Our proposal is for a 50% factor to be applied to the RSF unencumbered asset factor to reflect the funding of the asset.

This would align the NSFR secured financing treatment with the liquidity coverage ratio treatment of secured funding, giving cognisance to the difference between stress under the LCR and structural funding under the NSFR.

3.3 Required Stable Funding Factors

"Item 34 *of the consultative document: Assets assigned an 85% RSF factor*"

We are uncertain as to the reason for a higher RSF for "physical traded commodities, including gold." It seems anomalous that these assets , particularly gold, now receives an 85% RSF factor vs. 50% in the 2010 draft and believe that the treatment in NSFR 2014 should not lead to a worsening of treatment compared to the NSFR 2010 proposals unless there is a valid reason?

Appendix 1 of the NSFR proposal indicates that among the "key changes" to the NSFR 2014 are "additional granularity and lower RSF factors for certain other non-HQLA", including "physical traded commodities". Although gold is not specifically mentioned, it is hard to see why the RSF treatment of these assets should have been made more stringent, whereas various other comparable RSF factors have been reduced.

While physical traded commodities, including gold is a more important issue for some banks, as a matter of principle it seems wrong not only to penalize, but to increase the penalty given its generally recognised liquidity characteristics. Commodity prices can be volatile but remains highly liquid (in various forms) and its volatility is believed generally to be countercyclical. Banks in South Africa facilitate both soft and hard commodity flows out of Africa. These transactions are typically short dated in nature (with the longest period being for example, harvesting seasons).

Recommendation

Given the short term nature of these assets, we would recommend The Committee align factoring to the loans under paragraph 32(e) of the NSFR consultative document and re-apply the 50% RSF as this would be more realistic.

3.4 Factors applicable to Financial Entities and Institutions:

Under the new rule set, a 50% RSF factor applies from overnight to 1 year loans to financial entities. Under QIS Line 97 - Loans to financial entities (other than loans to banks subject to prudential supervision) that are not renewable.

Previously this line was consolidated together with banks and did not require stable funding. Under the new rule set, short term loans to financial entities require 50% stable funding. Given the short term nature of these loans (specifically Trade Financing and Factoring) and the franchise requirements for banks to provide these facilities, we feel that the 50% RSF requirement in the less than 6 month space is excessive. The requirement to hold 50% stable funding against short term loans may have a detrimental impact on certain business lines.

In considering an appropriate RSF factor for trade finance lending, the potential impact on credit supply brought on by adding an additional regulatory cost should be taken into account. We believe that it would be appropriate to consider a 0% RSF factor for any trade finance lending with residual maturity below 6 months. Using this as a base, 2 full cycles of turnover within 6 months are covered, thereby removing the need to apply maturity miss-transformation to trade finance. This will ensure that more of a bank's stable finance is applied to transactions above 12 months. A 0% RSF for trade finance under 6 months confirms that 100% of transactions less than 6 months can be funded without requiring long term stable funding.

Recommendation

As the NSFR is intended to be a "business as usual" metric for banking organizations over the course of 12 months, a 0% RSF factor for short term trade loans would not harm the overall purpose of the ratio or diminish protection of the franchise in times of stress."

4. Other comments related to the 2014 NSFR consultative document

4.1 Treatment of Derivatives

There is different accounting treatment for netting derivatives between IFRS and GARP and while LCR is clear, no clarity has been forthcoming on this issue. We feel that the finalisation of this treatment should however not hold back any implementation of NSFR and would welcome clarity on this issue.

The net derivative asset is assigned a RSF factor of 100% which appears high based on the following logic:

- Defaulted loans are unlikely to be repaid and hence should be assigned a RSF factor of 100%,
- As loans are repaid it is fair to assume that the proceeds of repayment are likely to be re-advanced, even in stress scenarios, as a bank must protect its franchise. Hence assigning a 50% to 100% RSF factor depending on the loan type seems to be correct.
- However a derivative asset is a self-liquidating instrument which creates cash as opposed to requiring stable funding. It therefore does not follow that a 100% RSF factor should be assigned**.**

We would welcome clarity on the prescribed *Derivative Netting Methodology* to be applied, especially with regards to maturity distinction and the treatment of margins.

4.2 The wording of SME

We applaud the Committee for their careful review of the original 2010 NSFR proposal and for the revisions which take into account, *inter alia*, the importance of Small and Medium Sized Enterprise (SME) finance and the much needed shift toward a structural approach in the overall definition of the ratio.

The use of "SME" as opposed to "small business" customers is confusing and inconsistent with previous Basel III (and II) liquidity standards. The Basel II "SME" term has a different definition. See ***Annexure A*** for details.

The latest Basel III QIS consistently uses the term "small business". We need a consistent definition for whichever term is used, unless they are to be considered interchangeable.

5. Request for clarification on specific items in the 2014 consultative document and in the QIS.

5.1 Section 18 (b)[6]: Liabilities and capital receiving a100% ASF factor.

Our interpretation of the contents of item 18 (b), is to include non-B3 compliant capital instruments greater than 1 year i.e. preference shares, hybrid debt and Tier 2 debt instruments, which are not included in item 18 (a).

Clarity is required with regards to the disclosure of Non-B3 compliant capital instruments with a maturity less than a year. Would the amounts be assigned to the respective counterparty under the "non-deposit unsecured funding" lines or would these amounts be reflected as "all other liabilities and equity categories not included above"

[6] 2014 NSFR Document

5.2 Line 87 and 97[7]

Loans to banks subject to prudential supervision that are *not renewable*/loans to financial entities (other than banks subject to prudential supervision) that is not renewable. Our understanding is that it is non-renewable in terms of protecting the banks' lending franchise.

Please confirm what is the definition of ***non-renewable***?

5.3 Section 29 (b): Assets assigned a 0% RSF factor

Total amount held in central bank reserves (including required and excess reserves) including banks' overnight deposits with the central bank, and term deposits with the Central bank that:

(i) are explicitly and contractually repayable on notice from the depositing bank; or
(ii) that constitutes a loan against which the bank can borrow on a term basis or on an overnight but automatically renewable basis (only where the bank has an existing deposit with the relevant central bank)."

Clarity is required on the wording "term deposits with the central bank that constitute a loan against which the bank can borrow on a term basis"?

5.4 Line 153, 183, 203 and 213

These line items refer to loans extended by counterparty types e.g. loans to financial entities, corporates etc. Clarity is required on whether these lines include securitised assets which are included as group consolidated assets but are regarded as encumbered as a result of the securitisation?

5.5 The Basel III LCR text explicitly states that the LCR ratio must be applied and met at an entity level. This issue is not explicitly addressed in the NSFR consultative document, however, our understanding is that the NSFR should apply at a consolidated level, thereby implying the fungibility of entity level assets and funding to a consolidated level.

Please confirm that the calculation of the NSFR should be at a consolidated level.

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[7] QIS Document

Annexure A

BCBS238: Basel III:
The Liquidity Coverage Ratio and liquidity risk monitoring tools

Small business definition

90. This category consists of deposits and other extensions of funds made by nonfinancial small business customers. "**Small business customers**" are defined in line with the definition of loans extended to small businesses in paragraph 231 of the Basel II framework that are managed as retail exposures and are generally considered as having similar liquidity risk characteristics to retail accounts provided the total aggregated funding41 raised from one small business customer is less than €1 million (on a consolidated basis where applicable).

91. Where a bank does not have any exposure to a small business customer that would enable it to use the definition under paragraph 231 of the Basel II Framework, the bank may include such a deposit in this category provided that the total aggregate funding raised from the customer is less than €1 million (on a consolidated basis where applicable) and the deposit is managed as a retail deposit. This means that the bank treats such deposits in its internal risk management systems consistently over time and in the same manner as other retail deposits, and that the deposits are not individually managed in a way comparable to
larger corporate deposits.

BCBS128b: BASEL II:
Framework Part 2: The First Pillar – Minimum Capital Requirements.

Definition of retail exposures

231. An exposure is categorised as a retail exposure if it meets all of the following criteria:

Nature of borrower or low value of individual exposures

- Exposures to individuals — such as revolving credits and lines of credit (e.g. credit cards, overdrafts, and retail facilities secured by financial instruments) as well as personal term loans and leases (e.g. instalment loans, auto loans and leases, student and educational loans, personal finance, and other exposures with similar characteristics) — are generally eligible for retail treatment regardless of exposure size, although supervisors may wish to establish exposure thresholds to distinguish between retail and corporate exposures.

- Residential mortgage loans (including first and subsequent liens, term loans and revolving home equity lines of credit) are eligible for retail treatment regardless of exposure size so long as the credit is extended to an individual that is an owner/occupier of the property (with the understanding that supervisors exercise reasonable flexibility regarding buildings containing only a few rental units — otherwise they are treated as corporate). Loans secured by a single or small number of condominium or co-operative residential housing units in a single building or complex also fall within the scope of the residential mortgage category. National supervisors may set limits on the maximum number of housing units per exposure.

- Loans extended to **small businesses** and managed as retail exposures are eligible for retail treatment provided the total exposure of the banking group to a small business borrower (on a consolidated basis where applicable) is less than €1

million. Small business loans extended through or guaranteed by an individual are subject to the same exposure threshold.

- It is expected that supervisors provide flexibility in the practical application of such thresholds such that banks are not forced to develop extensive new information systems simply for the purpose of ensuring perfect compliance. It is, however, important for supervisors to ensure that such flexibility (and the implied acceptance of exposure amounts in excess of the thresholds that are not treated as violations) is not being abused.

Definition of a SME
Firm-size adjustment for small- and medium-sized entities (SME)

273. Under the IRB approach for corporate credits, banks will be permitted to separately distinguish exposures to **SME** borrowers (defined as corporate exposures where the reported sales for the consolidated group of which the firm is a part is less than €50 million) from those to large firms. A firm-size adjustment (i.e. 0.04 x (1 – (S – 5) / 45)) is made to the corporate risk weight formula for exposures to SME borrowers. S is expressed as total annual sales in millions of euros with values of S falling in the range of equal to or less than €50 million or greater than or equal to €5 million. Reported sales of less than €5 million will be treated as if they were equivalent to €5 million for the purposes of the firm-size adjustment for SME borrowers.