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Secretariat
Basel Committee on Banking Supervision
Bank for International Settlements
CH-4002 Basel, Switzerland
baselcommittee@bis.org

Dear Sir/Madam

Basel Committee on Banking Supervision - Consultative Document: Review of the Pillar 3 disclosure requirements

The Australian Bankers' Association (**ABA**), on behalf of its members, appreciates the opportunity to comment on the Basel Committee on Banking Supervision's (**BCBS**) Consultative Document: *Review of the Pillar 3 disclosure requirements* (**consultative document**). The ABA welcomes this effort to modify Pillar 3 to make it more useful to users and to better meet its objectives.

The ABA takes this opportunity to comment on some aspects of the Pillar 3 proposals. These comments come under the broad headings of:

- Improving comparability and relevance
- Flexibility/Granularity
- Timing
- Enhancing credit RWA comparability and transparency

In considering these areas, the ABA would like to propose specific changes in respect of the following:

- Enhanced credit RWA disclosure, focussing on templates CR9 and CR12 and the use of benchmarking;
- Improvements to the Overview of RWA template (OV1) in order to give users a simple summary of the capital requirements applying to banks; and
- A new template that would reconcile risk-based capital ratios between the national implementation of Basel III and the Basel III text.

Improving comparability and relevance

In regards to the BCBSs proposals relating to *Disclosure of hypothetical standardised approach capital*, page 3, Part III (B). The ABA does not support the suggestion that disclosure of hypothetical capital requirements (calculated according to the standardised approach) for credit, market and operational risk would reduce opacity and enhance comparability of RWA of portfolios utilising Internal Rating Based (**IRB)** approaches.

The proposed calculation is counterproductive, could serve to undermine risk-based modelling approaches, and would involve significant cost to produce purely for disclosure purposes. In effect, the

re-introduction of the standardised approach recreates Basel I issues arising from the different risk profiles of each bank, which Basel II and Basel III have addressed through the adoption of more risk-sensitive (advanced) models. These issues include RWA not reflecting the risk and complexity of the credit portfolio. For comparability purposes, the default for readers would be to revert to the hypothetical disclosure, ignoring the risk sensitivities associated with the advanced calculation.

Rather than hypothetical standardised approach capital, the ABA believes that enhancements to credit RWA disclosures are a critical part of addressing unwarranted variation in credit RWA, and that such enhancements are crucial to allowing Pillar 3 reporting to play the market discipline role it is intended to play. Specific proposals for the key credit risk templates CR9 and CR12 are therefore included. Please refer to page 3 of this letter and the section titled: **Enhancing credit RWA comparability and transparency**.

We also believe Pillar 3 relevance could be improved by enhancing template OV1 Overview of RWA, and by the addition of a new template that would reconcile risk-based capital ratios between the national implementation of Basel III and the Basel III text. Please refer to page 5 of this letter and the section titled: **Proposed addendum to the common disclosure template.**

Flexibility/Granularity

Flexibility with respect to the frequency and content of disclosures is an important element in ensuring that disclosures remain relevant and reflective of each bank's risk profile and unique business model.

The ABA agrees with the goal of improving consistency across organisations, but believes it will be difficult to achieve due to differences in jurisdictional discretions. Some of these differences are likely to be made more obvious with higher granularity of disclosures. For example, the proposed specialised lending disclosure in table CR13 contains risk-weights that are not used by the Australian Prudential Regulation Authority. Furthermore, different financial institutions have different ways of measuring and monitoring risk and proposing to require all organisations to report a highly detailed level of granularity in a consistent manner will necessitate the making of assumptions and likely lead to a degeneration of comparability and utility of the disclosures across entities and jurisdictions.

The ABA supports the proposed securitisation disclosures. These proposed disclosures appear to be a simplification of the existing requirements and the ABA believes they will provide more clarity to readers of the bank's securitisation activity and associated risks.

The proposal to increase the disclosure frequencies for a significant number of requirements represents a significant uplift in the volume, granularity and cost to produce these quarterly disclosures. With close to 75% of quantitative disclosures proposed to be reported on a quarterly basis, the feasibility of producing relevant timely content and managing the governance process for such a volume of disclosures would be challenging. The ABA believes the following templates would not need to be produced quarterly:

- CR9 and CR13 – credit risk parameters are usually reviewed on an annual cycle. Quarterly disclosure therefore would not add much value to users;
- CR10 – credit risk mitigation would generally not change significantly quarter to quarter;
- CR12 – back-testing is also usually carried out on an annual cycle. Quarterly disclosure therefore would not add much value to users; and
- Counterparty credit risk tables – generally stable over time, so the value added from quarterly disclosure is questionable.

Securitisation tables

As an alternative to changing quarterly frequency, the ABA would support allowing a materiality filter to be applied to determine whether quarterly disclosure is required or not for these templates.

Equally, the considerable increase in granularity of disclosure has the potential to add confusion rather than enhance informed decision making. Detailed prudential information on a quarterly basis has the potential to overshadow the comparability and meaningfulness of prudential information.

The use of a predominantly standardised format diminishes the opportunity for banks to articulate their respective risk disclosures in a manner that most appropriately reflects individual business models. It also serves to restrict a bank's ability to adapt risk-based disclosures to change.

Timing

A major area of concern is the proposed implementation timing. In some instances, banks may require significant systems changes to implement the proposals effectively; requiring lead time to design and build requirements, fit within technology release schedules and implement revised governance processes. Given the volume of regulatory change to be implemented over the coming period; including other Basel regulatory disclosures such as the liquidity coverage ratio and leverage ratio, the ABA believes the proposed implementation date of the first reporting period on or after 1 April 2016 to be an unrealistic and an unduly costly expectation given the scope and frequency of changes currently faced by industry.

The ABA supports adopting a phased approach to the Pillar 3 requirements to help in overcoming these implementation challenges. We urge the Basel Committee to factor in other developments in coming up with this phased approach (including the work to reduce RWA variation, the fundamental review of the trading book and IFRS 9) in order to avoid substantial rework and redesign of the Pillar 3 templates.

Enhancing credit RWA comparability and transparency

A key issue has been the comparability and transparency of credit risk-weighted assets. We are aware of work currently underway by the Basel Committee and other organisations to address the issue of unwarranted variation in RWAs.

We believe the Pillar 3 proposals will not provide an adequate disclosure solution to resolving this issue. The use of fixed templates is a welcome step forwards to improving comparability. However, we believe that further enhancements to the key credit risk templates CR9 and CR12, and explicit linkage between these templates, would materially improve the proposals in enhancing credit risk RWA comparability and providing the mechanism for banks to give the market confidence that risk estimates underpinning RWA outcomes are valid and robust.

Template CR9

This template is crucial to enabling comparability of risk estimates used within IRB models. The key improvements we would suggest to improve comparability and relevance are:

- Clarifying that all risk parameters should be those used in internal credit risk models used for RWA determination (including any regulatory floors/adjustments). It is these risk estimates and the resulting RWA amounts that need to be compared between banks and explained.
- Ensure that the on balance sheet and off balance sheet exposures (columns a and b) link back to Template LI1. References to "exposure" throughout the Pillar 3 proposals should reflect EAD.
- Ensure that the risk parameters disclosed in CR9 are the same ones as those included in the "back-testing" results in CR12 (see further comments on CR12).

- The distinction between AIRB and FIRB could be done away with as both approaches use internal PD estimates, and this could be explained in narrative.
- Establish the use of Basel asset classes rather than portfolios determined using national discretion as the minimum requirement to aid comparability between banks.
- We also suggest that an aggregated summary across the entire portfolio should be added to enable simple comparisons at a whole of bank level. This would provide in one place a summary view of the bank's aggregated risk parameters and capital intensity.

Template CR12

- The purpose of this template is to give users information to form a view of whether risk estimates used are valid and robust compared to historical experience. This is therefore a key template in demonstrating that resulting capital requirements are appropriate.
- We therefore believe that this template should be expanded to include both LGD and EAD back-testing, not just PD.
- We also believe that it is crucial that the back-testing is of the PD, LGD and EAD parameters disclosed in CR9. It is these parameters, and the resulting RWA, that this template needs to demonstrate are valid and robust.
- By explicitly tying the back-testing to the risk estimates in CR9, variances will then need to be explained (where these are driven by regulatory minimums / overlays) or defended (where the estimates are lower than historical results). We believe this is an important element to demonstrating that the risk estimates are valid and robust.
- We think the minimum granularity requirement should be to do Template CR12 at the portfolio level (again defined as Basel asset class rather than determined using national discretion). This is the minimum level consistent with CR9, and the minimum level consistent with achieving the purpose of giving users information to form a view of overall risk estimate outcomes for banks. Flexibility can be retained to allow banks to choose whether to use more granular PD ranges or not. Although banks may use many models, the aggregated outcomes should still be capable of back-testing and explanation (even though this is not the level the models are actually calibrated to). We would argue that users are more interested in the aggregated outcomes of the models rather than the actual individual model parameters used by banks.

Benchmarking for Credit RWA

The current CR9 table does not directly incorporate benchmarking requirements apart from the proposed use of hypothetical RWA requirements using the standardised approach in Phase 2 of the Pillar 3 review.

Template CR9 could be enhanced further by introducing a benchmark into the template. The benchmark could be an average of the appropriate peer group for the bank. Where the bank's parameters are significantly different from the peer average, explanation and justification would be required. The information contained in Template CR12 would play a key role in the bank's explanation and justification of the differences.

The form of this explanation would be flexible, allowing banks to determine how best to present the information.

Improved Overview of RWA

We believe the overview of RWA can be materially enhanced by moving away from the concept of minimum capital requirements is RWA x 8%, and requiring:

- Narrative describing any Pillar 1 adjustments imposed at the jurisdiction level embedded within RWA determination. For clarity this would not extend to disclosure of bank specific Pillar 1 adjustments;
- Simple disclosure of the minimum regulatory capital requirements at all levels of capital (CET1, Tier 1, TRC). This would include disclosure of the prudential minimum, capital conservation buffer and countercyclical buffer requirements applicable to the bank. This could also easily be expanded in future to pick up other requirements (such as total loss absorbing capital requirements);
- Narrative disclosure of any explicit Pillar 2 adjustments that may have been applied at the jurisdiction level (e.g. Sweden's mortgage risk-weight floors). For clarity this would not extend to disclosure of bank specific Pillar 2 adjustments.

We believe these simple enhancements would make it easy for users to understand and obtain these basic elements of the capital requirements of banks from Pillar 3 disclosure.

The below sets out a proposal for how this template might look:

		a	b	c	d	e
		RWA	RWA	Pillar 1 capital		
		T	T-1	CET1	Tier 1	TRC
1	Credit risk (excluding counterparty credit risk)					
2	Counterparty credit risk					
3	Equity positions in banking book under market-based approach					
4	Settlement risk					
5	Securitisation positions in banking book					
6	Market risk					
7	Operational risk					
8	Amounts below the thresholds for deduction (subject to 250% risk-weight)					
9	Floor adjustment					
10	Total (1+2+3+4+5+6+7+8+9)					

RWA Narrative
Comment on any Pillar 1 adjustments included in RWA

Pillar 1 capital requirements (after deductions)
Describe minimum risk based capital requirements as % of RWA, including prudential

1. *CET1 minimum of 8% includes prudential capital requirement of 4.5% plus capital*
2. *Tier 1 minimum of 9.5% comprises CET1 minimum of 8% plus Additional Tier 1*
3. *Total Regulatory Capital minimum of 11.5% comprises Tier 1 of 9.5% plus Tier 2*

Proposed addendum to the common disclosure template

Attached for the Committee's consideration is our proposed Pillar 3 template. The ABA suggests the Committee's objective of clear, meaningful and comparable disclosure could be better met by promulgation of a common disclosure template which reconciles differences in the national implementation of Basel III and the Basel III text. While the BCBS introduced a common disclosure template in relation to the composition of capital in June 2012, that template currently falls short in enabling banks to demonstrate (a) their true internationally comparable capital ratios, and (b) their true

internationally comparable RWAs. An additional template such as the attached would enable both of these to be demonstrated and would provide more meaningful information to investors.

It is proposed that the additional template:

- be mandatory with flexible content;
- be published half yearly with the existing Pillar 3 common disclosure template;
- be agreed by each national regulator as to what items are included; and
- generally only include items identified in BCBS RCAP reviews of different jurisdictions.

If there are no material differences in a jurisdiction, it could simply be stated this is the case and that a table is not necessary.

We have attached a blank template and have also attached a completed example using Australia as the jurisdiction. The Australian template is illustrative only and not currently in use in Australia.

ADDENDUM TO BCBS BASEL III COMMON DISCLOSURE TEMPLATE - GENERIC		Common Equity Tier 1 capital A$m		Tier 1 capital A$m		Total capital A$m
National numerator						
Item 1						
Item 2						
Item 3						
Item 4						
Item 5						
Internationally comparable numerator		**0.0**		**0**		**0**
National RWAs (denominator)						
Item 1						
Item 2						
Item 3						
Item 4						
Item 5						
Item 6						
Item 7						
Item 8						
Item 9						
Item 10						
Item 11						
Internationally comparable RWAs (denominator)		**0.0**		**0**		**0**
Capital ratios						
National capital ratios		**#DIV/0!**		**#DIV/0!**		**#DIV/0!**
Internationally comparable capital ratios		**#DIV/0!**		**#DIV/0!**		**#DIV/0!**

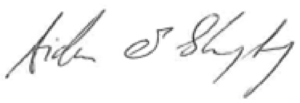
ADDENDUM TO BCBS BASEL III COMMON DISCLOSURE TEMPLATE - Australia - indicative jurisdictional example - for illustration purposes only	**Common Equity Tier 1 capital A$m**	**Tier 1 capital A$m**	**Total capital A$m**
APRA numerator			
Intangible assets			
Equity holdings			
Deferred tax assets			
Treasury shares			
Expected loss in excess of eligible provisions (LGD floor, Specialised lending/slotting, Investment home loans and Other credit risk differences impact)			
Internationally comparable numerator	**0.0**	**0**	**0**
APRA RWAs (denominator)			
APRA deductions which are risk -weighted under the internationally harmonised approach:			
Mortgage LGD (20%)			
Specialised lending / slotting			
Standardised - retail exposures			
Margin lending			
Currency threshold adjustments			
IRRBB			
Specialised lending scaling factor			
Undrawn corporate lending EAD			
Unsecured corporate lending LGD			
Other credit risk differences			
Internationally comparable RWAs (denominator)	**0.0**	**0**	**0**
Capital ratios			
APRA capital ratios	**#DIV/0!**	**#DIV/0!**	**#DIV/0!**
Internationally comparable capital ratios	**#DIV/0!**	**#DIV/0!**	**#DIV/0!**

Support for other industry submissions

The ABA supports the views expressed by IBFed in its submission to the Pillar 3 consultation and would also like to express support for the key messages in the joint submission of the Institute of International Finance (**IIF**), the International Swaps and Derivatives Association (**ISDA**) and the Global Financial Markets Association (**GFMA**).

Thank you for taking our comments into consideration and we would be pleased to discuss them further at your convenience.

Yours sincerely,



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