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March 27, 2015

The Basel Committee on Banking Supervision
Email: baselcommittee@bis.org

Dear Sirs,

The Basel Committee on Banking Supervision
Consultative Document:

«Revisions to the standardized approach for credit risk»

On behalf of the Association of Russian Banks (ARB), and particularly the ARB Committee on Basel II standards and Risk Management, we would like to thank the Basel Committee on Banking Supervision for the opportunity to deliver our opinion on the following Consultative Document «Revisions to the standardized approach for credit risk» published by the BCBS on December, 22, 2014 at [http://www.bis.org/bcbs/publ/d307.htm].

We would like to thank the Basel Committee for its great job in promoting credit risk management and measurement practices: the proposed revised standardized approach is very useful, particularly for emerging economies where external ratings are not wide spread.

We would like to propose to combine benefits of Basel I (fixed Risk-weights, RWs) and Basel II (link to external ratings) and proceed with both:

a) To use RWs for external ratings if they are available and coincide (are equivalent to plus or minus 2 subnotches across different rating agencies), use mean rating or mean RW.

b) To use updated RW metrics, as proposed. Please consider our comments in the Annex.

We are grateful to O. Zhdanova, N. Nalimova, A. Grabar, E. Rozanova, O. Kuznechenko, E. Arkhipova for their contribution in commenting the document.

We hope our comments and answers be of use for further development of the prudent international regulatory framework and stimulate its implementation.

In case of further questions, please, do not hesitate to get in touch with us through e-mail: arb@alfabank.ru.

Zeyn ADAM

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Basel II standards and Risk Management
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Annex.
Comments on
Consultative Document
«Revisions to the standardized approach for credit risk»

№	Main Topic	Consultative question	Answer	Overall opinion
1	**(2.1) Exposures to banks** **Capital adequacy**	What are respondents' views on the selection of the capital adequacy ratio? In particular, is the CET1 ratio superior to the Tier 1 ratio or the Leverage ratio? Do respondents agree that it is necessary to require calculations in accordance with Basel III in order to ensure a consistent implementation?	**Drawbacks of the proposed approach to calculation Banks RWA using CET1 and NPA ratios:** 1. The 2 proposed ratio for the Bank's risk assessment (CET 1 and NPA) are only reflect capital adequacy and assets quality of a Bank. Liquidity (which is highly important for a Bank's risk assessment) is not considered. 2. The requirements of calculations in accordance with Basel III requirements seemed not be possible to meet for majority of Banks. As a result a 300% risk weight for a significant portion of banks' exposures. 3. Calculations of ratios only once a year cannot timely reflect a Bank's risk. 4. If a Bank has an external rating it usually means that a number of more complex factors were considered (rather than before mentioned 2 factors) within risk assessment by recognized external rating agency (moreover rating date can be more recent and better reflect a Bank's risk). CET 1 cannot be a full measure a Bank's risk. We do believe that CET 1 ratio might be within set of proper measures in case it will be updated not less than quarterly. We do not agree that it should be compulsory to	It is not reasonable to avoid external ratings within RWA calculation on STA as they involves more risk factors and can provide better up-to-date assessment. We propose revise option 2 (external ratings) in part of applying the proposed approach (risk drivers) for banks without external rating. We do not believe that CET1 and NPA ratios will be timely indicators for looking forward risk assessment, especially when they based on only annual reporting. We do not support calculation of the ratios with Basel III requirements. This will lead to overestimation of RWA on such counterparties (300% even for short term claims) and hence block of financial system work through shortages in liquidity markets.

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			calculate in accordance with Basel III, as for majority of Banks it will not be possible.	
2	**(2.1) Exposures to banks** **Asset quality**	Do respondents believe the net NPA ratio is an effective measure for distinguishing a bank exposure's credit risk? What alternative asset quality measure, if any, should be considered by the Committee?	Please take note drawbacks mentioned in 1. We are aware about the following: Banks might use different definition of default and not always Basel. Does it imply that bank will calculate all of the ratios and disclose them? There could be strong difficulties to calculate the ratios for counterparties externally. Again in case of absence of information counterparty will be overcharged in terms of RWA.	We support to use ratios for unrated clients. For clients with adequate external ratings we propose to use external ratings.
3	**(2.1) Exposures to banks** **Treatment for short-term claims**	Do respondents have views on the proposed treatment for short-term interbank claims?	Having a lower risk weight for 3-months claims might be violated by a formal interruption and then a renewal (instead of contiguous renewal)	We support the idea that short-term interbank claims should have lower risk weight but with more clearly defined categories of such claims.
4	**(2.1) Exposures to banks** **Further consideration**	Do respondents have suggestions on how to address these concerns on the treatment of exposures to banks? In particular, do respondents have views on how to treat exposures to banks not subject to Basel III in a consistent and risk-sensitive manner?	We could not imagine that the proposed approach is possible to implement for not internationally active Banks, especially for countries where Basel III standards are not widely implemented and for Banks are not regulated by those standards. Even in case Banks can do those calculations for their counterparties it cannot be properly supervised.	We suggest not eliminating external ratings as part of RWA estimation as now it is more practical way for risk assessment taking into account that Basel III standards do not widely spread. We propose to assess an impact about applying RW 300% for the Banks which cannot calculate those Basel III ratios, as it could be overestimated. We are also aware about RWA methodology calibration (page 8): in practice maturity of exposures with banks

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				is shorter than 2.5 years, but LGD is higher than 45%. We suggest to use more real information for calibration of RWA values.
5	**(2.2) Exposures to corporates** **Risk drivers**	Do respondents have views on the selection of risk drivers and their definition, in particular as regards leverage and the incorporation of off-balance sheet exposures within the ratio? Would other risk drivers better reflect the credit risk of corporate exposures?	Revenue and leverage could be useful coefficients to use for unrated companies. But incorporation of off-balance exposure in those ratios seemed to be difficult to implement or assess, as not all companies will disclose it on current regulation. Leverage ratio especially would depend on companies industry. Liquidity or turnover ratios and debt/EBITDA could be other risk drivers.	We suggest to apply the proposed approach only for corporates without external rating (issued/reviewed less than 1 year). Requirements for a periodical review should be established. Thresholds nominated in foreign currency for revenue may cause unreasonable volatility of risk weights (especially for volatile national currencies).We propose to fix revenue thresholds in national currencies. Also specified revenue thresholds can be inconsistent with Russian market. In our opinion, revenue thresholds should be set at national discretion.
6	**(2.2) Exposures to corporates** **SME**	Do respondents have views on the appropriateness of the proposed treatment, especially with regard to SMEs? And about the more lenient treatment for start-up companies?	Since loans to small business can be often classified into a regulatory retail portfolio there will be many situations when the same small business will have 225% difference in risk weight depending on the size of the loan granted to it. At the same time we believe that 75% risk weight for the regulatory retail portfolio is adequate because of the granularity effect on the unexpected losses. It is better to propose a matrix for SME separately from other corporates. It is more difficult to hold a regular review. Moreover, SME in Russia could be on simplified	We suggest to adjust the left column of the table «Risk weights for senior debt corporate exposures» in order to ensure the smooth changes in the risk weights for small business around the threshold of 1 mln EURO loan size. Proposed approach is restricted for SMEs due to lack of necessary reporting and possible special programs with more simple risk assessment. For example, SMEs on simplified reporting have only revenues disclosure

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			special reporting that made difficult to assess their assets (only revenues could be assessed). Quality of reporting for SME is usually lower. Meanwhile, the proposed matrix seemed to be less conservative than a similar one for Banks. Better calibration is required. Using 110% risk weight for start-up companies is not fully justified (it is the same as for a company with Revenue EUR 1bn and leverage 5.1). We consider that it should be the same as for low level company in matrix (130%). We also propose to have a possibility to assess revenues / leverage of an Obligor Group / Guarantor in case of start-up companies to avoid a lower (130%) risk weight).	and could not be possible to assess their total assets (as it is not a compulsory reporting for them).
7	**(2.2) Exposures to corporates** **Risk sensitivity increase**	Do respondents think that the risk sensitivity of the proposal can be further increased without introducing excessive complexity?	Risk sensitivity can be increased by differentiation thresholds for risk drivers across industries.	We support a use of two proposed measures (Leverage and Revenues) only for not-rated companies. For externally rated companies we propose to use risk weights in relation to its ratings (if they are relevant).
8	**(2.2.2) Specialised lending**	Do respondents agree that introducing the specialized lending category enhances the risk sensitivity of the standardized approach and its alignment with IRB?	We agree with the proposal. Higher risk weights are reasonable for the specialized lending category (120%; 150%).	We think that financial ratios calculated on basis of cash flow model are more appropriate for specialized lending than revenue and leverage. Also financial structure of deal (e.g. the debt/equity ratio, the term of the debt and its repayment schedule) can be used to assess the risk of specialised lending.
9	**(2.4) Retail portfolio**	Can respondents suggest, and provide evidence on, how to increase the risk	We support the most unified approach to the standard retail exposure with the risk weight 75%.	To allow banks be more flexible with retail products (risks for which are properly diversified and relatively small),

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		sensitivity of the regulatory retail exposures treatment, either by differentiating certain product subcategories for which a specific risk weight may be appropriate; or by suggesting simple risk drivers that could be used to assess the risk of all retail exposures?		as well as due to impossibility to review financial standing of individuals we support not to introduce specific risk drivers for the standard retail exposure and use the risk weight 75% under standardized approach. IT costs overweight benefits from differentiation.
10	**(2.5.1) Exposures secured by residential real Estate**	Do respondents agree that LTV and/or DSC ratios (as defined in Annex 1 paragraphs 40 and 41) have sufficient predictive power of loan default and/or loss incurred for exposures secured on residential real estate?	LTV and DSC may have good predictive power (in case if they are updated), as exposures secured by residential real estate have usually big maturity, therefore can be significantly changed over time. Moreover, there is no market practice in Russia to oblige individual borrowers to provide a bank with their updated income, which could be highly changeable over time. Therefore for the current banking practice it seems possible to assess those ratios for individuals only on a stage of a loan granting. Otherwise, it is required to significantly change current banking practices.	LTV has better predictive power (in case it is updated at least quarterly) due to nature of risks of the exposures secured by real estate. It is hard to use up-to-date assessment of DSC, as individuals can easily change their working place without a bank's notice. Overall, it is hard to update LTV and especially DSC regularly. IT costs overweight benefits from differentiation. It would be better use a standard risk weight for residential real estate.

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11	**(2.5.1) Exposures secured by residential real estate**	Do respondents have views about the measurement of the LTV and DSC ratios? (In particular, as regards keeping the value of the property constant as measured at origination in the calculation of the LTV ratio; and not updating the DSC ratio over time.)	If DSC ratio is not updated over time it cannot provide a proper looking-forward assessment for RWA estimation.	LTV is possible to regularly update. DSC is not possible to update. But it is hard to update LTV and especially DSC regularly. IT costs overweight benefits from differentiation. It would be better use a standard risk weight for residential real estate.
12	**(2.5.1) Exposures secured by residential real estate**	Do respondents have views on whether the use of a fixed threshold for the DSC ratio is an appropriate way for differentiating risks and ensuring comparability across jurisdictions? If not, what reasonably simple alternatives or modifications would respondents propose while maintaining consistent outcomes?	A fixed threshold for the DSC ratio is an appropriate way for differentiating risks with different sets of LTV thresholds as the main risk driver.	As DSC ratio is not the main within risk weight assessment it is possible to use a fixed threshold. But it is hard to update LTV and especially DSC regularly. IT costs overweight benefits from differentiation. It would be better use a standard risk weight for residential real estate.
13	**(2.5.1) Exposures secured by residential real estate**	Do respondents propose any alternative/additional risk drivers for the Committee's consideration in order to improve the risk	No additional risk drivers. It would be better use a standard risk weight for residential real estate.	To rely more on LTV ratio rather than on DSC. But it is hard to update LTV and especially DSC regularly. IT costs overweight benefits from differentiation. It

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		sensitivity in this approach without unduly increasing complexity?		would be better use a standard risk weight for residential real estate.
14	**(2.5.2) Exposures secured by commercial real estate**	Which of the two options above is viewed as the most suitable for determining the risk-weight treatment for exposures secured on commercial real estate?	We suggest to apply the 2nd option – using a table of risk weights ranging between 75% and 120% based on LTV ratio.	We support the recognition of the real estate collateral and treating the exposure as secured.
15	**(2.5.2) Exposures secured by commercial real estate**	What other options might prudently increase the risk sensitivity of the commercial real estate treatment without unduly increasing complexity?	We suggest to supplement LTV risk driver for commercial real estate with the 2nd risk driver: Revenue. Risk drivers should be updated quarterly.	In our opinion, Revenue is the other option which might increase risk sensitivity of the commercial real estate treatment (additionally to LTV).
16	**(2.6) Risk weight add-on for exposures with currency mismatch**	Do respondents agree that a risk weight add-on should be applied to only retail exposures and exposures secured by residential real estate? What are other options for addressing this risk in a simple manner?	We agree with a risk weight add-on for a certain retail clients. We suggest to use for retail client DSC ratio (at the moment of the origination loan) as threshold (e.g. 35%): if DSC exceeds threshold a risk weight add-on is to be applied.	We do not support the additional risk weight for currency mismatch for all retail exposure as it is diversified enough. If DSC ratio is low at the moment of exchange rates increase the retail client will be more inclined to keep paying in order to keep own credit history good.
17	**(2.7) Off-balance sheet exposures**	Do respondents consider the categories for which a CCF is applied under the standardised approach to be adequately defined?	We agree with the proposal.	We agree with the proposal.
18	**(2.7) Off-balance sheet**	Do respondents agree that instruments allocated	We suggest to delegate to a national discretion to establish CCF for unconditionally cancellable	Unified CCF 10% for unconditionally cancellable commitments is too

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	exposures	to each of the CCF categories share a similar probability of being drawn and that the probabilities implied by the CCFs are accurate? Please provide empirical support for your response.	commitments.	conservative in our opinion, we cannot prove that by our law practice.
19	**(2.8) Past-due loans**	What are respondents' views on the alternative treatments currently envisaged for past-due loans?	We consider reasonable to apply a risk weight for past-due to a difference between past-due exposure and specific provisions.	We could offer to take into account a maturity of past-due to assign a higher risk weight for older past-due exposure.
20	**(2.9) Exposures to multilateral development banks**	Do respondents agree with the proposed treatment for MDBs?	0% risk weight for eligible MDBs and risk weight depending on MDB's rating sound reasonable for MDBs treatment.	We agree with the proposal.
21	**(2.10) Other assets**	What exposures would be classified under "Other assets"? Is a 100% risk weight appropriate? (Please provide evidence where possible).	We agree with a 100% risk weight for other assets.	We agree with a 100% risk weight for other assets.
22	**(3.2) Eligible financial collateral**	What are respondents' views on the above alternative ways to define eligible financial collateral?	We agree that senior debt securities could be accepted as eligible financial collateral using the concept of «investment grade». But we do not support stop using external ratings for that.	External ratings should be an option within eligible financial collateral definition.
23	**(3.2) Eligible financial**	What are respondents' views on the recalibrated	We agree with the increasing number of maturity buckets for other issuers but we do not support the idea	External ratings should be an option within haircut definition for eligible

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	collateral	supervisory haircuts shown in Table 4? What are respondents' views on how to eliminate references to ratings from the supervisory haircuts table? What could be the implications of eliminating references to external ratings?	of eliminating references to external ratings (it should be an option).	financial collateral.
24	**(3.3) Eligible credit protection providers**	What are respondents' views on the proposed corporate guarantor eligibility criteria?	We do not support the idea that only prudentially regulated financial institutions are eligible guarantors.	To have possibility to consider guarantees of corporate guarantors (at least with external ratings)