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To: the Basil Committee
[06 February 2016]

Dear Sir/Madam

RE: BCBS Consultative Document: TLAC Holdings

We are writing to you as China Banking Association representing the Chinese banking industry. China Banking Association (CBA) is a nationwide non-profit self-discipline organization of China's banking sector. CBA serves for the common interest of its members through the functions of self-discipline, rights protection, coordination and service so as to safeguard lawful rights and maintain market order of the banking sector, and promote the healthy and sustainable development of the industry. By September 2015, CBA has 383 members and 4 observers.

We sincerely appreciate the great endeavor FSB and BCBS have made in the field of enhancing international financial regulatory reforms and ending "too big to fail" for G-SIBs. Theoretically, the proposed deduction treatment for banks' investments in TLAC set out by the Basel Committee in this consultative document, may contribute to enhancing effective resolution regimes without the use of public funds, and promoting robust management of financial institutions and stability of global financial system. However, in practice, the proposed deduction treatment for banks'

investments in TLAC should take into consideration the realities and practical issues across jurisdictions, in case that too much rigorous deduction treatment would result in the procyclical amplification of the system-wide shock when it happens. We therefore wish to share the following observations with you from our perspectives as China Banking Association representing the Chinese banks, which we hope can be helpful.

First, we suggest that banks be required to deduct their holdings of TLAC instruments accordingly from their own TLAC resources.

Under Basel III, banks are required to deduct their holdings of capital instruments on a corresponding basis. If a bank is required to make a deduction from a particular tier of capital and it does not have enough of that tier of capital to satisfy that deduction, the shortfall will be deducted from the next higher tier of capital.

The consultative document proposed that internationally active banks (both G-SIBs and non-G-SIBs) be required to deduct their TLAC holdings from their own Tier 2 capital. This proposed deduction treatment is not in line with requirement of Basel III, and would increase the issuing costs of TLAC instruments to be equal to that of Tier 2 capital instruments. Thus, we suggest that banks be required to deduct their holdings of TLAC instruments accordingly from their own TLAC resources.

To this end, we suggest to apply a different treatment to G-SIBs and non- G-SIBs. It is suggested that G-SIBs' TLAC holdings should be deducted from their own TLAC, and the shortfall be deducted from the higher tier of capital. Non-G-SIBs' TLAC holdings could be subject to large exposure limits, including both the limit of holding TLAC against a single counterparty and the limit of overall TLAC holdings.

Second, we suggest that the deduction threshold of the minority investment on TLAC holdings be increased to 30% of bank's Common Equity Tier 1, from previously 10%.

The consultative document proposed that when a bank owns less than 10% of the common shares of the issuer, holdings of TLAC of that issuer should be deducted subject to the threshold of 10% of the bank's CET1.

However, the Committee has not specified the calculation of the threshold, whether by using the sum of TLAC and Tier 2 Investment over the total Common Equity Tier 1 Capital, or by using the only the TLAC investment over the total Common Equity Tier 1 . If it is the former, we suggest that the threshold should be increased correspondingly.

Firstly, 10% threshold is applied for capital holding deduction in Basel III by the Committee. However, the characteristic of TLAC instruments differs from that of capital instruments, and the requirement of TLAC instruments is much higher than that of Capital requirement. When the content of deduction expands from capital to include both capital and TLAC, we suggest that the threshold increase correspondingly from 10% to 30%.

Secondly, the endurable range of TLAC deduction threshold differs greatly across jurisdictions. For jurisdictions where G-SIBs account for large market shares, the market absorption capacity of G-SIBs' TLAC instruments would be much limited when non-G-SIBs, with small amount of Common Equity Tier 1 capital due to the low market share, are constrained by low deduction threshold (e.g. 10%) of TLAC investments.

Thirdly, the low level of deduction threshold will result in the procyclical amplification of the system-wide shock when it happens. A bank's Common Equity Tier 1 would suffer when facing a system-wide financial crisis and its Tier 2 capital would be easily deducted due to the low level of deduction threshold, causing the bank's capital adequacy level to decrease in an even faster pace, and resulting in the procyclical amplification of the system-wide shock.

In this respect, we suggest that the deduction threshold be set at 30% of bank's

Common Equity Tier 1, or the Committee allows national supervisors to have discretion in setting the deduction threshold within a broad range based on their local market conditions, while guidance for setting deduction threshold could be clarified by the Committee.

Third, the deduction of investment on TLAC instruments issued by G-SIBs headquartered in emerging markets jurisdictions should have the exemption period consistent with that of the TLAC requirement.

The consultative document proposed that the deduction of TLAC holdings should include TLAC instruments issued by Chinese G-SIBs, even though they are not initially subject to the minimum external TLAC requirement. However, we suggest that the deduction of TLAC holdings issued by G-SIBs headquartered in emerging market jurisdictions should be given the same exemption period as that of the TLAC requirement, which will be exempted until 2025.

Fourth, it is suggested that all instruments subject to TLAC deduction be identified for an investing bank's reference.

For G-SIBs adopting a statutory and structural subordination, loss absorption terms are not usually defined in the term sheets of issued instruments. For example, senior bonds issued by HSBC holdings will be counted as TLAC, while senior bonds issued by HSBC will be excluded from TLAC. In order to facilitate an investing bank to understand timely the relevant investment information of TLAC instruments issued by other banks, it is suggested that all instruments subject to TLAC deduction be identified.

Finally, it is suggested to apply a 100% risk weight to undeducted TLAC instruments when calculating RWAs.

Subordinated debts are subject to a 150% risk weight, according to the second

consultative document of *Revisions to the Standardised Approach for credit risk* issued in Dec 2015. The current consultative document of TLAC holdings does not specify the risk weight of undeducted TLAC instruments, and we suggest to apply a 100% risk weight to undeducted TLAC holdings due to the fact that TLAC holdings are further subordinated to normal Tier 2 capital.

Yours faithfully

A handwritten signature in black ink, reading 'Yang Zaiping', written in a cursive style.

Yang Zaiping

Executive Vice President

China Banking Association