

3 June 2016

William Coen
Secretary General
Basel Committee on Banking Supervision
Bank for International Settlements
Centralbahnplatz 2
4051 Basel
Switzerland

By email: www.bis.org/bcbs/commentupload.htm

Dear Mr Coen

Standardised Measurement Approach for operational risk

COBA welcomes the opportunity to comment on the BCBS's March 2016 consultative document proposing a standardised measurement approach for operational risk.

COBA is the industry body for Australia's credit unions, mutual building societies and mutual banks. Collectively, the sector we represent has A\$97 billion in assets and serves more than 4 million customers.

The customer-owned model is the proven alternative to the listed model in the Australian banking market, delivering competition, choice, and consistently market leading levels of customer satisfaction.

Prudential regulation in Australia

All of Australia's banks, building societies and credit unions are Authorised Deposit-Taking Institutions (ADIs) and are regulated by the Australian Prudential Regulation Authority (APRA), our 'national supervisor', under Australia's Banking Act 1959.

All Australian ADIs are subject to the same prudential framework. While customer-owned banking institutions are not currently "internationally active banks", APRA exercises its discretion to apply Basel frameworks to customer-owned banking institutions.

In Australia, there are two forms of operational risk capital calculation. The five largest banking institutions (Commonwealth Bank, National Australia Bank, Westpac, ANZ and Macquarie Bank) use the advanced measurement approach (AMA) to calculate operational risk capital requirements. All other Australian banking institutions, including customer-owned banking institutions, use APRA's standardised approach. This standardised approach is a reduced form of the Basel standardised approach.

Support the withdrawal of advanced measurement approaches

The consultative document proposes that all "internationally active banks" use a single non-model-based method. This consolidates the three approaches under the Basel II Framework into a single standardised measurement approach (SMA). The SMA would be used by all banks subject to the Basel regime.

COBA supports the withdrawal of the AMA proposal as it eliminates one of the advantages that the advanced banks have over institutions following the standardised approach.

This unfair advantage has already been identified in credit risk models where Australia's Financial System Inquiry found that "the relative riskiness of mortgages between internal-ratings based [advanced] and standardised banks does not justify one type of institution being required to hold twice as much capital".¹ COBA supports the Basel Committee's broader intentions to ensure that "the standardised approaches constitute a suitable alternative and complement to internal models".²

The single approach goes some way to narrowing the gap between standardised and non-standardised banking institutions. The proposed single approach will also increase the transparency of operational risk capital requirements.

The BCBS proposal and COBA members

Under the current proposal, banks are only subject to the loss multiplier component if they have a business indicator (BI) exceeding €1 billion. The paper notes these banks are generally medium to large banks with assets above €20 billion (A\$32 billion).

COBA represents a broad spectrum of customer-owned banking institutions with individual member's assets ranging from A\$10 million to A\$12 billion, well outside the proposed definition of medium to large banks.

COBA member feedback confirms that they would sit in 'bucket 1' and therefore not be subject to the loss multiplier. COBA therefore believes that this threshold is currently set at an appropriate level.

If COBA members were subject to the SMA, the operational regulatory risk capital (ORRC) charge would simply be a linear function of their business indicator (11 per cent of their BI). Further, while COBA members do not need to incorporate loss data into their ORRC, some larger COBA members already collect this operational loss event data for other purposes.

However, several COBA members have commented that the business indicator calculation is significantly more complex than what is required under APRA's current prudential regime. Some members also noted that while the figures for this calculation are generally available from accounting data, there may be difficulties if more detailed data were required. Members also sought clarification about whether there would be a similar 12.5 times 'uplift' factor to calculate the operational risk weighted assets as under the previous approach.

As always, when subjecting all institutions to the same prudential regime there is a risk that it could create excess burden on some entities. As noted by the consultation paper, the SMA approach will apply to "internationally active banks" and application below this level is at the discretion of national supervisors. We would welcome direct advice from the BCBS to national supervisors that this should not be applied to small domestic banks to avoid any ambiguity.

In summary, COBA supports measures, such as the proposed withdrawal of advanced measurement approach, that reduce the unfair advantages that advanced institutions have over standardised institutions. Standardised institutions, such as customer-owned banking institutions, improve diversity and competition in the banking sector.

¹ See Financial System Inquiry Final Report page 61

² Basel Committee on Banking Supervision: Revisions to the Standardised Approach for Credit Risk March 2015

Please do not hesitate to contact me on +61 2 8035 8450 to discuss any aspect of this submission.

Yours sincerely

A handwritten signature in black ink, appearing to read 'Sally Mackenzie', with a long horizontal flourish extending to the right.

SALLY MACKENZIE
Acting Head of Public Affairs