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# FFSA Response to the call for comments on the Basel Committee's consultative document on Revisions to the standardised approach for credit risk of banks

27 March 2015

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| **Subject:** | **Basel Committee's consultative document on Revisions to the standardised approach for credit risk of banks** |
| **From:** | French Federation of Insurance Companies (FFSA ) |
| **To:** | The Basel Committee's |

## I. Introduction / General remarks :

### 1) The proposals put forward should better take into account counterparty diversity and risk granularity in certain lines of business:

Risk weight calibrations built up on two risk criteria so as to apply that risk weighting to all companies does not take into account counterparty diversity and risk granularity observed in these lines of business.

The most striking example is treatment of exposure to insurance company risks where use of just one risk weight calibration irrespective of the company’s size, business sector and region where it operates, is just not practical.

It would be preferable if the risk criteria put forward could be further refined and differentiated depending on the business transacted. Several risk weight calibrations should be proposed for treating exposures to companies. One specific calibration, in particular, should be used for calculating the risk weight of banks' liabilities arising from insurance companies.

### 2) The changes proposed would lead to a disproportionate increase in the weighting of liabilities where the counterparty is an insurance company:

Whereas the document submitted for consultation (executive summary) lays down the principle that an increase in capital requirements is not the committee's objective, the risk weight calibration proposed for liabilities towards companies would mean that liabilities arising from insurance companies would, from now on, most often lie between 90 and

120%, against the previous level of 20% for companies with a good rating from credit rating agencies.

In view of the fact that risk weight levels calculated by the standard method will be used to calibrate the floor capital for banks, it is essential that these results should not deviate fundamentally from those calculated under their IRB models.

3) **Use of risk criteria instead of ratings issued by independent credit rating agencies would generally lead to less relevant and lower quality measurements.**

While the objective is that independent ratings should not replace risk assessment, the proposed risk weight calibrations are based on 2 or 3 risk criteria that are much less sophisticated than the prospective analysis employed by credit rating agencies. It would be better if these ratings were not totally excluded from the standard method except if the risk criteria employed provided better coverage of all risks and that they looked forward in time.

## II. <u>Replies to questions:</u>

The FFSA will only reply to questions that have an impact on accounting for a bank's liabilities towards its customers.

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| Q5. 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? |

We do not believe one single class of risk driver is sufficient to reflect the diversity of risk arising from different counterparties and different lines of business.

We do not think the two risk criteria proposed are sufficient to apply to the diversity of counterparties and business lines.

They may well vary considerably depending on accounting regulations in different countries.

They just cannot be calculated and are not appropriate for certain types of company.

A leverage ratio is just not appropriate for an insurance company whose leverage (before off-balance sheet items) will always exceed 5, which would lead to a weighting of between 90 and 130% depending on the value of premium income whereas some companies, however, do have a very high independent rating (between A+ and A) and so this does not take into account the actual level of risk.

It would appear necessary to treat insurance companies as a special case.

Mortgage loan insurance companies should be assessed on risk criteria that are appropriate for the business they transact.

We would therefore suggest that the Basel Committee uses risk indicators that are inherently suited to the features of the insurance industry.

Q7. Do respondents think that the risk sensitivity of the proposal can be further increased without introducing excessive complexity?

Risk sensitivity criteria are important because the results obtained would be used later as floor capital under the IRB approach.

The criteria to be adopted should be intuitive, unambiguous and appropriate for each risk type.

The criteria proposed would appear therefore to need further criteria for certain exposure types such as those on insurance companies. Following this a new impact study should be undertaken so as to measure the appropriateness of the calibration level determined.