European Bank
for Reconstruction and Development

Steven D. F. Kaempfer
Vice President
Finance

Mme Danièle Nouy
Secretary-General of the Basel Committee on Banking Supervision
Basel Committee on Banking Supervision
Bank for International Settlements
Centralbahnplatz 2
CH-4002 Basel
Switzerland

24, January 2003

Dear Mme Nouy

Commercial bank participation in Multilateral Development Bank loans

We much welcomed the approach proposed in the Technical Guidance for the third Quantitative Impact Study for commercial bank participation in Multilateral Development Bank loans. May I take this opportunity to suggest two changes to the text of Footnote 23 as outlined below which, we believe, would remove the potential for ambiguity in interpretation.

> 23 However, when an exposure arises through a bank's ~~sub~~-participation in a loan that has been extended by a Multilateral Development Bank (MDB) ~~whose preferred creditor status is recognised in the market and transferred to the sub-participants,~~ its convertibility and transfer risk can be considered to be effectively mitigated by national supervisory authorities. In such cases the borrower's domestic currency rating may be used for risk weighting purposes instead of his foreign currency rating.

In general, the more generic the text, the less likely it will lead to difficulties in future. More specifically, the rationale for suggesting these changes is as follows:

1. The term "sub-participation" is usually used to distinguish a particular form of participation such as a participation in another bank's participation which is not the intended meaning here. Therefore, "participation" is the correct term.
2. The notion that preferred creditor status is "recognised in the market" could create undesirable debate regarding the definition of the words "recognised" and "market" as well as the data or evidence required to prove this recognition.

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3. We believe there is no need to state that preferred creditor status is "transferred" to sub-participants, as this is already part of the notion of participation and is therefore redundant. Participating banks share in the MDB's preferred creditor status by virtue of their participation in the loan and the loan's structure. The bank benefits from preferred creditor status, but the preferred creditor status is not actually "transferred".

We understand the treatment proposed for the standard approach will provide guidance to supervisors when reviewing internal ratings based approaches.

I enclose for your information a copy of our letter of 20 January 2003 to the European Commission providing the corresponding suggestion with respect to the proposed Article 35 of the Commission's Working Document on Capital Requirements for Credit Institutions and Investment Firms.

With many thanks for your consideration of our comments previously expressed and those outlined in this letter.

Yours sincerely,

Enclosure: copy of EBRD's letter of 20 January 2003 to the European Commission

European Bank
for Reconstruction and Development

Steven D. F. Kaempfer
Vice President
Finance

Dr Alexander Schaub
DG Internal Markets
European Commission
Avenue de Cortenberg 107 (06/74)
1049 Brussels
Belgium

20 January 2003

Dear Dr Schaub,

"Working Document of the Commission Services on Capital Requirements for Credit Institutions and Investment Firms" 18 November 2002

The EBRD appreciates the opportunity to comment on the current working document. A significant amount of the loans made by the European Bank for Reconstruction and Development ("EBRD") are structured to attract and mobilise funds from the commercial banking sector Indeed, our mandate requires us to involve other sources of financing in our operations, and commercial banks are currently our main co-financing partners. The majority of EBRD loans involving commercial banks use the so-called A/B loan structure, where the B loans represent that portion of EBRD's loan that is sold to commercial banks. Thus, the B loan is an extremely important instrument for the EBRD in fulfilling its mandate to provide financing for the economies of central and eastern Europe.

In light of the above considerations, we have reviewed the relevant wording in the proposed text of Article 35 and would like to suggest a change to the text as outlined below which, we believe, would remove the potential for ambiguity in interpretation.

Article 35 **Domestic and foreign currency items**

1. A credit assessment that refers to an item denominated in the obligor's domestic currency cannot be used to derive a risk weight for another claim on that same obligor that is denominated in a foreign currency.

2. Notwithstanding the provision of paragraph 1 of this Article, competent authorities may, when an exposure arises through a bank's ~~sub-~~participation in a loan that has been extended by a Multilateral Development Bank ~~whose preferred creditor status is recognised in the market and transferred to the sub-participants,~~ allow that the credit assessment on the obligor's domestic currency item be used for risk weighting purposes instead of his foreign currency rating

The rationale for recommending these changes is as follows:-

- In general, the more generic the text, the less likely it will lead to difficulties in future, and, specifically;
- the term "sub-participation" is usually used to distinguish a particular form of participation such as a participation in someone else's participation which is not the intended meaning here;
- the notion that preferred creditor status is "recognised in the market" could create undesirable debate regarding the definition of the words "recognised" and "market" as well as the data or evidence required to prove this recognition;
- we believe there is no need to state that preferred creditor status is "transferred" to sub-participants, as this is already part of the notion of participation and is therefore redundant.

We hope that you find these recommendations useful, and we would welcome the opportunity to discuss the above with you or provide further comment should this be helpful.

In any event, I look forward to an early opportunity of seeing you again in Brussels or London.

Yours sincerely,

Steven Kaempfer

cc: Klaus Regling
Director General ECFIN
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1049 Brussels

Philippe Petit-Laurent, Director for E.C.
EBRD
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0.167
0.096
0.089
0.135
0.227
0.401
0.160
0.273
0.195
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1.996
0.667
0.762
0.103
0.305
0.028
0.379
11.779