



Update on joint Basel Committee and International Organization of Securities Commission work on the prudential treatment of some trading book items.

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New work on counterparty credit risk and trading book-related issues

As it announced in its press release, on 15 January 2004, the Basel Committee on Banking Supervision (BCBS) has set up a joint group, together with the International Organization of Securities Commissions (IOSCO), in order to review the treatment of certain counterparty credit risk and trading book-related items in the light of the Basel 2 framework. This joint group is co-chaired by Messrs Oliver Page (UK Financial Services Authority) and Michael Macchiaroli (US Securities and Exchange Commission). It comprises an equivalent number of BCBS and IOSCO representatives. The joint group has now met three times, in March, May and June.

During these meetings, the joint group had fruitful discussions with securities and banking associations, as well as with some individual banks and investment banks. These discussions helped to identify, define and prioritise issues for the joint group. To take forward its work, the joint group has set up three working groups, each co-chaired by a BCBS and an IOSCO member of the joint group. The first of these will deal with the treatment of counterparty credit risk for over-the-counter derivatives, repo-style and securities financing transactions. It will also consider cross-product netting. The second working group will consider the short-term maturity adjustment, in the internal rating-based approach, for some trading book-related items and also the treatment of double-default effects for hedged transactions. The third one will consider other trading book issues, including valuation, risk management and capital treatment for less liquid instruments held in the trading book. It will also consider the treatment of unsettled transactions and the use of commodities as collateral in certain transactions.

To improve its understanding of each issue identified, the joint group will carry out a survey of banks' and investment banks' trading books during the summer. To that end, it has been discussing with some industry participants a draft questionnaire to be sent out by mid-July with responses sought by mid-September.

As the joint group and its working groups take forward their work, they will continue to maintain a close interaction with the industry and other interested parties. This could include questionnaires aimed at following up the trading book survey on some specific issues.