

**15 January 2004**

The Basel Committee on Banking Supervision continues to make progress on its work to revise the international accord on bank capital following the agenda established in Madrid last October. At today's meeting in Basel, the Committee reviewed the progress made on outstanding matters to meet its mid-year 2004 objective and took decisions on key issues.

### **Public comments supported the Committee's proposal on credit-related losses**

The Committee received 52 comment letters from institutions and industry associations on its October 2003 proposal to revise the capital treatment for expected and unexpected credit losses. Respondents generally welcomed the Committee's solution and agreed that it will align regulatory capital more closely with the concepts underpinning leading banks' economic capital modelling processes. The Committee believes that these comments will be instrumental in strengthening the quality of the New Accord.

The Committee has decided on concrete modifications necessary to implement the proposal made in October and will publish them shortly. Moreover, the Committee agreed with industry comments that the cap on the recognition of excess provisions should not be based on Tier 2 capital components. Instead, it has decided to convert the cap to a percentage (to be determined) of credit risk-weighted assets.

### **Significant progress achieved on the treatment of securitisation exposures**

The Committee agreed to simplify the treatment of securitisation-related exposures and align it more closely to industry practice in response to public comments to the third consultative paper (CP3) on the New Accord. Under the new treatment, banks will be allowed to derive the risk weights on unrated exposures to asset-backed commercial paper conduits (mainly liquidity facilities) by mapping their internal risk assessments to external credit ratings; a less complex "Supervisory Formula" will be available for determining capital for unrated securitisation exposures; and both originating and investing banks will be able to make equivalent use of the "Ratings-Based Approach" (RBA) for rated securitisation exposures. Finally, the Committee reviewed the calibration of the securitisation RBA risk weights to ensure a closer alignment with the level of risk inherent in the positions.

The main points are set out in Attachment A. The Committee will also publish shortly a more detailed technical note specifying the revisions to the securitisation proposals.

Furthermore, progress was made in the following areas.

### **Advances on credit risk mitigation techniques and related issues**

The Committee has agreed to refine the rules for recognising credit risk mitigation techniques in response to industry comments. The Committee likewise recognises that the existing treatment of credit risk mitigation must continue to evolve in order to reflect industry practices, particularly as they relate to double default effects. The Committee believes that recognition of these effects is necessary, though it is essential to consider all of the implications, especially those related to measurement, before a solution is decided. The Committee will continue work on this topic with the intention of finding a prudentially sound solution as promptly as possible prior to implementation of the New Accord.

Alongside this work, the Committee plans to undertake a review of counterparty credit risk and trading book issues in coordination with the International Organisation of Securities Commissions (IOSCO).

### **Pillar 2 implementation clarified**

In response to recent discussions with banking organisations, the Committee agreed on clarifications for implementing the supervisory review of capital, or Pillar 2 of the New Accord. These clarifications are appended as Attachment B.

## **Cooperation between home and host supervisors**

Building on the principles published in August 2003 (*High-Level Principles for the Cross-border Implementation of the New Basel Capital Accord*), the Accord Implementation Group (AIG) of the Committee is evaluating several actual case studies. This exercise is contributing significantly to member authorities' understanding on practical aspects of cross-border implementation.

The Committee agreed on principles for the cross-border implementation of the advanced measurement approaches (AMA) for operational risk requirements. These principles balance the need for the adequate capitalisation and sound risk management of significant internationally active entities in cross-border banking groups with the need for the practical application of the AMA within these groups. The details of the proposal and related principles will be published shortly.

### **Schedule**

Working groups will make recommendations on the outstanding issues at the Committee's next meeting in May 2004, where the Committee will additionally address the calibration of capital requirements. Both efforts will allow the Committee to achieve its mid-year 2004 goal and ensure that the text will provide a solid basis for national implementation processes and the industry's preparations to proceed. In accordance with the decisions announced in its October 2003 press release, the Committee will again evaluate the New Accord's calibration prior to implementation.

The Committee reaffirmed its objective to maintain broadly the aggregate level of regulatory capital in the banking system. It intends for the simpler approaches to produce overall capital requirements that are broadly equivalent to those of the existing rules while establishing incentives to adopt the more advanced approaches. The Committee will moreover continue to work to ensure that the Accord remains up to date with the best practices in risk measurement and management.