The voice of banking
& financial services

27 July 2012

Cp-2012-08@eba.europa.eu
European Banking Authority

Dear Sirs,

Consultation paper on draft Regulatory Technical standards on Capital Requirements for CCPs

The BBA is pleased to respond to the consultation.

Key messages

We believe that in drafting proposals to mitigate systemic risk, the authorities should try to strike the right balance between financial stability, economic growth and financial innovation.

It makes sense to apply rules similar to that applied to regulated entities under the Capital Requirements Directive (CRD). However, the function of a CCP is to minimise risk whereas that of a regulated entity is to balance risk and reward. As a consequence, their capital structures are different and not all of the CRD proposals will be relevant to CCPs. In addition, there are issues such as large exposure limits which should to be addressed.

We note that the Basel Committee is working on the treatment of a CCP's default fund and reviewing the trading book. In addition, CRD IV and CRR, going through trialogue [as at the time of writing, late June 2012], refers to CCPs. We urge the EBA to factor these work streams into consideration and to build flexibility into the standards that are issued.

The approach that the Committee proposes for credit and counterparty risk related to non-covered activities is not risk-sensitive; in fact it seems even less risk-sensitive than Basel I for banks. A more risk-sensitive approach (such as Basel II IRB combined with IMM) would assign credit risk weights that depend on the counterparty and exposure that reflect the possible market values of an OTC trade. Such an approach would require the CCP to have internal models (CCPs presumably have some modeling capacity to set their margin requirements). The lack of risk-sensitivity can create undesirable incentives;

The approach that is being proposed for market risk related to non-covered activities is not very risk-sensitive either.

Annex 1 to our letter contains our formal response to the consultation, and further specific observations and questions arising from the proposals.

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We hope that you will find our comment useful. Please contact me by way of e-mail (irving.henry@bba.org.uk) or telephone on (00 44) 20 7216 8862 should you require further information.

Yours faithfully,

Irving Henry
Director, Prudential Capital and Risk

Annex 1

Q 1. Do you support this approach to capital requirements?

As stated above, we believe that in drafting proposals to mitigate systemic risk, the authorities should try to strike the right balance between financial stability, economic growth and financial innovation.

It makes sense to apply rules similar to that applied to regulated entities under the Capital Requirements Directive (CRD). However, the function of a CCP is to minimise risk whereas that of a regulated entity is to balance risk and reward. As a consequence, their capital structures are different and not all of the CRD proposals will be relevant to CCPs. Further, there are additional areas such as large exposure limits which require to be addressed.

Q 2. Do you have any other option to suggest that is not covered in this draft RTS?

No.

Q 3. Do you consider there to be any alternative approach which is more appropriate that would be consistent with Article 16 of the Regulation?

No.

Q 4. What is the incremental cost to your CCP for the implementation of this proposal?

This is a matter for CCPs and their regulators.

Q 5. What is the incremental benefit to your CCP for the implementation of this proposal?

This is a matter for CCPs and their regulators.

Q 6. What is the incremental cost for the supervisors for the implementation of this proposal?

This is a matter for CCPs and their regulators.

Q 7. What is the incremental benefit for the supervisors for the implementation of this proposal?

This is a matter for CCPs and their regulators.

Q 8. What is your view on the notification threshold? At which level should it be set?

We believe that 25% higher than the capital requirements is too low. We believe that the level should not be below 110%, which is the level set for firms regulated by the United Kingdom's Financial Services Authority although, given the business model of CCPs, consideration should be given as to whether a fixed or higher percentage is appropriate.

CCPs should be required to have policies and procedures in place, approved by the authorities, as to the steps to be taken in the case that the trigger is breached.

Q 9. In your view, in which case should restriction measures be taken by the competent authority once the notification threshold is breached?

This is a matter for CCPs and their regulators.

Q 10. Which criteria do you take into account for estimating the appropriate time span for orderly winding down or restructuring of the CCP’s activities?

This is a matter for CCPs and their regulators.

Q 11. What is your estimation for the number of months necessary to ensure an orderly winding-down or restructuring of the CCP’s activities?

This is a matter for CCPs and their regulators.

Q 12. What is the incremental cost or benefit to your CCP of this proposal assuming that the time span for winding down or restructuring a CCP’s activities is 12 months?

This is a matter for CCPs and their regulators.

Q 13. How do you currently measure and capitalise for operational risk?

This is a matter for CCPs and their regulators.

Q 14. Do you think that the banking framework is the most appropriate method for calculating a CCP’s capital requirements for operational risk? If not, which approach would be more suitable for a CCP?

In theory, firms agree with the EBA’s approach although the business model and systemic importance of CCPs will require changes to a basic CRD approach.

Q 15. Do you think that the Basic Indicator Approach set out for banks is appropriate for CCPs?

This is a matter for CCPs and their regulators.

Q 16. In your view, which alternative indicator should the EBA consider for the Basic Indicator Approach?

This is a matter for CCPs and their regulators.

Q 17. What would be the incremental cost of employing the basic indicator approach set out for banks for the calculation of your capital requirements for operational risk?

This is a matter for CCPs and their regulators.

Q 18. Do you think CCPs should be allowed to calculate the capital requirements for operational risk with an internal model, as in the advanced measurement approach?

We believe that the authorities should encourage CCPs to use internal models as per the AMA. We believe that the AMA is based on risks and involves the entire organisation. The same standards and supervision should be applied to a CCP as is applied to firms. As with the AMA requirements for firms, floors should be placed.

Q 19. Which other approaches should the EBA consider for operational risk measurement?

This is a matter for CCPs and their regulators.

Q 20. What are the incremental costs and benefits to your CCP for the implementation of the advanced measurement approach for operational risk?

This is a matter for CCPs and their regulators.

Q 21. Do you think CCPs should be allowed to calculate the capital requirements for market, credit and counterparty credit risks with internal models?

CCPs should be allowed to use internal models to calculate their capital, subject to the same standards that apply to regulated financial institutions. We do not believe that CCPs should be held to lower standards, but the ability to use internal models is essential for the default fund calculation.

Q 22. How do CCPs currently measure and capitalise for credit, counterparty credit and market risk stemming from non-covered activities?

This is a matter for CCPs and their regulators.

Q 23. Do you think that the banking framework is the most appropriate method of calculating a CCP's capital requirements for credit, counterparty credit and market risk stemming from non-covered activities?

Yes, we do.

Q 24. What are the incremental costs or benefits to your CCP of this proposal assuming that for credit risk stemming from non-covered activities is computed with the approach required in Article 8?

This is a matter for CCPs and their regulators.

Q 25. What are the incremental costs or benefits to your CCP of this proposal assuming that for counterparty credit risk stemming from non-covered activities is computed with the approach required in Article 8?

This is a matter for CCPs and their regulators.

Q 26. What are the incremental costs or benefits to your CCP of this proposal assuming that for market risk stemming from non-covered activities is computed with the approach required in Article 8?

This is a matter for CCPs and their regulators.

Q 27. Do you think that CCPs should be allowed to calculate their capital requirements for credit, counterparty credit and market risk using internal models?

Yes, we do.

Q 28. In your view, which other approaches should the EBA consider for credit, counterparty credit and market risk measurement?

We do not believe that there are others.

Q 29. What other risks should be considered in Article 9?

The EBA has covered all of the risks.

Annex 2

The British Bankers' Association ("BBA") is the leading trade association for the UK banking and financial services sector. We represent over 230 banking members, which are headquartered in 60 countries and have operations in 180 countries worldwide. These member banks collectively provide the full range of banking and financial services, and make up the world's largest international banking centre.