BVI

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BVI's position on the Consultative Document of the Basel Committee on Banking Supervision: Revision to the Standardised Approach for credit risk

BVI[1] gladly takes the opportunity to present its views on the proposals of the Basel Committee on Banking Supervision regarding the revision of the Standardised Approach for credit risk. We welcome the various goals pursued by the revision. We would like, however, to share with the Committee some observations and concerns with regard to the proposed measures.

Section (2.10) – Other assets

The reference point of the wording in brackets "(… and equity investments in funds)" is ambiguous. The phrase could either relate to "other exposures" (meaning that equity investments in funds are deemed other assets which are subject to a standard risk weight of 100%), or it could be an example for an exposure which is subject to a "distinct capital requirement framework" (meaning that this distinct framework shall prevail).

Given that the Committee has issued a policy framework for calculating the capital requirements for banks' equity investments in funds that are held in their banking book only in December 2013 ("the 2013 framework"), we understand the second interpretation is correct. This understanding is also supported by footnote 47 on page 20 of the current consultation paper. Still, we suggest clarifying this in the final Standards.

Section (2.2) – Exposures to corporates, and Annex 1, para. 20:

In Section (2.2), 3rd paragraph, as well as Annex 1, para. 20, reference is made to "funds" in the context of exposures to corporates. At the same time, the consultation paper states that the thresholds proposed "might not be appropriate" for all types of corporates, e.g. funds.

In the German investment fund market, the vast majority of open-ended collective investment schemes are structured as contractual-type funds. They have no legal personality and hence cannot be deemed to be "corporates". The same concept is being used e.g. in Luxembourg (fonds commun de placement, FCP) or Ireland (Common contractual fund, CCF).

As a result, including corporate-style funds in the definition of "corporates" and hence subjecting them to the specific risk-weigh for corporates would lead to an unjustified discrimination between corporate and contractual type funds. In addition, "all types of funds" (i.e. both corporate and contractual type) are already covered by the 2013 framework. Hence, the discrimination would also run counter to the all-

[1] BVI represents the interests of the German investment fund and asset management industry. Its 88 members manage assets in excess of EUR 2.5 trillion in UCITS, AIFs and assets outside investment funds. As such, BVI is committed to promoting a level playing field for all investors. BVI members manage, directly or indirectly, the assets of 50 million private clients over 21 million households. BVI's ID number in the EU Transparency Register is 96816064173-47. For more information, please visit www.bvi.de/en.

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embracing approach of this framework. We therefore suggest deleting the term “funds” in the context of exposure to corporates.

Look-through Approach (LTA) and Mandatory based Approach (MBA)

In Germany, in principle, institutions apply the look-through approach with full transparency regarding the underlying assets of the funds to calculate the capital requirements for credit risk exposures. In order to support institutions which invest in funds in fulfilling their obligations vis-à-vis the competent authority, investment management companies inform the institutions about the portfolio composition of the funds they manage. For preparation of this information investment management companies need information about the proposed alternative measures for risk assessment.

In general, we welcome the proposal to further reduce reliance on external credit ratings. However, we see the risk that under the proposed alternative measures not all relevant risks are under consideration. Credit rating agencies (CRAs) have broad experience in the assessment of credit risks of certain assets. External credit ratings are reliable quantitative and qualitative indicators to assess the probability of default or expected loss of a rated investment. The benefit lies in the independence and neutrality of the CRAs and in the transparency of methodology and process. The external rating can also be an indicator for the liquidity of a security, as e.g. investment grade issues can be purchased by a larger number of market participants. The quality of the outcomes of the calculation of credit risk on the basis of alternative measures may suffer as a result. We therefore propose to clearly define the number of the risk indicators and the criteria which should be relevant for the alternative measures.

In addition, the proposed alternative measures raise questions regarding the data quality and data availability. Most of the data needed are not publicly available. The approach that institutions or investment management companies should conduct their own investigations to analyse data would be very expensive and not appropriate. This applies in particular to the fact that there are no uniform standards for such process (such as accounting standards for non-listed companies for which the IFRS financial statements do not apply). A methodological uniformity and data comparability is therefore not guaranteed.

Moreover, figures of the balance sheet or revenues and earnings are usually volatile, an effect which is not necessarily related to a negative development of the creditworthiness (e.g. during the investment phase of sound enterprises). We therefore propose to review a levelling approach which can minimise such effects in the determination of risk indicators.