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Mr Jaime Caruana
Basel Committee on Banking Supervision
Bank for International Settlements
Central Bahnplatz 2
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Mr Andrew Sheng
Securities and Futures Commission
8th Floor, Chater House
8 Connaught Road Central
Hong Kong

9 December 2004

Dear Messrs. Caruana and Sheng,

RE : TRADING BOOK REVIEW

The European Banking Federation (FBE), the Institute of International Finance (IIF), the International Swaps and Derivatives Association (ISDA), the London Investment Banking Association (LIBA) and The Bond Market Association (TBMA) (together the Associations) share a strong interest in the Trading Book Review, and have actively collaborated with the Joint BCBS/IOSCO Working Group to achieve the much needed revision of the capital treatment of counterparty risk, including short term maturity, and double default risk.

The Associations welcome the commitment made in January 2004 by the Basel Committee to progress these important issues. The process launched by the Basel Committee and IOSCO has been swift, ambitious, and, on issues where industry input has been sought, very transparent and very well received.

It is our hope that the information the Associations have provided to the technical sub-groups established under the umbrella of the Working Group has been of assistance and we are looking forward to continuing our fruitful co-operation with these groups.

It is not our purpose to delve into the substance of the technical requirements in this letter, but to broach one important issue arising from the review process itself.

The Associations view the components of the trading book review as falling into two categories:

- (i) Issues pertaining to the treatment of credit risk in the trading book (and, as relevant, the banking book), including the capital treatment of counterparty credit risk, double default risk, short term credit risk, unsettled transactions and commodity collateral. These topics had been earmarked for further work

during the Basel Accord reform process, even before the Committee made its public acknowledgement earlier this year. Industry and regulators were therefore well prepared to address them when the Trading Book Review started, and have been working together closely for some time toward their resolution.

- (ii) Issues pertaining to the treatment of market risk, including the treatment of less-liquid assets in the trading book and trading book/banking book definitional issues. These points were not discussed in any detail during the Capital Accord reform and are therefore essentially new. Moreover, the industry consultation process on these issues has yet to begin. More importantly still, the questions addressed by the trading book survey and, we assume, by the relevant subgroup, raise complex issues, the appropriate treatment of which may require a substantial review of the Market Risk Amendment to the Accord.

In view of the different stage of thinking and preparedness apparent in relation to the two categories of issues above, the Associations would expect work to be conducted according to different time frames. On the first category, work should proceed relatively swiftly so that the Working Group can meet its target consultation date of March 2005. On the second category, the Associations favour a thorough examination and carefully crafting any solution on the basis of that analysis, rather than a hasty response. A sensible and coherent review of the market risk issues identified by the Working Group will in our opinion necessitate detailed consideration and broad consultation that should not be rushed.

Delaying the adoption of the first set of measures would be detrimental for several reasons. First, it would run contrary to the Committee's objective of ensuring that the Accord keeps pace with market developments and advances in risk management techniques. Second, it would not be consistent with the agreed international implementation timetable, and therefore cause further disruptions for regulators and firms. Third, we believe that the de-coupling of the credit risk issues, which need to be finalised soon, from the conceptually very different market-risk issues, is fully possible without compromising any substantial regulatory concerns during the time necessary to give the market-risk questions a broad, consultative analysis.

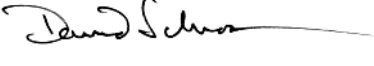
The Associations and the BCBS/IOSCO working group have already put considerable effort and resources into ensuring that the first set of measures can be adopted at the same time as the rest of the Accord. It would be most unfortunate if this objective were not met, for reasons that we do not perceive as well articulated. Therefore we strongly urge that the work on treatment of counterparty risk, double default risk and short term credit risk proceed and that its results be made available without delay, while giving the market-risk issues the full and transparent consideration they need.

Please contact Emmanuelle Septon (esepton@isda.org), Katharine Seal (Katharine.seal@liba.org.uk) or David Schraa (dschraa@iif.com) should you require further information on the above.

Yours sincerely,



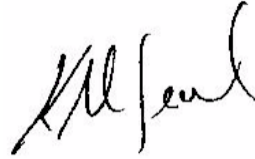
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