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LONDON INVESTMENT BANKING ASSOCIATION

International Swaps and Derivatives Association, Inc.

European Banking Federation

European Securitisation Forum

Director Elemér Tertak
European Commission
Directorate-General Internal Market and Services
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29th April, 2009

Re: "Commission Services Staff Working Document" on proposed amendments to the Capital Requirements Directive

Dear Mr Tertak,

The International Swaps and Derivatives Association (ISDA), the London Investment Banking Association (LIBA), the European Banking Federation (EBF), and the European Securitisation Forum (ESF), an affiliate of the Securities Industry and Financial Markets Association (SIFMA), are pleased to provide industry feedback on the "Commission Services Staff Working Document" on proposed amendments to the Capital Requirements Directive. We have recently completed our comments on the Basel Committee on Banking Supervision's (BCBS) consultative documents "Proposed Revisions to the Market Risk Framework", "Guidelines for Computing Capital for Incremental Risk in the Trading Book" (ISDA IIF LIBA IBFed) and "Proposed Enhancements to the Basel II framework" (ISDA LIBA IBFed ESF) and we welcome this additional opportunity to reflect on this work and provide European policy makers with our comments on the proposals.

We agreed with the Basel Committee in its recent press release (Enhancements to the Basel II Framework, January 16th 2009) that the Basel II capital framework, once implemented, is the appropriate global framework for capturing and assessing risk. It is a significant improvement on Basel I, and, subject to the adjustments to the proposed revisions set out in this letter, we believe it should provide the right incentives for firms to improve not just their risk management procedures, but also their governance and systems and controls infrastructure. Most importantly in the current market turmoil, Basel II promotes a better understanding of firm-wide risks and risk management.

International consistency in minimum regulatory capital rules is essential. Therefore we welcome the fact that the EU Commission is, in general, proposing a package that is consistent with Basel, that it is inviting feedback on these proposals and is keen to understand the impact on EU institutions of the higher capital charges. However we are concerned by the potential significant divergence of approach regarding the capital charges for re-securitisation, which would create major discrepancies between Europe and the US and as such would penalise the financing of the real economy in Europe (further detail in the key messages section below).

The joint associations understand the regulatory desire to increase the regulatory capital requirements in a number of specific areas of the framework as a result of recent events, for example the trading book and the treatment of certain structured finance transactions. Although we welcome the decision to revise the capital framework, and appreciate the targeted approach that is being taken, we do think that there are improvements that could be made. In this letter we reflect on our key messages concerning the Working Document. In the appendices we answer the questions set out in the consultation, highlight one area where we believe that there are differences with the Basel package and include for your reference our formal responses to each of the Basel consultation papers[1]. We consider the issues raised in these letters to be worthy of further consideration before the guidelines are completed, and we urge the Commission and the EU process as a whole to ensure that modifications to the Capital Requirements Directive remain consistent with the global agreements.

Key Messages

Timing and impact assessment

We agree that the international goal of restoring market confidence requires the capital framework to be reviewed. However we would also concur with the Basel Committee's comment that the timing of introduction of higher capital requirements requires careful consideration so that market recovery is not compromised with the risk of the availability of capital and credit to businesses consumers being further restricted. While firms continue to shrink their balance sheets, with de-leverage occurring throughout the world's capital markets, and while firms are pursuing mainly risk averse activities, we see significant risks in rushing through regulation, that could remain in place for many years to come, without fully understanding the likely impact on the financial crises or the impact it could have on any signs of market recovery. We are therefore concerned by the timing of the proposals as neither the Basel level review of the proposals, nor the Basel Quantitative Impact Study (QIS) will have been completed by the comment deadline set by the Commission. The short timeframe for this consultation has meant that Members have not yet been able to complete their analysis of the impact. Therefore we feel it is essential that neither the Basel Committee nor the EU should finalise proposals to amend the capital adequacy framework until there has been a comprehensive quantitative impact study to assess not only the impact on the global economy but also on the EU single market.

Re-securitisation

We acknowledge that certain structured finance transactions such as CDO of ABS, CDO^2 introduced higher leverage through multiple tranching that significantly increased the correlation and default risk and which was not appropriately factored in to the ratings. We therefore concur that it is appropriate to revisit the capital requirements in this area.

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[1] "Proposed Revisions to the Market Risk Framework", "Guidelines for Computing Capital for Incremental Risk in the Trading Book" (ISDA IIF LIBA IBFed) and "Proposed Enhancements to the Basel II framework" (ISDA LIBA IBFed ESF).

However Members are extremely concerned that the combination of a deduction from capital and the scope of transactions that firms believe will be captured by the proposed definition of re-securitisation will have very serious consequences for the EU banking system. Although Members have not been able to complete their impact assessment in time for this submission, their initial estimate of the increase in capital required for EU banks suggests it could be in excess of €150bn. In the current climate Members do not think it would be possible to raise such sums from the market and the deduction is likely to trigger a further round of selling. In addition Members do not believe that such a divergent approach should be taken in Europe to that being proposed globally. Furthermore, we believe that the statement that firms will not be able to meet the due diligence requirements of Article 122a (the rationale provided for full deduction), may not be correct because of the very broad definition of re securitisation proposed. Therefore we do not believe it is appropriate to pre-determine this outcome.

As regards the proposed definition, Members are particularly concerned about the capture of:

- ABCP conduits that are used to finance activities in the broader economy. At the end of 2008, there was $252bn of issuance outstanding by EU firm sponsored conduits. Multi-seller conduits provide funding to a variety of sectors of the market including SMEs, corporates and consumers. It is vital that such funding is not discouraged and we think multi seller conduits should not be captured.
- Re-structuring transactions as part of the efforts to address current market problems. These transactions take the form of either re-structuring a single note (or contiguous notes) from a single transaction, or notes from different transactions in the same sector. These transactions have been extensively discussed with, and agreed by, Regulators. We therefore think that it is vital that such regulatory approved re-structuring transactions are not captured so as not to undermine market re-building activities.

As indicated above, Members are still working through the impact of the proposals but it is becoming clear that there are potentially other transactions that are likely to be captured, which do not have the same risk characteristics as CDO of ABS or CDO^2; for example, CLOs, where it is quite common for the transaction documentation to include provision for a small percentage (typically 5%) of other CLOs, referencing the same asset class, to be held. Therefore in addition to narrowing the scope, in relation to multi seller conduits and regulatory agreed re-structurings, we think that it is important for the definition to include provision for a materiality threshold. We recommend 5-10%. It is also unclear whether the grandfathering provisions, such as those in Article 122a, would apply to the proposed rules for re-securitisation. If this were to be the case, it would alleviate some, although by no means all, of our concern regarding the capital implications of deduction.

Specific risk charge in the Trading Book

We understand the concerns about arbitrage between the banking book and the trading book and the existing incentives for holding credit related instruments in the trading book. Similarly, we can see how this has led to the question in the Commission Services Working Document related to an alternative approach that would involve calculating specific risk capital requirements for all net positions in the trading book as 8% of the relevant banking book risk weight. However, we do not support such proposals as we believe they would result in an inadequate treatment of risks. We believe that the proposals to strengthen the trading book capital regime are generally on the right track, and we do not believe that it would be relevant or useful to pursue the suggested alternatives raised at the end of the consultative paper. Fundamentally, the banking book framework is inappropriate for trading book assets because the framework is only concerned with credit risk and the event of default and as such only addresses one of the material risks to which trading book assets, recorded at fair value, are sensitive. The banking book rules also fail to address the off-setting of long and short positions. The requirement to compute both VaR-based and banking book regulatory capital will also result in significantly greater complexity, overhead and cost to firms' Basel II infrastructure, due to the need to capture the same trades in multiple systems consistently. Furthermore, because these positions would also be included in the general market risk VaR and "stressed" VaR capital charges, under such an alternative approach, they would attract considerably more regulatory capital than similar exposures in the banking book. This creates perverse incentives and encourages banks to hold trading exposures in the banking book. We do not believe the Commission intends to set a higher capital charge for trading assets than for assets with an otherwise similar risk profile held to maturity.

Correlation trading

We understand that in order to be consistent with a policy imposing the standardised measurement method for calculating incremental risks for securitisation positions, certain existing exceptions from the securitisation framework are removed from the Basel II framework (p718(xcv)). We believe this paragraph (replicated in 2006/49/EC, Annex V: Use of internal models to calculate capital requirements, point 5) provides useful language exempting certain exposures from the ratings-based securitisation framework since they result from credit derivative market-making activities based on liquid, transparent markets. Consistent with the proposed changes being considered by the Basel Committee the Commission's Working Document proposes to remove this wording. Without this exemption language, firms with significant market making activity (e.g. those offering portfolio credit protection or those with correlation trading businesses) will experience multiple fold increases in capital requirements not commensurate with the risks measured.

The impact of the proposed revisions for the calculation of the additional regulatory capital requirements with respect to the sole specific risk on the actively managed single tranches referencing single name liquid corporate CDS is expected to render the tranche derivative business uneconomic. A survey of 8 leading correlation dealers has indicated such increase to be at least 25 times the overall regulatory capital required under the current rule for the correlation trading activity. This is in stark contrast with the approach previously adopted by the Commission on the scope of the deduction rule, which had carved out exposures where dealers can "demonstrate to their competent authorities that in addition to trading intent that a liquid two way market exists" . Previously the Basel II framework recognised that rating was not an appropriate risk driver of the correlation tranche business. We would suggest that, where their main risk components are actively hedged on a liquid market, securitisation positions referencing liquid single name corporate CDS that are not re-securitisations should be allowed to receive a modelled market risk charge instead of the banking book charge. The modelled charge will be conservative, as the IRC is predicated upon an increased time horizon for default risk.

For more information on this business and the impact of the proposals please refer to the relevant Annex below.

Securitisations in the trading book

We also believe that carving out all securitisation positions from a trading desk's portfolio will lead to an incoherent picture of the risk, affecting capital charges for the portfolio in an unpredictable way and resulting in capital charges which are not commensurate with the risk. The appropriate response to the division of opinion at a Basel level on the state of modelling risk of securitisations in the trading book, evident in Annex V, paragraph 5a

("Scope"), should lead to incentives to further methodological development, not just blanket exclusion.

The use of the standardised approach for these positions counteracts the recent advancement of valuation techniques and risk modelling for such products. We believe this would be a step backward for more sophisticated firms, and will result in punitive regulatory capital treatment for many assets, which will be an impediment to recovery of the market's ability to finance activities in the broader economy through securitisation, while potentially under-capitalising others, for which the credit rating on its own may not reflect the potential unexpected loss.

Incremental Risk charge (IRC)

While firms embark on developing their IRC models and while these models evolve over time, and while the results of the Basel QIS are still unknown, we urge the Commission to hold off amending the Capital Requirements Directive (CRD) with respect to the IRC until there has been an opportunity for the Basel working group to re visit the framework in light of the results and with a better understanding of the capital impact of the IRC. Early work on the possible impact on regulatory capital requirements of incorporating both default and migration risks showed a disparate range of results, depending on the specific parameters used and the assumptions made in the models. We would hope that any subsequent amendments made to the IRC framework at a Basel level would be adopted in Europe, and this is consistent with our views relating to the importance of an international agreement preceding any further consultations on amendments to the CRD.

Stressed VaR component

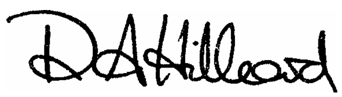
With respect to modifications to the market risk framework, we welcome the introduction of "stressed" VaR in the computation of market risk regulatory capital. However, we believe that over time it would be valuable for firms to have the incentive to demonstrate that their VaR measure has been made sufficiently conservative that it passes a back test over stressed periods, and that a separate "stressed" VaR component could be discontinued. This could be achieved via a more conceptually correct solution that would consider a weighted average of VaR and "stressed" VaR as an effective way of increasing the current market risk charge. Such an approach would avoid the double counting of risks inherent in a two-component VaR charge, while retaining regulatory incentives to ensure a sufficiently robust current VaR model.

Pillar 3

We are strongly supportive of the Commission's aim to improve market confidence by improving disclosure. However we believe that it is important to strike the right balance between more disclosure, the reporting burden on firms and the ability of users to assimilate and interpret the information. The new requirements represent a significant increase in the disclosure that will be required and we are not convinced that, in all areas, the proposals will achieve the desired objectives. In addition we would strongly urge the Commission to implement the new requirements to a timetable that is in line with the introduction of the new market risk requirements discussed above.

We are keen to continue to participate in an on-going dialogue between the EU Commission and the industry before these proposed amendments to the CRD are introduced. We would be happy to discuss any of these comments further and or hear your views on our response, and to arrange this please contact either Ed Duncan at ISDA, Katharine Seal or Diane Hilleard at LIBA, or Wilfried Wilms at the EBF.

Yours sincerely,



Diane Hilleard

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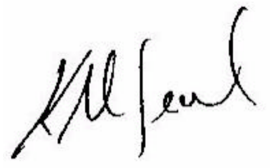

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Appendix 1:

EU "Commission Services Working Document" Questions:

1. In the proposals all capital requirements for specific risk for securitisation positions in the trading book would be based on the capital requirements on the banking book. As an alternative to singling out just securitisation positions, and in line with the Basel consultation, the EU Commission is seeking views on whether the calculation for specific risk should be based on all net positions in the trading book as 8% of the relevant banking book risk weight?

<u>Alternative approach</u>

We understand the concerns about arbitrage between the banking book and the trading book and the existing incentives for holding credit related instruments in the trading book. We can see how this has led to the Basel Committee and the Working Document to propose an alternative approach that removes the availability of trading book capital charges from certain exposure types. However, the banking book framework is inappropriate for trading book assets because the framework is only concerned with credit risk and the event of default and as such only addresses one of the material risks to which trading book assets, recorded at fair value, are sensitive. The banking book rules also fail to address the off-setting of long and short positions. Furthermore, because these positions would also be included in the general market risk VaR and "stressed" VaR capital charges, under such an alternative approach, they would attract considerably more regulatory capital than similar exposures in the banking book. This creates perverse incentives and encourages banks to hold trading book exposures in the banking book. We do not believe the Basel Committee intends to set a higher capital charge for trading assets than for assets with an otherwise similar risk profile held to maturity.

<u>Correlation trading</u>

We understand that in order to be consistent with a policy imposing the standardised measurement method for calculating incremental risks for securitisation positions, certain existing exceptions from the securitisation framework are removed from the Basel II framework (p718(xcv)). We believe this paragraph (replicated in 2006/49/EC, Annex V: Use of internal models to calculate capital requirements, point 5) provides useful language exempting certain exposures from the ratings-based securitisation framework since they result from credit derivative market-making activities based on liquid, transparent markets.

Correlation trading books combine trading in liquid CDS Index tranches and bespoke tranches with hedging in corporate CDS Indices and liquid single name corporate CDS. Both tranche products are OTC products with an active inter-dealer market. Both have prices dealt through broker screens and Bloomberg runs. The standardised corporate CDS Index tranches, in particular, are very liquid. Bespoke tranches reference portfolios of single name corporate CDS that are variations of the corporate CDS Index portfolios. There are also standard bespoke tranches which trade in the inter dealer market (for example bespoke TOTEM / inter-dealer standards such as Standard 1). Bespoke tranches trades are typically traded with institutional clients. Corporate CDS index tranches are traded with funds (including regulated funds) as well as with bank trading desks.

Correlation desks typically defease the core credit risk inherent in their activity with corporate CDS index tranches, corporate CDS Indices and single name corporate CDS. The desks remain exposed to a certain level of basis risk, for example between bespoke and index tranches. At sophisticated firms, these risks are measured through VaR, which typically includes base correlation VaR and specific risk VaR. Basis risk is monitored against limits, applied to both VaR measures and single name default exposures. Correlation trading enables firms to tailor their exposure to certain portfolios of liquid corporate exposure, to perform important market-making in those, and related, products while, at the same time, hedging the risk on a liquid market. Such transactions help banks to actively manage the concentration and counterparty risk of their loan books to large global corporates. This hedging reduces risk born by banks, frees up economic capital and enables banks to engage in further lending. The distribution of tranche risk across credit investors and associated hedging activity also contributes materially to liquidity in the credit market.

The demise of correlation trading activity would materially impact banks' capacity to hedge the concentration and corporate portfolio risks arising from their loan books and significantly inhibit new corporate lending. Overall liquidity of the CDS market is also expected to be severely affected as correlation credit hedging accounts for a large part of the corporate single name CDS and corporate CDS index trading volumes.

The impact of the proposed changes on credit correlation trading businesses cannot be overstated. We are extremely concerned that this business line, which provides liquidity, disperses risk and plays a key secondary role in banks' ability to provide credit, would be unreasonably penalised, leading to many institutions abandoning the business permanently.

In para 718 (xcv), the BCBS recognised that rating was not an appropriate risk driver of the correlation tranche business. Some firms currently make use of this carve out for calculating the capital requirement of correlation transactions forming part of their derivative business, including, in particular, trading activity relating to standard and bespoke tranches based on market standard CDS indices (such as iTraxx and CDX). We suggest that, where their main risk components are actively hedged on a liquid market, securitisation positions referencing liquid single name corporate CDS that are not re-securitisations should be allowed to receive a modelled market risk charge instead of the banking book charge. The modelled charge will be conservative, as the IRC is predicated upon an increased time horizon for default risk. We also note that the use of the Supervisory Formula Approach for the numerous unrated tranches traded in the correlation business (para 712(v)) would be unduly burdensome (application of the IRB Approach to any underlying asset of the tranches) and would bring no added quality to the risk assessment of those tranches.

Importantly, regulators will retain the ability to derecognise a model that fails to meet the stringent quantitative and qualitative requirements defined in the Accord, and to impose the standard risk weights instead. Our proposal is not to allow modelling in every case; we would expect eligible firms to have developed sophisticated modelling tools, and, in particular, to be able to model name-specific risk and convexity.

Firms should, as a matter of principle, have the ability to reflect in their regulatory capital computation the liquidity of corporate CDS index tranches and bespoke corporate CDS tranches, and the significant amount of hedging that is accomplished in correlation trading via liquid and transparent single name corporate CDS and corporate CDS Indices. Not doing so will divorce the tranches from their hedges, and introduce a strong disconnect between the regulatory capital and the economic capital treatment of the instruments.

2. Stakeholders are invited to discuss and provide any available evidence about the impact of the suggested changes a) on their capital requirements given the present structure of their trading books and b) on the future structure of their trading book business.

The EU Commission considers the main feature of the higher capital charges for securitisations to be the new charges for re-securitisation exposures (such as CDOs of ABS or CDO², however, in the context of the EU's stringent due diligence requirements on investors (Oct 2008) the complexity of these instruments suggests that it will be impossible for institutions to meet these requirements and therefore re securitisation exposures should rather than be risk-weighted be completely deducted from capital.

3. Stakeholders views are sought if all re-securitisation positions should be deducted from capital or if it is possible to set a rule identifying those where due diligence is possible and risk weights in line with those of the Basel consultation paper could be applied.

Members do not believe that it is appropriate to deduct all re-securitisation positions. They are extremely concerned by the implications of requiring a deduction from capital in combination with the perceived scope of the proposals. Members are currently working through the impact calculations but due to the short timetable for this consultation we are unfortunately unable to provide their results in time for this submission. However, the initial indications are that a deduction from capital, if applied to existing transactions, could add between €190 and €380 bn of capital requirements to EU firms. As you will appreciate Members regard such an outcome as punitive and likely to damage the prospects of recovery for the EU banking system as it would be extremely difficult to raise that level of capital from private sources. Deduction from capital is also likely to result in further distressed selling into an already fragile market, thereby triggering further losses and increasing the pressure on firms' capital.

Members also fail to understand how the proposed deduction from capital is consistent with pursuing a globally agreed solution to the current problems. The G20 leaders have emphasised the need for international agreement on regulatory solutions, and as a Member of the Financial Stability Board, we assume that the Commission shares this goal. Obviously where there are EU specificities that require alternatives to be considered the Commission should take them into account. However, we are unable to identify any particular issues that suggest that a different approach needs to be taken in this instance. However, it is certain that introducing deduction, in the absence of global agreement, will put EU firms at a serious disadvantage to their peers.

Furthermore the argument used to support the introduction of deduction pre-judges the outcome of supervisors' review of firms' implementation of the stringent due diligence requirements that form part of Article 122a of the CRD amendments currently being finalised; and it significantly increases the more proportionate penalty that we believe is being discussed. We think that the due diligence provisions are already appropriate since they already require firms to monitor information on underlying securitisations within a re-securitisation and provide for an appropriate penalty to be put in place. The scope of the proposed definition of re-securitisation means that we do not think that the rationale for imposing deduction is necessarily correct. Finally, by applying deduction to these positions, the proposal provides no incentive for firms to improve their risk management of these positions.

Even under the proposed risk weights put forward by the Basel Committee, firms have concerns about the capital implications. As you will no doubt be aware rating agencies have been strengthening their approaches to re-securitisations and introducing more conservative assumptions and models. There is therefore likely to be a dual impact of downgrades on existing transactions, more conservative ratings on new transactions going forward, which will in itself increase capital, and the impact of the proposals.

As regards the definition, Members believe that the proposal, based as it is on the existence of a single securitisation exposure in the pool, will cover a range of transactions that we do not believe should be captured. In particular we are concerned about:

- ABCP conduits that are used to finance activities in the real economy
- Certain re-structuring transactions that have been agreed with regulators as part of the effort to address current problems

Multi- seller conduits are a significant source of funding for receivables in the real economy. At the end of December 2008 there was $252.2bn of issuance by EU firm sponsored ABCP conduits was outstanding. Traditional multi seller conduits provide funding at a reasonable cost to a range of businesses including SME and larger corporate receivables, SME commercial loans, car loans and equipment leases. Given the desire of politicians and policy makers to find ways of increasing lending to companies and consumers, it is vital that such financing is not discouraged. In our letter to the Basel Committee on CP150 'Enhancing the Basel II framework', we provide suggested criteria for scoping out these transactions, which we would urge the Commission to consider.

As a result of recent market events firms are in the process of re-structuring certain transactions. This may be achieved by repackaging a single (or contiguous), note(s) from a single transaction, or by repackaging notes from several transactions within the same sector. In both cases the transactions have been discussed extensively with, and approved by, the regulators. It is essential that efforts made to address the current market problems are not undermined. The economic arguments for scoping these transactions out in the case of single structures are that the substance remains the same, i.e. it is as though the transaction had been unwound and re-tranched because no additional correlation or multiple leveraging is introduced.

As members are working through the implications of the definition of re-securitisation it is becoming clear that there are potentially other transactions captured within this definition, which do not have the same risk characteristics as CDO of ABS, CDO^2 etc. For example, it is not uncommon for CLOs to include provision in their documentation for the pool to hold a small (typically 5%) holding in other transactions (referencing the same sector), and the legal requirements for securitisation in some jurisdictions require a multiple vehicle structures, which could potentially bring such transactions within the re-securitisation definition. Although we recognise that it would be possible to structure some of these transactions differently going forward, we think that a more proportionate and risk based approach to the definition of re-securitisation would be to introduce a materiality threshold of between 5 and 10%, i.e. transactions containing securitisation positions with a nominal value of less than 5 top 10% of the nominal value of the pool would be deemed to be 'normal' securitisations'. At this level, the scope for introducing increased leverage and correlation is very limited and therefore prudential concerns are addressed.

Finally, it is not clear whether there are any grandfathering provisions associated with the proposed treatment of re-securitisation, such as those in Article 122a. In light of the potential capital implications of deduction, we think that grandfathering should be given serious consideration. However, although this would reduce some of our concern, it would not eliminate it and the points highlighted above are still relevant.

4. Stakeholders are furthermore invited to discuss and provide any available evidence about the impact of the potential changes on their capital requirements given their present investment in re-securitisations. In addition, stakeholders are invited to discuss their intentions to invest in re-securitisation products in the future.

See above

Also in the area of risk management and disclosure standards for securitisation positions, the Commission's proposal of October 1, 2008 already entailed important enhancements regarding how institutions should manage the risks of securitisation positions. Consequently, the Commission services would envisage no additional requirements on risk management to be added to European legislation at this stage.

5. Stakeholders views are in particular sought if additional elements from the Basel document should be included in the directive text. By contrast, the new requirements on disclosures that the Basel Committee is consulting on have also been included in the present working paper. In particular views from the users of these disclosures are sought as to the usefulness of these additional requirements.

As regards risk management standards, we concur with the Commission's view that there are no additional elements that need to be included in the CRD, since the existing amendment package already reflects the Basel Consultation.

In relation to Pillar 3, we are strongly supportive of the Commission's aim to improve market confidence by improving disclosure and recognise the need to provide appropriate information on the trading book as well as revisiting the quantitative disclosures for the banking book and the qualitative requirements. However we believe that it is important to strike the right balance between more disclosure, the reporting burden on firms and the ability of users to assimilate and interpret the information.

In some areas we believe that the proposals will not achieve the desired objective. The requirements now represent a mixture of accounting, risk and regulatory information. It is important for users to understand the basis on which the disclosures are prepared and that the regulations could help by more clearly signposting the basis for preparation. While we acknowledge the need for improved disclosure in relation to the trading book, many of the requirements are a straight copy of the equivalent banking book provision. However, because of the different approaches employed, this is not always appropriate; for example, the requirements transposed relating to credit risk mitigation. In addition we believe that more could be done to make terminology within the requirements consistent and to explain the purpose of the requirements to ensure that firms have a clearer understanding of what is required. For example, 'financial guarantors' is not a term used within the CRD.

In addition we believe that pipeline and warehousing risks relate to liquidity risk and would more appropriately be tackled in relation to firms' disclosure of their liquidity management. We recommend that the requirement to disclose assets to be securitised should be re-considered in this light. If such an approach is not considered appropriate, then consensus will need to be reached on the point at which such assets would be deemed to fall into this category

We would also like to highlight the finding of our implementation discussions on the existing requirements in relation to the requirement to provide information on transactions where no risk is retained. In this situation firms have not retained on their systems the information required to deliver the disclosures. Although we recognise that the retention requirements that are due to come into force will render this problem irrelevant, we think that it is necessary to provide firms with a derogation for existing transactions done on this basis.

The consultation paper is unclear as to the timing of introduction of the requirements. However, we would re-iterate our comment to the Basel Committee that the new requirements should be implemented concurrently with the introduction of the revised trading book rules.

Appendix 2 - Specific Commentary on Commission Working Document

We believe there are a number of inconsistencies between the proposals to revise Directive 2006/49/EC and the Basel proposals to amend the market risk framework (BCBS 148).

(a) Treatment of specific risk for securitisation positions

We have noted potential differences between the drafting of Annex I 16a and the corresponding paragraphs 712 (iii) to (v) of the Basel paper.

According to our reading of the Commission Working Document, paragraph16a. currently means:

a) A firm without an approved VaR model will apply the standardised banking book risk weights to securitisation positions in the trading book
b) A firm:
  (i) with an approved VaR model and which uses the standardised approach to credit risk in the banking book will apply the standardised banking book risk weights to trading book securitisation positions.
  (ii) with an approved VaR model and which uses the IRB approach to credit risk will apply either the standardised or the IRB banking book risk weights to trading book securitisation positions.

The corresponding Basel text (Paras 712 (iii) (iv) and (v) of BCBS consultation 148) do not offer the option of choosing between standardised and IRB risk weights where the firm is using VaR/IRB.

Additionally, 16a (b)(ii) appears to impose restrictions on the use of the Supervisory Formula Method where the firm is not the originator. In assessing the corresponding Basel text it is not clear why these restrictions have been incorporated and we recommend the deletion of that portion of text.

The treatment of unrated securitisation positions is also not clear. This is at least in part due to ambiguity in the Basel proposals. Basel permits firms to use the Supervisory Formula Approach to calculate the charge for unrated securitisation positions even if they firm does not have an IRB approval (712(v)). However this treatment conflicts with 712(iii) which simply states that firms using the standardised approach must simply deduct these positions from capital. When the Basel ambiguity is resolved the Commission text needs to be amended accordingly.

We would also note that the drafting in paragraph 16a of Annex I on the specific risk charge is not straightforward and could be improved. Member firms have been very confused by the language proposed, and we would be happy to suggest drafting improvements that could better express the intent.

Appendix 3: Joint Association response to the Basel Committee on Banking Supervision's (BCBS) consultative documents "Proposed Revisions to the Market Risk Framework", "Guidelines for Computing Capital for Incremental Risk in the Trading Book" (ISDA IIF LIBA IBFed)

See attached document

Appendix 4: Joint Association response to the BCBS "Proposed Enhancements to the Basel II framework" (ISDA LIBA IBFed ESF)

See attached document