Association for Financial Markets in Europe

St Michael's House
1 George Yard
London EC3V 9DH
Telephone: 44 (0)20 7743 9300
Email: info@afme.eu
Website: www.afme.eu

The voice of banking & financial services

British Bankers' Association
Pinners Hall 105-108 Old Broad Street London
EC2N1EX
T +44(0)20 7216 8800
F +44(0)20 7216 8811
Email info@bba.org.uk
Web www.bba.org.uk

ISDA®

International Swaps and Derivatives Association, Inc.

One Bishops Square
London, E1 6AD
Telephone: 44 (0)20 3088 3550
Facsimile: 44 (0)20 3088 3555
website: www.isda.org

Piers Haben
Pillar 2 & Stress Testing Policy
Financial Services Authority
25 The North Colonnade
Canary Wharf
London E14 5HS

Dear Piers,

The British Bankers' Association ('BBA'), the Association for Financial Markets in Europe ('AFME'), and the International Swaps and Derivatives Association ('ISDA') hereinafter referred to as the Joint Associations represent the UK, global, and european firms that constitute the financial services industry wiithin the UK. We are pleased to respond to the FSA's Consultation Paper CP09/30 on Capital Planning Buffers (CPB).

We have a number of key concerns that we urge the FSA to address the prior to implementation of the proposals set out in CP09/30, which are summarised below. Annex 1, attached, responds to the specific questions raised by the FSA. In Annex 2 we provide specific amendments to the BIPRU text.

The Joint Asssociations look forward to the FSA's response and to working with you as we seek to progress and conclude the approach to CPBs.

Key issues to be addressed prior to implementation of the proposals in 09/30

We understand the FSA's motivation in seeking to clarify its approach to CPBs, but we are concerned that the proposed changes will materially alter the way in which CPBs are assessed in the future. In fact, we are concerned that the FSA is seeking to hard code a practice in BIPRU text that has previously evolved as part of the ICG process and because that process is confidential between the FSA and the firm, it has not been widely visible to the industry, or formally discussed with industry.

The key issues the industry seeks the FSA's feedback on prior to the implementation of CP09/30 are:

International and EU Alignment: We believe that it is essential for a level playing field to exist internationally in the adoption of capital standards. The UK financial services sector should not be disadvantaged compared to international peers by the early adoption/enhancement of any one 'principle' when there is a whole range of mechanisms being considered internationally that would achieve a similar end. Therefore, to avoid super equivalence in the UK, we urge the FSA review its approach to CPBs and conduct a further consultation once current international discussions on capital, initiated by the BCBS's publication of 'Strengthening the Resilience in the Banking Sector', and supported by CRD4, are concluded.

The industry views further consultation as essential given that the discussions upon how CPBs will operate internationally, as outlined in section 6, are in the very early stages of review, and that once concluded, there will be overlap with the existing UK Pillar 1 and Pillar 2 CPB process. Review and consultation will therefore be needed with the industry to i) evaluate how the separate practices overlap and complement each other; ii) determine how they will operate for firms in practice and iii) ensure no double counting occurs. This calibration, and re-alignment will be extremely important if the UK is to remain a competitive financial services environment. We look forward to the FSA's response in this regard, and confirmation that further consultation will occur.

The manner in which the FSA envisages the ability to adjust levels of capital buffers also needs further discussion with the industry in terms of both the 'trigger points' the FSA will be taking into account, and how such a process would operate.

Enhanced Stress Testing should not lead to increase in capital minima: We note that the FSA has prepared CP09/30 to respond to questions raised on its Stress Testing (CP08/24) consultation. A key concern for members, arising out of the consultation on CP08/24, was that the enhanced Stress Test process would lead to an increase in a firm's minimum capital requirement as set by the FSA. In other words, the inevitable result of enhanced stress testing is a capital add-on. At that time the FSA confirmed that there was no automatic link and we are pleased to understand that this remains the FSA's position.

Firms which maintain a strong capital base that already encompasses a buffer suitable to meet the stress situations envisaged should not be faced with an additional capital buffer requirement as a result of the stress testing or reverse stress testing scenarios. This would be wrong. The FSA should place emphasis on identifying weaknesses/ vulnerabilities in banks' business models through stress testing and scenario analysis, rather than focusing on quantifying a capital planning buffer which is a rather blunt instrument.

We would further emphasise that, as commented within CP08/24 and our recent response to CEBS guidelines CP32, stress testing is not purely a 'mechanical' exercise but one that must be grounded in the strategy, business activity and risk profile of the individual firm. It must take account of existing bench-strength of the institution and quality of its corporate governance framework, as well as strength of management actions. Stress testing is therefore as much, if not more so, a qualitative exercise than a quantitative process. Any conclusions and recommendations drawn by the FSA from the review of the stress tests and analyses should be shared with a firm in a clear, and transparent manner.

The industry appreciates the work the FSA has undertaken as regards an anchor stress test scenario which facilitates a transparent and robust industry framework. Equally we reaffirm our agreement with the FSA that this is purely to be a guide, and will need to be suitably altered to fit the specifics of the individual firm. It has been noted that the current anchor is very 'retail' oriented with a strong focus on operations in the UK. As a consequence, it does not apply equally to firms operating in different sectors or markets and these firms need to alter it and/or enhance it to be more reflective of the environments they are operating in. It also needs to be given a more international dimension if it is to be useful to firms that are active globally. Overarching this of course is the need to ensure all firms have the ability to devise their own stress test scenarios, relevant to their business.

There should be no double counting, or capital add on, or 'buffer on top of a buffer'

The industry understands that CPB will be at the group rather than solo level, which we fully support.

The FSA has further assured the industry that there is no intention to double count. The industry understands this to mean that: by breaking the link between the CPB and the FSA's financial adequacy rule, and distinguishing between adequate financial resources (which are explicitly linked to ICG) and a CPB (which is a buffer that is not part of the regulatory minimum), the FSA is not creating a capital add on, or 'buffer on top of a buffer'. The industry understands that any firm currently carrying a buffer within the ICG process will not have a further buffer imposed on top of this; rather the ICG will be reset without a buffer and a separate recommendation made to the firm as to the CPB.

We welcome the FSA's willingness to re-issue to individual firms the relevant ICG notification letters to cover the ICG at the lower level, excluding any buffer. We understand that separate advice will then be provided to the firm on the recommended CPB which the industry believes should be provided as part of the ongoing supervisory process under Pillar 2.

The FSA has noted that the intention is not to expect a firm to carry its own internal buffer over and above its CPB. Any internal buffer held by the firm will count towards its CPB.

The industry supports these intentions which it views as imperative and seeks the FSA's confirmation of these points.

CPB should form part of Pillar 2 process, be confidential and not require disclosure

The FSA has confirmed that the buffer will remain as part of the Pillar 2 process and only be discussed between the firm and FSA. It will not be subject to public disclosure. The industry welcomes this assurance from the FSA. It is critical that a firm's CPB remain a private matter between the firm and the FSA to avoid the serious and potentially significant impact of any market or public knowledge, which could have serious and significant impacts on our members.

The CPB process outlined in CP09/30 has potentially critical implications for the disclosure obligations that it could trigger for firms, with the ensuing serious risk of reputational damage to the firm. We understand that the FSA has given this serious consideration (taking legal advice on the matter) and is now satisfied that using the CPB does not trigger disclosure obligations. Given the importance of this legal advice, it is essential that it is shared with firms to alleviate the concerns of the Boards and executive management. In addition, the policy statement should be altered to include comment by the FSA that in its opinion public disclosure will not be required

To further ensure that the intent of the CPB is fully understood by all parties, any reference to a 'breach' of the buffer should be removed from the policy statement. It should be very clear that use of the buffer is acceptable, and will not automatically lead to enhanced supervision.

In addition, it will be important that any reporting developed as part of the CPB process remains confidential between the firm and the FSA. This being so we recommend this report not be in any formal template but rather be part of the ongoing dialogue between the individual firm and its supervisory team within the FSA. This will reinforce the intent of the CPB as a recommended, rather than hard target, and help to avoid disclosure issues. We welcome the FSA's feedback upon this.

Eligible securities and proven loss absorbing instruments should continue to be eligible for planning buffer purposes.

The CPB should be met by Total capital, and existing instruments should continue to be recognised as appropriate for buffer purposes. The industry cautions the FSA against being over prescriptive on the instruments buffers are held in, and for the FSA to recognise that 'shifting' capital instruments is not a straightforward task.

Setting the buffer and using the buffer

In terms of the mechanism utilised to recommend a CPB level, the industry suggests that this be part of the ongoing dialogue under the Pillar 2 process between the individual firm and its supervisory team within the FSA. This will reinforce the intent of the CPB as a recommended, rather than hard target, and the implementation of the CPB as outlined in CP09/30 not leading to automatic double counting, or capital add on, or disclosure issues.

The FSA must provide clarity on the consequences to a firm in using the buffer. The industry is uncertain of the intention of the FSA's commentary that in using the CPB should be regarded as a 'trigger point for heightened supervisory interaction': It would be helpful to the industry for the FSA to clarify the intent of this comment as well as provide an overview of how the FSA envisage this operating in practice. The comment seems at odds with the policy statement that the CPB is to be available to absorb losses and increased capital requirements in adverse external circumstances and that it can be drawn down in these circumstances.

Due recognition should be given to recovery and resolution plans; management actions; and existing bench-strength when calculating the CPB

When deciding on the buffer, it is critical that the FSA take account of the robustness of the firm's recovery and resolution plans; and risk management disciplines including management prudence. These qualitative measurements should all contribute towards the CPB, and mitigate the resultant quantitative buffer sum.

Effective risk management and corporate governance

Whilst the industry recognises the importance of maintaining adequate capital resources the implementation of the buffer process as outlined in CP09/30 must be risk based; it must allow for qualitative review; it must not lead to 'capital add on', and it must take into account the existing strength of the institution's balance sheet, as well as its business and governance models.

The buffer cannot become a ‘defacto’ tool that acts as a replacement for ineffective risk management, corporate governance or indeed supervisory management. Capital is not the only, and rarely the best, answer for tackling the underlying issues of poor management practice. CPBs must not lead to penalising robust and soundly-managed institutions. Supervisors must exert sound judgment in assessing any buffer, including suitably taking into account the underlying strength of the firm’s business and risk management culture.

The industry stresses that firms operating robust capital planning processes, and procedures, with strong corporate governance and risk management infrastructures, which already maintain buffers above expected minima, should not be in any way disadvantaged by the implementation of CP09/30.

We also suggest that it is unnecessary for the FSA to set a CPB for firms that already have a substantial own buffer and are seen to be well run with adequate systems and controls. For such firms it would be sufficient simply to require the firm to notify the FSA if its Pillar 2 stress testing indicates that its own buffer would be fully utilised in the severe scenario to maintain minimum capital requirements. This approach would serve as an effective trigger mechanism without the difficulties involved in setting a precise quantity for the CPB.

In summary, the industry, urges the FSA prior to implementation of the initiatives outlined in CP09/30 to provide its response to the issues raised here, and to address the specific items identified in the attached response to the questions posed and comments upon the BIPRU text.

We look forward to hearing from you in this regard, and will be happy to meet with you further to progress these matters. In the meantime please do not hesitate to contact the undersigned with any questions.

Yours sincerely

Irene Graham
Director
BBA

Anita Millar
Managing Director
AFME

Antonio Corbi
Assistant Director
ISDA

31 March 2010

Sent Via e-mail to:CP09_30@fsa.gov.uk

Annex 1. RESPONSE TO SPECIFIC QUESTIONS

Q1. Do you agree with our market failure analysis and our summary cost benefit analysis?

Whilst fully agreeing with the need for robust, pragmatic and practical stress testing as part of a firm's prudential risk management, which should be fully embedded in the Pillar 2 process, we are concerned about how the CPB will be expressed. It should not become a specific, targeted quantitative minimum requirement that will sit 'in addition to/ on top of' the ICG or any other existing buffer.

There are a series of issues that the industry requires response/confirmation from the FSA upon if it is to be in a position to provide a view of the cost benefit analysis. At the moment the industry is concerned that this initiative, coupled with the ongoing international and European review of Capital Conservation buffers (CCB), and enhanced stress testing process, could lead to a situation of placing 'buffers on top of buffers' which will in turn lead to double counting. This will not only have considerable cost implications for banks but a negative effect on the real economy if capital is ' tied up' without being able to be utilised to provide the lending services needed by the underlying corporate and personal client base. The industry does not believe this to be an acceptable outcome.

Whilst we now understand that the intent of the FSA is to ensure the CPB remains a recommended rather than 'hard target' and that it is not intended to be an 'add on' to existing buffers that may exist within an existing ICG. This being so, to alleviate the strong industry concerns, we recommend that prior to implementation the FSA formally confirms the following to the industry:

1. The CPB will apply at consolidated level only.

2. The CPB process will remain as part of the Pillar 2 process and as such remain confidential between the firm and the FSA. It will also be a recommended target between the FSA and the firm as part of the ongoing Pillar 2 dialogue.

3. The CPB will not sit on top of the ICG; nor will there be the requirement for a firm to establish a separate internal buffer above the CPB. If a firm does already have a buffer within ICG and an internal buffer above that, then these will count towards the CPB level. The CPB will not be in addition to these.

4. Any buffer currently sitting within the ICG will therefore be removed by the FSA; and the ICG will be reissued at the lower level without a recommended buffer being included.

5. As indicated in 1 above, the buffer will not be a 'hard' target but rather it will be a 'soft' recommended target, which will form part of the ongoing dialogue between firms and their supervisors in relation to the firm's specific business activity. It will remain a recommended buffer to support the underlying activities of the firm, based on: i) appropriate risk assessment; ii) qualitative understanding of the business model and iii) qualitative understanding of the firm's overall corporate governance and risk management culture. Items i) to iii) will be taken into account when determining the buffer.

6. Eligible securities and proven loss absorbing instruments will remain instruments acceptable as capital buffers.

7. Due recognition will be given by the FSA to recovery and resolution plans; management actions; and existing corporate governance/ risk management bench strength when calculating the CPB i.e. these factors will 'count' and mitigate the quantitative sum defined as the buffer.

8. The FSA will confirm that there will be no adverse consequences to a firm that uses the buffer in adverse external circumstances, and will clarify what circumstances would lead to a consequence of a firm being under heightened supervision.

9. Using the buffer will not lead to disclosure requirements.

10. Further consultation will take place in the UK once the international recommendations on capital buffers (arising from the BCBS 164 and CRD4 consultation processes) have concluded. Review and consultation will be needed to determine how these buffers will operate, and to ensure there is no super equivalence, or overlap/ double counting.

The industry considers these assurances are necessary to clarify the current ambiguity arising because of the way in which the policy is written. As currently drafted, despite stated intention, CP09/30 has strong potential to introduce new qualities of capital and a new 'hard' target requirement for banks to adhere to, which would be wrong.

It should also be recognised that the calculation of a CPB will be very sensitive to the stress scenario chosen and the way it is applied to generate the stress forecast balance sheet, including management actions. This means that the FSA must ensure that the stress scenario must be relevant to the individual firm's business model, whilst at the same time the FSA would need to ensure a consistency between firms for, in particular, the severity of the scenario.

We look forward to the FSA's intended round table with firms to discuss further the anchor scenarios for stress testing; and how these will interact with, as relevant college of supervisors. We believe a joined up industry and FSA dialogue in this area is necessary and helpful, in order to ensure a transparent, credible, comparable and robust framework evolves. Of course as stated above, there is an overarching need to ensure all firms have the flexibility to devise their own stress test scenarios, relevant to their business.

It is of critical importance to the industry that the process of agreeing the stress test results with the FSA is efficient, particularly as these stress tests are complex and expensive to run involving people from all parts of the business.

Q2. Do you agree that breaking the link between GENPRU 1.2.26 and the capital planning buffer will make it clearer to firms, their boards and their auditors that the CPB is designed to be drawn down during adverse external circumstances?

The CPB process as described with 'drawdown' and 'breach' potential has serious implications in terms of the disclosure obligations that it would trigger, presenting firms with the ensuing serious risk of reputational damage to the institution which could undermine its continuing capability to access the capital markets. We understand the FSA has taken legal advice on these obligations and concluded that the use of the CPB will not trigger disclosure obligations. Although it is reassuring to be notified of this action, the industry believes it is essential that the FSA formally share this advice.

It is imperative that the use of the buffer does not trigger either corporate governance obligations and / or result in action that would alert the investor and/or public domain. Such an outcome could have far reaching consequences.

It is essential that the wording of the CPB policy statement be altered to remove language such as ‘requirement’ /and ‘breach’. This is necessary to further enforce the intent of the buffer and to ensure that there is no misinterpretation of its availability for use; and/ or misinterpretation by others such as investors/ auditors of it being a being a recommended rather than ‘hard’ target.

We would also reiterate that the management of the buffer process should form part of the ongoing dialogue between firms and their respective supervisors, and that is how it should be monitored.

Q3. Do you have any comments on our approach regarding the use, monitoring and rebuilding of capital buffers?

We would repeat the comments made within the cover letter and under questions 1 and 2 above; plus highlight the below:

i) Any CPB approach must be risk based and recognise the individual firm’s existing capital strength, and robustness of corporate governance/ risk management disciplines. This will be absolutely critical if the buffer is to work as intended, and for it not to in any way penalise firms who have a strong risk based culture; who already operate a strong capital planning process with inbuilt buffers, and have demonstrated a proven track record of solid risk management.

ii) Any CPB should be established at the group not solo level.

iii) The FSA must employ a clear and transparent process by which firms are able to fully understand the manner by which the FSA has derived the CPB figure.

In addition, the industry is unclear as to the intention behind the FSA’s commentary that in using the CPB firms’ should regard it as a ‘trigger point for heightened supervisory interaction’: It would be helpful to the industry for the FSA to clarify the intent of this comment as well as provide an overview of how the FSA envisage this operating in practice. The comment seems at odds with the policy statement that the CPB is to be available to absorb losses and increased capital requirements in adverse external circumstances.

Given the FSA’s stated intention that (i) CP09/30 is to provide clarity, simplicity and assurance to firms’ Boards, and auditors (ii) that it is acceptable for the buffer to be ‘utlised’ at given times, and (iii) its use will not trigger public disclosure:- we find the wording in the policy statement to be unhelpful and it should be rephrased. As it stands, it has the potential for significant unintended consequence and implies that disclosure will be inevitable.

We strongly recommend the wording in the policy statement be repositioned to reflect the fact that the CPB will be based on dialogue with the firm, as part of the day to day supervisory management process, and as such if the buffer is utilised’ /’dipped into’ it will be an action that is well understood by the FSA. The industry reiterates the need for the FSA to share the legal advice received as to use of the buffer not being a matter for disclosure to the market.

It is also unclear as to how the process should work when we are at or near the bottom of the economic cycle. The industry would expect the FSA to recognise that buffer levels should and will fluctuate, and should come down in times of an economic downturn or periods of stress as defined in the stress scenarios. The FSA's feedback in this area would be appreciated.

Q4. Do you understand our proposed clarification that we may specify elements of the CPB or ICG that should be held in particular forms of capital?

The formalisation of the FSA's right to specify elements of the CPB or ICG to be held in particular qualities of capital has the characteristics of a new requirement, which, in turn, suggests additional costs for firms.

It is also not at all transparent as to what 'forms of capital' the FSA would specify firms hold as part of the CPB or ICG, and over what time period it should be raised. We caution the FSA over this prescription and the practicalities involved. Shifting capital instruments is not a simple process; nor is necessarily raising capital – certainly not in any short time period or cross industry periods of 'stress'.

Moreover, at a time when international standards are being revised as part of the current Basel consultation process with the accompanying QIS analysis, we think it is essential that the FSA align its requirements with international standards and the CPB process be reviewed again in light of new international standards relating to capital planning buffers and their management. International alignment will be critical if the UK financial services industry and its global firms are to continue to operate on a level playing field. The industry looks forward to a further consultation with the FSA on the CPB process once Basel standards are defined, and international consensus reached as to how capital planning buffers will operate to allow fluctuation of them including movement downwards.

As stated previously, we would emphasise that in the discussion of the CPB due recognition should be given by the FSA to recovery and resolution plans, management actions, and existing corporate governance/ risk management capabilities. These factors should 'count' towards the buffer and be a mitigant to the sum defined. We reiterate that the FSA needs to ensure that CP09/30 does not give rise to: a capital 'add on; to new qualities of capital; or a new 'hard' target for firm's to adhere to. This would be wrong.

The industry will continue to use eligible securities and proven loss absorbing instruments as part of a CPB. We expect these to continue to be acceptable to the FSA.

In conclusion, the industry looks forward to the FSA responding to the comments provided in the questions above and in the covering letter before final implementation of the initiatives outlined in CP09/30. The industry remains very concerned that the FSA is 'front running' the capital planning buffer process prior to international consensus being reached. Whilst this is the case, the industry requires assurance from the FSA that the UK CPB process will be reviewed and recalibrated to align with international standards once these are concluded, which will include further consultation with the industry.

We look forward to hearing from you in this regard and will be happy to meet with you further to progress these matters

ANNEX 2. CP09/30: COMMENTS ON BIPRU TEXT

We underline our earlier comments that it is essential that an international level playing field be promoted in the adoption of capital standards. The UK financial services sector should not be disadvantaged by the early adoption/enhancement of any one 'principle' when there are a whole range of mechanisms being discussed internationally and in the EU that would achieve a similar end.

The industry firmly is of the view that it is too early to change the BIPRU text and to hard code a practice into regulations. First, the proposals for capital buffers contained in the Basel Committee's CP 164 and the EU Commission's proposals on CRD 4) may change the manner in which the CPB process operates in the UK. Second, there are a number of issues, already highlighted, that the FSA needs to address in regard to the implementation of CP09/30. We therefore recommend that any changes to the BIPRU text are delayed until the BCBS CP 164 and CRD 4 consultation processes are completed and the FSA engages with the industry on their outcome.

We very much hope the FSA can support this suggestion. It will guard against multiple changes to BIPRU text occurring in a short time frame.

That said, for your reference, the industry's comments to the current suggested changes to BIPRU are provided below. Our recommended changes to the BIPRU text reflect industry's significant concerns regarding disclosure, confidentiality of process as well as the practical manner in which the FSA would review quality of capital which, as stated above, we do not agree with.

Recommended changes to BIPRU suggested text (Appendix 1 to CP09/30)

Commencement date – as highlighted above should be deferred until the BCBS 164 consultation process is concluded and further review of this with the UK industry has been conducted to ensure the CPB process in the UK aligns with international standards.

Annex A: In the definition of capital planning buffer we recommend deletion of the reference to 'quality of capital' given our prior comments, and would insert the words 'at a consolidated level' and reference to 'existing risk management practices' as follows:

Capital planning buffer (in BIPRU 2.2) the amount ~~and quality~~ of capital resources that a firm should hold at a given time, at a consolidated level, in accordance with the general stress and scenario testing rule, so that the firm is able to continue to meet its ICG the ~~overall financial adequacy rule~~ throughout the relevant capital planning period in the face of a stress scenario, after allowing for realistic management actions and existing risk management processes.

Annex B: Amendments to the Prudential sourcebook for Banks, Building Societies and Investment Firms (BIPRU

We recommend changes as follows to certain of the sourcebook paragraphs.

2.2.11 G As part of its SREP, the FSA will consider whether the amount ~~and quality~~

of capital which a firm should hold to meet its CRR in GENPRU 2.1

(Calculation of capital resources requirements) is sufficient for that firm to comply with the overall financial adequacy

2.2.12 G After completing a review as part of the SREP, the FSA will normally give that firm ~~individual guidance (~~individual capital guidance~~)~~, advising it of the amount ~~and quality~~ of capital which it should hold to meet the overall financial adequacy rule.

2.2.12A G As part of its SREP, the FSA will also consider the amount ~~and quality~~ of capital which the firm should hold as a capital planning buffer in accordance with the results of its stress tests and scenario analyses and its assessment of management actions . The FSA will consider adequate a capital planning buffer which will allow the firm to continue to meet the overall financial adequacy rule throughout the capital planning period in the face of a stress scenario, after allowing for realistic management actions. The ~~firm's~~ capital planning buffer should be available only to absorb future losses or meet higher capital requirements in adverse circumstances~~. if a severe stress scenario materialises.~~

2.2.12B G After completing a review as part of the SREP, the FSA may ~~notify~~ advise the firm of the amount ~~and quality~~ of capital which it should hold as a capital planning buffer over and above the level of capital recommended as its ICG.

2.2.12C G Where the amount ~~or quality~~ of capital which the FSA considers a firm should hold to meet the overall financial adequacy rule ~~or as a capital planning buffer~~ is not the same as that which results from a firm's ICAAP, the FSA usually expects to discuss any such difference with the firm. ~~Where necessary, the FSA may consider the use of its powers under section 166 of the Act (Reports by skilled persons) to assist in such circumstances.~~ (The Industry does not believe this commentary necessary here given the FSA's overall authority and the potential for the commentary here to give rise to disclosure requirements)

2.2.13 G If a firm considers that the individual capital guidance given to it is inappropriate to its circumstances it should, consistent with Principle 11 (Relations with regulators), inform the FSA that it disagrees with that guidance. The FSA may reissue individual capital guidance if, after discussion with the firm, the FSA concludes that the amount ~~or quality~~ of capital that the firm should hold to meet the overall financial adequacy rule is different from the amount ~~or quality~~ initially suggested by the FSA.

2.2.13A G If a firm disagrees with the FSA's assessment as to the amount ~~or quality of the~~ capital planning buffer that it should hold, it should, consistent with Principle 11 (Relations with regulators), notify the FSA of its disagreement. The FSA may reconsider its initial assessment if, after discussion with the firm, the FSA concludes that the amount ~~or quality~~ of capital planning buffer that the firm should hold as capital planning buffer is different from the amount ~~or quality~~ initially suggested.

2.2.15 G If, after discussion, the FSA and a firm still do not agree on an adequate level of capital, the FSA may consider using its powers under section 45 of the Act to vary on its own initiative a firm's Part IV permission so as to require it to hold capital in accordance with the FSA's view of the capital necessary to comply with the overall financial adequacy rule or as a capital planning buffer. SUP 7 provides further information about the FSA's powers under section 45.

The drafting of individual capital guidance and capital planning buffer (unclear as to what the SFA intends here- is there text missing?)…

2.2.19A G Where the FSA ~~notifies~~ advises a firm that it should hold a capital planning buffer,the ~~notification~~ advice will ~~state~~ indicate what amount ~~and quality~~ of capital the FSA considers that is adequate for the firm to hold as such. BIPRU 2.2.17G to BIPRU 2.2.19G apply for the purpose of this paragraph as they apply to individual capital guidance. References in those provisions to individual capital guidance should be read as also applying to capital planning buffer.

Failure to meet individual capital guidance and monitoring and reporting on the capital planning buffer (unclear as to what the SFA intends here- is there text missing?)…

2.2.23. When a firm's analysis demonstrates that its capital resources are likely to fall to the point where its capital planning buffer will be fully utilised ~~eroded~~ - the firm consistent with Principle 11 (Relations with regulators) should notify the FSA of this as

soon as practicable. The firm's notification should at least state:

(1) what circumstances are ~~likely to force~~ causing the firm to draw down its

capital planning buffer;

(2) how the capital planning buffer will be ~~gradually~~ used up in line with

the firm's capital planning projections; and

(3) what plan is in place for the eventual restoration of the capital

planning buffer.

2.2.23A G The FSA will review the firm's notification and may provide its own

analysis and recommendations on the items listed in BIPRU 2.2.23G(1) to

(3). The FSA may ask the firm to continue reporting to it on the use of its capital planning buffer in accordance with the plan referred to in BIPRU ~~and may identify specific trigger porints leading to enhanced supervision~~.

Comment: The industry recommends this deletion given the preceding sentences which implicitly provide this right and thereby avoiding the use of word trigger points and enhanced supervision which gives rise to concerns on disclosure events. In addition to the regular reporting which may be agreed with the FSA, the firm should notify the FSA as soon as practicable if the use of its capital planning buffer has deviated materially from the plan notified to the FSA.

2.2.23B G ~~A firm should inform the FSA where its capital planning buffer is likely to start being eroded even if it has not accepted the FSA's assessment as to the~~

~~amount or quality of its capital planning buffer.~~(Not needed covered in 2.2.23 G)

2.2.23C G BIPRU 2.2.20G to BIPRU 2.2.23BG also apply to individual capital guidance and to capital planning buffer on a consolidated basis as referred to in BIPRU 2.2.19G.

2.2.29 G (1) A firm may take into account factors other than those identified in the

overall Pillar 2 rule when it assesses the level of capital it wishes to hold. These factors might include external rating goals, market reputation and its strategic goals. ~~However, a firm should be able to distinguish, for the purpose of its dialogue with the FSA, between~~

~~capital it holds in order to comply with the overall financial adequacy rule capital that it holds as a capital planning buffer and capital held for other purposes~~

2.2.39 G ~~To reduce the impact of cyclical effects, a firm should aim to maintain an~~

~~adequate capital buffer capital planning buffer during an upturn in business~~

~~and economic cycles such that it has sufficient capital available to protect~~

~~itself in unfavourable market conditions~~.

Comment: The industry strongly believes 2.2.39 G: should be deleted as it suggests a CCB approach which has yet to be decided upon at international levels given the current Basel and EU consultations, and therefore it is a new requirement which has the risk of "double counting" which the FSA has indicated it is seeking to avoid. This clause should therefore be deleted until such time as international consultation concludes and subsequent UK industry consultation takes place.

2.2.72 G A firm should not expect the FSA to accept as adequate any particular model that it develops or automatically to reflect the results from the model in any individual capital guidance or capital planning buffer. However, the FSA will take into account the results of a sound and prudent model when giving individual capital guidance or when dealing with the firm in relation to its capital planning buffer (see GENPRU 1.2.19G (Outline of provisions related to GENPRU 2.1 (Adequacy of financial resource): [Although this is in the existing BIPRU text the industry would appreciate clarification on this commentary]

Associations

The BBA is the leading association for the UK banking and financial services sector, speaking for over 200 banking members from 60 countries on the full range of UK or international banking issues and engaging with 35 associated professional firms. Collectively providing the full range of services, our member banks make up the world's largest international banking centre, operating some 150 million accounts and contributing £50 billion annually to the UK economy.

AFME represents a broad array of European and global participants in the wholesale financial markets, and its 197 members comprise all pan-EU and global banks as well as key regional banks, brokers, law firms, investors and other financial market participants. AFME was formed on 1st November 2009 by the merger of the London Investment Banking Association and the European operations of the Securities Industry and Financial Markets Association.

ISDA represents participants in the privately negotiated derivatives industry, and has over 810 member institutions from 57 countries on six continents. These members include most of the world's major institutions that deal in privately negotiated derivatives, as well as many of the businesses, governmental entities and other end users that rely on over-the-counter derivatives to manage efficiently the financial market risks inherent in their core economic activities.