Secretary General

Via email: acorbi@isda.org

Mr Antonio Corbi
International Swap and Derivatives Association
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17 July 2012

Dear Mr Corbi

Thank you for your letter of 29 June 2012 to both the Chairman of the Basel Committee and the Chairman of the International Accounting Standards Board. I am pleased to take this opportunity to clarify the Basel Committee's positions on the issues you raised.

The decision taken by the Basel Committee to remove the filter on unrealised losses (ie to ensure losses directly reduce Common Equity Tier 1 (CET1)) was based on the experiences of the financial crisis: that the practice of filtering out losses from Tier 1 undermined both the quality of regulatory capital and its credibility. In agreeing to Basel III's revised definition of regulatory capital, the Committee was fully aware of the potential for increased volatility in capital ratios in those jurisdictions that currently apply such a filter. Seeking less volatility through ignoring or reversing losses in capital, however, is simply avoiding acknowledgement of the underlying position. It also undermines the purpose of capital adequacy requirements, which is to measure a bank's capacity to absorb losses. The decision to remove the filter was therefore taken based on this principle; it was not based on any assumption that the scope of instruments that are fair valued would change by the time of implementation.

With respect to the Committee's decision to remove the filter for unrealised gains, the motivation was based on the principle of applying a treatment that is symmetrical with unrealised losses so that regulatory capital presents a more accurate representation of a bank's ability to absorb losses at any given point in time. Failure to recognise unrealised gains could lead to a situation where the same asset could be given a different value at different banks simply because it was purchased at different points in time.

The Committee continuously and closely monitors accounting policy developments, including those pertaining to IFRS 9 and the treatment of expected losses and recognition of provisions. However, the Committee does not at present see a need to reconsider these elements of the Basel framework.

Yours sincerely

Wayne Byres

Copy to:

- Mr Hans Hoogervorst - International Accounting Standard Board
- Ms Leslie Seidman - United States Financial Accounting Standard Board
- Mr Constantinos Trikoupis - Cyprus Presidency
- Ms Sharon Bowles - European Parliament
- Mr Jonathan Faull - European Commission
- Ms Francoise Flores - European Financial Reporting Advisory Group
- Mr Andrea Enria - European Banking Authority

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