September 11, 2015

Mr. William Coen
Secretary General
Basel Committee on Banking Supervision
Centralbahnplatz 2, Basel
CH-4002
SWITZERLAND

Dear Mr. Coen,

Following the publication on June 8, 2015 of the Basel Committee on Banking Supervision's consultative document on interest rate risk in the banking book (IRRBB), intended to ultimately replace the Basel Committee's 2004 *Principles for the management and supervision of interest rate risk*, the undersigned associations would like to draw your attention to some extremely important issues for our members.

The associations advocate for a genuine Pillar 2 approach

According to your current proposals, the methodology for assessing the interest rate risk is deeply strengthened, resulting in a significant increase in capital requirements:

- The standardized Pillar 1 approach is overly prescriptive and not suitable for all business models, for instance:
    - the modelling of retail / transactional non maturity deposits leads to an implied average maturity of just 1.8 years;
    - the maximum maturity of 6 years for core deposits is not adequate, considering the high preference for bank deposits in certain countries and the fact that certain banks use 10 years for their internal measurement systems;
    - the 50% pass-through floor for wholesale non maturity deposits overestimates the fact that wholesale funding is significantly funded by non-interest bearing deposits; and
    - equity is excluded from the calculation to analyse the exposure to interest rate risk.
- The so-called "enhanced Pillar 2" approach is based on an internal measurement system (IMS), but with the requirements such as disclosures based on a standardised model, it would become a de facto reference threshold and can be seen as a disguised Pillar 1.

As you may recall (*cf. joint letter to BCBS dated July 4 2014, attached*), we strongly advocate a Pillar 2 treatment, as contemplated in our countries, based on an outlier test to highlight institutions potentially exposed to elevated IRRBB and where it is the responsibility of the competent authority to decide whether or not an outlier institution should be subject to corrective measures. Moreover in the light of their individual business model, banks should be allowed to choose an earnings based approach, an economic value approach, or both. The methods should be flexible enough to take into account the banks' individual characteristics and market conditions.

The associations urge the BCBS to assess impact on different business models

Our associations are deeply concerned with the unintended consequences of a Pillar 1 approach. For instance, the consequences of the interest rate risk seem to be in total contradiction with the sustainability of our housing markets. They contain the seeds of the risk of a modification in the loan rules with the foreseeable end of the fixed rate offering and consequently, the risk of a modification in the equilibrium of the housing market, an essential aspect for citizens to maintain the quality of life, which in turn supports the activity and economic growth in our countries.

This work also appears unnecessary both in order to protect the borrower and to safeguard the lender:

- The financial crisis enabled our systems to demonstrate their reliability;
- The systematic analysis of the borrower's solvency and the guarantees associated with each mortgage dossier enabled current loans to be largely maintained.

As an unintended consequence, and in order to hedge an artificial interest rate risk, the BCBS's proposals would impose the transfer of fixed-rate loans to the development of variable-rate loans without a cap, in a much more risky environment, virtually automatically weakening the borrower's solvency – and therefore generating higher credit risks - and, in longer term, weakening the total demand and the quality of life of the households.

The same discussion about unintended consequences arises in project financing and longer term financing to support economical activities of the borrower, where banks are expected to be active in providing capital and maturity transformation function for a long while.

Our associations are deeply concerned about the consequences of your proposal. As already mentioned, it will definitively jeopardise our members' ability to grant fixed-rate mortgages and loans, whereas this practice was a source of banks' resilience during the last crisis.

Do not hesitate to contact us should you require any further information or wish to discuss this important issue.

Yours sincerely,

Marie-Anne Barbat-Layani
CEO
French Banking Federation

Prof. Dr. Liane Buchholz
Executive Managing Director
Association of German Public Banks (VÖB)

Shin Takagi
Vice Chairman and Senior Executive Director
Japanese Bankers Association

Michael Kemmer
General Manager
Association of German Banks

Michel Vermaerke
Chief Executive Officer
Febelfin