Progress in the Implementation of Basel III

During the financial crisis banks' capital buffers turned out to be insufficient to cover their losses from credit defaults, trading and off-balance sheet exposure. The loss of confidence in banks' solvency and li-quidity led to the collapse of several banking institutions, with severe consequences for the real economy.

In response to the lessons learned from the financial crisis, the Basel Committee on Banking Supervision, a body of representatives of bank supervisory institutions and central banks from 27 countries, has set up new guidelines for banking regulation and supervision referred to as Basel III (See BIS, 2011a).

Basel III primarily aims to increase the quality and the quantity of banks' capital base. Another goal is the improvement of transparency since the opaqueness of bank operations made it difficult for investors to assess the strength of an institution's capital base, as well as its risk exposure. In addition, the risk coverage of the capital framework is enhanced by the Basel III rules. The Basel Committee also introduces a leverage ratio and features to take into account the procyclicality of the capital framework. Finally, the regulatory rules address the interconnectedness between institutions, which was an aggravating factor of the financial crisis.

Since the agreements made among the members of the Basel Committee are not legally binding per se, the transfer of the Basel III guidelines into binding law at the national level is fundamental to strengthen the global banking system. For this reason, the Bank for International Settlements (BIS) has published a report on the implementation of Basel III in the 27 countries that seconded representatives to the Basel Committee (BIS, 2011b).

The progress as of September 2011 is summarised in Table 1. It focuses on the implementation of rules concerning capital requirements, while the progress of bringing liquidity ratios and the leverage ratio into force is beyond the scope of this report.

For the purpose of comparability, four levels of implementation of the Basel III regulations are defined. Level 1 indicates that not even a "draft law, regulation or other official document" is published in this country. At Level 2 a "draft law, regulation or other official document" is publicly available. This is a typical stage of implementation at which the regulations are subject to public or legislative discourse. Cases in which the regulatory framework is "finalised and approved" but not yet applicable to banks are classified as Level 3. Finally, Level 4 is assigned to countries in which the legal and regulatory framework is established and already applies to banks.

The Basel Committee agreed on a phase-in schedule for the implementation of Basel III. Table 2 shows that the first elements of the guidelines are only to be implemented as of 1 January 2013. The schedule aims to reach full scale applicability of Basel III as of 1 January 2019. Most capital requirements are supposed to be implemented at lower levels initially, and then gradually increased to the target levels. The Minimum Tier 1 Capital, for example, is planned to be at least 4.5 per cent as of 1 January 2013 and rise to 6.0 per cent by 1 January 2019. Only the Minimum Total Capital has to be set at 8 per cent immediately as of 1 January 2013.

As countries have time until January 2013 to bring the Basel III guidelines into force, it is not surprising that the overall picture in Table 1 shows that the implementation into national law is still at an early stage. No country has yet reached Level 4 of full implementation and application of the regulations.

Saudi Arabia is the leading country and has already provided banks with the final regulations, although they are not applicable yet. For member states of the European Union (EU), the European Commission published a proposal on 20 July 2011, which leads all EU members to be classified at Level 2.

For Japan, the final version of the regulation was scheduled to be published at the end of March 2012. In September 2011, however, Japan was still at Level 1 with public consultations yet to be held. The United States planned consultations during 2011, but the BIS (2011b) points out that an implementation of Basel III has to be aligned with the regulatory framework imposed by the Dodd-Frank Act.

China is also classified as a Level 2 country. When the BIS report was published in September 2011, the Chinese regulation was expected to be established in

November 2011 and applicable as of the start of 2012. This goal has not been met and a revised implementation schedule is awaited. It is therefore worth following the revisions of the expected status of implementation over the coming months.

M.W.

References

BIS – Bank for International Settlements (2011a), "Basel III: A global regulatory framework for more resilient banks and banking systems", revised version June 2011, http://www.bis.org/publ/bcbs189.pdf .

BIS – Bank for International Settlements (2011b), "Progress report on Basel III implementation", http://www.bis.org/publ/bcbs203.pdf .

Table 1

Status of Basel III adoption (as of end September 2011)

Country	Basel III	Next steps-implementation plans
Argentina	1	On-going work to draft preliminary documents.
Australia	1	Discussion paper (not draft regulation) issued which describes the key policy elements that will be included in the draft Prudential Standards - Consultation until 02/12/2011 - Draft Prudential Standards to be issued 02/2012.
Belgium	2	(Follow EU process - EU proposal published on 20 July 2011)
Brazil	1	Draft regulation expected in Q4 2011 - Road map for Basel III implantation published in February 2011.
Canada	1	Draft regulation expected in May 2012 and final guidance before the end of 2012 for implementation in Q1 2013. OSFI has issued a number of public communications concerning the implementation of Basel III.
China	2	Regulation expected in November 2011 - Application expected at the start of 2012.
France	(2)	(Follow EU process - EU proposal published on 20 July 2011)
Germany	(2)	(Follow EU process - EU proposal published on 20 July 2011)
Hong Kong	1	Formal consultation on a draft Banking (Amendment) Bill planned in Q4 2011 (legislative process). In parallel, industry consultation planned in Q4 2011 on HKMA policy proposals on implementation of the various requirements under Basel III.
India	1	Draft regulation to be released for consultation within next few months.
Indonesia	1	Draft regulation to be released for consultation with industry in Q1 2012.
Italy	(2)	(Follow EU process - EU proposal published on 20 July 2011)
Japan	1	Public consultation planned in early 2012 - Publication of final rules text by the end of March 2012 - Implementation of final rules (end of March 2013 - In Japan, the fiscal year for banks starts in April and ends in March).
Korea	1	Draft regulation to be published in the first half of 2012.
Luxembourg	(2)	(Follow EU process - EU proposal published on 20 July 2011)
Mexico	1	Consultation to end in the fourth quarter this year. Final rule expected at the end of 2011 for an application during 2012.
The Netherlands	(2)	(Follow EU process - EU proposal published on 20 July 2011)
Russia	1	Draft regulations under development.
Saudi Arabia	3	Final regulation issued to banks.
Singapore	1	Announcement made on 28 Jun 2011 on Basel III minimum capital requirements, capital con-servation buffer and transition arrangements - Draft rules to be published for consultation in Q4 2011.
South Africa	1	Draft amendments to legislation expected at the end of Q1 2012 for consultation.
Spain	(2)	(Follow EU process - EU proposal published on 20 July 2011)
Sweden	(2)	(Follow EU process - EU proposal published on 20 July 2011)
Switzerland	1	Draft regulation on Basel III to be published for public consultation on 17 October 2011 - Final SIFI regulation (level: Banking Act) adopted by parliament on 30 September 2011 - Draft SIFI regulation (level: accompanying ordinances) to be published in Q4 2011.
Turkey	1	Draft regulation expected to be published in mid-2012.
United Kingdom	(2)	(Follow EU process - EU proposal published on 20 July 2011)
United States	1	Draft regulation for consultation planned during 2011. Basel 2.5 and Basel III rulemakings in the United States must be coordinated with applicable work on implementation of the Dodd-Frank regulatory reform legislation.
European Union	2	Proposal (directive and regulation) published by the European Commission on 20 July 2011.

Source: BIS (2011b).

Table 2

Phase-in arrangements (bold indicates transition periods-all dates are as of 1 January)

	2011	2012	2013	2014	2015	2016	2017	2018	As of Jan. 2019
Leverage ratio	Supervisory monitoring		Parallel run 1 Jan 2013-1 Jan 2017 disclosure starts 1 Jan 2015				Migration to Pillar 1		
Minimum common Equity capital ratio			**3.5%**	**4.0%**	4.5%	4.5%	4.5%	4.5%	4.5%
Capital conservation buffer						**0.625%**	**1.25%**	**1.875%**	2.50%
Minimum common equity plus capital conservation buffer			**3.5%**	**4.0%**	**4.5%**	**5.125%**	**5.75%**	**6.375%**	7.0%
Phase-in of deductions from CET1 (including amounts exceeding the limit of DTAs, MSRs and financials)				**20%**	**40%**	**60%**	**80%**	100%	100%
Minimum tier 1 capital			**4.5%**	**5.5%**	6.0%	6.0%	6.0%	6.0%	6.0%
Minimum total capital			8.0%	8.0%	8.0%	8.0%	8.0%	8.0%	8.0%
Minimum total capital plus conservation buffer			8.0%	8.0%	8.0%	**8.625%**	**9.25%**	**9.875%**	10.5%
Capital Instruments that no longer qualify as non-core tier 1 capital or tier 2 capital			Phased out over 10 year horizon beginning 2013						
Liquidity coverage ratio	Observation period begins				Introduce minimum standard				
Net stable funding ratio	Observation period begins							Introduce minimum standard	

Source: BIS (2011a).