
Press release

AFME welcomes the UK PRA's publication of elements of Basel 3.1 standards implementation

12 December 2023

In response to today's publication of key components of the UK implementation of the final Basel 3.1 standards agreed in December 2017, which will enter into force in the UK, in combination with the remaining elements anticipated for publication in the second quarter of 2024, **Caroline Liesegang, Head of Prudential Regulation at the Association for Financial Markets in Europe (AFME)**, said:

"Implementing internationally agreed post-financial crisis reforms is an important step in maintaining the role of the UK as a leading international financial centre. Today's publication of near-final policies on key elements of the Basel 3.1 package is a milestone in this regard, particularly for banks that play an important role in financing the real economy. The policies are closely aligned with international standards with some adjustments to improve risk measurement.

"The adjustments include the recalibration of the alpha factor within the standardised approach for counterparty credit risk (SA-CCR). This limits any disproportionate increase in capital requirements for banks and the related impact on end-users' ability to access hedging products to mitigate their risks.

"The PRA has also helpfully adjusted its approach in relation to the default risk of sovereign bonds by removing the inconsistency between the standardised approach and internal models. Under the PRA rules, banks are required to use the standardised approach for central government and central bank exposures. This approach should help in facilitating banks' continued market making in UK government bond markets in support of the economy.

"However, there was scope for further improvements, for instance, through introducing greater differentiation in the treatment of regulated versus unregulated financial sector entities within the credit valuation adjustment framework. This would have recognised the lower risk of counterparties, such as insurance providers, that play a pivotal role in the real economy. Another example is the lack of recognition of insurance as a risk mitigant in the business indicator calculation in the operational risk framework - an approach that is inconsistent with other areas of the prudential framework and results in an overstatement of risk and disproportionate capital requirements.

"Nevertheless, we welcome the clarity brought through the publication of near final policies in these key policy areas and await the remaining elements: credit risk, the output floor, and reporting and disclosure requirements which will allow for the impact of the Basel 3.1 package to be assessed in its entirety.

"Additionally, we await the PRA's planned review of the Pillar 2 framework to ensure there is no overlap with risks newly captured within the Pillar 1 framework as this will have a critical role in avoiding any undue increases in overall capital requirements.

"In the meantime, it will be important to ensure there is a coordinated timeline for implementing the package internationally, particularly as it relates to market risk standards. Developments in major jurisdictions should also be considered to ensure global consistency and to avoid harming the UK's competitiveness."

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Notes:

1. AFME (Association for Financial Markets in Europe) promotes fair, orderly, and efficient European wholesale capital markets and provides leadership in advancing the interests of all market participants. AFME represents a broad array of European and global participants in the wholesale financial markets. Its members comprise pan-EU and global banks as well as key regional banks, brokers, law firms, investors and other financial market participants. AFME participates in a global alliance with the Securities Industry and Financial Markets Association (SIFMA) in the US, and the Asia Securities Industry and Financial Markets Association (ASIFMA) through the GFMA (Global Financial Markets Association). For more information please visit the AFME website: www.afme.eu
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