Circular No.: 361000021954
Date: 3 December 2014

From : Saudi Arabian Monetary Agency

To : All Banks CFOs and CROs

Subject: **Frequently Asked Questions concerning SAMA's various Guidance Document regarding Basel III**

1. Basel Committee on Banking Supervision (BCBS) Document regarding Liquidity Coverage Ratio Disclosure Standards

We refer to SAMA's circular # 351000133366 dated 25 August 2014 with regard to the Prudential Return Guidance document concerning the captioned BCBS document of 25 August 2014.

The Agency response to the issues banks have raised is described in the attached. (Annex 1)

2. SAMA detailed guidance document relating to Pillar 1, June 2006 – A Haircut to Collateral issued through circular # 290 dated 12 June 2006

We refer to page 156 of the captioned SAMA's guidance document with regard to haircut on collaterals where "KSA government bonds and bonds of public sector entities (PSE's) eligible for sovereign treatment in local currency had been set by SAMA at 0% haircut".

SAMA wishes to amend the above in order to bring supervisory haircut into line with BCBS requirement of para 151 as given in the Annex 2.

3. SAMA Circular # 361000005773 dated 4 November 2014 regarding National Discretions concerning SAMA's Implementation of Capital Reforms under Basel III Framework

We refer to the captioned circular where SAMA has provided its National Discretion concerning the implementation of Basel III. In this regard with reference to para 99 of BCBS document as given below should read as "Yes" and not as originally submitted as "No". (Refer to Annex # 3)

Para	Areas of national discretion	KSA
99	Apply para 104 instead of 98 non-IMM CVA charge	Yes

4. SAMA's Final document concerning Basel III IRB Approaches for Credit Risk issued through circular # 351000121270 dated 17 July 2014

The Agency with regard to its captioned guidance document wishes to amend para 106 to read …. "that Netting is permitted in KSA for capital purposes" and not as previously documented as ……."Netting is not permitted in KSA". (Annex 4)

5. What is meant by PON "Press release 1 (a) Apply Statutory approach" in the last row of the Annexes (refer to Annex 5)

Response

The captioned "PON" is an abbreviation of "Point of Non-viability" in the context of the BCBS press release of 13 January 2011 entitled "Basel Committee issue final elements of the reforms to raise the quality of regulatory capital".

This Press Release covers minimum requirements to ensure loss absorbency at the point of non-viability as described in Annex 4 where 1a refer to applying the statutory approach.

If you need further clarifications, please contact Mr. Tariq Javed at t_javed@sama.gov.sa or Mr. Abbas Hassan at ahassan@sama.gov.sa.

Best regards,

Alwaleed Alsheikh
Director of Banking Supervision

Annex # 1

Liquidity Coverage Ratio Disclosure Standards Frequently Asked Questions

Question # 1

With regards to the requirement that banks must make available on its website disclosures relating to prior reporting periods going back one year, would this mean that banks will need to make available such disclosures for the past four quarters of 2014?

Response

The BCBS requirement reads as follows "Banks must also make available on their websites, or through publicly available regulatory reports, an archive (for a suitable retention period determined by the relevant national authority) of all templates relating to prior reporting period.

As all reference dates are on after 1 January 2015, there is no requirement to make available such disclosures for the past four quarters of 2014.

Question # 2

The quantitative data must be presented as a simple average of daily observations over the period quarter. Given the need to present disclosures relating to prior reporting quarters of 2014 (as noted in point 1 above), would this effectively mean that daily observations must be made with retrospective effect from January 2014 onwards?

Response

No. refer to question # 1. As all reference dates are on after 1 January 2015, there is no requirement to make available such disclosures for the past four quarters of 2014.

Question # 3

As the quantitative data must be presented as a simple average of daily observations over the period quarter (i.e. the average is calculated over a period of 90 days), would this mean that data for non-working days be based on the previous working day's data?

Response

Yes. The observation period is to be over 90 days, which means data for non-working days be based on the previous working day's data is acceptable. However this will not be effective until January 2017. Refer to question # 4 below.

Question # 4

It is not clear to us whether SAMA will avail of the national discretion (Chapter 2.12) of using the average month-end figures as opposed to daily average until January 2017. The requirement for daily observations of the quantitative data effectively means that banks will need to calculate the Liquidity Coverage Ratio (LCR) on a daily basis and the ability to do so is highly dependent on systems capabilities. On this note, while Bank is currently in the process of acquiring the necessary systems to meet this requirement, this is not expected to be completed by January 2015 and we would appreciate if SAMA will allow for the disclosure data to be computed based on average of monthly figures till 1st January 2017, as provided in the BCBS document under national authorities discretion.

Response

Yes. SAMA will avail of the described national discretion (Chapter 2.13) of using the average month-end figures as opposed to daily average until January 2017. Consequently, SAMA will allow for the disclosure data to be computed based on average of monthly figures till 1st January 2017, as provided in the BCBS document.

Consequently, post January 2017, data must be presented as simple averages of daily observations over the previous quarter (i.e. the average is calculated over a period of, typically, 90 days).

Annex # 2

CREDIT RISK MITIGANTS

A. HAIRCUTS TO COLLATERALS

Debt Securities	• *As per issuer, maturity, and rating from 0.5% up to 15%. (Para 151)* • ***However, KSA Government bonds and bonds of Public Sector Entities (PSEs) eligible for sovereign treatment in local currency to be at 0% haircut.***

B. ADDITIONAL COLLATERALS

2nd mortgage-SIDF (Junior Lien)	*Residual value to be eligible CRM as per existing Basel II.*

Standard supervisory haircuts

151. These are the standard supervisory haircuts (assuming daily mark-to-market, daily remargining and a 10-business day holding period), expressed as percentages:

Issue rating for debt securities	Residual Maturity	Sovereigns	Other issuers
AAA to AA-/A-1	≤ 1 year	0.5	1
	>1 year, ≤ 5 years	2	4
	> 5 years	4	8
A+ to BBB-/ A-2/A-3/P-3 and unrated bank securities per para. 145(d)	≤ 1 year	1	2
	>1 year, ≤ 5 years	3	6
	> 5 years	6	12
BB+ to BB-	All	15	
Main index equities (including convertible bonds) and Gold		15	
Other equities (including convertible bonds) listed on a recognized exchange		25	
UCITS/Mutual funds		Highest haircut applicable to any security in which the fund can invest	
Cash in the same currency		0	

- As per issuer, maturity, and rating from 0.5% up to 15%. (Para 151)
- However, KSA Government bonds and bonds of Public Sector Entities (PSEs) eligible for sovereign treatment in local currency to be at 0% haircut.

Annex # 3

Basel III National Discretions

Para	Areas of national discretion	KSA
52	Consider appropriate audit, verification or review procedures	Yes
61	Apply a limit lower than 0.6% to excess provisions	No
78-79	FAQ14 consolidation alternative to deduction	No
80 FN 27	Permit banks to use a conservative estimate instead of look-through	Yes
80	Permit banks to exclude investments made in the context of resolution	Yes
84 FN 31	Permit banks to use a conservative estimate instead of look-through	Yes
84	Permit banks to exclude investments made in the context of resolution	Yes
99	Apply para 104 instead of 98 non-IMM CVA charge	Yes[1]
121	Allow banks to use unsolicited ratings	No
132 (c)	Apply at solo level	Yes
132 (d)	Impose time limits on draw down of buffers	Yes
133	Impose shorter transitional periods	No
142	FN 50 Apply at solo level	Yes
PON[2]	Press release 1 (a) Apply Statutory approach	No

[1] Originally submitted as "No", rectified as "Yes"
[2] Point of Non-viability

Annex 4

M. CREDIT RISK MITIGATION

General

103. Under the IRB approach, a Bank may take into account the effect of recognized credit risk mitigation in its calculation of risk-weighted amount of exposures, including:

(i) Recognized collateral
(ii) Recognized guarantees and recognized credit derivative contracts.

104. The risk-weighted amount of a Bank's exposure in respect of which recognized credit risk mitigation has been taken into account shall not be higher than that of an identical exposure in respect of which recognized credit risk mitigation has not been so taken into account.

Capital Treatment of Recognized Collateral

105. Under the IRB approach, collateral is recognized through the determination of LGD (see paragraphs 28 to 38 for corporate, sovereign and bank exposures and paragraphs 54 and 55 for retail exposures)

106 to 120 – Items (to be ignored) for the present as netting is not permitted.

Capital Treatment of Recognized Netting

(a) General

106. Where a Bank is entitled pursuant to a valid bilateral netting agreement to net amounts owed by the Bank to a counterparty against amounts owed by the counterparty to the Bank, the Bank may take into account the credit risk mitigating effect of the recognized netting in calculating the EAD of its exposure to the counterparty. **(However, netting is not permitted in KSA for capital purposes)**

(b) EAD measurement for on-balance sheet netting

107. In respect of on-balance sheet exposures which fall within the IRB class of corporate, sovereign, bank, retail or other exposures, a Bank may net the debit balances from the credit balances in the accounts of the same counterparty in accordance with the formula set out in paragraph 148 and report the net credit exposure amount as on balance sheet exposures before recognized guarantees/credit derivative contracts.

108. Below is the formula for calculating the net credit exposure with a counterparty for on-balance sheet exposures, adjusted for the credit risk mitigating effect of a valid bilateral netting agreement:

Net credit exposure = max [0, exposures - liabilities x (1 - Hfx)]

Guidance note on Basel II Prudential Returns Draft # 2 of March, 2006.

109. Hfx is the haircut to be applied in the case of a currency mismatch between exposures and liabilities, which is 8% assuming a **minimum holding period** of 10 business days, daily remargining and daily marking-to-market. It should be adjusted in accordance with the provisions set out in SAMA based on the frequency of remargining.

110. Treatments for maturity mismatch in respect of on-balance sheet netting are set out in paragraphs 142 to 144.