

Extending the G-SIFI Framework to domestic systemically important banks

Progress Report to G-20 Ministers and Governors

I. Introduction

At the Cannes Summit in November 2011, the G20 Leaders endorsed the Financial Stability Board (FSB)'s policy framework on systemically important financial institutions (G-SIFIs), comprising a new international standard for resolution regimes, more intensive and effective supervision, and requirements for cross-border cooperation and recovery and resolution planning as well as, from 2016, additional loss absorbency for those banks determined as global systemically important financial institutions (G-SIFIs). At that meeting, the FSB was asked to deliver, in consultation with the BCBS, a progress report by the G20 April Finance meeting on the definition of the modalities to extend expeditiously the G-SIFI framework to domestically important banks.

The international effort to address the issues related to SIFIs focuses primarily on minimizing the adverse externalities caused by their distress or failure. These externalities are strains brought about on other financial firms and on markets as well as on the broader economy, including through, as in the recent crisis, the commitment of large sums of public funds in dealing with the problem. The G-SIB framework assesses the externalities from a global perspective (i.e., where distress or failure would disrupt the global financial system), making no distinctions about impacts on individual jurisdictions.

II. The domestic perspective

The framework being considered for D-SIBs is best understood as taking the complementary perspective, namely that of assessing the impact of the failure associated with the *local* presence of a bank in a given jurisdiction, whether a national or an internationally active bank.

The Basel Committee and the FSB examined at their meetings in March 2012 a minimum framework for domestic systemically important banks (D-SIBs), based on a set of principles, covering both the methodology for assessing the systemic importance of domestic institutions, and the policy tools that national authorities could apply to contain the systemic risks they pose. The framework is based on assessment by local authorities, who are best placed to identify which banks are systemic within their borders.

III. Jurisdictional specificities and international interest

The adoption of a complementary perspective with respect to the G-SIB framework, including the role of local authorities in assessing banks that are systemic at the domestic level, has two implications.

The first is that the framework must recognise jurisdictional specificities: in order to accommodate the structural characteristics of individual jurisdictions, the assessment and application of policy tools should include an appropriate degree of national discretion. This contrasts with the prescriptive approach in the G-SIB framework.

The second implication is that, because a D-SIB framework is still relevant for reducing cross-border externalities that may be negligible from a global perspective but nonetheless very significant from the jurisdictional perspective, the effectiveness of local authorities in addressing systemic risk at the domestic level is of interest to a wider group of countries. There is therefore an international interest in appropriate D-SIBs frameworks being in place in all jurisdictions. Ensuring that individual jurisdictions do not adopt widely different approaches in dealing with D-SIBs will also promote a level playing field internationally.

The principles for D-SIBs being considered therefore seek to establish a minimum framework that would ensure compatibility with the G-SIB framework, address the cross border externalities that the failure of a domestic systemic institution may nonetheless pose, and preserve a level playing field within and across jurisdictions. The principles would include guidelines for national authorities to assess the systemic importance of banks in a domestic context, as well as an agreed appropriate unit of analysis, i.e. the entity that is being assessed for systemic importance at the domestic level.

Most of the factors considered in the G-SIB assessment framework, such as size, interconnectedness, substitutability/financial institution infrastructure and complexity, also play a role when assessing domestic systemic importance. In addition, national authorities may also consider country specific factors, such as size of the banking sector relative to the domestic economy, or the concentration of the banking sector itself.

The framework being considered would further cover the frequency and disclosure of the assessment methodology by national authorities, as well as the policy tools and measures that can be applied, including for higher loss absorbency, in light of country-specific factors and of the nature and specific characteristics of the D-SIBs, such as their legal form.

The principles would allow for appropriate national discretion to accommodate structural characteristics of the domestic financial system, including the possibility for countries to go beyond the minimum framework and impose additional requirements based on the country and domestic banking sector specificities, for example with regard to higher loss absorbency. At the same time, the implementation of the principles will need to be combined with a strong peer review process to ensure that appropriate and effective frameworks for domestic SIBs are in place.

IV. Relationship with the G-SIB framework and compatibility with G-SIB requirements

An important aspect of a D-SIB framework relates to its compatibility with the G-SIB framework, to ensure that adequate and consistent incentive structures are in place at the domestic level as well as at the international level, and across various types of institutions. The G-SIB and D-SIB frameworks will need to be compatible. An issue that needs further consideration in this regard concerns the treatment of the subsidiaries of G-SIBs that may be of systemic importance within a host jurisdiction. The goal is to ensure the overall consistency between the D-SIB and the G-SIB frameworks from the perspective of both home and host countries.

V. Next steps

The BCBS and the FSB will conduct further work on the set of principles as a minimum framework for D-SIBs. The proposals will be finalised by the BCBS for endorsement by the FSB in the autumn.

The outcome of the work will be submitted to the G20 Ministers and Governors Meeting in November.