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Further step towards implementing Basel III in Switzerland

FINMA opens consultation on leverage ratio and disclosure circulars

The Basel III international banking standards prescribe an unweighted leverage ratio. The Swiss Financial Market Supervisory Authority FINMA is today opening a consultation on the new circular "Leverage ratio – banks" to determine the calculation rules required in Swiss regulation. Basel III also requires that both the leverage ratio and the liquidity coverage ratio, which had already been the subject of a consultation on implementing provisions in Switzerland, be disclosed from 2015 onwards. To this end, FINMA is revising the circular "Capital adequacy disclosure – banks". The consultation period for both circulars ends on 31 August 2014.

Basel III has tightened requirements on risk-weighted equity capital for banks, supplementing them with a simple and non-risk-based measure, the leverage ratio. It also introduces new standards defining minimum liquidity requirements. These measures are intended to make both individual institutions and the banking sector as a whole more crisis-resistant. The FINMA circulars under consultation from today form the basis for ensuring that this phase of Basel III can be implemented on time in Switzerland in line with the international standards. As regards the introduction of the leverage ratio requirement, this is the first step towards implementation (provisions specific to Switzerland already exist for large banking groups), while for liquidity coverage ratio (LCR) the rules on disclosure are the final step towards implementation in Switzerland. The consultation process for the LCR implementing provisions is over and those provisions will soon be published.

Calculating leverage ratio

The aim of the non-risk-based leverage ratio is to avoid excessive indebtedness in the banking sector. Basel III defines the leverage ratio as the ratio of an institution's eligible core capital (Tier 1) to its total exposure. The leverage ratio includes all on and off-balance-sheet positions. The new FINMA Circular 2015/xx "Leverage ratio – banks" sets out how this total exposure is calculated. The definition of

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eligible core capital thus follows the terms of the Capital Adequacy Ordinance (CAO) that came into force in 2013 and those of FINMA Circular 2013/1 “Eligible equity capital – banks”.

The Basel Committee on Banking Supervision will set the required leverage ratio applicable from 2018 after an observation period. Any remaining questions about total exposure will be clarified during this period. The current, non-binding guide value for the leverage ratio is 3%, but this may change after the observation period. Accordingly, the FINMA circulars under consultation from today do not contain minimum requirements for the leverage ratio for banks and securities dealers.

Disclosure of leverage ratio and liquidity coverage ratio

The intention is for banks and securities dealers to disclose both the leverage ratio and the ratio of the liquidity buffer (liquidity coverage ratio) from 2015. The LCR defines a liquidity buffer made up of high-quality liquid assets (HQLAs), for example Swiss Confederation bonds, cantonal bonds or Swiss mortgage bonds. A bank must be able to call on this buffer to offset increased net cash outflows (calculated in accordance with a specific stress scenario) for at least 30 days. The LCR will be introduced in 2015 as a regulatory minimum standard for liquidity and is already stipulated in the Liquidity Ordinance. The draft revision of FINMA Circular 2008/22 “Capital adequacy disclosure – banks” submitted for consultation today is aimed at regulating how the leverage ratio and LCR are disclosed from 2015. Securities dealers have no requirements to meet with regard to the LCR.

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