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APRA

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To All Authorised Deposit-taking Institutions (ADIs)

BASEL III REFORM PACKAGE RELEASED

On 16 December 2010, the Basel Committee on Banking Supervision (BCBS) published its final package of banking sector reforms, *Basel III: A global regulatory framework for more resilient banks and banking systems*. The full details of the reforms can be located on the Bank for International Settlements' website (www.bis.org).

The capital components of these reforms will:

- increase the minimum common equity requirement from 2 per cent to 4.5 per cent. In addition, institutions will be required to hold a capital conservation buffer of 2.5 per cent, bringing the total common equity requirement to 7 per cent. The total Tier 1 capital requirement will be 8.5 per cent;
- address excess credit growth through the introduction of a countercyclical buffer that extends the capital conservation mechanism; and
- introduce an internationally harmonised leverage ratio to serve as a backstop to the risk-based capital measure and to contain the build-up of excessive leverage in the system.

The BCBS has yet to finalise additional entry criteria for Additional Tier 1 and Tier 2 capital as set out in its August 2010 consultative document, *Proposal to ensure the loss absorbency of regulatory capital at the point of non-viability*. Once finalised, the additional criteria will be added to the regulatory framework.

The BCBS reforms also introduce, for the first time, two internationally consistent regulatory standards for liquidity risk supervision, which aim to promote stronger liquidity buffers (both in quality and quantity) and ensure that banking systems are more resilient to liquidity stresses. These standards are:

- the Liquidity Coverage Ratio (LCR), which aims to promote short-term resilience by ensuring that banking institutions have sufficient high-quality liquid assets to survive an acute stress scenario lasting for one month; and
- the Net Stable Funding Ratio (NSFR), which aims to promote longer-term resilience by creating additional incentives for banking institutions to fund their activities with more stable sources of funding (e.g. deposits or long-term debt) on an ongoing structural basis.

Further information about the implementation of the LCR in Australia can be found in the joint Media Release issued by APRA and the Reserve Bank of Australia (www.apra.gov.au).

As a member of the Basel Committee, APRA has been actively involved in developing these global reforms and it fully supports the package announced by the BCBS. APRA has begun work on developing draft prudential standards, prudential practice guides and reporting requirements to give effect to these reforms in Australia. APRA anticipates that it will begin consultation on the reforms in the first half of 2011 and continue into 2012.

Yours sincerely,

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