SHEARMAN & STERLING LLP

FINANCIAL INSTITUTIONS ADVISORY &
FINANCIAL REGULATORY

CLIENT PUBLICATION

17 September 2013

Basel III Framework: US/EU Comparison

If you wish to receive more information on the topics covered in this publication, you may contact your regular Shearman & Sterling contact person or any of the following:

Contacts

Barnabas W.B. Reynolds
London
+44.20.7655.5528
barney.reynolds@shearman.com

Thomas Donegan
London
+44.20.7655.5566
thomas.donegan@shearman.com

Donald N. Lamson
Washington, DC
+1.202.508.8130
donald.lamson@shearman.com

Bradley K. Sabel
New York
+1.212.848.8410
bsabel@shearman.com

Hervé Letréguilly
Paris
+33.1.53.89.71.30
hletreguilly@shearman.com

Tobia Croff
Milan
+39.02.0064.1509
Rome
+39.06.697.679.209
tobia.croff@shearman.com

Winfried M. Carli
Frankfurt
+49.69.9711.1220
wcarli@shearman.com

Colin Law
Hong Kong
+852.2978.8090
Beijing
+86.10.5922.8190
colin.law@shearman.com

The US and EU rules implementing Basel III follow many aspects of Basel III closely, but there are major differences in approach in several key areas. Financial institutions have been engaged in a "race to the top" to show strong capital ratios but rules on leverage appear to be the most challenging and may require significant business restructuring. The interplay between the US and EU implementation of Basel III and the gradual "phase in" of certain rules, particularly on liquidity and leverage, will have a profound impact on the relative competitiveness of relevant US and EU financial institutions. This client publication, and the accompanying US/EU comparison and summary table, highlight points of international consistency and divergence.

Basel III establishes a new set of global standards for capital adequacy and liquidity for banking organizations. Although principally aimed at banks, these standards also apply to certain other types of financial institution (e.g., EU investment firms) as well. The Basel Committee on Banking Supervision (the "**Basel Committee**") developed Basel III to supplement and, in certain respects, replace, the existing Basel II standards, the composite version of which was issued in 2006 as an update to Basel I.[1] The core elements of Basel III were finalized at the international level in 2010 and implementing rules have now been issued in 25 of the 27 jurisdictions that comprise the Basel Committee.[2]

[1] The Basel Committee is an international supervisory group in which banking supervisors from the US, the UK, and 25 other nations participate.

[2] Basel Committee report: "G20 Monitoring and Implementing of Basel III Regulatory Reforms," August 2013.

Contacts (cont.)

Azad Ali
London
+44.20.7655.5659
azad.ali@shearman.com

David L. Portilla
New York
+1.212.848.4468
david.portilla@shearman.com

Sylvia Favretto
Washington, DC
+1.202.508.8176
sylvia.favretto@shearman.com

Kolja Stehl
Frankfurt
+49.69.9711.1623
kolja.stehl@shearman.com

Ellerina Teo
London
+44.20.7655.5070
ellerina.teo@shearman.com

James Campbell
London
+44.20.7655.5570
james.campbell@shearman.com

Like Basel I and II, Basel III is not legally binding in any jurisdiction but rather is intended to form the general basis for national (or regional) rulemaking. As with Basel I and II, Basel Committee members have taken different approaches to implementing Basel III. The US and EU rules implementing Basel III differ in a number of key areas, including:

- Treatment of capital instruments;
- Risk weight calculation;
- The leverage ratio;
- Adjustments for derivative counterparty risk (the "credit valuation adjustment");
- References to external credit ratings; and
- Large exposures.

Implementing rules are now in place in the US and EU, although many requirements are to be "phased in" ahead of the timetable for full implementation of Basel III by January 1, 2019. The timing of the US and EU phase-in of certain rules, such as leverage and liquidity requirements, is not consistent.

Basel I and II are widely perceived to have had various shortcomings that may have contributed to the financial crisis. The Basel Committee believes that the previous framework neither adequately accounted for risks posed by exposures to transactions such as securitizations and derivatives nor required institutions to maintain adequate levels of capital. Other perceived deficiencies included the lack of quantitative liquidity standards and the failure to take into account systemic risks associated with the build up of leverage in the financial system. In response to these shortcomings, the Basel III framework sets out quantitative and qualitative enhancements for capital adequacy, new liquidity and leverage ratio requirements, as well as other elements to help contain systemic risks.

The US and EU rules implementing Basel III, as well as the interplay between these rules, will have a profound impact on the relative competitiveness of US and EU institutions as well as the product mix that banking institutions will offer to customers and the types of debt and equity instruments sold to investors. This client publication includes a US/EU comparison table (the "**US/EU Comparison Table**") comparing and contrasting the US and EU rules in the above key areas.

Basel III Implementation in the US

In July 2013, the Board of Governors of the Federal Reserve System (the "**Federal Reserve**") and other bank regulatory agencies approved final rules ("**Final US Rules**") that codify the US Federal regulatory agencies' regulatory capital rules into a single, comprehensive regulatory framework. The Final US Rules implement the Basel III capital framework as well as relevant provisions of the Dodd Frank Wall Street Reform and Consumer Protection Act (the "**Dodd-Frank Act**"). In addition, the Final US Rules replace the Basel I-based capital system that has been in place in the US. In particular, the Final US Rules, among other things:

- Revise the definition of regulatory capital;
- Implement new minimum requirements for Common Equity Tier 1 and an overall Tier 1 capital requirement;

- Add a supplemental leverage ratio for "advanced approaches" banks;[3] and
- Amend the methodology for determining risk weighted assets.

The Final US Rules were adopted largely as proposed. Notable changes from the proposed rules include:

- Non-Advanced Approaches Banks may make a one-time election not to include most elements of "accumulated other comprehensive income" (known as "**AOCI**") in regulatory capital calculations, and instead use the existing framework that excludes most AOCI from regulatory capital;
- The proposed treatment of residential mortgages was not adopted, so the current treatment for residential mortgage exposures under the general risk-based capital rules will continue to apply. Specifically, the Final US Rules assign a 50 or 100 per cent. risk weight to exposures secured by one-to-four family residential properties;
- The Final US Rules permanently grandfather trust-preferred securities and other non-qualifying capital instruments that were issued before May 19, 2010 in the Tier 1 capital of depository institution holding companies with total consolidated assets of less than $15 billion as of December 31, 2009; and
- Non-Advanced Approaches banking organizations and savings and loan holding companies ("**SLHCs**") must generally begin complying with the Final US Rules on January 1, 2015. Advanced Approaches banking organizations that are not SLHCs must begin complying with the Final US Rules on January 1, 2014.[4]

Basel III Implementation in the EU

The EU has implemented Basel III through two legislative acts, the Capital Requirements Regulation ("**CRR**") and Capital Requirements Directive ("**CRD**") (together, "**CRD IV**"), which were published in the Official Journal of the European Union on June 27, 2013. CRD IV consolidates the previous capital framework and amends that framework to implement Basel III.

The CRR will enter into force from January 1, 2014 and as a "regulation" it will be directly applicable in the legal systems of all EU Member States without the need for transposition at the Member State level. This contrasts to the previous framework which used directives only, which rely upon national implementation measures of Member States. The aim is to create a "single rulebook" which applies equally to all Member States and minimizes the scope for variations across Member States. The CRR addresses the quantity and quality of capital required (impacting the regulatory capital base of many institutions as certain outstanding instruments no longer qualify as regulatory capital), liquidity, counterparty credit risk, and leverage.

The CRD requires Member States to promulgate compliant national legislation by December 31, 2013. A directive, unlike a regulation, gives Member States a certain amount of discretion to implement EU requirements in a form and manner that is suitable to them. The CRD contains provisions addressing prudential supervision and the new capital conservation and counter cyclical capital buffers, as well as certain areas not covered by Basel III, but which the EU nevertheless wishes to implement, including requirements relating to corporate governance, sanctions, regulation of variable remuneration and measures to reduce reliance on external credit ratings.

[3] US banking groups with consolidated assets of at least $250 billion or consolidated total on-balance sheet foreign exposures of at least $10 billion qualify as "Advanced Approaches Banks".

[4] The Final US Rules do not apply to the following SLHCs: top-tier SLHCs that are insurance underwriting companies, top-tier SLHCs that held 25% or more of total consolidated assets in subsidiaries that are insurance underwriting companies (excluding assets associated with insurance for credit risk) as of June 30, of the previous calendar year, and, top-tier SLHCs that are grandfathered unitary SLHCs that derived 50% or more of total consolidated assets or 50% or more of total revenues on an enterprise wide basis from non-financial activities as of June 30 of the previous calendar year. Other SLHCs are covered by the rule and are referred to in this client publication as "covered SLHCs."

The European Banking Authority (the "**EBA**") will play a new role in implementing Basel III in the EU, a matter historically dealt with largely by national regulators. Certain provisions in CRD IV mandate the EBA to develop and publish technical standards to "flesh out" certain parts of CRD IV. The EBA has already produced a number of consultation papers containing final draft technical standards, such as in relation to own funds requirements and credit risk adjustment.

As with the EU's implementation of Basel II, CRD IV generally applies to all credit institutions (such as banks and building societies) and also to investment firms (which generally encompasses broker dealer businesses). Therefore, broadly all financial institutions in the EU are subject to the new Basel III regime, with a much wider scope than that applicable in the US. However, EU firms providing investment advice and/or executing brokerage services only and which do not hold client monies will, as under previous legislation, be exempt under CRD IV. In addition, firms that are subject to CRD IV but engage predominantly in advising and arranging activities are not subject to much of the CRD IV regime by virtue of the limited credit and market risks assumed by such firms. Also, EU financial institutions can select whether to be subject to the Standardized Approach or obtain permission to be subject to the Internal Ratings Based ("**IRB**") Approach (which is equivalent to the Advanced Approach in the US).

Highlights: Points of Comparison

Despite a degree of commonality in the US and EU implementation of Basel III, there is significant divergence in some respects which may give rise to certain arbitrage opportunities.

- **Impact of the Dodd-Frank Act**: The Dodd-Frank Act introduced several capital-related provisions unique to US financial institutions that are inconsistent with, and stricter than, the Basel III framework. For example:
  - ***Regulatory Capital Base***: As described in greater detail in the US/EU Comparison Table, the criteria for capital instruments to qualify as regulatory capital differ from—and are stricter than—existing qualification standards. Accordingly, groups subject to the new rules should evaluate outstanding instruments against the new qualification standards and phase out schedules. In this regard, the Dodd-Frank Act: (i) requires an accelerated three year phase out schedule for certain "hybrid" capital instruments issued by large US banks that would no longer count as regulatory capital or as the same type of capital, (ii) provides permanent grandfathering treatment for certain capital investments made by the US government in banks that would not otherwise qualify, and (iii) requires mandatory deduction from capital of investments in hedge funds and private equity funds "organized and offered" by US banking entities in accordance with the Volcker Rule.
  - ***Removal of References to External Credit Ratings***: The financial crisis highlighted the risks of over-reliance on external credit ratings which are dominated by a small pool of credit rating agencies. Several changes to US asset risk weightings were driven by the Dodd-Frank Act requirement to remove from US regulations reliance on external credit ratings (e.g., in the context of investments in securitized assets or sovereign debt). Final US Rules offer several alternatives to use of these ratings. For example, the Organization for Economic Cooperation and Development ("**OECD**") "country risk classification" codes are used for purposes of determining risk weights of exposures to non-US sovereigns and non-US banks.

    Similarly, and in line with G20 commitments,[5] CRD IV contains provisions designed to reduce over-reliance on external ratings, requiring financial institutions to strengthen their own credit risk assessment and not to rely solely and mechanistically on external credit ratings. For example, institutions with a material number of exposures in a given

[5] The Financial Stability Board issued a progress report to the G20 on August 29, 2013 ("Credit Rating Agencies: Reducing Reliance and Strengthening Oversight"), containing a "roadmap" for national and supra-national authorities to amend existing rules, guidance and encourage reporting and disclosure of credit risk assessment procedures and strategy, aimed at ending the mechanistic reliance on external credit ratings.

portfolio will be required to develop internal ratings for that portfolio and to use external ratings to benchmark the resulting capital requirements to their internal credit opinions. If the internal credit opinion shows that the external ratings are by comparison too favorable, then Pillar II discretion should be used to require the holding of additional capital in respect of these risks (Articles 135 and 136 CRR). In its June 2013 publication on new rules on credit ratings ("**MEMO/13/571**"), the European Commission referred to US rules which require the removal of reference to credit ratings in legislation and indicated that the EU would adopt a cautious approach by abolishing references to credit ratings in EU legislation by January 1, 2020, only once appropriate alternatives have been identified and implemented.

  - ***Collins Amendment Capital Floor***: The so-called Collins Amendment of the Dodd-Frank Act (Section 171) prevents Advanced Approaches Banks from having minimum capital requirements below the general risk-based capital requirements. As a result, a non-US bank employing the Advanced Approaches of Basel III and pursuing a strategy of lower risk loans and investment grade assets may enjoy a competitive advantage over US institutions, as the capital floor imposed under the Collins Amendment would eliminate any ultimate capital relief large US banks may otherwise obtain under the internal models approach of Basel III.

- **New Risk Weight Calculations Included as Part of the US Basel III Rules**: The Final US Rules would significantly modify risk weighted asset calculations under the "Standardized Approach", effective January 2015. On the other hand, the EU has not effected a wholesale change to asset risk weightings. Changes in the relative capital charges applied to assets held by US institutions, as compared to those applied in the EU, would change the competitive dynamic between institutions located in those jurisdictions and potentially introduce opportunities for arbitrage.

- **Leverage Ratio Implementation**: The Basel III leverage ratio is a non-risk-based ratio which includes off-balance sheet exposures and is intended to complement capital requirements by acting as a backstop to risk-based capital requirements. In the US, Advanced Approaches Banks will be required to comply with the Basel III leverage ratio standards (3 per cent.), as well as the existing Tier 1 capital-to-assets leverage ratio (generally 4 per cent.). Further, the Federal Reserve, the Federal Deposit Insurance Corporation ("**FDIC**"), and the Office of the Comptroller of the Currency ("**OCC**") have, separately from Basel III, proposed an "enhanced supplementary leverage ratio" for the largest banking organizations. If adopted, this enhanced supplementary leverage ratio would make the US version of Basel III even stricter than the Final US Rules. Under this proposal, covered bank holding companies would be required to maintain a supplementary Basel III-based leverage ratio of at least 5 per cent. in order to avoid restrictions on capital distributions and discretionary bonus payments. In addition, insured depository institution subsidiaries of those covered bank holding companies would be required to maintain a leverage ratio of 6 per cent. to be considered "well capitalized" under the applicable prompt corrective action framework. In the EU, the leverage ratio has not been introduced outright as a binding requirement, but as a Pillar II measure (i.e., the national regulator will determine whether or not the leverage ratio of a particular institution is too high and whether the institution should hold more capital as a consequence). In the EU, credit institutions and investment firms must calculate their leverage ratios from January 1, 2014 and report them to national regulators from January 1, 2015. The leverage ratio may be introduced as a binding measure in 2018, following the Basel Committee review and calibration of leverage ratio requirements in the first half of 2017.

- **The Credit Valuation Adjustment**: The credit valuation adjustment ("**CVA**") for derivatives trades covers mark-to-market losses on expected counterparty risk. In the EU, corporates, sovereigns, and pension funds are exempt from the new CVA charge. US banks are concerned that the absence of a similar exemption in the US rules gives an unfair pricing advantage to banks trading within the EU which are not required to hold capital against similar exposures. Other critics have argued that the CVA exemption is inconsistent with aims to achieve globally harmonized prudential requirements. Some EU Member States are reportedly considering imposing a Pillar II capital add-on to compensate for the CVA exemption.

- **Super-equivalence**: The implementation of Basel III in the EU was delayed as a result of political disagreement between EU Member States over the ability of a Member State to impose higher capital requirements than applicable under CRD IV, (i.e., by "gold-plating"). The final CRD IV position is to prohibit super-equivalent standards being imposed by Member States. The rationale for this restriction is that there would otherwise be regulatory arbitrage, with risky activities migrating to Member States with lower capital and liquidity requirements. Member States may, however, increase the capital ratio by use of the countercyclical, systemic risk, and the global and systemic institution buffers. As noted above in the context of the CVA exemption, Pillar II discretionary powers have the potential to undermine the objective of EU-wide uniform capital requirements. As demonstrated by the proposed enhanced supplemental leverage ratio and the lack of a CVA exemption in the Final US Rules, the US Federal banking regulators have determined to adopt more stringent rules in certain instances.

- **Large Exposures**: The CRR contains requirements on large exposures relating to the reporting and calculation of own funds requirements for large exposures in the trading book. These requirements do not materially differ from pre-existing EU rules on large exposures in the Banking Consolidation Directive (2006/48/EC). This is an area that is subject to change in the near future. In its March 2013 proposal for a new large exposures framework for measuring and controlling risks associated with the failure of a large counterparty (the "**Large Exposures Proposal**"), the Basel Committee expressed concern that while existing Basel rules recognise the need for banks to limit the size of their exposures in relation to their capital, existing rules fail to explain in sufficient detail the methodology by which banks should measure and aggregate their exposures to large counterparties. The Large Exposures Proposal would supplement rather than replace existing rules. The key points to note are that: (i) a large exposure to a counterparty would arise if an institution's exposure to a counterparty or group of connected counterparties amounts to 5 per cent. (under CRD IV this is currently 10 per cent.) or more of a bank's eligible capital base, and (ii) exposures to a counterparty or group of connected counterparties would be prohibited if 25 per cent. or more of a bank's Common Equity Tier 1 or Tier 1 capital is exposed towards the counterparty or group of connected counterparties (under CRD IV banks are currently limited to exposures of 25 per cent. of total regulatory capital). Banks would be prohibited from using their internal methodologies for calculating exposures. Further, the Large Exposures Proposal contains special rules for certain defined entities including sovereigns, central counterparties, and global systemically important banks ("**G-SIBs**"). The Basel Committee intends to introduce new rules to regulate large exposures following a review of responses to the Large Exposures Proposal consultation, which closed on June 28, 2013. In the US, in December 2011, the Federal Reserve proposed a single counterparty credit exposure limit for large US banking holding companies, and issued a similar proposal for foreign banking organizations in December 2012, in each case, as a part of the Federal Reserve's proposed enhanced prudential standards under Section 165 of the Dodd-Frank Act. If these proposals are adopted, the US large exposures regime would differ from the Large Exposures Proposal in a number of ways.

- **Other Considerations**:

  - The new rules require that banks in the US and EU have in place adequate procedures and resources (including data and systems) to comply with the range of capital, liquidity, leverage, and counterparty requirements. The costs of implementation of the rules are likely to have a substantial impact on the regulatory costs of systemically important institutions and relative costs for small firms also could be significant.

  - Market participants and regulators have expressed concerns that differences in international accounting standards could lead to competitive advantages or disadvantages.

  - The Final US Rules do not address the Basel III liquidity requirements. The US requirements are being left for a future proposal that regulators have said will be issued after the Basel Committee has finalized its approach in this area. The

US Federal Reserve Board Governor, Daniel Tarullo, has called for the liquidity requirements to be eased. In contrast, the EU rules incorporate the Basel III liquidity standard.[6]

- Additional Basel III and other requirements—including the capital "surcharge" for G-SIBs and a minimum equity and long-term debt requirement for the largest US banking organizations—are also expected to be implemented in the US through subsequent rulemakings over the next couple of years.

Conclusion

Basel III arguably represents the most important international response to the financial crisis. Divergences in approach between the US and the EU follow, among other reasons, as a result of the prior, hard-wired constraints imposed by Dodd-Frank in the US and fraught political negotiations in the EU in the run-up to implementation. The breadth and impact of the relative cost advantages stemming from divergence in the rules will differ by asset class. Despite implementation of Basel III in the US and EU, many rules are to be "phased-in" over the coming years and in the US regulators are expected to propose future rulemakings in the areas of capital and liquidity. As a result, the resulting scope of the competitive differences may not become entirely clear for some time.

[6] Basel III rules on liquidity, in particular, in relation to the "net stable funding ratio" liquidity buffer, are subject to possible change in the future, as discussed in the Basel Committee report "Basel III: The Liquidity Coverage Ratio and liquidity risk monitoring tools", January 2013.

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US/EU Comparison Table: Implementation of Basel III

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Glossary

TERM	DEFINITION	US OR EU-RELATED TERM
AOCI	Accumulated Other Comprehensive Income.	US
AT1	Additional Tier 1 capital.	Both
Advanced Approaches Banks	Refers to those US banks required to apply the internal model driven Advanced Approaches of Basel III.	US
BIS	The Bank for International Settlements.	Both
CCP	Central Counterparty. An entity that interposes itself as the counterparty to both the buyer and seller (or intermediaries thereof). Such transactions are considered to have a lower credit risk than bilateral transactions entered into with financial institutions.	Both
CDO	Collateralized Debt Obligation.	Both
CEIO	Credit Enhancing Interest Only Strip.	US
CET1	Common Equity Tier 1 capital.	Both
CIS	Collective Investment Scheme.	EU
Collins Amendment	Section 171 of the Dodd-Frank Act.	US
CRC	Country Risk Classification Codes assigned by the Organization for Economic Cooperation and Development.	Both
CRD	Capital Requirements Directive.	EU
CRD I	The First Capital Requirements Directive, which implemented the Basel II framework in the EU.	EU
CRD II	The Second Capital Requirements Directive, which amended the CRD I framework by strengthening requirements in relation to, inter alia, securitization, large exposures, and liquidity risk.	EU
CRD III	The Third Capital Requirements Directive, which further amended the CRD I framework and implemented Basel 2.5 in the EU and included further amendments relating to securitization, remuneration of FI employees and aspects of the market risk framework (including an Incremental Risk Charge and Stressed VaR).	EU
CRD IV	CRD and CRR are collectively referred to as CRD IV.	EU
CRR	Capital Requirements Regulation.	EU
CVA	Credit Valuation Adjustment. CVA risk is the risk that a firm will need to make an adjustment to the market value of an over the counter (OTC) derivative contract to take into account the deterioration in the creditworthiness of a counterparty.	Both
DTA	Deferred Tax Asset.	Both
DTL	Deferred Tax Liability.	Both
DvP	Delivery versus Payment. Securities or commodities transaction in which the buyer is obligated to make payment only if the seller has made delivery of the securities or commodities and the seller is obligated to deliver the securities or commodities only if the buyer has made payment.	Both
EBA	European Banking Authority.	EU
ECAI	External Credit Assessment Institution, i.e., credit rating agency.	EU
ECB	European Central Bank.	EU
Eligible Credit Derivatives	Refers to recognized credit derivatives for credit mitigation purposes under the US rules. Criteria includes: (i) for CDS or nth to default swap, the contract includes certain designated credit events, (ii) if the contract allows for cash settlement, the contract incorporates a robust valuation process, and (iii) if the credit derivative is a credit default swap or nth to default swap, the contract clearly identifies the parties responsible for determining whether a credit event has occurred.	US
Eligible	Refers to recognized guarantees for credit mitigation purposes under the US rules. Criteria include: (i) direct claim against the protection provider, (ii) protection provider makes payment to the beneficiary on the	US

TERM	DEFINITION	US OR EU-RELATED TERM
Guarantees	occurrence of a default (as defined in the guarantee) of the obligated party in a timely manner, (iii) does not increase the beneficiary's cost of credit protection on the guarantee in response to deterioration in the credit quality of the reference exposure, and (iv) is not provided by an affiliate (subject to certain exceptions).	
Eligible Guarantors	Refers to recognized guarantors for credit mitigation purposes under the US rules including: sovereign entities, Basel Committee, International Monetary Fund, European Central Bank, European Commission, Federal Home Loan Banks, Farmer Mac, a multilateral development bank, a depository institution, a bank holding company, a thrift holding company, a foreign bank, or an entity other than a special purpose entity that has investment grade debt, whose creditworthiness is not positively correlated with the credit risk of the exposures for which it provides guarantees and is not a monoline insurer or reinsurer.	US
EMIR	European Markets Infrastructure Regulation.	EU
ESCB	European System of Central Banks.	EU
FI	Under CRD IV, "financial institution" (i.e., EU credit institutions and EU investment firms).	EU
Financial Collateral	Refers to recognized collateral for credit mitigation purposes under the US proposed rules. Includes, cash on deposit at the banking organizations (or 3rd party custodian); gold; investment grade securities (excluding resecuritizations); publicly traded equity securities; publicly traded convertible bonds; money market mutual fund shares; and other mutual fund shares if a price is quoted daily. In all cases, the banking organization must have a perfected, 1st priority interest.	US
FX	Foreign Exchange.	Both
GAAP	Generally Accepted Accounting Principles.	Both
GSE	Government Sponsored Entity.	Both
HAMP	US Home Affordable Modification Program.	US
HVCRE Loans	High Volatility Commercial Real Estate Loans.	US
IRB approach	Internal Ratings-Based Approach. This is a method by which certain FIs calculate risk weightings using their own quantitative models. This is the EU equivalent of the "Advanced Approach" in the US.	EU
ITS	Implementing Technical Standards. ITS are technical standards generally developed by the EBA and formally adopted as legislative acts by the European Commission, which implement EU legislation by specifying how a particular requirement must be applied or enforced, such as specifying uniform formats, frequencies for reporting, and IT solutions (see also definition of "RTS" below).	
LCR	Liquidity Coverage Ratio.	Both
LGD	Loss Given Default. This is a variable used as part of the IRB Approach. This variable reflects the amount the FI would lose on a counterparty default.	Both
LTV	Loan to Value Ratio.	Both
MiFID	Markets in Financial Instruments Directive.	EU
MSRs	Mortgage Servicing Rights.	Both
NSFR	Net Stable Funding Ratio.	Both
OTC	Over-the-Counter. A transaction in an instrument that is negotiated and executed bilaterally, contrasting with exchange trading.	Both
PD	Probability of Default. This is a variable used as part of the IRB Approach and is the probability of default on a particular exposure.	EU
Private Sector Credit Exposures	In the US rules, Private Sector Credit Exposures refers to an exposure to a company or an individual that is included in credit risk weighted assets, not including an exposure to a sovereign, the Basel Committee, the European Central Bank, the European Commission, the International Monetary Fund, a multilateral development bank, a public sector entity, or a government sponsored enterprise.	US
PSE	Public Sector Entity.	Both
PvP	Payment versus Payment. Foreign exchange transaction in which each counterparty is obligated to make a final transfer of one or more currencies only if the other counterparty has made a final transfer of one or more currencies.	US

TERM	DEFINITION	US OR EU-RELATED TERM
Qualifying CCP	Qualifying Central Counterparty.	US
Qualifying Master Netting Agreements	Refers to a written, legally enforceable netting agreement that meets certain criteria required for recognition of netting under the US rules. Criteria include: (i) single legal obligation for all individual transactions covered, (ii) the banking organization has the right to accelerate, terminate, and close out on a net basis all transactions under the agreement, (iii) sufficient legal review is performed to conclude enforceability, (iv) procedures are in place to monitor possible changes in relevant law and to ensure that the agreement continues to satisfy the requirements, and (v) the agreement does not contain a "walkaway" clause.	US
RTS	Regulatory Technical Standards. These are technical standards generally developed by the EBA and formally adopted as legislative acts by the European Commission, which "flesh out" certain non-essential technical aspects of CRD IV, such as clarifying definitions (see also definition of "ITS" above).	EU
RWA	Risk Weighted Asset.	Both
SLHC	Savings and loan holding company.	US
SPV	Special Purpose Vehicle.	Both
SSFA	Simplified Supervisory Formula Approach is an approach to calculating risk weights for securitization positions. The risk weight is based on the risk weight applicable to the underlying exposures, the relative position of the securitization position in the structure (subordination), and measures of delinquency and loss on the securitized assets.	US
T2	Tier 2 capital.	Both
TARP	Troubled Asset Relief Program.	US

Scope of Application

<table>
<tr><th>ISSUE</th><th>US APPROACH</th><th>EU APPROACH</th></tr>
<tr><td rowspan="2">General coverage of the Basel framework</td><td>Institutions covered:
▪ US banks.
▪ US thrifts.
▪ US bank holding companies (with over $500 million in assets).
▪ US savings & loan holding companies.
Rules apply on a consolidated basis.
(Subpart A, Section 1 Final US Rules).</td><td>Institutions covered:
▪ all EU credit institutions (deposit taking banks).
▪ all EU investment firms
(Art 2 CRD, Art 1 CRR).
Requirements generally apply on both a solo and consolidated basis with discretion for national regulators to waive solo capital, leverage, and liquidity requirements in certain limited circumstances.</td></tr>
<tr><td colspan="2">Key differences/comments
▪ EU requirements apply to investment firms in addition to banking groups.
▪ “Investment firms” in the EU would include institutions that conduct securities brokerage/dealing activities and advisory firms. In general, the CRD IV regime applies to a much lesser extent to advisers and brokers as such firms do not generally assume credit or market risks against which capital must be held.</td></tr>
<tr><td rowspan="2">Application to the largest/most complex banks</td><td>Must comply with all general requirements; in addition, the following apply only to Advanced Approaches Banks:
▪ Advanced Approaches method of risk weighting.
▪ “Supplementary Leverage Ratio”.
▪ Countercyclical capital buffer.
▪ Special disclosure requirements relating to AT1 and T2 regulatory capital instruments.
▪ Advanced Approaches Banks will not be permitted to hold less capital than would similarly situated banks that are not Advanced Approaches Banks (“Collins Amendment”).
Special disclosure requirements related to regulatory capital instruments apply only to institutions with over US $50 billion assets.
(Subpart C, Sections 61–63 Final US Rules).</td><td>Broadly, all firms to comply with all requirements set out in CRD IV.
Each member state will also have the flexibility to introduce a systemic risk buffer, also to be met with CET1 capital, which may be applied to the financial sector or to one or more subsets of the sector. Member states will be able to apply systemic risk buffers of up to 3 per cent. for all exposures and up to 5 per cent. for domestic and third country exposures, without having to seek prior Commission approval, while they could impose even higher buffers with prior Commission authorisation in the form of a delegated act. If a member state decides to impose a buffer of up to 3 per cent. for all exposures, the buffer has to be set equally on all exposures located within the EU
(Arts 128 – 142, Art 160 CRD).</td></tr>
<tr><td colspan="2">Key differences/comments
▪ EU requirements generally do not differentiate according to size (although some exemptions are optional for individual Member States to implement, such as an optional exemption for small and medium investment firms from additional capital buffers) (Art 129(2) CRD and Art 130(2) CRD).
▪ In the EU, the level of the countercyclical capital buffer will be at the discretion of national regulators (Arts 135-136 CRD, Art 440 CRR).</td></tr>
<tr><td rowspan="2">Application to other (smaller) institutions</td><td>Institutions (other than Advanced Approaches Banks) must comply with general US Basel III requirements (but not Advanced Approaches Bank specific requirements).
In general, bank holding companies with pro forma consolidated assets of less than $500 million are not covered by the US Basel III requirements
(Subpart A, Section 1 Final US Rules).</td><td>Certain investment firms that do not assume principal risk can hold capital by reference to credit and market risk components or 12.5x quarter of the preceding year’s fixed overheads. Other firms without a license to deal on their own account or underwrite on a firm commitment basis are required to hold capital in an amount of the sum of those two measures
(Art 95-98 CRR and Art 29 CRD).</td></tr>
<tr><td colspan="2">Key differences/comments
▪ In the EU, only investment firms that (broadly speaking) do not assume principal risk benefit from a lower measure of capital (for example, advisory firms, or executing brokers (Art 29 CRD, Art 96 CRR).
▪ Certain firms in the EU, broadly “investment advice only” firms that do not hold client money, may be excluded from the CRD regime by virtue of an optional exemption from MiFID available to individual EU Member States (Art 96(1)(b) CRR). These optional exemptions are also currently present in the EU Commission’s MiFID II proposals.
▪ In the US, applies to a broad range of banks, including many community banks.</td></tr>
</table>

<table>
<tr><th>ISSUE</th><th>US APPROACH</th><th>EU APPROACH</th></tr>
<tr><td rowspan="2">Form of implementation of Basel III in US and EU</td><td>The capital rules have been implemented through a joint final rule of the US Federal banking agencies.[7]</td><td>Basel framework implemented in the EU via two legislative acts: the Capital Requirements Regulation and a Capital Requirements Directive, both of which amend and consolidate existing EU legislation.

<u>CRR</u>: Legislation applicable across EU in exactly the same form; a “single rule book”. The CRR contains provisions implementing capital, liquidity, and leverage requirements.

<u>CRD</u>: Legislation covering matters where national supervisory discretion is required which takes the form of a binding “instruction” to EU Member States to implement certain requirements by January 1, 2014. This confers greater flexibility on EU Member States in implementing certain Basel III requirements, including as to capital conservation and countercyclical capital buffers, prudential supervision, and certain leverage requirements.</td></tr>
<tr><td colspan="2">Key differences/comments
▪ Due to the fact that CRD is a Directive and requires Member State implementation, there may be divergence in implementation. Recital 41 CRD notes that “Member States should be able to provide for additional penalties to, and higher levels of administrative pecuniary penalties than those provided for in this Directive. Member States may not “gold plate” own funds requirements.</td></tr>
<tr><td rowspan="2">Integration of the Basel framework into the national supervisory framework</td><td>Ratios are widely used as triggers/qualification criteria as part of the supervisory framework:
▪ “prompt corrective action” requirements.
▪ “financial holding company” election.
▪ establishment of a financial subsidiary;
▪ M&A and other regulatory approvals.</td><td>Under CRD IV national supervisors are generally responsible for prudential supervision of FIs in their jurisdiction. This may change, however, if the ECB is made prudential supervisor of banks in the Eurozone.</td></tr>
<tr><td colspan="2">Key differences/comments
▪ In the EU, there is a proposed EU Recovery and Resolution Directive whereby firms experiencing distress will be subject, if triggers are breached, to bail in of debt, capital raising, or other measures. In addition, national regulators are able to impose more stringent capital requirements in certain circumstances (including through the countercyclical capital buffers and any systemic risk and Pillar II buffers).
▪ US Federal banking agencies reserve the authority to require a banking organization to hold a different amount of regulatory capital from what otherwise would be required under the minimum capital requirements.</td></tr>
</table>

[7] The Final US Rules are available on the Federal Reserve’s website at, http://www.federalreserve.gov/bcreg20130702a.pdf. The FDIC recently published its interim final rule implementing Basel III in the Federal Register at 78 Fed. Reg. 55340 (Sept. 10, 2013). Citations to particular sections of the Final US Rules in this client publication are to the subpart and section of the US Final Rules, as set out in the version of the US Final Rules available on the Federal Reserve’s website.

Definition of Regulatory Capital

ISSUE	US APPROACH	EU APPROACH
	Capital Components/Eligibility Criteria	
Common Equity Tier 1 capital	▪ Ordinary common equity capital instruments (net of treasury stock) that satisfy 13 specified criteria and related surplus. ▪ Retained earnings. ▪ Accumulated other comprehensive income. ▪ Qualifying CET1 minority interests in consolidated subsidiaries. (Subpart C, Section 20(b) Final US Rules).	▪ Capital instruments satisfying specified criteria, typically ordinary shares or the equivalent thereof and related share premium accounts. ▪ Retained earnings. ▪ Accumulated other comprehensive income. ▪ Other reserves. ▪ Funds for general banking risk. ▪ Qualifying CET1 minority interests in consolidated subsidiaries. ▪ Each of the above will constitute CET1 only where they are available to the institution for unrestricted and immediate use to cover risks or losses as soon as these occur (Art 26 CRR).
	Key differences/comments ▪ The above are subject to regulatory adjustments and deductions, but the constituent parts of CET1 are materially the same under US and EU approaches.	

Additional Tier 1 capital	▪ AT1 capital instruments that satisfy 14 specified criteria and related surplus (generally, non-cumulative perpetual preferred stock).
	  ▪ Specifically, such instruments are required to be perpetual instruments subordinated to Tier 2 instruments, in general, with restricted right of redemption only after five years from point of issue, but with no incentive to redeem; dividends cancelable and non-cumulative and with no dividend pushers/stoppers (except dividend stoppers with respect to common stock).
	▪ Qualifying AT1 minority interest that is not included in a banking organization's CET1 capital.
	▪ No requirement to write off or convert to common equity at the point of "non-viability".
	▪ Advanced Approaches Banks must disclose that holders may be subordinated to interests held by US government under US law.
	(Subpart C, Section 20(c) Final US Rules).
		▪ Capital instruments satisfying certain criteria (generally, non-cumulative perpetual preferred stock) and related retained earnings and share premium accounts
		(Arts 51 and 52 CRR).
		  ▪ Specifically, such instruments are required to be perpetual instruments subordinated to T2 instruments with restricted right of redemption after five years from point of issue, but with no incentive to redeem; dividends cancelable and non-cumulative, and with no dividend pushers/stoppers (except dividend stoppers with respect to common stock)
		  (Art 52 CRR).
		▪ Instruments subject to write-down or conversion into CET1 when CET1 capital falls below 5.125 per cent. or higher percentage specified in AT1 instrument
		(Art 54 CRR).
		▪ Qualifying AT1 minority interests in consolidated subsidiaries are also included
		(Art 81 CRR).

	Key differences/comments ▪ The criteria differ from – and are stricter than – the previous Tier 1 capital qualification standards. Recognition of outstanding instruments that no longer qualify as Tier 1 capital will generally be phased out over time. Outstanding Tier 1 instruments in the US and EU should be evaluated against the new qualification standards. ▪ The US/EU AT1 requirements set out above are subject to regulatory adjustments and deductions, for example, own holdings in AT1 instruments. ▪ In the US, instruments need not include a mandatory write off or conversion provision triggered at the point of "non-viability", unlike in the EU where there will be a mandatory write down or conversion provision. ▪ In the US, AT1 instruments issued under the TARP program are grandfathered permanently. ▪ In the EU, AT1 instruments are subject to fewer requirements relating to dividends.	
Tier 2 capital	▪ Capital instruments that satisfy 11 criteria and related surplus (principally subordinated debt and certain preferred instruments with a minimum original maturity of at least five years). ▪ T2 instruments are required to be subordinated, with maturity in excess of five years, no incentive to	▪ T2 instruments are required to be subordinated, with maturity in excess of five years, no incentive to redeem and redemption permitted only in limited circumstances after five years from date of issue; dividend/interest payments not to be modified based on the credit standing of FI/FI's parent; and instruments qualification for T2 purposes reduces pro rata in the final five years

ISSUE	US APPROACH	EU APPROACH
	redeem and redemption permitted only in limited circumstances after five years from date of issue; dividend/interest payments not to be modified based on credit standing of issuer/issuers' parent; and instrument's qualification for T2 purposes reduces pro rata in the final five years of maturity. ▪ Qualifying minority interests of consolidated subsidiaries not included in a banking organization's Tier 1 capital. ▪ Limited amounts of allowance for loan and lease losses (Advanced Approaches Banks may instead include a limited amount (0.06 of credit risk weighted assets) of the excess of eligible credit reserves over its total expected credit losses). ▪ For a bank that makes an AOCI opt-out election, 45% of unrealized gains on AFS equity securities. ▪ Advanced Approaches Banks must disclose that holders may be subordinated to interests held by the US government under US law. (Subpart C, Section 20(d) Final US Rules).	of maturity (Arts 63 and 64 CRR). ▪ Qualifying T2 capital and related retained earnings (Art 82 CRR) and share premium accounts of consolidated subsidiaries (Art 62(b) CRR). ▪ T2 instruments not subject to requirement for write down to CET1. Only AT1 subject to write-down to CET1 (Arts 54(2) and 54(4)(c) CRR).
	Key differences/comments ▪ The criteria differ from—and are stricter than—the existing T2 capital qualification standards. Recognition of outstanding instruments that no longer qualify as T2 capital will generally be phased out over time. Outstanding T2 instruments in the US and EU should be evaluated against the new qualification standards. ▪ In US, instruments need not include a mandatory write off or conversion provision triggered at the point of "non-viability". Similarly, in the EU, the CRR does not require that T2 instruments have a write off or conversion provision, but note that bail in requirements under the proposed EU Recovery and Resolution Directive will apply to such instruments. ▪ Consistent with Basel III, sub categories of "T2" capital are eliminated under both US and EU rules. ▪ The foregoing is subject to regulatory adjustments and deductions, for example, own holdings in T2 instruments.	
Tier 3 capital	Eliminated.	Eliminated.
CET1, AT1 and T2 instruments issued by subsidiaries and held by non-consolidated entities (minority interests)	<u>CET1</u>: ▪ The issuing entity must be a depository institution or foreign bank. ▪ The amount of recognized CET1 is limited – would not be permitted to include the portion of the "surplus" CET1 held by third party investors. (Subpart C, Section 21(c) Final US Rules). <u>AT1 and T2</u>: ▪ The amount of recognized AT1/T2 is limited – would not be permitted to include the portion of the "surplus" AT1/T2 held by third party investors. ▪ May include certain REIT preferred capital instruments (where the issuer is an operating company and the instruments otherwise qualify as AT1/T2) including ability to cancel dividends. (Subpart C, Sections 21(d), (e) Final US Rules).	▪ The issuing entity must be a FI (Art 81). ▪ Such minority interests to comprise CET1, AT1, and T2 as applicable if: the subsidiary is an undertaking subject to CRD IV, is consolidated, and the relevant instruments are owned by persons other than those included within the consolidation (Art 81-82 CRR). ▪ Minority interests funded directly or indirectly through SPVs of any parent or subsidiary undertaking of the FI will not qualify as consolidated CET1, AT1, or T2 (Art 81 CRR). ▪ Amount of recognized minority interest is pro rata CET1 of the subsidiary minus surplus above minimum CET1 levels (including the capital conservation and countercyclical capital buffers, and any systemic risk and Pillar II buffers) (Art 84).
	Key differences/comments ▪ Both US and EU approaches are broadly consistent with Basel III. EU proposals do not address MSRs as a constituent of capital or as a deduction.	

ISSUE	US APPROACH	EU APPROACH

Qualifying holdings outside the financial sector	▪ No generally applicable deduction for holdings in companies outside of the financial sector (as is the case under existing US law). Holdings to be treated as equity exposures subject to varying risk weights (see Equity Exposures below).
	▪ Special deduction for investments, including extensions of credit, in subsidiaries of thrifts that engage in activities impermissible for national banks.
	(12.C.F.R. 3.22(a)(8) and 12.C.F.R. 324.22(a)(8)).
		▪ National supervisors in EU Member States to be given the flexibility to either apply a 1250 per cent. risk weight to (or alternatively deduct) the greater amount of the following (or to prohibit such holdings):
		  ▪ the amount of any holding in a non-FI above 15 per cent. of the FI's capital.
		  ▪ the total amount of holding in non-FIs that exceed 60% of the FI's capital
		(Art 89(3) CRR).
		▪ For smaller holdings, the risk weight is determined according to the Standardized Approach or IRB Approach for equity exposures
		(Arts 108-110 CRR).

	Key differences/comments ▪ The EU approach generally follows Basel II which is unchanged in this respect under Basel III.	
Grandfathering of existing capital instruments that would no longer qualify as the same type of regulatory capital	<u>For banks with less than $15 billion in assets as of December 31, 2009</u>: Limited grandfathering of non-qualifying AT1 and T2 capital instruments issued prior to May 19, 2010. (Subpart C, Section 22(c) Final US Rules). <u>For banks with $15 billion or more in assets as of December 31, 2009</u>: Limited grandfathering of non-qualifying AT1 and T2 capital instruments issued prior to May 19, 2010 subject to phase-out provisions. ▪ Capital investments by the US government in banking groups are grandfathered permanently. (Subpart G, Section 300(c) Final US Rules).	<u>All FIs</u>: CET1, AT1, and T2 non-qualifying capital instruments issued prior to December 31, 2011, to be phased out commencing on January 1, 2014, and decreasing each year on January 1 every succeeding year in defined increments, ending December 31, 2021 (Arts 484-486 CRR).
	Key differences/comments ▪ For large banks, US has adopted much shorter timeframe than the EU to phase out "hybrid" capital instruments. ▪ The US approach to permanently grandfather capital investments made by the US government is a departure from the Basel III approach.	
Approval of new capital elements	Banks may request agency review/approval for inclusion of a new capital element in regulatory capital (whether CET1, AT1, or T2 capital). (Subpart C, Section 22(c) Final US Rules).	No ability in the CRR to recognize capital instruments that do not meet prescribed criteria as regulatory capital.
	Key differences/comments ▪ In theory, the US approach is more flexible and goes beyond Basel III.	
	Deductions from Capital and Other Adjustments	
Losses for current financial year	Losses are reflected in retained earnings, and thus, CET1 as well.	Deducted from CET1 (Art 36 CRR). EBA mandated to publish RTS to specify further detail.
	Key differences/comments ▪ No material difference between the US and EU approaches.	
Intangible assets	Required to deduct (other than MSRs which are subject to separate rules) and amount deducted is reduced by associated deferred tax liabilities.	Required to deduct. Amount deducted to be reduced by associated deferred tax liabilities that would be extinguished due to impairment or being derecognized under applicable accounting standards (Art 36 CRR).
	Key differences/comments ▪ Both US and EU approaches are broadly consistent with Basel III.	

ISSUE	US APPROACH	EU APPROACH
Negative amounts arising from expected credit loss amounts (for Advanced Approaches Banks/IRB banks)	Advanced Approaches Banks only: Required to deduct the amount of expected credit loss that exceeds eligible credit reserves. Expected credit loss includes expected credit losses on wholesale and retail exposures (Subpart C, Section 22(a) Final US Rules).	IRB banks only: Required to deduct negative amounts resulting from the calculation of expected loss amounts under the IRB Approach (Art 36(1)(d) CRR). Expected loss amounts not to be reduced by a rise in DTAs that rely on future profitability, or other additional tax effect, that could occur if provisions were to rise to a certain level (Art 36(1)(c) CRR, Art 40 CRR).
	Key differences/comments ▪ Both US and EU approaches are generally consistent with Basel III. ▪ The US definition of expected credit loss deviates from the Basel definition of expected loss as regards wholesale and retail exposures.	
Deferred tax assets reliant on future profitability	Required to deduct from CET1. Deduction may be reduced by associated deferred tax liabilities in relation to the same taxation authority subject to certain limitations. (Subpart C, Section 22(d) Final US Rules).	Required to deduct from CET1 subject to deduction threshold (together with significant investment holdings deduction, see further below) (Art 48 CRR). Deduction may be reduced by associated deferred tax liabilities if there is a legally enforceable right under national law to set off such liabilities (Art 37-Art 38 CRR). Tax overpayments and current year tax losses referable to previous years are not deductible (Art 39 CRR).
	Key differences/comments ▪ The US approach is consistent with Basel III and the EU approach has certain differences (see threshold exemptions from deductions below).	
Deferred tax assets arising from temporary differences	DTAs that cannot be realized through net operating loss carrybacks: Limited recognition subject to "threshold deduction" caps (together with significant financial investment holdings and MSRs); may be reduced by associated deferred tax liabilities in relation to the same taxation authority subject to certain limitations. Where recognized, a risk weighting of 250% is to be applied. (Subpart C, Section 22(d) Final US Rules). DTAs that can be realized through net operating loss carrybacks: No deduction – 100% risk weighting.	Recognition in limited circumstances: (i) where automatic tax credit in the event of loss; (ii) permitted to offset tax credit against tax liability; and (iii) if tax credits exceed tax liabilities, a direct claim on central government is available. Where recognized, a risk weighting of 100% is to be applied, otherwise deducted. Note that this deduction is subject to the threshold exemption set out below (where the threshold is exceeded, a risk weighting of 250% applies) (Art 39 CRR).
	Key differences/comments ▪ Both US and EU approaches are generally consistent with Basel III. ▪ To the extent DTAs that cannot be realized through net operating loss carrybacks are recognized, US would apply a greater risk weighting commencing in 2018.	
Defined benefit pension fund assets	(For an institution that is not an insured depository institution), required to deduct unless the institution has unrestricted/unfettered access to the assets; amount to be deducted to be reduced by the amount of associated deferred tax liabilities. (Subpart C, Section 22(a) Final US Rules).	Deducted, but reduced by the amount that is subject to unrestricted use and by the amount of associated deferred tax liabilities due to impairment or being derecognized under the applicable accounting standard (Art 36 CRR).
	Key differences/comments ▪ Both US and EU approaches are generally consistent with Basel III.	
Holdings of own capital instruments	Required to deduct all direct, indirect and synthetic holdings in CET1, AT1, and T2 including in relation to index securities. May calculate on the basis of net long position if certain conditions have been met. (Subpart C, Section 22(c) Final US Rules).	Net long position in CET1, AT1, and T2 instruments deductible including holdings through positions in index securities (Arts 42, 57 and 67 CRR).
	Key differences/comments ▪ Both US and EU approaches are generally consistent with Basel III.	

<table>
<tr><th>ISSUE</th><th>US APPROACH</th><th>EU APPROACH</th></tr>
<tr><td rowspan="2">Significant investments in financial institutions</td><td>

Limited recognition of CET1 investments with recognition capped at 10% CET1 of the investing bank and aggregate limitation of 15% CET1 of the investing bank (when aggregated together with certain deferred tax assets and MSRs); amounts not deducted are subject to 250% risk weighting.
There is a significant investment where a banking organization owns more than 10% of the outstanding CET1 of an unconsolidated financial institution.
Underwriting positions held for five business days or less are exempt from the deduction.
Investments subject to the deduction include direct, indirect, and synthetic holdings of capital instruments (e.g., banks are required to look through holdings of index securities and investments in unconsolidated entities to determine their underlying holdings of capital).
Generally includes short term (“trading book”) and long term (“banking book”) shareholdings in financial institutions.
Also required to deduct AT1 and T2 holdings.

(Subpart C, Sections 22(c),(d) Final US Rules).</td><td>

Required to be deducted. Amounts not deducted are subject to a 250% risk weighting (see threshold exemption below) (Art 48(4) CRR).
There is a significant investment in an unconsolidated financial institution where a holding exceeds 10% of the CET1 instruments issued by that financial institution (Art 43(a) CRR) or where there are “close links” (a 20% interest) with the FI (Art 43(b) CRR) or such FI is part of accounting but not prudential consolidation (Art 43(c) CRR).
Underwriting positions held for five business days or less are exempt from the deduction (Art 47 CRR).
Includes direct, indirect, and synthetic holdings.
Generally includes short term (“trading book”) (Art 4(1) CRD) and long term (“banking book”) shareholdings in FIs.
Also required to deduct AT1 and T2 holdings

(Arts 36, 48, 68, 69 CRR).</td></tr>
<tr><td colspan="2">Key differences/comments

The CRR includes an alternative of consolidation rather than deduction from CET1 in relation to significant investments in insurers (Art 49 CRR). The Basel Committee has highlighted that there is no requirement in the CRR for the consolidation alternative to be as stringent as the deduction option in Art 47 CRR.
US: The US employs a broad definition of “financial institutions” including companies predominantly engaged in certain financial activities (i.e., 85% or more of the consolidated total assets or gross revenues are derived from financial activities).
EU: The specific meaning of the term “financial institution” for these purposes is to be determined by each Basel member country; CRD IV includes a wide variety of financial institutions including banks, broker dealers, hedge fund managers, and other asset managers.
</td></tr>
<tr><td rowspan="2">Holdings of capital instruments of financial institutions where there is a reciprocal cross-holding designed to inflate regulatory capital</td><td>Gross long positions of such holdings are deducted in the case of CET1, AT1, and T2 instruments.</td><td>Gross long positions of such holdings are deducted in the case of CET1, AT1, and T2 instruments.</td></tr>
<tr><td colspan="2">Key differences/comments

US and EU approaches are generally consistent with Basel III.
</td></tr>
<tr><td>Holdings of non-significant investments in financial institutions</td><td>

Banking organizations are required to deduct if aggregate holdings of CET1, AT1, and T2 in financial institutions (where there is no significant investment) exceed 10% of the investing institution’s CET1.
A non-significant investment in an unconsolidated financial entity is where a banking organization owns 10% or less of the outstanding CET1 of such entity.
A corresponding deduction approach is to be applied, e.g. pro rata amount of AT1 holdings should be deducted from the financial institution’s AT1.
Underwriting positions held for five business days or less are exempt from the deduction.
Investments subject to the deduction include direct, indirect, and synthetic holdings of capital instruments (e.g., banks are required to look through holdings of index securities to determine their underlying holdings of capital).
Both short term (“trading book”) and long term (“banking book”) shareholdings of financial institutions are generally included.

(Subpart C, Section 22(c) Final US Rules).</td><td>

Required to deduct if aggregate holdings of CET1, AT1, and T2 in financial institutions (where there is no significant investment) exceed 10% of the investing FI’s CET1

(Arts 46, 60, and 70 CRR).

A non-significant investment in an unconsolidated entity is where an institution owns 10% or less of the outstanding CET1 of such entity.
A corresponding deduction approach is to be applied, e.g. pro rata amount of AT1 holdings should be deducted from the financial institution’s AT1.
Underwriting positions held for five business days or less are exempt from the deduction.
Investments subject to the deduction include direct, indirect, and synthetic holdings of capital instruments (e.g., banks are required to look through holdings of index securities to determine their underlying holdings of capital).
</td></tr>
</table>

ISSUE	US APPROACH	EU APPROACH
	Key differences/comments ▪ The US and EU approaches largely follow the Basel III approach which is unchanged from Basel II. ▪ See "Significant investments in financial institutions" above for additional considerations.	
Investments in hedge/private equity funds	Required to deduct investments in private funds "organized and offered" by the investing banking institution.	See risks weighting applied to "high risk" items.
	Key differences/comments ▪ Final Volcker Rule regulations implementing the deduction have yet to be issued.	
Threshold deductions	▪ Items subject to threshold deduction include: Significant investments (i.e., more than 10%) in financial institutions, MSRs, and DTAs that arise from temporary differences that cannot be realized through net operating loss carrybacks. ▪ Mandatory deduction to the extent any of the items individually exceed 10% CET1 and mandatory deduction to the extent in the aggregate these items exceed 15% of CET1. ▪ Items not deducted are to be given a 250% risk weighting.	▪ Items subject to threshold deduction include: Significant investments in financial institutions and DTAs that arise from temporary differences (Art 48(1)(a) and (b) CRR). ▪ Exemption from deduction to the extent these items individually are equal to or less than 10% CET1 of the FI and to the extent in the aggregate these items are equal to or less than 15% of CET1. ▪ Items exempt from deduction are to be given a 250% risk weighting (Art 58(4) CRR). MSRs are not included within the threshold exemption (and are not otherwise referred to in the CRR).
	Key differences/comments ▪ In the EU, MSRs are not included within the threshold deduction and DTAs reliant upon future profitability are included with the exemption. The EU rules differ from Basel III in both these respects.	
Gain on sale associated with a securitization exposure	Deducted (other than increase in equity capital resulting from receipt of cash). (Subpart C, Section 22(a) Final US Rules).	Deducted. Institutions shall derecognize in the calculation of CET1 any increase in equity capital resulting from a securitization transaction, such as that associated with expected future margin income resulting in a gain-on-sale (Art 32 CRR). EBA has published draft RTS on this point (EBA/RTS/2013/03 on the concept of Gain on Sale associated with future margin income in a securitisation context "Gain on Sales RTS").
	Key differences/comments ▪ Both US and EU approaches are consistent with Basel III.	
Changes in the banking organization's creditworthiness	▪ Required to deduct any unrealized gain from and add back any unrealized loss due to changes in a banking organization's creditworthiness. ▪ Advanced Approaches Banks: Deduct from CET1 any unrealized gains associated with derivative liabilities resulting from the widening of a banking organization's credit spread premium over the risk free rate. (Subpart C, Section 22(b) Final US Rules).	▪ FIs are not permitted to include any gains or losses on their liabilities resulting from changes in the creditworthiness of that FI, except where such gains and losses are offset by changes in the value of another financial instrument measured at fair value resulting from changes in own credit standing of FI (Art 33 CRR).
	Key differences/comments ▪ The EU approach in allowing recognition of certain gains and losses deviates from Basel III and has been criticized by the Basel Committee as potentially being material for a firm in financial difficulty that has attempted to hedge its own credit position.	
Adjustment – requiring unrealized gains and losses on investment securities to flow through to capital	Proposed Volcker Rule would require deduction of investments in private funds "organized and offered" by the investing banking institution pursuant to the Volcker Rule.	See risks weighting applied to "high risk" items below.
	Key differences/comments ▪ Final Volcker Rule regulations implementing the deduction have yet to be issued.	

ISSUE	US APPROACH	EU APPROACH
Investments in hedge/private equity funds	▪ Unrealized gains and losses on "available for sale" securities are reflected in CET1. ▪ Non-Advanced Approaches Banks may make a one-time permanent election to continue the treatment of AOCI under current capital rules.	The Gain on Sales RTS (referred to above) sets out how unrealized gains and losses in relation to various items, including unrealized gains and losses on "available for sale" securities, will be reflected in capital.
	Key differences/comments ▪ The US agencies have responded to comments by allowing non-Advanced Approaches Banks to make a one-time election to opt out of the AOCI treatment under the new rules. (Subpart C, Section 22(b) Final US Rules).	
Adjustment – treatment of cash flow hedges	All Advanced Approaches Banks and banks that elect to include AOCI in regulatory capital, required to deduct any unrealized gain, and add any unrealized loss on cash flow hedges to CET1, net of applicable tax effects, which related to hedging of items that are not recognized at fair value on the balance sheet. (Subpart C, Section 22(b) Final US Rules).	Fair value reserves related to gains or losses on cash flow hedges of financial instruments that are not valued at fair value (including projected cash flows) <u>not</u> to be included in any element of capital (Art 33 CRR).
	Key differences/comments ▪ Both US and EU approaches are consistent with Basel III.	
	Effective Date/Phase-In	
Non-qualifying capital instruments	Non-Advanced Approaches Banks and Advanced Approaches Banks that are covered SLHCs must comply with new definitions of CET1, AT1, and T2 on January 1, 2015, with grandfathering provisions for certain non-qualifying existing capital instruments (as indicated above). All Advanced Approaches Banks must comply on January 1, 2014.	New definitions of CET1, AT1, and T2 in CRR (effective from January 1, 2014) and CRD (which requires implementation by Member States by December 31, 2013), with grandfathering provisions for certain non-qualifying existing capital instruments.
	Key differences/comments ▪ In the US, there is an accelerated phase out schedule for non-qualifying instruments issued by large banks and permanent grandfathering of investments in banking groups held by the US government.	
Deductions from capital and other adjustments	All regulatory capital adjustments and deductions fully phased in by January 1, 2018. Different transitional measures apply for different deductions. Goodwill will be deducted from CET1 immediately upon implementation. (Subpart C, Section 300(b) Final US Rules).	All regulatory capital adjustments and deductions fully phased in by January 1, 2018. Certain transitional measures apply, <u>e.g.</u> losses for the current financial year and intangible assets are subject to 15% cap until December 31, 2017 (Arts 469, 474, 476 CRR).
	Key differences/comments ▪ In the US, the full deduction for goodwill (net of any associated DTLs) is stricter than that under Basel III, which transitions the goodwill deduction from CET1 in line with the rest of the deductible items. In the EU, the deduction for goodwill is transitioned consistent with Basel III.	

Risk-Based Capital Requirements

ISSUE	US APPROACH	EU APPROACH
	Minimum Capital Ratios	
Common Equity Tier 1 capital ratio	Introduces a minimum requirement of 4.5% (phase for Advanced Approaches Banks that are not SLHCs in 2014 (4.0%) and 2015 (4.5%)). (Subpart B, Section 10 Final US Rules).	CET1 to increase from 2% to 4.5% (Art 92 CRR).
	Key differences/comments ▪ Both US and EU approaches are consistent with Basel III.	
Overall Tier 1 capital ratio	Increases the minimum requirement from 4% to 6% (by 2015). (Subpart B, Section 10 Final US Rules).	Overall T1 minimum requirement to increase from 4% to 6% (Art 92 CRR).
	Key differences/comments ▪ Both US and EU approaches are consistent with Basel III.	
Tier 2 capital ratio	No specific requirement imposed.	No specific requirement imposed.
	Key differences/comments ▪ Both US and EU approaches are consistent with Basel III.	
Total capital ratio (Tier 1 and Tier 2)	Minimum unchanged (remains at 8%). (Subpart B, Section 10 Final US Rules).	Minimum unchanged (remains at 8%) (Art 92(1)(c) CRR).
	Key differences/comments ▪ Both US and EU approaches are consistent with Basel III.	
	Capital Buffers	
Capital conservation buffer	Size: Must be in an amount of CET1 greater than 2.5% of total RWAs to avoid pay out restrictions following phase in: 2016 (0.625%), 2017 (1.25%), 2018 (1.875%), and 2019 (2.5%). (Subpart B, Section 11(a) Final US Rules). Elements subject to pay out restriction: Discretionary bonus payments for executive officers and the following capital distributions restricted if capital conservation buffer does not exceed 2.5%: ▪ repurchase of T1 or T2 instruments. ▪ dividend declaration on T1 capital instrument. ▪ discretionary dividend declaration or interest payment on T2 capital. ▪ any similar transaction that the agencies determine to be in substance a distribution of capital. (Subpart B, Section 11(a) Final US Rules). Method to determine maximum pay out amount on bonuses/distributions: Determined by reference to the amount by which the banking organization's CET1 exceeds the minimum CET1 requirement and the banking institution's capital conservation buffer in the previous quarter and "eligible retained income"; i.e., adjusted net income for the four calendar quarters preceding the current calendar quarter. (Subpart B, Section 11(a) Final US Rules).	All FIs: To be implemented under CRD IV. Capital conservation buffer to be 2.5% CET1 when fully implemented (Art 129 CRD). Phase in: 2016 (0.625%), 2017 (1.25%), 2018 (1.875%), and 2019 (2.5%) (Art 160 CRD). Measures to be applied in the event that FIs fail to meet the capital conservation buffer requirement will extend to restrictions in dividends, bonuses, and distributions on AT1 instruments (Art 141 CRD), and will ultimately depend on the approach taken by national supervisors in individual EU Member States (Art 142 CRD). The maximum amount available for distribution for bonuses and dividends is determined by a formula based upon the extent to which the FI's CET1 exceeds the minimum CET1 requirement (minimum includes the capital conservation and countercyclical capital buffer) (Art 141 CRD).
	Key differences/comments ▪ In the EU, where a buffer falls below the prescribed minimum restrictions on distributions and bonuses would depend on the individual approaches of EU Member States. ▪ In the US, a US Federal banking agency has discretion (which is not provided under the Basel III framework) to allow	

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	exceptions to pay out restrictions if the agency determines that the distribution is not contrary to the purposes of the capital conservation buffer framework or to the safety and soundness of the bank.	
Countercyclical capital buffer	<u>Application</u>: US buffer may apply only to Advanced Approaches Banks. (Subpart B, Section 11(b) Final US Rules). <u>Size</u>: 0 2.5% of CET1. <u>Application Trigger</u>: For the US, Federal Reserve, OCC, and FDIC make joint determinations based on the condition of the overall US financial system (no one factor is determinative). (Subpart B, Section 11(b) Final US Rules). <u>Elements subject to pay out restriction and determination of maximum pay out amount</u>: Elements subject to pay out restriction are the same as for the capital conservation buffer. An Advanced Approaches Bank's maximum payout ratio would vary depending on its capital conservation buffer and countercyclical buffer amount. (Subpart B, Section 11(b) Final US Rules).	<u>All FIs</u>: Also to be implemented as part of CRD IV (Art 130 CRD). <u>Size</u>: 0 2.5%, of CET1 (Art 136(4) CRD), although a buffer of greater than 2.5% may be imposed in certain scenarios (Art 137 CRD). <u>Application Trigger</u>: Buffer will be set by national supervisors in EU Member States and imposed in the event of perceived excessive credit growth within the financial system (Art 136 CRD). <u>Small and medium investment firm exemption</u>: An option is given to EU Member States to include an exemption for small and medium investment firms, as long as such exemption would not result in any threat to the financial stability of that EU Member State (Art 130(2) CRD).
	Key differences/comments ▪ US agencies have asked for comment on which approaches should be considered for purposes of determining whether/when to impose the countercyclical buffer (including whether a formula based approach might be appropriate). ▪ EU approach mirrors Basel III but buffer requirement is left to individual EU Member States and can therefore vary across the EU.	
Systemic risk buffer	Not addressed to date.	National supervisors in EU Member States have power to introduce an additional CET1 buffer across the financial sector or a subset of it. Systemic risk buffers of up to 3% CET1 (Art 133(11) CRD) for all exposures and up to 5% CET1 for domestic and third country exposures (Art 133(13) CRD), permitted without having to seek prior EU Commission approval (Art 133(11) CRD), and higher buffers permitted but with approval.
	Key differences/comments ▪ EU is ahead of the US in setting out measures for a systemic risk buffer. ▪ The UK government has committed to applying higher capital requirements to retail banks than required under Basel III. It is generally believed that the systemic risk buffer may provide flexibility for the UK government and other EU Member States to apply such higher capital requirements. However, the degree to which individual EU Member States will have flexibility to apply higher capital requirements remains unclear at this time.	
G SIB (Global Systemically Important Banks) surcharge	Not addressed to date.	The systemic risk buffer (see above) could be the vehicle through which the EU implements the Basel III requirement for an additional G SIB capital buffer. A mandatory systemic risk buffer comprising of CET1 capital for banks that are identified as "globally systemically important" on the basis of Basel Committee methodology for identifying G-SIBs. The identification criteria and the allocation into categories of "SIFI-ness" are in conformity the G-20 agreed G-SIFI criteria and include size, cross border activities, and interconnectedness. The mandatory surcharge will be between 1 and 3.5% CET 1 and apply from January 1, 2016 onwards (Art 131 CRD).
	Key differences/comments ▪ EU is ahead of the US in setting out measures for a systemic risk buffer.	

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	Asset Risk Weightings – General	
Alternative approaches	All Banks: All banks must apply the Standardized Approach. (Subpart D, Section 30, and Subpart A, Section 1(c) Final US Rules). Advanced Approaches Banks: Must apply and meet minimum risk-based capital standards under both the Standardized Approach and the Advanced Approach to risk weighting. (Subpart D, Section 30, Subpart E, Section 100 and Subpart A, Section 81(c) Final US Rules).	All FIs: FIs to apply the Standardized Approach, unless permission is given by a national supervisor to apply the IRB Approach (equivalent to the Advanced Approach) instead (Art 107(1) CRR).
	Key differences/comments ▪ Standardized and IRB Approaches are alternatives in the EU, whereas in the US, the Standardized Approach effectively operates as a floor to capital requirements for credit risk.	
References to external credit ratings	Not permissible under US law (Dodd-Frank Act). Section 939A of the Dodd-Frank Act requires all Federal agencies where feasible to remove references to, and requirements of, reliance on credit ratings from their regulations and replace them with appropriate alternatives for evaluating creditworthiness.	Use of external ratings to be permitted under CRD IV, but with an approach aimed at significantly reducing reliance on external ratings and increasing reliance on internal ratings (Recitals 70–73 CRD).
	Key differences/comments ▪ US prohibition on the use of credit ratings is a divergence from the Basel III accord.	
	Asset Risk Weightings – The Standardized Approach to Credit Risk	
	On Balance Sheet Assets	
Cash in hand	0% (Subpart D, Section 32(a) Final US Rules).	0% (Art 134(2) CRR).
	Key differences/comments ▪ Both US and EU approaches are consistent with Basel III.	
Exposures to sovereigns/central banks	US government/agencies/Federal Reserve: 0% or 20%, if a conditional claim. Non-US sovereigns: Risk weight depends on CRC applicable to the sovereign and ranges between 0% and 150%. 100% for non-OECD sovereigns that do not have a CRC. (Subpart D, Section 32(a) Final US Rules). 150% for a sovereign that has defaulted within the previous five years. (Subpart D, Section 32(a) Final US Rules).	EU central governments and central banks (same currency): Exposures to central governments and central banks of Member States denominated and funded in the domestic currency of that central government and central bank: 0% (Art 114(4) CRR). Until 2018, exposures denominated in another Member State currency will also be treated as a 0% exposure; in 2018, exposures will increase to 100% of risk weighting based on ECAI assessment (see below) (Art 114(5) and (6) CRR). Non-EU central governments and central banks: Exposures to other central governments and central banks: 0% to 150% depending on credit assessment by ECAI. If no ECAI rating exists, risk weighting is 100% (Art 114(7) CRR). European Central Bank: 0% (Art 114(3) CRR).
	Key differences/comments ▪ EU generally follows the Basel II approach, which is unchanged. The US relies upon CRCs for non-US sovereign and its approach differs from Basel II.	
Exposures to non-central government sector entities (PSEs)	US PSEs: 20% for general obligations; 50% for revenue obligations. (Subpart D, Section 32(e) Final US Rules). Non-US PSEs: Risk weight depends on the home	Regional governments or local authorities EU regional governments are treated the same as central governments (where no difference in risk). Third party regional governments and local authorities in jurisdictions with supervisory regimes equivalent to the EU's to be

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	country's CRC and ranges between 20% and 150% for general obligations, and between 50% and 150% for revenue obligations. ▪ 100% for exposures to a PSE in a non-OECD home country that does not have a CRC. ▪ 150% for a PSE in a home country with a sovereign default. (Subpart D, Section 32(f) Final US Rules).	treated the same as central government exposures. Exposures to regional governments or local authorities not within the scope of the foregoing to be assigned a risk weight of 20% (Art 115(5) CRR). PSEs PSEs in the EU to be given a risk weighting of between 20% and 150% depending on their credit rating assessment by a nominated ECAI or the rating of their central government. Exposures to PSEs with no rating (or sovereign rating) to be assigned a 100% risk weighting. All public sector entity exposures with an original maturity of 3 months or less to be assigned a 20% risk weighting. Non-EU PSEs may be treated as EU PSEs if the supervisory regime is equivalent to that of the EU's, otherwise a risk weighting of 100% will apply (Art 116 CRR).
	Key differences/comments ▪ US PSEs: The US risk weights do not take into account the potential downgrade of the US sovereign rating (and thus, differs from the Basel framework). ▪ Non-US PSEs: The US approach relies on CRC codes rather than external credit ratings (and thus, differs from the Basel framework).	
Exposures to multilateral development banks	Exposures to various multilateral development banks to be given 0% risk weighting. (Subpart D, Section 32(b) Final US Rules).	Exposures to various multilateral development banks to be given 0% risk weighting (Art 117 CRR).
	Key differences/comments ▪ US rules would apply a 0% risk weight to exposures to any multilateral lending institution or regional development bank in which the US government is a shareholder or contributing member.	
Exposures to international organizations	Exposures to the following international organizations to be assigned 0% risk weighting: ▪ The European Commission. ▪ International Monetary Fund. ▪ Bank for International Settlements. ▪ European Central Bank. (Subpart D, Section 32(b) Final US Rules).	Exposures to the following international organizations to be assigned 0% risk weighting (Art 118 CRR): ▪ European Union. ▪ International Monetary Fund. ▪ Bank for International Settlements. ▪ European Financial Stability Facility. ▪ European Stability Mechanism. ▪ "Rescue funds" created by a Member State or States for the benefit of another Member State or other Member States.
Exposures to financial institutions	US banks: 20%; 100% risk weight for an instrument included in the depository institution's regulatory capital (unless the instrument is an equity exposure or deduction treatment applies). (Subpart D, Section 32(d) Final US Rules). Non-US banks: Risk weight depends on home country's CRC rating and ranges between 20% and 150%. The weight applied to the bank would be one category less favorable than that applied to the sovereign country's risk weight. ▪ 100% for foreign bank whose non-OECD home country does not have a CRC. ▪ 150% in the case of a sovereign default in the bank's home country. ▪ 100% for an instrument included in a bank's regulatory capital (unless that instrument is an equity exposure or deduction treatment applies). (Subpart D, Section 32(d) Final US Rules).	All FIs: Exposures to FIs to be given a risk weighting of between 20% to 150% depending on the credit rating of the FI. The risk weighting will depend on the credit assessment rating of the FI according to a nominated ECAI. If an FI has no such rating, the risk weight will be based on the assessment given by a nominated ECAI in relation to the central government of the state in which the FI is incorporated. If there is no rating available, the risk weighting is 100%. Exposures to unrated FIs with an original effective maturity of three months or less to be assigned a risk weighting of at least 20% and one risk weight less than that ascribed to the sovereign of such FI (Art 120-121 CRR).

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	<u>Securities Firms</u> 100%. However, if the exposure is an instrument included in the capital of the securities firm, deduction treatment may apply. (Subpart D, Section 32(d) Final US Rules). <u>Other</u> 100% (for non-equity exposures). However, if the exposure is an instrument in the capital of the financial institution, deduction treatment may apply. (Subpart D, Section 32(d) Final US Rules).	
	Key differences/comments ▪ Unlike the EU approach, the US approach does not closely correspond to the Basel III framework. ▪ For US banks: the US approach does not take into account the potential downgrade of the US sovereign credit rating (and thus, differs from the Basel III framework). ▪ For non-US banks: the US approach relies on CRC codes rather than external credit ratings (and thus, differs from the Basel III framework).	
Exposures to non-financial corporates	100%. (Subpart D, Section 32(f) Final US Rules).	Exposures to corporates for which a credit rating assessment by a nominated ECAI is available will be risk weighted between 20% and 150% depending on the rating (Art 121 CRR). Exposures to unrated corporates to be either 100%, or the risk weight of exposures to the central government of the jurisdiction in which the corporate is located, whichever is higher (Art 121(2) CRR).
Loans secured by residential property	<u>Standard 30-year mortgages</u>: 50% for high quality seasoned mortgages; 100% for all other mortgages. <u>Multi-family properties</u>: 50% or 100% (if criteria in the regulation are not met). (Subpart D, Section 32(8) Final US Rules).	Exposures fully and completely secured by residential property subject to satisfying certain requirements to be assigned a 35% risk weighting (Art 125 CRR). National regulators will be required to periodically (at minimum, annually) review residential mortgage risk weightings (Art 101(a)-(c) CRR) and, if appropriate on the basis of financial stability reasons, set a risk weighting higher than 35% (up to 150%) (Art 124 CRR). <u>"Non-residential" mortgages</u>: If not within the scope of the above, 100% for exposures fully secured by a mortgage on immovable property that is not commercial property or residential property (Art 124 CRR).
	Key differences/comments ▪ The US rules appear to be significantly stricter than those of the EU. Whereas many interests secured by residential mortgage will be assigned a 35% risk weighting in the EU, the equivalent in the US would likely be assigned a higher risk weighting depending on LTV and whether the exposure is a "high quality" loan. The difference between the US and EU approaches may be less significant in practice, however, if national regulators in individual EU Member States exercise their discretion to increase risk weightings where deemed appropriate.	
Claims on modified/restructured residential property loans	<u>Modified Loans</u>: 100%. (Subpart D, Section 32(g) Final US Rules). <u>HAMP Loans</u>: Not treated as a restructured loan. (Subpart D, Section 32(g) Final US Rules).	No special rules for FIs.
Claims secured by commercial property	<u>HVCRE acquisition, development or construction loans</u>: 150%. (Subpart D, Section 32(j) Final US Rules).	Exposures fully and completely secured by commercial property within one of the following to be assigned a 50% risk weighting

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	<u>Other Loans</u>: 100%. (Subpart D, Section 32(l) Final US Rules).	(Art 126 CRR): ▪ mortgage on offices or other commercial premises. ▪ tenant under a property leasing transaction concerning offices or other commercial premises under which the FI is lessor and tenant has an option to purchase. ▪ certain other requirements set out at Article 121 of the CRR are met. National regulators will be required to periodically (at minimum, annually) review commercial mortgage risk weightings and, if appropriate on the basis of financial stability reasons, set a risk weighting higher than 50% (up to 150%) (Art 101(d)-(f) CRR). If not within the scope of the above, 100% for exposures fully secured by mortgage on immovable property that is not commercial or residential property (Art 124 CRR).
	Key differences/comments ▪ For certain types of commercial real estate loans, the EU rules assign a significantly lower risk weighting than the US. However, as with residential mortgage loans, the difference between the US and EU rules may be less significant in practice, if national regulators in individual EU Member States exercise their discretion to increase risk weightings where deemed appropriate.	
Exposures in default/past due	150% for the portion that is not guaranteed or secured by Financial Collateral/Eligible Guarantees/Eligible Credit Derivatives (does not apply to sovereign exposures or residential mortgage exposures). (Subpart D, Section 32(k) Final US Rules).	150%, where any specific credit risk adjustment is less than 20% of the unsecured exposure value (assuming that there was no such adjustment), and 100% if the credit risk adjustment is at least 20% of such exposure value (Art 127(1) CRR).
	Key differences/comments ▪ EU assigns a lower risk weighting (depending on proportion of exposure subject that is secured, guaranteed, or subject to other credit risk adjustment). ▪ Under the existing US general risk-based capital rules, the risk weight of a loan does not change if it becomes past due, with the exception of certain residential mortgage loans.	
Unsettled transactions (securities, FX and commodities)	<u>For DvP or PvP transactions</u>: Capital requirement is set at the difference between the agreed settlement price for the instrument in question and its current market value multiplied by a factor dependent upon the number of days until settlement takes place. ▪ 5 – 15 working days, 100%. ▪ 16 – 30 working days, 625%. ▪ 31 – 45 working days, 937.5%. ▪ 46 or more working days, 1,250%. (Subpart D, Section 38(d) Final US Rules). <u>For Non-DvP or Non-PvP transactions more than five days past the settlement date</u>: Capital requirement is based on the current market value of deliverables owed to the bank multiplied by 1,250%. The capital requirement for unsettled transactions would not apply to, among other transactions, cleared transactions that are marked to market daily and subject to daily receipt of variation margin. (Subpart D, Section 38(e) Final US Rules).	Capital requirement set at the difference between the agreed settlement price for the instrument in question and its current market value multiplied by a factor dependent upon number of days until settlement takes place. ▪ 5 – 15 working days, 8%. ▪ 16 – 30 working days, 50%. ▪ 31 – 45 working days, 45%. ▪ 46 or more working days, 100% (Art 378 CRR).
	Key differences/comments ▪ In general, the US assigns significantly higher risk weightings to unsettled transactions.	
Retail exposures/consumer	100%.	75% (Art 123 CRR).

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loans	(Subpart D, Section 32(k) Final US Rules).	
High risk items	No special categorization of "high risk" items. Certain equity investments in private equity funds/hedge funds are to be deducted in accordance with the Volcker Rule (see also "Equity exposures" and "Exposures to collective investment undertakings/schemes" below).	FIs required to assign a 150% risk weight to exposures associated with particularly high risks (including exposures in the form of shares or units in CISs associated with such risks). Exposures with particularly high risks deemed to include: ▪ investments in venture capital firms. ▪ investments in alternative investment funds that are leveraged. ▪ investments in private equity. ▪ speculative immovable property financing (Art 128 CRR).
Covered bonds	No special rules. Exposures are treated as if they were exposures to the issuing institution or as securitizations.	Covered bonds for which a credit assessment by a nominated ECAI is available to be assigned a risk weight between 10% and 100% (Art 129(4) CRR). For unrated covered bonds, a risk weight will be assigned according to the risk weight assigned to senior unsecured exposures to the issuing FI as follows: ▪ if the FI risk weight is 20%, the covered bond risk weighting is 10%. ▪ if the FI risk weight is 50%, the covered bond risk weighting is 20%. ▪ if the FI risk weight is 100%, the covered bond risk weighting is 50%. ▪ if the FI risk weight is 150%, the covered bond risk weighting is 100% (Art 129(5) CRR).
Equity exposures (other than to investment funds)	<u>Simple Risk Weight Approach</u>: 0%: Equity exposures to a sovereign, certain supranational entities, or a (multilateral development bank) whose debt exposures are eligible for 0% risk weight. 20%: Equity exposures to a public sector entity, a federal home loan bank, or the Federal Agricultural Mortgage Corporation ("**Farmer Mac**"). 100%: Equity exposures to community development investments and small business investment companies and non-significant equity investments (<u>i.e.</u>, equity exposure to the extent that the aggregate adjusted carrying value of the exposures does not exceed 10% of the banking organization's total capital). 250%: Significant investments in the capital of unconsolidated financial institutions that are not deducted from capital pursuant to the "threshold approach". 300%: Most publicly traded equity exposures. 400%: Equity exposures that are not publicly traded. 600%: Equity exposures to certain investment funds. This category includes commitments to acquire equity and derivatives contracts referencing equity instruments (that are not subject to the market risk capital rules). (Subpart D, Section 52 Final US Rules).	100% unless: already deducted, regarded as a high risk item attracting a 150% risk weight, or assigned a 250% (Art 133(2) CRR).
	Key differences/comments ▪ US approach of assigning exposures to one of seven risk weighting categories would be a significant change from the current US approach. Currently, US bank holding companies must deduct from Tier 1 capital the sum of appropriate percentages of the adjusted carrying value of all non-financial equity investments held by the holding company and its subsidiaries. Any portion of non-financial investments that is not required to be deducted from Tier 1 capital is	

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	assigned a 100% risk weight and is included in risk weighted assets.	
Equity exposures to collective investment undertakings/schemes	Three alternative methods may be applied for each exposure to an investment fund: Full look-through: Risk weighted asset amount: risk weight the assets of the fund (as if owned directly) multiplied by the banking organization's proportional ownership in the fund. Simple modified look through: Risk weighted asset amount: multiply the banking organization's exposure by the risk weight of the highest risk weight asset in the fund. Alternative modified look through: Risk weighted asset amount: assign risk weight on a pro rata basis based on the investment limits in the fund's prospectus multiplied by the banking organization's exposure to the fund.	100% unless the FI applies one of the methods set out below: Credit risk assessment method: Exposures to FIs and corporates for which a credit assessment by a nominated ECAI is available will be assigned a risk weight corresponding to that credit assessment, between 20% and 150%. Look through approach: If FI is aware of the underlying exposures of a CIS, it may look through those underlying exposures to calculate an average risk weight. Average risk weight approach: If FI is not aware of the underlying exposures of a CIS, it may calculate an average risk weight on the assumption that the CIS invests in the most risky assets to the maximum extent possible under the CIS's mandate (Art 132 CRR).
	Key differences/comments ▪ The US and EU approaches are broadly similar.	
Other items	100%, except for: ▪ gold bullion held in own vaults (or in another depository institution's vaults on an "allocated" basis), 0%. ▪ exposures that arise from the settlement of cash transactions (such as equities, fixed income, spot foreign exchange and spot commodities) with a central counterparty, 0%. ▪ cash yet to be collected, 20%. (Subpart D, Section 32(1) Final US Rules).	100%, except for: ▪ gold bullion held in own vaults, 0% (Art 134(4) CRR); or ▪ cash yet to be collected, 20% (Art 133(3) CRR).
Off balance sheet items (credit conversion factors)	Low risk: 0% Applies to the unused portion of a commitment that is unconditionally cancelable by the banking organization. (Subpart D, Section 33(b) Final US Rules). Medium/low risk: 20% Applies to the unused portion of a commitment with an original maturity of one year or less that is not unconditionally cancelable. This risk weight also applies to self-liquidating trade related contingent items. (Subpart D, Section 33(b) Final US Rules). Medium risk: 50% Applies to the unused portion of a commitment over one year that is not unconditionally cancelable and to transaction related contingent items (performance bonds, bid bonds, warranties, and standby letters of credit). (Subpart D, Section 33(b) Final US Rules). Full risk: 100% Applies to guarantees, repurchase agreements, securities lending, and borrowing transactions, financial standby letters of credit, and forward agreements. (Subpart D, Section 33(b) Final US Rules).	Low risk: 0% Includes undrawn credit facilities cancelable unconditionally at any time without notice (Art 111 and Annex 1 CRR). Medium/low risk: 20% Includes documentary credits, in which underlying shipment acts as collateral, and other self-liquidating transactions and certain undrawn credit facilities with an original maturity of up to and including one year which are not unconditionally cancelable (Art 111 and Annex 1 CRR). Medium risk: 50% Includes certain documentary credits issued and confirmed, warranties and indemnities and guarantees not having the character of credit substitutes, undrawn credit facilities with an original maturity of more than one year and note issuance facilities (NIFs) and revolving underwriting facilities (RUFs) (Art 111 and Annex 1 CRR). Full risk: 100% Includes guarantees, credit derivatives, acceptances, endorsements on bills not bearing the name of another institution, transactions with recourse, irrevocable standby letters of credit having the character of credit substitutes, assets purchased under outright forward purchase agreements, forward deposits, and unpaid portion of partly paid shares and securities

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		(Art 111 and Annex 1 CRR).
	Key differences/comments ▪ The US and EU approaches are broadly similar. ▪ The exposure value of an off balance sheet item is determined by multiplying the exposure by the appropriate credit conversion factor as identified above. The resulting credit risk capital requirement is determined by multiplying the exposure value by the risk weight ascribed to the counterparty.	
	Asset Risk Weightings – The Advanced Approach (US) or IRB Approach (EU) to Credit Risk	
General approach	The regime relating to the Advanced Approach largely remains in force with several amendments, including: ▪ changes to assumptions for holding periods of collateral in repo style and derivatives transactions. ▪ enhancements to "internal model methodology" for repo style transactions, eligible margin loans, and derivatives. ▪ similar alternatives to credit ratings as in the Standardized Approach. ▪ CVA capital charge. (Subpart E, Final US Rules)	CRD IV restates the previous regime relating to the IRB Approach (which has now been in force in the EU for several years) and contains no substantial amendments (Art 107 CRR) (save for the CVA capital charge, for which see below).
	Key differences/comments ▪ The Basel Committee has highlighted CRR provisions that permit an FI to permanently apply, subject to supervisory approval, the Standardized Approach to sovereigns, PSEs, and certain other exposures without the Basel III condition that this be permitted only where such exposures are immaterial in terms of size and risk profile. ▪ The US Advanced Approaches framework is largely consistent with the Basel IRB Approach. Exceptions include: (i) the definition of qualified revolving retail exposures, which is less strict than the Basel definition, (ii) the absence of capital requirement for dilution risk for purchase receivables as required by Basel, and (iii) the definition of expected credit loss, which deviates from the Basel definition.	
	Asset Risk Weightings – Credit Risk Mitigation	
Guarantees and credit derivatives	Recognizes guarantees from Eligible Guarantors. (Subpart D, Section 36 Final US Rules) Substitution Treatment allows the banking organization to substitute the risk weight of the protection provider for the risk weight ordinarily assigned to the exposure. Applies only to Eligible Guarantees and Eligible Credit Derivatives, and adjusts for maturity mismatches, currency mismatches, and where (for a credit derivative) restructuring involving forgiveness or postponement of principal, interest, or fees is not treated as a credit event. (Subpart D, Section 36(c) Final US Rules).	Recognition of guarantees and credit derivatives with eligible providers (Art 213 CRR). Value of unfunded credit protection reduced by 40% if maximum protection amount is exposure value. If the credit protection value exceeds the exposure value, the extent of the credit protection value is capped at 60% of the exposure value. If currency or maturity mismatch, further adjustment is required (Art 233(2)(a) CRR).
	Key differences/comments ▪ In the US, a banking organization would be permitted to recognize a credit risk mitigant with a maturity mismatch *vis à vis* the hedged exposure only if the mitigant's original maturity is greater than or equal to one year and the residual maturity of the mitigant is greater than three months.	
Collateral	Financial Collateral only, provides two approaches for institutions using the Standardized Approach. (Subpart D, Section 37(a) Final US Rules). <u>Simple Approach</u>: A banking organization may apply a risk weight to the portion of an exposure that is secured by the market value of collateral by using the risk weight of collateral, with a general risk weight floor of 20% (save that the risk weight is 0% for OTC derivative contracts that are marked to market on a daily basis to the extent that they are collateralized by cash on deposit (or 10% if collateral is sovereign debt with 0% risk weight) or for transactions collateralized by cash on deposit or where financial	Firms using Standardized Approach can use the following methods: <u>Financial Collateral Simple Method</u>: In relation to the collateralized portion of the exposure, the FI has exposure instead to the relevant collateral instruments and may apply a risk weight subject to a minimum of 20% (Art 222(3) CRR), save that the risk weight is 0% (or 10% if collateral is sovereign debt) for repos, securities lending and also for marked to market derivative transactions to the extent of the collateral when no currency mismatch exists

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	collateral is an exposure to a sovereign that qualifies for a 0% risk weight and the banking organization has discounted the market value by 20%). There must be a collateral agreement for at least the life of the exposure; collateral must be revalued at least every 6 months; collateral other than gold must be in the same currency. (Subpart D, Section 37(b) Final US Rules). Collateral Haircut Approach: Use of standard supervisory haircuts or own estimates of haircuts for eligible margin loans, repo style transactions, collateralized derivative contracts (if financial collateral is marked to market on a daily basis and subject to a daily margin maintenance requirement). (Subpart D, Section 37(C) Final US Rules).	(Art 222(4) – (6) CRR). Other transactions: FIs may assign a 0% risk weight to a collateralized portion of exposure if there is no currency mismatch, and collateral is cash or cash equivalent, or is sovereign debt that is discounted by 20% (Art 222(6) CRR). Financial Collateral Comprehensive Method: Adjustments required reflecting volatility of the market value of collateral, including any currency volatility (Art 223(1) CRR). FIs using the Financial Collateral Comprehensive Method may take into account the effect of bilateral netting contracts covering repos, securities, or commodities lending or borrowing transactions or other capital market driven transactions; further such firms are able to use certain other items as eligible collateral (Art 218 CRR).
	Key differences/comments ▪ US and EU approaches differ although the respective 'simple' approaches are broadly similar.	
Collateral – Advanced Approach/IRB approach	Single uniform definition of Financial Collateral for each of the Standardized and Advanced Approaches. (Subpart D, Section 37 Final US Rules).	FIs permitted to use the IRB Approach may use additional types of collateral, including immovable property (Art 228(1) CRR), receivables (not including receivables associated with securitizations, sub participations, credit derivatives, and intra group debts) (Art 229(2) CRR), certain other physical collateral, and leasing transactions (Art 229(3) CRR).
	Key differences/comments ▪ In the US, resecuritizations, conforming residential mortgages, and debt securities that are not investment grade would no longer qualify as Financial Collateral.	
On balance sheet netting	Recognition for Qualifying Master Netting Agreements. For most transactions, a banking organization may rely on sufficient legal review instead of an opinion on the enforceability of the netting agreement. (Subpart D, Section 34 Final US Rules).	FIs permitted to use on balance sheet netting of mutual claims between itself and its counterparty as an eligible form of funded credit risk mitigation. Eligibility is generally limited to reciprocal cash balances between the FI and the counterparty (Art 195 CRR).
	Asset Risk Weightings – Securitization	
Securitization positions	Deduction for the after tax gain on sale of a securitization (for a traditional securitization). 1,250% risk weight for a CEIO; 100% for interest only MBS that are not credit enhancing. (Subpart D, Sections 42(a),(g) Final US Rules) One of two methods may be applied: Gross Up Approach: The risk weighted asset amount is calculated using the risk weight of the underlying assets amount of the position and the full amount of the assets supported by the position (that is, all of the more senior positions), or Simplified Supervisory Formula Approach (SSFA): The risk weight for a position is determined by a formula and is based on the risk weight applicable to the underlying exposures, the relative position of the securitization position in the structure (subordination), and measures of delinquency and loss on the securitized assets. 1,250% otherwise. (Subpart D, Section 43 Final US Rules).	Rated securitizations If a credit assessment has been issued or endorsed in accordance with the EU Credit Ratings Regulation (No. 1060/2009), FIs will be required to calculate a risk weighting as follows: securitization positions to be given a risk weighting of 20%, 50%, 100%, 350%, or 1,250% (Art 251 CRR). Resecuritization positions (typically CDOs) to be given a risk weighting of 40%, 100%, 225%, 650%, or 1,250% (Art 251 CRR). EBA to issue technical standards to determine certain credit quality steps to be associated with credit assessments. These credit quality steps will be used to determine appropriate risk weightings (Art 270 CRR). Additional capital requirements to be applied for securitization of revolving exposures with early amortization provisions (Art 256 CRR).

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		Unrated securitizations A risk weighting of 1,250% to be applied (Art 253 CRR).
	Key differences/comments ▪ The US approach (which does not reference any external credit ratings) is considered materially non-compliant with the Basel framework which references credit ratings. The SSFA is driven mainly by standardized risk weights and actual delinquency rates of the underlying asset pool. Limited data suggests that the SSFA can result in risk weights that are significantly higher on average than those calculated under the Basel ratings based approach. US regulators recently sought comment on a "skin in the game" requirement. ▪ The EU securitization framework includes a "skin in the game" requirement whereby an originator or sponsor is required to retain at least 5% of an issue.	
Advanced Approach/IRB approach aspects	Deduction for the after tax gain on sale of a securitization (for a traditional securitization). 1,250% risk weight for a CEIO. (Subpart E, Section 142 Final US Rules). Supervisory Formula Approach: The risk weight for a position is determined by a formula and is based on the risk weight applicable to the underlying exposures and certain other factors. The risk weighted amount for each securitization exposure would be equal to the risk-based capital requirement for the exposure multiplied by 12.5, (Subpart E, Section 143 Final US Rules). or if data to calculate the SFA is unavailable: Simplified Supervisory Formula Approach (SSFA): The risk weight for a position is determined by a formula and is based on the risk weight applicable to the underlying exposures, the relative position of the securitization position in the structure (subordination), and measures of delinquency and loss on the securitized assets. 1,250% otherwise. (Subpart E, Section 144 Final US Rules).	Rated securitizations As with the Standardized Approach, if a credit rating has been issued, FIs are required to calculate the applicable risk weighting based on specific risk weightings (the Ratings Based Method). The Ratings Based Method for the IRB Approach provides that the relevant risk weight should be applied to the exposure value and the result should be multiplied by 1.06. The risk weights vary from 7% to 1,250% for securitizations and from 20% to 1,250% for resecuritizations (Art 261(1) CRR). Unrated securitizations FIs with IRB Approach permission are able to use the Supervisory Formula Method whereby PD (and where applicable exposure value and LGD) are used as inputs into the formula to determine the risk weighting (Art 259(b) CRR). There is also an Internal Assessment Approach whereby the FI assigns the unrated position a derived rating (such derived ratings to correspond to the credit ratings of ECAIs) (Art 259(c) CRR). In all other cases, a risk weight of 1,250% applies (Art 259(d) CRR).
	Key differences/comments ▪ The US approach removes all references to external credit ratings. US Advanced Approaches Banks would be required to conduct more rigorous credit analysis of securitization exposures than under current rules.	
	Asset Risk Weightings – Counterparty Credit Risk	
Derivatives - OTC	The treatment of OTC derivatives depends upon whether the banking organization is an Advanced Approaches Bank or not. Non-Advanced Approaches Banks: *Current exposure method*: Risk weighted asset amount is determined by multiplying the exposure amount for the contract by the risk weight based on the counterparty, eligible guarantor, or recognized collateral. Conversion to an on balance sheet exposure amount based on current exposure plus potential future exposure and a set of conversion factors. Equity derivatives exposures are treated as equity exposures (unless the contract is subject to the market risk capital rules). In general, a special counterparty credit risk requirement need not be computed for credit derivatives. No maximum risk weight cap on OTC exposures. (Subpart D, Section 34 Final US Rules). Advanced Approaches Banks: Advanced Approaches Banks may choose between two alternative methods:	OTC derivatives are generally subject to two capital charges: counterparty credit risk charge and CVA risk charge (for which see further below). There are three methods that will normally be used to determine the appropriate counterparty credit risk exposure, including: ▪ Mark-to-market method: FIs are required under this method to add the current market value of contracts with positive values to an amount representing the potential future credit exposure to generate the exposure value (Art 274 CRR). ▪ Standardized method: this is a more risk sensitive method involving the calculation of an exposure value based on a specific formula which is applied individually for each netting set, net of collateral (Art 276 CRR). ▪ Internal model method: this method is only available for FIs that have elected this method and been given permission by their supervisors (Art 283(1) CRR). The FI is required to devise a model that specifies the

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	<u>*Current exposure method*</u>: see description above. <u>*Internal models methodology*</u>: This method is available only for banking organizations that have elected this method and been given permission by their supervisors. The organization is required to devise a model that specifies the forecasting distribution of changes in the market value of the relevant instruments due to changes in relevant market variables, such as interest rates, FX rates, *etc.*, and calculating the exposure value at each future date on that basis. Posting of margin is included in the model. Basel III enhancements (including regarding wrong way risk) adopted. CVA risk charge imposed on Advanced Approaches Banks (for which see further below). (Subpart E, Section 132 Final US Rules).	forecasting distribution of changes in the market value of the relevant instruments due to changes in relevant market variables, such as interest rates, FX rates, etc. and calculating the exposure value at each future date on that basis (Art 284(1) CRR). Posting of margin is included in the model (Art 284(2) CRR). FIs using the IMM method are also required to devise a CCR management framework (Art 287 CRR). There is a further Original Exposure Method which is applicable to small trading books comprising of interest rate, FX and gold derivatives. Under this method, the contract principal is adjusted by a conversion factor which varies dependent on the nature of the instrument and its maturity (Art 275 CRR).
	Key differences/comments ▪ The EU generally follows the Basel III approach. ▪ In the US, an OTC derivative contract would include an exposure of an institution that is a clearing member to its clearing member client where the institution is either acting as financial intermediary and enters into an offsetting transaction with a central counterparty or where the banking organization provides a guarantee to the central counterparty on the performance of the client.	
Derivatives - cleared	Advantageous risk weighting (either 2% for a clearing member or 2% or 4% for a clearing member client) for exposures to so called “qualifying central counterparty” (or QCCP) (<u>i.e.</u>, a central counterparty that satisfies certain specified financial standards and other eligibility criteria). Apply standard risk weighting for exposures to CCPs that are not QCCPs. (Subpart D, Section 35 Final US Rules). Capital charge imposed on an institution’s exposure (if any) to a central counterparty’s “default fund”. The specific methodology employed to calculate the risk weighted asset amount for a default fund contribution would also depend upon whether the central counterparty qualifies as a QCCP. (Subpart D, Section 35(d) Final US Rules).	Advantageous risk weighting of 2% for exposures to CCPs (Art 306(1)(a) CRR). CCP definition based on EMIR legislation in the EU (Art 4(34) CRR). If “bankruptcy remote”, <u>i.e.</u> within the scope of special client asset protection arrangements, a 0% risk weighting is permitted (Art 306(2) CRR). Separate calculation for own funds requirement to determine pre-funded contributions to CCP’s “default fund” (Art 307 CRR).
	Key differences/comments ▪ Both EU and US approaches are broadly consistent with the Basel approach as set out in the July 2012 interim final rule.	
	Credit Valuation Adjustment	
General approach	<u>Advanced Approaches Banks only</u>: Intended to reflect the CVA due to changes of counterparties’ credit spreads. All references to credit ratings have been removed and banking organizations generally have a choice to apply simple or Advanced Approaches (with credit ratings removed). Advanced Approaches are only available to banking organizations that are subject to the market risk capital rule and have obtained prior supervisory approval. (Subpart E, Final US Rules).	Input for calculation of CVA charge is changes in CDS spreads for firms that are permitted to use the Internal Model Approach. Certain CDS contracts permitted as hedges in certain circumstances (Art 383(1) CRR, eligible hedges defined in Art 386 CRR). FIs in the EU are permitted to use credit ratings (although overreliance on ratings is not permitted under CRD IV) (Art 384 CRR). FIs in the EU are to use the Standardized Approach unless they have elected to use the IRB Approach (Art 384(1) CRR). Trades with the ESCB and certain other EU national bodies performing similar functions, including European sovereign debt management offices and the BIS, are excluded from the CVA charge (Art 382(4)(d) CRR).

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	Key differences/comments ▪ The US approach is broadly consistent with Basel III, although the CVA charge is only applied to Advanced Approaches Banks in the US and all references to credit ratings have been removed under the US approach. The EU has departed from Basel III by implementing an exemption for corporates, sovereigns and pension funds (Art 382 CRR).	
	Effective Date/Phase-In	
New asset risk weightings - standardized approach	January 1, 2015. (Subpart A, Section 1(f) Final US Rules).	Immediately in force.
New asset risk weightings - Advanced Approach	January 1, 2014. (Subpart A, Section 1(f) Final US Rules).	Immediately in force.

Liquidity Requirement

ISSUE	US APPROACH	EU APPROACH
Liquidity requirement	No US proposals to implement Basel III liquidity requirements to date; a proposal under Section 165 of the Dodd-Frank Act would require banking institutions with total consolidated assets equal to or greater than $50 billion to maintain liquidity buffers of highly liquid assets—a concept that is broadly consistent with the goals of the Basel III liquidity ratios.	EU approach follows Basel III on both LCR and NSFR liquidity standards but without prescribing the minimum required liquidity ratios (Art 411 CRR).
	Key differences/comments ▪ The EU is ahead of the US in implementing the Basel III liquidity standards but is nonetheless awaiting further proposals from the Basel Committee. ▪ Section 165 of the Dodd-Frank Act requires the Federal Reserve to establish prudential liquidity requirements for non-bank financial companies supervised by the Board and bank holding companies with total consolidated assets equal to or greater than $50 billion. The Federal Reserve has issued a proposal that builds on the 2010 Interagency Policy Statement on Funding and Liquidity Risk Management issued by the Federal banking agencies and the Conference of State Bank Supervisors and includes, among other things, projected cash flows, stress testing, and contingency funding plan requirements as well as provisions addressing board of director and senior management responsibilities for overseeing and implementing a company's liquidity program. The proposed standards also would require affected firms to maintain liquidity buffers of highly liquid assets and to establish limits on funding concentrations and maturities—concepts that are broadly consistent with the goals of the Basel III liquidity ratios.	
Liquidity	Not addressed to date.	Supervision and reporting requirements relating to LCR and NSFR to phase in by January 1, 2018.
	Key differences/comments ▪ EU to impose supervision and reporting requirements, but main requirements left by both US and EU to a later date.	
Liquidity coverage ratio (LCR)	Not addressed to date.	Liquid assets, outflows, and inflows are detailed in CRR, albeit subject to further refinements by way of regulatory standards drafted by EBA and adopted by the EU Commission (Art 415(3) CRR).
	Key differences/comments ▪ EU approach follows Basel III but no liquidity ratios are yet prescribed.	
Liquid assets	Not addressed to date.	▪ Includes: cash, claims on or guaranteed by central banks, other transferable assets of high liquidity, and credit quality (Art 416(1) CRR). ▪ Excludes: securities issued by financial institutions (apart from covered bonds) (Art 416(2) CRR). ▪ Bank debt (apart from covered bonds or government guaranteed debt used for public policy purposes). ▪ Valuation of liquid assets at market value subject to haircut (min. 15% for securities) (Art 418(1) CRR).
Liquidity outflows	Not addressed to date.	▪ Generally 10% of retail deposits (Art 421(2) CRR) (potentially 5% if deposit subject to guarantee scheme) (Art 421(1) CRR). ▪ Other liabilities generally payable/callable within 30 days including amount of liability exceeding collateral securing liability where collateral counts as a liquid asset (Art 422(4) CRR); or 25% of liability to PSE (Art 422(2)(d) CRR). ▪ Net payables (including net of liquid assets held as collateral) expected over 30-day period

ISSUE	US APPROACH	EU APPROACH
		(Art 422(6) CRR). ▪ Other liabilities – Institutions shall multiply liabilities resulting from the institution's own operating expenses by 0% (Art 422 CRR). ▪ Collateral posted for derivatives trades subject to haircut of 15% or 20% depending on liquidity/credit quality of collateral (Art 423(1) CRR). Additional outflow potentially applied by national supervisor if additional collateral or liquidity outflow provided for under contract as a result of deteriorating creditworthiness (Art 423(3) CRR).
Liquidity inflows	Not addressed to date.	▪ 50% of principal payments by non-financial customers (Art 425(2)(a) CRR). ▪ Monies due from secured lending and capital markets transactions minus haircutted liquid assets posted as collateral that shall be subject to a haircut (Art 425(2)(d) CRR). ▪ Deposits held at other FIs subject to the LCR, in an amount of assumed outflow of that FI (Art 425(2)(e) CRR). ▪ Undrawn credit/liquidity facilities disregarded (Art 425(2)(g) CRR), unless higher inflow amount allowed by national regulator where counterparty is group entity in same jurisdiction and is subject to LCR and is applying symmetric or more conservative outflows, and there are reasons to expect a higher inflow (Art 425(4) CRR). ▪ Net payables expected over 30-day period (Art 425(3) CRR).
Net stable funding ratio (NSFR)	Not addressed to date.	▪ Only reporting of stable funding sources and required funding only addressed at the moment. NSFR expected to be in force as at 2018 (Art 427 CRR). ▪ Stable funding is categorized into maturities below 3 months, 3–6 months, 6–9 months, 9–12 months, after 12 months (Art 427(2) CRR). ▪ Available stable funding: regulatory capital, deposits, funding from financial customers, collateralized funding from secured lending, and capital market transactions, covered bond proceeds, securities sold to UCITs, other liabilities (Art 427(1) CRR). ▪ All items of funding to be allocated to 5 maturity buckets (Art 428(2) CRR). ▪ Items requiring stable funding – liquid assets that count as liquid assets under LCR, other securities, precious metals, non-renewable receivables, derivatives receivables, certain undrawn credit facilities, other assets (Art 428(1) CRR).

Leverage Requirement

ISSUE	US APPROACH	EU APPROACH
Tier 1 to total on balance sheet assets leverage ratio	Depository institutions/holding companies must maintain a minimum leverage ratio of 4% effective January 1, 2015. (Under current rules, certain banks are permitted to maintain a 3% minimum.) (Subpart B, Section 10(a) Final US Rules).	Art 430 CRR requires institutions to submit to the competent authorities all necessary information on the leverage ratio and its components from January 1, 2015, in accordance with Art 429 CRR (leverage). The Basel III leverage ratio may be introduced as a binding measure in 2018, following the Basel Committee review and calibration of leverage ratio requirements in the first half of 2017.
	Key differences/comments ▪ The US leverage requirement (which has no equivalent in the EU) is similar to the Basel III Leverage Ratio but does not take into account off balance sheet exposures.	
Tier 1 to total leverage exposure ratio (Basel III leverage ratio)	Advanced Approaches Banks: 3% minimum to be calculated and reported by Advanced Approaches Banks from January 1, 2015 and imposed as regulatory requirement from 2018. (Subpart B, Section 10(a) Final US Rules). Other Banks: Not applicable.	Calculation of leverage ratio requirement from January 1, 2014, start of disclosure of leverage ratio from January 1, 2015 and EU to decide whether to introduce binding leverage ratio in 2018 following Basel Committee review of leverage ratio in the first half of 2017.
	Key differences/comments ▪ Referred to as the "Supplemental Leverage Ratio" in the US rules. No binding leverage ratio in EU currently (although European Commission has acknowledged that leverage disclosure requirements and market pressure may make leverage ratio akin to a "binding" requirement prior to 2018). ▪ The US agencies have solicited comments on how to calculate the Basel III Leverage Ratio – concerns include differences in international accounting.	

599 LEXINGTON AVENUE | NEW YORK | NY | 10022-6069