

29 September 2012

IBCSI ٢٤٩٧٩

From : Saudi Arabian Monetary Agency

To : All Banks

Attention : Managing Directors, Chief Executive Officers and General Managers

Subject : **SAMA's Consultative Draft Concerning the Implementation of Basle II.5 (Standardized and IRB Approaches)**

The Basel II.5 framework of the BCBS was issued through its document given below in July 2009 and December 2010 covering Pillar 1, Pillar 2 and Pillar 3 aspect.

- "Enhancement to the Basel II Framework" – July 2009 (A)
- "Revisions to the Basel II Market Risk Framework" – December 2010 (B)

The aforementioned documents were issued to respond to the financial crisis (also referenced to as the "sub-prime" crisis) that began in Mid 2007 which closely affected major international banks and banking systems with significant losses incurred on their investments in complex structured and restructured products. These losses were largely concerning Credit Risk and from the cascading of Other financial and non-financial risks into Market risk. Consequently, the BCBS issued the aforementioned documents where "A" above was to respond to Credit risk and "B" to Market risk.

The Agency had decided to delay the implementation of the Basel II.5 framework as a whole as the Saudi banks' investments and other exposures was limited to such structured and restructured product was limited. Therefore, the legacy treatment under Basel II (BCBS document of June 2004) continued where SAMA under its National Discretion applied a 100% Risk Weights (RW) to such exposures.

Consequently, SAMA is issuing for Banks' comments its attached documents for implementing the Basle II.5 Framework comprising of all Pillar 1, Pillar 2, and Pillar 3 requirements. In this regard, the attached SAMA documents comprising of Guidance Notes and Prudential Returns have been compiled on the basis of the two aforementioned BCBS document which represent enhancements and amendments to the BCBS Basel II Framework with regard to securitization and re-securitization activities. Consequently, the implementation of SAMA's Basel II.5 as a whole i.e. Pillar 1, Pillar 2 and Pillar 3 will be carried out through the adjustments and enhancements to its Basel II Framework.

A. Pillar 1

With regard to implementing Basel II.5 – Pillar-1 risk, we refer to the following SAMA Circulars concerning the implementation of Basle II Standardized and IRB Approaches.

- SAMA – Basle II Prudential Returns Consultative Draft # 2 Circular # BCS 180 of 22 March 2007.
- SAMA Basle II Guidance Document to banks in Saudi Arabia of 6 June 2006.
- SAMA Amended IRB Prudential Return and Guidance Notes of 18 January 2012 Circular # BCS 5318.

While SAMA's implementation framework incorporates i) Guidance Notes and ii) Prudential returns concerning Credit Risk and Market Risk for both the Standardized Approach and IRB Approaches, IRB approaches would only be applicable where SAMA has provided approval to utilized IRB approaches.

With regard to implementing model in the context of Basel II.5 Market risk, SAMA wishes to wait until substantial Trading Book issues under BCBS deliberations are resolved as per its document of May 2012 entitled "Fundamental Review of the Trading Book".

With regard to Operational Risk, there were no refinements to Basel II under Basel II.5.

It should be noted that these Prudential Returns are not applicable to branches of foreign banks as the Agency will discuss the Basle II implementation with their Head Offices and Home Supervisory Authorities, and ensure that they include the branches in Saudi Arabia in their Capital Adequacy plans.

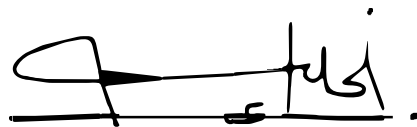
B. Pillar 2

- Basel II.5 Pillar 2 ICAAP Requirements
 - Please refer to P. 40

C. Pillar 3

- Basel II.5 Pillar 3 Disclosure Requirements
 - Please refer to P. 42

All banks are expected to review this package and provide comments to SAMA by 10 October 2012, as this exercise will assist in finalizing this package. SAMA will issue its Finalized Basel II.5 Guidance Document before 31 December 2012. Consequently, SAMA Basel II.5 Framework will be effective 1 January 2013. Banks will submit their first quarterly prudential returns for data as of 31 March 2013 to be sent to SAMA by 30 April 2013.



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