



IBCSI ٢٥٨٠٨

From : Saudi Arabian Monetary Agency

To : All Banks

Attention : Managing Directors, Chief Executive Officers and General Managers

Subject : **Guidance Document Concerning Implementation of Capital Reforms Under Basel III Framework Based on Relevant BCBS Documents**

The implementation of the Basel II.5, and Basel III is to be carried out concurrently effective 1 January 2013. The Basel II.5 Framework has already been finalized through SAMA Circular 25478 dated 21 October 2012. Consequently, the attached represents SAMA's Draft Guidance Document and Prudential Returns concerning the implementation of Basel III Standardized and IRB Approaches, which is to be achieved by 2019. This Draft Basel III Implementation Document is for Banks to provide their comments by 25 November 2012 which will be reviewed for further clarification or enhancement. A final SAMA Circular will be issued in December 2012 and Banks will also commence the implementation of Basel III in Saudi Arabia from 1 January 2013.

The attached SAMA's Basel III implementation framework has been developed through the BCBS documents and related SAMA Circulars which are given below.

- a. Basel III: A Global Regulatory Framework for More Resilient Banks and Banking System – December 2010 (revised June 2011) issued through SAMA Circular # BCS 27885 dated 12 November 2011.
- b. Basel III: International Framework for Liquidity Risk Measurement, Standards and Monitoring issued through SAMA Circular # 28266 dated 19 November 2011.
- c. Final Elements of the Reform to Raise the Quality of Regulatory Capital – Loss Absorbency at the Point of Non-Viability issued through SAMA Circular # BCS 5611 dated 13 February 2011.

The attached SAMA's Draft implementation Guidance Document comprises of all Basel III Pillar 1, Pillar 2, and Pillar 3 requirements composed of Guidance Notes and where relevant Prudential Returns. These document represent enhancements and amendments to the BCBS Basel II and Basel II.5 Framework already issued by SAMA, with regard to Risk Weighted Assets and Regulatory Capital.

**Models for Market Risk for Basel II.5 and Basel III**

With regard to implementing Models for Market Risk in the context of Basel III and Basel II.5, SAMA has decided to wait until substantial Trading Book issues under review in the BCBS are resolved. These issues were documented in the BCBS document of May 2012 entitled "Fundamental Review of the Trading Book" which was also circulated to all banks through SAMA Circular # 37422 BCS 18819 dated 13/7/1433 (Hijri). Consequently, for Basel II.5 and Basel III Market Risk components, SAMA will be implementing only the Standardized Approach level for Market Risk related Risk Weight Assets.

With regard to Operational Risk, there were no refinements under Basel II.5, and Basel III. Consequently, the Basel III Operational Risk Weighted Assets are identical to Basel II.

It should be noted that these Prudential Returns are not applicable to branches of foreign banks as the Agency will discuss the Basle II.5 and Basel III implementation with their Head Offices and Home Supervisory Authorities, and ensure that they include their branches in Saudi Arabia in their Capital Adequacy plans.

The implementation of Basel III represents an entirely new Definition of Regulatory Capital according to a more pure and detailed Basel III capital structure for which a Prudential Return is provided. However, with regard to Risk Weighted Assets, an incremental approach as given below is adopted, where banks will complete only the relevant Prudential Returns concerning RWA under their Basel II, Basel II.5 and Basel III framework with regard to Pillar 1, Pillar 2 and Pillar 3 components.

A. **Pillar 1:**

Basel III Pillar 1 requirements will be an aggregate of Risk Weighted Assets under Basel II, Basel II.5 and Basel III. Therefore, banks will continue to calculate their P1 Risk Weighted Assets utilizing the Prudential Return Q17 series of Basel II, Basel II.5 and Basel III frameworks with regard to Credit Risk, Market Risk and Operational Risks.

B. **Pillar 2:**

Basel III Pillar 2 ICAAP framework will be composed of the aggregation of Pillar 2 requirements under the Basel II, Basel II.5 and Basel III framework.

C. **Pillar 3:**

Basel III Pillar 3 Disclosure Requirements framework will also be composed of aggregation of requirements under Basel II, Basel II.5 and Basel III.

**Quarterly Monitoring and Parallel Runs**

The quarterly monitoring of SAMA Basel III Framework with regard to Leverage Ratios and Liquidity Ratios (LCR and NSFR) will continue as usual, while the monitoring of Basel III Capital Ratios will commence effective 1 January 2013 and Banks will submit their first quarterly prudential returns for data as of 31 March 2013 to be sent to SAMA by 30 April 2013.

Additionally, banks should be aware of the following aspects regarding parallel runs:

1. In order to ensure the accuracy of Basel III implementation, parallel runs will be carried out over two quarter ends commencing January 1 to June 30, 2013 for Capital Adequacy Ratios and related details under Basel II, Basel II.5 and Basel III regarding Regulatory Capital, RWA's, etc.
2. The Regulatory Capital framework under Basel II and Basel II.5 will be eventually discontinued following the parallel runs and only the III will continue thereafter.

*for*  *Ibrahim Almasa*  
**Abdulrahman A. Al-Kalaf**  
*Deputy Governor*  
*for Technical Affairs*