

July 15, 2016

Comments on the Consultative Document: *Prudential treatment of problem assets – definitions of non-performing exposures and forbearance*, issued by the Basel Committee on Banking Supervision

Japanese Bankers Association

We, the Japanese Bankers Association (“JBA”), would like to express our gratitude for this opportunity to comment on the consultative document: *Prudential treatment of problem assets – definitions of non-performing exposures and forbearance* issued on April 14, 2016 by the Basel Committee on Banking Supervision (“BCBS”). We welcome the BCBS’s initiative to define non-performing exposures and forbearance from the perspectives of appropriate identification of credit risk by financial institutions and enhancement of comparability for supervisors and investors.

We respectfully expect that the following comments will contribute to your further discussion.

**1. Application of non-performing status should be permitted both at the level of each exposure and at the level of each counterparty.**

In paragraph 19, the consultative document proposes to apply non-performing status at the level of each counterparty, instead of each exposure, for non-retail counterparties.

Paragraph 24, on the other hand, includes “all exposures impaired in accordance with the applicable accounting framework” as one of the criteria for the definition of non-performing exposures. However, major accounting standards require categorisation of non-performing exposures at the exposure level, which gives rise to inconsistency with paragraph 19 of the consultative document. If, nevertheless, the categorisation of non-performing exposures will be harmonised on a counterparty basis, instead of the each exposure basis, there will be inconsistency in categorisation between the accounting framework and the Basel framework in some cases. This may have adverse effects on enhancement of comparability which is one of the objectives of the consultative document.

Exposures are categorized on a counterparty basis under credit risk management practice, in principle. However, there are some exposures such as non-recourse loans that should be categorised and disclosed on an exposure basis.

If the categorisation of non-performing exposures will be harmonised on a borrower basis, performing nonrecourse loans may be categorised as non-performing, leading to a concern that public disclosure inconsistent with actual practice against the market. Moreover, if an exposure which is deemed as performing at the exposure level is categorised as non-performing under the Basel framework, banks might need to treat such exposure as non-performing, in practice.

As such, banks should be permitted to apply both exposure level and counterparty level categorization for disclosure purposes.

## **2. Definition of forbearance**

### **Review of exit criteria for forborne exposures**

Paragraph 41 stipulates that “a forborne exposure will be identified as such until it meets both of the following exit criteria: (i) When repayments as per the revised terms have been made in a timely manner (principal and interest payments) over a continuous repayment period of not less than one year (minimum probation period for reporting) (...); and (ii) The counterparty has solved its financial difficulties”.

In this context, it would not be appropriate to apply the above (i) as exit criteria uniformly even in cases where financial institutions can sufficiently assess the probability of repayments. As a result of assessing repayment plan developed based on forbearance, if it is concluded that repayments of principal and interest as per the revised term are highly probable, such exposures seem appropriate to be exited from the forborne exposures category, regardless of the probation period.

The consultative document states that the probation period is set at not less than one year because many jurisdictions have a minimum one year probation period (paragraph 130). This, however, lacks reasonable supportive evidence. Concerning the exit criteria, determining in a comprehensive and practical manner by taking into consideration credit quality, the repayment status of borrowers and other factors seems appropriate.