



**MINISTRY OF INDUSTRY, BUSINESS
AND FINANCIAL AFFAIRS**

Valdis Dombrovskis
Vice-President of the European Commission

**MINISTER FOR INDUSTRY,
BUSINESS AND FINANCIAL
AFFAIRS**

Dear Vice-President Dombrovskis

Thank you for the opportunity to respond to the consultation on the finalisation of Basel III reforms.

Following the financial crisis, many important reforms have been implemented in the field of financial services in order to reduce the likelihood of future crises as well as mitigate the effects of these. We now have a much stronger financial sector than before the crisis. This should be taken into account when implementing the Basel III reforms.

On the specific elements in the final recommendations from the Basel Committee on Banking Supervision (BCBS) in December 2017, first of all, we have strong reservations in relation to the output floor. The output floor has a number of negative implications that could cause serious harm to financial stability and the real economy. Most importantly, the output floor will decrease the risk sensitivity in the capital requirements of financial institutions by effectively disregarding the internal models currently used by the largest credit institutions in e.g. Denmark. Doing this, credit institutions will have an incentive for increased risk taking as they can take on more risky exposures without corresponding increases in the capital requirements.

In addition, an expert group established by the Danish Government has estimated that the Basel III package will lead to a significant and unjustified increase in capital requirements, increasing the capital requirements of the largest Danish credit institutions by 34 percent. The output floor is the main contributor to this very significant increase.

Denmark has been and continues to be a strong supporter of measures to strengthen financial stability. We believe that financial stability is best achieved by a risk sensitive approach to capital requirements - properly regulated and supervised. Therefore, we also support the regulatory review of the IRB approach conducted by The European Banking Authority (EBA) with the aim of reducing unjustified variability in IRB models, ensuring comparability of risk estimates while at the same time preserving risk sensitivity of capital requirements. Non-

**MINISTRY OF INDUSTRY,
BUSINESS AND FINANCIAL
AFFAIRS**

Slotsholmsgade 10-12
1216 Copenhagen K
Denmark

Tlf. +45 33 92 33 50
Fax. +45 33 12 37 78
CVR-nr. 10092485
EAN nr. 5798000026001

risk based capital requirements such as the output floor should generally work as a backstop to risk based capital requirements. If the recommendations are implemented without taking European specificities into account, the Basel III reforms will direct credit institutions onto a less risk sensitive path and reduce the risk sensitivity of capital requirements and that will in our view contradict the fundamental purpose of the reforms

We generally think that any inappropriateness in the IRB framework should be addressed by improving the IRB framework, through the current work in EBA, instead of introducing a non-risk sensitive capital requirement which effectively suspends the models without taking the current functioning of the models into account.

Following the above, we cannot support an implementation of the proposed output floor without taking into account European specificities thereby preserving a risk sensitive approach.

Aside this very important point, there are many reasonable and, in our view, positive adjustments (e.g. the changes to operational risk and IRB models for credit risk) to the already very sound prudential framework in the recommendations. This should be implemented in the EU, taking into account European specificities and business models. While these adjustments will result in an increase in capital requirements, we find that they are important in order to reduce risks and ensure a sound and stable financial sector and a level playing field on a global scale.

We are looking forward to assisting you and the Commission services in the implementation of the Basel III reforms in order to preserve risk sensitivity in the financial sector and consider European specificities. In the attached annex, please find the specific Danish comments to the Commission consultation.

As always, I remain at your disposal should you have any questions or comments.

Yours sincerely,



Brian Mikkelsen