Basel 3.1
Don’t delay: the time for action is now
The implementation of Basel 3.1 is one of the biggest priorities for banks operating in the UK as they move into 2024. For many, the PRA’s recent announcement pushing the go-live date back to 1 July 2025 may have prompted a positive response that there is now a further six months to prepare. The delay offers banks a window of opportunity to recalibrate their compliance approaches and strategies, refine their systems and ensure that they are fully equipped to navigate the complexities of the Basel 3.1 landscape. However, given the extent of change required, banks cannot afford to ease off on their preparations.

The changes to Basel rules create significant work for banks. However, this should be considered as an opportunity not only to ensure regulatory compliance but also to consider the capital impacts and how their business should evolve to deliver future profitability.

KPMG in the UK has the skills and expertise to support you through all the stages of this transformative journey. Read on for a summary of our views on the challenges banks will likely face as they look towards implementation and to learn more about potential strategies for successfully navigating the complex Basel 3.1 requirements.

The timeline

The PRA published its proposals for the implementation of Basel 3.1 in November 2022 (CP16/22). On 27 September 2023, the PRA delayed the UK implementation start date from January 2025 to 1 July 2025, and shortened the phase-in period for the output floor to 4.5 years. The revised UK start date is in line with current US proposals – the EU is continuing to work towards a start date of 1 January 2025.

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<tr>
<th>BCBS</th>
<th>UK</th>
<th>EU</th>
<th>US</th>
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<tr>
<td>Nov 2022: PRA consultation on UK implementation of Basel 3.1</td>
<td>2022</td>
<td>2023</td>
<td>2024</td>
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<td>BCBS target implementation  - Jan 2023 to Jan 2028  • Market risk, credit risk, CVA, operational risk, leverage ratio framework: 1 Jan 2023  • Output floor: 1 Jan 2023 to 1 Jan 2028</td>
<td>Q4 2023 PRA Policy Statement: market, CVA, counterparty credit &amp; operational risk</td>
<td>2024</td>
<td>IMA application by 1 Jul 2024</td>
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<td>Q2 2024: PRA Policy Statement: credit risk, output floor &amp; disclosures</td>
<td>2025</td>
<td>IRB application by 1 Jan 2025</td>
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<td>UK implementation: Jul 2025 to Jan 2030. Output floor phased in over 4.5 years</td>
<td>2030</td>
<td>2025</td>
<td>EU implementation – Jan 2025 to Jan 2030  • Market risk, credit risk, CVA, operational risk, leverage ratio framework: 1 Jan 2025  • Output floor: 1 Jan 2025 to 1 Jan 2030</td>
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<td>US implementation – Jul 2025 to Jul 2028</td>
<td>2026</td>
<td>2027</td>
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Implementation considerations

Firms have significant work to do to ensure timely compliance with the Basel 3.1 requirements. This includes, but is not limited to:

- Standing up and executing a strategic implementation programme
- Performing gap analysis assessments against the new rules
- Data sourcing for new attributes required for real estate, unrated corporates and institutions
- Reviewing and updating existing policy interpretations
- Identifying and making necessary changes to operating models
- Building and implementing RWA calculators for the new standardised approaches for credit, market and operational risk
- Building the standardised floor calculation for Internal Ratings Based (IRB) banks
- Submitting model applications or re-applications to continue using IMA and IRB approaches at least six and 12 months respectively before the start of the implementation period
- Re-visiting impacts with front office and educating board and executive management

The PRA’s consultation has raised concerns across the banking industry, not least:

- The “very clear feedback from firms” on areas which are too punitive, for example the lending to unrated corporates, SMEs, trade finance and accounting provisions.
- The importance of maintaining a level playing field across jurisdictions to prevent regulatory fragmentation – to prevent unintended consequences and market distortions.

Banks in the UK have been tracking the strategic impact on capital ratios since the Basel Committee first published its final reforms, through exercises such as the quantitative impact studies (QIS), and have established implementation programmes for components such as SA-CCR and FRTB. However, most large banks only set up holistic Basel 3.1 programmes in Q4 2022 and many smaller firms have not yet commenced the necessary impact analysis.

There are opportunities as well as challenges to be found in the implementation process, not least around balance sheet optimisation. Basel 3.1 will fundamentally change the way in which banks need to manage their balance sheets, presenting opportunities to:

- Drive efficiencies through improved capital deployment
- Increase balance sheet velocity
- Enhance earnings / deployment of capital and return on capital
- More dynamically manage risk appetite
- Reduce balance sheet volatility and stress impact
- Create optionality / recovery actions in stress

Asset origination and distribution economics will change as a result of the output floor. Effective balance sheet management requires banks to look for divergence between the regulatory capital assumed risk and the market assumed risk. The output floor and adjustments to the standardised and IRB approaches will create a dislocation between these assumed risk metrics, that may benefit from an increase in structural distribution mechanisms; for example, through the use of Significant Risk Transfers (SRTs).

Many banks still have significant work to do to deliver the final Basel reforms. As a clearer picture emerges of the likely differences in approach between the UK, EU and US, programmes can now be mobilised to begin work on no regrets actions.”

Rob Smith,
Partner & Risk and Regulatory Advisory Lead
Considerations for a successful Basel 3.1 implementation

- Strong sponsorship, engagement and governance
- Effective PMO and programme structure
- Awareness of jurisdictional differences and complementary regulation
- Detailed gap analysis
- Focus on data sourcing, integrity and governance
- Capital calculations and risk weights
- IT infrastructure and systems integration
- Balance sheet optimisation
How can KPMG help?

KPMG professionals can support you through the various stages of your Basel 3.1 implementation:

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<th>Feature</th>
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<td><strong>Global view and local expertise</strong></td>
<td>KPMG firms’ global network of Basel subject matter experts can help ensure you have the latest perspectives on regulatory and technical mandates. We can also bring insights on how jurisdictional differences are being managed at global and cross border firms.</td>
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<td><strong>Regulatory horizon scanning</strong></td>
<td>KPMG’s Regulatory Horizon tracks, curates and distributes regulatory content to help you stay on top of the ever-changing regulatory landscape. The Regulatory Horizon can also provide insights from KPMG firms’ regulatory specialists on key developments and customised horizon scanning reports.</td>
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<td><strong>Policy interpretation</strong></td>
<td>We can review your existing policy interpretations against the new requirements and assess the impact the changes will have on your capital requirements. We have insights into how other firms are interpreting the new requirements and are planning to address data gaps. Where interpretations are required, we can draft governance documents to support your decision-making.</td>
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<td><strong>Impact assessment and rule decomposition</strong></td>
<td>We can perform a line-by-line impact assessment leveraging our prepared decompositions. This method ensures full traceability back to the regulatory text.</td>
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<td><strong>Programme management office (PMO) support</strong></td>
<td>We can perform central programme management office functions, co-ordinating resources across teams, helping to manage risks and dependencies and assisting with proactive engagement with the necessary stakeholders.</td>
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| **Technology implementation support** | KPMG professionals can help with your technology implementation, including:  
- Drafting user stories and functional specifications  
- Data derivation from existing inventory of systems  
- User Acceptance Testing (UAT) and implementation planning  
- The development of reporting. |
| **Assessing data requirements** | We can perform the data discovery process for new attributes and document the data lineage for these in line with market leading practice. Through our work we will improve data governance through providing full data traceability which will deliver benefits if future changes are required. |
| **Capital impacts and balance sheet optimisation** | KPMG specialists can help you to understand the capital impact of Basel 3.1 on your business and identify opportunities to optimise your strategy and balance sheet, to drive enhanced returns. |
| **Implementation assurance** | Independent review of your implementation approach to help ensure compliance with PRA requirements including:  
- Completeness and traceability back to rules  
- Policy  
- Governance  
- Process and control testing  
- User acceptance testing. |
| **Training and upskilling** | KPMG professionals can provide “off the shelf” and tailored training to upskill teams across your business on regulatory change, requirements and impacts. |
In summary

Whilst the PRA’s final Basel 3.1 rules have not yet been published, enough is known for firms to make meaningful progress on a ‘no-regrets basis’. Given the volume of change required, firms need to act now to ensure sufficient time to implement everything and be compliant.

Several of the proposed changes will have significant impacts, affecting not only the amount of capital banks are required to hold, but also the type of business that they are able and wish to engage in going forward. Basel 3.1 is not only about interpreting and applying regulations – it is about getting ahead of the ways in which the new requirements could impact your business and ensuring future profitability. KPMG member firms already supporting many clients on their Basel 3.1 journey and can share learnings and insights from this work.
Some or all of the services described herein may not be permissible for KPMG audited entities and their affiliates or related entities.