



# **PRIVATE SECTOR CONSULTATION**

**Regulatory Policy on Domestic Systemically  
Important Deposit Taking Institutions**

**and**

**Rule on Domestic Systemically Important Deposit  
Taking Institutions**

## Private Sector Consultation

### Regulatory Policy on Domestic Systemically Important Deposit Taking Institutions

and

### Rule on Domestic Systemically Important Deposit Taking Institutions

#### A. Introduction

1. Section 34(1)(a) of the Monetary Authority Act (2020 Revision) ("MAA") states that:

*After private sector consultation and consultation with the Minister charged with responsibility for Financial Services, the Authority may –*

- a) *issue or amend rules or statements of principle or guidance concerning the conduct of licensees and their officers and employees, and any other persons to whom and to the extent that the regulatory laws may apply.*

2. Requirements specific to the private sector consultation are outlined in section 4(1) of the MAA as follows:

*When this Law requires private sector consultation in relation to a proposed measure –*

- a) *the Authority shall give to each private sector association a draft of the proposed measure, together with –*

- i. *an explanation of the purpose of the proposed measure;*
- ii. *an explanation of the Authority's reasons for believing that the proposed measure is compatible with the Authority's functions and duties under section 6;*
- iii. *an explanation of the extent to which a corresponding measure has been adopted in a country or territory outside the Islands;*
- iv. *an estimate of any significant costs of the proposed measure, together with an analysis of the benefits that will arise if the proposed measure is adopted; and*
- v. *notice that representations about the proposed measure may be made to the Authority within a period specified in the notice (not being less than thirty days or such shorter period as may be permitted by subsection (3)); and*

- b) *before proceeding with the proposed measure, the Authority shall have regard to any representations made by the private sector associations, and shall give a written response, which shall be copied to all the private sector associations.*

3. The Cayman Islands Monetary Authority ("the Authority") seeks consultation and comment from the private sector associations concerning the proposed:

- a) Regulatory Policy on Domestic Systemically Important Deposit Taking Institutions (**Appendix 1**); and
- b) Rule on Domestic Systemically Important Deposit Taking Institutions (**Appendix 2**)

(together referred as "the proposed Measures" or "Measures").

## **B. Background**

4. In November 2011, the Basel Committee on Banking Supervision ("BCBS") issued *Global systemically important banks: assessment methodology and the additional loss absorbency requirement*, which sets out the framework for identifying and supervising global systemically important banks (the "BCBS G-SIB Framework"). *Inter alia*, the BCBS G-SIB Framework introduced Higher Loss Absorbency Requirement ("HLA Requirement") for global systemically important banks ("G-SIBs") as a means of reducing their risk of failure by applying a prescriptive approach to increasing their capacity to absorb losses.
5. Subsequently, in October 2012, the BCBS issued the framework for dealing with Domestic Systemically Important Banks (the "BCBS D-SIB Framework"). The BCBS D-SIB Framework is complementary to the BCBS G-SIB Framework and focuses on the impact that the failure or distress of a bank may have on a jurisdiction's domestic financial system and/or real economy.
6. Under the BCBS D-SIB Framework, national authorities are responsible for establishing a methodology for assessing the degree to which banks<sup>1</sup> are systemically important to the domestic economy and calibrating the level of HLA requirement. They are also responsible for setting any other expectations to address the risks posed by such institutions. Unlike the G-SIBs Framework, the BCBS D-SIB Framework adopts a principles-based approach which allows for national discretion in establishing the assessment methodology for identifying domestic-systemically important institutions; and in calibrating the HLA Requirement.
7. The Regulatory Policy on Domestic Systemically Important Deposit Taking Institutions (**Appendix 1**) sets out, among others, the Authority's assessment methodology and supervisory expectations for deposit taking institutions identified as being domestic systemically important.
8. The Rule on Domestic Systemically Important Deposit Taking Institutions (**Appendix 2**) sets out, among others, the regulatory obligations for institutions identified as being domestic systemically important.

## **C. International Standards**

9. The BCBS D-SIB Framework consists of twelve principles that are broadly categorised into two groups: the first group focusing mainly on the assessment methodology for Domestic-Systemically Important Banks ("D-SIBs") and the second group focusing on higher loss absorbency for the D-SIBs.
10. With regards to the assessment methodology, the BCBS D-SIB Framework provides, among others, that:
  - (1) the assessment methodology should reflect the potential impact of, or externality imposed by, a bank's failure on the domestic economy;
  - (2) home authorities should assess banks for their degree of systemic importance at the consolidated group level, while host authorities should assess subsidiaries in their jurisdictions, consolidated to include any of their own downstream subsidiaries;
  - (3) the impact of a D-SIB's failure on the domestic economy should, in principle, be assessed having regard to bank-specific factors such as size, interconnectedness, substitutability and complexity. Other factors such as size of the domestic economy could be used to further inform the bank-specific factors;

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<sup>1</sup> In the context of the Cayman Islands, this includes non-bank deposit taking institutions supervised by the Authority.

- (4) the assessment of systemic importance should be carried out on a regular basis to keep it current and that the interval between D-SIB assessments should not be significantly longer than the G-SIB assessment frequency; and
  - (5) national authorities should publicly disclose information that provides an outline of the methodology employed to assess the systemic importance of banks in their domestic economy.
11. With regards to HLA Requirement for D-SIBs, the BCBS D-SIB Framework provides that:
- (1) the purpose of an HLA Requirement for D-SIBs is to reduce further the probability of failure compared to non-systemic institutions, and should be commensurate to the impact a D-SIB failure is expected to have on the domestic financial system and economy;
  - (2) the methodologies and considerations used to calibrate the level of HLA Requirement for D-SIBs should be documented. The level of HLA calibrated for D-SIBs should be informed by quantitative methodologies (where available) and country-specific factors without prejudice to the use of supervisory judgement or overlay;
  - (3) where the subsidiary of a bank is considered to be a D-SIB by a host authority, home and host authorities should make arrangements to coordinate and cooperate on the appropriate HLA Requirement, within the constraints imposed by relevant laws in the host jurisdiction; and
  - (4) the HLA Requirement should be met fully by Common Equity Tier 1 (CET1). In addition, national authorities should put in place any additional requirements and other policy measures they consider to be appropriate to address the risks posed by a D-SIB.

**D. Purpose of Proposed Measures and Consistency with the Authority's Functions**

12. Section 6(1) of the MAA outlines the principal functions of the Authority, which include, among others, *"to regulate and supervise financial services business carried on in or from within the Islands"*.
13. Section 6(2) (a and b) of the MAA provides that in performing its functions and managing its affairs, the Authority shall:
- (a) *act in the best economic interests of the Islands; and*
  - (b) *promote and maintain a sound financial system in the Islands.*
14. The purpose of the proposed Measures is to set out:
- a) the Authority's criteria for identifying and designating Domestic-Systemically Important Deposit Taking Institutions ("D-SIDTIs"), which are institutions that could cause significant disruption to the Cayman Islands' financial system and economy in the event of their distress or failure; and
  - b) the Authority's approach to mitigating negative externalities posed by D-SIDTIs. This includes regulatory and supervisory expectations aimed at reducing probability of their failure by, among others, increasing the D-SIDTIs' going-concern loss absorbency.

## **E. Jurisdictional Comparison**

15. The Authority conducted jurisdictional comparison comprising of Australia, Hong Kong, Malaysia, Canada and United Kingdom. The jurisdictional comparison covered various components of D-SIB frameworks for each of the jurisdictions. These included:
  - (1) factors used to measure systemic importance;
  - (2) approach to weighting on the factors used to measure systemic importance;
  - (3) approach used for bucketing and calibrating HLA Requirement;
  - (4) transition period allowed by the jurisdictions when they implemented their respective D-SIB frameworks;
  - (5) frequency of assessment and listing of D-SIBs; and
  - (6) frequency of review of the D-SIB assessment methodology including indicators used to assess systemic importance.
2. The Authority's proposed D-SIDTI Framework compares well across all the factors used to measure systemic importance albeit with the following adaptations based on national discretion:
  - (1) for the size factor, off-balance sheet assets are considered as part of supervisory overlay process rather than directly within the quantitative approach of the D-SIDTI Framework;
  - (2) for substitutability factor, payments activity is considered under supervisory overlay;
  - (3) for complexity factor, volume and nature of over-the-counter derivatives are also considered under supervisory overlay; and
  - (4) an additional factor to incorporate domestic context is included in the D-SIDTI Framework. This additional factor is based on resident deposits from households in the Cayman Islands.
3. With regards to weighting of the factors used to measure systemic importance, the BCBS D-SIB Framework provides for national authorities to exercise discretion as appropriate for their jurisdictions. In this regard, the proposed framework for Cayman Islands assigns equal weighting to each factor category (including sub-factors within each category). This approach is similar to the United Kingdom's framework.
4. With regards to calibration and imposition of HLA Requirement, most of the jurisdictions use a bucketing approach with graduated HLA Requirement based on a systemic score. Additionally, most of the jurisdictions require that the HLA Requirement be met from Common Equity Tier 1 capital (CET1 capital). The approach proposed under the Authority's D-SIDTI Framework is consistent with these, albeit with HLA Requirement being met through an increase in minimum capital requirements. The Authority continues to implement Basel III reforms and it is expected that, once Basel III capital requirements are introduced, the HLA Requirement will be met from CET1 capital.

## **F. Cost and Benefit Analysis**

5. **Table 1** provides a summary of the estimated costs and benefits of the proposed Measures.

**Table 1 – Estimated Costs and Benefits of Proposed Measures**

	<b>Costs</b>	<b>Benefits</b>
<b>CIMA</b>	<ol style="list-style-type: none"> <li>1. Development of the Measures and conducting consultations.</li> <li>2. Staff training on the implications of the Measures on supervision.</li> <li>3. Administrative costs of implementing the Measures comprising of the cost of undertaking the scoring process, applying supervisory judgment, producing the list of D-SIDTIs and performance of enhanced supervision in line with the Measures.</li> </ol>	<ol style="list-style-type: none"> <li>1. Enhances the Authority’s Risk Based Approach to supervision by applying differentiated intensity of supervision to D-SIDTIs based on the risks they pose to the local financial system and the real economy.</li> </ol>
<b>Cayman Islands</b>	<ol style="list-style-type: none"> <li>1. Potential for D-SIDTI currently in the Islands to exit the jurisdiction instead of complying with the higher capital and supervisory requirements.</li> <li>2. Gazettal of the Measures upon approval.</li> </ol>	<ol style="list-style-type: none"> <li>1. Enhances the macroprudential supervision by mitigating the impact on of failure of a D-SIDTI on the domestic financial system and/or real economy.</li> <li>2. Enhances the jurisdiction’s compliance with best practices for the supervision of D-SIDTIs.</li> </ol>
<b>Regulated Entities</b>	<ol style="list-style-type: none"> <li>1. Staff training on the requirements for compliance with the Measures.</li> <li>2. Administrative costs of implementing the requirements under the Measures.</li> </ol>	<ol style="list-style-type: none"> <li>1. Reduces probability of failure through the HLA Requirement.</li> <li>2. Improves risk management and corporate governance for the entities.</li> </ol>
<p>Overall, the benefits from the Measures outweigh the costs associated with their development, implementation and monitoring. Additionally, it is expected that the Measures will further strengthen the Authority’s macroprudential supervision and its Risk Based Approach to supervision.</p>		

**G. Consultation Feedback and Comments**

16. Before proceeding with the proposed Measures, the Authority shall have regard to any representations made by the private sector associations only. Feedback submitted by individuals, entities, or other bodies, unless acting on behalf of private sector associations, will not be accepted by the Authority. Representations from private sector associations must be submitted as a consolidated document, and a listing of the entities which provided feedback should be included. Private sector associations should ensure that conflicting positions are resolved prior to submission to the Authority. Where positions conflict within or across associations, the Authority will consider all available information in taking a decision, which will be at its sole discretion.
17. To ensure that all responses are given due consideration, it is important that private sector associations make clear reference to the sections of the measure being commented on, and that responses are unambiguous, clearly articulated and based on

fact. The consultation process is not designed to address complaints or grievances. Feedback of this nature should be submitted through the established complaints process.

18. In cases where the feedback proposes to change a policy position of the Authority or substantially amend any requirement of the draft measure, information to support the position of the association must be provided. The table below provides an example of the Authority’s expectation with regard to feedback for the proposed measure.

Reference	Example of a Helpful Comment	Examples of Comments needing more Support
Rule 4.2 <sup>2</sup>	<p>In Rule 4.2 the current text omits the fair value measurement of liabilities. Also, as defined it is not asymmetrical with the Market Price definition and thus scenarios exists that fall into neither category.</p> <p><b>Suggested wording:</b>  <i>Hard-to-Value Securities means an asset or liability for which there is no Market Price which is required to be measured at fair value pursuant to 5.2</i></p>	<ul style="list-style-type: none"> <li>× This is not what is done in other jurisdictions.</li> <li>× I don’t think we should do this.</li> <li>× CIMA is not considering the position of the experts.</li> </ul>

19. All feedback submitted by private sector associations will be given due consideration, nevertheless, the decision to adopt any feedback provided into a proposed measure will be at the sole discretion of the Authority.

## H. Notice of Representations

20. The Authority seeks consultation through written comments and representations from the private sector associations concerning the proposed:
- a) Regulatory Policy on Domestic Systemically Important Deposit Taking Institutions (**Appendix 1**); and
  - b) Rule on Domestic Systemically Important Deposit Taking Institutions (**Appendix 2**).
21. The Authority must receive representations by 1700hrs on **Wednesday February 1, 2023**. Representations received after this deadline may not be considered and will not form part of the collated written response provided to private sector associations.

<sup>2</sup> This example is not reflective of the content of the proposed measure.

22. Comments and representations must be addressed to<sup>3</sup>:

The Managing Director  
Cayman Islands Monetary Authority  
P.O. Box 10052  
SIX, Cricket Square  
Grand Cayman KY1-1001  
Cayman Islands  
Tel: 345-949-7089  
Fax: 345-946-5611  
Email:

[consultation@cima.ky](mailto:consultation@cima.ky)

and copied to [[KennedyMutunga@cima.ky](mailto:KennedyMutunga@cima.ky)]

23. The Authority shall have due regard to any representation made by the private sector associations and industry stakeholders. The Authority shall provide a written response collating the feedback received and the Authority's position on this feedback. This response shall be copied to all relevant private sector associations only.

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<sup>3</sup> Where the private sector association or industry stakeholder has no comments or representations on the proposed measure, it is recommended that the Authority be informed of this fact.





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