



Federal Financial Analytics, Inc.

KEY U.S. BASEL ISSUES OUTLINED IN PETROU TALK

“Throughout all of the years it will take the agencies to finalize Basel II and let your banks use it, the markets will be moving and critical M&A decisions await. It is, thus, I think an urgent priority to review this proposal, along with the IA one, in light of current and prospective market trends to decide whether your bank is a winner or loser and what you want to do in either case.”

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WASHINGTON, D.C. – The latest round of Basel rulemaking in the U.S. forces a series not only of “how-to” decisions, but also critical “should-we” ones, Federal Financial Analytics managing partner Karen Shaw Petrou today told the American Bar Association in Tampa, Florida. The talk also outlined the major points in the complex proposal released last week by the Federal Reserve Board.

Petrou noted with particular concern all the caveats in the latest Basel II proposal. She said, “The rule will be a work in progress even after it is finalized. Thus, for all its pages and every little detail, a bank can spend millions to comply and still not know if the Basel II standards apply.” She also criticized the decision to retain the leverage ratio – a unique U.S. standard that will offset the risk-based incentives fundamental to risk-based capital.

Petrou's talk also highlights ongoing problems related to the decision to retain a capital charge for operational risk, where the rule does not provide capital relief for risk mitigation as is, she said, rightly done for credit risk. The complexity of the rule is also daunting, arguing, Petrou said, for quick action on widely-understood problems in the current capital regime so that U.S. banks are not put at a competitive disadvantage to those around the world. For them, Basel II – without many of the issues raised by the U.S. proposal – is a reality, with banks coming under the new standards on January 1, 2007.

The Petrou speech is attached.

Federal Financial Analytics, Inc. has for the past eighteen years counseled large financial institutions and even their regulators on major legislative, regulatory and policy issues that pose strategic risk. It does not lobby on behalf of clients, but advises them on appropriate responses in light of identified challenges, working on an array of GSE, Basel II, and acquisition-value issues. The firm publishes numerous information and analytical services, including Financial Services Management and GSE Activity Report.

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