# Getting Crypto Capital Requirements Right

Tags: Basel Committee on Banking Supervision, Capital, Crypto Assets, Cryptocurrencies, Digital Assets

*ISDA Chief Executive Officer* ***Scott O'Malia*** *offers informal comments on important OTC derivatives issues in derivatiViews, reflecting ISDA's long-held commitment to making the market safer and more efficient.*

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For participants in the crypto-asset market, these have been unsettling times, with plummeting asset values, falling market capitalization and several high-profile casualties. Promoting appropriate risk management in this fledgling market has never been more important. That is why we welcome the Basel Committee's work to develop a robust capital framework for bank exposures to crypto assets.

On June 30, the Basel Committee published its latest consultation on the prudential treatment of banks' crypto-asset exposures. The new consultation builds on proposals first published last year and retains a generally conservative approach, but it achieves this through more risk-sensitive measures, rather than simply imposing onerous capital requirements.

A very punitive risk weight of 1,250% for crypto assets such as Bitcoin is replaced with a new category of assets that meet certain hedge recognition criteria. For assets in this new group, modified versions of standardized capital models could be used to calculate capital requirements.

But the Basel Committee has also introduced limits on how much banks can trade in this market. A new group-two exposure limit would cap a bank's total exposures at 1% of tier-one capital, applied at the aggregate level without the benefit of netting exposures. This would constitute a significant constraint on the extent to which banks can participate and may lead them to conclude it is not worth the investment.

Other changes have also been proposed, including the removal of the link between capital requirements and accounting treatment, which will avoid banks having to apply a capital deduction to crypto assets if classified as intangible assets under the accounting framework. In addition, a new infrastructure risk add-on of 2.5% of the exposure value has been introduced for all group-one assets to account for the risk associated with distributed ledger technology.

As we work with our members to evaluate the impact of the proposals, there is much to welcome in the latest iteration of the framework. The move away from a deliberately blunt, conservative capital requirement is a big step forward. We believe capital should be risk-sensitive, even if this requires a more complex methodology to effectively capture the risks in a relatively new market. In its proposal for the classification and capital treatment of crypto assets, the Basel Committee has made progress towards this approach.

But while the new proposal gives banks the leeway to hold risk-appropriate levels of capital and respond to client demand for intermediation in crypto assets, the exposure limit threatens to choke off that capacity by allowing only limited participation. The Basel Committee has said it will review the exposure limit periodically, but we believe the design and calibration of this additional measure should be reconsidered.

Given the volatile market conditions that have knocked confidence in crypto markets in recent months, it is clearly important that these standards are appropriately calibrated and closely monitored. We will continue to work with members and policymakers to achieve a framework that ensures bank participation in this market is appropriately capitalized.