BANK INDONESIA REGULATION
NUMBER: 5/12/PBI/2003
CONCERNING
THE MINIMUM CAPITAL REQUIREMENT FOR COMMERCIAL
BANKS TAKING ACCOUNT OF MARKET RISK

THE GOVERNOR OF BANK INDONESIA,

Considering: a. whereas in the calculation of bank capital, it is necessary to take account of credit risk and market risk;
   b. whereas to calculate market risk into bank capital, it is necessary to take preparatory measures so that in due time, banks will be able to comply with the minimum capital requirement taking account of market risk;
   c. now therefore it is deemed necessary to stipulate provisions concerning the minimum capital requirement for commercial banks taking account of market risk in a Bank Indonesia Regulation;

In view of: 1. Act Number 7 of 1992 concerning Banking (State Gazette of the Republic of Indonesia Number 31 of 1992, Supplement to the State Gazette Number 3472), as amended by Act Number 10 of 1998 (State Gazette of the Republic of Indonesia Number 182 of 1998, Supplement to the State Gazette Number 3790);
   2. Act Number 23 of 1999 concerning Bank Indonesia (State Gazette of the Republic of Indonesia Number 66 of 1999, Supplement to the State Gazette Number 3843);

3. Bank …
3. Bank Indonesia Regulation Number 3/21/PBI/2001 concerning Capital Adequacy for Commercial Banks (State Gazette of the Republic of Indonesia Number 149 of 2001, Supplement to the State Gazette Number 4158);

HAS DECREED:

To enact : THE BANK INDONESIA REGULATION CONCERNING THE MINIMUM CAPITAL REQUIREMENT FOR COMMERCIAL BANKS TAKING ACCOUNT OF MARKET RISK.

CHAPTER I
GENERAL PROVISIONS

Article 1

The terminology used in this Bank Indonesia Regulation has the following meanings:

1. Bank is a Commercial Bank as defined in Act Number 7 of 1992 concerning Banking as amended by Act Number 10 of 1998, including branch office of a foreign bank.

2. Market Risk is the risk of losses on balance sheet and off-balance sheet positions and from derivative transactions resulting from overall changes in market conditions, including risk of change in option prices.

3. Interest Rate Risk is the risk of losses resulting from changes in prices in the Bank position in the Trading Book brought about by changes in interest rates.

4. Foreign
4. Foreign Exchange Risk is the risk of losses resulting from changes in foreign currency values, including changes in gold prices, to the position of the Bank in the Trading Book and Banking Book.

5. Trading Book is the entire proprietary position of the Bank in financial instruments on balance sheet and off-balance sheet and in derivative transactions:
   a. intended to be held and resold in the short-term;
   b. held for purposes of short-term gain from actual and/or potential difference between selling value and buying value or from other price or from interest rate differential;
   c. generated from brokering and market making; or
   d. taken for hedging components of another Trading Book.

6. Banking Book is all other elements/positions not included in the Trading Book;

Article 2

(1) Banks meeting the criteria referred to in Article 3 are required to comply with the 8% (eight percent) minimum capital requirement taking account of market risk.

(2) Market Risk taken into account under this Bank Indonesia Regulation is:
   a. Interest Rate Risk, encompassing specific risk and general market risk; and
   b. Foreign Exchange Risk.

Article 3

(1) Banks required to take account of Market Risk as referred to in Article 2 paragraph (1) are Banks meeting one of the following criteria:
a. Bank with total assets equal to or greater than Rp 10,000,000,000,000 (ten trillion rupiahs);

b. Foreign Exchange Bank with a securities position and/or derivative transaction position in the Trading Book equal to or greater than Rp 20,000,000,000 (twenty billion rupiahs);

c. Non-Foreign Exchange Bank with a securities position and/or derivative transaction position in the Trading Book equal to or greater than Rp 25,000,000,000 (twenty-five billion rupiahs).

(2) The requirement for taking account of Market Risk in the minimum capital requirement as referred to in Article 2 paragraph (1) shall apply to Banks meeting the criteria referred to in paragraph (1) after the enactment of this Bank Indonesia Regulation and/or during the 3 (three) through 12 (twelve) most recent consecutive months prior to the enactment of this Bank Indonesia Regulation.

(3) The requirement for taking account of Market Risk as referred to in Article 2 paragraph (1) shall also apply to any Bank having an office network in other countries and any branch office of a Bank having its head office in another country (internationally active banks).

Article 4

Any Bank having met the criteria referred to in Article 3 shall be required to continue to take into account Market Risk in the minimum capital requirement, even though the Bank no longer meets the criteria referred to in Article 3.
CHAPTER II
CAPITAL
Article 5

(1) A Bank may include Tier 3 Capital for the purpose of calculating the minimum capital requirement.

(2) Inclusion of Tier 3 Capital into the calculation of the minimum capital requirement as referred to in paragraph (1) may only be used for calculation of Market Risk.

(3) Accounts that may be included as Tier 3 Capital as referred to in paragraph (1) are Short-Term Subordinated Loans meeting the following criteria:
   a. not guaranteed by the Bank concerned and paid up in full;
   b. having a contractual term of not less than 2 (two) years;
   c. may not be repaid in advance of the schedule stipulated in the loan agreement, unless approved by Bank Indonesia;
   d. contain a lock-in clause stipulating that no payment may be made of principal or interest, including payment at maturity, if the payment may cause the Bank to fail to comply with the minimum capital requirement under prevailing regulations.
   e. there is a clear loan agreement, including repayment schedule; and
   f. has prior approval from Bank Indonesia.

(4) Tier 3 Capital as referred to in paragraph (1) for taking account of Market Risk may only be used subject to the following criteria:
   a. not exceeding 250% (two hundred and fifty percent) of the portion of Tier 1 Capital allocated for taking account of Market Risk;
   b. the sum of Tier 2 Capital and Tier 3 Capital does not exceed 100% (one hundred percent) of Tier 1 Capital.

(5) Any unused Tier 2 Capital may be added to Tier 3 Capital subject to the requirements referred to in paragraph (4).

(6) Subordinated …
(6) Subordinated Loans as stipulated in prevailing regulations and exceeding 50% (fifty percent) of Tier 1 Capital may be used as a component of Tier 3 Capital notwithstanding such use shall be subject to the requirements referred to in paragraph (4).

CHAPTER III
MARKET RISK
Trading Book Policy and Guidelines

Article 6

(1) Banks are required to put together and apply Trading Book policy and guidelines as part of the risk management policy and guidelines of the Bank.

(2) The Trading Book policy and guidelines referred to in paragraph (1) shall be applied on a consistent basis.

Article 7

Bank Indonesia Certificates held by a Bank shall not be calculated into Market Risk.

Article 8

(1) Securities held by a Bank in portfolios available for sale shall be included in the Trading Book.

(2) Sharia bonds may only be held by a Bank for investment purposes, and shall therefore not be included in the Trading Book.

(3) A Bank may transfer sharia bonds as referred to in paragraph (2) to the Trading Book for the purpose of meeting liquidity needs.

Article 9 …
Article 9

(1) In calculating Market Risk, the mark to market process shall be applied to all positions in the Trading Book on a daily basis.

(2) In the event that market value is not available for the mark to market process as referred to in paragraph (1), appraisal of the Bank position shall be made using:
   a. the present value method during the period of up to 30 (thirty) days;  
   b. the present value and deflator factor method during the period after 30 (thirty) days through 1 (one) year.

(3) In the event that market value is still not available after a period of 1 (one) year as referred to in paragraph (2) letter b, then in departure from the provisions of Article 6 paragraph (2) the Bank shall be required to transfer the Trading Book position to the Banking Book.

(4) In the event that market value is not available after a period of 1 (one) year as referred to in paragraph (3), but notwithstanding the Bank will use a securities financial instrument as collateral in order to obtain a Short-Term Funding Facility (FPJP), the financial instrument shall in any event be booked in the Trading Book.

(5) Appraisal of the Bank position for the period referred to in paragraph (4) shall be made using the method referred to in paragraph (2) letter b.

Calculation of Market Risk

Article 10

Calculation of Market Risk into the capital adequacy ratio shall apply the Standard Method.
Article 11

(1) Calculation of Interest Rate Risk using the Standard Method as referred to in Article 10 shall be performed in respect of specific risk and general market risk in the Trading Book.

(2) The method used for calculation of general market risk may be the maturity method or duration method.

(3) Use of methods as referred to in paragraph (2) shall comply with requirements stipulated in a Circular Letter of Bank Indonesia.

(4) Capital charge in respect of Interest Rate Risk shall be applied with use of weighting as stipulated in a Circular Letter of Bank Indonesia.

Article 12

(1) For the purposes of Interest Rate Risk calculations by Banks, Bank Indonesia shall designate a recognized Rating Agency.

(2) The designation of Rating Agency as referred to in paragraph (1) shall be set forth in a Circular Letter of Bank Indonesia.

Article 13

(1) Calculation of Exchange Rate Risk by the Standard Method as referred to in Article 10 shall be performed for all positions in the Banking Book and Trading Book.

(2) Capital charge for the purpose of taking account of Exchange Rate Risk shall be applied at 8% (eight percent) of the existing Net Open Position.
CHAPTER IV
CALCULATION OF THE MINIMUM CAPITAL REQUIREMENT

Article 14

With the enactment of this Bank Indonesia Regulation, the required calculation of the minimum capital requirement for Banks as referred to in Article 3 shall cover:

a. the entire minimum capital requirement for risk-weighted assets based on credit risk factors as referred to in the prevailing regulation concerning the Minimum Capital Requirement for Commercial Banks, but not including positions in the Trading Book for which specific risk has been calculated for Interest Rate Risk; and

b. the entire minimum capital requirement for Market Risk as stipulated in this Bank Indonesia Regulation.

CHAPTER V
REPORTING

Article 15

(1) Banks are required to report positions calculated into Market Risk on a monthly basis on-line in accordance with the format stipulated by Bank Indonesia and with reference to the provisions concerning Commercial Bank Periodic Reports.

(2) Reporting as referred to in paragraph (1) shall be performed during the third report submission period for Commercial Bank Periodic Reports.

(3) For as long as it is not possible to submit reports on-line, Banks shall submit reports off-line to Bank Indonesia at the following addresses:

a. the relevant Directorate of Bank Supervision, Jl. M.H. Thamrin No. 2, Jakarta 10110, for a bank having its head office in the working area of the Bank Indonesia head office; or

b. the local …
b. the local Bank Indonesia Regional Office, for a Bank having its head office outside the working area of the Bank Indonesia head office, with a copy to the Directorate of Bank Licensing and Information, Jl. M.H. Thamrin No. 2, Jakarta 10110.

CHAPTER VI
TRANSITIONAL PROVISIONS

Article 16

(1) The requirement for Banks to comply with the minimum 8% (eight percent) capital requirement taking account of Market Risk at the end-of-month position shall come into force 18 (eighteen) months after the enactment of this Bank Indonesia Regulation.

(2) The requirement for Banks to report positions calculated into Market Risk and calculation of capital as referred to in Article 15 shall come into force commencing from the reporting of the December 2003 position.

(3) Prior to the enactment of the requirement for Banks to comply with the minimum 8% (eight percent) capital requirement taking account of Market Risk, Banks shall be required to maintain compliance with the minimum capital requirement in accordance with prevailing regulations.

CHAPTER VII
SANCTIONS

Article 17

Any Bank failing to comply with the minimum capital requirement as referred to in this Bank Indonesia Regulation shall be subject to administrative sanctions as referred to in the prevailing Bank Indonesia Regulations concerning the Minimum Capital Requirement.
Article 18

Any Bank failing to comply with reporting requirements as referred to in Article 15 shall be subject to sanctions as stipulated in the prevailing regulations concerning Commercial Bank Periodic Reports.

CHAPTER VIII
CONCLUDING PROVISIONS

Article 19

Further provisions to this Bank Indonesia Regulations shall be stipulated in a Circular Letter of Bank Indonesia.

Article 20

This regulation shall come into force on the date of its enactment

Enacted in Jakarta
Dated: July 17, 2003

THE GOVERNOR OF BANK INDONESIA

(signed)

BURHANUDDIN ABDULLAH

STATE GAZETTE OF THE REPUBLIC OF INDONESIA NUMBER 83 OF 2003
DPNP
ELUCIDATION
TO
BANK INDONESIA REGULATION
NUMBER: 5/12/PBI/2003
CONCERNING
THE MINIMUM CAPITAL REQUIREMENT FOR COMMERCIAL
BANKS TAKING ACCOUNT OF MARKET RISK

I. GENERAL REVIEW

One of the most fundamental aspects in the application of prudential banking principles is adequacy of bank capital. This has become a major focus of supervisory authorities and bank regulators around the world. The capital held by a bank must essentially be sufficient to cover all business risks faced by a bank. The major risks comprising the focus of attention are credit risk, market risk, and operational risk.

In this regard, the Basle Committee on Banking Supervision of the Bank for International Settlements, the key point of reference in this matter, adopted the 1988 Capital Accord concerning the method for calculation of capital taking account of credit risk. Subsequently in 1996, the Basle Committee on Banking Supervision amended the Capital Accord by including market risk.

Calculation of capital as currently applied in Indonesia accommodates the 1988 Capital Accord that takes account of credit risk Bank capital adequacy. Furthermore, pursuant to this Bank Indonesia Regulation, the calculation of the Bank capital adequacy shall also take into account Market Risk. Because the complexity of the methodology for calculation of Market Risk requires that banks attain a state of readiness, the application of Market Risk calculations shall be introduced in stages, commencing with the application of the Standard Method, while banks may use the Internal Model for internal …
for internal risk management purposes or in anticipation of future banking policy.

To enable banks to achieve the required capital taking into account Market Risk within the stipulated timeframe, the banking system needs to take preparatory steps in the management and calculation of Market Risk. Thus during the transitional period, Banks are required only to calculate and report Market Risk to Bank Indonesia. Subsequent to this, the requirement for calculation of Market Risk into Bank capital shall commence upon the expiration of the transitional period stipulated in this Bank Indonesia Regulation.

II. ARTICLE BY ARTICLE

Article 1

Number 1 through number 6
Self-explanatory.

Article 2

Paragraph (1)
Under this provision, the capital adequacy ratio shall be calculated by comparing capital with risk-weighted assets, both for credit risk and Market Risk.

Paragraph (2)
Specific risk is defined as risk of change in price of a financial instrument as a result of factors linked to the issuer of that financial instrument.

General market risk is defined as risk of change in prices of financial instruments as a result of general prices changes on the market.

Article 3 …
Article 3

Paragraph (1)
Letter a
Self-explanatory
Letter b and letter c
Securities position in Trading Book is defined as securities registered in the trading portfolio and in the portfolio available for sale at the Bank.

Paragraph (2)
Self-explanatory.

Paragraph (3)
Self-explanatory.

Article 4
Self-explanatory.

Article 5

Paragraph (1)
Self-explanatory.

Paragraph (2)
Self-explanatory.

Paragraph (3)
Self-explanatory.

Paragraph (4)
Letter a
Under this regulatory provision, at least 28.5% (twenty eight point five percent) of Market Risk shall be charged against Tier 1 Capital not used to cover credit risk from risk-weighted assets in accordance with the prevailing Bank Indonesia …
Indonesia regulation concerning the Minimum Capital Requirement.

Letter b

Tier 1 Capital and Tier 2 Capital is capital meeting the requirements stipulated in the prevailing regulations concerning the Minimum Capital Requirement.

Paragraph (5)

Tier 2 Capital that may be added is Tier 2 Capital meeting the requirements stipulated in the prevailing regulations concerning the Minimum Capital Requirement.

Paragraph (6)

Self-explanatory.

Article 6

Paragraph (1)

Self-explanatory.

Paragraph (2)

Under consistent application, Banks are not permitted to transfer any position in the Trading Book to the Banking Book.

Article 7

Bank Indonesia Certificates are not calculated into Market Risk in view of the fact that the secondary market for trading of Bank Indonesia Certificates has not been developed at this time.

Article 8

Paragraph (1)

Securities in this paragraph include but are not limited to securities sold by a Bank under a Repurchase Agreement.

Paragraph (2) …
Paragraph (2)
Self-explanatory.

Paragraph (3)
Self-explanatory.

Article 9

Paragraph (1)
The mark to market process shall apply market value as follows:

a. market value of financial instruments traded on the secondary market, e.g., Surabaya Stock Exchange, NASDAQ, Dow Jones, Nikkei, Han Seng, and Bloomberg;

b. if market value as referred to in letter a is not available, the value used is the value of the secondary market as referred to in letter a, formed from transactions occurring over not more than the latest 10 (ten) working days;

c. if market value as referred to in letters a and b is not available, the value used in the average quotation from a minimum of 2 (two) market makers or brokers.

Paragraph (2)
The definition of non-availability of market value includes market value formed from transactions that are insignificant in comparison to the position held by the Bank.

The deflator factor shall be applied taking into account factors such as the function of daily market turnover of securities and volume of the Bank position.

Paragraph (3)
Self-explanatory.

Paragraph (4)
Self-explanatory.

Paragraph (5) …
Paragraph (5)
Self-explanatory.

Article 10
In principle, according to the recommendations of the Basle Committee on Banking Supervision, Market Risk may also be calculated using the Internal Model. Notwithstanding, Bank Indonesia believes that for the time being, the Standard Method is more appropriate for calculation of Market Risk by Banks. The Internal Model for calculation of Market Risk may only be used on an internal basis for risk management and to anticipate future developments in banking policies.

Article 11
Paragraph (1)
Self-explanatory.
Paragraph (2)
Self-explanatory.
Paragraph (3)
Self-explanatory.
Paragraph (4)
Self-explanatory.

Article 12
Paragraph (1)
Self-explanatory.
Paragraph (2)
Self-explanatory.

Article 13 …
Article 13

Paragraph (1)
Self-explanatory.

Paragraph (2)
Net Open Position is defined as the Net Open Position as stipulated in the prevailing Bank Indonesia regulations concerning the Net Open Position for Commercial Banks.

Article 14
Self-explanatory.

Article 15

Paragraph (1)
Self-explanatory.

Paragraph (2)
Under this provision, the report for the position at December 2003 shall be submitted during the third report submission period, namely from the 16th day through the 21st day of January 2004.

Paragraph (3)
Reports submitted off-line shall be submitted on diskette and in hard copy.

Article 16

Paragraph (1)
Self-explanatory.

Paragraph (2)
Self-explanatory.

Paragraph (3)
Self-explanatory.

Article 17 …
Article 17
Self-explanatory.

Article 18
Self-explanatory.

Article 19
Self-explanatory.

Article 20
Self-explanatory.