

EBA/RTS/2016/02

13 June 2016

FINAL draft Regulatory Technical Standards

on Assigning Risk Weights to Specialised Lending Exposures under
Article 153(9) of Regulation (EU) No 575/2013 (Capital
Requirements Regulation – CRR)

1. Executive Summary

The Capital Requirements Regulation (CRR) and the Capital Requirements Directive (CRD)¹ set out prudential requirements for banks and other financial institutions which have been applied from 1 January 2014. Among other things, the CRR contains specific mandates for the EBA to develop draft regulatory technical standards (RTS) to specify how institutions shall take into account the following factors in assigning risk weights to specialised lending exposures: ‘financial strength, political and legal environment, transaction and/or asset characteristics, strength of the sponsor and developer, including any public private partnership income stream, and security package’. The EBA aims to fulfil this mandate through the final draft RTS specified in Section 3.

Main features of the draft RTS

Specialised lending exposures are a specific type of exposure, where the exposure relates to an entity which was created specifically to finance or operate physical assets or is an economically comparable exposure, the contractual arrangements give the lender a substantial degree of control over the assets and the income that they generate and the primary source of repayment of the obligation is the income generated by the assets being financed, rather than the independent capacity of a broader commercial enterprise. Within the Internal Ratings Based (IRB) approach, the CRR allows for a special treatment of specialised lending exposures, in the event that the institution is not able to estimate the Probabilities of Default (PDs) or the institution’s PD estimates do not meet the requirements of PD estimation. For these types of exposures, the CRR puts forward a set of supervisory risk weights, which have to be assigned on the basis of a classification in five categories, depending on the underlying credit risk, as well as the remaining maturity. This approach is also known as the supervisory slotting criteria approach for specialised lending exposures in the Basel framework.

These final draft RTS use the Basel framework as a baseline given that it has been adopted nationally in a number of EU Member States, although taking into account the European experiences. These final draft RTS define four classes of specialised lending: project finance, real estate, object finance or commodities finance. Within each class these final draft RTS specify how the factors, i.e. ‘financial strength, political and legal environment, transaction and/or asset characteristics, strength of the sponsor and developer, including any public private partnership income stream, and security package’ are to be taken into account. In addition, these final draft RTS specify how the abovementioned factors should be combined in order to determine the final assignment to a category.

¹ Regulation (EU) No 575/2013 of 26 June 2013 of the European Parliament and of the Council on prudential requirements for credit institutions and investment firms and amending Regulation (EU) No 648/2012, and Directive 2013/36/EU of the European Parliament and of the Council of 26 June 2013 on access to the activity of credit institutions and the prudential supervision of credit institutions and investment firms, amending Directive 2002/87/EC and repealing Directives 2006/48/EC and 2006/49/EC.

In order to tailor the reported information to the specific supervisory treatment of specialised lending exposure, these final draft RTS propose specific documentation requirements.

Finally, the EBA acknowledges that institutions may require additional time to implement the framework set out in these final draft RTS. The current framework is already in place in many jurisdictions, but the additional elements, such as the combination of factors, may give rise to changes in the current processes of institutions. Consequently, it is proposed that these final draft RTS apply from one year after the time of publication.

2. Background and introduction

The Capital Requirements Regulation (CRR) and the Capital Requirements Directive (CRD)² set out prudential requirements for banks and other financial institutions which have been applied from 1 January 2014. Among other things, the CRR contains specific mandates for the EBA to develop draft regulatory technical standards (RTS) to specify how institutions shall take into account the following factors in assigning risk weights to specialised lending exposures: ‘financial strength, political and legal environment, transaction and/or asset characteristics, strength of the sponsor and developer, including any public private partnership income stream, and security package’.

Background to the final draft RTS

Specialised lending exposures are a special type of exposure within the corporate exposure class in the Internal Models Based (IRB) approach. The CRR defines specialised lending exposures in Article 147(8) of the CRR as follows:

- (a) the exposure is to an entity which was created specifically to finance or operate physical assets or is an economically comparable exposure;
- (b) the contractual arrangements give the lender a substantial degree of control over the assets and the income that they generate;
- (c) the primary source of repayment of the obligation is the income generated by the assets being financed, rather than the independent capacity of a broader commercial enterprise.

Article 153(5) of the CRR specifies ‘For specialised lending exposures in respect of which an institution is not able to estimate PDs or the institutions’ PD estimates do not meet the requirements set out in Section 6³, the institution shall assign risk weights to these exposures according to Table 1, as follows:

² Regulation (EU) No 575/2013 of 26 June 2013 of the European Parliament and of the Council on prudential requirements for credit institutions and investment firms and amending Regulation (EU) No 648/2012, and Directive 2013/36/EU of the European Parliament and of the Council of 26 June 2013 on access to the activity of credit institutions and the prudential supervision of credit institutions and investment firms, amending Directive 2002/87/EC and repealing Directives 2006/48/EC and 2006/49/EC.

³ On the requirements for the IRB approach.

Remaining Maturity	Category 1	Category 2	Category 3	Category 4	Category 5
Less than 2.5 years	50%	70%	115%	250%	0%
Equal or more than 2.5 years	70%	90%	115%	250%	0%

In assigning risk weights to specialised lending exposures, institutions shall take into account the following factors: ‘financial strength, political and legal environment, transaction and/or asset characteristics, strength of the sponsor and developer, including any public private partnership income stream, and security package’.

The EBA has the mandate (stemming from Article 153(9) of the CRR) to develop the RTS to specify how institutions shall take into account these factors in assigning risk weights to specialised lending exposures for which an institution is not able to estimate PDs or the institutions’ PD estimates do not meet the requirements.

The current Basel text (Annex 6) contains detailed criteria for assessing the credit risk of different types of specialised lending, which are referred to as the slotting criteria. Given the well-established use of these criteria, these final draft RTS are drafted on the basis of this international guidance.

The Basel text includes five sub-classes of specialised lending: project finance, object finance, commodities finance, income-producing real estate, and high-volatility commercial real estate. However, Annex 6 of the Basel text contains only four tables with supervisory slotting criteria for specialised lending: (1) project finance, (2) income-producing real estate and high-volatility commercial real estate, (3) object finance and (4) commodities finance. As such, Basel does not differentiate the slotting criteria for income-producing real estate and high-volatility commercial real estate. Given that the CRR does not include specific requirements which differentiate between income-producing real estate and high-volatility commercial real estate, these final draft RTS differentiate between the four mentioned classes and include separate assessment criteria in order to take into account the factors of financial strength, political and legal environment, transaction and/or asset characteristics, strength of the sponsor and developer and security package. This approach ensures that the assessment criteria are tailored to the nature and specificities of the different specialised lending exposure.

These final draft RTS specify how the abovementioned factors, as well as the sub-factors which lay down further specifications of these factors, should be assessed, as well as how institutions should combine these factors in order to determine the final assignment to a category. In particular, these draft RTS require institutions to specify the weight that they assign to each factor, where that weight should not be lower than 5% and not be higher than 60%. On this basis,

institutions should calculate the weighted average of the (cardinal) numbers of the categories to which the exposure has been assigned to for each factor.

For the purpose of assigning a specialised lending exposure to a category ranging from 1 to 5, institutions should first verify whether a specialised lending exposure is considered in default in accordance with the conditions set out in Article 178 of the CRR. When a specialised lending exposure is considered to be in default, institutions shall assign that exposure to category 5. When a specialised lending exposure is considered not to be in default, institutions should assign that exposure to category 1, 2, 3 or 4 by taking into account the assessment criteria which are laid out in Annexes I–IV.

In order to tailor the reported information to the specific supervisory treatment of specialised lending exposure, these final draft RTS set out specific documentation requirements.

Finally, banks are given a period of 1 year from the time of publication. The EBA acknowledges that banks may require time to amend current processes, despite the fact that large elements of these final draft RTS are aligned with the existing frameworks in place at national authorities. However, some elements, such as the combination of factors, just as country-specific implementation may require changes to existing processes. Consequently, the EBA – in response to the industry feedback – have introduced a 1-year phase-in of these final draft RTS.

Advantages and disadvantages of the slotting approach

The slotting approach used for specialised lending exposures is part of the IRB framework in the CRR. The use of this approach is motivated by the fact that, for these exposures, it is not always possible to estimate PD (and/or LGD) or the PD estimates do not meet the requirements of the CRR. The slotting approach, however, allows capital requirements to be determined in a risk-sensitive way, consistent with the risk profile of the relevant specialised lending exposures, which allows an ordinal ranking of the risk of these exposures.

The EBA is currently in the process of reviewing the overall IRB framework, as illustrated in a recent discussion paper on the future of the IRB approach⁴. The slotting approach has, however, received limited attention in this regard, due to its application to only around one-quarter of all specialised lending exposures under the IRB approach⁵. However, the EBA enquired, through the consultation paper (CP) that was published for these draft RTS, about the usefulness of the slotting approach in a broader context. In particular, the EBA questioned stakeholders on the operational challenges of using the slotting approach, whether it is possible to obtain comparable capital requirements across institutions using the slotting approach, and whether the slotting approach should be extended to other types of exposures. The results of this enquiry are presented in Section 4.2.

⁴ See <http://www.eba.europa.eu/regulation-and-policy/credit-risk/discussion-paper-on-the-future-of-the-irb-approach>.

⁵ See Table 3 in Section 4 of this final draft RTS.

3. Final draft RTS on Assigning Risk Weights to Specialised Lending Exposures

COMMISSION DELEGATED REGULATION (EU) .../..

of XXX

supplementing Regulation (EU) No 575/2013 of the European Parliament and of the Council with regard to regulatory technical standards for assigning risk weights to specialised lending exposures

(Text with EEA relevance)

THE EUROPEAN COMMISSION,

Having regard to the Treaty on the Functioning of the European Union,

Having regard to Regulation (EU) No 575/2013 of the European Parliament and of the Council of 26 June 2013 on prudential requirements for credit institutions and investment firms and amending Regulation (EU) No 648/2012⁶, and in particular the third subparagraph of Article 153(9) thereof, Whereas:

- (1) In accordance with Article 153(5) of Regulation (EU) No 575/2013, institutions are required, for the purpose of assigning risk weights to a specialised lending exposure, to assess the remaining maturity of the exposure and assign the exposure to a category ranging from 1 to 5 as referred to in Table 1 of the first subparagraph of that Article. As a result, for the purpose of taking into account the factors referred to in the second subparagraph of Article 153(5) of Regulation (EU) No 575/2013 when assigning risk weights to specialised lending exposures, institutions should essentially assign the specialised lending exposure to one of the categories of Table 1 referred to in the first subparagraph of that Article based on their assessment of each specialised lending exposure against each of those factors. In order to ensure a harmonised approach with regard to the assignment of specialised lending exposures to categories, it is appropriate to specify how factors should be taken into account by linking the relevant factors directly to the corresponding categories of that Table.

⁶ OJ L 176, 27.6.2013, p. 1.

- (2) In order for the institutions to adequately take into account each of the factors of financial strength, political and legal environment, transaction and/or asset characteristics, strength of the sponsor and developer, and security package when assigning risk weights to specialised lending exposures, it is appropriate to specify those factors in the form of sub-factors which provide further clarification about the assessment criteria for each of them. In order to adequately assess certain sub-factors, it is furthermore necessary to specify those sub-factors in sub-factor components.
- (3) In order to take into account the specificities of different classes of specialised lending exposures, such as project finance, real estate, object finance and commodities finance, with regard to their purpose and the origin of the income generated by the assets, in accordance with Article 147(8) of Regulation (EU) No 575/2013, it is appropriate to provide different assessment criteria for each of those classes to be applied when taking into account the factors referred to in the second subparagraph of Article 153(5) of that Regulation. Accordingly, institutions should assign the specialised lending exposures subject to the treatment of Article 153(5) of Regulation (EU) No 575/2013 to that class which most closely corresponds to the description of one of those classes. This is also consistent with the internationally-agreed standards on assigning risk weights to specialised lending exposures, as specified by the Basel Committee on Banking Supervision in the Basel II framework⁷ ('BCBS standards').
- (4) Where a default is considered to have occurred with regard to an exposure in accordance with Article 178 of Regulation (EU) No 575/2013, the risk of losses is so great that the institutions should assign the exposure to category 5 of Table 1 in the first subparagraph of Article 153(5) of Regulation (EU) No 575/2013. This is consistent with the higher expected loss values for specialised lending exposures assigned to category 5 as referred to in Table 2 of Article 158(6) of Regulation (EU) No 575/2013 and is consistent with the approach taken in the BCBS standards.
- (5) Institutions should combine the assignments to categories of the sub-factor components to determine the assignments to categories of the sub-factors, where relevant, and determine the assignments to categories of the sub-factors to determine the assignments to categories of the factors, on the basis of their relative importance. In order to achieve consistency in the assignment of specialised lending exposures to categories and in line with the requirement of consistency in the assignment to grades or pools, referred to in point (a) of Article 171(1) of Regulation (EU) No 575/2013, institutions should specify for each type of exposure how the different factors are combined in the final assignment of the specialised

⁷ International Convergence of Capital Measurement and Capital Standards, A Revised Framework, Comprehensive Version, June 2006.

lending exposure to one of the categories of Table 1 of the first subparagraph of Article 153(5) of Regulation (EU) No 575/2013. The final assignment to a category should be done on the basis of the weighted average of the cardinal numbers of the categories to which the exposure has been assigned, for each factor. In order to ensure that institutions assign risk weights to specialised lending exposures in a sufficiently prudent way, a minimum and a maximum weight should be laid down. The weight that institutions assign to each factor should not be lower than that minimum weight and not be higher than that maximum weight.

- (6) In order to ensure the possibility to review the correct application of the rules regarding specialised lending exposures, institutions should be required to sufficiently document their decisions regarding how to take into account the factors referred to in the second subparagraph of Article 153(5) of Regulation (EU) No 575/2013. In that context, it is appropriate to require them to document several of the elements of the process of how risk weights are assigned to specialised lending exposures according to this Regulation. Given Article 175 of Regulation (EU) No 575/2013 requires institutions to document the assignment of risk weights under the IRB approach, it is appropriate to specify those documentation requirements with regard to the specific methodology for assigning risk weights to the specialised lending exposures as referred to in Article 153(5) of that Regulation.
- (7) As specified in the first subparagraph of Article 153(5) of Regulation (EU) No 575/2013, the framework for assigning risk weights to specialised lending exposures provided by this Regulation is an alternative rating system for the assignment of risk weights by an institution in accordance with the IRB approach. This becomes evident from the fact that specialised lending exposures subject to the treatment referred to in Article 153(5) of Regulation (EU) No 575/2013 belong to the corporate exposure class within the IRB approach, and the reference to Article 153(5) of that Regulation also in Article 170(2) of that Regulation, which refers to the structure of rating systems. As a result, all requirements of the IRB approach mentioned in that Regulation with regard to rating systems, apply, to the extent relevant and in accordance with the first sub-paragraph of Article 153(5) of that Regulation, also to these specialised lending exposures. This includes, amongst others, the requirements for assigning exposures to grades or pools in accordance with Article 171 of that Regulation, in particular the requirements for applying conservatism where institutions have less information on certain factors or sub-factors in accordance with Article 171(2) of that Regulation, as well as the possibility of deviating from the final assignment to one of the categories of Table 1 of the first subparagraph of Article 153(5) of Regulation (EU) No 575/2013 or deviating from the assignment to one of the factors, sub-factors or parts of these sub-factors, in accordance with Article 172(3) of that Regulation. Further, the application of the rules for assigning specialised lending exposures to the relevant

categories should be based on the relevant rules for each type of exposures within the meaning of Article 142(1)(2) of Regulation (EU) No 575/2013.

- (8) In order to ensure a harmonised application of the framework for the assignment of specialised lending exposures to the relevant categories of Article 153(5) of Regulation (EU) No 575/2013, institutions should be required to consider all factors and sub-factors provided in the Annexes to this Regulation. Nevertheless, as a result of the application of the IRB provisions for applying overrides in accordance with Article 172(3) of Regulation (EU) No 575/2013 also with regard to specialised lending exposures, where institutions do not apply a certain sub-factor or sub-factor component, for an individual specialised lending exposure, on the basis of that sub-factor or sub-factor component not being relevant, this should be considered as an override. Where institutions do not apply a certain sub-factor or sub-factor component for a particular type of specialised lending exposures within the meaning of Article 142(1)(2) of Regulation (EU) No 575/2013, on the basis of their not being relevant, institutions should also be required to document this decision and provide a justification for why this sub-factor or sub-factor component is irrelevant for all specialised lending exposures belonging to that type of specialised lending exposure.
- (9) Further, given the breadth and variety of specialised lending exposures and given the specificities of such exposures, it could be argued that the existing international standards for specialised lending exposures assignment to relevant categories, on which this Regulation is based, do not fully capture all potentially relevant risk drivers, which institutions might identify in their daily business, for either particular types of exposures within the meaning of Article 142(1)(2) of Regulation (EU) No 575/2013 or for individual specialised lending exposures or for both. As a result, in those exceptional cases, and based on the requirements of Article 171(2) of Regulation (EU) No 575/2013 for institutions to take into account all relevant information, it should be possible for institutions to consider that additional risk driver jointly with the sub-factor which most closely corresponds to that risk driver of the specialised lending exposure framework, documenting those decisions and their appropriateness. Where this situation occurs for an individual specialised lending exposure, this should be considered as the application of an override.
- (10) It is appropriate to allow the institutions a sufficient period of time to adapt their system for assigning risk weights to specialised lending exposures in order to comply with the rules laid down in this Regulation.
- (11) This Regulation is based on the draft regulatory technical standards submitted by the European Banking Authority to the Commission.
- (12) The European Banking Authority has conducted open public consultations on the draft regulatory technical standards on which this Regulation is based, analysed the potential related costs and benefits and requested the opinion of the Banking

Stakeholder Group established in accordance with Article 37 of Regulation (EU) No 1093/2010 of the European Parliament and of the Council⁸,

HAS ADOPTED THIS REGULATION:

Article 1

Process for taking into account the factors affecting risk weights

1. When assigning risk weights to specialised lending exposures in respect of which the obligors are in default as set out in Article 178 of Regulation (EU) No 575/2013, institutions shall do all of the following:
 - (a) determine to which class of exposure ('project finance', 'real estate', 'object financing', 'commodities financing' as referred to in Article 2) the specialised lending exposure belongs;
 - (b) take into account the factors referred to in the second subparagraph of Article 153(5) of that Regulation by assigning those exposures to category 5 of Table 1 set out in Article 153(5).
2. When assigning risk weights to other specialised lending exposures than those referred to in paragraph 1, institutions shall take into account the factors referred to in the second subparagraph of Article 153(5) of Regulation (EU) No 575/2013, by proceeding in accordance with the following sequence:
 - (a) they shall determine to which class of exposure ('project finance', 'real estate', 'object financing', 'commodities financing' as referred to in Article 2) the specialised lending exposure belongs and which assessment criteria among those referred to in Annexes 1 to 4 are applicable to the specialised lending exposure, in accordance with Article 2;
 - (b) they shall assess the specialised lending exposure with reference to each factor, against the assessment criteria provided for each of the sub-factors, some of which are, in turn, further specified in sub-factor components, contained in the relevant Annex to this Regulation;
 - (c) they shall assign the specialised lending exposure to category one, two, three or four of Table 1 of Article 153(5) of Regulation (EU) No 575/2013, in accordance with paragraphs 3 and 4.
3. For the purposes of determining to which overall category the specialised lending exposure is to be assigned in accordance with paragraph 2(c), institutions shall do all of the following:
 - (a) where one or several of the sub-factors are further specified in sub-factor components, determine the cardinal numbers of the categories to which the specialised lending exposure is assigned for each sub-factor component on the

⁸ Regulation (EU) No 1093/2010 of the European Parliament and of the Council of 24 November 2010 establishing a European Supervisory Authority (European Banking Authority), amending Decision No 716/2009/EC and repealing Commission Decision 2009/78/EC (OJ L 331, 15.12.2010, p. 12).

basis of the assessment referred to in paragraph 2(b), and combine the assignments of these sub-factor components on the basis of their relative importance to determine the cardinal numbers of the categories of these sub-factors;

(b) where none of the sub-factors are further specified in sub-factor components, determine the cardinal numbers of the categories to which the specialised lending exposure is assigned for each sub-factor on the basis of the assessment referred to in paragraph 2(b);

(c) combine the assignments of the sub-factors on the basis of their relative importance to determine the cardinal number of the categories of the respective factors;

(d) specify the weight in percentage that they assign to each factor, on the basis of the relative importance of each factor under the condition that such a weight is not lower than 5% and not higher than 60%;

(e) determine the weighted average of the cardinal numbers of the categories under which they have classified the specialised lending exposure for all factors;

(f) where the weighted average is a decimal number, round that number to the nearest cardinal number;

(g) assign the specialised lending exposure to category one, two, three or four of Table 1 of Article 153(5) of Regulation (EU) No 575/2013 on the basis of that weighted average referred to in points (e) and (f).

4. Where the assessment criteria provided for one or several of the sub-factors are the same across several categories for that sub-factor ('overlapping criteria'), institutions shall assign the relevant factor to a category based on the assignment of the specialised lending exposure of the sub-factors with no overlapping criteria. Where the combined assignment based on the sub-factors with no overlapping criteria is to a lower cardinal number than the combined assignment of the sub-factors with the overlapping criteria, they shall make appropriate and conservative adjustments to that assignment. Where there are overlapping criteria for one or several of the sub-factor components, institutions shall apply the same principle.

Article 2

Applicable assessment criteria for different classes of specialised lending exposures

For the purposes of point (a) of Article 1(2), all of the following shall apply:

(a) where the purpose of the specialised lending exposure is to finance the development or acquisition of large, complex and expensive installations, in particular, power plants, chemical processing plants, mines, transportation infrastructure, environment, and telecommunications infrastructure, so that the income generated by the assets is the money generated by the contracts for the facility's output obtained from one or several third parties ('project finance exposures'), institutions shall apply the assessment criteria referred to in Annex I;

- (b) where the purpose of the specialised lending exposure is to finance the development or acquisition of real estate, including, in particular, office buildings to let, retail space, multifamily residential buildings, industrial or warehouse space, hotels, and land, so that the income generated by the real estate is lease or rental payments or the proceeds from the sale of such real estate obtained from one or several third parties ('real estate exposures'), institutions shall apply the assessment criteria referred to in Annex II;
- (c) where the purpose of the specialised lending exposure is to finance the acquisition of physical assets, including in particular ships, aircraft, satellites, railcars, and fleets, so that the income generated by the assets is lease or rental payments obtained from one or several third parties ('object financing exposures'), institutions shall apply the assessment criteria referred to in Annex III;
- (d) where the purpose of the specialised lending exposure is to finance reserves, inventories or receivables of exchange-traded commodities, including, in particular, crude oil, metals, or crops, so that the income generated by the assets would typically be the proceeds from the sale of the commodity ('commodities financing exposures'), institutions shall apply the assessment criteria referred to in Annex IV.

Article 3
Documentation

1. Institutions shall document for each type of specialised lending exposure the assignment of weights to each factor and the justification for these assignments in accordance with Article 1(3)(d).
2. Institutions shall document all of the following information for each specialised lending exposure for which they assign risk weights in accordance with Article 153(5) of Regulation (EU) No 575/2013:
 - (a) the class of the specialised lending exposure;
 - (b) the category of Table 1 of the first subparagraph of Article 153(5) of Regulation (EU) No 575/2013 to which the specialised lending exposure has been assigned;
 - (c) the remaining maturity in accordance with Table 1 of the first subparagraph of Article 153(5) of Regulation (EU) No 575/2013;
 - (d) the assessment of the specialised lending exposure at each step of the process referred to in Article 1 that led to its assignment to one of the categories of Table 1 of the first subparagraph of Article 153(5) of Regulation (EU) No 575/2013.

Article 4
Entry into force

This Regulation shall enter into force on the twentieth day following that of its publication in the *Official Journal of the European Union*.

It shall apply from [Instructions to the PO: insert a date one year after the date of publication].

This Regulation shall be binding in its entirety and directly applicable in all Member States.

Done at Brussels,

For the Commission

The President
On behalf of the President

Annex I – Assessment criteria for project finance exposures

	Category 1	Category 2	Category 3	Category 4
Factor: financial strength				
(a) Sub-factor: market conditions	Few competing suppliers or substantial and durable advantage in location, cost, or technology. Demand is strong and growing.	Few competing suppliers or better than average location, cost, or technology but this situation may not last. Demand is strong and stable.	Project has no advantage in location, cost, or technology. Demand is adequate and stable.	Project has worse than average location, cost, or technology. Demand is weak and declining.
(b) Sub-factor: financial ratios (e.g. debt service coverage ratio (DSCR ⁹), Interest Coverage Ratio (ICR ¹⁰), loan life coverage ratio (LLCR ¹¹) and debt-to-equity ratio)	Strong financial ratios considering the level of project risk; very robust economic assumptions.	Strong to acceptable financial ratios considering the level of project risk; robust project economic assumptions.	Standard financial ratios considering the level of project risk	Aggressive financial ratios considering the level of project risk.
(c) Sub-factor: stress analysis on the basis of the income being generated during the tenor of the loan ¹²	The project can meet its financial obligations under sustained, severely stressed economic or sectoral conditions.	The project can meet its financial obligations under normal stressed economic or sectoral conditions. The project is only likely to default under severe economic conditions.	The project is vulnerable to stresses that are not uncommon through an economic cycle, and may default in a normal downturn.	The project is likely to default unless conditions improve soon.
(d) Sub-factor: financial Structure				
<ul style="list-style-type: none"> • Amortisation schedule (sub-factor component) 	Amortising debt without bullet repayment	Amortising debt with no or insignificant bullet repayment	Amortising debt repayments with limited bullet payment.	Bullet repayment or amortising debt repayments with high bullet repayment.
<ul style="list-style-type: none"> • Market/cycle and refinancing risk (sub-factor component) 	There is no or very limited exposure to market or cycle risk since the expected cashflows cover all future loan repayments during the tenor of the loan and there are no significant delays between the cashflows and the loan	The exposure to market or cycle risk is limited since the expected cashflows cover the majority of future loan repayments during the tenor of the loan and there are no significant delays between the	There is moderate exposure to market or cycle risk since the expected cashflows cover only a part of future loan repayments during the tenor of the loan or there are some significant delays	There is significant exposure to market or cycle risk since the expected cashflows cover only a small part of future loan repayments during the tenor of the loan or there are some significant

⁹ The Debt Service Coverage ratio ('DSCR') refers to the ratio of the cashflow available for debt service which can be generated from the asset to the required repayment of the principal and the interest payments during the life of the loan, where the cashflow available for debt service is calculated by subtracting operating expenditure, capital expenditure, debt and equity funding, taxes and working capital adjustments from the revenues generated by the project.

¹⁰ The Interest Coverage Ratio ('ICR') refers to the ratio of the cashflow available for debt service which can be generated from the asset to the required repayment of the interest payments during the life of the loan, where the cashflow available for debt service is calculated by subtracting operating expenditure, capital expenditure, debt and equity funding, taxes and working capital adjustments from the revenues generated by the project.

¹¹ The Loan Life Coverage Ratio ('LLCR') refers to the ratio of the net present value of the cashflow available for debt service to the outstanding debt balance, and refers to the number of times the cashflow available for debt service which can be generated from the asset can repay the outstanding debt balance over the scheduled life of the loan, where the cashflow available for debt service calculated by subtracting operating expenditure, capital expenditure, debt and equity funding, taxes and working capital adjustments from the revenues generated by the project.

¹² The tenor of a loan refers to the amount of time left for the repayment of a loan.

	repayments. There is no or very low refinancing risk.	cashflows and the loan repayments. There is low refinancing risk.	between the cashflows and the loan repayments. Average refinancing risk.	delays between the cashflows and the loan repayments. High refinancing risk.
(e) Sub-factor : foreign exchange risk	There is no foreign exchange risk because there is no difference in the currency of the loan and the income of the project or because the foreign exchange risk is fully hedged.	There is no foreign exchange risk because there is no difference in the currency of the loan and the income of the project or because the foreign exchange risk is fully hedged.	There is a difference in the currency of the loan and the income of the project, but the foreign exchange risk is considered low because the exchange rate is stable or because the foreign exchange risk is hedged to a large extent.	There is a difference in the currency of the loan and the income of the project, and the foreign exchange risk is considered high because the exchange rate is volatile and the foreign exchange risk is not hedged to a large extent.
Factor: political and legal environment				
(a) Sub-factor: political risk, including transfer risk, considering project type and mitigants	Very low exposure; strong mitigation instruments, if needed	Low exposure; satisfactory mitigation instruments, if needed	Moderate exposure; fair mitigation instruments	High exposure; no or weak mitigation instruments
(b) Sub-factor: force majeure risk (war, civil unrest, etc)	No or very low exposure to force majeure risk	Limited exposure to force majeure risk	Significant exposure to force majeure risk which is not sufficiently mitigated	Significant exposure to force majeure risk which is not mitigated
(c) Sub-factor: government support and project's importance for the country over the long term	Project of strategic importance for the country (preferably export-oriented). Strong support from Government	Project considered important for the country. Good level of support from Government	Project may not be strategic but brings unquestionable benefits for the country. Support from Government may not be explicit	Project not key to the country. No or weak support from Government
(d) Sub-factor: stability of legal and regulatory environment (risk of change in the law)	Favourable and stable regulatory environment over the long term	Favourable and stable regulatory environment over the medium term	Regulatory changes can be predicted with a fair level of certainty	Current or future regulatory issues may affect the project
(e) Sub-factor: acquisition of all necessary supports and approvals for such relief from local content laws	Strong	Satisfactory	Fair	Weak
(f) Sub-factor: enforceability of contracts, collateral and security	Contracts, collateral and security are enforceable	Contracts, collateral and security are enforceable	Contracts, collateral and security are considered enforceable even if certain non-key issues may exist	There are unresolved key issues in respect if actual enforcement of contracts, collateral and security
Factor: transaction characteristics				
(a) Sub-factor: design and technology risk	Fully proven technology and design	Fully proven technology and design	Proven technology and design — start-up issues are mitigated by a strong completion package	Unproven technology and design; technology issues exist and/or complex design.
(b) Sub-factor: construction risk				
• Permitting and siting (sub-factor component)	All permits have been obtained	Some permits are still outstanding but their receipt is considered very likely	Some permits are still outstanding but the permitting process is well defined and they are considered routine.	Key permits still need to be obtained and are not considered routine. Significant conditions may be attached.

<ul style="list-style-type: none"> Type of construction contract (sub-factor component) 	Fixed-price date-certain turnkey construction EPC 13 (engineering and procurement contract)	Fixed-price date-certain turnkey construction EPC	Fixed-price date-certain turnkey construction contract with one or several contractors	No or partial fixed-price turnkey contract and/or interfacing issues with multiple contractors
<ul style="list-style-type: none"> Likelihood to finish the project at the agreed time and cost (sub-factor component) 	It is almost certain that the project will be finished within the agreed time horizon and at the agreed cost.	It is very likely that the project will be finished within the agreed time horizon and at the agreed cost.	It is uncertain whether the project will be finished within the agreed time horizon and at the agreed cost.	There are indications that the project will not be finished within the agreed time horizon and at the agreed cost.
<ul style="list-style-type: none"> Completion guarantees¹⁴ or liquidated damages¹⁵ (sub-factor component) 	Substantial liquidated damages supported by financial substance and/or strong completion guarantee from sponsors with excellent financial standing	Significant liquidated damages supported by financial substance and/or completion guarantee from sponsors with good financial standing	Adequate liquidated damages supported by financial substance and/or completion guarantee from sponsors with good financial standing	Inadequate liquidated damages or not supported by financial substance or weak completion guarantees
<ul style="list-style-type: none"> Track record and financial strength of contractor in constructing similar projects (sub-factor component) 	Strong	Good	Satisfactory	Weak
(c) Sub-factor: operating risk				
<ul style="list-style-type: none"> Scope , nature and complexity of operations and maintenance (O & M) contracts (sub-factor component) 	Strong long-term O&M contract ¹⁶ , preferably with contractual performance incentives ¹⁷ , and/or O&M reserve accounts ¹⁸ , although an O&M contract is not strictly necessary to perform the required maintenance because the O&M activities are straightforward and transparent	The O&M activities are relatively straightforward and transparent, and there is a long-term O&M contract, and/or O&M reserve account	The O&M activities are complex and an O&M contract is necessary. There is a limited long-term O&M contract and/or reserve account	The O&M activities are complex and an O&M contract is strictly necessary. There is no O&M contract. There is therefore the risk of high operational cost overruns beyond mitigants.
<ul style="list-style-type: none"> Operator's expertise, track record, and financial strength (sub-factor component) 	Very strong, or committed technical assistance of the sponsors	Strong	Acceptable	Limited/weak, or local operator dependent on local authorities

¹³ An Engineering and Procurement Contract ('EPC') or 'turnkey contract' refers to an agreement between the engineering and procurement contractor ('EPC contractor') and the developer, whereby the EPC contractor agrees to develop the detailed engineering design of the project, procure all the equipment and materials necessary, construct and deliver a functioning facility or asset to the developer, usually within an agreed time and budget.

¹⁴ A completion guarantee refers to a guarantee provided by the contractor to the project's lenders to undertake to deliver the project within the specified timeframe, and to pay for the cost overruns, if any.

¹⁵ A liquidated damage refers to a monetary compensation for a loss, detriment or injury to a person's rights or property, awarded by a court judgment or by a contract stipulation regarding breach of contract.

¹⁶ An Operation and Maintenance ('O&M') contract refers to a contract between the developer and the operator. The developer delegates the operation, maintenance and often performance management of the project to an operator with expertise in the industry under the terms of the O&M contract (i.e. scope, term, operator responsibility, fees, and liquidated damages).

¹⁷ Performance incentives or performance based contracting refer to strategic performance metrics which directly relate contracting payment to these performance metrics. Performance metrics may measure availability, reliability, maintainability, supportability.

¹⁸ An O&M reserve account refers to a fund into which money is deposited to be used for the purpose of meeting the costs of operation and maintenance of the project.

(d) Sub-factor: revenue assessment, including off –take risk ¹⁹				
<ul style="list-style-type: none"> What is the robustness of the revenue contracts (e.g. off-take contracts ²⁰, concession agreements, public private partnership income stream, and other revenue contracts)? What is the quality of the termination clauses ²¹? (sub-factor component) 	Excellent robustness of the revenues	Good robustness of the revenues	Acceptable robustness of the revenues	The revenues of the project are not certain and there are indications that some of the revenues may not be obtained.
<ul style="list-style-type: none"> If there is a take-or-pay ²² or fixed-price off-take contract (sub-factor component) 	Excellent creditworthiness of off-taker; strong termination clauses; tenor of contract comfortably exceeds the maturity of the debt.	Good creditworthiness of off-taker; strong termination clauses; tenor of contract exceeds the maturity of the debt	Acceptable financial standing of off-taker; normal termination clauses; tenor of contract generally matches the maturity of the debt.	Weak off-taker; weak termination clauses; tenor of contract does not exceed the maturity of the debt.
<ul style="list-style-type: none"> If there is no take-or-pay or fixed-price off-take contract (sub-factor component) 	Project produces essential services or a commodity sold widely on a world market; output can readily be absorbed at projected prices even at lower than historic market growth rates.	Project produces essential services or a commodity sold widely on a regional market that will absorb it at projected prices at historical growth rates	Commodity is sold on a limited market that may absorb it only at lower than projected prices	Project output is demanded by only one or a few buyers or is not generally sold on an organised market.
(e) Sub-factor: supply risk				
<ul style="list-style-type: none"> Price, volume and transportation risk of feed-stocks; supplier’s track record and financial strength (sub-factor component) 	Long-term supply contract with supplier of excellent financial standing.	Long-term supply contract with supplier of good financial standing.	Long-term supply contract with supplier of good financial standing — a degree of price risk may remain.	Short-term supply contract or long-term supply contract with financially weak supplier — a degree of price risk definitely remains.
<ul style="list-style-type: none"> Reserve risks²³ (e.g. natural resource development) (sub-factor component) 	Independently audited, proven and developed reserves well in excess of requirements over lifetime of the project.	Independently audited, proven and developed reserves in excess of requirements over lifetime of the project	Proven reserves can supply the project adequately through the maturity of the debt.	Project relies to some extent on potential and undeveloped reserves.
Factor: strength of sponsor (including any public private partnership)				
(a) Sub-factor: financial strength of the sponsor	Strong sponsor with high financial	Good sponsor with good financial	Sponsor with adequate financial	Weak sponsor with clear financial

¹⁹ Off-take risk refers to the risk that the demand for the output or service does not exist at the price at which it is provided or the off-taker is unable or refuses to honour his commitment to purchase the output or service.

²⁰ An off-take contract refers to a contract between a producer of a resource/product/service and a buyer (‘off-taker’) of a resource to purchase/sell portions of the producer’s future production. An off-take contract is normally negotiated prior to the construction of a facility in order to secure a market for the future output of the facility. The purpose is to provide the producer with stable and sufficient revenue to pay its debt obligation, cover the operating costs and provide certain required return.

²¹ A termination clause refers to a provision in a contract which allows for its termination under specified circumstances.

²² A take-or-pay contract refers to a contract in which it is agreed that a client buys the output or service from the supplier or the client pays the supplier a penalty. Both the price and the penalty are fixed in the contract.

²³ Reserve risk refers to the risk that the accessible reserves are smaller than estimated.

	standing	standing	standing	weaknesses
(b) Sub-factor: track record of the sponsor and its country/sector experience	Sponsor with excellent track record and country/sector experience	Sponsor with satisfactory track record and country/sector experience	Sponsor with adequate track record and country/sector experience	Sponsor with no or questionable track record or country/sector experience
(c) Sub-factor: sponsor support, as evidenced by equity, ownership clause ²⁴ and incentive to inject additional cash if necessary	Strong. Project is highly strategic for the sponsor (core business — long term strategy)	Good. Project is strategic for the sponsor (core business — long term strategy)	Acceptable. Project is considered important for the sponsor (core business)	Limited. Project is not key to sponsor's long term strategy or core business
Factor: security package				
(a) Sub-factor: assignment of contracts and accounts	Fully comprehensive	Comprehensive	Acceptable	Weak
(b) Sub-factor: pledge of assets, taking into account quality, value and liquidity of assets	First perfected security interest ²⁵ in all project assets, contracts, permits and accounts necessary to run the project	Perfected security interest in all project assets, contracts, permits and accounts necessary to run the project	Acceptable security interest in all project assets, contracts, permits and accounts necessary to run the project	Little security or collateral for lenders; weak negative pledge clause ²⁶
(c) Sub-factor: lender's control over cash flow (e.g. cash sweeps ²⁷ , independent escrow accounts ²⁸)	Strong	Satisfactory	Fair	Weak
(d) Sub-factor: strength of the covenant package (mandatory prepayments ²⁹ , payment deferrals ³⁰ , payment cascade ³¹ , dividend restrictions ³² ...)	Covenant package is strong for this type of project Project may issue no additional debt	Covenant package is satisfactory for this type of project Project may issue extremely limited additional debt	Covenant package is fair for this type of project Project may issue limited additional debt	Covenant package is Insufficient for this type of project Project may issue unlimited additional debt
(e) Sub-factor: reserve funds (debt service, O&M, renewal and replacement, unforeseen events, etc)	Longer than average coverage period, all reserve funds fully funded in cash or letters of credit from highly rated bank	Average coverage period, all reserve funds fully funded	Average coverage period, all reserve funds fully funded	Shorter than average coverage period, reserve funds funded from operating cash flows.

²⁴ An ownership clause refers to a provision that states that a project cannot be owned by a different entity than the actual owner (sponsor).

²⁵ First perfected security interest refers to a security interest in an asset (mortgaged as a collateral) protected from claims by other parties. A lien is perfected by registering it with appropriate statutory authority so that it is made legally enforceable and any subsequent claim on that asset is given a junior status.

²⁶ A negative pledge clause refers to a provision that indicates that the institution will not pledge any of its assets if doing so gives the lenders less security.

²⁷ A cash sweep refers to the mandatory use of excess free cash flows to pay down outstanding debt rather than distribute it to shareholders.

²⁸ An independent escrow account refers to an account held in the sponsor's name by a bank under the support of an escrow account agreement between the lender and borrower providing for irrevocable instructions from the borrower to the effect that all operational revenue or proceeds from sale of assets of the project will be paid into this account, and where the bank is authorised to make payments from available funds only as agreed in the project financing documents.

²⁹ A mandatory prepayment refers to a provision that requires the borrower to prepay a portion of the debt with certain proceeds if and when received before the maturity date.

³⁰ A payment deferral refers to a provision that indicates that the borrower is allowed to start making payments at some specified time in the future.

³¹ A payment cascade refers to a provision whereby the project's cash flows are summarised using a cash flow waterfall, which shows the priority of each cash inflow and outflow.

³² A dividend restriction refers to a provision that defines the circumstances in which the lender is able to prevent equity distributions.

Annex II – assessment criteria for real estate exposures

	Category 1	Category 2	Category 3	Category 4
Factor: financial strength				
(a) Sub-factor: market conditions	The supply and demand for the project's type and location are currently in equilibrium. The number of competitive properties coming to market is equal or lower than forecasted demand	The supply and demand for the project's type and location are currently in equilibrium. The number of competitive properties coming to market is roughly equal to forecasted demand	Market conditions are roughly in equilibrium. Competitive properties are coming on the market and others are in the planning stages. The design and capabilities of existing comparable properties are not state of the art as compared to new projects	Market conditions are weak. It is uncertain when conditions will improve and return to equilibrium. Comparable properties in the market are losing tenants at lease expiration. New lease terms of comparable properties are less favourable compared to those existing
(b) Sub-factor: financial ratios, i.e. Indicators of the borrower's ability to repay	The property's financial ratios, measured by the property's debt service coverage ratio (DSCR 33) or interest coverage ratio (ICR 34), are considered strong and are expected to remain strong taking into account the past evolution in financial ratios. DSCR or ICR is not relevant and should not be calculated for properties that are in the construction phase.	The property's financial ratios, measured by the property's DSCR or ICR, are considered good and are expected to remain good taking into account the past evolution in financial ratios. The DSCR or ICR is not relevant and should not be calculated for properties that are in the construction phase.	The property's financial ratios measured by the property's DSCR or ICR are satisfactory and are expected to remain satisfactory taking into account the past evolution in financial ratios. The DSCR or ICR is not relevant and should not be calculated for properties that are in the construction phase.	The property's financial ratios, measured by the property's DSCR or ICR are weak and are expected to remain weak taking into account the past evolution in financial ratios. The DSCR or ICR is not relevant and should not be calculated for properties that are in the construction phase.
(c) Sub-factor: advance ratio, i.e. the loan-to-value (LTV 35) ratio as an indicators of the borrower's willingness to repay	The property's loan to value ratio (LTV) is considered low given its property type. Where a secondary market exists, the transaction is underwritten to market standards.	The property's LTV is considered satisfactory given its property type. Where a secondary market exists, the transaction is underwritten to market standards.	The property's LTV is considered relatively high given its property type	The property's LTV ratio is well above underwriting standards for new loans.
(d) Sub-factor: stress analysis on the basis of the income being generated during the tenor of the loan ³⁶	The property's resources, contingencies and liability structure allow it to meet its financial obligations during a period of severe financial stress (e.g. interest rates, economic growth)	The property can meet its financial obligations under a sustained period of financial stress (e.g. interest rates, economic growth). The property is likely to default only under severe economic conditions	During an economic downturn, the property would suffer a decline in revenue that significantly increase the risk of default	The property's financial condition is strained and is likely to default unless conditions improve in the near term

³³ The Debt Service Coverage ratio ('DSCR') refers to the ratio of the cashflow available for debt service which can be generated from the asset to the required repayment of the principal and the interest payments during the life of the loan, where the cashflow available for debt service is calculated by subtracting operating expenditure, capital expenditure, debt and equity funding, taxes and working capital adjustments from the revenues generated by the project.

³⁴ The Interest Coverage Ratio ('ICR') refers to the ratio of the cashflow available for debt service which can be generated from the asset to the required repayment of the interest payments during the life of the loan, where the cashflow available for debt service is calculated by subtracting operating expenditure, capital expenditure, debt and equity funding, taxes and working capital adjustments from the revenues generated by the project.

³⁵ The Loan-to-Value ratio ('LTV') refers to the ratio of the loan amount to the value of the pledged assets.

³⁶ The tenor of a loan refers to the amount of time left for the repayment of a loan.

(e) Sub-factor: cash-flow predictability				
<ul style="list-style-type: none"> For complete and stabilized property (sub-factor component) 	<p>The property's leases are long-term with creditworthy tenants and their maturity dates are scattered, or a public private partnership guarantees a considerable part of the tenancy contracts.</p> <p>The property has a track record of tenant retention upon lease expiration. Its vacancy rate is low. Expenses (maintenance, insurance, security, and property taxes) are predictable</p>	<p>The majority of the property has several tenant lease contracts that are long-term, and with tenants that have on average a high creditworthiness, and with scattered maturity dates. A public private partnership may guarantee part of the tenancy contracts. Where the property has only one lease contract or one tenant has a very significant share in the income generated by the property, this tenant is of excellent creditworthiness and the contract includes covenants that ensure lease payments until the end of the project life or beyond.</p> <p>The property experiences a normal level of tenant turnover upon lease expiration. Its vacancy rate is low. Expenses are predictable</p>	<p>Most of the property's leases are medium rather than long-term with tenants that range in creditworthiness. A public private partnership may guarantee only a minor part of the tenancy contracts. Where the property has only one lease contract or one tenant has a very significant share in the income generated by the property, this one tenant, the contract includes covenants that ensure lease payments until the end of the project life or beyond but the tenant has moderate creditworthiness.</p> <p>The property experiences a moderate level of tenant turnover upon lease expiration. Its vacancy rate is moderate. Expenses are relatively predictable but vary in relation to revenue</p>	<p>The proportion of short term leases is significant with tenants that range in creditworthiness, or the property has only one lease contract, or one tenant has a very significant share in the income generated by the property, where that tenant has a low creditworthiness and/or the contract does not include the necessary covenants that ensure lease payments until the end of the project life or beyond.</p> <p>The property experiences a very high level of tenant turnover upon lease expiration. Its vacancy rate is high. Significant expenses are incurred preparing space for new tenants</p>
<ul style="list-style-type: none"> For complete but not stabilized property (sub-factor component) 	<p>The cashflows obtained from the leasing activity, for instance obtained from a public private partnership, meet or exceed the expected cashflows used in the valuation of the property. The project should achieve stabilization in the near future</p>	<p>The cashflows obtained from the leasing activity, for instance obtained from a public private partnership, meet or exceed the expected cashflows used in the valuation of the property. The project should achieve stabilization in the near future</p>	<p>Most of the cashflows obtained from the leasing activity meet the expected cashflows used in the valuation of the property however, stabilization will not occur for some time</p>	<p>The cashflows obtained from the leasing activity do not meet the expected cashflows used in the valuation of the property. Despite achieving target occupancy rate, cash flow coverage is tight due to disappointing revenue</p>
<ul style="list-style-type: none"> For construction phase (sub-factor component) 	<p>The property is entirely preleased through the tenor of the loan³⁷ or pre-sold to a tenant or buyer of high creditworthiness, or the bank has a binding commitment for take-out financing from a tenant or buyer of high creditworthiness, for instance through a public private partnership.</p>	<p>The property is entirely pre-leased or pre-sold to a creditworthy tenant or buyer, or the bank has a binding commitment for permanent financing from a creditworthy lender, for instance through a public private partnership.</p>	<p>Leasing activity is within projections but the building may not be pre-leased and there may not exist a take-out financing. The bank may be the permanent lender</p>	<p>The property is deteriorating due to cost overruns, market deterioration, tenant cancellations or other factors. There may be a dispute with the party providing the permanent financing</p>
Factor: political and legal environment				
(a) Sub-factor: legal and regulatory risks	<p>Jurisdiction is very favourable to repossession and enforcement of contracts</p>	<p>Jurisdiction is generally favourable to repossession and enforcement of contracts</p>	<p>Jurisdiction is generally favourable to repossession and enforcement of contracts, but repossession might be long and/or difficult</p>	<p>Poor or unstable legal and regulatory environment. Jurisdiction may make repossession and enforcement of contracts lengthy or impossible</p>

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The tenor of a loan refers to the amount of time left for the repayment of a loan.

(b) Sub-factor: political risk, including transfer risk, considering property type and mitigants	Very low exposure; strong mitigation instruments, if needed	Low exposure; satisfactory mitigation instruments, if needed	Moderate exposure; fair mitigation instruments	High exposure; no or weak mitigation instruments
Factor: asset/transaction characteristics				
(a) Sub-factor: location	Property is located in highly desirable location that is convenient to services that tenants desire	Property is located in desirable location that is convenient to services that tenants desire	The property location lacks a competitive advantage	The property is located in an undesirable location
(c) Sub-factor: design and condition	Property is favoured due to its design, configuration, and maintenance, and is highly competitive with new properties	Property is appropriate in terms of its design, configuration and maintenance. The property's design and capabilities are competitive with new properties	Property is adequate in terms of its configuration, design and maintenance	The property's configuration, design and maintenance have contributed to the property's difficulties. Weaknesses exist in the property's configuration, design or maintenance.
(d) Sub-factor: property is under construction	Construction budget is conservative and technical hazards are limited. Contractors are highly qualified and have high credit standing	Construction budget is conservative and technical hazards are limited. Contractors are highly qualified and have good credit standing	Construction budget is adequate and contractors are ordinarily qualified and have average credit standing	Project is over budget or unrealistic given its technical hazards. Contractors may be under qualified and have low credit standing
(e) Sub-factor: financial structure:				
• Amortisation schedule (sub-factor component)	Amortising debt without bullet repayment	Amortising debt with no or insignificant bullet repayment	Amortising debt repayments with limited bullet payment	Bullet repayment or amortising debt repayments with high bullet repayment
• Market/cycle and refinancing risk (sub-factor component)	There is no or very limited exposure to market or cycle risk since the expected cashflows cover all future loan repayments during the tenor of the loan and there are no significant delays between the cashflows and the loan repayments. There is no or very low refinancing risk.	The exposure to market or cycle risk is limited since the expected cashflows cover the majority of future loan repayments during the tenor of the loan and there are no significant delays between the cashflows and the loan repayments. There is low refinancing risk.	There is moderate exposure to market or cycle risk since the expected cashflows cover only a part of future loan repayments during the tenor of the loan or there are some significant delays between the cashflows and the loan repayments. Average refinancing risk.	There is significant exposure to market or cycle risk since the expected cashflows cover only a small part of future loan repayments during the tenor of the loan or there are some significant delays between the cashflows and the loan repayments. High refinancing risk.
Factor: strength of sponsor/developer (including any public private partnership)				
(a) Sub-factor: financial capacity and willingness to support the property.	The sponsor/ developer made a substantial cash contribution to the construction or purchase of the property. The sponsor/developer has substantial resources and limited direct and contingent liabilities. The sponsor/developer's properties are diversified geographically and by property type	The sponsor/ developer made a material cash contribution to the construction or purchase of the property. The sponsor/developer's financial condition allows it to support the property in the event of a cash flow shortfall. The sponsor/developer's properties are located in several geographic regions	The sponsor/ developer's contribution may be immaterial or non-cash. The sponsor/developer is average to below average in financial resources	The sponsor/ developer lacks capacity or willingness to support the property
(b) Sub-factor: reputation and track record with similar properties.	Experienced management and high sponsors' quality. Strong reputation and lengthy and successful record with similar properties	Appropriate management and sponsors' quality. The sponsor or management has a successful record with similar properties	Moderate management and sponsors' quality. Management or sponsor track record does not raise serious concerns	Ineffective management and substandard sponsors' quality. Management and sponsor difficulties have contributed to difficulties in managing properties in the past

(c) Sub-factor: relationships with relevant real estate actors	Strong relationships with leading actors such as leasing agents	Proven relationships with leading actors such as leasing agents	Adequate relationships with leasing agents and other parties providing important real estate services	Poor relationships with leasing agents and/or other parties providing important real estate services
Factor: security package				
(a) Sub-factor: nature of lien	Perfect first lien ³⁸	Perfect first lien	Perfect first lien	Ability of lender to foreclose is constrained
(b) Sub-factor: assignment of rents	The lender has obtained an assignment for the majority of the rents. They maintain current tenant information that would facilitate providing notice to remit rents directly to the lender, such as a current rent roll and copies of the project's leases	The lender has obtained an assignment for a significant part of the rents. They maintain current tenant information that would facilitate providing notice to the tenants to remit rents directly to the lender, such as current rent roll and copies of the project's leases	The lender has obtained an assignment for a relatively small part of the rent. The lender has not maintained current tenant information that would facilitate providing notice to the tenants to remit rents directly to the lender, such as current rent roll and copies of the project's leases	The lender has not obtained an assignment of the leases
(c) Sub-factor: quality of the insurance coverage	Very good quality	Good quality	Appropriate quality	Substandard quality

³⁸ Lenders in some markets exclusively use loan structures that include junior liens. Junior liens may be indicative of this level of risk if the total LTV inclusive of all senior positions does not exceed a typical first loan LTV.

Annex III – assessment criteria for object finance exposures

	Category 1	Category 2	Category 3	Category 4
Factor: financial strength				
(a) Sub-factor: market conditions	Demand is strong and growing, strong entry barriers, low sensitivity to changes in technology and economic outlook	Demand is strong and stable. Some entry barriers, some sensitivity to changes in technology and economic outlook	Demand is adequate and stable, limited entry barriers, significant sensitivity to changes in technology and economic outlook	Demand is weak and declining, vulnerable to changes in technology and economic outlook, highly uncertain environment
(b) Sub-factor: financial ratios, i.e. DSCR39 or ICR40	Strong financial ratios considering the type of asset. Very robust economic assumptions	Strong / acceptable financial ratios considering the type of asset. Robust project economic assumptions	Standard financial ratios for the asset type	Aggressive financial ratios considering the type of asset
(c) Sub-factor: advance ratio, i.e. loan-to-value (LTV41) ratio	Strong LTV ratio considering the type of asset.	Strong/good LTV ratio considering the type of asset.	Standard LTV ratio for the asset type	Aggressive LTV ratio considering the type of asset
(d) Sub-factor: stress analysis on the basis of the income being generated during the tenor of the loan42	Stable long-term revenues, capable of withstanding severely stressed conditions through an economic cycle	Satisfactory short-term revenues. Loan can withstand some financial adversity. Default is only likely under severe economic conditions	Uncertain short-term revenues. Cash flows are vulnerable to stresses that are not uncommon through an economic cycle. The loan may default in a normal downturn	Revenues subject to strong uncertainties; even in normal economic conditions the asset may default, unless conditions improve
(e) Sub-factor: market liquidity	Market is structured on a worldwide basis; assets are highly liquid	Market is worldwide or regional; assets are relatively liquid	Market is regional with limited prospects in the short term, implying lower liquidity	Local market and/or poor visibility. Low or no liquidity, particularly on niche markets
Factor: political and legal environment				
(a) Sub-factor: legal and regulatory risks	Jurisdiction is favourable to repossession and enforcement of contracts	Jurisdiction is favourable to repossession and enforcement of contracts	Jurisdiction is generally favourable to repossession and enforcement of contracts, even if repossession might be long and/or difficult	Poor or unstable legal and regulatory environment. Jurisdiction may make repossession and enforcement of contracts lengthy or impossible
(b) Sub-factor: political risk, including transfer risk, considering object type and	Very low exposure; strong mitigation instruments, if needed	Low exposure; satisfactory mitigation instruments, if needed	Moderate exposure; fair mitigation instruments	High exposure; no or weak mitigation instruments

³⁹ The Debt Service Coverage ratio ('DSCR') refers to the ratio of the cashflow available for debt service which can be generated from the asset to the required repayment of the principal and the interest payments during the life of the loan, where the cashflow available for debt service shall be calculated by subtracting operating expenditure, capital expenditure, debt and equity funding, taxes and working capital adjustments from the revenues generated by the project.

⁴⁰ The Interest Coverage Ratio ('ICR') refers to the ratio of the cashflow available for debt service which can be generated from the asset to the required repayment of the interest payments during the life of the loan, where the cashflow available for debt service shall be calculated by subtracting operating expenditure, capital expenditure, debt and equity funding, taxes and working capital adjustments from the revenues generated by the project.

⁴¹ The Loan-to-Value ratio ('LTV') refers to the ratio of the loan amount to the value of the pledged assets.

⁴² The tenor of a loan refers to the amount of time left for the repayment of a loan.

mitigants				
Factor: transaction characteristics				
(a) Sub-factor: amortisation schedule	Amortising debt without bullet repayment	Amortising debt with no or insignificant bullet repayment	Amortising debt repayments with limited bullet payment	Bullet repayment or amortising debt repayments with high bullet repayment
(b) Sub-factor: market/cycle and refinancing risk	There is no or very limited exposure to market or cycle risk since the expected cashflows cover all future loan repayments during the tenor of the loan ⁴³ and there are no significant delays between the cashflows and the loan repayments. There is no or very low refinancing risk.	The exposure to market or cycle risk is limited since the expected cashflows cover the majority of future loan repayments during the tenor of the loan and there are no significant delays between the cashflows and the loan repayments. There is low refinancing risk.	There is moderate exposure to market or cycle risk since the expected cashflows cover only a part of future loan repayments during the tenor of the loan or there are some significant delays between the cashflows and the loan repayments. Average refinancing risk.	There is significant exposure to market or cycle risk since the expected cashflows cover only a small part of future loan repayments during the tenor of the loan or there are some significant delays between the cashflows and the loan repayments. High refinancing risk.
(c) Sub-factor: operating risk				
• Permits / licensing (sub-factor component)	All permits have been obtained; asset meets current and foreseeable safety regulations	All permits obtained or in the process of being obtained; asset meets current and foreseeable safety regulations	Most permits obtained or in process of being obtained, outstanding ones considered routine, asset meets current safety regulations	Problems in obtaining all required permits, part of the planned configuration and/or planned operations might need to be revised
• Scope and nature of O & M contracts (sub-factor component)	Strong long-term O&M contract ⁴⁴ , preferably with contractual performance incentives, and/or O&M reserve accounts (if needed)	Long-term O&M contract, and/or O&M reserve accounts ⁴⁵ (if needed)	Limited O&M contract or O&M reserve account (if needed)	No O&M contract: risk of high operational cost overruns beyond mitigants
• Operator's financial strength, track record in managing the asset type and capability to re-market asset when it comes off-lease (sub-factor component)	Excellent track record and strong re-marketing capability	Satisfactory track record and re-marketing capability	Weak or short track record and uncertain re-marketing capability	No or unknown track record and inability to re-market the asset
Factor: asset characteristics				
(a) Sub-factor: configuration, size, design and maintenance (i.e. age, size for a plane) compared to other assets on the same market	Strong advantage in design and maintenance. Configuration is standard such that the object meets a liquid market	Above average design and maintenance. Standard configuration, maybe with very limited exceptions — such that the object meets a liquid market	Average design and maintenance. Configuration is somewhat specific, and thus might cause a narrower market for the object	Below average design and maintenance. Asset is near the end of its economic life. Configuration is very specific; the market for the object is very narrow
(b) Sub-factor: resale value	Current resale value is well above debt value	Resale value is moderately above debt value	Resale value is slightly above debt value	Resale value is below debt value
(c) Sub-factor: sensitivity of the asset value and liquidity to economic cycles	Asset value and liquidity are relatively insensitive to economic cycles	Asset value and liquidity are sensitive to economic cycles	Asset value and liquidity are quite sensitive to economic cycles	Asset value and liquidity are highly sensitive to economic cycles

⁴³ The tenor of a loan refers to the amount of time left for the repayment of a loan.

⁴⁴ An Operation and Maintenance ('O&M') contract refers to a contract between the developer and the operator. The developer delegates the operation, maintenance and often performance management of the project to an operator with expertise in the industry under the terms of the O&M contract (i.e. scope, term, operator responsibility, fees, and liquidated damages).

⁴⁵ An O&M reserve account refers to a fund into which money is deposited to be used for the purpose of meeting the costs of operation and maintenance of the project.

Factor: strength of sponsor (including public private partnership)				
(a) Sub-factor: sponsors' track record and financial strength	Sponsors with excellent track record and high financial standing	Sponsors with good track record and good financial standing	Sponsors with adequate track record and good financial standing	Sponsors with no or questionable track record and/or financial weaknesses
Factor: security package				
(a) Sub-factor: asset control	Legal documentation provides the lender effective control (e.g. a first perfected security interest ⁴⁶ , or a leasing structure including such security) on the asset, or on the company owning it	Legal documentation provides the lender effective control (e.g. a perfected security interest, or a leasing structure including such security) on the asset, or on the company owning it	Legal documentation provides the lender effective control (e.g. a perfected security interest, or a leasing structure including such security) on the asset, or on the company owning it	The contract provides little security to the lender and leaves room to some risk of losing control on the asset
(b) Sub-factor: rights and means at the lender's disposal to monitor the location and condition of the asset	The lender is able to monitor the location and condition of the asset, at any time and place (regular reports, possibility to lead inspections)	The lender is able to monitor the location and condition of the asset, almost at any time and place	The lender is able to monitor the location and condition of the asset, almost at any time and place	The lender is able to monitor the location and condition of the asset are limited
(c) Sub-factor: insurance against damages	Strong insurance coverage including collateral damages with top quality insurance companies	Satisfactory insurance coverage (not including collateral damages) with good quality insurance companies	Fair insurance coverage (not including collateral damages) with acceptable quality insurance	Weak insurance coverage (not including collateral damages) or with weak quality insurance

⁴⁶

First perfected security interest refers to a security interest in an asset (mortgaged as a collateral) protected from claims by other parties. A lien is perfected by registering it with appropriate statutory authority so that it is made legally enforceable and any subsequent claim on that asset is given a junior status.

Annex IV – assessment criteria for commodities finance exposures

	Category 1	Category 2	Category 3	Category 4
Factor: financial strength				
(a) Sub-factor: degree of over-collateralisation of trade	Strong	Good	Satisfactory	Weak
Factor: political and legal environment				
(a) Sub-factor: country risk	No country risk	Limited exposure to country risk (in particular, offshore location of reserves in an emerging country)	Exposure to country risk (in particular, offshore location of reserves in an emerging country)	Strong exposure to country risk (in particular, inland reserves in an emerging country)
(b) Sub-factor: mitigation of country risks	Very strong mitigation: Strong offshore mechanisms Strategic commodity 1st class buyer	Strong mitigation: Offshore mechanisms Strategic commodity Strong buyer	Acceptable mitigation: Offshore mechanisms Less strategic commodity Acceptable buyer	Only partial mitigation: No offshore mechanisms Non-strategic commodity Weak buyer
Factor: asset characteristics				
(a) Sub-factor: liquidity and susceptibility to damage	Commodity is quoted and can be hedged through futures or OTC instruments. Commodity is not susceptible to damage	Commodity is quoted and can be hedged through OTC instruments. Commodity is not susceptible to damage	Commodity is not quoted but is liquid. There is uncertainty about the possibility of hedging. Commodity is not susceptible to damage	Commodity is not quoted. Liquidity is limited given the size and depth of the market. No appropriate hedging instruments. Commodity is susceptible to damage
Factor: strength of sponsor (including public private partnership)				
(a) Sub-factor: financial strength of trader	Very strong, relative to trading philosophy and risks	Strong	Adequate	Weak
(b) Sub-factor: track record, including ability to manage the logistic process	Extensive experience with the type of transaction in question. Strong record of operating success and cost efficiency	Sufficient experience with the type of transaction in question. Above average record of operating success and cost efficiency	Limited experience with the type of transaction in question. Average record of operating success and cost efficiency	Limited or uncertain track record in general. Volatile costs and profits
(c) Sub-factor: trading controls and hedging policies	Strong standards for counterparty selection, hedging, and monitoring	Adequate standards for counterparty selection, hedging, and monitoring	Past deals have experienced no or minor problems	Trader has experienced significant losses on past deals
(d) Sub-factor: quality of financial disclosure	Excellent	Good	Satisfactory	Financial disclosure contains some uncertainties or is insufficient
Factor: security package				
(a) Sub-factor: asset control	First perfected security interest 47 provides the lender legal	First perfected security interest provides the lender legal control of the	At some point in the process, there is a rupture in the control of the assets by	Contract leaves room for some risk of losing control over the assets.

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First perfected security interest refers to a security interest in an asset (mortgaged as a collateral) protected from claims by other parties. A lien is perfected by registering it with appropriate statutory authority so that it is made legally enforceable and any subsequent claim on that asset is given a junior status.

	control of the assets at any time if needed	assets at any time if needed	the lender. The rupture is mitigated by knowledge of the trade process or a third party undertaking as the case may be	Recovery could be jeopardised
(b) Sub-factor: insurance against damages	Strong insurance coverage including collateral damages with top quality insurance companies	Satisfactory insurance coverage (not including collateral damages) with good quality insurance companies	Fair insurance coverage (not including collateral damages) with acceptable quality insurance companies	Weak insurance coverage (not including collateral damages) or with weak quality insurance companies

4. Accompanying documents

4.1 Cost-Benefit Analysis / Impact Assessment

4.1.1 Introduction

Article 153(9) of the CRR requires the EBA to develop draft RTS to specify how institutions will take into account the following factors when assigning risk weights to specialised lending: financial strengths, political and legal environment, transaction and/or asset characteristics, strength of the sponsor and developer, including any public and private partnership income stream, and security package.

As per Article 10(1) of the EBA regulation (Regulation (EU) No 1093/2010 of the European Parliament and of the Council), any draft RTS developed by the EBA – when submitted to the Commission for adoption – shall be accompanied by an Impact Assessment (IA) annex which analyses ‘the potential related costs and benefits’. Such an annex shall provide the reader with an overview of the findings as regards the identification of the problem, the options identified to remove the problem and their potential impacts.

This annex presents the impact assessment of the provisions included in the final draft RTS.

4.1.2 Problem definition

The core problem which the RTS aim to address is the lack of a European harmonised framework in the interpretation of circumstances to measure the underlying risks for specialised lending exposures to which the risk weights (RWs) are assigned on the basis of a set of supervisory RWs, which are specified in Table 1 of Article 153(5) of the CRR.

The interpretation and the implementation of the factors may vary across Member States, and it can be expected that the lack of common standards in assessing the underlying risk of the special lending exposures and the assignation of the corresponding RWs could lead to problems, including:

- a) uneven playing field: the *same* specialised lending exposures that are subject to similar circumstances and factors located in two different jurisdictions can be treated differently if the conditions and the factors for the assessment of the underlying risk and the corresponding RWs are not consistent between jurisdictions;
- b) distortion in competition: a regulatory framework which provides less strict assessment criteria for the exposures of institutions gives these institutions an unfair competitive advantage with respect to institutions operating under a strict regulatory framework; and

- c) obstacles to effective cooperation in supervisory practices: the lack of common rules across jurisdictions may lead to different supervisory practices among supervisory authorities. This will be relevant, in particular but not solely, when handling cross-border cases.

At the larger scale, such problems in the regulatory framework may prevent the effective and efficient functioning of the EU banking sector as well as the internal market.

4.1.3 Objectives

The objective of these RTS is to promote (a minimum level of) harmonisation when institutions assess the risk associated with specialised lending exposures for which they assign RWs according to Table 1 in Article 153(5) of the CRR.

A central element to establishing such a harmonised framework is to specify a common set of indicators and conditions which can be used by the authorities across Member States when assessing the underlying risk of the specialised lending exposures of an institution. A common framework is also expected to facilitate cooperation among authorities in EU Member States when they handle cross-border cases. The framework ultimately aims to promote the effective and efficient functioning of the EU banking sector.

4.1.4 Use of slotting criteria across EU

In 2004, the Basel Committee on Banking Supervision introduced a framework for supervisors to determine the capital requirements for specialised lending exposures for which banks do not meet the requirements for the estimation of PD under the corporate IRB approach. These requirements were set out in the 2004 Revised Framework on International Convergence of Capital Measurement and Capital Standards, commonly referred to as Basel II⁴⁸. The Basel standards require banks to map their internal grades to five supervisory categories, each of which is associated with a specific RW. Furthermore, the Basel text provides for five sub-classes of specialised lending: project finance (PF), income-producing real estate (IPRE), high volatility commercial real estate (HVCRE), object finance (OF) and commodities finance (CF). The Basel text provides detailed supervisory slotting criteria which are specific to the sub-classes of specialised lending. These sub-classes have been transformed into four classes of specialised lending in this draft RTS: project finance, real estate (RE), object finance and commodities finance.

There are currently nine EU Member States which are member of the BCBS and which are therefore committed to implement the Basel framework, which includes the supervisory slotting criteria used in these draft RTS, with regard to internationally active banks: Belgium, France, Germany, Italy, Luxembourg, the Netherlands, Spain, Sweden and the UK. It is expected that these countries have implemented the Basel framework, but it does not indicate to what extent

⁴⁸ <http://www.bis.org/publ/bcbs107.htm> for the original Basel II text and <http://www.bis.org/publ/bcbs128.pdf?l=en> for the Comprehensive Version of the revised framework (2006).

the slotting approach based on the Basel framework is used in the EU Member States which are not members of the BCBS.

In order to obtain information on the use of slotting criteria by institutions in the EU member states, the data assembled under the EBA⁴⁹ COREP⁵⁰ templates have been used. On the basis of the reported data for 2014Q3, the EBA found evidence that slotting criteria are being used for assigning RWs to specialised lending exposures in nineteen EU Member States for a total of 45 institutions. Tables 1 and 2 summarise the exposure values that are reported by the reporting institutions for specialised lending⁵¹ under the slotting approach in the COREP database⁵² in 2014Q3⁵³, in absolute numbers (millions of euros) (Table 1) and in the share of the total amount of exposures under the slotting approach (Table 2). Slotting is used most often (in terms of the number of institutions) in the UK (7 institutions), Spain and Germany (6 institutions) and Austria and France (4 institutions). When expressed in terms of the magnitude of the exposure value under the slotting approach, 58.6% of SL exposures under slotting are reported by UK banks, followed by 19.34% by institutions in Spain, 9.5% in Austria, and 3.62% and 3.47% in France and Germany, respectively. As such, the majority of specialised lending exposures under the slotting approach are reported by institutions in the UK.

Table 1 Specialised lending exposure values under slotting criteria by Member State and by category (in EUR millions, 2014Q3 COREP data)

MS	No. of institutions	Category 1	Category 2	Category 3	Category 4	Category 5	Total SL exposures in slotting
Austria	4	4 378	11 549	2 392	1 491	2 737	22 546
Belgium	1	0	20	49	0	54	123
Bulgaria	1	111	166	174	3	248	702

⁴⁹ This Impact Assessment makes use of the reported COREP data under Data Point Model 2.1 for the Framework Release 03/2014 for the ITS on Supervisory Reporting (<http://www.eba.europa.eu/regulation-and-policy/supervisory-reporting/implementing-technical-standard-on-supervisory-reporting-data-point-model-/-/regulatory-activity/consultation-paper>).

⁵⁰ The institutions for which data are reported under the ITS on Supervisory Reporting differ between reporting periods, and are governed by the EBA Decision of 14 May 2014 (<https://www.eba.europa.eu/documents/10180/16082/EBA+DC+090+%28Decision+on+Reporting+by+Competent+Authorities+to+the+EBA%29.pdf/9beaf5be-2624-4e36-a75b-b77aa3164f3f>). In 2014Q3, 156 institutions reported data under the COREP/FINREP templates, representing around EUR 32 000 billion of total assets, which is 83.5% of total EU banking assets, where total EU banking assets refers to the total assets held by EU MFIs as reported in the ECB Statistical Data Warehouse for 2013Q4 for domestic banking groups and stand-alone banks, foreign (EU and non-EU) controlled subsidiaries and foreign (EU and non-EU) controlled branches.

⁵¹ Specialised lending exposures are reported under sheet C 08.01.a (Credit and counterparty credit risks and free deliveries: IRB approach to capital requirements) of the COREP template, more specifically sheets C 08.01.a(090) and C 08.01.a(010) which cover Specialised Lending with (090) or without (010) own estimates of LGD or conversion factors within the Corporate exposure class.

⁵² Note that a zero value has been assumed in the relevant templates where the reported value was a missing value.

⁵³ Note that the COREP database covers institutions that report at both a consolidated and a solo level. As a rule, reporting should be undertaken at the highest consolidation level of any given banking group and for non-EEA banking subsidiaries (<https://www.eba.europa.eu/documents/10180/16082/EBA+DC+090+%28Decision+on+Reporting+by+Competent+Authorities+to+the+EBA%29.pdf/9beaf5be-2624-4e36-a75b-b77aa3164f3f>).

Croatia	1	3	93	1	34	256	387
Czech Republic	1	826	317	78	130	103	1 455
Denmark	1	0	9	3	3	6	21
Estonia	1	5	43	22	28	26	124
France	4	7 336	314	709	95	161	8 615
Germany	6	2 767	3 869	1 154	129	346	8 266
Greece	1	94	855	473	65	667	2 155
Italy	2	202	612	673	147	331	1 963
Latvia	1	5	43	22	28	26	124
Lithuania	1	0	7	1	8	17	34
Luxembourg	1	490	472	79	36	72	1 149
Portugal	1	170	1 297	251	101	141	1 959
Slovakia	3	513	1 135	434	122	186	2 390
Spain	6	11 348	24 533	5 332	1 424	3 415	46 052
Sweden	2	17	337	60	71	56	542
United Kingdom	7	51 862	40 334	14 889	6 453	25 915	139 453
Total	45	80 128	86 005	26 796	10 367	34 764	238 060

Note: The following risk weights apply to categories 1–5 in Table 1, according to Article 153(5) of the CRR:

Cat. 1: 50% (maturity below 2.5 years) and 70% (maturity equal to or above 2.5 years); Cat. 2: 70% (maturity below 2.5 years) and 90% (maturity equal to or above 2.5 years); Cat. 3: 115%; Cat. 4: 250%; Cat. 5: 0%.

Table 2 Specialised lending exposure values under slotting criteria by category as a share of total specialised lending exposures under slotting criteria by Member State (in per cent, 2014Q3 COREP data)

Member state	No. of institutions	Category 1	Category 2	Category 3	Category 4	Category 5
Austria	4	19%	51%	11%	7%	12%
Belgium	1	0%	17%	40%	0%	44%
Bulgaria	1	16%	24%	25%	0%	35%
Croatia	1	1%	24%	0%	9%	66%
Czech Republic	1	57%	22%	5%	9%	7%
Denmark	1	1%	44%	13%	12%	29%
Estonia	1	4%	34%	17%	23%	21%
France	4	85%	4%	8%	1%	2%
Germany	6	33%	47%	14%	2%	4%
Greece	1	4%	40%	22%	3%	31%
Italy	2	10%	31%	34%	7%	17%
Latvia	1	4%	34%	17%	23%	21%
Lithuania	1	0%	21%	3%	25%	51%
Luxembourg	1	43%	41%	7%	3%	6%
Portugal	1	9%	66%	13%	5%	7%
Slovakia	3	21%	48%	18%	5%	8%
Spain	6	25%	53%	12%	3%	7%
Sweden	2	3%	62%	11%	13%	10%
United Kingdom	7	37%	29%	11%	5%	19%
Total	45	34%	36%	11%	4%	15%

Note: The following risk weights apply to categories 1–5 in Table 1, according to Article 153(5) of the CRR:

Cat. 1: 50% (maturity below 2.5 years) and 70% (maturity equal to or above 2.5 years); Cat. 2: 70% (maturity below 2.5 years) and 90% (maturity equal to or above 2.5 years); Cat. 3: 115%; Cat. 4: 250%; Cat. 5: 0%.

The slotting approach is not the only approach used to determine capital requirements for specialised lending exposures. Indeed, the CRR sets out in Article 153(5) of the CRR that for those specialised lending exposures for which the institution is not able to estimate the PD, or the PD estimations do not meet the PD requirements in the CRR, the institution should assign RWs according to the table specified in Article 153(5) of the CRR. As such, one can identify three approaches for assigning RWs to specialised lending exposures: the Foundation IRB approach (where the institution does not use own estimations of LGD and conversion factor), the Advanced IRB approach (where own estimations of LGD and conversion factor are used), and supervisory slotting criteria, which are the subject of these draft RTS. In terms of magnitude of the exposures within each of these approaches, the COREP data⁵⁴ (of 2014Q3) indicate that 28% of the SL exposures falls under the F-IRB approach, 48% under the A-IRB approach and 23% under the slotting approach (see Table 3).

Table 3: Specialised lending exposure values under slotting, F-IRB and A-IRB (in EUR millions and in per cent, 2014Q3 COREP data)

Approach	Exposure value	Share in total SL
Specialised lending under F-IRB	291 126.00	28%
Specialised lending under A-IRB	496 045.30	48%
Specialised lending under slotting	238 001.40	23%
Total amount of specialised lending exposure value	1 025 172.70	

It should also be noted that specialised lending exposures fall within the IRB corporate exposure class, where they represent a share of 11% of the total exposure values in this class (see Table 4).

Table 4: Exposure values in the corporate exposure class (in EUR millions and in per cent, 2014Q3 COREP data)

	Exposure value	Share in total corporate exposure class
Corporate – SME	1 305 825.60	19%

⁵⁴ Note that the number of institutions reporting data under the corporate exposure class is 101 (i.e. smaller than the 156 institutions which report COREP data in 2014Q3) because not all institutions reported data in this exposure class (i.e. some institutions reported no values, that is, blanks).

Corporate – SL	787 171.30	11%
Corporate – other	4 856 533.70	70%
Total corporate	6 949 530.60	

On the basis of the COREP data, it is, however, not possible to differentiate among the classes of specialised lending (i.e. project finance, real estate, object finance and commodities finance). As such, the information in these templates is the aggregate of all classes (in those Member States that differentiate between different classes of specialised lending).

4.1.5 Assessment of the technical options

Given the widespread use of the Basel supervisory slotting criteria, it has been considered the logical policy choice to draft these RTS on the basis of the Basel supervisory slotting criteria for Specialised Lending. This means that this final draft has taken over the Basel sub-classes of specialised lending to minimise the impact for institutions, with the exception of the distinction between IPRE and HVCRE which have been combined into one category of specialised lending, because no different treatment is allowed in the CRR for either type. As such, these final draft RTS allow for four classes of specialised lending: project finance, real estate, object finance and commodities finance.

It should, however, be noticed that the Basel text does not specify how the assignment of specialised lending exposures according to the different factors should be combined in order to make the final assignment to a category. One of the main policy choices that was analysed is, therefore, the harmonisation of the combination of the different factors. The table below summarises the main advantages and disadvantages of either approach.

Table 5: Potential advantages and disadvantages of harmonising the combination of factors

	Potential benefits / advantages	Potential costs / disadvantages
No harmonisation of the combination of the different factors	A certain level of supervisory discretion is retained	Discretion of supervisors may create uncertainty for the market players
	Harmonisation is achieved through the specification of common factors	A lack of consistency across jurisdictions may develop, leading to diverging capital requirements
	Allows an approach that is tailored to the specific exposure, which potentially enhances the risk sensitivity	Great variations may make the cross-border cooperation less efficient and effective
Harmonisation on the combination of	Higher level of convergence is achieved across jurisdictions	Supervisory discretion is more limited; some exposure-specific considerations could potentially not be taken fully into

the different factors	account
More clarity and transparency is provided to market participants as well as institutions	Harmonising the combination of the different factors puts a constraint to the models used by institutions. Given that specialised lending is still within the IRB approach, it could be argued that no constraints should be put on the combination of the factors
	There are costs for institutions associated with the introduction of new regulatory requirements by institutions

On the basis of the advantages and disadvantages discussed in the table above, it has been concluded that the harmonisation of the combination of the different factors would contribute to a greater consistency across capital requirements at a minimum cost. It is, therefore, the most cost-effective approach.

On that basis, the CP for these draft RTS consulted on two alternative options for how the different factors should be combined.

In the first option, a relatively straightforward rule was proposed, whereby the final assignment to a category can be, at most, only one step lower than the cardinal number of the highest category of all factors. However, in line with the specification in the CP for the draft RTS on assessment methodology for IRB approach, overrides are allowed in certain circumstances but should be documented, and the performance of these exposures should be analysed. The advantage of this rule is its simplicity, as well as the possibility to accommodate for special circumstances, and it would allow for a prudent assessment of the underlying credit risk for all specialised lending exposures subject to the approach in Article 153(5) of Regulation (EU) No 575/2013. One potential disadvantage of this option is that the final assignment of an exposure may be determined by only one or a few factors, meaning that not all factors determine the final assignment.

In the second option that was proposed in the CP, institutions would specify the weight that they assigned to each factor in order to determine the final assignment to a category. This option requires that the institution determine the final assignment to a category on the basis of the weighted average of the cardinal numbers of the categories to which all factors have been assigned; the CP consulted on the minimum weight (10% was suggested) that should be applied to each factor. The institution should then round this, when required, in order to determine the final assignment of the exposure to a category. It was mentioned that the practical implementation of this option is potentially less straightforward than that of the first option, but that it has the advantage of being clear and transparent. Furthermore, this option would rule out the possibility for institutions to discard one or several factors in assigning a category.

On the basis of the feedback received from the industry and the thorough analysis of national supervisors on this issue, it has been decided to specify the combination of factors on the basis of

the weighted average of the categories to which the specialised lending exposure is assigned for each factor, where institutions should specify the weight they assign to each factor, under the condition that no weight should be below 5% and no weight should be higher than 60%. The minimum risk weight is lowered to 5% to address the critique that sufficient risk sensitivity should be allowed by institutions and retained in the supervisory slotting approach. The maximum weight of 60% is introduced to avoid that institutions assign an excessive weight to one factor. Note that the maximum weight of 60% was implicitly included in the CP, where a minimum weight of 10% was proposed, which means a maximum weight of 60% (on the basis of 5 factors).

In Section 4.3, an analysis of the feedback and the conclusion is presented.

4.2 Feedback on the public consultation

The EBA publicly consulted on these draft RTS. The consultation period lasted for 3 months and ended on 11 August 2015. A total of 17 responses were received, of which 14 were published on the EBA website.

This paper presents a summary of the key points and other comments arising from the consultation, the analysis and discussion triggered by these comments and the actions taken to address them if deemed necessary.

In many cases, several industry bodies made similar comments, or the same body repeated its comments in its responses to different questions. In such cases, the comments and the EBA's analysis are included in the section of this paper where the EBA considers them most appropriate.

Changes to the draft RTS have been incorporated as a result of the responses received during the public consultation.

Summary of key issues and the EBA's response

a. Operational challenges of the slotting approach

The EBA enquired, through the consultation paper (CP) of these RTS, about the usefulness of the slotting approach in a broader context. This question has been included with the intention of feeding the responses into the ongoing discussions at international level (i.e. the Basel Committee on Banking Supervision, BCBS), where it is currently being discussed how greater consistency can be achieved in the bank's risk weighting practices, in particular the variability of the model outcomes in the Internal Ratings Based (IRB) approach. Furthermore, the Standardised Approach is currently under revision by the BCBS (a consultative document for a revised standardised approach was published in December 2014, and a second consultative document was published in December 2015) and the inclusion of a more risk-sensitive treatment for specialised lending exposures is one of the options.

The main conclusions of this enquiry are the following:

- a) The use of slotting criteria does not present particular operational challenges.
- b) Respondents do not deem it appropriate to extend supervisory slotting to other exposures. They caution against extending the slotting approach to other types of exposures under the IRB Approach, since slotting is considered less risk sensitive than IRB models.
- c) Several respondents advise the extension of specialised lending to the Standardised Approach, as considered in the BCBS consultation paper for the revision of the Standardised Approach, because it would ensure greater risk sensitivity than the current treatment in the corporate exposure class.

b. Combination of factors

The EBA enquired about the best approach to combine the assessment of specialised lending exposures against the factors to the final assignment to one of the categories, and proposed two options. An analysis of the advantages and disadvantages is presented in the Cost-Benefit Analysis / Impact Assessment in Section 4.1.

None of the respondents was in favour of the first option as (i) this option was considered unduly conservative, (ii) under this option the weakest factor may determine the final assignment of the risk weight, which is not deemed sufficiently risk sensitive, and (iii) the first option does not take into account whether any effective mitigation measures were in place to address the weakest factor. Several respondents argued that the second option would be preferred over the first because (i) the second option is more risk sensitive, (ii) the first option is unduly conservative, and (iii) the second option implies a more balanced assessment of the risks. The respondents also mentioned, however, that the imposed minimum weight of 10% could lead to the overestimation of the importance of a particular risk factor, and therefore advised that no minimum weight would be required for each factor when the second option would be chosen, or that the minimum weight would be lowered.

On the basis of the feedback received from the industry and the thorough analysis of national supervisors on this issue, it has been decided to specify the combination of factors on the basis of the weighted average of the categories the specialised lending exposure is assigned to for each factor, where institutions should specify the weight they assign to each factor, under the condition that no weight should be below 5% and no weight should be higher than 60%. The minimum risk weight is lowered to 5% to address the critique that sufficient risk sensitivity should be allowed by institutions and retained in the supervisory slotting approach. The maximum weight of 60% is introduced to avoid that institutions assign an excessive weight to one factor. Note that the maximum weight of 60% was implicitly included in the CP, where a minimum weight of 10% was proposed, which means a maximum weight of 60% (on the basis of 5 factors).

c. Discarding an irrelevant risk drivers or adding an additional risk drivers

The question of whether one of the risk drivers can be disregarded if it is found to be irrelevant was raised. In this regard, it should be mentioned that the EBA does not deem it possible that any of the factors is completely irrelevant with respect to a specialised lending exposure. However, for some sub-factors, it can indeed, in exceptional cases, be argued that they are irrelevant for a certain type of specialised lending exposure, where type of exposure should be understood within the meaning of Article 142(1)(2) of the CRR. Therefore, when a sub-factor or a part of it is found to be irrelevant for a particular type of exposure, the institution may disregard that sub-factor in the combination of sub-factors in order to determine the category for the corresponding factor and thereby also in the final assignment of this type of specialised lending exposures to a category. When, in an exceptional case, such a situation should occur for a single specialised lending exposure, the institution should apply an override but this should be motivated and documented as specified in the documentation requirements. These aspects have been clarified in recital 8 in the draft RTS.

Similarly, the question of whether institutions can also take into account additional risk drivers to those listed in the CP was raised. In this regard, the EBA notes that the assessment criteria specified by the factors and sub-factors are already very broad and take into account a wide variety of risks in types of specialised lending exposures, such that it should be only in exceptional cases that an additional risk driver is found which is not yet captured by one of the existing sub-factors or parts of a sub-factor. Where an institution finds an additional risk driver for a type of specialised lending exposure which is not yet sufficiently captured by one of the sub-factors in the draft RTS and where the institution can show that this additional risk driver has a significant impact on the final assignment of the specialised lending exposure to one of the categories, the institution may consider this additional risk driver jointly with the sub-factor which most closely corresponds to that risk driver. Furthermore, it should be noted that where such an additional risk driver is found to be significant only for a single specialised lending exposure, the institution should consider this as an override in line with the provision in Article 172(3) of the CRR, and this should be motivated in the documentation. These aspects have been clarified in recital 9 in the draft RTS.

Summary of the responses to the consultation and the EBA's analysis

	Summary of responses received	EBA analysis	Amendments to the proposals
Question 1: What are the operational challenges of using the slotting approach? Is it possible to obtain comparable capital requirements across institutions using the slotting approach? Should the slotting approach in your view be extended to other types of exposures; if yes, to which types of exposures would this be particularly relevant?			
1	<p>Most respondents comment that the use of slotting criteria does not present particular operational challenges. Several respondents note that it would not be appropriate to extend supervisory slotting to other exposures. They caution against extending the slotting approach to other types of exposures under the IRB Approach, since slotting is considered less risk sensitive than IRB models, making capital levels less reflective of the true risk level. In addition, other arguments are mentioned: (i) internal models contribute to the development of expertise in risk management, (ii) internal models limit the reliance on external ratings. However, the respondents advise the extension of specialised lending to the Standardised Approach, as considered in the first</p>	<p>The EBA notes that this question has been included with the intention to feed the responses into the ongoing discussions at international level (i.e. the BCBS), where it is currently being discussed how greater consistency can be achieved in the bank's risk weighting practices, in particular the variability of the model outcomes. Furthermore, the Standardised Approach is currently under revision by the BCBS (a first consultative document for a revised standardised approach was published in December 2014 and a second one in December 2015) and the inclusion of a more risk-sensitive treatment for specialised lending exposures is one of the options.</p>	<p>No change.</p>

	<p>and second consultation paper for the revision of the current Standardised Approach by the BCBS, where institutions are not required to measure the underlying risk levels of specialised lending exposures which are treated in the Standardised Approach (SA) for capital requirement purposes. One respondent points out that there would be advantages to extending the slotting approach to IRB corporate segments that are characterised by low default populations. Another respondent suggests extending slotting to transactions which cannot be assessed on quantitative elements, such as acquisition finance transactions made by leverage buyout deals.</p>		
2	<p>Several respondents point out that the limited number of risk weight categories under slotting gives rise to a significant mismatch between true economic risk and regulatory capital outcomes.</p>	<p>While the EBA agrees that the number of risk weight categories is limited (only five categories with five different risk weights are provided under Article 153(5) of the CRR), creating additional categories is beyond the EBA mandate in accordance with Article 153(9) of the CRR, as the RTS should specify how institutions should take into account the specified set of factors when assigning risk weights to specialised lending categories.</p>	<p>No change.</p>

3	<p>Several respondents note that the capital requirements are not comparable between the supervisory slotting approach and the IRB Approach, where PDs and LGDs are estimated by institutions, due to the fact that the risk weights and the EL values are not calibrated with the IRB PD and LGD values. According to the respondents, this leads to significantly higher capital requirements for banks using slotting compared with banks using the A-IRB or F-IRB Approach. The respondents suggest improving the consistency in risk-weighted exposure amounts by introducing some extra low-risk-weight categories.</p>	<p>One of the EBA's objectives is to contribute to greater comparability of capital requirements. In this context, the EBA aims to contribute to enhancing the robustness and the comparability of the internal risk estimates of European institutions, and several regulatory products have been or are being developed in this area, as summarised in the Discussion Paper on the Future of the IRB Approach published in March 2015⁵⁵). However, the IRB Approach is currently also under revision at the global level (BCBS) and it is therefore necessary to ensure that the EBA's efforts are aligned with these international developments. As such, major revisions of the supervisory slotting approach are currently not considered desirable and warranted.</p>	No change.
4	<p>One respondent points out that the current lack of a harmonised interpretation by competent authorities in terms of the conditions under which supervisory slotting should be applied creates larger distortions to competition than the distortions arising from a different implementation of the supervisory slotting criteria.</p>	<p>The EBA notes that the mandate for these RTS only allow specifying '... how institutions should take into account the factors ... when assigning risk weights to specialised lending exposures'. Hence, the conditions under which supervisory slotting should be applied cannot be specified in these RTS. Furthermore, the EBA notes that these conditions are specified in Article 153(5) of the CRR: 'For specialised lending exposures in respect of which an institution is not able to estimate PDs or the institutions' PD estimates do not meet the requirements set out in Section 6, the institution shall assign risk weights to these exposures according to Table 1'. In this regard, the</p>	No change.

⁵⁵ <https://www.eba.europa.eu/documents/10180/1003460/EBA-DP-2015-01+DP+on+the+future+of+IRB+approach.pdf>

		EBA is currently developing guidelines on the estimation of the PD and on the definition of default, which should contribute to a greater understanding and robustness of the PD estimates.	
5	One respondent notes that there are too many factors and sub-factors to be assessed for the classes of real estate and project finance, which adds to the operational costs of implementing the slotting approach and dilutes the assessment.	The EBA agrees that there is a multitude of factors and sub-factors which need to be assessed for the purpose of assigning risk weights to specialised lending exposures. It is, however, necessary to have so many factors in order to capture all potential major risk drivers within types of specialised lending exposures in each class. Furthermore, the specification of these factors and sub-factors is consistent with the specification of the supervisory slotting criteria in the Basel text. Given that no major deviations from the Basel text are desired or warranted at this stage, the specifications of the factors and sub-factors will mostly be maintained in the draft RTS. Note, however, that some duplication of sub-factors is removed and that some elements are further clarified (see below).	No change.
6	Several respondents note that the slotting approach is prone to enforce pro-cyclicality in capital requirements. One respondent advises that capital requirements be made counter-cyclical, by using a long-term value for the financed asset as a valuation criterion.	The EBA acknowledges that some capital requirement regulations, including the slotting approach, may be pro-cyclical. However, the EBA monitors the pro-cyclicality of capital requirements on a regular basis (for instance, in the EBA report on pro-cyclicality under the IRB Approach published in December 2013 ⁵⁶) and aims to contribute to regulatory products which reduce pro-cyclicality (as mentioned in the Discussion paper on the future of the IRB Approach ⁵⁷). The advice relating to the use of a long-term value as a valuation criterion is acknowledged, but the EBA notes that (i) the specification of such a long-term value concept is not within the scope of the mandate, and that (ii) the CRR provides for two valuation criteria for immovable property collateral, i.e. market value (MV) and mortgage lending value (MLV). Given that both concepts are allowed as	No change.

⁵⁶ <https://www.eba.europa.eu/documents/10180/15947/20131217+Report+on+the+pro-cyclicality+of+capital+requirements+under+the+IRB+Approach.pdf>

⁵⁷ <https://www.eba.europa.eu/documents/10180/1003460/EBA-DP-2015-01+DP+on+the+future+of+IRB+approach.pdf>

		valuation criteria in the CRR, it is not possible to reduce these options in the draft RTS.	
7	One respondent notes that for all classes of specialised lending it should be specified that specific extra collateral (i.e. cash collateral accounts covering construction phase or similar) should be taken into account as EL mitigating measure.	<p>The EBA notes that the eligibility of the asset to serve as collateral is assessed in the credit risk mitigation framework (Chapter 4 of Title II Part Three of CRR). In particular, it should be verified whether the asset meets the eligibility criteria of collateral to serve as credit risk mitigation in Article 197 of the CRR.</p> <p>Furthermore, the specification of elements that could mitigate the EL estimation is outside the scope of these RTS. The EL values to be used by institutions who assign risk weights to specialised lending exposures under the slotting approach are specified in Table 2 in Article 158(6) of the CRR.</p>	No change.
<p>Question 2: What would be the preferred approach for the combination of the factors into a final assignment to a category? What are the advantages and drawbacks of either approach? Are both options equally clear or should further guidance be provided? Are there other approaches that could be used to harmonise the combination of the different factors into a final assignment for the risk weight?</p>			
8	<p>Several respondents note that both options would lead to a lower risk differentiation and risk management capability, and therefore prefer that institutions are given more rather than less flexibility to interpret the slotting criteria.</p> <p>None of the respondents to this question was in favour of option 1, as (i) this option was deemed unduly conservative, (ii) under this option the weakest factor may determine the final assignment of the risk weight, which is not deemed sufficiently risk sensitive, and (iii) option 1</p>	<p>The EBA acknowledges that there are several disadvantages to option 1, which outweigh the benefits, and has agreed that the approach presented in option 2 is favourable, albeit with a 5% floor for the weight to be assigned to each factor (instead of the 10% which was the number suggested in the CP). This way, the advantages of harmonising the combination of the assignments of the factors are obtained while minimising the disadvantages of imposing a floor to the assigned weight. In particular, it has been decided to lower the floor in order to ensure that the assigned weight to each factor reflects its actual importance.</p> <p>The EBA notes that Article 173 of the CRR (in particular Article 173(1)(b) of the CRR) refers to a different issue:</p>	<p>Article 1(3) has been redrafted; option 2 (specified in the CP) is retained. Similarly, recital 5 is redrafted in order to retain option 2, i.e. institutions should specify the weight that they assign to each factor, where the weight should not be lower than 5% and not be higher than 60%. The maximum weight of 60% is introduced to avoid that institutions assign an excessive weight to one factor. Note that the maximum weight of 60% was implicitly included in the CP, where a</p>

	<p>does not take into account whether any effective mitigation measures were in place to address the weakest factor. One respondent notes that option 1 would not be consistent with Article 173 of the CRR which requires institutions to adjust assignments in light of all available material information.</p>	<p>'institutions shall review the assignment of an exposure if material information on the obligor or exposure becomes available'.</p>	<p>minimum weight of 10% was proposed, which means a maximum weight of 60% (on the basis of 5 factors). The final assignment to a category should be done on the basis of the weighted average of the cardinal numbers of the categories to which the exposure has been assigned to for each factor.</p>
9	<p>Several respondents note that option 2 would be preferred over option 1 because (i) option 2 is more risk sensitive, (ii) option 1 is unduly conservative, and (iii) option 2 implies a more balanced assessment of the risks.</p> <p>Several respondents note that option 2 is also not preferred because this option would not ensure that the final assessment reflects the underlying risk of the exposure. Since a minimum weight of 10% is imposed, this option could lead to the overestimation of the importance of a particular risk factor. The respondents therefore advise that no minimum weight should be required to each factor when option 2 would be chosen, or that the proposed minimum weight of 10% should be lowered. One respondent notes that option 2 does not rule out the option that too high a weight would be given to one factor, thereby disproportionately affecting the final assignment to a category.</p>	<p>Same analysis as in row 8.</p>	<p>See row 8.</p>

10	<p>One respondent suggests that if a factor or sub-factor is found to be irrelevant in a particular case, it should be treated as such and given a zero weighting.</p>	<p>On the specific question of whether some factors can be disregarded if they are found to be irrelevant, the EBA notes that it is not deemed possible for any of the factors to be completely irrelevant with respect to a specialised lending exposure. However, for some sub-factors, it can indeed be argued that they are irrelevant for a certain type of specialised lending exposure. One example of such a case is the factor 'Asset/Transaction characteristics', sub-factor 'property is under construction' in Annex 2 of the draft RTS (assessment criteria for real estate) which is not relevant for properties which are not under construction. Therefore, when a sub-factor is found to be irrelevant for a particular type of exposure, the institution may disregard that sub-factor in the combination of sub-factors in order to determine the category for the corresponding factor and thereby also in the final assignment of this type of specialised lending exposures to a category.</p>	<p>It is now clarified in the draft RTS that all factors and sub-factors should be considered against the assessment criteria in the annexes to the draft RTS, and that when a sub-factor is found to be irrelevant for a particular type of exposures, the institution may disregard that sub-factor in the combination of sub-factors in order to determine the category for the corresponding factor and thereby also in the final assignment of this type of specialised lending exposures to a category, but the institution should, however, document and include the motivation for why that sub-factor has not been considered relevant to this type of exposures.</p> <p>Where, as an exception, a risk driver is irrelevant only to a single specialised lending exposure, an institution may consider this by applying an override to the inputs or outputs of the assignment process for this specialised lending exposure</p>

			<p>in accordance with Article 172(3) of the CRR if the impact of this risk driver justifies such an override.</p> <p>These provisions can be found in the draft RTS in recitals 8 and 9.</p>
11	<p>One respondent explains that they currently use a scorecard-based approach, whereby scores, obtained through ratings and recovery expectations, are mapped to slotting categories. It is mentioned that the scorecard-based approach is a direct interpretation of option 2. The respondent notes that it does not see any methodological advantages to option 1, and that option 1 would force them away from using the current scorecard approach. The respondent further notes that it should be further regulated whether banks applying the scorecard approach should, under option 2, integrate certain factors or sub-factors in their scorecards where such factors or sub-factors are currently disregarded in those scorecards and are being considered only in the final calibration of the scorecards, although they are considered relevant factors in the CRR and/or relevant sub-factors in the final draft RTS.</p>	<p>The EBA notes that it is essential to the supervisory slotting approach that institutions consider each factor and sub-factor for the assignment of risk weights to the specialised lending exposure. This is clearly specified in the draft RTS and it is therefore included in the documentation requirements of the draft RTS that the assignment of the exposure according to the factors and sub-factors to one of the categories should be documented.</p> <p>It should also be mentioned that the EBA deems it impossible that any of the factors is completely irrelevant with respect to a specialised lending exposure. As also explained in the analysis to the above comment, a sub-factor may be found to be irrelevant for a particular type of exposures in an exceptional case, in which case the institution may disregard that sub-factor in the combination of sub-factors in order to determine the category for the corresponding factor and thereby also in the final assignment of this type of specialised lending exposures to a category.</p> <p>As regards the comment related to option 1 and 2, the reader is directed to the analysis in rows 8 and 9 of this feedback table.</p>	<p>No change.</p>

12	<p>One respondent disagrees with the inclusion of the references to Article 172(3) of the CRR on overrides, since it is argued that none of the final assignments should be overruled unless one of the two options specified in the CP were to be adopted in the RTS.</p>	<p>The EBA would like to clarify that the supervisory slotting approach in Article 153(5) of the CRR is a rating system, given the references to the slotting approach in the corporate exposure class within the IRB Approach, but also because of the references to ‘the methods set out in Article 153(5) of the CRR for assigning risk weights for specialised lending exposures’ in Article 170(2) of the CRR, which is a part of Sub-section 1 on Rating Systems, as part of Section 6 of Chapter 3 (Internal Ratings Based Approach) in Title II of Part Three of CRR. As a result, the rules governing the IRB Approach also apply to the supervisory slotting approach where relevant. In particular, the provision on overrides in Article 172(3) of the CRR also applies to the supervisory slotting approach. This is necessary and warranted for the purpose of assessing the specialised lending exposure against the factors and sub-factors specified in the draft RTS. As such, not all human judgement should be considered an override. More specifically, only where an institution makes a change to the final assignment of the specialised lending exposure to a category which is the result of applying the rules in the draft RTS, or where after applying the regular assignment process an override is applied to the assessment of a particular factor, sub-factor or a part of a sub-factor, should this be seen as an override. This follows from the wording of Article 172(3) of the CRR, which refers to ‘override the inputs or outputs of the assignment process’. The use of overrides was mentioned in Article 1(4) of the CP, but only with regard to a change to the final assignment of a specialised lending exposure to a category.</p>	<p>The wording of recital 7 of the draft RTS is changed to reflect the fact that overrides concern not only a change of the final assignment of a specialised lending exposure but also the change of any assessment of a factor, sub-factor or a part of a sub-factor that has been derived within the regular assignment process for a certain type of exposure.</p> <p>The wording of recital 7 of the draft RTS is changed to clarify that where an institution assigns risk weights using the methods set out in Article 153(5) of the CRR, such an institution is applying a rating system to which all relevant provisions related to internal models apply, to the extent that they are relevant, including the provisions regarding the possibility of human judgement overriding, in accordance with Article 172(3) of the CRR, the final assignment of a specialised lending exposure to one of the categories of Table 1 of Article 153(5) of the CRR as well as of the assignments of the factors or sub-factors.</p>
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13	<p>One respondent questions whether institutions can also take into account other risk drivers than those listed in the consultation paper.</p>	<p>First, it should be mentioned that the EBA's mandate is strict, i.e. 'develop draft RTS to specify how institutions shall take into account the factors (financial strength, political and legal environment, transaction and/or asset characteristics, strength of the sponsor and developer, including any public private partnership income stream, and security package) when assigning risk weights to specialised lending exposures'. For this reason, the draft RTS specify only these factors for the assignment of risk weights. Second, the assessment criteria and the set of sub-factors, which provide further clarity to the factors, is already very broad and takes into account a wide variety of risks in types of specialised lending exposures, such that it should be only in exceptional cases that an additional risk driver is found which is not yet captured by one of the existing sub-factors or parts of a sub-factor. Furthermore, the EBA promotes the comparability of risk-weighted assets across institutions and Member States, and is therefore cautious about diverging implementations in order to avoid the comparability of assignments to categories suffering.</p>	<p>An additional recital (recital 9) is included in the draft RTS in order to clarify that in the exceptional case that an institution finds an additional risk driver for a type of specialised lending exposure which is not yet sufficiently captured by one of the sub-factors in the draft RTS, the institution may consider this additional risk driver jointly with the sub-factor which most closely corresponds to that risk driver. Furthermore, it should be noted that where such an additional risk driver is found to be significant only for a single specialised lending exposure, the institution should consider this an override in line with the provision in Article 172(3) of the CRR. The latter is specified in the draft RTS in recital 9. In both cases, this should be included in the documentation of the specialised lending exposure.</p>
14	<p>One respondent notes that these options should be seen as an additional methodology for which the EBA does not have a mandate.</p>	<p>The EBA's mandate is to specify how institutions shall take into account the specified set of factors when assigning risk weights to specialised lending exposures. It is, therefore, within the mandate to specify how these factors should be combined in order to assign the risk weight to a specialised lending exposure.</p>	<p>No change.</p>

15	Some respondents point to the management effort and operational burden that would arise as a result of the redesign and calibration of the specialised lending approaches in response to both option 1 and 2, due to the higher level of human interaction.	The EBA understands that any change in the regulatory requirements has resource and IT implications for the institutions subject to these changes. However, the purpose of these draft RTS is to create consistency in the way institutions assign risk weights to specialised lending exposures, which contributes to the level playing field in the banking sector. Furthermore, the potential benefits and potential costs of these proposals have been carefully assessed in the impact assessment and it has been concluded that these proposals would contribute to greater consistency of capital requirements at a minimum cost.	No change.
16	One respondent proposes an alternative approach, i.e. to specify, for each class of specialised lending, a set of material factors or sub-factors, such that the final assignment to a category cannot be better (i.e. the category cannot be of a lower cardinal number) than the categories to which these material factors or sub-factors have been assigned.	This proposal has been duly considered but the EBA notes that a wide range of potential types of specialised lending exposures exist, i.e. even within each class of specialised lending exposures, there are several types of exposures. Hence, it would be operationally very difficult to anticipate each type of specialised lending exposure and therefore each class of specialised lending, which are the material factors or sub-factors.	No change.
17	One respondent questions whether the proposed options for the aggregation of the assignments of the factors also apply for the aggregation of the assignments of the sub-factors when determining the relevant category for the corresponding factor.	No, the draft RTS do not impose any rules on institutions harmonising how the results of the assessments of the sub-factors (and also the parts of the sub-factors) should be aggregated into the assessment of the factor.	This aspect is clarified in recital 5 of the draft RTS.
18	One respondent questions whether the assessment of a given factor should be a cardinal number or whether it could also be a decimal number, for instance as a result of the aggregation of the	This comment is related to the comments and analysis in rows 8 and 9 regarding the approach to combining the assignments of different factors into the final assignment, where the draft RTS specify that institutions should determine the weight that they assign to each factor (where the weight	Article 1(3) of the draft RTS is redrafted to clarify that institutions should round the weighted average to the nearest cardinal number, in the event that the weighted average

assessments of the sub-factors.

One respondent suggests an alternative option to combine the individual factors into a category, i.e. the creation of an internal model that reflects the bank's portfolio but is based on the mandatory factors and the ultimate output would be not the PD or LGD estimates but rather one of the regulatory categories of specialised lending. The respondent notes that as part of this model, the bank would propose a specific mapping between the model's outcome (for instance, a score) and the final assignment to a category. The advantage of such an approach would be the possibility of subsequently promoting the model from slotting to the regular IRB Approach with the use of own risk parameter estimates.

should not be lower than 5%) and determine the weighted average of the categories to which they have classified the factors.

The EBA acknowledges that the CP did not specify what should be done in the event that this weighted average is a decimal number. Since it was deemed warranted to clarify this aspect, it is now clarified in these draft RTS that, in the event that the weighted average is a decimal number, institutions should round this number to the nearest cardinal number in order to determine the category to which they shall assign the exposure.

The EBA acknowledges the potential usefulness of the suggested internal model based on the mandatory factors for the assignment of a regulatory category. For the purpose of this mandate regarding supervisory slotting, it is, however, not warranted to impose that institutions develop such a model, as it is required only that institutions take into account the factors and sub-factors as they are laid out in these draft RTS.

is a decimal number, in order to determine the category to which the specialised lending exposure should be assigned.

Question 3: Do you agree with the classification of specialised lending and the descriptions given?

19	One respondent points out that this classification is similar to the Basel text but not exactly the same, and that there should not be any changes between the legal text of the RTS and the Basel text.	Although both texts are very similar in content, the EBA agrees that there are some differences in wording. However, the Basel text is an international agreement, whereas the text in the consultation paper is to be used as the basis for a legal text. As such, some differences in wording cannot be avoided.	No change.
20	One respondent suggests that part of the wording of the specification of project finance should be changed to ‘...where the funding is used to finance the development or acquisition of large, complex ...’	The EBA agrees that this would clarify the legal text.	Article 2(a) of the draft RTS has been changed to ‘...where the purpose of the specialised lending exposure is to finance the development or acquisition of large, complex ...’
21	One respondent suggests that the wording of the specification of real estate should include the phrase ‘...lease or rental payments obtained from one or several third parties or the proceeds ...’	The EBA acknowledges that this would clarify the text, as is the case for object finance where this wording is also used.	The wording ‘obtained from one or several third parties’ is added to Article 2(b), as well as Article 2(a).
22	One respondent notes that the acquisition of land should not be included in the definition of the real estate class, as this is rather asset-based lending, and land plot financing is not coherent with the principle of specialised lending to add or increase the value of the assets.	The definition of a specialised lending exposure is included in Article 147(8) of the CRR, and it has a broader scope of application than the scope of the RTS, which covers only the supervisory slotting approach. Hence, the specification of a specialised lending exposure is not in the scope of the mandate of these RTS. According to this definition, if an entity was specifically created to finance or operate the land or is economically comparable, if the lender has a substantial degree of control over the land and the income, and if the primary source of repayment of the loan is the income generated by the land, such acquisition of land qualifies as specialised lending exposure. If	No change.

	<p>One respondent notes that it should be clarified that leases should in general not be classified as specialised lending and that it is confusing that the term ‘lease’ is used in the specifications of real estate and object finance in the consultation paper. The argument is that, in order to qualify as specialised lending, the exposure must meet the criteria in Article 147(8) of the CRR, in particular that the primary source of repayment of the obligation is the income generated by the assets being financed, rather than the independent capacity of a broader commercial enterprise. It is argued that in most types of leases, the income generated by the leased asset is not used to repay the obligation.</p>	<p>this draft RTS were applied, such specialised lending exposure would qualify as real estate, according to the specification in Article 2(b). It is important that such an exposure meeting the requirements in accordance with Article 147(8) of the CRR would most likely also have to be assigned to the real estate class without any reference to the acquisition of land in the specification of the real estate class, as in this case an assignment to the class to which the specialised lending exposure most closely corresponds to would be required in accordance with recital 3 of the draft RTS. Furthermore, this approach is in line with the BCBS approach, where the acquisition of land is included in the Basel text (under the category of High-Volatility Commercial Real Estate (HVCRE)), for which with the assessment criteria in Annex 6 are equal to those for Income-producing real estate (IPRE).</p> <p>A similar reasoning applies for leasing, where it should be assessed whether the primary source of repayment of the obligation is the income generated by the leased asset, in order to assess whether such exposure qualifies as a specialised lending exposure.</p>	
23	<p>One respondent suggests splitting the class of real estate into two groups: (i) income-producing real estate and (ii) acquisition, development and construction, as this would better allow institutions to consider the significant differences between these two types of lending. This would make this RTS consistent</p>	<p>The EBA notes that a split between acquisition, development and construction (ADC) and IPRE is proposed in the first as well as the BCBS consultative paper on a revised SA, where it is suggested that specialised lending be included in the SA. It should, however, be mentioned that the SA is still under revision and no final decision has yet been taken on this issue. Furthermore, specifying separate assessment criteria for IPRE versus ADC would be a major deviation from the currently applicable Basel text, and such major deviations from the Basel text are not preferred at this stage, given that revisions at the BCBS are considered for both the Internal Ratings Based</p>	No change.

	with the Basel consultative document on a revised Standardised Approach, where these two categories are also suggested.	Approach and the SA. Finally, the above suggested clarifications apply (i) in exceptional cases when an additional risk driver is found to have a significant effect on the final assignment of a type of specialised lending exposure to a category, and (ii) the suggested clarification applies in case an institution considers a certain sub-factor to be irrelevant. The reader is directed to rows 10 and 13 of this feedback table for further explanations.	
24	One respondent notes that, except for project finance, none of the specifications of the classes of specialised lending refers to the size of the exposure which is being financed and argues that the application of these slotting criteria on relatively small exposures causes an operational burden which is not justified.	Whereas the consultation paper specifies several classes of specialised lending exposures, according to their type, these classes do not explicitly specify any minimum size for assigning an exposure to a particular class, since the definition of a specialised lending exposure in accordance with Article 147(8) of the CRR does not provide for any differentiation in this regard. The EBA notes that the draft RTS contain the words 'large' and 'expensive' in the specification of project finance, but that this is only for this class of specialised lending and adds clarification to the meaning of this class.	No change.
25	One respondent notes that the specification of commodities finance in Article 2(2)(d) of the draft RTS should refer to the monitoring and controls that are provided in the commodities transactions by transaction monitoring teams. According to this respondent it is only when there are controls around such transactions that commodities finance should be considered specialised lending. It is also pointed out that the	According to the definition of a specialised lending exposure in Article 147(8) of the CRR, it is not a requirement to have monitoring and controls to qualify as a specialised lending exposure. Furthermore, recital 3 of the draft RTS specifies that 'institutions should assign ... to that class which most closely corresponds to the description of one of those classes'. It is, therefore, unnecessary to add this extra criterion because this would narrow down the specification of commodities finance. Furthermore, it is not deemed warranted to deviate from the supervisory slotting criteria specified by the BCBS on this aspect. The EBA would also like to clarify that it is not required to meet the requirements on legal certainty, enforceability, etc., for the purpose of classifying an exposure as a specialised lending exposure. As regards the specific suggestion on the wording of 'income generated by the assets', it should be noted that this wording is	No change.

<p>wording of ‘income generated by the assets’ should be amended and replaced by ‘receipts generated by assets’, in order to avoid confusion over the fact that the reference is to the receivable due from the sale of the commodity.</p>	<p>deemed sufficiently clear and it is consistent with the specification of specialised lending in the CRR (in Article 147(8)(c)). It is, therefore, preferable that the same wording be maintained to keep both regulations consistent.</p>
<p>It is also pointed out that, in the specification of commodities finance, it would be more accurate to replace the wording ‘receivables of exchange-traded commodities’ with ‘commodities of a type capable of being traded on an exchange’, since many commodities which are exchange-traded are in practice not deliverable to an exchange because the commodities do not meet the exchange’s criteria.</p>	<p>The EBA understands that some stakeholders may have a different understanding of what is meant by an ‘exchange-traded commodity’, depending on whether it is possible that the commodity is factually deliverable or not. However, when an exposure is classified as specialised lending according to Article 147(8) of the CRR, and the RTS on specialised lending would be applied according to Article 153(5) of the CRR, recital 3 of the draft RTS already clarifies that ‘institutions should assign any of the specialised lending exposures ... to that class which most closely corresponds to the description of one of those classes’.</p>

Question 4: Do you agree with these documentation requirements for each specialised lending exposure for which risk weights are assigned according to this Regulation?

<p>26</p>	<p>Most respondents either did agree with the proposed documentation requirements or did not provide any response to this question. One respondent suggests that the list of elements to be</p>	<p>The EBA acknowledges the rationale and the reasons for applying any overrides or a reference to the applicable internal guidance on these matters should be added to the list of required documentation as such information is deemed necessary to assess the results of the assignment process.</p>	<p>Article 3 of the draft RTS is changed to require that institutions document the assessment of the specialised lending exposure at each step of the process in Article 1. This way, all aspects of the assessments, including the application of</p>
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	documented is supplemented with the rationale behind the rating assignment process and the reasons for overriding.		overrides, if any, should be motivated. The application of overrides should be consistent with the provisions in Article 172(3) of the CRR, and this is clarified in recital 7.
27	One respondent notes that they currently use a scorecard approach where risk drivers are mapped to the factors. The respondent does not agree with the documentation requirement in accordance with Article 3(d) of the draft RTS as the proposed wording does not allow for approaches where specialised lending exposures are assigned to a category ('a slot') only at the end of the assessment process but not at the level of individual factors or sub-factors. The respondent argues that this is an additional burden for banks on the path towards IRB compliance.	The documentation requirements in accordance with Article 3 of the draft RTS are closely linked to the requirement for assigning specialised lending exposures in accordance with Article 1 of the draft RTS and are an essential part of the supervisory slotting approach. When the draft RTS enter into force, institutions will have to ensure that they meet the relevant requirements for assigning exposures to risk weights and the corresponding documentation requirements. While the EBA is aware that this may entail a cost due to the change this implies versus the current regulatory practice, such costs are unavoidable in an EU harmonisation.	No change.
Question 5: Do you have any suggestions or comments on the assessment criteria for project finance?			

28	<p>One respondent notes that some sub-factors should be more differentiated, i.e. for project finance under financial structure in the financial strength factor, there are two sub-factors which contain the same specification.</p> <p>One respondent notes that the description of ‘amortisation schedule and refinancing risk’, under financial structure, under financial strength, should be changed in order to make categories 1 and 2 mutually exclusive. It is argued that the assignment of a loan with a small bullet repayment to category 3 is too conservative.</p>	<p>Article 1(4) of the draft RTS specifies that where the assessment criteria provided for one or several of the sub-factors are the same across several categories for that sub-factor (‘overlapping criteria’), institutions shall assign the relevant factor to a category based on the assignment of the specialised lending exposure of the sub-factors with no overlapping criteria. Where the assignment based on the sub-factors with no overlapping criteria is to a lower cardinal number than the sub-factor with the overlapping criteria, they shall make appropriate and conservative adjustments to that assignment.</p> <p>Nevertheless, to further clarify the assessment criteria, some minor wording changes are applied to the sub-factor ‘Financial Structure’ which should also address the concern in the case where there is only an insignificant bullet repayment.</p>	<p>The assessment criteria in Annex 1 are changed under ‘amortisation schedule’ in categories 1 (amortising debt without bullet repayment) and 2 (amortising debt with no or insignificant bullet repayment).</p> <p>Note also that some other wording changes are introduced under the sub-factor ‘Financial Structure’. These are further explained in row 34 of this feedback table.</p>
29	<p>One respondent notes that the descriptions of ‘foreign exchange risk (after taking into account hedging)’ should also note that this assessment is made after taking into account the effect of hedging.</p>	<p>The EBA understands that this should be clarified and therefore agrees to introduce some amendments to the specification of the sub-factor ‘Foreign exchange risk (after taking into account hedging)’.</p>	<p>The wording ‘after taking into account hedging’ is removed from the row heading and introduced in the assessment criteria for categories 1–4. In particular, the wording ‘or because the foreign exchange risk is fully hedged’ is added to the wording of categories 1 and 2. The wording of category 3 is changed to ‘foreign exchange risk is considered low because the exchange rate is stable or because the foreign exchange risk is hedged to a large extent’ and the wording of</p>

			category 4 is changed to 'foreign exchange risk is considered high because the exchange rate is volatile and the foreign exchange risk is not hedged to a large extent'.
30	One respondent points out that the description of political and legal environment, force majeure risk, refers to categories 1 and 2 for the exposure to that risk, whereas categories 3 and 4 refer to the level of protection, which are different subjects. The respondent advises that this be clarified.	The EBA understands that this wording is confusing and therefore proposes to change the assessment criteria for the four categories and to refer to both the exposure to force majeure risk and the level of protection in the event that there is such a risk.	The wording of category 1 is changed to 'No or very low exposure to force majeure risk', the wording of category 2 is changed to 'Limited exposure to force majeure risk', the wording of category 3 is changed to 'Significant exposure to force majeure risk which is not sufficiently mitigated', and the wording of category 4 is changed to 'Significant exposure to force majeure risk which is not mitigated'.
31	One respondent notes that the description of operating risk under transaction characteristics is confusing: the exposure should be assigned to category 1 in the event that an O&M contract does not exist but is not necessary, but the exposure should be assigned to category 4 in the event that there is no O&M contract.	The EBA acknowledges that this wording may be confusing and proposes several clarifications to the assessment criteria for this sub-factor.	The first and last bullet points are integrated to 'Scope, nature and complexity of O&M activities and contract'. The wording of category 1 is changed to 'There is a strong O&M contract, preferably with contractual performance incentives, and/or O&M reserve accounts, although an O&M contract is not strictly necessary because the O&M activities are straightforward and transparent'. The wording of category 2 is changed to 'The O&M activities are

			<p>relatively straightforward and transparent, and there is a long-term O&M contract, and/or O&M reserve account'. The wording of category 3 is changed to 'The O&M activities are complex and an O&M contract is necessary. There is a limited long-term O&M contract and/or reserve account'. The wording of category 4 is changed to 'The O&M activities are complex and an O&M contract is strictly necessary. There is no O&M contract. There is therefore the risk of high operational cost overruns beyond mitigants'.</p>
<p>32</p>	<p>One respondent notes that the descriptions of the strength of the sponsor are confusing, as they capture both the sponsor's track record and his financial standing. The respondent questions how this factor should be assigned to a category in the event that the sponsor has a good financial situation but a limited track record.</p>	<p>The EBA acknowledges that the sponsor's track record and its country/sector experience is different from its financial strength, and therefore proposes to split this sub-factor in two sub-factors.</p>	<p>For the sub-factor 'Financial strength of the sponsor', category 1 is named 'strong sponsor with high financial standing', category 2 is named 'Good sponsor with good financial standing', category 3 is named 'sponsor with adequate financial standing', and category 4 is named 'weak sponsor with clear financial weaknesses'. The sub-factor 'track record of the sponsor and its country/sector experience' will be specified in category 1 as 'sponsor with excellent track record and country/sector experience', in category 2 as 'sponsor with satisfactory track record and</p>

			<p>country/sector experience’, in category 3 as ‘sponsor with adequate track record and country/sector experience’, and in category 4 as ‘sponsor with no or questionable track record or country/sector experience’.</p>
<p>Question 6: Do you have any suggestions or comments on the assessment criteria for real estate?</p>			
<p>33</p>	<p>One respondent advises that some of the sub-factors be removed since they are already accounted for in other sub-factors.</p> <p>An example is given for financial strength, which mixes market conditions with assets quality (the project’s design and capabilities ...) and cash-flow predictability (project is losing tenants at lease expiration ...)</p> <p>Another example is given for asset characteristics, where in the ‘Location’ sub-factor, elements of configuration, design and maintenance can be found, which repeats information in the sub-factor design and condition. The description in category 4 should be reworded to ‘the property is situated in an undesirable location’.</p>	<p>The EBA acknowledges that there is some overlap between some of the sub-factors, but notes that this is to some extent unavoidable, since the potential risk drivers of each class of specialised lending are multi-faceted.</p> <p>Nevertheless, it can be argued that the market conditions and asset quality of the exposure are two different risk drivers, and the corresponding provisions should indeed be reworded to reflect this difference.</p> <p>It is also agreed that the overlap between the sub-factors ‘Location’ and ‘Design and condition’ of the factor ‘Asset characteristics’ should be removed.</p>	<p>The wording of the assessment criteria in the draft RTS is changed for the sub-factor ‘Market conditions’ under the factor ‘Financial Strength’ in category 3 and 4. In particular, the wording of category 3 is changed to ‘Market conditions are roughly in equilibrium. Competitive properties are coming on the market and others are in the planning stages. The design and capabilities of existing comparable properties are not state of the art as compared to new projects’. The wording of category 4 is changed to ‘Market conditions are weak. It is uncertain when conditions will improve and return to equilibrium. Comparable properties in the market are losing tenants at lease expiration. New lease terms of comparable properties are less favourable</p>

			<p>compared to those existing’.</p> <p>The wording of the sub-factor ‘Location’ under the factor ‘Asset characteristics’ is changed in category 4 to ‘The property is located in an undesirable location’.</p> <p>For the sub-factor ‘Design and condition’, category 4 is changed and ‘The property’s configuration, design and maintenance have contributed to the property’s difficulties’ is added to the description.</p>
34	<p>One respondent notes that the slotting criteria focus excessively on idiosyncratic risk and insufficiently on market, cycle and refinancing risk, which are the strongest determinants of losses. The criteria are also said to be pro-cyclical, whereby some aspects are double-counted across the factors or sub-factors. One respondent advises that capital requirements be made counter-cyclical, by using a long-term value for the asset being financed as a valuation criterion. One respondent notes that refinance risk should be taken into account as a separate sub-factor under transaction</p>	<p>The advice to use a long-term value as a valuation criterion is acknowledged, but the EBA notes that (i) the specification of such a long-term value concept is not within the scope of the mandate, and that (ii) the CRR provides for two valuation criteria for immovable property collateral, i.e. market value (MV) and mortgage lending value (MLV). Given that both concepts are allowed as valuation criteria in the CRR, it is not possible to reduce these options in the draft RTS. Furthermore, it should be mentioned that market risk and cycle risk are taken into account, under the factor ‘Financial strength’ where the ‘stress analysis’ and ‘cash-flow predictability’ should be assessed as sub-factors. Nevertheless, it is agreed that market, cycle and refinancing risk could be further addressed and specified. Therefore, additional aspects related to the financial structure are included in the draft RTS.</p>	<p>The assessment criteria are amended to incorporate market, cycle and refinancing risks in the assessment criteria for real estate specialised lending. In particular, the factor ‘Asset characteristics’ is renamed to ‘Asset/Transaction characteristics’ and an additional sub-factor ‘Financial structure’ is created under that factor. Under this sub-factor, an assessment should be made about the risks stemming from the amortisation schedule, as well as market/cycle and refinancing risk. It should be noted that this sub-factor is similar to the sub-factor under the factor ‘Financial Strength’ of the class of project finance, although some wording changes</p>

	characteristics.		have been applied there, mainly to clarify the text and to ensure consistency. For the class of object finance, the same applies (the same wording is used under the factor 'Transaction characteristics').
35	One respondent notes that a better differentiation can be achieved by including separate assessments of LTV, DSCR and ICR instead of combining these ratios.	The EBA agrees that DSCR and ICR are combined in one sub-factor ('financial ratios') for the factor 'financial strength' in the draft RTS. Given that the draft RTS do not impose a rule on how the assessments against the sub-factor should be combined into the assessment against the factor, making such further differentiation would not have an impact on the final assessment. Given that these ratios contain very similar information, it makes sense to combine this information into one assessment. Furthermore, the LTV is already being considered under a separate sub-factor.	No change.
36	One respondent points out that the DSCR and the ICR financial ratios are relevant and applicable only to IPRE (income-producing real estate) exposures, and not to ADC (acquisition, development and construction). The respondent points out that credit institutions use specific ratios to evaluate the overall risk and to assign the risk weight to ADC exposures. The respondent suggests including specific criteria	Given that the IRB approach is currently also under revision at the global level (BCBS), it is necessary to ensure that the EBA's efforts are also aligned with these international developments. As such, major deviations between the RTS on assigning risk weights to specialised lending exposures and the supervisory slotting criteria as agreed by the BCBS are not warranted at this stage. Given that the same supervisory slotting criteria apply for IPRE and for ADC at BCBS level, it is preferable to take the same approach in the EU. Nevertheless, it should be noted that, according to the draft RTS, institutions are allowed, in exceptional cases, to consider additional risk drivers for a type of specialised lending exposure jointly with the sub-factor which most closely corresponds to that risk driver. Similarly, if the institution has considered a certain sub-factor for a type of	An additional recital (recital 9) is included in the draft RTS in order to clarify that in the exceptional event that an institution finds an additional risk driver for a type of specialised lending exposure which is not yet sufficiently captured by one of the sub-factors in the draft RTS, the institution may consider this additional risk driver jointly with the sub-factor which most closely corresponds to that risk driver.

	<p>for ADC, similar to cash-flow predictability where three types of exposures are identified. Alternatively, the respondent suggests allowing institutions on the basis of their expert judgement to replace these ratios by internal ratios which are more appropriate.</p>	<p>specialised lending which is found to be irrelevant, the institution may discard this sub-factor if the reasons for doing so are plausible and stated in the documentation. The reader is directed to rows 10 and 13 of this feedback table for further explanations on these provisions.</p>	<p>Recital 8 is included in the draft RTS to clarify that when a sub-factor is found to be irrelevant for a particular type of exposures, the institution may disregard that sub-factor in the combination of sub-factors in order to determine the category for the corresponding factor and thereby also in the final assignment of this type of specialised lending exposures to a category, but the institution should, however, document and include the motivation for why that sub-factor has not been considered relevant to this type of exposures.</p>
37	<p>One respondent points out that the factors should be designed to be mutually exclusive, and that this is not always the case. One respondent notes that for some sub-factors no differentiation can be made between categories 1, 2 and sometimes even category 3, which the respondent points out is sub-optimal for good risk discrimination. The respondent advises that the factors be specified in such a way that they are as mutually exclusive as possible. As such, it is argued that</p>	<p>The EBA acknowledges that it is preferable to specify the sub-factors in such a way that their assessment is mutually exclusive between categories, especially when there is only one sub-factor such that the rule specified in Article 1(4) of the draft RTS cannot be applied. Hence, some wording changes are applied to the sub-factor 'Legal and regulatory risks' for the factor 'Political and legal environment'. Furthermore, some aspects of political risk are not yet captured in the current specification. Hence, the sub-factor 'Political risk, including transfer risk, considering property type and mitigants' is added with the wording taken from the class project finance. In order to address as much as possible the overlap among categories for some of the sub-factors of the factor 'Security Package', several wording changes are applied to the draft RTS.</p>	<p>The wording of the sub-factor 'Legal and regulatory risks' is changed in category 1 to 'Jurisdiction is very favourable to repossession and enforcement of contracts', category 2 to 'Jurisdiction is generally favourable to repossession and enforcement of contracts', and category 3 to 'Jurisdiction is generally favourable to repossession and enforcement of contracts, but repossession might be long and/or difficult'. No changes are applied to category 4. The sub-factor 'Political risk, including transfer risk, considering property type and</p>

	<p>the rule specified in Article 1(5) of the draft RTS cannot be applied. This case arises for real estate exposures, factor political and legal environment, and factor security.</p> <p>One respondent notes that the factor security should be a binary factor, since the security is either adequate or non-adequate, and where the security is considered non-adequate, the final assignment should not be better than weak (i.e. category 4).</p>		<p>mitigants’ is added to the factor ‘Political and legal environment’. The same wording is used as for project finance. Similarly, this sub-factor is added for object finance (‘Political risk, including transfer risk, considering object type and mitigants’).</p> <p>The wording of the sub-factor ‘Quality of the insurance coverage’ under the factor ‘Security Package’ is changed in category 1 to ‘Very good quality’, category 2 to ‘Good quality’, category 3 to ‘Appropriate quality’, and 4 to ‘Substandard quality’.</p>
38	<p>Several respondents note that the assessment criteria are ill-defined for property under construction, where in particular the criteria should be specified to ensure that construction risk is assessed as lower (i.e. credit quality is higher) when the construction progresses. For the factor ‘asset characteristics’, sub-factor ‘property is under construction’, the credit standing of the contractor as well as its qualification should be taken into account.</p>	<p>The EBA acknowledges that the credit quality of a property improves when the construction progresses. However, it should be mentioned that this increase in creditworthiness will be reflected in the sub-factor ‘Advance ratio, i.e. the LTV ratio’ under the factor ‘Financial strength’ when the construction progresses.</p> <p>Regarding the comment that both the credit standing and the qualification of the contractor should be taken into account, some wording changes are applied to reflect this element.</p>	<p>The wording for the sub-factor ‘Property is under construction’ for the factor ‘Asset characteristics’ is changed under category 1 to ‘Construction budget is conservative and technical hazards are limited. Contractors are highly qualified and have high credit standing’, under category 2 to ‘Construction budget is conservative and technical hazards are limited. Contractors are highly qualified and have good credit standing’, under category 3 to ‘Construction budget is adequate and contractors are ordinarily qualified and have average credit standing’ and under category 4 to</p>

			<p>‘Project is over budget or unrealistic given its technical hazards. Contractors may be underqualified and have low credit standing’.</p>
39	<p>One respondent points out that it is unclear what is meant by ‘DSCR or ICR is not relevant for the construction phase’, i.e. whether this means that this sub-factor should be zero-weighted for properties under construction or whether this sub-factor should be assigned to category 1 or 2.</p>	<p>The EBA would like to clarify that this means that these ratios (DSCR and ICR) should not be calculated or assessed for properties that are under construction. In the event that the institution finds that an additional risk driver is useful for a specific type of specialised lending exposure (for instance properties under construction), then the abovementioned rule applies, as mentioned in the next column.</p>	<p>It is now clarified in the wording of the sub-factor ‘Financial ratios’ of the factor ‘Financial strength’ that these ratios should not be calculated for properties that are under construction.</p> <p>It should be mentioned here (see also row 13 of this feedback table), that an additional recital included in the draft RTS in order to clarify that in the exceptional case that an institution finds an additional risk driver for a type of specialised lending exposure which is not yet sufficiently captured by one of the sub-factors in the draft RTS, the institution may consider this additional risk driver jointly with the sub-factor which most closely corresponds to that risk driver.</p>
40	<p>Several respondents note that the description of financial strength, financial ratios as well as advance ratio, is not consistent, since the description in categories 1 and 2 refers to the state, whereas the description in</p>	<p>The EBA acknowledges that this wording may confuse institutions and has, therefore, made changes to the assessment criteria to ensure that these reflect both the current stage as well as the expected financial strength.</p>	<p>The wording of the sub-factor ‘Financial ratios, i.e. indicators of the borrower’s ability to repay’ has been changed in category 1 to ‘... are considered strong and are expected to remain strong taking into account the past evolution in financial ratios’,</p>

	<p>categories 3 and 4 refers to its deterioration.</p>		<p>in category 2 to ‘The property’s financial ratios, measured by the property’s DSCR or ICR, are considered good and are expected to remain good taking into account the past evolution in financial ratios’, in category 3 to ‘The property’s financial ratios, measured by the property’s DSCR or ICR, are satisfactory and are expected to remain satisfactory taking into account the past evolution in financial ratios’ and in category 4 to ‘The property’s financial ratios, measured by the property’s DSCR or ICR, are weak and are expected to remain weak taking into account the past evolution in financial ratios’.</p> <p>For the sub-factor ‘Advance ratio, LTV’, the wording of category 3 is changed to ‘The property’s LTV is considered relatively high’. The wording of category 4 is changed to ‘The property’s LTV ratio is well above underwriting standards for new loans’.</p>
<p>41</p>	<p>One respondent points out that the description of financial strength, cash flow predictability, should specify how the exposure should be assigned to a category in the event that the structure of</p>	<p>The EBA acknowledges that these elements should be clarified in the assessment criteria, and, therefore, changes have been applied to the draft RTS to incorporate the risk assessment in case the property has only one tenant or one tenant has a very significant share in the income generated by the property.</p> <p>In order to clarify that the assessment should be based on the average</p>	<p>For category 2, the wording of the bullet point ‘For complete and stabilised property’ is changed to ‘The majority of the property has several tenant lease contracts that are long-term, and with tenants that</p>

<p>tenants is very dispersed. It is argued that an assessment of the creditworthiness of each tenant is extremely difficult if the property has many individual (sometimes small) tenants (for instance, many small places to rent in a shopping centre).</p> <p>Another respondent suggests distinguishing appropriately between loans against single tenant and multi-tenanted properties, given that the current assessment criteria do not adequately recognise this element.</p>	<p>creditworthiness of tenants, this aspect is added to the description in category 1. The same concern is addressed by applying some wording changes to the sub-factor 'Assignment of rents' under the factor 'Security Package'.</p>	<p>have on average a high creditworthiness, and with scattered maturity dates. A public-private partnership may guarantee part of the tenancy contracts. Where the property has only one lease contract or one tenant has a very significant share in the income generated by the property, this tenant is of excellent creditworthiness and the contract includes covenants that ensure lease payments until the end of the project life or beyond'. The wording of category 4 is changed to 'The proportion of short term leases is significant with tenants that range in creditworthiness, or the property has only one lease contract, or one tenant has a very significant share in the income generated by the property, where that tenant has a low creditworthiness and/or the contract does not include the necessary covenants that ensure lease payments until the end of the project life or beyond.'</p>
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42	<p>One respondent points out that for the sub-factor cash-flow predictability under the factor financial strength in the case of properties under construction the description should be broadened to take into account physical persons. In the consultation paper, reference is made to investment grade, which cannot be assigned to physical persons.</p>	<p>The EBA acknowledges that it is not intended to exempt physical persons from these assessment criteria, and therefore suggests changing the wording of category 1 to ensure that the assessment can comprise also physical persons.</p>	<p>For category 1, the wording of the bullet point ‘For construction phase’ of the sub-factor ‘Cash-flow predictability’ is changed to ‘pre-sold to a tenant or buyer of high creditworthiness’.</p>
43	<p>One respondent notes that for the factor ‘strength of the sponsor/developer’, sub-factor ‘financial capacity and willingness to support the property’, it is not clear how to assign the exposure for that sub-factor, since the description captures both the financial capacity as well as the willingness to support the property.</p>	<p>It should be clarified that the assessment criteria for this sub-factor refer both to the capacity and the willingness of the sponsor/developer to support the property. Both criteria are closely connected and they should be assessed in a cumulative way. If it is assessed that the sponsor has the willingness to support the property, it should be assessed whether the sponsor also has the capacity to support the property. If the sponsor/developer has made a high contribution to the property, this can be seen as an indication of his willingness and determination to support the property.</p>	<p>No change.</p>
44	<p>One respondent notes that for the factor ‘strength of the sponsor/developer’, sub-factor ‘relationships with relevant real estate actors’, it is very difficult to assess which description best matches the exposure, mostly due to lack of information but also because real estate actors are not needed in many real</p>	<p>It should be clarified that this information is necessary to assess this sub-factor. If insufficient information is available to assess this sub-factor, the institution should apply the provision in Article 171(2) of the CRR, i.e. ‘The less information an institution has, the more conservative shall be its assignments of exposures to obligor and facility grades or pools’.</p> <p>Furthermore, it should be mentioned that if the institution has considered a certain sub-factor for a type of specialised lending which is found to be irrelevant, the institution may discard this sub-factor if the reasons for doing so are plausible and documented (see also row</p>	<p>No change.</p>

	estate projects.	10 of this feedback table for further explanations).	
45	One respondent suggests that the assessment criteria should be broader and harmonised across the categories of specialised lending.	It should be mentioned that the distinction between the four classes of specialised lending and the four sets of assessment criteria is necessary to ensure that the criteria are sufficiently risk sensitive. Furthermore, the objective of harmonisation of the RTS cannot be achieved if these criteria are not sufficiently specific. Finally, these four sets of supervisory slotting criteria are also specified in the BCBS text; hence, these are taken as the basis for the draft RTS.	No change.
46	One respondent notes that the reference to capital expenditure in the assessment criteria for the sub-factor 'Stress analysis' of the factor 'Financial strength' is not an appropriate benchmark because this may not be relevant or material to all real estate specialised lending exposures.	The EBA agrees that it is not intended to limit the scope of the stress test in this category, and agrees to amend the text.	The wording of category 3 of the sub-factor 'Stress analysis' is changed to 'During an economic downturn, the property would suffer a decline in revenue that significantly increase the risk of default'.
47	One respondent points out that the factor 'Political and legal environment' for a real estate project in France would always be assigned to the first category. The respondent also points out that these assessment criteria are based only on legal considerations and therefore suggests that an assessment of risks related to economic environment should be covered	The EBA notes that these assessment criteria are constructed to assess exposures of real estate projects with geographical locations across the world. As such, it may indeed be the case that projects located in one EU Member State are always assigned to one category. However, this is only one factor and the assessment of the other factors and sub-factors also drivers the final assignment to one of the five categories. The EBA acknowledges that the wording of the factor 'Political and legal environment' refers to legal and regulatory aspects, but this is intended because of the alignment with the Basel text. However, the EBA acknowledges that some aspects of political risk are not yet captured in the current specification. Hence, the sub-factor 'Political	Row 37 of this feedback table explains which wording changes are applied to the factor 'Political and legal environment'.

	by the factor 'Financial Strength'.	risk, including transfer risk, considering property type and mitigants' is added with the wording taken from the class project finance. This is also explained in row 37 of this feedback table.	
48	One respondent notes that the assessment criteria should appropriately distinguish between loans against single tenant and multi-tenanted properties, in particular those of the sub-factor 'Assignment of rents (for projects leased to long-term tenants)' of the factor 'Security package' and do not adequately recognise these differences.	The EBA acknowledges that this aspect should be improved in the assessment criteria of the sub-factor 'Assignment of rents (for projects leased to long-term tenants). The wordings of this sub-factor should therefore change to reflect that there may be single- as well as multi-tenanted properties.	The wording of this sub-factor is changed to 'Assignment of rents' in order to ensure that this sub-factor is assessed even if there are no long-term tenants and therefore no assignments of rents. The wording of category 1 is changed to 'The lender has obtained an assignment for the majority of the rents. They maintain ...', the wording of category 2 is changed to 'The lender has obtained an assignment for a significant part of the rents. They maintain ...', the wording of category 3 is changed to 'The lender has obtained an assignment for a relatively small part of the rent. They have not maintained ...' and the wording of category 4 is changed to 'The lender has not obtained an assignment of the leases'.
Question 7: Do you have any suggestions or comments on the assessment criteria for object finance?			
49	One respondent points out that the criterion 'operator's financial strength, track record in managing the asset type' is being considered under 'operating risk' but also under 'strength of the sponsor/developer'. The respondent	The EBA acknowledges that this is confusing, and agrees to delete the sub-factor 'Operator's financial strength, track record in managing the asset type and capability to re-market the asset when it comes off-lease' from the factor 'Strength of the sponsor', since this sub-factor is an assessment of the operator and is already captured under the sub-factor 'Operating risk' for	The sub-factor 'Operator's financial strength, track record in managing the asset type and capability to re-market the asset when it comes off-lease' is deleted from the factor 'Strength of the sponsor'.

	suggests avoiding this double-counting by deleting this risk driver in the 'strength of the sponsor'.	the factor 'Transaction characteristics'.	
Question 8: Do you have any suggestions or comments on the assessment criteria for commodities finance?			
50	One respondent notes that the wording under the factor 'security package' should be less strict, because most of these exposures are eligible only for the category satisfactory (i.e. category 3), since it is a requirement that first perfected security interest provides legal control of the assets at all times for the sub-factor asset control to be assigned to category 1 or 2.	<p>The EBA agrees that these criteria are relatively strict, but argues that this is necessary, since the asset control is an important indicator of the credit quality of the specialised lending exposure. Furthermore, asset control is one sub-factor of the factor 'security package'; therefore, the sub-factor 'insurance against damages' also needs to be taken into account when assigning the factor security package to one of the categories, and the draft RTS do not prescribe any methodology to combine the assessments of the sub-factor to the assessment of the factor. Nevertheless, it should be clear that insurance cannot be regarded as a direct mitigant of the first sub-factor ('Asset control'); these are separate sub-factors which deal with different risks.</p> <p>Finally, it should be mentioned that major revisions of the supervisory slotting approach are considered not desirable and warranted at this stage due to the ongoing revisions of the IRB Approach at the global level (BCBS).</p>	No change.
Question 9: Do you have any suggestions or comments on the Impact Assessment?			
51	One respondent notes that the impact assessment overestimates the perceived benefits of harmonising the combination of factors into a final	The EBA is fully aware and acknowledges that any change in regulation requires redevelopment and estimation costs. However, in this case, the chosen option (option 2 specified in the CP) is deemed to be relatively simple to implement, since	No change.

category assignment pointing to the necessary redevelopment and implementation costs, which will disproportionately affect those Member States in which slotting criteria are most used (i.e. UK and ES).

One respondent notes that the impact assessment overemphasises the benefits of harmonisation within the slotting approach, and underemphasises the benefits of harmonisation across specialised lending under slotting versus under the regular IRB Approach with the use of own risk parameter estimates. The respondent disagrees with the conclusion that the two options of combining factors into a final assessment will contribute to greater consistency in capital requirements, as it is argued that there is insufficient information to reach such a conclusion.

institutions are required to assign a specialised lending exposure to factors and sub-factors and to subsequently determine the weighted average of these assignments to factors, in order to determine the category.

The EBA also acknowledges that there are regulatory differences across the treatment of specialised lending exposures, i.e. whether that is under the supervisory slotting approach, the Foundation IRB or Advanced IRB approach. However, the scope of the EBA's mandate is limited to the harmonisation of the supervisory slotting approach.

Regarding the last point, i.e. that there is insufficient information to conclude that the specification of the combination of the assignments to factors would contribute to greater harmonisation, the EBA points out that this mandate has been discussed extensively with the national competent authorities and it has been agreed that such specification would contribute positively to the harmonisation in this area.

52	<p>One respondent notes that the impact assessment underestimates the need for the mitigation of the systemic risk associated with specialised lending exposures, particularly those related to IPRE, as the currently proposed assessment criteria for these exposures contribute to pro-cyclicality.</p>	<p>The EBA acknowledges that systemic risk may arise from specialised lending exposures, in the same way that these risks may arise from any other exposure class. The CRR and CRD IV, however, contain several provisions to address these systemic or macroprudential risks, and it is outside the scope of this mandate to address these risks here. Furthermore, the harmonisation of the LTV ratio is not within the scope of this mandate.</p>	No change.
Other comments received not related to the above questions			
53	<p>One respondent notes that it is unclear whether all three elements in the definition of specialised lending exposures in Article 147(8) of the CRR should be strictly met. In particular, the respondent questions whether the criterion ‘entity which was created specifically to finance or operate physical assets’ can also be met by a structure substitute for an SPV (‘economically comparable exposure’).</p>	<p>The EBA notes that the specification of a specialised lending exposure is contained in Article 147(8) of the CRR, and it has a broader scope of application than the scope of the RTS, which covers only the supervisory slotting approach. Hence, the specification of a specialised lending exposure is not in the scope of the mandate of these RTS. The EBA notes that the EBA Q&A tool⁵⁸ would be more appropriate in order to obtain clarity on whether all three elements of the specification of specialised lending should be met simultaneously, as well as on the correct interpretation of ‘an economically comparable exposure’.</p>	No change.

⁵⁸ <http://www.eba.europa.eu/single-rule-book-qa>

54	One respondent notes that in the case of real estate and object finance, the company may have both income generated by the assets being financed and income deriving from other activities, such that the institution has applied specific criteria to isolate the specialised lending exposure from the other activities of the company.	The EBA notes that point (c) in Article 147(8) of the CRR merely requires that ‘the primary source of repayment of the obligation is the income generated by the assets being financed’. Furthermore, the EBA notes, similarly to the question above, that the specification of a specialised lending exposure is contained in Article 147(8) of the CRR, and is therefore not within the scope of the mandate of these draft RTS. If additional clarification is sought with respect to this specification, the EBA Q&A tool would be more appropriate ⁵⁹ .	No change.
55	Several respondents point out that the specification of the remaining maturity of specialised lending exposures as set out in recital 4 of the draft RTS is not within the EBA’s mandate, and is not considered appropriate given that refinancing risks are already addressed as part of the slotting criteria themselves. Several respondents advise that the applicable remaining maturity should be the contractual maturity, as this would be consistent with the A-IRB and the Standardised Approach for credit risk.	The EBA acknowledges that it is important to maintain consistency with the Standardised Approach for credit risk and the A-IRB, and given further the defined scope of the mandate, the recital should be removed from the draft RTS.	Recital 4 is removed from the draft RTS, given the limitations of the scope of this mandate.
56	One respondent advises that the RTS on specialised lending should be applied prospectively, i.e. only to new specialised lending exposures granted post adoption of the RTS.	The EBA notes that it is not legally possible to allow one rating system for one or several exposures and another rating system for the others, if these exposures are of the same type of exposure, where type of exposure should be understood as with the meaning of Article 142(1)(2) of the CRR. In particular, Article 143(3) of the CRR specifies that ‘The range of application	Article 4 of the draft RTS is changed to reflect that the RTS enter into force one year after their publication in the <i>Official Journal of the European Union</i> , and recital 10 has been added.

⁵⁹ <http://www.eba.europa.eu/single-rule-book-qa>

		<p>of a rating system shall comprise all exposures of the relevant type of exposures for which that rating system was developed'. As such, this proposed prospective application of the RTS would not be legally allowed.</p> <p>However, the EBA acknowledges that the application of the rules regarding the combination of the factors may need the change of IT systems and other operational changes, and therefore proposes that the RTS enter into force one year after their publication in the Official Journal.</p>	
57	<p>One respondent points to the need to clarify whether institutions can specify different risk weights for individual transactions, or whether each class of specialised lending should be treated the same in this regard.</p>	<p>Recital 6 of the draft RTS specifies that the applicable rules apply to each type of exposures within the meaning of Article 142(1)(2) of Regulation (EU) No 575/2013.</p>	<p>No change.</p>