POLISH BANK ASSOCIATION

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Warsaw, 9 Jan 2013

Ref. Polish Bank Association response on EBA discussion paper on draft regulatory technical standards on prudent valuation EBA/DP/2012/3

Dear Sirs,

The Polish Bank Association welcomes the opportunity to share the views on the European Banking Authority (EBA) discussion paper relating to draft regulatory technical standards (RTS) on prudent valuation under articles 31 and 100 of the draft capital requirement regulation (CRR). In our opinion, when drafting the final RTS, it is very important to take into consideration most of all, two matters: the global level playing field by ensuring harmonisation with the practices and accounting standards of other jurisdiction and the problem of valuation uncertainty which is caused by the lack of reliable data, and therefore is difficult to quantify.

In response to EBA/DP/2012/3 please find our remarks on some questions in Discussion Paper:

Q1. Do you believe that a proportionality threshold should be considered before requiring an institution to assess the prudent value of all fair value positions? If yes, how would you define the threshold?

A1. Yes, a proportionality threshold, which should be assessed before requiring an institution to assess the prudent value of all fair value positions, should be established. This threshold may be defined, e.g. as a relation of the Fair Value of the positions potentially subject to the calculation of AVAs to the common equity Tier 1 capital, set on such a level which would exclude necessity of AVA calculations which would have immaterial effect on capital adequacy ratios.

Q3. Should a specific time horizon for exit be set when assessing the prudent valuation? If so, how the time horizon should be set (e.g. the same time horizon for calculating Value-at-Risk (VaR), Credit Risk Capital Requirements, etc.), what should it be and how would it feed into the calculating of AVAs?

A3. In our opinion no particular time horizon should be set for the purpose of calculating AVAs. It should be estimated at constant market conditions.

Q4. Do you support the concept of a specified level of confidence to determine AVAs? If not, why? Are there any AVAs where the use of a specified level of confidence is not appropriate?

A4.

- We do not support the use of a systematic and prescribed level of confidence to determine AVAs. In principle, the concept of AVA determination at a specified confidence level seems reasonable. However, its applicability may create technical problems mainly related to availability of the data required to derive the sound statistics and to run statistical tests. The allowance of having judgmental approach to derive AVA at the given confidence level in case of no availability of sufficient data does not help much as in that case one would have to support these values in the absence of sound statistics behind. It might be difficult to calculate the AVA for model risk at a specified confidence level or even to assign the confidence level to the calculated AVA for model risk.
- Only if there are enough data points (market quotes) the idea of calculating a confidence interval makes sense from a statistical point of view. But even in

this situation it is not clear why a bank is obliged to take e.g. the lowest quote out of 20 quotes. Banks have to consider the quality of market data they use and when a quote is only available for a very small position, it would be more practical to use a professional or expert judgment for prudent value.

Q6. How prescriptive do you believe the RTS should be around the number of data points that are required to calculate a 95% level of confidence without any more judgemental approach being necessary?

A6.We are afraid that in many cases a confidence level will not be possible to calculate statistically.

Q11. Are there any other indicators of large market price uncertainty which should be included?

A11.

- First of all, a clear distinction should be made between AVA for market price uncertainty and other AVAs, like concentration and liquidity AVA or close-out costs AVA, in order to avoid potential overlaps of the calculated AVAs.
- Clarification should be provided about whether the prudent value is a point estimate. In Article 100 of CRR it seems like possible future changes to markets (e.g. going from normal to stress situations) should be taken into consideration when estimating the AVA's. This somewhat contradicts the definition of fair value and prudent value.

Yours faithfully,

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President of Polish Bank Association