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CEBS

Via E-Mail

Ihr Zeichen, Ihre Nachricht vom	Unser Zeichen, Sachbearbeiter	Durchwahl	Datum
	BSBV 115/Dr.Ru/Br	3137	24th of Jan, 2008

Re: Consultation Paper on Large Exposures

Referring to the above mentioned issue the bank and insurance division of the Austrian Federal Economic Chamber welcomes the opportunity to comment on CEBS' consultation paper as follows:

General remarks

First of all we would like to thank CEBS for producing this detailed consultation paper with a lot of analyses and alternatives. Together with CP 14 this is a profound work on the Large Exposure regime. Many questions require additional work to find out the relevant costs and benefits as well as the pros and cons of different options. Considering this our comments have to be seen as preliminary.

Responses to the questions raised in the CP

Q1. We share CEBS' view of different policy options and also think that an amended limit based backstop regime is the most effective supervisory tool to address the relevant market failures. However, any changes of the existing LE regime should lead to an alignment with capital requirements and internal risk management, especially for complex banks. Additionally proportionality aspects have to be taken into consideration for non-complex banks.

Option 6 should allow discretions for large banks to incorporate internal best practice in the large exposure regime (e.g. exposure definition, limit setting etc.).

The review of the LE Regime and the alignment with the provisions of the CRD is highly appreciated by the banking industry. Nevertheless the alignment of regulations shall not be biased by recent events in financial markets. The recent developments demonstrated risk concentrations in areas which may not be adequately manageable through the LE regime. If the recent events warrant a refinement on the regulation for managing risk concentrations, it would have to be addressed in the CRD and in the LE regime.

Q2. We agree with CEBS concerning the interpretation of 'control' and 'interconnectedness'. These definitions are also already implemented in Austrian Banking Act. As for the financial dependency the time frame should be considered. A timely restricted financial dependency should not be interpreted as 'interconnectedness' and thus not constitute a group of connected clients.

The interpretation of 'interconnectedness' still misses to set objective criteria, moreover the indications listed add rather subjective criteria. The need for clarification in this respect still remains.
Although it is theoretical correct to consider interconnected customers as one group we have strong concerns about the practical feasibility. Since concrete guidelines for the question when customers are interconnected are missing, the recognition of interconnected customers will lead to uncertainties and also to more requests of the authorities, effecting a higher burden for the institutions.

Furthermore we want to stress that the definition of connected clients must be strictly aligned between the CRD and the LE Regime. Deviating definitions would lead to an unacceptable burden for control and reporting systems in each institution.

Moreover, the assessment process with supervisors to clarify the composition of a group of connected clients should be treated more precisely. We understand that supervisory authorities have the right for a final decision whether a client must be regarded as part of a group of connected clients, but it has to be considered that the supervisor has often not all the detailed information as institutions (should) have, so the composition of a group of connected clients should always be reconciled with the relevant institution.

Q3. Both on- and off-balance sheet items should be calculated net of accounting provisions and value adjustments.
Nevertheless internal approval guidelines currently also take into account the gross exposure. With respect to derivatives and other financial instruments internal calculation methods for credit equivalents instead of mtm + regulatory add-on shall be applicable, if the institution can prove that the internal calculation method is set to better reflect potential future exposure.

Q4. We refer to our comments to CP 14 and think that CCF used by most member states have proved their merits and should be maintained. We think that a 100% conversion factor would be too conservative and are against this 100% conversion factor for all off-balance sheet items.

Q5. We are of the opinion that a 0% conversion factor for low risk items would be adequate and justified. Moreover, this would be a further step to align LE regime with CRD. So we plead for the same conversion factors as used in CRD (0, 20, 50 and 100%). A harmonization of the convergence factors and the elimination of national discretions would also reduce the costs for institutions.

Q6. We consider it as adequate to use conversion factors for undrawn credit facilities depending on the maturity. So the existing Article 113(3)(t) of Directive 2006/48/EC could be renounced and national discretions eliminated.

Q7. Using the Institutions' own exposure calculation for large exposure regulation as well as capital requirement and internal steering would institutions move to harmonize and streamline calculations, risk monitoring and internal/external/regulatory reporting. The proposed set of principles is clear and acceptable. The harmonization would reduce IT and reporting costs.

As the LE regime is considered as a limit based backstop regime for unforeseen credit risk events we think that in general advanced IRB institutions also should have the same limits and exposure calculations. However, as the conversion factors for advanced IRB institutions are similar to the ordinary ones, we think it appropriate for allowing using the same conversion factors as for capital requirements. Off-balance-sheet items according to Annex 1 could be treated differently by advanced IRB institutions as this is already done with financial derivatives.

Q9. Furthermore we consider the existing recognition of credit risk mitigation as, all in all, appropriate and there are indeed cases where it is justified to treat mitigation techniques in a different way from the treatment under the minimum capital requirements framework. The liquidity arguments are adequate for a LE regime.

We belief that the treatment of mitigation techniques should not differ from the capital requirements regime as this would lead to disproportional costs for the institutions. Especially in terms of physical collaterals we belief that there are more liquid markets for collaterals other than real estate collaterals. A "one size fits all solution" appears not to be the best from our point of view! Because of that and due to the fact that the implementation of new CRM techniques will cause disproportional costs to institutions leading to little benefits we strongly recommend to align the CRM techniques with those already applied in the CRD.

Q10. Considering the liquidity arguments some credit institutions (c.i.) agree with CEBS' opinion that proposal 2 would be the most suitable alternative.

Other c.i. agree with proposal 1 made by CEBS and consider proposal 2 and even more proposal 3 leading to disproportionate high implementation costs as well as to higher costs caused by running a further calculation model.

Q11. We share CEBS' view concerning costs and benefits for the 3 alternatives.

Q12. We think that the substitution approach could be used by institutions that use the simple method. The main and possible advantage is a harmonization of LE regime and CRD.

Q13. We think that physical collaterals should be treated in the same way as under the CRD. This alignment could reduce costs and we see no danger of increasing the unforeseen risk events in the LE regime. National discretions could be eliminated.

Q14. Indirect exposures should be treated in Pillar 2 of CRD and not in a LE regime. It is more appropriate to require stress tests instead of installing a system of limits and reports.

Q15. For smaller c.i. banking and trading book should be treated differently, in CRD as well as in the LE regime. However, there should be clear accounting rules to ascertain no abuse of booking business in the trading book to avoid excess of limits.

Larger c.i. on the other hand could live with 1 rule for both as we would not have any problems with a large exposure limit in the banking book.

Q16. See Q15.

Q18. Any c.i. don't think that credit related products in the trading book require special attention and different treatment. It must be guaranteed that these products really belong to the trading book, but the treatment of trading book positions should be the same.

For other c.i. a comprehensive understanding of the product is necessary. A product approval process for new products should be mandatory also for trading book exposures and incorporate accounting, performance and risk issues. There should be a common understanding between the transactor, accounting and risk management about risk, performance and price of each product. The seller has a reputational risk and should ideally be able to explain complex products to the buyer.

Q25. We agree with CEBS proposal. This regulation is already applied in Austria.

Q26. We agree with CEBS' proposal to remove the national discretion and to exempt exposures to sovereigns and other international organisations (within Art 113.3 (a-f)), as well as some regional governments and local authorities.

Q31. The current treatment of interbank exposures is sufficient and we think there is no need for a change. Moreover, this treatment has been introduced recently (with January, 1st 2008), so it remains to be seen, if the limits are appropriate or not. In our opinion there is a broad range of national discretions concerning the risk-weighting, even within EU member states (see Table 33, page 101). It would make sense to harmonize these risk-weightings and eliminate national discretions to a great extent.

We think it should be kept in mind that a regime, enabling larger banks to use their own best practice, would be appropriate.

Q32. We think that a 25% limit on all interbank exposures would not unduly affect institutions' ability to manage their liquidity as long as the discretions and risk weights of Art. 113 of 2006/48/EC are being kept. As already stated above we think that maturity of the exposure should not play a role.

Q34. We see the LE regime as a limit based backstop regime. However, there might be cases which cause an excess of these limits. We think that such a breach of limits shouldn't be

charged, but the excess should lead to a deduction of own funds. We therefore are for option 3 or a combination of option 2 and 3.

Q35. From our point of view, a reporting based on the internal reports of the institutions will be a possible way to report large exposures. Reporting in this way would save the costs which are needed to implement and maintain a separate reporting to the authority. Nonetheless we understand CEBS´ concerns that this would exacerbate the authorities´ possibility to compare the data which could lead to an increased amount of questions.
Given that the large exposure regime will be further aligned with the capital requirements regime, we also can think of a reporting through a report defined by the supervisors. Here we would like to stress out that this report should not lead to a higher administrative burden for the institutions!
Regarding the frequency of the respect we are in favour of a reporting on a quarterly basis.

Q36. As mentioned above, we could accept reporting on basis of a predefined report as long as this report will not lead to a higher administrative burden for the institutions.

Q37. We think that the existing reporting regime is sound and appropriate. The most of the points have been applied in Austria so that this will not lead to a lower workload for the institutions.

Q38. We think that the LE regime with limits should be applied by all institutions.

- ad 180ff: We believe that the current level of own funds for investment firms which are in line with the European UCITS framework should not necessarily be changed since they proved to be useful. However, if there are any amendments in this regard, they clearly have to be in line with the UCITS framework.

- ad 236ff: We agree with the statement that investment management firms do not appear to represent a significant risk of contagion due to their specific nature. It is also true that investment firms generally do not have large unsecured exposures. Moreover, it is important to stress as in point 238 that investment management firms are not funded by depositors and that the costs associated with failures of investment firms are likely to be relatively limited. In this regard, one characteristics of an investment management firm is that they are obliged to hold the client assets separately from the firm's assets. Besides that, it has to be stressed that in terms of market failure analysis / cost benefit analysis, the regulatory and compliance burden for investment management companies is relatively high, since unfortunately most regulatory initiatives in this regard are simply imposed on these firms, so a more tailor-made approach in line with the UCITS framework would be favoured by the industry.

Yours sincerely

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