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Banking supervision
And Accounting issues Unit
The Director

Paris, September 27h 2012

The French Banking Federation comments on the draft RTS on the specification of the calculation of specific and general credit risk adjustments according to Article 105(4) of the draft Capital Requirements Regulation (CRR) (EBA/CP/2012/10)

Dear Madam,

The French Banking Federation (FBF) is the professional body representing over 450 commercial, cooperative and mutual banks operating in France. It includes both French and foreign-based organizations.

The FBF welcomes the opportunity to comment on the draft RTS. We appreciate the concern of the EBA to specify the calculation of specific credit risk adjustment (SCRA) and general credit risk adjustments (GCRA) in accordance with the new CRR requirements.

Nevertheless, we would like to point out our main concern related to differentiation of treatment between the specific and general credit risk adjustments (GCRAs and SCRAs). Under the current CRD rules, GCRA and SCRA are deducted from exposure value which makes sense as both GCRA and SCRA are constituted through P&L and therefore are already deducted from CET1. The draft CRR limits the deduction, under the Standardized approach, to SCRA and does not allow deduction of GCRA from exposure value which has no economic rationale. To ensure consistency of the CRR with the accounting rules and the neutrality of the prudential treatment of credit risk adjustment to any forthcoming changes in accounting standards, we encourage the EBA to support the technical amendment made to the Commission's CRR initial proposal to withdraw any distinction between SCRA and GCRA and, thus, to revert to the current CRD rules.

Mrs Isabelle VAILLANT
European Banking Authority
Tower 42 (level 18)
25 Old Broad Street
London EC2N 1HQ
United Kingdom

Besides, the upcoming accounting reform (IFRS 9) will define new impairment buckets ("buckets 1 and 2") based on expected losses that will be qualified for GCRA and that will affect the Tier 1 ratio. We recommend the EBA to anticipate as much as possible on IFRS 9 rules and adopt the same criteria for GCRA classification and IFRS 9 buckets 1 and 2 criteria. Indeed, the consequences of setting up diverging prudential and accounting standards for GCRA will be highly detrimental for prudential soundness and risk management purposes: this would result, for example, in huge difficulties in reconciling risk and accounting data (which goes against principles set out in the Basel Committee's *Principles for Effective Risk Data Aggregation and Risk Reporting*), and additional costs in maintaining two parallel provisioning frameworks.

Finally, it is worth noting that the proposed Basel III requirements have been calibrating under current CRA provisions. However, the future IFRS 9 accounting rules will considerably increase provisioning requirements. Therefore, in order to avoid any overestimation of capital requirements in the future, it would be advisable to allow deduction of GCRA from Tier 2 rather than Tier 1 capital or to re-calibrate Basel III proposals taking into account forthcoming provisioning rules.

You will find in the appendix attached our responses to the questions of the consultation paper. We hope you find these comments useful and remain at your disposal for any questions you might have.

Yours sincerely,

Jean-Paul CAUDAL

Appendix.

Identification of GCRAs and SCRAs

Q1. Are the provisions included in this draft RTS on criteria that specify which amounts shall be included in the calculation of GCRAs or SCRAs respectively, sufficiently clear? Are there aspects which need to be elaborated further?

As mentioned in our cover letter, our main concern is the differentiation of treatment between the specific and general credit risk adjustments (GCRAs and SCRAs) proposed by the RTS. The draft CRR limits the deduction to SCRA under the Standardized approach without any economic rationale. It maintains the deduction of GCRA and SCRA whilst requiring that GCRA should not be deducted from exposure value. Thus, we strongly advocate the EBA to support the technical amendment that has been proposed on the paragraphs of level 1 text related to credit risk adjustment which consists in reverting back to the current CRD rules.

We recommend GCRAs to be deducted from Tier 2 rather than Tier 1. Indeed, the upcoming IFRS 9 standard will define new impairment buckets ("buckets 1 and 2") based on expected losses. It will affect the Tier 1 ratio whereas the capital ratios under Basel III requirements would be calibrated under current CRA provisions.

We question the wording used and notably the notion of "evidence of credit deterioration". Indeed any inconsistency in accounting and prudential referential for the same concept would generate difficulties of interpretation and divergence of application between the accounting and prudential framework without merit. Without having an explicit reference to specific accounting standards, same wording should be used in both set of rules.
Related paragraphs of the RTS should be amended in accordance with the definition of impairment allowance for expected losses as it will be defined in the accounting standard and in a way the prudential treatment should not be affected by the upcoming IFRS rule Given that IFRS 9 impairment phase is still at a project stage, we believe that the RTS should be finalized when the IFRS 9 impairment chapters will be issued.

Q2: Are there any issues regarding the timing of recognition of provisions, value adjustments or impairments in profit or loss and in Common Equity Tier 1 capital?

No comments at this point. We would need some more clarification on the notion of "timing of recognition".

Calculation of GCRAs and SCRAs for own funds requirements

Q3: Are the provisions included in this draft RTS on criteria to assign SCRAs for a group of exposures sufficiently clear? Are there aspects which need to be elaborated further?

Assigning SCRAs for a group of exposures on the basis of RWA associated with those exposures leads to a burdensome calculation of RWA, without taking into consideration SCRAs. A much easier and less burdensome methodology would consist in assigning SCRAs for a group of exposures on the basis of EAD rather than RWA.

Q4: Are the provisions included in this draft RTS sufficiently clear? Are there aspects which need to be elaborated further?

As far as the determination of a default is concerned, we question the definition retained in the Article 174 of CRR that considers a default has occurred when notably the obligor is past due more than 90 days on any material credit obligation. As a consequence, the 90-days past due trigger is applicable regardless of the nature of exposure.

Moreover, we suggest clarifying Art. 5 of the draft RTS by adding the following paragraph *"for institutions applying the IRB approach, all SCRAs and GCRAs calculated at points (1) and (2) need to be sum up for all exposures treated under the IRB approaches across the institution, without prejudice of Art. 3(3). The resulting sum, calculated on a solo basis, sub-consolidated basis or consolidated basis, depending on the level of application of requirements as defined in Title II, Part I, is used to make the comparison with expected losses calculated on the same perimeter, as provided for at Art. 155 of the CRR."*

Q5: Do you support the policy proposal, in particular to the preferred policy option (3), and the EBA"s assessment that its impact is relatively immaterial to the CRR text? If not please explain why and provide estimates of such impacts whenever possible.

We understand the concern of EBA to promote consistent application of the RTS and avoid any discrepancy in regulatory practices. Thus we support EBA's option 3 although some banks would favor assigning SCRAs for a group of exposures on the basis of EAD.

Cost-benefit analyses
Q6: What is the incremental cost to your institution for the implementation of this proposal?
Q7: What is the incremental cost for the ongoing compliance with this proposal?
Q8: What is the incremental benefit to your institution for the implementation of this proposal?
Q9: What is the incremental benefit for the ongoing compliance of this proposal?

Meeting the RTS requirements implies costs of implementation and of ongoing compliance due to changes in current practices. However, the costs would increase if issues mentioned above could not be resolved, i.e. divergence of definitions between the accounting standards and the provisions of the RTS related to impairment notions.