

French Banking Federation response to EBA Consultation Paper on the sequential implementation of the IRB Approach and permanent partial use under the Standardised Approach under Articles 148(6), 150(3) and 152(5) of Regulation (EU) n°575/2013 (Capital Requirements Regulation – CRR) (CP/2014/10)

The French Banking Federation (FBF) represents the interests of the banking industry in France. Its membership is composed of all credit institutions authorized as banks and doing business in France, i.e. more than 390 commercial, cooperative and mutual banks. FBF member banks have more than 38,000 permanent branches in France. They employ 370,000 people in France and around the world, and service 48 million customers.

The FBF welcome the opportunity to share its view on EBA Consultation paper relative to a draft regulatory technical standard on the permanent and temporary uses of the IRB approach.

1 GENERAL COMMENTS

We welcome the EBA intent to clarify the conditions of application of permanent and temporary use of the Standardised Approach by institutions in order to foster the harmonisation for IRB institutions using this method. In all cases related to the involved article, the draft consultative paper mentions that institutions have to comply with quantitative and qualitative criteria.

We agree on the qualitative requirement allowing flexibility and supporting the institutions in the management of a customized roll-out plan and their use of Standardised Approach on a permanent basis. However, we express our concerns regarding quantitative criteria. We think they are too stringent, difficult to understand in some cases and to implement.

We really think institutions should not have to face complexity when implementing the requirements related to Articles 148 §6, 150 §3 and 152 §5. Securitization seems not to be submitted to these requirements; could you confirm or clarify the non-applicability to securitization? However, as far as quantitative criteria are concerned, we propose to:

- Adjust the different proposed thresholds (see answers to the different questions (1 to 4) for the proposed level) ;
- Generally refer to existing regulatory definitions (reference to Regulation (EU) n°575/2013). In particular refer to a unique metric : the exposure value, in line with CRR definition ;
- Introduce grandfathering in respect with authorization given by Competent Authorities;
- Introduce flexibility as far as compliance with quantitative thresholds is concerned.

Could you please clarify the articulation between the two different standards, i.e. the RTS on the PPU and the RTS on the conditions for assessing the materiality (Commission delegated regulation EU 529/2014 of 12 march 2014)?

Our understanding is these requirements would not be applied to acquisition of a portfolio or a new business. Indeed these cases are potentially subject to RTS on the conditions for assessing the materiality of extensions and changes of internal approaches when calculating own funds requirements for credit and operational risk in accordance with Articles 143(5) and 312(4)(b) and (c) of Regulation (EU) No 575/2013 (Capital Requirements Regulation – CRR).

We also propose the requirements to be applied both on a consolidated basis and on an individual basis only for supervised entities that have to report on a solo basis to Competent Authorities. When supervised entities have to report to only one Competent Authority, these Authority should be able to decide the relevant level to appreciate quantitative thresholds.

To sum up, we would like to insist on the need to maintain simplicity in respect of the use of the sequential implementation of the IRB Approach and of the permanent partial use under the Standardised Approach based among others on flexibility associated with both qualitative as well as quantitative conditions institutions have to comply with. As to the former, the draft paper offers a fair compromise. We think this is not the case for the latter. Therefore, we would like to emphasize on the need to have objective measures that refer to less stringent ratio levels, to only one metric and to regulatory text.

2 RTS SPECIFIC QUESTIONS

2.1 QUESTION 1 : DO YOU AGREE WITH THE PROPOSED DRAFT RTS REGARDING THE SEQUENTIAL APPLICATION OF THE IRB APPROACH?

We agree with the idea of setting quantitative limits as far as the sequential application of the IRB Approach is concerned. However, we have some concerns that relate to:

- The management of this limit compliance over time due to exposure variations through mergers, sales and acquisitions. Such situations may change the institution's distribution of exposures and therefore lead to a non-compliance with the RTS ;
- The way to deal with situations where setting such limits may create some difficulties when switching to IRBA. For instance, this could be the case when an entity has the following exposure distribution: 40% corporate exposures, 40% retail exposures and 20% other types of exposures.

The threshold at 50% of exposures and RWEA is a too stringent condition. We have a question regarding the application of the 50% coverage ratio: Banks have to be compliant with the 50% coverage ratio when banks demand the permission to switch into IRBA or banks

As a consequence, we propose to:

- Use only one metric for the 50% threshold : the exposure amount as defined in Regulation (EU) n°575/2013 (articles 111 and 166) as per the exposure class defined before CRM;
- To introduce flexibility and allow discussions with Competent Authorities on a case by case basis and if necessary that institutions present a plan to return to compliance or demonstrate the effect of the non-compliance is immaterial (Article 146 of Regulation (EU) n°575/2013).

Our proposal is based on the following elements:

- Exposure value is a more objective measure than RWEA which is already based through models and CRM types. Moreover, it is more appropriate for comparison purposes ;
- Referring to one metric is more appropriate because there is no 1 to 1 relation between exposure amount and risk weighted amount exposure ;
- Defining exposure amounts in accordance with regulation allows homogenous and objective concepts to which all regulated institutions refer to.

2.2 QUESTION 2 : DO YOU AGREE WITH THE PROPOSED DRAFT RTS REGARDING PERMANENT PARTIAL USE OF THE STANDARDISED APPROACH FOR THE EXPOSURES SPECIFIED IN ARTICLE 150 (1)(A) AND (B) OF THE CRR?

This draft RTS proposes a combination of quantitative and qualitative conditions to authorise an institution to permanently use the Standardised Approach on its exposures to central governments and central banks as well as exposures to institutions.

According to Article 150 §1 a and b, institutions may apply the Standardised Approach for exposures to central governments and central banks as well as to institutions where:

- The number of material counterparties is limited ;
- It would be unduly burdensome for the institution to implement a rating system for these counterparties.

We don't have any remark on the second condition.

The first condition deals with quantitative conditions:

- We notice that the proposed percentage ratios institutions have to comply with are not mentioned in the CRR. Therefore this questions the validity of such limits ;
- We agree on the necessity to set limit referring to material counterparties but we have some concern on the number that has been set (20).

We agree on the combination of qualitative and quantitative conditions but, as far as the latter are concerned, we propose:

- To increase the number of material counterparties to 100. We think this is a fair number because it is still statistically insignificant. It is also a more adequate measure for institutions that have specific activities ;
- To consider "connected counterparties" as defined for the Large exposures requirements rather than the definition mentioned in the draft Consultation Paper. Indeed, dealing with connected counterparties is a measure that :
 - refers to regulatory texts ;
 - is already managed by institutions ;
 - is already part of supervisory controls.

However, in case the percentage ratio is maintained, we suggest:

- To use only one metric : the exposure amount as defined in Regulation (EU) n°575/2013 (articles 111 and 166) ;
- To set the ratio level at 15% ;
- To introduce flexibility in the compliance with the thresholds.

This last proposal is based on the same rationale as exposed in question 1 (for more details, see answer to question 1).

For a better understanding of the text, we would like to know what does “the aggregate exposure value” mean (Article 2 §1a of Consultative Paper EBA/CP/2014/10 – 26 June 2014). Does that mean “total exposure value”? We would like to have a concrete example. We have the same request for the “set of relevant exposures”.

2.3 QUESTION 3 : DO YOU AGREE WITH THE PROPOSED DRAFT RTS REGARDING PERMANENT PARTIAL USE OF THE STANDARDISED APPROACH FOR THE EXPOSURES SPECIFIED IN ARTICLE 150 (1)C? WHICH OF THE TWO ALTERNATIVE PROPOSALS PRESENTED IN THE IMPACT ASSESSMENT SECTION UNDER “TECHNICAL OPTIONS CONSIDERED” DO YOU PREFER?

Regarding Permanent Partial Use of the Standardised Approach for small business unit exposures, we think that setting quantitative limit is appropriate but that the 8% threshold is too restrictive.

As a consequence, we suggest that:

- The percentage ratio only refers to one metric: the exposure amount before CRM. Our rationale for this proposition relies on the same reasons as those mentioned in answer to question 1. The exposure amount is more appropriate to estimate whether small business units are immaterial in terms of size as requested in Article 150 §1 c of Regulation (EU) n°575/2014 ;
- The ratio limit be set at 15% ;
- To ensure homogeneity flexibility (discussions with Competent Authorities) be introduced to allow for portfolio management in case of mergers, acquisitions...;
- The Competent Authorities consider in the implementation of the threshold the different mechanisms of mutual recognition of the decisions (home-host mechanism); the authorisation based on the host authority opinion won't be possible when the host jurisdiction hasn't implemented the Basel II agreement ;
- The set of relevant exposures be the same for each exposure class, i.e. central governments and central banks, institutions, and small business units or immaterial exposures as well as for those under roll-out. It should be equal to all exposures of the institution excluding equity exposures as referred to in articles 133 §1 and 147 §6 and all exposures for which the institutions has received permission to apply the Standardised Approach on the basis of Article 150 §1 d to f, I, j of Regulation (EU) n°575/2013 ;
- The set of relevant exposures be precisely defined. Indeed, we have great difficulties in understanding what this concept refers to. Indeed, we need examples to monitor this notion.

We understood that the draft Consultative Paper introduces some kind of flexibility. Indeed, the text proposes two alternatives to manage threshold overruns.

- To manage such situations, we prefer the first alternative where the overall threshold could be complemented by an analysis of the immateriality/non significance of the different types of exposures, exposure classes and business that fall under that overall threshold.
- It should be highlighted that the alternatives proposed are very difficult to understand and appears complex to implement (especially the alternative 2). We have major problems in understanding the underpinned adjustments both in terms of interpretation and implementation.
- In any case the respect of the former supervisory authorizations should be ensured by including a grandfathering clause.

Therefore, we really prefer that flexibility relies on discussions with Competent Authorities and if necessary that institutions present a plan to return to compliance or demonstrate the effect of the non-compliance is immaterial (Article 146 of Regulation (EU) n°575/2013).

Besides, we think that Article 3 needs some clarification (there might be typo problem : “ For the purposes of application of Article 150 (1) (c) of Regulation (EU) No 575/2013, the application of the Standardised Approach shall be considered as being limited to classes or types of exposures that are immaterial in terms of size and perceived risk profile as well as to exposures in non-significant business units and the conditions that allow competent authorities to permit the application of the Standardised Approach according **to Article 152(b)** of Regulation (EU) No 575/201 shall be considered to be met, if both conditions below are met”.

2.4 QUESTION 4 : DO YOU AGREE WITH THE QUANTITATIVE THRESHOLDS PROPOSED IN ARTICLE 2(1), 3 AND 4(2) OF THESE DRAFT RTS? IF NOT, WHAT THRESHOLDS DO YOU CONSIDER MORE SUITABLE?

Generally speaking, we have some concerns regarding quantitative criteria. Quantitative limits are too stringent and do not allow for enough flexibility.

Our concerns are posted in answers to questions 1, 2 and 3. They are summarised below:

- Article 4 (2): 50% sequential roll out limit in terms of exposure amount and RWEAs.
 - We propose a coverage ratio at 50% of the exposure amount only. In case the percentage threshold is maintained, we would like that grandfathering be authorized as well as flexibility ;
 - We would like the threshold to refer to only one metric: the exposure value.
- Article 2 (2): exposures to central banks and governments and institutions : 8% limit in terms of exposure amount and RWEAs and number of material counterparties in each exposure class (below 20).
 - We propose to increase the number of material counterparties in each involved exposure class up to 100. In case, the percentage threshold is maintained, we suggest the threshold to refer only one metric : the exposure value. The threshold level should be 15%
- Article 3: small business units and immaterial exposures : 8% limit in terms of exposure amount and RWEAs.

- We propose ratios to refer only to one metric: the exposure amount and to increase the threshold up to 15%. In order to manage flexibility, we prefer it to be based on discussions with Competent Authorities.
- In case we need to decide between the two proposed alternatives, we choose the first one, the qualitative one (p19). However, we have huge concerns on how to implement it and on the partiality it introduces.

In any case, we support the idea of flexibility based on discussions with Competent Authorities, the need for objective measures as well as the need to refer to regulatory definitions (Regulation (EU) n°575/2013). We believe that it would not be useful to introduce complexity when dealing with Article 148 §6, 150 §3 and 152 §5 of Regulation (EU) n°575/2013.

The following remarks relates to all the proposed quantitative limits.

- Regulatory references :
 - Necessity to refer to regulatory references (Regulation (EU) n°575/2013 as far as the following concepts are concerned) :
 - Material counterparties : reference to Large exposures requirement.
 - Exposure amount : reference to Article 111 and 166.
- Set of relevant exposures
 - Necessity to precisely define the set of relevant exposure for each exposure class under the Permanent Partial Use and for exposures under roll out.
 - Requirement of the same definition of set of relevant exposures for each class under the Permanent Partial Use and for exposures under roll out.
- Ratio in terms of percentage :
 - When dealing with thresholds' expressed in terms of percentage, use of only one metric : the exposure amount.
- Portfolio management
 - Necessity to introduce flexibility in order to allow portfolio management over time and variations of exposure amounts through mergers, acquisitions...
- Technical concepts
 - Need for explanation of the second alternative and the 3 associated adjustments.

2.5 QUESTION 5 : DO YOU THINK THAT SEPARATE QUANTITATIVE THRESHOLDS SHOULD APPLY FOR APPLICATION OF THESE DRAFT RTS ON AN INDIVIDUAL AND ON A CONSOLIDATED BASIS? WHICH OF THE TWO ALTERNATIVES PROPOSALS PRESENTED IN THE IMPACT ASSESSMENT SECTION UNDER "TECHNICAL OPTIONS CONSIDERED" DO YOU PREFER?

We encountered serious difficulties in circumscribing the proposed options in the draft Consultative Paper as regards to the level of application of the thresholds. Moreover, we did not understand the different arguments used to support one or other of the proposed alternatives.

Therefore we propose to apply the thresholds on both a consolidated basis where applicable and on an individual basis only for supervised entities that are due to report on a solo basis to Competent Authorities.

2.6 DO YOU AGREE WITH OUR ANALYSIS OF THE IMPACT OF THE PROPOSALS IN THIS CONSULTATION PAPER? IF NOT, CAN YOU PROVIDE ANY EVIDENCE OR DATA THAT WOULD EXPLAIN WHY YOU DISAGREE OR WHICH MIGHT ASSIST OUR ANALYSIS OF THE POSSIBLE IMPACT OF THE PROPOSALS?

We agree with the idea that institutions should not have to cope with difficulties when applying the requirement that refer to Articles 148 §6, 150 §3 and 152 §5 of Regulation (EU) n°575/2013. However, we think that the proposed draft RTS underestimates the impact of the proposed measures and lacks the necessary degree of flexibility required for the sequential implementation of the IRB approach within the French institutions.