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Finance for Europe

Association for Financial Markets in Europe

AFME response – EBA consultation on proportionate risk diversification methods

February 2025

The Association for Financial Markets in Europe (AFME) welcomes the opportunity to respond to the EBA's **consultation on guidelines on proportional risk diversification methods.**

AFME represents a broad array of European and global participants in the wholesale financial markets. Its members comprise pan-EU and global banks as well as key regional banks, brokers, law firms, investors and other financial market participants. We advocate stable, competitive, sustainable European financial markets that support economic growth and benefit society. AFME is the European member of the Global Financial Markets Association (GFMA) a global alliance with the Securities Industry and Financial Markets Association (SIFMA) in the US, and the Asia Securities Industry and Financial Markets Association (ASIFMA) in Asia. AFME is listed on the EU Register of Interest Representatives, registration number 65110063986-76.

General comments

In summary, we think that the proposed diversification test may create an additional computational burden that is unnecessary for large institutions. To address this, we would like to propose a derogation for institutions whose retail portfolio represents a total amount due by clients greater than EUR500M. In addition to this, we think some clarifications to the proposed method are needed to support its application.

Q1. What is the percentage of exposures within your retail portfolio that are part of a group of connected clients?

N/A

Q2. Do you identify any implementation issue in implementing the diversification method?

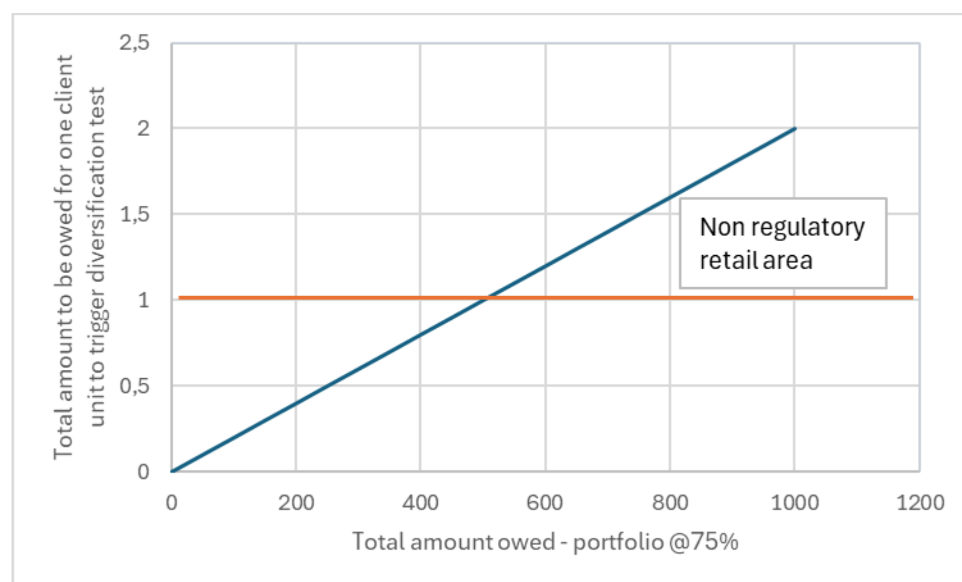
We welcome the willingness of EBA to take a proportionate approach to reduce the burden. Nevertheless, we are of the opinion that the two-step approach which is contemplated could be further simplified to better leverage on the existing computation applied for the classification of regulatory retail exposures eligible for the 75% risk-weight. Specifically, we recommend a derogation for institutions whose retail portfolio represents a total amount due by clients greater than EUR500M.

Indeed, as per CRR Article 123, we would like to recall that the criteria of the EURM 1 threshold is to be computed based on the total amount owed by the clients and connected clients, excluding exposures secured by immovable properties up to the property value. This notion is based on the current outstanding of the loans to the same set of clients, i.e. the part that they have already drawn. This notion is different from the one of EAD which also encompasses the undrawn amount subject to a CCF.

Thus, we would suggest enhancing the principle of proportionality by basing the diversification test on the same metric as the regulatory retail threshold instead of EAD, i.e. the total amount owed by the clients. This

would notably allow large institutions not to have to run an unduly burdensome new computation which would always show a proportionate diversification in respect of their size.

Indeed, by adjusting to a metric already developed by all institutions based on a concrete regulatory requirement, the EBA would ease the diversification test for institutions with portfolio of 75%-eligible exposures representing an aggregated total amount owed of EUR 500M (excluding exposures secured by immovable properties up to the property value). Beyond this threshold 0,2% of the total amount owed at portfolio level is going to be greater than EURM 1 and, by definition, no set of regulatory retail clients can have a total owed amount greater than EURM 1.



This is already anticipated by the EBA, starting in Section 5:

"20. Larger institutions can be in a better position to have less concentrated retail portfolios, in case retail exposures are a relevant part of the business activities of this institution, and in such case are expected to meet the 0.2% granularity criterion more easily compared with smaller institutions. Thus, diversification concerns are limited for larger retail portfolios and the introduced measure is of particularly relevance and provides flexibility for those institutions with retail portfolios with obligors for which the total amount owed by all these obligors or groups of connected clients to the institution, its parents and its subsidiaries (other than for RRE) is lower than EUR 500mn."

Alternatively, should the test metric not be amended, giving explicit exemption to institutions with retail portfolios with obligors for which the total amount owed by all these obligors or groups of connected clients to the institution, its parents and its subsidiaries (other than for RRE) is no less than EURM 500 would greatly increase the proportionality and, for groups, allow to better manage the EBA guideline for assessing diversification at all the levels of the group that are subject to prudential requirements. Additionally, it would prevent banks from undertaking an unduly burdensome calculation.

Irrespective of whether our suggestion to simplify the requirement is taken on board, we recommend some clarifications to the calculation proposed in the guidelines as follows:

- For the calculation of the exposure value, credit risk mitigation should be disregarded (in line with the Basel framework).
- The EBA proposes to include those exposures secured by mortgages on immovable property that are to be risk-weighted as retail for the unsecured portion. The draft EBA Guidelines do not specify whether only the portion above 55% of the property value must be included in this diversification test. We would propose that only the portion above 55% of the property value is included since only this portion receives the 75% risk weight for retail. This point was clarified in the EBA public hearing, but since it is not clear based on the draft text, we would welcome an explicit clarification in the final text.
- Clarify if this framework is intended to capture securitisations when institutions use SEC-SA. AFME's view is they should not be captured – this would be very hard to do and validate via the ESMA templates to identify if the pool is under or over the €500M. This is a larger issue for institutions holding securitisations in non-retail subsidiaries, as there isn't a large pool of direct retail exposures to compare this underlying pool against.
- Clarify the concept of a subset portfolio.

Q3. Which methods do you currently use to assess retail diversification? Please elaborate.

Members have identified the following methods which they use:

Principle-based:

- The size of our retail portfolios ensures meeting the Basel threshold.
- Clients and products segmentation belonging to retail portfolio translates into diversification.

Q4. Under the proposed approach, in the first step of the calculation before any exclusion, what is the share in terms of exposure value of the large eligible retail exposures as defined under the proposed approach compared to all the eligible retail exposures?

N/A

Q5. What is the impact of the proposed diversification assessment set out in these Guidelines compared to the diversification assessment that you currently perform on your retail portfolio?

None besides undue operational burden.

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