European Banking Authority

EBA Consultation Paper
Guidelines on the application of the definition of default under Article 178 of Regulation (EU) 575/2013

http://www.eba.europa.eu/documents/10180/1198203/EBA-CP-2015-15+%28CP+on+GL+on+the+application+of+the+definition+of+default%29.pdf

The British Bankers' Association ("BBA") is the leading trade association for the UK banking sector with 200 member banks headquartered in over 50 countries with operations in 180 jurisdictions worldwide. Eighty per cent of global systemically important banks are members of the BBA. As the representative of the world's largest international banking cluster the BBA is the voice of UK banking.

All the major banking players in the UK are members of our association as are the large international EU banks, the US banks operating in the UK and financial entities from around the world. The integrated nature of banking means that our members are engaged in activities ranging widely across the financial spectrum encompassing services and products as diverse as primary and secondary securities trading, insurance, investment banking and wealth management, as well as deposit taking and other conventional forms of banking.

Our members manage more than £7 trillion in UK banking assets, employ nearly half a million individuals nationally, contribute over £60 billion to the UK economy each year and lend over £150 billion to UK businesses.

The BBA is pleased to respond to the European Banking Authority's (EBA) EBA Consultation Paper: Guidelines on the application of the definition of default under Article 178 of Regulation (EU) 575/2013.

We would be happy to have further discussion with the EBA to explain in further detail our comments.

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European Banking Authority EBA Consultation Paper
Guidelines on the application of the definition of default under Article 178 of Regulation (EU) 575/2013

Summary

We welcome the objective of the Guidelines to harmonise the definition of default to ensure consistency of its application, transparency and comparability of risk parameters between banks across the Member States.

However, we think that there are many changes needed to the CP before our members would be in a position to support the implementation of EBA guidelines as mandated by Article 178(7) of the CRR.

Given that the definition of default is a fundamental building block of the modelling of risk and a primary input into the calculation of regulatory and economic capital, our recommendation is that the EBA would be wise to reissue the CP taking into account EU-wide feedback for a further consultation before issuing the finalised guidelines.

At a minimum, we would urge a further public hearing in which the EBA could provide its response to the many issues set out in our and other responses in particular the EBF response. We draw out some key themes of our response within this letter, and will elaborate further on more detailed points within the Annex.

Time needed for implementation

- We consider that the guidelines should be phased in commencing from 1 January 2019 in line with transition dates for the completion of the implementation of the CRD IV. But we express caution with mandating a final date until the policy is finalised and the banking sector consulted.

- We would suggest that the EBA allows banks a minimum three year transition to full compliance with a completion date of 1 January 2022. This would allow a three-year period during which banks could choose when to adopt the new guidelines to take into account operational changes, parallel running or implementation.

- Finally, we are of the view that implementation of the new definition should not precede the entry into force of the IFRS 9 standard.

IFRS 9

- We think that the guidelines could do more to harmonise with IFRS9 and we recommend changes to the CP in order to do so. More details are given within the responses to questions

- For example, we think that it would be beneficial to confirm that the counting of days past due (section 3.2.1 in the pre-amble) commences from the 91st day and that the EBA and IFRS are aligned

Frequency of calculation of default

- We are concerned with the requirement to calculate default on a daily basis (Para 19). The implication of this has major ramifications including a presumption of the daily calculation of many ratios. Certainly for retail portfolios this is impractical.

- The paragraph refers to obligor default but it is not clear whether this requirement also applies to retail facility level defaults.

- For regulatory capital purposes retail products are managed on a monthly basis. Banks do not therefore calculate regulatory default on a daily basis for credit risk management purposes.

- For some products the number of days past due at month end is used in order to establish regulatory default. For other products default is established by dividing the outstanding balance by the contractual payment and not to perform a days past due count. It is not clear whether these practices (that are approved by the competent authority) will be allowed to continue. We would encourage the EBA to permit this flexibility that is country specific to continue.

Retrospective application of guidelines

We do not support the retrospective application of the guidelines

- Adjusting historical data to the proposed application of the default definition will be challenging in terms of required cost and time, if not impossible in certain cases due to unavailability of the data (in particular when the unlikeliness to pay trigger is changed). Retrospective application would imply manual review in order to assess whether the customer should be considered defaulted according to the new definition.

- Besides, in certain instances the retrospective application of the definition of default will not be appropriate. This is valid for example for distressed restructurings and sales of credit obligations. It is likely that different considerations would have been made when outlining the restructuration plan or the sale conditions, if the definition of default had been different.

- We believe an approach based on "best estimates" following the new rules would be operationally least challenging, although we acknowledge that it would open the door to a high degree of inconsistency, contrary to the CP's harmonization objective.

Materiality thresholds

- The BBA notes that the EBA has previously consulted on the topic of Regulatory Technical Standards on materiality threshold of credit obligation past due, [1] and that the BBA and two of our largest members (HSBC and Barclays) commented upon the proposals.

- We encourage the EBA to take the industry response to that consultation into account and the further comments set out in our response to this consultation.

[1] https://www.eba.europa.eu/regulation-and-policy/credit-risk/regulatory-technical-standards-on-materiality-threshold-of-credit-obligation-past-due

National Discretion

- We note that the UK will continue to be permitted to use 180 days past due for Retail exposures (excluding retail SME exposures) [2]

- Para 28 refers to competent authorities allowing 90 days to be replaced by 180 days past due. We welcome this approach but are concerned that the national discretion is due to be revisited by the end of 2017 to establish whether it may continue past the end of 2019.

- We believe that the national discretion should continue but we need clarity over this at the same time as other requirements i.e. banks will not be expected to revise their definition of default to meet the requirements of the Guidelines and then again subsequently if the national discretion is removed.

Bankruptcy

- We support the clarification of protection similar to bankruptcy in paragraph 45.

- However, CRR 178 3(f) links bankruptcy to unlikeliness to pay "*where this would avoid or delay repayment of a credit obligation to the institution*". Bankruptcy orders often allow the debtor to retain their primary residence and exclude mortgage payments from the action, as they acknowledge the bankrupt party has to live somewhere. So such mortgage exposures should not automatically be treated as default. The guidelines do not take this into account.

- Additionally, analytical evidence does not justify this approach. Where a bankruptcy is identified it should be included in the assessment of PD but not automatically trigger a default. Finally, where a retail facility level approach is adopted the contagion effects (joint accounts) should not apply.

Consistent identification of default of a single obligor

- We broadly agree the principal of proposed approach. However we think that the proposals are too restrictive. Given the increasing mobility of retail clients across national jurisdictions, the incidence of exposure to the same retail client across jurisdictions and thus exposure to different legal entities within a group is becoming more frequent.

- However, our view is that rather than look at the materiality of non-compliance which itself requires a definition of materiality, it would be more practical for an institution to establish over-riding policies to its assessment of risk when the same retail client / obligor has legal contracts in multiple jurisdictions. This should take into account the legal structure of the institution.

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[2] Refer BIPRU 4.6.19 - 22 Definition of Default: Release 164: Aug 2015
https://www.handbook.fca.org.uk/handbook/BIPRU/4/6.pdf

- In cases where the exposure is within single point of entry legal structure (branches in multiple jurisdictions) it may make sense to apply a consistent treatment across the client. However, when the client's exposure are to separate legal subsidiaries of the group it makes sense to look at the treatment on a standalone legal entity basis.

- There is also a need to respect data protection. It may well be that some jurisdictions do not permit the sharing of personal credit data cross-border.

- These factors need to be taken into account and permitted.

ANNEX

Question 1:

Do you agree with the proposed definition of technical defaults?

We think that the proposals should be refined.

Restricting the definition of technical defaults to errors caused by the Bank, as seems to be suggested, is not supported.

The current approach whereby a firm can review the individual status of an account to confirm default recognises the complexity of individual banking relationships and should not be rescinded.

Do you believe that other situations should be included in this definition?

The definition should be expanded to allow for non-credit related factors.

Examples of non- credit related issues will include more than materiality thresholds or system/process errors on the part of the bank. For example:

The provisions for technical defaults appear to only contemplate the instance of bank errors (IT system and processes) which may arise as a result of system and organisational complexities. However, the same may be said of large complex customers, particularly in the Wholesale portfolios, which may be subject to similar operational risks and issues not related to the quality of credit risk.

Non-credit related disputes especially in relation to HP and Leasing transactions, trade debtors and factoring arrangements where there could be 3rd party issues involved (e.g. dispute over goods/services provided). The narrowing of the definition to exclude Administrative Oversights is particularly restrictive for operating leasing businesses where rentals and associated administrative charges and fees are typically invoiced to obligors. Where invoices are submitted to large organisations, e.g. local government offices, health authorities etc. there are often administrative delays in payment that are outside the control of the invoicing business and are not reflected of credit risk. The scope of these issues also impacts the factoring business.

Actions taken which are outside the control of the Bank, such as mandatory closure of banking / payment systems, environmental / social impacts e.g. disruption to the banking system as a result of a natural disaster or civil unrest and or action taken by Governments.

If yes, please provide detailed proposals on how to address further possible situations.

It is important that the EBA avoid prescriptive descriptions that preclude a common sense approach to avoid unintended consequences: We urge the EBA to establish minimum guidelines with examples of exceptions that take into account a common-sense approach and the ability to use expert judgment to determine non-credit related events as is the case for the guidelines on sale of credit obligations. It is important that modelling of default remains just so and does not become polluted with purely operational events. Otherwise this will further complicate the segmentation between credit risk an operational risk modelling.

Question 2:

Do you consider the requirements on the treatment of factoring arrangements as appropriate and sufficiently clear?

We think that requirements could be improved

If not, please provide proposals for additional clarifications.

In the factoring arrangements where the ceded receivables are not fully transferred to the factor, the timing for reimbursement/regularization of advances is contractually specified, therefore, the counting of days past due should refer to that date. It does not necessarily require a breach in the percentage agreed between the factor and the client.

The treatment of exposures to debtors stemming from IAS/IFRS compliant purchased trade debts within a factoring agreement with a client (i.e. where the risks and benefits related with the assigned receivables are fully transferred to the factor and the factor has exposures to the debtors of the client) should take into account that the reliability of the due date of the invoices may be affected by numerous events related to the trade relationship between the buyer and its supplier.

In such cases, a significant delay of the payment may occur without any sign of deterioration of the situation of the debtor. Such situations may originate from contractual provisions or also from informal communication and exchange between the buyer and the supplier.

In such situations, we believe that a relief should be introduced by way of a rebuttable presumption on the automatic classification as past due of trade debtors or of a suspension of days past due counting when the factor is aware of these events, regardless the degree of formality. These occurrences shall however trigger an analysis of the debtor's situation in order to assess possible indications of unlikeliness to pay.

In particular, when the buyer disputes a receivable (e.g. receivables not existing at all or just partially existing, commercial supply not regular or different to the agreements, etc.), the amount or even the very existence of the invoice may be challenged. It is very uncommon that disputes are brought to a court. While disputing parties are usually try to settle the dispute outside the court, the process can nevertheless be time-consuming and exceed the 90 days. The opportunistic use of disputes in order to hide financial difficulties could easily be detected through the analysis of the debtor’s situation triggered by the occurrence of the dispute.

In the case of receivables purchased within a factoring agreement in which risks and benefits have been fully transferred to the factor, but the debtor has not been informed of the factor's interest on the purchased debts, the debtor will pay on the client's account (usually a trusted account with a bind in favour of the factor), the client being obliged to transfer as soon as possible the collected amount to the factor. Therefore, it may happen that the payment has been made, correctly and on time, to the client but the latter did not yet transfer the amount to the factor or, again, the factor and his client may have agreement so that the latter transfers the amount for all collected invoices at certain agreed dates rather than one by one. In these cases, a kind of "technical default" may occur regarding the exposures to the debtor and therefore a relief from counting the days past due should be envisaged.

Specific credit risk adjustments (SCRA)

Question 3:

Do you agree with the approach proposed for the treatment of specific credit risk adjustments?

We welcome the clarification made by EBA that the “incurred but not reported losses” (IBNR), which is a current notion of IAS 39 should not be considered as an indication of unlikeliness to pay (§ 26 of the CP)

We consider that such a clarification should encompass the stage 2 of IFRS 9.

We believe the guidelines should reflect clearly that the IFRS 9 stage 2 should not be specifically considered as an indication of default. This is all the more important given that § 178.3 b) of the CRR mentions *“a significant perceived decline in credit quality*” as an indication of unlikeliness to pay that might be misleading and wrongly analogised with the stage 2 of IFRS 9 (“*significant increase in credit risk*”).

We agree the alignment with IFRS stage 3 subject to the following clarification:

The stage 3 of IFRS 9 includes exposures where the credit risk of a financial asset increases to the point that is considered credit impaired. While most of the defaulted exposures would be classified as ‘Stage 3’ under IFRS 9, we believe it should not be assumed automatically.

Fraud accounts which are classed as Stage 3 should not be considered as defaulted as fraud is an Operational Risk.

Sale of the credit obligation

Question 4:

Do you consider the proposed treatment of the sale of credit obligations appropriate for the purpose of identification of default?

We do not agree the proposed approach. Specifically we do not agree with a strict formulaic determination of whether a sale or restructuring determines an economic loss.

We think that the threshold of 5% is an arbitrary threshold. It may be that sales would happen with a discount of more than this percentage change that are not an indication of default. Deciding and thus modelling defaults based upon changes upon on a materiality value sets a precedent that we do not support. It would undoubtedly lead to other unintended consequences.

Where the sale is for credit related reasons it is anticipated that a default would have already been identified ahead of the sale due to other default/impairment conditions. We would propose that the sale of a credit obligation is considered as an indication of unlikeliness to repay in conjunction with other criteria but should not be considered on indicator on a standalone basis

There needs to be some flexibility for banks to determine whether the sale is due to unlikeliness to pay rather than a market perceived decrease in credit quality such that the pricing to risk is out of balance. The EBF makes a good point in it being difficult to separate the influencing factors in the overall discounted value.

We believe banks should be allowed to establish thresholds that take into account factors such as the type of assets to be sold, the economic situation and the absolute level of interest rates and also the treatment of similar assets within a portfolio that share common attributes, and are sold en-masse with a discount but may include non-defaulting assets.

The recent history has proved that when financial markets are highly volatile, some bonds could be under 95% of their par value because the markets anticipate a future decrease of the credit market without the issuer being itself in default. In consequence, the bank may cease granting facilities to the obligor and this could trigger an actual payment default.

Credit obligations could be sold for another reason than the anticipation of a decrease in credit quality of the issuer. A decision to sell participations in loans on performing clients and with a significant loss may be dictated by: regulatory capital savings or deployment of capital, liquidity management, balance sheet management, country risk exposures, imposition of counter-cyclical capital buffers, counterparty exposure management derived from economic capital modelling and or hedging, single limit concentration management.

A sale price of an asset, which is the fair value, will include other elements besides the credit quality such as liquidity premium; general changes to market conditions, etc and it may not always be straightforward to distinguish which part of the economic loss is related to the deterioration in credit quality. We suggest to a set of objective criteria to identify sales of credit obligations not related to credit risk.

We would propose that the sale of credit obligations is considered as an indication for unlikeliness to pay and not as a stand-alone criterion. Finally, we would appreciate a clarification by the EBA on whether securitized credits have to be considered within the “sale of credit obligation” category.

Distressed restructuring

Question 5:

Do you agree that expected cash flows before and after distressed restructuring should be discounted with the customer's original effective interest rate or would you prefer to use the effective interest rate applicable at the moment before signing the restructuring arrangement?

Do you consider the specification of the interest rate used for discounting of cash flows sufficiently clear?

We would advocate the discounting with interest rate that is used as an approximation of the original effective interest rate on a best effort basis.

Considering the 1% threshold for the diminished financial obligation proposed in the QIS, we believe the threshold should be removed. In our view, the relevant measure for recognition of default should be set at a level, when the new cash flow (NPV) would no longer be adequate to cover the value at origination of the obligation, regardless of the decline in NPV.

In addition art 178 (3.d) of CRR considers "material forgiveness,…, of principal, interest or, where relevant fees". The proposed threshold seems not to be consistent with the above mentioned materiality criterion and has therefore to be set at a significantly higher level.

We would also see no need for specifying additional indicators to be considered for identification of default if the net present value of expected cash flows on the distressed restructuring arrangement is higher that the net present value of expected cash flows modifications.

In addition, we believe that the cash flows should be calculated at the level of customer.

Concerning the formula for calculation of the diminished financial obligation (DO), it is not clear whether the cash flows include the expectation of recovery. If they do not take into account recovery expectation, the threshold would not make much sense as the new restructured loan could include a reinforcement of the collateral value which might mitigate (partially or totally) the diminished financial obligation measured with the proposed formula.

Also the formula provides possibility to hide a distressed situation by sufficiently extending maturity and maintaining an equivalent NPV of cash flows. It is also not clear if the two NPV parameters only include the future contractual cash flows or also PD and LGD associated to those cash flows in each moment. In the case of latter, the approach would suffer from a circularity problem. Some restructuring would not be considered as defaulted under the proposed formula for instance when the credit obligation is turned into a PIK loan (payment in kind) with capitalized interest during the period. The proposed formula gives an economic loss of 0.

Concerning paragraph 43, we see it contradictory to the Chapter 5 part D. Paragraph 43 states that "All exposures classified as forborne non-performing …. should be classified as default and subject to distressed restructuring".

Chapter 5 Accompanying Documents part D however states that the preferred option of EBA is a "non-obligatory alignment of the definition of default with the non-performing exposures' given the unintended consequences and high default rate should definition of default be aligned with the non-performing exposures. This would be consistent with EBA answer on 2/10/2015 to a question for "exit criteria NPE" where it is mentioned that "the category of

non-performing exposures can be broader that the category of defaulted or impaired exposures. Defaulted or impaired exposures are mandatorily considered as non-performing but non-performing exposures need not be impaired or defaulted.“

Finally, we would like to underline that the concept of distressed restructuring does not apply in case a revision of the conditions is allowed by the contract (e.g. embedded clauses) or by specific laws (e.g. moratoria issued by banking association/government) or to commercial renegotiations (e.g. change of interest rate for commercial purposes or alignment with current market practices).

Forborne non-performing exposures

IFRS 9 takes forbearance into consideration and calculates the expected loss after modification discounted at the original EIR in line with the proposed approach in the EBA Consultation Paper.

However under IFRS this loss is recognised separately and the book value is adjusted for the “forbearance loss”. Consequently IFRS 9.5.5.12 states that the banks shall assess significant increase in credit risk by comparing the risk of a default occurring at the reporting date (based on the modified contractual terms). For that reason forbearance measures that diminish the cash flows of the contract do not necessarily automatically result in a credit impaired status (default status) under IFRS 9.

Concerning paragraph 43, we see it contradictory to the Chapter 5 part D. Paragraph 43 states that “*All exposures classified as forborne non-performing …. should be classified as default and subject to distressed restructuring*”.

Chapter 5 Accompanying Documents part D however states that the preferred option of EBA is a “non-obligatory alignment of the definition of default with the non-performing exposures’ given the unintended consequences and high default rate should definition of default be aligned with the non-performing exposures. This would be consistent with EBA answer on 2/10/2015 to a question for “exit criteria NPE” where it is mentioned that “the category of non-performing exposures can be broader that the category of defaulted or impaired exposures. Defaulted or impaired exposures are mandatorily considered as non-performing but non-performing exposures need not be impaired or defaulted. “

Other indications of unlikeliness to pay

Question 6:

Do you agree that the purchase or origination of a financial asset at a material discount should be treated as an indication of unlikeliness to pay?

We disagree.

We do not support a definition of default based upon on the price of purchased asset.

The price of an asset ought to reflect its value at that point in time. A material discount may have been applied for reasons other than financial distress e.g. market conditions, negotiations etc. Linking default to the price of purchased (sold) assets could be a disincentive for banks to purchase / sell assets at a discount especially where the purchaser has other exposure to the same obligor that would need to be defaulted as a result. This approach could have a negative effect on the role of banks as intermediaries and impact business models (originate and hold vs, originate to distribute vs. buy to hold)

Default should be triggered for reasons that are directly linked to the credit risk of the counterparty and should be identified from the due diligence undertaken and in this respect symmetry with sale of assets (Q4). Price paid may form part of the indication of unlikeliness to repay but should not be considered as a standalone indicator.

Other considerations

We think that para 47 f) and h) are problematic because retail exposures are viewed at a facility level. There is no cross-division (commercial–retail), nor cross-retail view available to create defaults as proposed.

Regarding Para 50 we think it would be helpful to clarify that non-credit related fraud should be treated as operational risk. We disagree that a credit fraud should be considered as an additional indication of unlikeliness to pay.

7. Criteria for the return to a non-defaulted status
Minimum conditions for reclassification to a non-defaulted status
Question 7:

What probation periods before the return from default to non-defaulted status would you consider appropriate for different exposure classes and for distressed restructuring and all other indications of default?

We believe the institutions are best placed to recognize when a customer is no longer in default and we consider the set probation periods inappropriate. The institutions should determine the probation period in a way that that minimizes the 're-defaults" of the clients.

Any probation period from default to non-default status is inconsistent with what is set out in Article 178(5) where it is stated that: *"If the institution considers that a previously defaulted exposure is such that no trigger of default continues to apply, the institution shall rate the obligor or facility as they would for a non-defaulted exposure".*

Also, under IFRS 9 favourable changes in credit risk should be recognised symmetrically with unfavourable changes in credit risk (IFRS 9 BC 5.210). By applying a probation period, financial instruments would move into default quicker than back to non-defaulted status. This can result in exposure being classified as defaulted but not credit impaired under IFRS 9 (bucket 2 exposures) or the exposure would be classified as defaulted and credit impaired (in bucket 3) but with no loan loss allowance which is contra intuitive.

The suggested 3 months' probation period is considered too long in relation to both large corporate exposures and retail consumers in particular when applied together with the strict definition of the technical default as proposed in the CP. In case of retail customers, payments are not always fully automatized by systematic debit of the customer's account. Also, in some countries, loans with an undefined maturity are common for SMEs portfolios. Delays in payments of large corporates may be caused by systems or data errors. Such defaults would not necessarily mean a deterioration in the credit quality of the borrower especially if the cure period is short (less than 30 days). We would suggest that in such cases, customers being classified as defaulted could return to non-default status as soon as the obligation is paid in. The three months period should therefore be eliminated as mandatory provision at least for default trigged by past due.

In case of distressed restructuring, we believe it is the assessment and expert judgement of remaining unlikeness to pay, that ought to be the determining criteria for a decision to return the exposure to non-defaulted status, not a minimum period of time. However, if the proposed cure period for distressed restructuring will be maintained in the final draft of the Guidelines, having regard to Article 59 of the Consultation Paper, it is opportune to specify which repayment suspensions shall be considered as a "grace period". In particular, if a restructuring arrangement provides a temporary suspension of the sole interest share of the loan, it is not clear if that suspension shall be treated as a grace period, considering that the principal share of the loan will not be suspended.

Similarly, should a defaulted client of a bank be bought by another client of the bank (client B) that is not in default, the exposures of the client B should not be considered defaulted if there is no decrease in the credit quality of client B (due to the acquisition). The remaining unlikeliness to pay should be the decisive criteria. Depending on the portfolio specific characteristics, there might be different or no probation periods.

Finally, we believe the following should be added at the end of paragraph 60a): *…"or the debtor has otherwise demonstrated its ability to comply with the post forbearance conditions".*

9. Application of the definition of default for retail exposures

Level of application of the default definition for retail exposures

Question 8:

Do you agree with the proposed approach as regards the level of application of the definition of default for retail exposures?

We support the proposal that the credit institution may decide when to apply the default definition at obligor level and/or facility level.

We note that EBA has set out the contagion effect as an example.

We do not support the suggestion that banks may adopt a rule that the default of a mortgage loan results in default of all other exposures to the obligor.

We do not agree that the contagion rules should apply where exposures are managed separately across divisions and or legal entities. In such circumstances exposures will be managed by separate policies, processes, systems and credit approval areas.

We think that the data should be allowed to speak for itself. A mortgage default might result in a higher probability of default on other products but not necessarily a default.

Application of the definition of default for retail exposures at the facility level

Question 9:

Do you consider that where the obligor is defaulted on a significant part of its exposures this indicates the unlikeliness to pay of the remaining credit obligations of this obligor?

We do not agree that where the obligor is defaulted on a significant part of its exposures this necessarily indicates unlikeliness to pay on the remaining credit obligations of this obligor.

In some jurisdictions the application of the default definitions at facility level for retail obligors is a legal requirement.

We think that the data should be allowed to speak for itself. If it is demonstrated that defaults on other exposures are a risk driver then this should be included within the assessment of PD. Thus for example a mortgage default might result in a higher Probability of Default on other products but not necessarily a default. This assessment should be performed on a portfolio by portfolio basis.

There are banks that use a facility not obligor view of default in retail, they do not have a cross bank view to allow for the pulling effect as set out in 3.7.2.

It is also important to recognise forbearance is often considered a default event but is designed to help customers. Establishing a policy that any customer who is in mortgage forbearance would be deemed to have defaulted on their other products would negate the aim of the forbearance programme.

Application of the definition of default for retail exposures at the obligor level

Question 10:

Do you agree with the approach proposed for the application of materiality threshold to joint credit obligations?

We do not agree as it is not possible to apply contagion across commercial and retail exposures.

We suggest assessment/judgement of each institution on a case by case basis.

If a joint obligation towards an institution defaults, the individuals taking part in the joint obligations (and their individual obligations, respectively) should not be automatically considered as defaulted. This mechanism is even more problematic when applied to joint obligations consisting of a large number of individuals in which case considering all the individuals involved in the joint obligation automatically as defaulted may not be economically justified at all.

We propose that analysis of joint obligations should be performed to ascertain whether default on a joint exposure is a risk indicator for an individuals' exposure. If it is then this should be included within the assessment of PD.

Internal governance requirements for banks applying the IRB Approach

Question 11:

Do you agree with the requirements on internal governance for banks that use the IRB Approach?

The requirements seem to be in line with CRD IV.

It should be ensured however that there is also an alignment with the final Basel Committee Guidelines on credit risk management processed to be applied in accounting for expected credit losses.

End