



The voice of banking  
& financial services

15 March 2011

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Dear Sirs,

#### CEBS draft guidelines on AMA changes (CP 45)

The British Bankers' Association ("BBA") is the leading association for UK banking and financial services for the UK banking and financial services sector, speaking for over 230 banking members from 60 countries on the full range of the UK and international banking issues. I am pleased to say that 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.

The BBA is pleased to respond to the consultation on the draft guidance on AMA changes.

#### Comments

The BBA supports the principal objective of CP 45 to clarify banks' approval processes for AMA changes and the necessary communication with and, where appropriate, approval by bank regulators.

We have concerns regarding two principal areas of the consultation paper:

- i. Home-host issues – specifically not fully taking into account the circumstance where an EU bank which has a non-EU parent has an approved AMA model; and
- ii. Overly complex categorisation of types of AMA changes and (as currently defined) the requirement to have too many types of changes pre-approved/communicated in advance.

The Annex to our letter contains our formal response to the principles and guidelines proposed in the consultation, and further specific observations and questions arising from the proposals.

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We hope that you will find our comments useful. Please contact me by way of email ([irving.henry@bba.org.uk](mailto:irving.henry@bba.org.uk)) or telephone on (0) 20 7216 8862 should you require further information.

Yours faithfully,



Irving Henry  
Director, Prudential Capital and Risk

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## Annex

Colleges of supervisors/home-host issues

We are concerned that the consultation does not sufficiently take into account the well-established principles regarding home-host co-operation and information sharing amongst supervisors with respect to the approval and ongoing assessment of AMA methodologies. In particular we do not believe that the consultation adequately takes into account the practicalities of an AMA approval by a host regulator, particularly where the home regulator is not based in the EU.

The key element of home-host co-operation is information sharing to facilitate timely and effective implementation of AMA rollouts and supervisory assessment of AMA models. The home-host principles specifically anticipate the attribution of group operational risk capital to legal entities by means of approved allocation mechanisms. In such circumstances legal entities in a host jurisdiction are likely to follow group wide operational risk policies and procedures, including those specifically relating to AMA capital calculations. In such circumstances it will be impractical for subsidiary legal entities to seek pre-approval of changes that have already made in a group wide context, particularly where the home regulator is based outside the EU. Specifically, the requirement to seek pre-approval of "major changes" and "fundamental changes in the organisational and operational structure of the operational risk management function" (classified as a "significant change") cannot always be pre-advised to a host country regulator. For these changes we would recommend that they be discussed and agreed with the host country regulator on a timely basis, but not necessarily in advance of any such change.

Although paragraph 4 makes a passing reference to Article 129 Paragraph 2 of Directive 2006/48/EC regarding the home-host principle, we feel that the guidelines would benefit from expanding on the topic to enable the reader to know that Article 129 Paragraph 2 deals with home-host, to include situations where either the parent or subsidiary is an EU institution. Further, the Guidelines should acknowledge that although host affected legal vehicles have an obligation to pre-notify the host regulator of material AMA changes, host regulators have a similar responsibility to coordinate closely with and to resolve any issues with the home regulator as necessary. Accordingly, we would suggest the following amendments:

Paragraph 4: Extensions and some changes to the AMA can have a considerable impact on the quality and reliability of the AMA and the institution's capital requirements at group and solo level; it is therefore necessary to involve the competent authority prior to their implementation. If requests to extend or significantly change the AMA are submitted by an EU parent credit institution or jointly by the subsidiaries of an EU parent financial holding company, or by EU subsidiaries of a non-EU parent credit institution or financial holding company, competent authorities will follow the procedures envisaged by Article 129 Paragraph 2 of Directive 2006/48/EC.

AMA change policy (ACP)

Paragraph 13 details four categories. It should be left to firms to define their policy. The differences between material and other changes should be handled with common sense, rather than prescribed in detail. Further, only changes in policy, as opposed to procedural matters, should be consulted on with regulators.

The four categories of AMA changes proposed are overly complex and we suggest that these are simplified as follows:

- i. Material changes (comprising both extensions to the AMA framework and other significant AMA changes); these would require formal approval before implementation, as set out in paragraphs 19 to 22.

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- ii. Other changes that require notification on a timely basis, taking into account the materiality of the impact of the changes; notification pre-implementation and approval is not required.

Accordingly, we would suggest the following amendments:

13. The ACP should use the following **categorisation scheme**, defined in more detail in the annex to these Guidelines, ~~as to the first three categories:~~

- a) ~~Material~~ changes (comprising Extensions and Significant changes)
- b) Other ~~Significant~~ changes
- ~~c) Major changes~~
- ~~d) Minor changes~~

3.2, paragraph 23, supervisory procedures for other changes

An institution should inform its competent authority in good time, where practicable prior to the planned implementation, of other changes to its AMA (see also Annex item C). Moreover, it should produce the necessary documentation, including the outline of the change, its rationale, objective and the effects on the AMA regulatory capital.

Delete 3.3, paragraphs 24 – 27.

Annex C, major changes to the AMA

The annex should specify that it relates primarily to material changes to AMA policy / methodology. The term “methodology” better reflects the underlying principles of internal loss data collection; procedures normally relate to internal activities that may change frequently without impacting the principles of loss data collection. Notifying the regulator of procedural changes would likely cause a significant administrative burden, while providing little insight into bank policies.

Guidance on what constitutes a relevant alteration to operational risk capital would be helpful.

Accordingly, we would suggest the text in the Annex be replaced with the following:

1. This Annex provides for material changes (comprising extensions and significant changes) - a non-exhaustive list of examples. This list acts as a guide to grading changes according to their severity.
2. The ACP should encompass the categories outlined in paragraph 13. The examples in those categories should be integrated in the internal ACP if feasible. The institution may add further detail in the ACP consistent with the characteristics of the institution’s internal governance and AMA framework.

#### Material changes:

##### a) *Extensions to the AMA framework*

- Extensions to the *scope of application* of the AMA
  - Extension to parts of the institution not yet covered by the approval, if not contained in the roll-out plan submitted with the application for the use of the AMA; and
  - Variation of a hitherto applied Partial Use relating to individual locations, legal units or business units, if not contained in the implementation plan submitted with the application for the use of the AMA.
- Extensions to the *measurement system*

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- First-time reduction of the AMA regulatory capital by the expected loss offset;
- First-time introduction of operational risk mitigation techniques (e.g. insurance or other risk transfer mechanisms);
- First-time introduction of diversification benefits; and
- First-time introduction of an allocation mechanism at group level.

*b) Significant changes in the AMA*

- Fundamental changes in the structure and characteristics of the calculation data set (e.g. first-time use of new external data sources, switch from incorporated external data sources);
- Fundamental changes in the measurement system due to modification in the logics or methods (e.g. a switch from essentially data-related approaches to mainly scenario-based models or vice versa, changes in the criteria for the use or weighting of the four elements and changes in the distributional assumptions/parameter estimation procedure), or to important modifications within the group structure (e.g. abandonment of significant business units, including subsidiaries);
- Fundamental changes in the logics and drivers of the allocation mechanism; and
- Changes that cause a material alteration to the operational risk capital charge.

**Other changes:**

- Changes to the institution's internal policy for collecting internal loss data, performing scenario analysis and determining business environment and internal control factors;
- Changes to the measurement system due to modification in the logics or methods, or to important changes in the group structure;
- Significant changes to IT systems for the AMA framework, data administration or reporting procedures;
- Changes to the institution's processes for internally validating and reviewing the AMA framework; and
- Significant changes in the organisational and operational structure of the operational risk management function.

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