APPENDIX

Q1. Do you agree that building definitions of forbearance and non-performing by taking into consideration existing credit risk related concepts enables to mitigate the implementation costs? If not, please state why.

We agree that such an approach would help mitigate implementation costs. However, the proposed definitions extend far beyond existing credit risk related concepts, which are already embedded within capital and financial disclosure standards and practices, and thus the proposed definitions will not be effective in mitigating implementation costs. In particular:

- The proposed definition encompasses trading portfolios for which, given their nature, there is no established framework for capturing forbearance/non-performing information as they are not managed within a traditional banking book credit process (under IFRS the risk of default and credit quality is incorporated into the fair value). Specifically, credit risk for trading portfolios is not managed using transaction level credit assessment which is a fundamental feature of the approval of banking book exposures. In contrast, trading exposures are preapproved in central matrices allowing trading desks to buy and sell without seeking specific approval of each exposure. The individual assessment that is required to determine forbearance and non performing status is therefore not undertaken through established credit processes and these would need to be introduced solely for the purpose of FINREP reporting. We therefore recommend that the scope of CP06 is limited to loans and advances to customers and banks measured at amortised cost. Such an approach will create consistency with existing financial reporting and risk management techniques, as well as mitigating the cost of implementation.

- Regulators have taken care to ensure that the definition of forbearance required for capital purposes relates closely to the definition required for financial disclosures. However, the proposed definition is significantly different from existing definitions in the following ways:

    - The introduction of a 30 days past due non-performance test within a three month window when assessing forbearance.
    - The introduction of a cure period to reflect situations other than repayment or write-off of the renegotiated loan or its return to the original terms of the loan.
    - The introduction of the concept of forborn cures.

    The effect of the detailed rules proposed is to introduce an alternate definition of forbearance to those already used. This will require the creation and application of credit risk assessment processes that are in addition to existing processes in order to determine, capture, store and present the required information

- Similarly, the industry and regulators have sought to align the definition of impairment and default for financial reporting and capital purposes. Whilst the definition of non performing is broadly aligned to the CRR definition we strongly believe that leveraging these definitions, howsoever they are applied in each member state, should be encouraged rather than imposing the proposed FINREP definition. For example, not all exposures are necessarily subject to the 90 days past due definition and requiring these to be assessed as non performing (when for capital purposes they are treated as non performing) will require parallel data capture processes and reporting structures to be introduced to meet capital, financial reporting and FINREP requirements. In addition, the proposals propose introducing a de facto materiality test described as the ‘pulling effect’. Firms currently assess this threshold based on their own internal policies for managing customers in default under the CRR.

In summary, we have significant concerns about the proposed creation of another set of (complex and prescriptive) definitions (and associated rules) over and above the existing definitions applied for financial disclosure, impairment and capital/regulatory reporting purposes. This will create significant implementation and ongoing costs - and could also result in confusion among investors and others who may not understand the differences in definitions. We encourage the EBA to work with others to arrive at a single definition, preferably in accordance with the existing accounting and regulatory rules.

Q2. Do you agree with the proposed definitions? Especially, do you agree with the inclusion of trading book exposures under the scope of the non-performing and forbearance definitions? If you believe alternative definitions could lead to similar results in terms of identification and assessment of asset quality issues, please explain them.

We do not agree with the proposed definitions. We are concerned about scope (i.e. application to trading book exposures), and the complex and prescriptive definitions of both forbearance and non-performance. Our detailed views are set out in our response to question 1.

We have the following detailed comments in respect of the other components of the proposed definitions:

- We believe the inclusion of a 30 day past due assessment category is unnecessary to determine forbearance. Further detail is given in our response to question 5.
- The concept of forborne cures does not exist in credit risk management techniques and systems. We believe loans which have been renegotiated should retain this designation until maturity or derecognition to help firms understand whether such assets carry additional risks over and above loans which have never been renegotiated.
- The definition proposes to group all of a counterparty's products/positions together and class them as non-performing when specified thresholds are exceeded (e.g. when a debtor has exposures past due more than 90 days representing 20% of all its exposures, all on and off balance sheet exposures to this debtor shall be considered as non-performing). In addition to the thresholds being arbitrary, the grouping of products/positions is not consistent with current credit risk management techniques, especially in respect of retail exposures. We recommend that the arbitrary thresholds are removed.
- The definition of off balance sheet positions is discussed further in question 7.

Q3. How long will it take you to implement, and collect data on, the definitions of forbearance and non-performing?

A project of this size takes at least 18 to 24 months to implement from the point the rules are finalised. A requirement to implement in a shorter time-frame is likely to undermine data quality and result in significant risk to the quality of delivery. Reliance on proxy categorisations derived from existing capital and reporting treatments is very likely to be required for an extended period of time while supportive credit assessment processes are developed and implemented.

Q4. What definitions of forbearance and non-performing are you currently using respectively for accounting and prudential purposes?

In current reporting the term forbearance is synonymous with renegotiated loans, and 'non-performing' is not used. For the purposes of this question we outline below our existing definitions for renegotiated loans and impaired loans.

<u>Accounting</u>

Renegotiated loans – Loans for which the contractual terms have been changed because of significant concerns about the borrower's ability to meet the contractual payments when due.

Impaired loans – Loans where the Group does not expect to collect all the contractual cash flows or expects to collect them later than they are contractually due.

Impaired loans and advances are those that meet any of the following criteria:

- loans and advances classified as defaulted for internal risk and capital purposes (i.e. bearing default grades of CRR 9, CRR 10, EL 9 or EL 10, outlined on page 253 of our 2012 Annual Report and Accounts);
- retail exposures (EL1 to EL8) 90 days or more past due, unless individually they have been assessed as not impaired; or
- renegotiated loans and advances that have been subject to a change in contractual cash flows as a result of a concession which the lender would not otherwise consider, and where it is probable that without the concession the borrower would be unable to meet its contractual payment obligations in full, unless the concession is insignificant and there are no other indicators of impairment. Renegotiated loans remain classified as impaired until there is sufficient evidence to demonstrate a significant reduction in the risk of non-payment of future cash flows, and there are no other indicators of impairment.

<u>Prudential</u>

A *default* will be deemed to have occurred on a retail account in either of the following two circumstances:

- The bank considers that the obligor is unlikely to pay their credit obligations in full, without recourse by the bank to actions such as realising security; or
- The obligor is past due by more than 180 days in the case of a facility to an individual or 90 days in the case of an SME, as defined in the respective jurisdiction.

Businesses may adopt a period shorter than 180 days past due for individual obligations if either:

a) required to do so by local regulators; or

b) a shorter outcome period is in line with local business practice and policy.

Indications of likelihood not to pay must include the following events:

- the bank makes a charge-off (including partial) or raises an individual impairment allowance;
- the bank sells the obligation at a material credit-related loss;
- the bank consents to a ‘distressed' restructuring;
- the obligor has been placed in bankruptcy or similar protection;
- the security guaranteeing a facility is repossessed;
- the obligation has been put onto non-accrual status;
- a judgmental decision is taken that the obligor is unlikely to pay the obligation in full.

Additional local default trigger events may be included in local policies.

A *corporate*[1] *default* is considered to have occurred with regard to a particular obligor when either or both of the following events have taken place:

- The bank considers that the obligor is unlikely to pay its credit obligations to the Group in full or on originally agreed repayment terms, without recourse by the bank to actions such as realising security (if held).
- The obligor is past due more than 90 days on any material credit obligation to the Group. In the case of revolving facilities and instalment loans, this means 90 days past repayment date. In the case of overdrafts, it means 90 consecutive days over agreed limit.

Indications of *unlikeliness to pay* include:

a) The bank makes a charge-off or raises an impairment allowance based on a significant perceived decline in credit quality.

b) The bank sells the credit obligation at a material economic loss.

c) The bank consents to a distressed restructuring of the credit obligation which results in a diminished financial obligation caused by the material forgiveness, or postponement of principal, interest or (where relevant) fees. Further detailed guidance is given to users around the conditions necessary for a distressed restructuring to have occurred.

d) The bank (or another creditor) has filed for the obligor's bankruptcy (or similar order) so affecting the obligor's credit obligation to the Group.

e) The obligor has sought or has been placed in bankruptcy or similar protection where this would avoid or delay repayment of the credit obligation to the Group.

f) Sustained or continuing deterioration in the financial condition or outlook of the borrower to the extent that capacity or willingness to repay is considered doubtful.

Q5. Do you agree with the types of forbearance measures covered by the forbearance definition? In not, what other measure(s) would you like to be considered as forbearance?

The types of forbearance measures provided in principle appear to be reasonable interpretations of the forbearance definition. The focus on payment related concessions is clear and appropriate. We would not agree with the inclusion of non-payment covenant concessions, although not stated in the definition, could be inferred based on examples provided; we have described these below.

In our view all loans for which the contractual terms have been changed because of significant concerns about the borrower’s ability to meet the contractual payments when due (that is, due to financial difficulty) should be classified as forborne loans. We suggest that this should apply even where the loan has never been past due. However, we do not agree that all loans that have been more than 30 days past due can be assumed to have been modified as a result of financial difficulty, and therefore we do not agree with the creation of the 30 day past due

[1] Also applies to financial institutions and central banks and governments.

backstop. Examples of situations in which a loan might have been more than 30 days past due, but not a credit related concession, include:

- A customer misses a mortgage payment due to administrative errors, for example a direct debit payment not being transferred correctly following a change in the customer's current account supplier.
- Short-term trade facilities past due for technical reasons such as delays in documentation, for which the facility has consequently been renegotiated, but where there is no concern over the creditworthiness of the counterparty.

It is key to the current definition of forbearance and default caused by distressed restructurings that the credit distress necessary should be such that, without the concession granted, it is highly likely that the obligor will go on to experience default by exhibiting other indicators of unlikeliness to pay, or to go 90 days past due (180 for some retail products). For individually assessed exposures, a case which is between 30 and 90 days past due may indeed be judged unlikely to pay but it is important that this be subject to fundamental credit assessment to avoid capturing cases like a) and b) above. Setting the threshold at 30 days mechanistically will not necessarily be aligned to the credit deterioration necessary to meet the financial reporting or capital treatments.

We note that the term "notwithstanding" in the introduction to the examples implies that the examples would qualify as forborne loans even if the forbearance definition was not met. We suggest replacing this with the words "For the purposes of applying the first paragraph of the definition…". This is because, in our view, the examples should provide guidance on the application of the definition, rather than those examples being an extension of the definition.

The fourth example states: "the modification made to a contract implies a total or partial cancellation by write-offs of the debt…". This criteria would not always result in forbearance. For example, in the situation where a financial institution grants a concession to a customer in order to retain the customer's business rather than as a credit related concession (such as a reduction in an interest rate charged to a customer to a rate that reflects current competitor rates), a strict reading of the proposed rules would require this to be classified as forbearance (notwithstanding the forbearance definition), despite the fact that the concession is not credit related. Some element of credit distress is necessary to trigger both financial reporting and prudential treatments, and this should be clear in the proposed definitions and examples.

Taking the above points into account, and in response to the question about other measures that we would like to be considered as forbearance, we refer to our disclosure on "Identifying renegotiated loans" on page 254 of our 2012 Annual Report and Accounts that provides situations that would be regarded as indicators of "financial difficulties".

Where these indicators are present and the terms of the loan are modified, then the modification qualifies as forbearance unless there is other evidence to demonstrate that the concession was granted for a reason other than for credit purposes:

- A modified contract includes more favourable payment terms than those that the debtor could have obtained in the market;
- The customer is currently in default on any of its debt;
- The debtor has declared or is in the process of declaring bankruptcy or entering into a similar process;
- There is significant doubt as to whether the debtor will continue as a going concern;
- Currently, the debtor has securities that have been delisted, are in the process of being delisted, or are under threat of being delisted from an exchange as a result of trading or financial difficulties;
- Based on estimates and projections that only encompass the current business capabilities, the financial institution forecasts that the debtor's entity-specific cash flows will be insufficient to service the debt (both interest and principal) in accordance with the contractual terms of the existing agreement through maturity. Thus actual payment default may not yet have occurred; and
- Absent the modification, the debtor cannot obtain funds from sources other than the existing creditors at an effective interest rate equal to the current market interest rate for similar debt for a non-distressed debtor.

Q6. Do you agree with the following elements of the forbearance definition:
a) the criteria used to distinguish between forbearance and commercial renegotiation?
b) the criteria used to quantify refinancing as forbearance measures?
c) a 30 days past-due threshold met at least once in the three months prior to modification or refinancing, as a safety net criterion to always consider modification or refinancing as forbearance measures?
d) the proposed treatment for exposure with embedded forbearance causes?
In case you disagree with the EBA proposals on the above-mentioned issues, please explain and provide an alternative to them.

We do not agree with the criteria in a) and b), as they are applied using mechanistic rules which do not take into account the facts and circumstances relevant to specific loans. In our view, the distinction between forbearance and commercial renegotiation should be principles-based. For example, in our response to question five we provide the circumstance of a concession by way of a reduction in interest rate which is granted in order to retain a customer. As currently drafted, such a concession would be captured by the first bullet in the list of safety net requirements. We also do not agree with the 30 day criteria included in the safety net, and have provided examples of where this would not apply in our response to question five.

We do not agree with the safety net criteria in c). Please see our response to question 5.

We do not agree that the instance of a debtor exercising its current right under the terms of a contract that is not modified should be classified as forbearance in d). To do so would not be consistent with the definition of forbearance in that it is critical to forbearance that there should be an explicit agreement to withhold contractual enforcement and to amend the terms of the contractual relationship. It is clear that in building such clauses into the contract to begin with a credit deterioration of the magnitude envisaged is clearly being established as acceptable in advance, and that in effect no concession is being granted. It is key to the definition of forbearance that the degree of distress requires a customer to seek relief in part from their contractual obligations. Where these are agreed in advance there is no deviation from the contractual norm. We also object to the reference to 30 days past due as being overly mechanistic and not necessarily aligned to risk severity as noted above. Aside from technical objections we also would not wish to disincentivise the setting up of contracts which very sensibly anticipate the management of the relationship under circumstances where the customer anticipates having to manage their cash flow responsibly and is able to do so without fearing that its relationship with the bank would prejudiced. Such terms, where offered, are valued by customers and are regarded as examples of responsible lending. Furthermore, it would require unduly costly manual processes to firstly identify at what point such a right would qualify as forbearance, and secondly, to monitor this distinction on a consistent basis. In our view, to clearly distinguish forbearance as the modification of existing contractual terms creates a clearly understandable approach which is operationally achievable.

If it is determined that this requirement will remain, then we recommend a clarification that the modification should very clearly “due to the financial difficulty of the debtor”, and that the standard for judging this be in line with determining the severity of credit distress necessary for an unplanned modification.

Q7. Do you agree with the proposed scope of on- and off-balance sheet exposures to be covered by the definition of forbearance?

We do not agree with the scope of exposures to be covered by the definition of forbearance. Our views in respect of the application to on balance sheet trading book exposures are set out in question 1. In respect of off balance sheet commitments, the scope should be aligned to the general forbearance definition therefore excluding loan commitments that are modified for commercial reasons. In addition, it would be more meaningful to limit the scope to irrevocable loan commitments.

Q8. Do you agree not all forbearance transactions should be considered as defaulted or impaired?

Yes. There are occasions where a forbearance transaction would not require an impairment or be considered as defaulted. See the response to question 9 for details.

Q9. What types of forbearance transactions are likely, according to you, not to lead to the recognition of default or impairment?

The following situations would be considered to be forbearance, but would not be classified as impaired or lead to the recognition of default:

- Previously impaired renegotiated loans that have demonstrated satisfactory performance over a period of time or have been assessed based on all available evidence as having no remaining indicators of impairment.
- A contract where the negotiation was on market terms, such that the increase in interest compensates for the reduction in cashflows, and results ultimately in the present value of the contract being the same or larger. We would expect that this scenario would occur only in rare circumstances.
- Where a concession granted is deemed insignificant and there are no other indicators of impairment. Substantially all the renegotiated loans that meet this definition are first time re-ages that are less than 60 days past due at the time of re-age, with no other indicators of impairment.

Q10. Do you agree with the proposed definitions of debtors and lenders and the scope of application of the forbearance definition (i.e. accounting scope of consolidation)?

We do not wholly agree with the definition of debtor as stated. To avoid unnecessary complexity, we believe the scope of recognition should be limited to the legal entities which are seeking relief through contractual renegotiation.

For prudential capital purposes firms commonly adopt rating frameworks which recognise the extent of accounting group interdependence. Where these frameworks would lead to a default to be applied to an accounting group member, such group rating frameworks will normally determine whether other group members should also be regarded as in default. Where such a 'cross-default' arises, unlikeliness to pay will be considered for such connected group members in determining whether impairment has occurred.

We acknowledge the point regarding use of funds to provide relief elsewhere in the accounting group. However the above rating approach will in most instances act to ensure that a holistic view of impairment and default is taken. Where the rating structure is such that there is sufficient credit independence between entities, we do not agree that lending to a healthy group member to refinance a less healthy group member should be treated as an instance of forbearance across both. Such reorganisations are best seen as financing a non-distressed customer so that they can rescue a distressed group relative. On the one hand the distressed obligor is enabled to meet their contractual terms and on the other the non-distressed obligor is unlikely to have met the test of credit distress severity that would qualify any concession made to it as forbearance. Looking through such relationships is likely to be very difficult in practice and we question the extent to which this occurs in practice and whether it warrants the concern expressed.

We agree with the definition of lender for the purposes of reporting although we do not understand the example provided at the top of page 20 ("For instance, in the case of…"). Please can you provide an example of how you intend this to work.

In respect of the accounting scope of consolidation, we note that this approach would be inconsistent with the other FINREP requirements which are based on a regulatory scope of consolidation. We have previously commented that using a regulatory rather than accounting scope of consolidation will cause significant implementation issues and result in differences between published financial information and FINREP. We strongly support an accounting scope of consolidation (based on IFRSs) and encourage the EBA to apply this basis to the broader FINREP requirements. If this is not possible it is unclear how the FINREP requirements will interact with CP06 from a reporting and data perspective and we believe further consultation will be necessary.

Q11. Do you agree with the proposed mixed approach (debtor and transaction approaches) for forbearance classification?

We agree that a mixed approach is required, and that forbearance measures should only be applied to specific restructured contracts.

Q12. Do you agree with the exit criteria for the forbearance classification? In particular:
a) what would be your policy to assess whether the debtor has repaid more than an insignificant amount of principal or interests?
b) do you support having a probation period mechanism?

We do not agree with the concept that exposures are able to exit forborne status. Exit from forbearance should only be recognised where the facility is repaid, written off or if the facility recovers to meet the original terms. This will ensure that regulators have a high degree of confidence that the relative riskiness of a forborne loan versus one not forborne is not disguised over time.

Q13. Do you agree with the proposed approach regarding the inclusion of forborne exposures within the non-performing category? In particular:
a) do you agree the generic non-performing criteria allow for proper identification for neither defaulted nor impaired non-performing forborne exposures? Would you prefer to have the stricter approach (all forborne exposures identified as non-performing) implemented instead?
We agree the EBA's preferred approach and that a forborne exposure should be considered as non-performing only to the extent it meets the non-performing criteria. As the industry has aligned impairment and forbearance definitions we agree that at the point of recognition of a distressed restructuring the severity of credit distress necessary is sufficient to also act as a loss event for impairment purposes and will in most cases result in impairment assessment.

b) do you agree with the proposed consequences of forbearance measures extended to an already non-performing exposure? Especially, are the proposed exit criteria strict enough to prevent any misuse of forbearance measures or would stricter criteria be needed?

Please refer to our response to question 22.

Q14. Do you agree with the following elements of the non-performing exposures definition:
a) the use of 90 days past-due threshold to identify exposures as non-performing?
b) the proposed guidance for past-due amounts?
c) the proposed treatment of collateral and especially the proposed valuation methodology for its reporting?
In case you disagree with the EBA proposals on the above mentioned issues, please explain and provide an alternative to them.

a)
We would prefer that default should continue to act as a trigger for impairment consistent with financial disclosure principles and that the days past due threshold for these purposes be used consistently in the context of FINREP reporting. 90 days past due is appropriate and well aligned to risk recognition of credit distress for wholesale exposures, but the same may not be true for retail.

b)
We disagree with the guidance around defining what constitutes past-due. The guidance refers to a period of 90 days where there has been any amount(s) outstanding for that period would be considered to be non-performing. Operationally, we allocate payments on a FIFO basis (to the oldest past-due amounts), thereby our interpretation of days past due is the period of time where the outstanding balance has not been paid, rather than a period of time where there have not been full payments (which is akin to the use of a LIFO method). Whilst we understand the prudent reasoning for such a view (i.e. that the contract has not been up-to-date with their payments for a period of time), this is operationally ineffective, as it provides no incentive for the customer to pay anything in this period, as it would not improve their magnitude of default. The severity and difficulty of introducing a days past count for FINREP which differs from prudential criteria should not be underestimated in terms of the scope of system changes required. From experience in managing the introduction of Basel 2 a days past count mechanism is likely to take at least two years to introduce and operationalise – with a similar scale of cost. We are not aware that days past counting is being challenged in a prudential context and would strongly recommend that consistency with existing prudential mechanisms for FINREP be followed to avoid duplicative and competing views of risk within firms. The cost of introducing such uniformity should be explored carefully against any analytical benefit to be derived. It is our recommendation that firms be required to indicate which measure is used in their reporting.

c)
We are in agreement of the proposed treatment of collateral in relation to the classification of the contract. However, we disagree with the proposed valuation methodology, as explained below. By reference to the definition of non-performing loans, a contract may be classified as such where the “exposures present a risk of not being paid back in full without collateral realisation”. Whilst we understand that the aim is to focus on the recovery of the contractual cashflows, rather than the realisation of the collateral, both should be considered, when valuing the contract.

When we no longer expect to recover the principal and interest due on a loan in full or in accordance with the original terms and conditions, it is assessed for impairment. If exposures are secured, the current net realisable value of the collateral will be taken into account when assessing the need for an impairment allowance. No impairment allowance is recognised in cases where all amounts due are expected to be settled in full on realisation of the security, however the loan is still reported as impaired.

To this end, we disagree with the statement that “in practice collateral is not used in the assessment of non-performing exposures in the banking book”.

Q15. Do you agree with the coverage of the proposed definition and with the application of the generic non-performing criteria to all fair-valued non-performing exposures? Do you expect challenges when implementing them and collecting data on fair-valued non-performing exposures? Would you suggest other criteria instead?

We disagree with the proposed application of the non performing definition to exposures measured at fair value as outlined in our response to question 1. The application of the non-performing definition to fair-valued exposures would require significant transformation of risk processes in order to undertake the necessary judgemental assessments. This introduces unnecessary risk process change which is not aligned to the scale and speed with which such business are required to operate, introduces permanent variable cost and would not deliver any clear benefits. We strongly urge careful reconsideration of scope in this regard.

Q16. Do you agree with the proposed treatment for derivatives exposures? If not, what criteria would you suggest to enable identification of non-performing derivatives?

We agree derivative exposures should be excluded from the definition.

Q17. Do you agree with the proposed criteria to identify off-balance sheet exposures as non-performing?

We believe the guidance in respect of the application of non-performing assessment to off balance sheet exposures needs to be expanded. In saying that, consistent with our response to question 7, we believe it would be more meaningful to limit the scope to irrevocable loan commitments.

Q18. Do you agree not to consider exposures subject to incurred but not reported losses as non-performing?

We agree with this point. The IBNR losses are recognised in relation to exposures that are classified as performing as there has been no individual indication of a loss event that has an impact on the estimated future cash flows that has come to our attention, but for which historical experience indicates that for some (although undeterminable) exposures such a loss event will have occurred.

Q19. Do you agree with the proposed approach regarding the materiality threshold?

We agree although we would note that a threshold for forbearance has actually been proposed on page 13 and we are therefore not certain how that text relates to this section.

Q20. Do you agree with the proposed definitions of debtors and lenders and the application of the non-performing exposures definition on an accounting scope of consolidation?

In respect of the definition of a debtor we agree with the provisions set out although we note that the principles are not aligned with the debtor level proposals for forbearance which is likely to be confusing in practice.

In respect of the accounting scope of consolidation, please refer to our comments set out in question 10.

Q21. Do you agree with the proposed approaches (debtor approach for non-retail exposures, and possibility of a transaction approach for retail exposures)? In particular, do you agree with the idea of a threshold for mandatory application of the debtor approach? If so, which ratio methodology would you favour and why?

We support the principles set out on page 30 which are aligned to the practices of impairment recognition and default for prudential purposes. We believe, however, that the "pulling effect" thresholds would contravene industry practice especially in respect of the retail portfolios and are arbitrary/unnecessarily complex. We see no reason for FINREP to impose reporting threshold calculation methods which compete with prudential methods. Repurposing of methods used for prudential purposes should be entirely sufficient, and where such methods are not currently imposed they should not be introduced outside of the process for determining the approach for Article 174 (5).

Q22. Do you agree with the exit criteria from the non-performing category?

The exit criteria require "any concern related to its full repayment, according to its original or when applicable modified conditions, has been lifted" and "the exposure does not have any payment past-due". We agree that these are both good examples of where a contract would exit the non-performing (or impaired) category, in principle.

There is no explanation as to when the concerns are deemed to be lifted, which is appropriate as these can vary in differing circumstances. However, it would be difficult to conclude that any concern related to its full repayment could ever be lifted, and so we recommend replacing the wording to "a significant reduction in the concern related to its full repayment according to its original or when applicable modified conditions, such that the credit quality is similar to equivalent loans that have not been forborne has been lifted", or the following wording:
"The renegotiated loan will continue to be disclosed as impaired until there is sufficient evidence to demonstrate a significant reduction in the risk of non-payment of future cash flows, and there are no other indicators of impairment." We refer to our disclosure on "Credit quality classification of renegotiated loans" on page 255 of our 2012 Annual Report and Accounts.

Q23. Do you agree with the separate monitoring in a specific category of exposures ceasing to be non-performing? Do you think this specific category should be integrated within the performing or the non-performing category?

We agree with the separate monitoring of a specific category. When an exposure ceases to be non-performing, it is placed into the 'renegotiated loan' classification, which is maintained separately from performing loans that have never undergone forbearance, for allowance calculation purposes. As noted in our response to Q9, this is the same category that houses exposures where the renegotiation has resulted from significant concern about a borrower's ability to meet their contractual payment terms but the renegotiated terms are based on current market rates and contractual cash flows are expected to be collected in full following the renegotiation.

Q24. Would you favour the specific exit or specific separate monitoring criteria for non-performing exposures to which forbearance measures extended?

We favour both the specific exit and specific separate monitoring criteria for non-performing exposures. The removal of an exposure out of a non-performing classification due to a significant reduction in the concern related to a debtor's full repayment according to its original or modified conditions, allows the exposure to be more faithfully considered in the calculation of an allowance as it demonstrates a lower risk of non-payment. However, the risk is still larger than an exposure that has no history of forbearance and so once the exposure has exited the non-performing classification, should be held in a specific separate monitoring classification.

Q25. Could you indicate whether all the main drivers of costs and benefits have been identified in the table above? Are there any other costs or benefits missing? If yes, could you please specify which ones?

We believe the cost of introducing the requirements as set out in the consultation paper will be significant for three main reasons:

- The scope of the definitions are far broader than those set out in existing accounting disclosure and regulatory frameworks, particularly in respect of their application to trading portfolios. The broad scope leads to a requirement to define reporting policies/frameworks, create underlying data and capture information in new systems and risk management processes.
- The complex and prescriptive nature of the definitions, particularly in respect of the 'safety net' criteria for assessing forbearance, the probation period for forborn cures, and the arbitrary 'pulling effect' thresholds for non-performing exposures.
- The requirement to present forborn and non performing exposures by country of residence of the counterparty is not aligned to how banks' capture and monitor these positions.

As a result, the proposed requirements will require significant investment in current systems and, in some cases, the creation of new systems to capture the necessary information. Staff hire and training will also incur significant costs. The associated cost will be amplified to the extent that the requirements are implemented in any time frame less than 24 months from the date the rules are final.

In addition to the costs identified in *Table 1 – Summary of the costs of the proposals* there will also be significant one-off cost incurred for the following:

- In addition to data collection, a significant amount of data will need to be created to apply the rules to trading portfolios and to introduce the concept of cured forborn exposures.
- The new definitions could lead to a requirement to reconcile existing financial disclosures and regulatory reporting to FINREP for control purposes and in order to address stakeholder questions. There will also be a need to educate stakeholders on the differences between the various data sets.
- Enhanced Credit audit data quality management and testing to ensure that FINREP alternate definitions are not contaminating external or regulatory disclosure definitions.

Q26. For institutions, could you indicate which type of one-costs (A1, A2, A3) and on-going costs (B1, B2, B3) are you more likely to incur? Could you please explain what exactly drives theses costs and give us an indication of their exact scale?

Please refer to our answer for question 25.

Q27. 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 might further inform our analysis of the likely impacts of the proposals?

The impact of the proposal as drafted will be significant. The assertion set out at the bottom of page 7 that implementation costs will be lessened because the proposed definitions are not at odds with existing accounting and regulatory frameworks and practices is incorrect. The proposal leads to a requirement to create, capture, monitor and manage an entirely new data set and not simply build on existing processes. This is particularly the case in respect of the proposed application to trading portfolios, the introduction of a cured concept for forbearance and the generally prescriptive/mechanical nature of the definitions of forbearance and non performing.

Q28. Do the instructions provide a clear description of the reporting framework? If not, which parts should be clarified?

Please refer to response provided in Q30.

Q29. Are there specific aspects of forbearance and non-performing loans that are not covered or addressed properly in the templates?

Please refer to response provided in Q30.

Q30. Do the reporting requirements include items which would be disproportionately costly to implement? If yes, how the templates could be modified to cover the necessary supervisory information? Institutions are especially encouraged to provide their views on which break-downs are easier to fill in, or whether they believe there are redundancies with information reported in other supervisory reporting templates, or if they believe alternative definitions could achieve similar results as those in this Consultation Paper but at lesser costs.

The following reporting requirements would be disproportionately costly to implement:

- The requirement to present forborn and non performing exposures by country of residence of the counterparty. This presentation is not aligned to how banks' capture and monitor these positions. Presentation by country of booking is more aligned with how the positions are managed and consistent with the majority of the other FINREP requirements.
- The requirement to track the accumulated changes in fair value due to credit risk for debt instruments measured at fair value through profit and loss in order to arrive at a proxy of their 'gross amount'. This information is not used to manage the risks associated with exposures measured at fair value and therefore is not captured in banks' underlying systems. We suggest that the gross amount should align to the balance sheet presentation.