European Association of Co-operative Banks
Groupement Européen des Banques Coopératives
Europäische Vereinigung der Genossenschaftsbanken

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EBA Consultation Paper on Draft Regulatory Technical Standards on the conditions for assessing the materiality of extensions and changes of internal approaches when calculating own funds requirements for credit, market and operational risk under articles 138(5), 301(3)(a) and 352(3)(a) of CRR

Ladies, Gentlemen,

The European Association of Co-operative Banks (EACB) welcomes the opportunity to comment on the EBA Consultation Paper on Draft Regulatory Technical Standards on the conditions for assessing the materiality of extensions and changes of internal approaches when calculating own funds requirements for credit, market and operational risk under articles 138(5), 301(3)(a) and 352(3)(a) of CRR (EBA/CP/2013/02).

Please find our general remarks and responses to selected questions in the following pages.

We will remain at your disposal,

Yours sincerely,

Hervé Guider
General Manager

Volker Heegemann
Head of Legal Department

Brussels, 11 June 2013

EACB position paper on EBA Consultation Paper on Draft Regulatory Technical Standards on the conditions for assessing the materiality of extensions and changes of internal approaches when calculating own funds requirements for credit, market and operational risk under articles 138(5), 301(3)(a) and 352(3)(a) of CRR

A. GENERAL REMARKS

We appreciate that the EBA clearly defines the categorisation of extensions and changes and calculation of thresholds that define the materiality. Nevertheless, the proposed thresholds are very low and at a detailed level. Moreover, the proposed rules on categorization seem very detailed as well. According to our experts, if these rules are to be followed, almost all model related changes would fall into the first and second categories. Even slight changes in risk management's tasks would require ex-ante notification. This would result in an extra administrative burden and increased costs for banks and supervisors as well. According to the information submitted by members of EACB, the costs for documentation, impact analysis and communication of the described changes to supervisors would be material. Complying with these changes would require hiring of additional staff and would lead to an estimated cost of € 1 million at single institution level.

Below you can find our responses to specific questions.

B. ANSWERS TO SPECIFIC QUESTIONS

Question 1:
Are the provisions included in this draft RTS that specify the principles of categorisation of extensions and changes, sufficiently clear? Are there aspects which need to be elaborated further?

The categorization of extensions and changes to the internal models seems sufficiently clear. However, according to our members the proposed rules on categorization are rather too detailed. In addition to this the proposed thresholds are very low. According to our experts, the combination of these two factors would lead to almost all model related changes would fall into the first and second categories.

Question 2:
Are the provisions included in this draft RTS on the calculation of the quantitative threshold for the IRB approach sufficiently clear? Are there aspects which need to be elaborated further?

The calculation of the threshold for the IRB approach seems clear.

Question 3:
Do you support the calculation proposal of the quantitative threshold for the IRB approach in terms of design of the metrics and level of thresholds? (Please also take into account the arguments provided in Tables 2 to 5 of the Impact Assessment)

The proposed thresholds are very low. This could result in unnecessary burden for banks and supervisors as well.

Question 4:
Do you support for the IRB approach the three month period for notification of the changes before implementation?

The three months ex-ante period for notification of less material changes is considerably too long. More flexibility should be allowed. A period of two weeks would be more feasible and would also reflect the current practice of notification of changes to supervisors in some countries.

In practice, notifications are sent to supervisors when changes are internally approved and right before implementation. This allows banks to show the final version to the supervisors. A 3 month period of waiting for supervisory action is very long, and would threaten smooth and efficient functioning of internal processes and risk methods.

From a practical point of view, the draft standards need to provide further details with regard to the process of approval. To give some predictability and legal protection to institutions, a maximum supervisory handling time for all material changes (changes under RTS article 1(1)(a)) should be fixed.

Question 9:
Are the provisions included in this draft RTS on the calculation of the quantitative threshold for the IMA sufficiently clear? Are there aspects which need to be elaborated further?

The proposed quantitative thresholds seem sufficiently clear (for comments regarding the levels of the thresholds see answer to question number 10).

Question 10:
Do you support the calculation proposal of the quantitative thresholds for the IMA in terms of design of the metrics and level of thresholds? (Please also take into account the arguments provided in Tables 2 to 5 of the Impact Assessment)

According to our experts the 5% threshold of the overall own fund requirements for market risk is very strict. Market movements alone may result in substantial moves of VaR and Stress VaR figures, resulting in a direct increase in own fund requirements. Additionally, an internal model that calculates VaR with less scenarios may have a large statistical error. Therefore, it would not be possible to clearly separate effects of model changes from statistical errors.

In practice the implementation of the proposed thresholds might lead to non-material changes being classified as material. This would lead to a significant increase in the number of changes classified as material without a proportional increase in the added value of the exercise for the purpose of for risk management processes. This could result in supervisors being flooded with information that might not be relevant, a slower implementation of the best practices in the risk management process and a weakening of banks' capability in efficiently measuring the market risk.

Question 11:
Do you support for the IMA the one month period for notification of the changes before implementation?

The one month ex-ante period for notification of less material changes is considerably too long. More flexibility should be allowed. A period of two weeks would be more feasible.

From a practical point of view, the draft standards need to provide further details with regard to the process of approval. To give some predictability and legal protection to institutions, a maximum supervisory handling time for all material changes (changes under RTS article 1(1)(a)) should be fixed.

With regard to the classification of "ex-ante" changes according RSA Annex 3, we would like to make a couple of remarks:

- Part I, Title I; paragraph (3) - the integration of a portfolio (such as in cases of portfolio acquisitions and corporate takeovers) should be seen as material only in case of breaking the thresholds given in Article 7, 1 (c) (i),(ii) or (iii).
- Part II, Title II; paragraph (3) - the changes in grid-points on an interest curve, or an extension of an implied volatility surface should not be viewed as needing ex-ante notification. The suggested treatment might lead to inflexibility when it comes to adapting to new market standards and changes in the market.

Question 12:
Do you support for the IMA the 60-day observation period for the purpose of comparing the modelling result before and after a proposed change?

A 60-day observation period is too long and would lead to large computational efforts also for immaterial changes. This might lead to an inflexibility and inability to quickly response to new market developments and best practices. We suggest a 20-day observation period and only in the case of significant changes.

Question 13:
Do you support that for the IMA for those modelling approaches which are only required to be calculated once a week (stressed VaR, IRC, CRM) to compare only twelve numbers for Article 7 paragraph 1(c)(iii)?

Yes.

Question 14:
Do you support that for the IMA no quantitative differentiation between changes requiring notification prior vs. post implementation is made?

Yes, the classification of changes requiring notification prior or post implementation is clear from the comprehensive list given in RSA Annex 3; Part I, Title II and Part II, Title II.

Question 15:
Are the provisions included in this draft RTS on the documentation requirements sufficiently clear? Are there aspects which need to be elaborated further?

Internal validation is a part of banks' policies. However, the requirement to include with the ex-post the notification reports of the institutions' independent review or validation in the case of non-material changes is unnecessary. This might lead to unnecessary resources being spent on non-material (and minor) changes and could decrease banks' resources and flexibility to react sufficiently quickly to changes in the market.

Question 16:
Do you support the view that costs arising for institutions from the documentation requirements included in the draft RTS are not expected to be material? If not, could you please indicate:
- the main cost driver: i) additional IT equipment, ii) additional on-going Staff/hours, iii) other (please specify).
- the % increase in total yearly costs of internal models management for credit/operational/market risk induced by the proposed documentation requirements (specify whether the costs arise only for some of the risk categories covered by the provisions).
- indicative monetary amount of these additional costs (specifying currency and unit)

Question 17:
Do you support the view that the additional costs, for institutions, of computing the quantitative impacts of the implemented model extensions/changes are expected to be non-material, given that institutions already carry out impact analysis in the current framework? If not please indicate:
- the main cost driver: i) additional IT equipment, ii) additional ongoing Staff/hours, iii) other (please specify).
- the implied % increase in total yearly costs of internal model management for credit/operational/market risk induced by the quantitative impact analysis (specify whether the costs arise only for some of the risk categories covered by the provisions).
- indicative monetary amount of these additional costs (specifying currency and unit).

Question 18:
Do you support the view that, for institutions, the costs of ex-ante/ex-post notification of extensions/changes are expected to be non-material? If not, please indicate:
- the main cost driver: i) additional IT equipment, ii) additional ongoing Staff/hours, iii) other (please specify).
- the % increase in total yearly costs of internal models management for credit/operational/market risk induced by the notification requirements (specify whether the costs arise only for some of the risk categories covered by the provisions).
- an indicative monetary amount of these additional costs (specifying currency and unit).

Answer to questions 16-18:

According to the information submitted by members of EACB, the costs for documentation, impact analysis and communication of the described changes to supervisors would be material. Complying with these changes would require hiring of additional staff and would lead to an estimated cost of € 1 million at single institution level.