Comments

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

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The **German Banking Industry Committee** is the joint committee operated by the central associations of the German banking industry. These associations are the Bundesverband der Deutschen Volksbanken und Raiffeisenbanken (BVR), for the cooperative banks, the Bundesverband deutscher Banken (BdB), for the private commercial banks, the Bundesverband Öffentlicher Banken Deutschlands (VÖB), for the public-sector banks, the Deutscher Sparkassen- und Giroverband (DSGV), for the savings banks finance group, and the Verband deutscher Pfandbriefbanken (vdp), for the Pfandbrief banks. Collectively, they represent more than 2,000 banks.

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The draft RTS is based on three different mandates under the CRR. However, the individual draft RTS shall be submitted to the EU Commission on different dates. Whilst the date scheduled for the IRBA is the 31 December 2013, the draft RTS for AMA and IMA will only have to be submitted on 31 December 2014. We welcome the joint preparation of an RTS since it is an attempt to avoid inconsistencies between the requirements for the various internal approaches and seeks to ensure the promulgation of harmonised rules. However, there is no compulsory need for the requirements on the various model classes to come into effect on the very same point in time. In our understanding, the EBA seeks to comply with the European legislator's intents and purposes. Hence, we feel it is appropriate to refrain from scheduling an earlier effective date for the IMA and AMA. Notwithstanding the foregoing, a joint submission to the EU Commission can still take place as per 31 December 2013.

The list of the model changes appears to be extremely comprehensive. As a consequence, compared to the present policy, more likely than not, there will be a sharp increase of model changes that require approval by or have to be reported to the supervisory authorities. In order to ensure high quality internal approaches, there is a regular need for timely adjustments. The current proposals would jeopardise this. The proposed new rules will render the process more complex and also drive up costs considerably for institutions as well as for supervisors.

The regulatory scope should not cover changes aimed at remedying shortcomings identified by the authorities during their audit of internal approaches. Furthermore, over and above the policies laid down, upon identification of any spontaneous problems in terms of the internal approaches it should be within the supervisor’s own vested interest to be able to agree a fast-track procedure with the respective bank on a bilateral basis.

On a more general note, the forthcoming provisions should not lose sight of the underlying rationale of any supervisory activity, i.e. appropriate risk coverage and financial market stability. Hence remedying shortcomings that were either identified by the supervisor or that were identified internally should not be unduly constrained by additional logistics and long approval times.

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Specific answers to the questions

Q1: 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?

We agree with the breakdown of the categories into three different groups. Under the current proposals, however, there would be no changes which would not have to be reported at least in regular intervals to the supervisor. In our view this is inconsistent with the principle of proportionality. In our assessment, there should be one further category of minor changes that may be implemented without being reported to the supervisor. In our understanding this category should be comprised of normal maintenance, technical adjustments as well as troubleshooting exercises. In terms of their economic feasibility, the proposed rules appear unwarranted, given that compliance with the minimum requirements for the use of the internal approaches is verified by the supervisor on a regular basis, anyway.

Also, the definition of quantitative thresholds which – when exceeded - will invariably suggest a materiality of the underlying change, appears to be essentially fit for purpose. However, we hold the view that the level of the quantitative thresholds is clearly too low. Please see the paragraphs on the respective risk type for further details.

As far as the "Extensions and changes that require notification before their implementation" specified under Article 1 (2) (a) are concerned, it is our preliminary understanding that these changes and extensions merely require reporting and do not have to approved by or discussed with the supervisor.

At this juncture, however, a problem arises: According to Art. 2, the quantitative impact of *any* individual change on own funds requirements shall be calculated. In our view, this is in breach of the principle of proportionality. Our reservations are partly owed to the fact that it is possible to use estimates (Art. 2 lit. b). During the cost benefit analysis, EBA assumes that given that banks already carry out these calculations anyway, the mandatory calculation of the quantitative impact of model changes on own funds requirements will not incur any additional costs (page 33). Whilst this may be correct with regard to changes that are material indeed, more likely than not, the by far largest part of the changes will be of a non-material nature. As such, under the present approach, they will not be calculated for the purposes of determining the own funds requirement changes. Hence there should be an exemption from the obligation to calculate the own funds requirements changes for those changes where, right from the outset, it is obvious that the quantitative thresholds will not be exceeded. At this point, suitable categorisation criteria should be prepared jointly with the banking industry.

On the other hand, we feel that the quantitative thresholds should be designed as a *de facto* backstop solution meaning that there should be no need to calculate the own funds requirements impact in cases where banks already identified a change as material on the basis of the lists in the annexes.

Apart from this, the interpretation of Article 2, No. 2(b) is of pivotal importance. If an exact analysis of the quantitative impact of the model change is unfeasible, the impact could be calculated on the basis of

a representative sample or other "reliable inference methodology". In our view, *inter alia* given the impact on the IT implementation, there will be many banks that will have to draw upon the option of making estimates. Hence, there should be a clarification that this option constitutes also *de facto* an equally viable method for determining the impact on own funds requirements.

The requirement to assess the aggregate materiality of changes that are technically related *en bloc* (Art. 2(3) is understandable. However, it is not sufficiently clear which policy needs to be adopted when handling consecutive changes where the quantitative threshold will be exceeded at a certain point in time.

Q2: 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?

We are unclear about deterring the quantitative thresholds on a consolidated level pursuant to Article 4, 1. (a) (iii) compared to Article 3, 1.(c) (i).

Article 3 No. 1.(c) (i):
*"in a decrease of 1.5 % or more of the overall **EU parent institution's** consolidated risk-weighted exposure amounts for credit and dilution risk or of the overall risk-weighted exposure amounts for credit and dilution risk in the case of an institution which is neither a parent institution, nor a subsidiary;"*

Article 4 No. 1.(a) (iii):
*"Changes which result in a decrease of at least 5 % of the overall risk-weighted exposure amounts for credit and dilution risk at the consolidated level of a **parent institution which is NOT an EU parent institution** or of the overall risk-weighted exposure amounts for credit and dilution risk of any subsidiary **where the parent institution has not received the permission to use the IRB approach**;"*

We have difficulties in comprehending the rationale for the reference to diverging baselines. In order to achieve a clear categorisation, an identical criterion would have to be linked to different quantitative thresholds. For instance, this is the case as far as the second quantitative criterion is concerned.

If there was a reference to identical baselines, a 1.5% quantitative threshold for material changes and a 5% quantitative threshold for non-material changes that are subject to a prior reporting obligation would imply that each and any change would automatically have to be regarded as material.

On principle, we endorse the method of categorising changes to the IRB approach on the basis of their quantitative impact. However, as far as certain products / approaches are concerned, the exclusive focus on changes in the percentage ratios may potentially lead to a clear increase in reporting requirements. This is due to the fact that said product / approaches regularly feature major changes in terms of the percentage ratios the absolute amount of which, however, is that low that in our view, a renewed mandatory approval requirement would be inappropriate.

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Also, the RWA quantitative threshold, the percentage ratio of which is defined at the ratings approach level, incurs disadvantages for banks featuring well segmented ratings approaches. This is due to the fact that the quantitative threshold will be triggered faster if the bank's portfolio is diversified across a large number of different ratings approaches.

Hence, we would welcome the definition of an additional absolute minimum threshold which will have to be exceeded during an extension or change on top of the percentage threshold in order to be subsumed under a respective category.

In our preliminary understanding, Art. 3 No. 2 and Art. 4 No. 2 concerning the consolidation level mean that there are no plans for an independent model change process as far as subsidiaries are concerned. However, this will be necessary for subsidiaries which are group parents themselves (sub-group). The forthcoming proposals should be clarified to this effect.

Art. 3(2) sentence 2 stipulates that the quantitative threshold calculations "shall refer to the same point in time). In our view, there should be a clarification that this does not require a parallel operation of the individual versions of the rating approaches.

Q3: 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)

No, we do not support the calculation proposal; compared to the threshold levels for operational risk and market risk, we hold the view that at the consolidated level the 1.5% threshold is excessively low. This would mean that already a small RWA change would incur material changes that are in need of supervisory approval. Potentially, this could lead to longer waiting times during the approval of changes and might delay the implementation of required changes.

In our opinion, by way of analogy to the proposals for market risk and operational risk, credit risk should similarly receive a quantitative threshold of 10 percent. There should only be one quantitative threshold that is invariably based on the RWA which are tied up as a result of the transactions covered by the regulatory scope of the applicable approach. Furthermore, sometimes variable model factors may change over time (e.g. discount factors, market values in the portfolio, repayments) in the absence of any change to the system for inferring such factors; these fluctuations, too, should be explicitly excluded from the RWA changes.

The calculation of the impact which IRBA approach changes may have on the RWA is not sufficiently clear: It remains unclear whether, at this juncture, also the impact of credit risk mitigation techniques will have to be taken into account. This should be elaborated further.

Changes to the allocation of exposures to supervisory exposure categories shall be deemed material changes and, as such, would require *ex ante* approval by the supervisor (Annex 1, Part II, Title I(1) lit.

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a). We have difficulties in comprehending the rationale behind this approach. Our reservations are owed to the fact that this allocation leaves banks with virtually no room for discretion under the prudential supervision rules. Hence, we gather that this allocation remains identical as long as the supervisory criteria for the allocation are not being changed. Consequently, this requirement could be deleted.

Changes to the rating criteria that change the rating grade of obligors shall always be deemed "material changes" (Annex I Part II Title I para. 2 lit. d). We are of the opinion that this fails to meet the principle of proportionality. After all, as a result of this proposed new rule, each and any recalibration of rating approaches would have to be approved by the supervisor in advance. Consequently, at this juncture we recommend that only those changes shall be classified as material that lead to a material change in the rating grade.

Under the current proposals, also those extensions shall be deemed material extensions where the lending decision is being taken by a third party. This requirement is not sufficiently clear. We suggest elaborating it further.

Q4: Do you support for the IRB approach the three month period for notification of the changes before implementation?

A three month lead time incurs the risk of clearly delaying the implementation of material changes. In our view, this deadline is excessively long. We are of the opinion that – similar to the market risk - a one month lead-time ought to be sufficient. Apart from this, any changes should be deemed to have been approved if they are not challenged within this window of time. In this context, we would also welcome it if the RTS included a deadline within which the supervisor will have to approve material changes to risk measurement approaches. This would provide banks with greater planning certainty. What is more, it is also of crucial importance for the joint development of rating approaches via pool solutions.

Q5: Are the provisions included in this draft RTS on the calculation of the quantitative threshold for the AMA sufficiently clear? Are there aspects which need to be elaborated further?

No comment

Q6: Do you support the calculation proposal of the quantitative thresholds for the AMA 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)

On principle, we welcome the proposed quantitative threshold for the purposes of defining material adjustments to the AMA based on the percentage change of the OpRisk netting amount. However, in our view the scenarios listed under *Annex 2* cover the content of any potential material extensions and changes to the AMA in a comprehensive manner and only assign a subsidiary importance to an additional

quantitative threshold. Instead of the 10% figure specified under Article 5, we therefore suggest using the 20% threshold currently required by Deutsche Bundesbank and the German Supervisory Authority BaFin in its information leaflet on changes to AMA models *("Merkblatt zu Änderungen von Modellen bei Fortgeschrittenen Messansätzen (Advanced Measurement Approach – AMA)" dated 31 January 201*2).

Furthermore, any extension of the AMA model to include previously exempt institutional business lines or subsidiary group companies have to be considered as an extension triggering a notification obligation if and when the change of the relevant indicator amounts to more than 1% during the current fiscal year (with the maximum ceiling being 5%). Also at this juncture, Germany does not employ a 5% parameter. Instead, a threshold that is twice as high has stood the test of time. Furthermore, an annual 5% fluctuation of the OpRisk risk capital charge is absolutely normal even in the absence of any underlying model change. Hence, this ratio should be increased to 10%.

Q7: Do you support for the AMA the three month period for notification of the changes before implementation?

Said three month notification period under the provisions of Article 6(a) may delay the implementation of required further AMA developments. In our view, this period is inappropriate as far as non-material extensions and changes are concerned.

Particularly in combination with the requirements specified under Article 9 1. e, f concerning the internal approval approach prior to the notification, the proposed deadline would effectively incur a lead time of approximately three to four quarters. Hence, we are concerned that the current proposals will be become an obstacle for the timely further development of the AMA that may become necessary in order to accommodate changed requirements. These provisions are thus incompatible with the objective jointly pursued by supervisors and banks alike – i.e. continuously strengthening banks' OpRisk management. In an attempt to facilitate faster responses to market conditions and in view of lead times between three and four quarters, banks might shy away from strengthening the link between OpRisk related issues (for instance internal control system, business continuity management, fraud risk analysis) and the qualitative AMA framework.

In our experience, a notification period of four weeks is appropriate. Given the usual schedules of quarterly bodies (involving executive board members) for approval of such changes (approx. 6-7 weeks prior to the quarter's deadline), the lead time can thus see a significant reduction.

A four week deadline is also in line with the regulatory proposal for market risk models proposed under Article 8 and the proposals for the IRB approach made in our comments (cf. above). What is more, any changes should be deemed to have been approved if they are not challenged within this period. In this context, we would also welcome it if the RTS specified a deadline within which the supervisor will have to have approved material changes to risk measurement approaches. This is of crucial importance for banks' planning security.

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Q8: Do you support that for the AMA no quantitative differentiation between changes requiring notification prior vs. post implementation is made?

No comments

Q9: 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?

In order to determine whether the envisaged change to a model meets the criteria for a material change, there is already a need to carry out a 60 day parallel calculation. In the final analysis, this would mean that banks would have to go to such great lengths already for any minor change or model extension. This requirement would render any kind of operational work on an internal model virtually impossible. For the purposes of reviewing the criteria we suggest a two-stage model: Any changes which, more likely than not, will incur but marginal changes to the model result shall require a calculation of the change to the value-at-risks for the current deadline and also for a deadline which is based on a period of crisis. The need to carry out a comprehensive comparative calculation should only be triggered if the aforementioned calculation reveals a delta in excess of 7%.

Q10: 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)

Under the EBA proposal, any changes and extensions shall be deemed material if the change to the model result amounts to 10% or more for the risk model's scope of application. In Germany, in practice a 20% value-at-risk threshold has proven a sufficiently conservative standard for such changes. This value should also be used at EU level. Any other value would tie up a disproportionately large amount of personnel and technical resources.

Furthermore, all extensions and changes shall be deemed material changes which incur a change of 5% or more in terms of own funds requirements for market risk at the level of the group or at the level of the individual bank. We hold the view that this figure is excessively conservative. In the current prudential supervision practice, there is no single supervisory authority which adopts such a low level in market risk under its jurisdiction. We suggest modelling the forthcoming rules on those existing requirements that have stood the test of time. Hence, a value of 10% would be more productive. This change would also avoid any undue discrimination against banks that calculate their own funds requirements largely on the basis of internal approaches.

We suggest clarification concerning the nature of the changes to be covered by the provisions under Annex 3 Part II Title I (1). In our opinion, this can only refer to the risk model and cannot possibly already refer to the valuation model. Otherwise, this would result in a considerable interference with banks' corporate decisions in the absence of any rational justification for such interference.

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With this in mind, the proposed new rules thwart the intended goal of consistency between the pricing models for trading and for risk management. In regard to trading models, institutions have to act quickly and implement changes on short notice. If this is not possible for the risk management model too, the uncoupling of the two models will lead to a lower quality of risk management and controlling.

According to Article 8, a number of changes will trigger a prior notification requirement. In our view, some of these notification obligations are excessive. For instance, we hold the view that it is inappropriate if the additional inclusion of individual risk factors (for instance in response to the ongoing validation, c.f. Annex 3 Part II Title I (3), the change of market data providers as far as individual instruments are concerned or smaller changes in the IT data landscape (Annex 3 Part II Title I (4)) and individual personnel changes (Annex 3 Part II Title II (17)) will have to be notified in advance. In practice, such long lead times are not feasible and potentially even jeopardise the model quality. In terms of the personnel changes, the (possibly post implementation) notification should be limited to employees in senior executive functions.

Also concerning Annex 3 Part II Title II (5), (14) and (16), we hold the view that a post implementation notification would be more useful in ensuring that changes can be implemented immediately thus safeguarding the requisite synchronisation between economic P&L and "dirty backtesting" on the one hand and the balance sheet or, moreover, income statement on the other hand.

Not all of the changes set out under Annex 3 Part II are specified in a sufficiently clear manner. Hence, for instance, also changes would be conceivable which might be subsumed both under Title I (3) and under Title II (3), (7) or (9).

Q11: Do you support for the IMA the one month period for notification of the changes before implementation?

A notification period of one month carries the danger of unduly delaying changes to better reflect current market developments in the model framework. Our own experience with typical implementation times and release cycles would rather favour a shorter notification period (e.g. two weeks).

Q12: 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 parallel calculation with old and new model settings for a period of effectively three months poses considerable operative challenges and would significantly enhance infrastructure requirements to support additional quasi-productive IT environments. From our experience with current regulation, much shorter observation periods (e.g. two weeks for essential changes or a few sample days for minor changes) are sufficient for a reliable impact assessment of longer-term model results in most cases.

Given the fact that this would tie up such major resources, banks might adopt a policy where adjustments will only be tackled in the context of extremely comprehensive model changes. Minor adjustments which,

on aggregate, have a considerable impact on model quality may either be postponed until such time or might be abandoned altogether.

Q13: 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)?

We support that the observation periods for approaches with only weekly required calculations should be in line with those with daily calculation. However, as for Q 12, a period of twelve weeks is deemed to be unappropriately long.

Q14: Do you support that for the IMA no quantitative differentiation between changes requiring notification prior vs. post implementation is made?

Yes, we support this.

Q15: Are the provisions included in this draft RTS on the documentation requirements sufficiently clear? Are there aspects which need to be elaborated further?

In our view, the provisions on the documentation requirements for extensions and changes to the approach are very comprehensive. Whilst not limited to, our reservations apply particularly to changes which merely have to be reported to the supervisor on a regular basis. As far as these changes are concerned, it should be sufficient if the requirements are confined to the provisions under Art. 9 (1) lit. a and b. Furthermore, also the additional documentation requirements will incur considerable additional costs for banks - costs which are primarily driven by increased payroll expenses.

IRB:

On Article 9, 1. e:

The meaning behind "independent review or validation" (Art. 9(1 (e)) is not sufficiently clear. Does this refer to an upstream audit which has already been carried out or does this refer to conventional validations and tests during the model development stage? We are of the opinion that the usual validations and tests that are a corollary of the model development process should be sufficient. The latter applies in particular if the persons in charge of the downstream, independent model validation actively accompanied the model development process (i.e. by reviewing concepts and analyses during of model development stage). More specifically, it is not sufficiently clear whether the scope of the requirement extends beyond the validation reports in a 100% model environment.
Example:
Organisational changes in the credit field resulting from business policy decisions

On Article 9(1) lit. h:

This documentation requirement should deleted entirely.

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Rationale:
Supervisors should already be in possession of all documents from the certification as well as past extensions / changes. Any renewed submission (particularly during non-material changes which have to be reported annually on a post implementation basis) would lead to a needless inflation of the documentation to be supplied and does not yield any additional insights as far as the underlying information is concerned. The supervisor will specifically request the resubmission of any particular documents if and when needed. This does not require any separate rule.

On Article 9(1) lit. i:
The documentation requirement for material changes within the meaning of Article 9(1)(i) (*details of all extensions planned over the next 12 months)* is utterly inconsistent with common market practices. The planning timelines for model changes are usually clearly shorter. Whilst this applies to market risk in particular, it equally holds true for the various other risk types. Any overview of envisaged changes over a twelve month horizon will invariably be incomplete. What is more, more often than not, it will quickly become obsolete in view of the emergence of new requirements and market changes.

On Article 9(2):
Under the current proposal (compared to the aggregated notification of immaterial changes currently practiced in Germany based on an official information leaflet on IRBA systems issued by German banking supervisor BaFin) there will be a sharp increase in the requirements with regard to the documentation that needs to be submitted. Here, too, we hold the view that, given the underlying low level of materiality, the proposed new rules are inappropriate. We feel that it would be more constructive to adopt the policy championed by the German supervisor BaFin in its information leaflet.

AMA:
Article 9(1) lit. h, i specifies documentation requirements which, in our view, are inappropriate as far as the AMA is concerned. The respectively applicable AMA documentation will have been submitted to the supervisor. Any renewed submission will result in additional red tape and may potentially delay the approval process. Concerning requirement (i), on principle, it is only possible to specify those changes for the next twelve months which are already envisaged at the date on which the notification is filed meaning that this list will always run the danger of being inherently incomplete.

In the event of non-material changes we feel that presenting a report on an independent review (Article 9(1)(e)) will be unnecessary. Hence, we hold the view that the requirement set out under Article 9(2) will result in undue delays as far as the implementation of required adjustments is concerned (c.f. also Q7).

IMA:
The documentation requirement for material changes as outlined under Article 9 Nr 1 lit. i (details of all extension planned over the next 12 months) appears to be remote from any sensible industry practice. Planning horizons for model changes usually are significantly shorter. Any prospective schedule for changes over a full year is most likely to be necessarily incomplete and will in most cases soon be superseded by new market developments.

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On Article 9(2):

In our view, the requirement concerning the submission of the institutions' independent review of validation (Article 9(1)(e)) for such changes is unnecessary given the low degree of the underlying materiality. Hence, this requirement should be deleted.

Q16: 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 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 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)**

No, we do not support this view. One key cost driver will consist in the higher number of material changes (resulting from the qualitative criteria) in particular and their ensuing higher costs; please cf. also Q15 and our comments on Annex 1).

Q17: 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).**

Whilst not limited to, particularly the IT infrastructure in the area of market risk requires major investments. Partly, these go beyond the risk application and also extend to the trading systems. As far as the coordination and evaluation of the comparative calculations is concerned, additional staff will be required. Whilst not limited to, the same applies to the field of adjustments in need of notifications. On aggregate, in our view, model maintenance will require up to 50% more resources.

IRB:

No, we do not support this view: In the market areas, the costs for impact analyses concerning organisational or process changes which have to be reported will see a marked increase.

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IMA:
Additional costs for computing quantitative impacts over a time of three months will be considerable, apart from the operative burden associated with such parallel runs. Impact analysis carried out under the current framework is typically based on much shorter observation periods, with still a high degree of long-term reliability.

Q18: 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).**

No, we do not support this view; the documentation requirements will be the main cost driver.

General comments on the three lists (Annexes 1, 2 and 3)

The EBA seeks to provide an exhaustive list of those changes to the IRB approaches, AMA or market risk models which can be subsumed under one of the three categories specified under Article 1. Although this could, in principle, enhance banks' planning security, we hold the view that it might curtail the banks' discretionary decisions which are indispensable for an application of the rules that is fit for purpose. Hence, we would welcome it if the aforementioned model change categories listed in the annexes were included as mere examples of a general nature. These examples of a general nature should then be interpreted on a bank specific basis within the framework of a "model change policy" to be agreed with the supervisor.

Apart from this, not all scenarios categorised as material in the lists constitute material changes always and without exception. The proposed rules would lead to a situation where, for instance, any minor change to the IRBA's scope of application or any insignificant change to the validation methods would require an *ex ante* authorisation by the supervisor. Also concerning the internal market risk models, this appears excessive, for instance in the event of changes to external data sources or IT data landscape; hence, from the point of view of risks, this would be unwarranted. In effect, the proposed rules would lead to a situation where supervisory authorities would be faced with a spate of change requests. The resulting longer processing times would obstruct banks' internal implementation processes in an unnecessary manner. What is more, this might even entirely prevent such implementation. Based on the

foregoing, only those changes should require an *ex ante* supervisory approval as "material" changes if and when their implications are quantitatively material.

The German Banking Industry Committee (GBIC) would like to reiterate (cf. Q4) its reservations over a feedback period of three months. In our view, this is excessive as far as the IRBA is concerned. Our reservations are compounded by the fact that the total approval process duration is not sufficiently clear. On the whole, this would result in a significant inflation of IT costs. For instance, there would be no planning certainty and it would potentially become necessary to run several releases in parallel.

Annex 1 – Changes to the IRB approach

The list of material changes contains numerous changes which, in our view, cannot be deemed material in each and every case and which, consequently, should not require any official approval, either. We should like to mention the following (non-exhaustive) examples:

- Changes in the definition of default (Annex 1, Part II, Title 1(3);
- Changes to the validation methodology or validation processes (Annex 1, Part II, Title 1(4);

With regard to the aforementioned items, there should be a clarification that merely material changes shall be covered.

We would like to reiterate a point already made in our response to question 3 namely that changes in the methodology for assigning exposures to rating systems (Annex 1, Part II, Title 1(1) lit. b) shall be removed from the list of material changes in need of prior supervisory approval.

Furthermore, we are of the opinion that a number of qualitative criteria lack a sufficiently clear language, for instance:

- Annex, Part II, Title 1 (1) (d) (iii): "distribution of obligors, facilities or exposures (...)". Nearly every change will have an impact on the latter.
- Annex, Part I, Title 1 (1)(a) / (2)(b): Extension to another business unit.

It remains unclear how business unit changes resulting from corporate policy decisions shall be categorised (carve-out, merger, changed organisational allocation). The requirement also comes as a surprise because rating approaches are approved at the level of the legal entity / technical clients /business delimitation yet, they are not approved at the level of business units.

Annex 2 – Extensions and Changes to the AMA

On principle, we welcome the qualitative criteria for classification of extensions and changes to the AMA.

However, we feel that the following items constitute a relevant change to the AMA under specific circumstances, and we expect difficulties during the implementation of the current proposals:

Part II, Title II, (1) (a): The issue described is linked to a host of potential process changes to the central and decentralised OpRisk management functions. It is difficult to infer a direct link to the specific AMA elements. We feel that the feasibility of this proposal hinges on a further elaboration of the underlying issue.

Part II, Title II, (1) (b): In our view, the scope of a reporting for operational risk that provides readers with decision-relevant information should essentially allow a certain degree of flexibility in order to facilitate speedy adjustments to changed conditions. A prior notification of such changes erodes the objective of speedy reporting responses (cf. Basel Committee on Banking Supervision „Principles for effective risk data aggregation and risk reporting").

Title II, (2) (b): Given the close integration of OpRisk control with related technical areas, the exact number of staff allocated to OpRisk is difficult to single out. Hence, we do not believe that measurement and follow-up of the allocated resources would be meaningful. Furthermore, the heterogeneous design of central and decentralised OpRisk functions renders a cross-bank comparison of said ratios even more difficult.

Annex 3 – Extensions and Changes to the IMA

In principle, we support the definitions and explanations made in the Annex regarding the classification of changes requiring ex-ante notification to competent authorities, especially in those cases where they are related to fundamental elements of the IMA directly.
In most of the cases, required material thresholds can be derived and have a direct influence to own fund requirements and/or - where applicable - to risk-weight exposure before and after the envisaged change. However, we do not see any relations or effects resulting in consequences for own funds or risk-weight exposures from changes to the organisational and operational structure of risk management and internal governance processes, especially organisational changes, changes to the new product process or internal organisation and staff changes.
Even if relevant in the context of the IMA and its organisational and process-related setup, it is not feasible from our perspective that changes relating to these mentioned characteristics should require an ex-ante notification to the supervisor based on a one month notice period, as they are referring to continuous processes on an operative level.
Additionally, it is not transparent for us how required documents - referenced under Title V, Article 9, clause 2 - like scope of application with volume characteristics, and a quantitative impact of the expected effects on the risk weighted assets or the own fund requirements shall be produced in this context.

Yours faithfully,
For and on behalf of the
German Banking Industry Committee

Dr. Martin Lippert Dr. Johannes Voit