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European Banking Authority
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**Online Submission**

**GUIDELINES ON THE APPLICATION OF THE DEFINITION OF DEFAULT UNDER ARTICLE 178 OF REGULATION (EU) 575/2013**

Moody's Investors Service ("MIS") appreciates the opportunity to provide comments to the European Banking Authority ("EBA") on the consultation paper: *Guidelines on the application of the definition of default under Article 178 of Regulation (EU) 575/2013* ("Guidelines"). Our comments relate to the benefit of an increase in the consistency and comparability of information used and disclosed by financial institutions but with a suggestion that these proposals remain within the confines of the prudential framework of supervised financial institutions.

## 1. Proposed definition of default under the Capital Requirements Regulation

MIS, as a user of default information in its analysis, has noticed that institutions have established their own detailed rules for the identification of default based on their experience and portfolio characteristics. This has led to a lack of comparability across institutions. MIS therefore supports the guidance provided on the various aspects on the application of the definition of default in the Guidelines and the consistency and comparability this is intended to achieve. We believe this would lead to an increase in comparability across institutions and also assist cross-border institutions in complying with different requirements in different Member States.

As noted in the Guidelines, the details with respect to the definition of default could lead to many institutions having to implement new procedures and systems. Whilst MIS supports an implementation phase, this could create further inconsistency in the application of the definition of default unless clear guidance is provided. We therefore agree that the proposed governance requirements in the Guidelines are crucial as changes are likely to result in structural breaks in historical data.[1]

[1] MIS supports the requirement that "institutions should keep a register of all current and past versions of the default definition starting at least from the date of application of these guidelines. If more than one definition of default is used in a banking group the scope of application of each definition should be clearly specified."

## 2. Use of external ratings in the application of the definition of default

MIS notes that with respect to the use of external data for institutions that use the IRB approach, that the Guidelines suggest that such institutions should assess the differences between the definitions of default used internally and in external data and their impact on the default rate. MIS does not believe this should be construed as an indication that the definition of default used in the external data should be equivalent to the definition proposed in the Guidelines.

The definition of default used by MIS is applied in the context of rating a bond or other liability issued by a sovereign, corporate, insurance company, fund or bank and not on the whole borrower itself, and speaks only to credit risk. As a consequence, the criteria used by MIS are necessarily applicable only to debt and debt like obligations which is a narrower set of obligations applicable to a bank. For example, in comparison to the Guidelines, which addresses the definition of default for all types of exposures banks may take on directly to borrowers, MIS rates a more limited universe of obligations (debt, hybrids, deposits and so on) of various types of borrowers (corporates, sovereigns, funds, banks, insurance companies and so on). For a more comprehensive explanation of how MIS expresses its views on credit risk and our use of the term "expected loss."[2], please see our Ratings Symbols and Definitions Handbook[3] which can be found on Moodys.com.[4]

We appreciate the opportunity to comment and would be pleased to discuss our comments further with the EBA or their staff.

Yours sincerely

**/S**

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[2] Other rating agencies may have different means of communication their opinions.
[3] https://www.moodys.com/researchdocumentcontentpage.aspx?docid=PBC_79004.
[4] Expected loss takes into consideration both the probability of default and expected loss in case of default.