Deutsche Bank

EU Transparency Register ID Number 271912611231-56

Mr. Adam Farkas
Executive Director
European Banking Authority
Floor 46, One Canada Square
London E14 5AA
United Kingdom

Deutsche Bank AG
Winchester House
1 Great Winchester Street
London EC2N 2DB

Tel: +44 20 7545 8000

Direct Tel +44 20 7545 1903
Direct Fax +44 20 7547 4179

Dear Mr. Farkas,

DB response to the Draft Regulatory Technical Standards (RTS) on materiality threshold of credit obligation past due under Article 178 of Regulation (EU) 575/2013

Deutsche Bank (DB) welcomes the opportunity to comment on the European Banking Authority's (EBA) consultation paper on materiality threshold of credit obligation past due. In our opinion there are four key themes that should be taken into consideration with regard to the Draft RTS:

1) **Harmonisation**: Defining a concrete and stringent materiality threshold approach to allow better comparability across banks in different jurisdictions. To better achieve this objective we recommend that there are fixed absolute and relative thresholds, and not only define them as upper limits as proposed.

2) **Definition of credit obligation past due:** We are supportive of Option 1 which we believe provides a reasonable balance between simplicity and risk sensitivity. It is also relatively quicker to implement and helps provide a higher degree of comparability across institutions. We therefore see Option 1 as an alternative that banks should be allowed to implement.

3) **Distinction between Retail and Non-Retail**: We do not see the necessity of differentiating materiality thresholds between retail and non-retail asset classes – especially since the Draft RTS methodology thresholds for retail and non-retail do not lead to a significant difference on the default count and rating systems.

4) **Transitional period/implementation efforts:** We are pleased to see that the Draft RTS already takes into consideration the need for a transition period to allow bank's to adapt to any change in the default definition. The transitional period should not be less than 5 years to reflect the new materiality thresholds in our IT systems, processes, credit risk parameter settings and rating models.

We provide more detailed comments in Annex I and Annex II. Please do not hesitate to let us know if you have questions or wish to discuss these issues further.

Yours sincerely,

Daniel Trinder
Global Head of Regulatory Policy

Annex I – Overarching Comments

Harmonisation

The Draft RTS refers to the materiality thresholds applied to the default identification in the event that the obligor is more than 90 days (or 180 days if the competent authority has decided to replace the 90 days with 180 days in accordance with Article 178(1)(b) of the CRR). Such a materiality criterion is already applied using an array of implementation approaches as outlined in the RTS-Section "Baseline scenario". Therefore, defining a more concrete and stringent materiality threshold approach is appreciated for comparability reasons across banks in different jurisdictions. To better achieve this objective we recommend that there are fixed absolute and relative thresholds, and that they are not defined as upper limits as proposed in the Draft RTS.

It should also be noted that comparability is limited by having a national discretion rule in place that allows for optionality between using a 90 and 180 days past due for certain products/asset classes. In our view a uniform 90 days past due requirement would provide a consistent parameter. In this context, DB understands that this is not a specific topic discussed in the context of the Draft RTS. However, we would like to raise this since it should be considered from the point of view of driving towards harmonised requirements as articulated in Draft RTS.

Definition of credit obligation past due

The Draft RTS contains a comparison of different options assessed to define the credit obligation past due. Although, the preferred option in the Draft RTS refers to the sum of amounts past due (option 3), DB is in favor of defining the whole single credit obligation as the reference amount (option 1).

As highlighted in the Draft RTS under "Advantages" for option 1 this approach is considered to be conservative with less extensive implementation adjustments compared to other approaches. The latter would also shorten respective transition periods for implementing the new materiality thresholds. However, the stated disadvantage of not accounting for small credit obligations does not hold true if the absolute and relative thresholds are defined appropriately. Therefore, we see option 1 as an alternative option banks should be allowed to implement.

Distinction between Retail and Non-Retail

We do not see the necessity of differentiating materiality thresholds between retail and non-retail asset classes, especially, since the difference between the absolute amounts proposed (please see Figure 1 below; 200 vs. 500 EUR) is not anticipated to have a significant impact on the default count. For counterparts that might not fall within the parameters of these asset classes (e.g., legal entities with an exposure amount around 1mn EUR), different default definitions might lead to a change in default status by changes in exposure size only. Furthermore, rating systems are in place with both retail as well as corporate classified exposures (e.g., rating systems for small business/self-employed clients). For these rating systems two different default/materiality definitions would be in place in parallel.

The implementation of a facility-based threshold for retail exposures should be optional. If a bank decided to implement customer ratings instead of facility ratings for retail rating systems, an aggregation on the customer level with respect to the materiality threshold should be allowed as for non-retail exposure.

Transitional period/Implementation efforts

To account for bank-internal activities triggered by any change in the default definition a transitional period is required. It should be noted that for banks operating under the Internal Ratings Based Approach (IRBA) a change in the existing materiality thresholds has a significant impact. This impact relates to IT system and process implementation efforts as well as changes in credit risk parameter settings and rating models driving the Risk Weighted Asset (RWA) levels.

Of specific note, the following activities would have to be performed:

Data basis / IT Systems

- Not all of the data will be initially available in the requisite form needed. This will require reengineering the interfaces and systems for example in the RWA calculation, credit risk parameters and model recalibrations.
- A retroactive adjustment of historical default and non-default data would be difficult and might in some instances not be possible.

Credit Risk Parameters/Rating Models

- Validation and recalibration of credit risk parameters and rating models based on the modified default definition. This impacts a significant number of IRBA approved rating systems and credit risk parameter settings.

Process

- Implications of the re-calibrated credit risk parameter and rating models need to be assessed.
- Updating of internal and external governance process, including the approval process by supervisory authorities and use test requirements.
- Training for credit officers and users of recalibrated rating models.
- Implementation of recalibrated parameter and models - including piloting and test runs.
- Updating the respective disclosure requirements.

Therefore, the required length of a transitional period depends on four main factors. First, whether the amount overdue is already available in data bases/systems used for RWA calculation as well as credit risk parameter and model recalibrations, or whether a tactical solution to determine this amount will be allowed by supervisory authorities. Second, the necessity to adjust default and loss data histories. Third, the number of credit risk parameters and models to be validated and recalibrated. Fourth, the intensity and timelines of the supervisory approval process.

In our opinion the transitional period should allow for sufficient time to adapt to the new materiality thresholds affecting the business units, e.g. RWA changes and changes in the application process.

For these reasons a transitional period should not be less than 5 years to reflect the new materiality thresholds in all related IT systems, processes and credit risk parameter settings and rating models.

The approach to a transitional period would also have to be defined. In our view, it should be a phased-in approach. This means the new thresholds are implemented at a certain point in time, but use of the default and loss data history based on the previous threshold implementation for parameter and model calibration/validation purposes would be allowed to continue. In case the current implementation cannot be directly compared to the new one, this data history should be modified by a factor assessing the difference between the old and new default count if such a factor can be derived from the available data. If not, the usage of the existing data should still be allowed. In this case the data history window should be moved year-by-year until a time period with homogenous default definition is reached. Then the data history window can be extended again. Afterwards, rating systems would be approved in a phased approach. We believe that this recommended phased approach is reasonable even though it differs from the approach reflected in the Draft RTS that suggests submitting only one change application.

Annex II – Responses to the Consultation Paper Questions

Question 1

Do you agree with the approach proposed in the draft RTS (option 1) that default should be recognized as soon as one of the components of the threshold (absolute or relative limit) is breached? Or would you rather support the alternative option, i.e. recognition of default after both thresholds are breached (option 2)?

Answer: Option 2 is the preferred option. Under option 1 the relative materiality threshold becomes not relevant for (total) credit obligations beyond 10 EUR (retail) and 25 EUR (non-retail) when the upper materiality thresholds as outlined in the Draft RTS are used. Especially, in the case of non-retail exposures, the relative threshold would become almost irrelevant (please see Figure 1 below).

However, the sole use of only one of these thresholds would lead to small overdue amounts becoming "material" due to the relative threshold (e.g., 30 EUR in case of a 1500 EUR retail consumer loan).

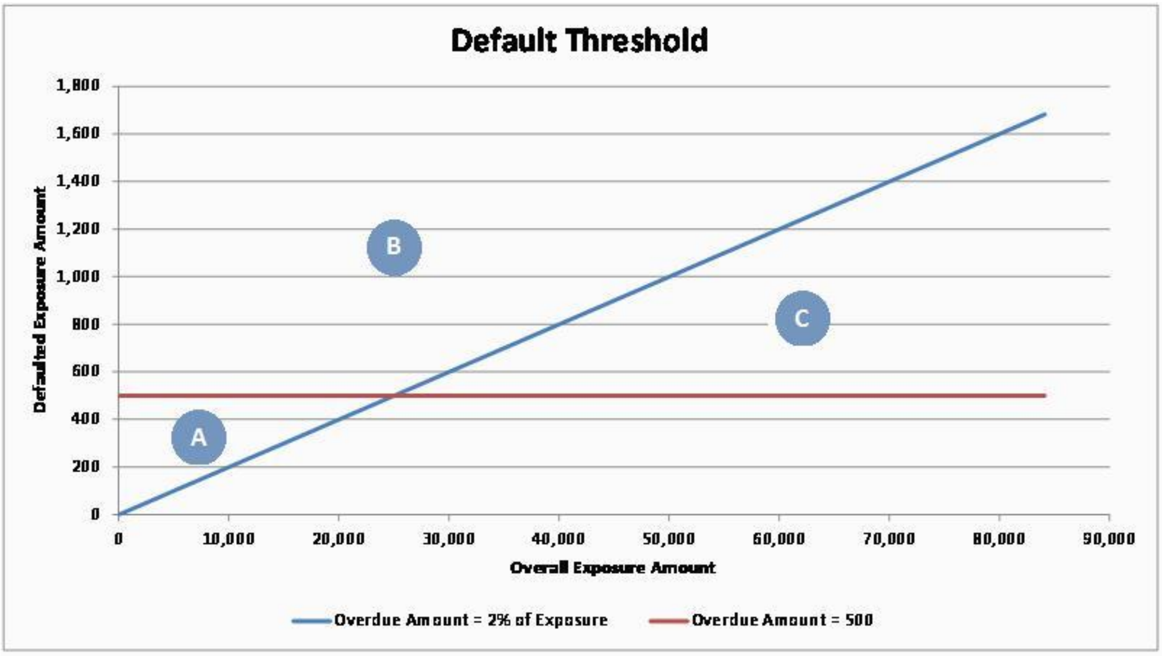

Figure 1. Example: Non-Retail. Option 1: default is recognized if either of absolute or relative limit is breached (represented by Areas A, B and C in the pictorial representation). Option 2: default is recognized if both the absolute and relative limit is breached (represented by Area B).

Question 2

Do you agree with the proposed maximum levels of the thresholds?

Answer: Yes. However, rating system specific exceptions should still be possible, subject to supervisory approval. Additionally, DB is unclear why the Draft RTS defines these as maximum levels but still allows for national discretion.

Question 3

How much time is necessary to implement the threshold set by the competent authority according to this proposed draft RTS? What is the scope of work required to achieve compliance?

Answer: There are substantial implementation efforts that would be required. Please see Annex I section "Transitional period / Implementation efforts" for details. The length of time required is a result of four main factors.

- Whether the amount overdue is already available in data bases and systems used for RWA calculations as well as credit risk parameter and model recalibrations, or whether a tactical solution to determine this amount will be allowed by supervisory authorities. As stated above in Annex I, not all of the data will be initially available in the requisite form needed. This will require reengineering the interfaces and systems for example in the RWA calculation, credit risk parameters and model recalibrations. A retroactive adjustment of historical default and non-default data would be difficult and in some instances might not be possible.
- To meet the need to adjust default and loss data history to meet the draft RTS requirements.
- To work though the credit risk parameters and models that need to be validated and recalibrated to meet the requirements.
- The intensity and timelines of the supervisory approval process.

Question 4

Do you agree with the assessment of costs and benefits of these proposed draft RTS?

Answer: Yes we agree with these aspects. As stated above, for banks operating under IRBA a change in the existing materiality thresholds has a significant impact and therefore the process of implementing necessary adjustments relating to the IT systems, processes, credit risk parameter settings and rating models is costly and time intensive.

Question 5

What is the expected impact of these proposed draft RTS?

Answer: A longer time period would be needed to assess the expected impact. This time period as well as the impact depends on the first three factors stated under Q3: data availability in the requisite form needed, necessity of historical data adjustments, and the number of credit risk parameters and models to be validated and recalibrated.