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31 January 2015

European Banking Authority
Floor 46
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Your ref: EBA/CP/2014/32

Dear Sir/Madam

Draft Regulatory Technical Standards on Materiality Threshold of Credit Obligations Past Due under Article 178 of Regulation (EU) 575/2013

Barclays welcomes the opportunity to comment on the EBA's Draft Regulatory Technical Standards on the Materiality Threshold of Credit Obligations Past Due and valued the opportunity to attend the EBA's public hearing this month. We thought it would be helpful to divide our response into two sections: Section 1 - General Comments and Section 2 - Consultation Questions.

Section 1: General Comments

Barclays welcomes the attempt to maintain a balance that avoids undue complexity with a desire to improve harmonisation. Barclays recognises that differing definitions of default and materiality thresholds contribute to divergences in RWAs and resolving the differences will assist with moving towards RWA comparability.

Clarity of Rule: In order for the RTS to achieve its objective, the final rules developed need to be clear and simple in order to minimise the different interpretations that could arise. It would be helpful to include worked examples in the final rules to demonstrate the meaning, for example, to clarify whether the absolute threshold is related to the size of any excess or the size of debt.

Risk Management and the Threshold: Barclays considers that the approach should be flexible enough to align with risk management. The thresholds proposed do not work for all categories of non-retail and a size consideration needs to be included to differentiate between (a) retail and small non-retail and (b) large non-retail.

Alignment with other initiatives: Barclays understands that the EBA will be issuing a further consultation on all aspects of Article 178, definition of default, including guidance on how to count days past due in a consistent way. BCBS will also be issuing consultations aimed at reducing RWA variability. In addition the IFRS9 guidance will impact the definition of default and therefore needs to be taken into account. It is important that any changes proposed need to be fully aligned and integrated with any proposals from BCBS and also the IFRS9 guidance.

Disclosures: In order to improve RWA comparability, transparency will be an important factor. Barclays considers that there should be a disclosure requirement for firms to show how they have interpreted the final RTS requirements, as this is more likely to drive RWA consistency and enables issues to be addressed.

Operational Impacts/Implementation: it is important to keep the final solution or approach as simple and clear as possible in order to minimise the operational impacts and also a realistic period of grandfathering and phase in to enable any models and systems development to take place. In addition grandfathering will reduce the strain on competent authority resources by avoiding the need for applications for approval to be submitted for all IRB models.

We thank you for your consideration of our letter and answers to the consultation questions and should this be of assistance, we would welcome opportunities to engage further with the EBA in assisting to develop the technical standards and the approach in this area.

Yours faithfully

William Hayward
Director, Prudential Regulatory Risk
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Section 2: Consultation Questions

Q1: Do you agree with the approach proposed in the draft RTS (option 1) that default should be recognised as soon as one of the components on 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)?

Barclays would not support the introduction of either option 1 or option 2 in their current form. This is because Barclays would recommend a simplified approach, which is a modification of option 1 and option 2. Barclays proposes a modification to reflect the difference in the nature between (a) Retail exposures and small non-retail and (b) Large non-retail, and their consequential risk management. Barclays recommends the following:

(a) Retail exposures and small non-retail exposures: There should be a single defined absolute threshold limit which is consistent across all exposures because it is clear and practical as it enables efficient management of a large volume of small exposures for which the process would be typically automated. A relative threshold is not considered necessary or helpful.

(b) Large non-retail exposures: Unless the absolute threshold is set at a sufficiently meaningful level, there should only be a relative threshold limit for large non-retail exposures as this will reduce the volume of technical defaults which are not actual defaults.

Q2: Do you agree with the proposed maximum levels of the thresholds?

In practice due to the differences in the nature of large non-retail exposures and retail and small non-retail exposures, for risk management purposes a different threshold is required. Barclays recommends the following:

(a) Retail exposures and small non-retail exposures: Barclays does not disagree with the proposed threshold of Euro 200, but consider that there should be flexibility to operate lower thresholds should a bank judge it appropriate for risk management or operational purposes.

(b) Large non-retail exposures: Barclays considers that a proposed threshold of Euro 500 is too small for large multi million Euro exposures and would not be an appropriate measure for default. Barclays considers that there should be a relative threshold for such exposures to reflect the size of the loan and risk.

(c) Errors due to administrative oversight: Barclays supports the introduction of clear and consistent thresholds but notes that current UK interpretation (BIPRU 4.3.61) recognised that errors and mistakes can occur. Where the firm holds sufficient information and evidence that the 90 days past due default trigger is purely administrative in nature, a PD of 1 may be adjusted to the previous recorded PD. Barclays would propose retaining these current procedures for administrative oversights, which are controlled by Credit, regardless of new materiality thresholds.

Q3: 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?

Without flexibility in interpretation modifications to models and systems will be required which will involve a significant amount of development and implementation time. In practice this is likely to span a few years and so it is important to allow 'grandfathering' of current approaches whilst the changes are phased in. If such a 'grandfathering' period is not permitted this will lead to strain on resources and operational difficulties both within firms and also for national competent authorities who would be required to review and reapprove all existing IRB models.

Q4: Do you agree with the assessment of costs and benefits of these proposed draft RTS?

At present the full implementation costs are not quantified as to the extent to which firms will be permitted to 'grandfather' existing interpretations which are more conservative. If a full rebuild of all existing IRB models is required, it is probable that the implementation costs will have been understated.

It is not wholly apparent how much of the RWA variability in evidence across member states is attributed to the inclusion of technical defaults. All other things being equal (i.e. there is no wide scale restatement of LGD models) for firms such as Barclays, who operate a lower absolute threshold for retail and small non-retail exposures, the level of capital held will fall if a higher default threshold is mandated.

For large non-retail, if the thresholds are maintained at the proposed RTS levels this will result in additional technical defaults and the need to unnecessarily hold capital against technical defaults rather than actual defaults.

Q5: What is the expected impact of these draft RTS?

At present it is too early to judge what the impact of the draft RTS alone will be.

As the RTS permits competent authorities the scope to set different thresholds, it will not remove RWA variability and will therefore defeat the objective of the proposed RTS.

Barclays agrees that this needs to be considered as part of the overall activity related to Article 178 definition of default and alongside the proposed BCBS measures that are being developed.