

# KBC response to EBA/CP/2013/07

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Below you find the answer of KBC to the questions posed as well as a proposal for the allowance of other information requirements when the detailed information is too costly to come by.

In summary, we ask for clarification about the calculation of the exposure value and propose some ways of calculating this.

**Q1: Is the treatment provided in Article 5 sufficiently clear and do the examples provided appropriately reflect this treatment?** Yes, the examples are a good way to clarify the texts, but we still have some questions on how the exposure value to a transaction will be calculated and on how to treat the situation where only a part of the underlying exposure and obligors are known. For our questions related to the exposure value, see our response to Q2.

Our other set of questions relate to the treatment of the situation where a bank has a part but not all underlying asset information. We will ask our questions by presenting a potential situation.

Suppose a bank holds an ABS transaction consisting of 500 underlying exposures and obligors and the volume of the transaction is 100. Further suppose that the bank has information for 350 underlying exposures and obligors and these 350 account for 80% of the volume.

For this transaction, which part has to be assigned to the single, unknown client?

- 100 as the full volume has to be assigned because not all underlying exposures and obligors are known?
- 20 as this is the volume of the part which the bank cannot assign to individual obligors?

We believe that a bank who can prove a part of the composition of its transactions should be allowed in this case to assign in this case 20% of the total transaction exposure to the same, single unknown client instead of 100%.

**Q2: Is there an appropriate alternative way of calculating the exposure values in the case of securitizations, which would be compatible with the large exposures risk mitigation framework as set out by the draft CRR?**

Due to the examples provided, we are unclear about the amount that needs to be used for the exposure value. Is it possible to define which of the following amounts need to be used: original notional of a securitization, the adjusted notional and the mark-to-market valuation?

Suppose we buy a RMBS that at origin has the same underlying portfolio than in example 1. If we have to evaluate the exposure value after 5 years where all underlyings are 25-year mortgages with linear capital pay downs and suppose no credit events have happened, then all underlying assets' notional have to be reduced to 80% of its original value. We call this new notional the adjusted notional.

Now suppose even further that the market conditions for this RMBS have significantly worsened (but without credit events) and the mark-to-market valuation shows a significant loss, then this RMBS (if in a trading book) would be marked-to-market and thus a loss would be taken for this securitization. In our example let's suppose the market value has been reduced to 3.

How should the exposure value be calculated in this instance? We propose three situations of which we believe the third one to be the most appropriate for trading book exposures, while the second is the most appropriate for banking book exposures:

1. **Using the original notional:** In the same way as in example 1, meaning 5 to underlyings A and B, 2 to underlyings C to F and 1 to underlyings G and H
2. **Using the adjusted notional:** in the same way as in example 1, but now having 4 to underlyings A and B ( $1/5 * (25 * 80\%)$ ), 1.6 to underlyings C to F ( $1/5 * (10 * 80\%)$ ) and 0.8 to underlyings G and F ( $1/5 * (5 * 80\%)$ )
3. **Using the lower of the market value of the securitization and the method of calculating using the adjusted notional:** we would now have 3 to underlyings A and B ( $=\min(3; 1/5 * 25 * 80\%)$ ); 1.6 to underlyings C to F ( $=\min(3; 1/5 * 10 * 80\%)$ ) and 0.8 to underlyings G and F ( $=\min(3; 1/5 * 5 * 80\%)$ ).

We thus believe that the market value should be used if securitizations are marked-to-market. The effect of the credit event/default can then not be more than the remaining market value.

**Q3: Would the application of requirements provided by Article 6 (3) and (4) imply unjustified costs to the institutions? Would the introduction of a materiality threshold be justified on a basis of a cost-benefit analysis? Please provide any evidence to support your response.** Similar to our response on question 5, the cost-benefit analysis will always be negative for a bank if the benefit is zero. The benefit would be zero in cases where the bank does not have enough exposure to securitizations to breach the 25% threshold even if all this exposure would be assigned to the same, single unknown client. Any cost made for getting the information would then be unreasonable if solely this large exposure legislation proposal would be taken into account.

**Q4: Keeping in mind that such materiality threshold would need to be sufficiently low in order to justify that all unknown underlying assets of a single transaction would be assigned to this transaction as a separate client, what would be the right calibration? Would the reference value (the institution's eligible capital) be appropriate for this purpose? Please provide any evidence to support your response.** The banks eligible capital seems appropriate.

**Q5: Would the requirement to monitor the composition of a transaction at least monthly, as provided by Article 6 (5), imply unjustified costs to the institutions? Please provide any evidence to support your response.** The cost-benefit analysis of monthly monitoring can only be negative for a bank if the benefit is zero. The benefit would be zero in cases where the bank does not have enough exposure to securitizations to breach the 25% threshold even if all these exposures would be assigned to the same, single unknown client. Any cost made for getting the information would then be unreasonable if solely this large exposure legislation proposal would be taken into account.

It would be beneficial that banks that can demonstrate that their exposure in credit securitization is far below the threshold would not be required to monitor the detailed construction of its securitizations.

**Q6: Are there other conditions that could be met by the structure of a transaction in order to not constitute an additional exposure according to Article 7?** No, not that we know of.

**Extra: alternative information requirements for banks when detailed underlying assets information is too costly to come by**

Suppose an European bank holds an ABS portfolio consisting of 80% American RMBS and 20% Asian RMBS. If the bank is not able to monitor the thousands of different underlying assets within this portfolio, it has to assign the total exposure value of the portfolio to the same, single unknown client. We believe that a bank who can prove the composition of its portfolio should be allowed in this case to assign 80% of the total portfolio exposure value to the same, single unknown client instead of 100%.

For a more real live securitization portfolios example, we believe that banks should be allowed to demonstrate the composition of its securitization portfolio along two high level dimensions.

- Underlying asset type (corporates, SME's, retail)
- Geography (Europe, America, Asia)

<b>Geography/Underlying obligor type</b>	<b>Corporates</b>	<b>SMEs</b>	<b>Retail</b>
Europe	15%	1%	4%
America	50%	0%	15%
Asia	11%	1%	3%

If a bank is capable of deconstructing its securitization portfolio along these two high level dimensions, we believe the regulation could state that for example the sum of the two biggest percentage weight (50%+15%=65%) should be added to the single, unknown client instead of 100%. Perhaps an add-on could be added to the 65% to account for any possible miscalculation as some generalization has to be made.

This method of working is still in accordance to the objectives of the large exposure regulation while at the same time it eases the information requirements for the banks as only two high level dimensions must be known. This will require less workload for the banks than identifying and tracking all underlying obligors by name.