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The Deputy Director General

November, the 2nd 2005

FBF RESPONSE ON GUIDELINES ON THE IMPLEMENTATION, VALIDATION AND ASSESSMENT OF ADVANCED MEASUREMENT (AMA) AND INTERNAL RATINGS BASED (IRB) APPROACHES CP10

Dear Mr Roldan,

The French Banking Federation (FBF) welcomes the opportunity to comment on CEBS' consultation document about the European procedures that supervisory authorities are expected use in processing, assessing and making decisions on an institution's implementation of the Advanced Measurement (AMA) or the Internal Ratings Based (IRB) approach for regulatory purposes.

We welcome the objectives of CEBS to continue to work towards convergence on the implementation of the IRB and AMA approaches. Our following general remarks would like to contribute to a consistent and practical execution for banking industry :

- FBF wonders what are the status of this document and the use regulators will make of it. What is expected from each national supervisor ? To follow strictly the guidance, to choose part of it ? Or can he ignore it ? What is the level of discretion left to him ?
- FBF does not clearly understand why this document has been published now. Is it in order to enable banks to know precisely what will be required from them in the application form, or to define the national discretion areas ? FBF hopes that this document is only a first step in the right direction and asks CEBS to clarify its intentions or definitions.
- The industry is now in a pre-validation phase, based on requirements issued by national supervisors in line with the form that banks currently apply. The FBF urges CEBS to take account of this situation and to include all these pre-validation works in the validation process.

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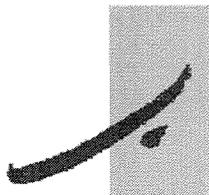
- The proposals are very prescriptive and much more precise than the Capital Requirement Directive (CRD), but this high level of details is not helpful and sets unnecessarily high standards. CEBS proposals include requirements which go further than CRD's field and some terms used in this document and the CRD one are confused.
- The documentation required (procedures, processes, policies...) for the internal practices of a group and all of its entities is incredibly detailed and does not add value in home/host issues.
- The guidance is overly burdensome as regards how a bank must structure its internal governance. These proposals must be checked to be made coherent with the issues raised by the Basel Committee on Banking Supervision (BCBS) consultation on corporate governance. We believe that the proposed standards are excessively intrusive and interfere too largely with the responsibilities of both the supervisory and management functions. While the Industry agrees that management implication is a key to good management, particularly on risk issues, it considers that the proposed internal governance guidance implies such an organisation and management process, that it may not be appropriate and would eventually infringe upon the fundamental responsibilities of both the supervisory and executive management bodies.

Please find our specific remarks in annex.

Yours sincerely



Pierre de Lauzun



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Specific remarks

- § 23: FBF thinks that this sentence should be taken off : “However, as these guidelines are neither comprehensive nor exhaustive, supervisors may impose stronger or more details requirements than those listed in the guidelines”. It leaves an open-door for increasing more specific supervisor requirements. CEBS has to promote necessary requirements that will be defined on a common basis and not on an unlimited area.
- § 38: The interaction between the pre-application phase and the application process is unclear. Banks do not want to go through *multiple qualification processes*. The *formal application stage* should only be the conclusion of the pre-approval work and must avoid any overcharge.
- § 47: The word “legally” should be deleted because it is confusing and adds nothing more.
- § 48: The official application form should be built on the outcome of the pre-validation phase and must not mean the replicating of what has already been done. We found the wording “official and legally binding statement” of the application as unclear -to say the least-, and as unfair to say that banks do not commonly provide their supervisors with reliable or honest documents. In addition, we believe that the application form is mainly directed to the home supervisor and cannot be construed as the best media to exchange information between home and host supervisors: it may be complicated or it may require explanation and investigation, or it does not convey the assessment of the supervisor on the bank’s compliance with the CRD requirements. We therefore suggest that the supervisors develop a kind of “qualification certificate or passport” to help the information flow among supervisors and not only European ones.
- § 67 : Banks are concerned with the burden and cost of translation that this paragraph could impose. Policies, internal models processes, systems are numerous and their full documentation can not be

gathered within the comprehensive application file which CEBS refers to. We recommend that no more than 2 languages may be requested for the most basic documents and that only the operational language is used for the more technical processes and associated documentation and procedures. Only summaries and abstracts should be made available in a handy manner and only on site investigation.

- §132 : Delete “eg between a pricing PD and the rating PD”. The reference to pricing PDs should be taken off. We do not think that regulators should look at pricing policies. We hope the wording used does not mean restricting the way banks intend to manage their risk and more generally their business. For example, allocation of internal capital should neither be an obligation nor necessarily be based on regulatory capital. This comment is also worth for pricing.
- §133 : The text says : “This relationship needs to be documented clearly, and any differences validated and explained to supervisors.” Though this sentence could be understood as standard internal control practice (process documentation and internal audit review), the banks would be concerned if Supervisors translate this recommendation into a requirement for detailed documentation of any difference and a specific validation process involving an independent entity still to be identified. We would suggest : “This relationship should be explained in the general documentation of the related process, and internal control procedures should include an appropriate level of control on material differences.”
- § 146-149 : We are not sure to correctly understand what is the experience test period: is it the period before regulatory use is authorized, when banks may use rating systems broadly in line –and not fully compliant– with minimum requirements and when default and loss estimates don’t yet play an essential role in the bank’s risk management, credit approval and internal capital allocation?
- § 205 : The Industry does not agree with the detailed definition of “work out” and “collection cost”. The concept of “indirect cost” is highly debatable and inclusion of corporate overhead is very arguable and is not a standard practice.
- § 240 and after : It seems to us that regarding CF, only undrawn amounts of commitments are dealt with in the text. Nothing is said about the way to calculate own estimates of CF (conversion factor) on guarantees given by the bank.
- § 258 : We don’t understand why banks will not be allowed to mix internal and supervisory estimates in a single legal entity. Without intent of regulatory arbitrage, we think that one must consider differently CF on undrawn amounts of commitments and CF on guarantees given by the bank, and that it should be possible to mix internal estimates for one category and supervisory estimates for the other.

- § 306 : Similarly to the remark on §133, this paragraph could be understood as an internal control standard practice recommendation (data quality controls and internal audit review); however, the Banks would be concerned if Supervisors translate this recommendation into a requirement for specific controls and validation process, involving systematically an independent party still to be identified. We would rather suggest: "All data referred to in §292 should be subject to appropriate quality controls, according to their criticality."
- § 352 : What does "quantitative validation" mean for Low Default Portfolios? At different parts of the CP10, the CEBS refers to benchmarking, which could be understood as one possible technique for the "quantitative validation" referred to. However, benchmarking is possible only if banks make relevant data public, which is usually not the case.
- § 437 and § 448 : We suggest to delete the examples as we believe that they may be retained as local requirements.
- § 452 : The reference to section 3.5.1 is unclear as it refers to the IRB approach. This is a potential source of misunderstanding. The paragraph should be reworded and adapted according to the AMA approach.
- § 455 & 456 : We do not intend to combine the four elements of operational risk using a weighted average. There are other possible methods. The words "weighting" (§455) and "weighted" (§456) should be removed, "combined" is enough.
- § 456 : The second bullet point should be deleted as it is deemed redundant with the first bullet point
- § 481
5th bullet point : We do not think that external loss experience must be systematically included in the reporting. We would rather suggest : "internal loss, and external loss when appropriate".