Febelfin

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Committee for European Banking Supervisors
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By email: cp31@c-ebs.org

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CP 31, Management of concentration risk under the supervisory review process, Febelfin comment

Dear Sir,

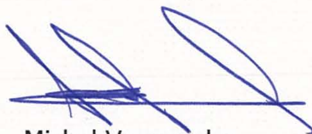
Febelfin, i.e. the Federation which regroups four trade associations from the Belgian financial industry[1], welcomes the opportunity to express its views on the consultation document mentioned above.

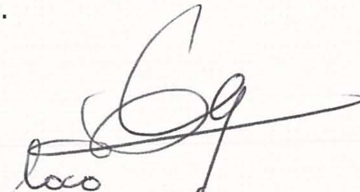
Our members are of the opinion that the existing rules for concentration risk would seem to be sufficient to coop with concentration risk. We fear that the proposed guidelines add too much detail to the existing management of concentration risk and will therefore be very burdensome to implement, especially for smaller institutions. We therefore advocate that in the application of the proposed guidelines, the proportionality principle is taken into account.

While the change of certain procedures could be supported, we advocate that the internal models which are used to measure credit concentration risk ought not to be changed.

We hope that our remarks will be taken into account. Please do not hesitate to contact our services and our working group, should you want any further information.

Yours sincerely,





Michel Vermaerke
Chief Executive Officer

Daniel Mareels
General Manager

cc. Mr. Jean-Paul Servais, Chairman, Banking, Finance and Insurance Commission.

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[1] The following trade associations are constituents of Febelfin: the Belgian Bankers' and Stockbroking Firms' Association (ABB/BVB); the Professional Union of Credit Providers (UPC/BVK); the Belgian Asset Management Association (BEAMA), the Belgian Leasing Association (BLA). In addition, the following federations have joined Febelfin as associate members : the Belgian Private Banking Association, the Belgian Private Equity and Joint Venture Association. Equally, other financial market infrastructure providers, such as Euroclear, SWIFT and Euronext have taken the status of associate members.

CP 31, Management of concentration risk under the supervisory review process, Febelfin comment, annex

General comments:

In our view the existing rules for concentration risk are more than sufficient to coop with this kind of risk. We fear that the proposed guidelines add too much detail to the existing management of concentration risk and will therefore be very burdensome to implement, especially for smaller institutions. We therefore advocate that in the application of the proposed guidelines, the proportionality principle is taken into account.

For example it remains unclear to us how we could link the proposed definition of inter-risk to established definitions of connected clients.

We would appreciate more clarification on the relationship between CP31 and the recently amended large exposures rules.

Guideline 1: The general risk management framework of an institution should clearly address concentration risk and its management.

Paragraph 22: we propose to change the wording as follows: "*The concentration risk policy should be adequately documented….. both at group and solo level, as appropriate*". We are of the opinion that entities which do not face material risks do not need to be included. Though including them will not have any meaningful impact on the data, preparing policies and procedures that apply at all group entities may be cumbersome and would not necessarily lead to better management of concentration risks.

Guideline 2: In order to adequately manage concentration risk, institutions should have an integrated approach for looking at all aspects of concentration risk within and across risk categories (intra- and inter-risk concentration).

No comment.

Guideline 3: Institutions should have a framework for the identification of intra- and inter-risk concentrations.

We agree that institutions should be allowed to assess themselves which risk concentrations are significant. This is of particular importance where uncommitted exposures are concerned. When uncommitted credit lines, for example, can be cancelled unilaterally with immediate effect, or when such lines can only be drawn against good quality collateral, risk concentrations are unlikely to materialise.

Guideline 4: Institutions should have a framework for the measurement of intra- and inter-risk concentrations. Such measurement should adequately capture the interdependencies between exposures.

No comment.

Guideline 5: Institutions should have adequate arrangements in place for actively controlling, monitoring and mitigating concentration risk.

Paragraph 35: We propose to change the wording as follows: "*An institution should set top-down and group-wide concentration risk limit structures, as appropriate*"

With regard to mitigation techniques: we agree that institutions should not over-rely on specific mitigation instruments. However, not all instruments are equal in that respect. For example, reliance on collateral in the form of well-rated government bonds can be considered as an effective mitigation measure, irrespective of the concentration in such instruments.

Guideline 6: Institutions should have adequate arrangements in place for reporting concentration risk. These arrangements should ensure the timely, accurate and comprehensive provision of appropriate information to management and the management body about levels of concentration risk.

Paragraph 43: We propose to change the wording as follows: "*The reports should include information at both consolidated and solo levels, as appropriate, spanning business lines, geographies and legal entities.*"

Guideline 7: Institutions should ensure that concentration risk is taken into account adequately within their ICAAP and capital planning frameworks. In particular, they should assess, where relevant, the amount of capital which they consider to be adequate to hold given the level of concentration risk in their portfolios.

Paragraph 47: We note that the calculation of a net exposure to concentration risk is only meaningful for realised exposures. Uncommitted credit lines that would only be used against good quality collateral should not be taken into account, as noted under Guideline 3.

Paragraph 50: We note that *"common main sources of funding"* are difficult to assess if not publicly disclosed.

Guideline 8: Institutions should employ methodologies and tools to systematically identify their overall exposure to credit risk with regard to a particular customer, product, industry or geographic location.

No comment.

Guideline 9: The models and indicators used by institutions to measure credit concentration risk should adequately capture the nature of the interdependencies between exposures.

We note that paragraph 12 of the consultation document states that: '*the implementation of some specific aspects of the guidelines may require modifications to institutions' current procedures*'.

While the change of certain procedures could be supported, we advocate that the internal models which are used to measure credit concentration risk ought not to be changed.

Guideline 10: An institution's assessment of concentration risk should incorporate the potential effect of changing liquidity horizons

No comment.

Guideline 11: Institutions should clearly understand all aspects of OPRC in relation to their business activities.

We feel that the definition and understanding of operational risk concentrations still needs to be further refined.

HFMI and LFHI loss events should only be considered as contributing to concentration risk if they

have a common cause (which may be, for example, inadequate controls or procedures). Otherwise, there are no indications that this is not pure coincidence.

Guideline 12: Institutions should use appropriate tools to assess their exposure to OPRC.

Paragraph 79: We feel it necessary to precise that the role of Internal Audit is not to assess exposures to risk but to ensure that existing procedures are adequate and adequately applied.

Guideline 13: In order to be able to identify all major kinds of liquidity risk concentrations, institutions need to have a good understanding of their funding structure and be fully aware of all underlying influencing factors over time. When relevant, depending on its business model, an institution should be aware of the vulnerabilities stemming form its funding structure, e.g. the proportions of retail and wholesale funding. Also, when relevant, the identification of liquidity risk concentrations should include an analysis of geographic specificities. Finally, the identification of concentrations in liquidity risk should take into consideration off-balance sheet commitments.

Paragraph 91: We wonder what is meant by "non-contractual commitments" (as contractual commitments are illustrated at length). To our understanding, if there is no contract, there is no commitment.

Paragraph 91: We propose to change the wording as follows: "*Another important factor influencing liquidity risk concentration is off-balance sheet items, as appropriate*".

Guideline 14: In identifying their exposure to funding concentration risk institutions should actively monitor their funding sources. A comprehensive analysis of all factors that could trigger a significant sudden withdrawal of funds or deterioration in their access to funding should be performed.

No comment.

Guideline 15: The qualitative assessments of concentrations in liquidity risk should be complemented by quantitative indicators for determining the level of liquidity risk concentration.

No comment.

Guideline 16: Institutions should take into account liquidity risk concentrations when setting up contingency funding plans.

No comment.

Guideline 17: Supervisors should assess whether concentration risk is adequately captured in the institution's risk management framework. The supervisory review should encompass the quantitative, qualitative and organisational aspects of concentration risk management.

No comment.

Guideline 18: In cases where supervisory assessment reveals material deficiencies, supervisors, if deemed necessary, should take appropriate actions and/or measures set out in the Article 136 of the CRD.

No comment.

Guideline 19: Supervisors should assess whether institutions are adequately capitalised and have appropriate liquidity buffers in relation to their concentration risk profile, focusing on buffers (liquidity and capital) in relation to the unmitigated part of any concentration risk.

We advocate that requiring extra capital above the minimum requirements should be a measure of last resort only.

We note that the guideline refers to the 'unmitigated part of any concentration risk'. We do not agree with this approach and are of the opinion that the guideline should take into account the existing rules on concentration risk.

We also note the difficulty for IRB banks in this regard. In contrast to SA banks, the IRB method does not allow to make a difference before and after risk mitigation.

Guideline 20: Supervisors should assess whether concentration risk is adequately captured in firm-wide stress testing programmes.

No comment.

Guideline 21: Supervisors should pay particular attention to those institutions which are highly concentrated, e. g. by customer type, specialised nature of product or funding source.

We do not consider that there should always be a "*positive relation between the degree of concentration and the level of capital*". This will depend on how much risk this concentration brings. For example, concentration in less risky business lines, or in long-term stable funding sources, or concentration of mitigants in well-rated government bonds should not be penalized.

Annex 1

No comment.

Annex 2

We would appreciate if annex 2 could be elaborated and integrated into the guidelines. As currently proposed, the enumeration of a number of 'indicators' does not allow a clear understanding of how regulators would like to see evolve the management of concentration risk.