BBVA Creating Opportunities

BBVA comments on ECB Guide on ICAAP

BBVA welcomes the ECB's publication of the draft Guide to the Internal Capital Adequacy Assessment Process (ICAAP) and the opportunity to comment on it. We see this Guide as being part of the ECB's ongoing efforts to provide transparency on its expectations on the ICAAP and on ICAAP requirements, following from Article 73 CRD IV, and to assist institutions in strengthening their ICAAP and at encouraging the use of best practices. We, therefore, appreciate the ECB's efforts to improve the ICAAP framework and for our part, we also fully commit to working together with supervisors to make ICAAP play a key role in the risk management of institutions and also in the supervisory practices, as it feeds into the Supervisory Review and Evaluation Process (SREP).

Before going into the template with detailed comments, our general assessment of this Guide is very positive, since we consider it incorporates the supervisor flavour (as compared to the narrower regulatory vision of the EBA Guidelines of February 2017), which brings it much closer to our management approach. Specifically, we quite sympathize with concepts such as i) ICAAP-based risk-adjusted performance indicators (para. 23), ii) ICAAP as an ongoing process (para. 26), iii) consistency and coherence between ICAAP and recovery planning (para. 32), iv) capital adequacy at relevant levels of consolidation and for relevant entities within the group (para. 33) or v) aiming for sufficient management buffers over the medium-term horizon (para. 35).

#	Chapter	Paragraph	Page	Type of comment	Detailed comment	Concise statement as to why your comment should be taken on board
1	1	3	2	Clarification	According to this introductory paragraph "In the ECB's view, a sound, effective and comprehensive ICAAP is based on two pillars: the economic and the normative perspectives". Both perspectives are expected to complement and inform each other".	We sympathize with this, however, paragraphs 38 and following, in our opinion, tend to blur both perspectives; in particular, it seems to us that the economic perspective could end up being contaminated by certain normative requirements, jeopardizing the credibility of the model and limiting its usefulness for internal capital management.
2	P1	15 and 21	5 and 6	Amendment	According to the guide, "The management body is expected to produce and <u>sign</u> the CAS […]". "The authority to sign the CAS on behalf of the management body is expected to be decided by the institution in light of national regulations and relevant prudential requirements and guidelines…"	Please note that the formal execution of the CAS would not increase the stringent diligence duty the management body has to comply with in each and all of its decisions, and it would add more operational complexity. Additionally, the expectation that the document is signed on behalf of the management body is a mere formality which is not consistent with the decision-

						making process of the management bodies (through voting majorities) foreseen in national regulations. Therefore, we suggest amending the wording as follows: "the management body is expected to produce and approve the CAS."
3	P1	15	5	**Amendment / Deletion**	"The management body is expected to […] approve the key elements of the ICAAP, for example: the governance framework; internal documentation requirements; the perimeter of entities captured, the risk identification process, and the internal risk inventory and taxonomy, reflecting the scope of material risks; risk quantification methodologies, including high-level risk measurement assumptions and parameters (e.g. time horizon, diversification assumptions, confidence levels, and holding periods), supported by reliable data and sound data aggregation systems; methodologies used to assess capital adequacy (including the stress-testing framework and a well-articulated definition of capital adequacy)."	The management body defines and oversees the implementation of the strategy, key policies and governance arrangements to ensure effective and prudent management of the institution (EBA guidelines on internal governance, Title II, section 1). The operational implementation of these strategies on a day-to-day basis, on the other hand, corresponds to the senior management. In our opinion, some of the elements listed as examples of those matters expected to be approved by the management body (such as the "internal documentation requirements" or the "risk identification process") cannot be considered "key" or strategic elements of the ICAAP. Instead, they are part of the day-to-day capital management and, as such, within the remit of the senior management. In particular, we suggest the following amendments / deletions: ● Delete "internal documentation requirements" for its minor relevance; ● Amend the reference that the management body is expected to approve "the risk identification process and the internal risk inventory and taxonomy"; as it is not consistent with paragraph 57, stating that the management body is also responsible for deciding which types of risk are material and to be

						covered with capital. ● Amend the paragraph regarding "risk quantification methodologies", including a reference to the governance framework and the role and responsibilities of the management body regarding risk quantification methodologies and ICAAP established in other ECB Guides and supervisory guidelines, to ensure consistency.
4	**P1**	**17**	**6**	**Clarification**	"According to Article 73 CRD IV, the ICAAP shall be subject to regular internal review Both qualitative and quantitative aspects, including, for example, the use of ICAAP outcomes, the stress-testing framework, risk capture and the data aggregation process, are expected to be considered by this regular internal review,7 including proportionate validation processes for internal risk quantification methodologies used. For this purpose, the institution is expected to have in place adequate policies and processes for internal reviews".	We would like to have further clarification on the expectation about this point, mainly regarding roles and responsibilities of second and third lines of defense.
5	**P2**	**33**	**10**	**Clarification**	"The ICAAP is expected to ensure capital adequacy at relevant levels of consolidation and for <u>relevant</u> entities within the group, as required by Article 108 CRD IV."	The scope of the ICAAP as foreseen in this paragraph is not clear. We understand that the reference to "relevant entities" should be interpreted as "applicable entities" (i.e. those entities individually falling under the scope of Article 108 CRD IV). This understanding is in line with paragraph 11 of the guide ("[…] a parent institution in a Member State […] shall meet the ICAAP obligations set out in Article 73 CRD IV on a consolidated basis"). The current wording of this paragraph could also be interpreted as a requirement that parent institutions' ICAAPs should also cover "significant" (relevant) subsidiaries' ICAAPs. However, this interpretation would not be consistent with the scope of Article 108 CRD IV and disregards the fact that

						subsidiaries may be subject to their own individual ICAAP requirements under local regulations. We suggest replacing “relevant entities” with “applicable entities”.
6	**P3**	**38**	**12**	**Clarification**	The statement that "the normative perspective is not limited to the Pillar 1 risks recognised by the regulatory capital requirements. When assessing its capital adequacy under the normative perspective, the institution is expected to take into account all relevant risks it has quantified under the economic perspective" seems to blur normative and economic perspectives.	In our opinion, normative perspective should stick to Pillar 1 risks; other risks are considered within P2R. Current wording hybridizes normative perspective with economic perspective, leading to confusion.
7	**P3**	**49**	**18**	**Clarification**	The expectation "to assess under the normative perspective the extent to which the risks identified and quantified under the economic perspective may impact on its own funds and total risk exposure amount (TREA) in the future. Hence, the projections of the future capital position under the normative perspective are expected to be duly informed by the economic perspective assessments" again, seems to blur normative and economic perspectives.	In our opinion, normative perspective should be independent from economic perspective. The current wording hybridizes normative perspective with economic perspective, leading to confusion.
8	**P5**	**66 (Ex. 5.1)**	**27**	**Clarification**	“Example 5.1: internal capital definition starting from regulatory own funds” suggests that the internal capital definition should dismiss the value of certain items, which are expected to be deducted from regulatory own funds (eg. goodwill). Again, we think the model is somewhat perverted by hybridizing normative and economic perspectives.	In our opinion, normative perspective should be independent from economic perspective. Why should we consider that goodwill is economically worth zero by default, specially when having a diversified footprint? As regards DTAs, unlike the recovery, the ICAAP process is an exercise made under going-concern situation, in which case this type of items may very well have positive economic value.