Template for comments

Public consultation on the revised ECB guide to internal models

Institution/Company
German Banking Industry Committee

Contact person

Mr/Mrs
Mr

First name
Christian

Surname
Drefahl

Email address
c.drefahl@bvr.de

Telephone number
49228509424

☐ Please tick here if you do not wish your personal data to be published

General comments

Template for comments

Public consultation on the revised ECB guide to internal models

Please enter all your feedback in this list.
When entering feedback, please make sure that:
   - each comment deals with a single issue only;
   - you indicate the relevant chapter/section/paragraph, where appropriate
   - you indicate whether your comment is a proposed amendment, clarification or deletion.

Deadline:	15 September 2023

ID	Chapter	Section	Paragraph	Page	Type of comment	Detailed comment	Concise statement as to why your comment should be incorporated	Name of commenter	Institution	Personal data
1	General topics	1.8 General principles on climate-related and environmental risks	25	12	Amendment	We suggest to move the requirement mentioned in the first sentence to the respective risk specific chapters (e.g. paragraph 96 for credit risk) and delete the second sentence.	In general, we understand and accept emphasizing the requirements on the consideration of climate-related and environmental risk drivers in internal models. The proposed concept is fully in line with the common social and political efforts to build a more sustainable economy. Moreover, they are consistent with the requirements in the Guidelines on loan origination and monitoring.

However, the first sentence mixes the concepts of "risks" and "risk drivers". Certain climate-related and environmental risks may constitute an own sub-category of non-financial risks, which are not in scope of this guide. However, with regard to financial risks like the ones covered in this guide, they are more of a (potential) driving force for existing financial risk categories. Therefore, their handling should be generally consistent with all other potential driving forces considered in internal models, e.g. obligor-related or financial information. Moreover, the second sentence is tautological. From the methodological perspective, it is a necessary condition for any internal model in place that all its risk drivers are relevant and material and vice versa, that all risk drivers found to be relevant and material are considered in the model. | Drefahl, Christian | German Banking Industry Committee | Publish |
| 2 | General topics | 1.9 General principles for the implementation of a changed or extended model | 26 | 12 | Amendment | If any pre-defined limit for the implementation period was deemed inevitable, it should not be less than 12 months. | The requirement in paragraph 26 to implement model changes within three months after notification of approval is hardly feasible in practice. Implementation of a materially changed model is quite complex and requires proper preparation. Often it is followed by an assessment of the changes by an independent function (typical internal audit), which must also be factored in. Thus, a more flexible approach is needed. | Drefahl, Christian | German Banking Industry Committee | Publish |

3	General topics	2.2 Application of the IRB approach	28	14	Amendment	In our view, exposures that have been permanently excluded from the application of the IRBA under Article 150 (a) and (b) CRR should be excluded from the IRB coverage ratio. Exposures in the form of a share in an undertaking for collective investment (CIU) within the meaning of Article 4(1)(7) CRR should also be excluded from the IRB coverage ratio.	In footnote 32, the ECB lists those exposures that should not be taken into account when calculating the IRB coverage ratio. On the one hand, these are exposures for which the CRR does not require the application of the IRBA. In this context, the ECB correctly wishes to exclude exposures that have been permanently excluded from the application of the IRBA under Article 150 (1) (d), (e), (f), (i) or (j) CRR. In our view, however, exposures that have been permanently excluded from the application of the IRBA under Article 150 (a) and (b) CRR should also be excluded with the same justification. In addition, the ECB would also like to exclude from the IRB coverage ratio those exposures which are IRBA exposures but which (at least in part) do not fall within the scope of a "normal" rating system (e.g. equity exposures or securitizations). In our view, exposures in the form of a share in an undertaking for collective investment (CIU) within the meaning of Article 4(1)(7) CRR should also be excluded from the IRB coverage ratio with the same justification.	Drefahl, Christian	German Banking Industry Committee	Publish
4	General topics	2.6 Reversion to a less sophisticated approach	41-45	17-19	Clarification	The guide should reflect Article 494d of the CRR III draft. This article introduces a deviation from Art. 149 on which the EGIM refers allowing for a simplified process. It should be clarified that legally required reversals (move to CR-SA for equity exposures and FIRB for exposures to large corporates, institutions and financial sector entities) do not trigger any application and approval process. Instead, an ex-ante notification including the date by which the change will be rolled out should be sufficient.	Revisions to less sophisticated approaches have been and will continue to be a key concern for institutions. Thus, in principle we support the attempt to clarify this issue with additional guidance. However, it should be noted that the respective level 1 requirements are about to change. With CRR III coming into force, the model landscape will change significantly and a whole new partial use philosophy will prevail. This should be anticipated and reflected in the EGIM.	Drefahl, Christian	German Banking Industry Committee	Publish
5	General topics	6.6 Assignment of exposures to grades or pools	103	42	Clarification	In our view, it should be clarified that only ratings that are solely based on outdated rating details are considered as outdated.	For instance, retail ratings are inevitably partially based on older rating details as some rating details are gathered only at application. This should not automatically lead to the rating itself being classified as outdated. For example, the use of financial statements for retail ratings should be defined more precisely. As no yearly update of financial statements is given for retail clients, institutions need to be able to use older financial statements without the whole rating being deemed outdated.	Drefahl, Christian	German Banking Industry Committee	Publish
6	General topics	7.5 Impact assessment	122	49	Clarification	Exceptions from the nine-month rule should be possible	The nine-months rule (requirement that the time between the reference date and the date of notification shall not exceed nine months) should be feasible in most cases. However, there might be cases where the snapshot has to be older. Exception for well documented cases should be possible, for example - Where external data delivery is needed for the calculation - Where manual input is needed for the re-rating	Drefahl, Christian	German Banking Industry Committee	Publish

7	General topics	8.3 Third-party involvement in internal functions and tasks	137	53	Amendment	In our opinion, this regulation – taking into account the regulation in Art. 4 (3) of Delegated Regulation 2022/439 ("RTS on assessment methodology") – should not be applied at third party level, but rather only at the level of individual rating models.	In paragraph 137 (d) EGIM, the ECB would like to clarify that third parties that have been involved in the development of rating models or have performed credit risk monitoring unit (CRCU) tasks in the past or that are currently performing these activities may only perform validation tasks for the institution after an appropriate cool-off period has elapsed. In this regard, we would like to note that the requirement in this generality contradicts Article 4 (3) of Delegated Regulation 2022/439 ("RTS on assessment methodology"), according to which, in the case of so-called pooled rating systems, third parties that have been involved in the development of a rating system may support institutions in the validation process by performing validation tasks that require access to the pooled data. In these cases, the external third party performs only parts of the validation actions. The results of the pool validation are not decided by the pool service provider, but by the independent validators of the institutions participating in the pool. Such a pool validation thus only serves as input for the independent internal validation of the respective institute, the result of which is also decided entirely by the institute's validation unit. The responsibility for the validation therefore remains with the institute. If the regulation were applied literally, external third parties would be forced to organizationally separate those entities that develop rating models for an institution from those that assist the institution in validation. Such a rule would interfere significantly with the business models of the external providers and require them to maintain an organizational separation not found even among the major accounting firms. It is of utmost importance in this context to bear in mind that an institution that receives validation support from an external third party cannot realistically ensure that this third party exclusively performs validation actions for its various clients. Especially in low-default portfolios, involvement in development issues (for a different model) can ensure a much stronger practical relevance for the validator. Calculated statistics in these portfolios often give only an incomplete picture, cannot be substantiated by statistical significance statements or ignore relevant correlations between borrowers. The underlying issues can only be learned with sufficient model experience and can only be evaluated correctly by supervising a model in cooperation with the technical contact persons. This is a particular challenge for external third parties.	Drefahl, Christian	German Banking Industry Committee	Publish

| 8 | Credit risk | 2.2 IT systems: infrastructure and implementation testing | 7 | 61 | Amendment | We advocate deleting the word "production" to ensure that the requirements mentioned can also be met in a simulation environment. | It is our understanding that the introduction of this chapter aims at improvements in two areas:
1) the ability to execute the model, i.e. to provide own funds requirements and impact assessments
2) the ability to provide evidence that the model is ready to be implemented in a timely manner after the approval.
If an institution applies for initial approval of a model, it should provide evidence that it has implemented the proposed model in a live or, if duly justified, in a non-live production environment, according to paragraph 7 of EGIM.

The explicit requirement is disproportionately burdensome. That is because it is not the only way to achieve sufficient improvements towards the above-mentioned key objectives while at the same time associated with severe drawbacks. We therefore advocate deleting the word "production" to ensure that the requirements mentioned can also be met in a simulation environment.

For instance, it should be sufficient that
1) at the time of model submission, institutions should be able to run high quality impact assessments in a timely manner on the new model utilising latest required input data. Subsequent impact assessments should also utilise the same model with the latest required input data to preserve integrity of the assessments.
2) institutions should be able to provide full evidence of the entire implementation of a model change in advance of the on-site audit review. This allows that the model is implemented end-to-end in a timely manner post approval. At the same time, business readiness should be embedded in the institution's policies and processes upon model submission. | Drefahl, Christian | German Banking Industry Committee | Publish |

| 9 | Credit risk | 2.2 IT systems: infrastructure and implementatio n testing | 8 | 62 | Deletion | Paragraph 8 should be dispensed with | The requirement regarding changes to existing models should take into account that, based on current experience, 2 to 3 years regularly pass between the notification of a significant model change and its approval*.

According to paragraph 8, it must be taken into account that the IT implementations are highly integrated into the credit processes. These rating systems and processes are always affected simultaneously by numerous requirements from different areas, which regularly make it necessary to continuously optimise and adapt the systems. Thus, if the complete IT implementation of an optimised rating system displayed with a model change indicator were to take place in a production environment, this implementation would have to be adapted in parallel to further optimisations of other aspects in the meantime. This process would be very time-consuming and cost-intensive, but also very error-prone.

Currently, it is common practice that applications for model approval are submitted after development has been completed and internal validation and internal audit have taken place? This is quite efficient and saves time overall, as the waiting time for approval - often up to 2 years - can be used for the IT implementation. If the latter has to be done separately in the future, already in advance, this will considerably prolong the entire process until go-live. In the end, this means that for bureaucratic reasons, any model weaknesses will be maintained for an unnecessarily long time or sensible model improvements will be held back for an unnecessarily long time. This is neither in the interest of the institutions nor in the interest of supervision.
Furthermore, it should be taken into account that if an optimised rating system is implemented, the change of which has been indicated by means of an MCPnotification, users in a production environment may use or be influenced by the rating grades determined from this optimised rating system in rating decisions of the rating system currently in use, or that this influence will be difficult to avoid.

Ultimately, the existing process with regard to model changes is sufficient with regard to the above-mentioned objectives.

* The problem of implementing a full IT implementation thus regularly arises only for substantial model changes, since in the case of insignificant model changes (MCP 2 model changes) only 2 months regularly elapse between notification of the model change and its approval (through confirmation of the category). | Drefahl, Christian | German Banking Industry Committee | Publish |

#	Category	Section	Para	Page	Type of comment	Detailed comment	Concise statement why your comment should be taken on board	Name	Organisation	Publish
10	Credit risk	3.2 Use of external data	38	70	Amendment	We propose to adjust the requirement so that negative analysis results are only a strong indication of bias and should therefore trigger further valid analyses. Remaining uncertainties can also be addressed by a category B MoC.	According to paragraph 38 EGIM, an institution may use external data even if it cannot sufficiently demonstrate that these data are representative. However, this is to be conditional on it demonstrating (through quantitative analysis or qualitative reasoning) that the information gained from the use of the external data outweighs any disadvantages arising from the identified deficiencies and that an appropriate margin of conservatism (MoC) is applied. In particular, institutions should demonstrate that the performance of the model does not deteriorate when information from the external data is included and that the parameter estimates are not biased. To assess these aspects, institutions are to conduct quantitative and qualitative analyses specifically designed for this purpose. In this regard, we would like to note that a testing approach, regardless of the statistical significance, runs the risk of drawing overly simplistic conclusions. We therefore propose to adjust the requirement so that negative analysis results are only a strong indication of bias and should therefore trigger further valid analyses. Remaining uncertainties can also be addressed by a category B MoC. Especially in portfolios with few defaults, a single default event with closely related borrowers at the institution level may lead to artifacts that could only be cured by economically inappropriate risk differentiation or quantification. If a large number of tests with the same direction are carried out for sub-samples (i.e. for portfolios of institutions) on the basis of a limited database, individual institutions must become conspicuous for statistical reasons alone. On the one hand, such an approach would run counter to the objective of avoiding excessive overfitting in the models (see paragraph 95 EGIM); on the other hand, it is precisely the participation in a data pool that can help in the assessment of relevant issues. Moreover, it would counteract the overall goal of avoiding RWA differences if such artifacts resulted in unjustified calibration differences between institutions. Such differentiations should therefore only be introduced if there is a sufficient data basis or a thorough analysis of the causes.	Drefahl, Christian	German Banking Industry Committee	Publish
11	Credit risk	3.7 Use of data in the case of consolidations	55, 57	76	Amendment	Institutions should be allowed to exclude not representative data where justified.	There might be cases where the default history of an acquired portfolio is not representative to an extent which cannot be healed by appropriate adjustments.	Drefahl, Christian	German Banking Industry Committee	Publish
12	Credit risk	4.2 Consistency of the application	62	79	Deletion	Proposed Rewording: The materiality thresholds for the purpose of the definition of default applied by an institution outside the SSM area and a parent significant institution may be different, even if both belong to the same banking group, because a materiality threshold which differs from the one set by the ECB may apply under national law outside the SSM area. This scenario is one of those addressed by paragraphs 83 to 85 of the EBA Guidelines on DoD.	It can be assumed that the number of clients having exposure under both, SSM and non SSM jurisdictions within one institution is very immaterial. Costs related to processes needed to identify those joint clients are therefore too burdensome for very little impact. Ultimately, the requirement of ECB would result in running the 90 dpd calculation for common clients at least twice.	Drefahl, Christian	German Banking Industry Committee	Publish
13	Credit risk	4.3 Days past due criterion	67	80	Amendment	We propose the following clarification in paragraph 67: "However, in the specific case of factoring **or leasing** arrangements where the purchased receivables are recorded in the balance sheet of the institution, if the counter at obligor level reaches 90 but none of the receivables to the obligor is more than 30 consecutive days past due at facility level, then this should be recognised as a technical past due situation according to paragraph 23(d) of the EBA Guidelines on DoD and the default should not be triggered."		Drefahl, Christian	German Banking Industry Committee	Publish
14	Credit risk	4.3 Days past due criterion	71, 73	81, 82	Amendment	It should be allowed to treat such defaults due to disputes similarly to the technical defaults.	In our view, there is a partial contradiction between the treatment of disputes (paragraph 71) and technical defaults (paragraph 73). In particular, according to the last sentence of paragraph 73, the ECB has the expectation that disputes are not treated as technical defaults. At the same time, paragraph 71 clarifies that disputes can lead to a DpD counting suspension. Consequently, it should be allowed to treat such defaults due to disputes similarly to the technical defaults. (if for example for technical reason a dispute is recognized after 90DpD, which might retrospectively lead to DpD suspension and thus should lead to similar treatment as the ones allowed for technical defaults).	Drefahl, Christian	German Banking Industry Committee	Publish

15	Credit risk	4.4 Unlikeness to pay criterion	77	83	Clarification	We propose the following clarification in paragraph 77: "When applying the formula, the sale price should be used without any type of adjustment. It should be noted that sales of credit obligations in the context of true sale securitisations where there is a significant risk transfer according to Article 244 of the CRR and the EBA Guidelines on SRT are also considered sales of credit obligations for the purposes of this unlikeliness to pay criterion."		Drefahl, Christian	German Banking Industry Committee	Publish
16	Credit risk	4.4 Unlikeness to pay criterion	79	84	Amendment	The requirement from paragraph 79 should at least be adjusted so that a present value calculation is only necessary if it is required for the default calculation (e.g., because there is no default yet and exceeding the 1% threshold is doubtful) OR if it is required for the LGD estimate. If neither of these is the case, a present value calculation should be dispensed with, as it then offers no added value and would cause disproportionate effort.	According to paragraph 79 EGIM, institutions shall calculate the "diminished financial obligation" for all restructured loans. The calculation should therefore also be performed in those cases where the threshold is blatantly exceeded, e.g. when a large portion of the capital is forgiven. This requirement should be deleted as it would have the effect of requiring a present value loss to be calculated for each restructured loan. It seems disproportionate to us, as the result can only be used to identify the default. Furthermore, no mandatory present value calculation should have to be performed if the reason for default, distressed restructuring, has already been recorded irrespective of the amount of any present value loss.

The EBA justifies the requirement that a net present value must always be calculated for restructured loans, even if this does not play a role for the default setting, with the fact that the net present value is needed for the RDS in the LGD development. However, there is no requirement that this present value must actually be used for own LGD estimates. The use of the present value from default detection also appears doubtful, since this present value must be discounted with the transaction's own effective interest rate. For LGD modelling, on the other hand, there is a requirement that artificial cash flows must be discounted at EURIBOR+5%. In paragraph 153(b), the ECB itself claims that no double counting is intended by these artificial cash flows and the present value calculation. The use of the present value from default detection is therefore generally not necessary and would be inconsistent with other requirements for LGD modelling.
- In particular, paragraph 132 EBA GL sets out that the economic loss should be calculated based on the outstanding amount at the time of default (including interests/fees) minus any recoveries realised after the default. Additional losses due to a reduced NPV are not mentioned.
- Paragraph 134 refers to losses incurred through forgiveness or write-offs only (which to our understanding means reduction of the principal amount) not to reductions of interest/fee payments or to prolonging the payback schedule.
- Paragraph 137 sets out that interests/fees need to be taken into account for the calculation of the realised LGD only up to the time of default but not thereafter.
Moreover, it would contradict the accounting regime. Bookings of loan loss provisions also only take into account book value changes with do not factor in maturity / interest / fee changes for hold to maturity transactions (and only for those LLP needs to be calculated).
- Last but not least, the level playing field with institutions outside the SSM area would be distorted. | Drefahl, Christian | German Banking Industry Committee | Publish |
| 17 | Credit risk | 4.5 Return to non-defaulted status | 85 | 85 | Clarification | Current regulatory developments regarding the probation period should also be taken into account in the EGIM. | According to paragraph 85 part b of the EGIM, institutions may only consider exposures that have been restructured as non-defaulted again when the debtor is no longer in default with payments. This is to apply even if the delay in payment is immaterial or lasts less than 90 days. However, in contrast to paragraph 86 part b EGIM, this paragraph does not contain any explicit statement as to whether, in the event of a payment default, the minimum probation period of one year applicable to restructured exposures is terminated or continues. According to EBA Q&A 2022_6527, the probation period is generally restarted for delays in payment of 30 days or more. However, institutions can refute this presumption by demonstrating that the delayed payment is not related to financial difficulties of the debtor. In our view, this should also be taken into account in the EGIM. | Drefahl, Christian | German Banking Industry Committee | Publish |

18	Credit risk	4.7 Adjustments to risk estimates in the case of changes to the definition of default	92	88	Clarification	There should be the additional possibility to qualitatively estimate the effects of minor, qualitative adjustments to the definition of default or the effects within the scope of the determination processing in an expert-based manner.	Paragraph 92 requires that for any changes to the default definition, a quantitative assessment of the impact should be made in the form of at least a 2-year retrospective simulation, a parallel survey or a similar classification of the reference data set (RDS) based on the application of the new definition of default. In the case of qualitative changes to the definition of default, the parallel or retrospective survey in manual processes is not expedient, as a deviating result could have an influence on the current default survey by the processor. In the case of quantitative changes, any change to the failure definition would require parallel IT implementation with corresponding lead times for implementation. Any adjustments in the processes of the institutions cannot be mapped in a machine parallel survey, simulation or classification of quantitative changes. Therefore, only the worst-case scenario can be derived. These disadvantages must be taken into account especially in the case of minor adjustments to the definition of default as well as in the context of processing findings on the default definition, with partly short- to medium-term processing periods.	Drefahl, Christian	German Banking Industry Committee	Publish
19	Credit risk	4.7 Adjustments to risk estimates in the case of changes to the definition of default	92	88	Clarification	In our view, it should be clarified that purely editorial changes (e.g., change in the name of an organizational unit) and substantive clarifications, minor process changes or additional default information that does not change the default definition (e.g., transfer risk event as additional information in the case of an existing default reason) should not be considered material changes. The same should also apply to the adaptation to new statutory regulations.	According to the RTS on the change of internal models, any change to the default definition is to be considered a material change that may only be applied after supervisory approval. The ECB's proposed interpretative guidance in this regard (paragraphs 89-93 EGIM) risks making changes to the default definition disproportionately difficult.	Drefahl, Christian	German Banking Industry Committee	Publish

| 20 | Credit risk | 4.7 Adjustments to risk estimates in the case of changes to the definition of default | 92 | 88 | Amendment | In our opinion, a qualitative impact statement should be sufficient as a basis for testing the material change for all changed or newly added soft failure criteria to be processed manually.
In addition, the risk differentiation is to be proven on the data collected in parallel. If this is not possible, not only a recalibration but also a reparameterization shall be performed (full model review).
In the case of changes to the default definition, the approach called for in the consultation draft with regard to the impact analysis required for material changes should be limited to automated portfolios such as those in the retail business. For all other portfolios, a qualitative analysis on a smaller data basis should also be possible, as described above.
The requirements in case the adjustments do not cover the entire observation period (last sentence, paragraph 92) should be deleted altogether. | According to paragraph 92 EGIM, institutions should create an appropriate data set reflecting the new default definition for the comparison of the new default definition with the old one. For this purpose, they can usually adjust historical granular data collected based on the old default definition to achieve broad equivalence with the new default definition. This can be done through a parallel run, retrospective simulation, or similar classification of the data according to the new default definition.
If the adjustments in the granular data do not cover the entire historical observation period of the model, institutions may fill in the missing periods by applying correction factors to aggregate ratios, model components or risk estimates. In doing so, the correction factors should be based on a reference data set covering at least two years of data adjusted at the granular level through a retrospective simulation, parallel run, or similar classification of the data according to the new default definition.
This would mean that extensive analyses would have to be carried out for every change in the default definition, which we believe would be largely unfeasible outside of automated retail business. Moreover, the required parallel data collection for at least two years would lead to very high costs in the case of minor changes or manual reasons for default, such as the elimination of the minimum threshold for the reason for default, depreciation. At the same time, processing is likely to take longer than the supervisor has conceded, because supervisory findings or general new supervisory requirements regarding the definition of default could then only be processed after more than two years due to the minimum two-year parallel run. Due to the recommended (and, from the bank's point of view, mandatory) consistency of the default definitions between CRSA and IRBA portfolios, the implementation of any identified need for change would require correspondingly long periods of time for all portfolios. In manual analysis in the non-retail segment, parallel operation of two default definitions is also practically impossible. In terms of a conservative assessment, credit analysts would inevitably record a default whenever one of the two default definitions indicates a default; this would mean that the two default definitions would produce identical results in parallel operation.
In our view, retroactive application is not feasible for soft default criteria, i.e., default criteria that do not necessarily result in a default, but rather trigger a default assessment. For example, in the context of a supervisory review, the supervisory authority requires the definition of a certain threshold for the review for the default reason of insufficient debt service capacity. Not only would those calculations, which did not exist in the past, have to be performed manually and retrospectively on the basis of historical annual financial statements, but above all credit analysts would also have to go back in time and simulate the default check process retrospectively, mentally masking out all creditworthiness-relevant information that has been added since that time. In our opinion, it will be impossible to prevent the rating from being distorted by information that has been added in the meantime. | Drefahl, Christian | German Banking Industry Committee | Publish |
| 21 | Credit risk | 5.1 Structure of PD models | 95 | 91 | Clarification | We propose to add the following sentence to paragraph 95:
"The expectations set out above in this paragraph are specifically related to the model development phase. Model calibration sample and the corresponding statistical uncertainty in the model estimates are not in the scope of the stated expectations and should reflect all available information on realised default rates." | "Carving out" a part of a development sample (i.e. a sample used to define the process of assigning exposures to grades or pools) results into a smaller sample with more statistical uncertainty. It is our understanding that the calculation of Margin of conservatism can still be based on a full sample. Otherwise it would mean an increase in MoC and correspondingly the capital requirements for financial institutions as compared to the currently valid EGIM version." | Drefahl, Christian | German Banking Industry Committee | Publish |

| 22 | Credit risk | 5.1 Structure of PD models | 103 | 94 | Clarification | It should be clarified that the wording used in the requirement "to empirically confirm the risk differentiation across grades" can also be understood as meaning that the score values derived from a data-based risk differentiation function (scoring function) can be calibrated to a differentiated, uniformly used master scale in accordance with the requirements in Chapter 5.2.3 "Calibration to the LRA default rate". Empirical evidence of the difference between all pairs of adjacent rating classes should not be required, but empirical evidence of the quality of the risk differentiation function, in combination with a calibration in accordance with the requirements and general evidence of risk differentiation across the rating classes, should be sufficient. | The use of a very granular master scale is ultimately a necessity for retail rating systems with a lot of data and the possibility of data-based derivation of a very differentiated risk differentiation function (scoring function) in order to fulfil the requirements of paragraph 102 (homogeneity within grades). Only by using a very differentiated master scale can the homogeneity of ratings within a rating class and the heterogeneity of ratings between rating classes be achieved. The use of a uniform master scale within an institution across the different calibration segments of a rating system is a central aspect for user acceptance, but also for risk management, process management and also for credit pricing. For example, limit systems, competencies or cut-offs can be defined uniformly and thus transparently and easily comprehensible on the basis of this uniformly used master scale. A uniform, differentiated master scale also offers the advantage of a uniform categorisation of all borrowers, which is a great advantage for user acceptance in the institution but also for the institution's credit customers. If, for example, due to a lack of empirical evidence of risk differentiation between two neighbouring rating classes of a single calibration segment, the two rating classes were to be combined, a new categorisation would be created that would not exist in other calibration segments and there would no longer be a uniform categorisation across calibration segments. The "closing" of individual rating classes also does not appear to be an appropriate solution, as this would result in increased jumps in the PD for minor changes in the input parameters. Furthermore, in the case of rating systems for the retail portfolio, it must also be taken into account that in addition to calibration segments with a great deal of data, there are often calibration segments with significantly less data that are very similar in terms of the area of application. The necessity of these calibration segments regularly results from empirically observed, rather small but significant level differences of the default rates, which have to be mapped via own calibration functions. If a modified master scale had to be used for such calibration segments due to the lack of evidence of risk differentiation between individual neighbouring classes, this would severely impair user acceptance and comparability of the rating grades. Risk management for such calibration segments would then also be significantly more difficult, as different migration matrices would have to be used for different master scales, for example. Finally, the risk differentiation capability would also be reduced, as the lack of empirical evidence of risk differentiation between individual pairs of neighbouring rating classes does not necessarily mean that there would be no risk differentiation between these classes. | Drefahl, Christian | German Banking Industry Committee | Publish |

| 23 | Credit risk | 5.1 Structure of PD models | 103 | 94 | Deletion | The ECB expects a very granular rating scale to be used only in cases where the institution is able to empirically confirm the differentiation of risk between classes described in this paragraph (paragraph 103 EGIM). The requirement would in effect prevent the use of a differentiated master scale and should therefore be deleted. | In order to meet the requirement to ensure adequate risk differentiation between classes or pools, institutions shall ensure that there is no material overlap in the distribution of default risk between classes or pools. This is to be ensured by a meaningful differentiation of the default rates of the individual classes. In particular, the ECB expects a very granular rating scale to be used only in cases where the institution is able to empirically confirm the differentiation of risk between classes described in this paragraph (paragraph 103 EGIM). The latter requirement would in effect prevent the use of a differentiated master scale and should therefore be deleted. With a master scale, the identical rating grades with identical default probability are used across all rating systems of the bank. The significance of the individual rating grades is thus the same across all systems, and the processes in the institution can be set up in a uniform manner. Different ranges of the master scale are sometimes necessary for different portfolios with different risk characteristics. Omitting certain levels of the master scale or using differently adapted scales for different models would lead to large and uneconomic leaps, which would strongly influence the acceptance of the rating system. This will be illustrated in the following using three examples: Example 1: Within a rating system, certain ranges of the master scale may not be used at all in the standalone rating model. However, a rating transfer may result in the use of a level not occupied by the standalone model. In this case, the assignment to another rating level of the master scale would make no economic sense. Example 2: Particularly in the good rating grades, the risk differentiation of individual grades on the basis of defaults is in part not demonstrable, whereas it is readily demonstrable when several grades are aggregated. Omitting rating grades from the master scale would lead to outsized changes in default probabilities in the case of small changes in the input parameters – with corresponding consequences for the stability and acceptance of the rating results (from the analyst's point of view, several rating grades would be skipped each time). The situation is similar with regard to overrides, which would only be possible in certain gradations. Example 3: Certain ranges of the master scale may only be relevant in certain phases of the cycle, because with a fixed master scale and a responsive rating philosophy, customers move across the rating levels over the course of the cycle. Again, the appropriate differentiation cannot be proven at every point in time; omitting rating levels, on the other hand, would lead to absurd leaps. | Drefahl, Christian | German Banking Industry Committee | Publish |

24	Credit risk	5.1 Structure of PD models	103	94	Deletion	We propose to drop paragraph 103.	For institutions using the same predefined master scale across all portfolios, the empirical evidence required in paragraph 101 can hardly be provided. In those cases, qualitative justifications should be sufficient. The requirement in paragraph 103 practically does not allow for the use of a global master scale. This is an improper intervention in the bank steering. It makes comparability between portfolios and a meaningful use test very difficult and thus results in several unwarranted consequences: 1. Without a master scale concept, comparability of ratings from different rating systems is not given anymore. This is in particular relevant in case of rating transfer and third party support. For example, when performing a rating transfer between a subsidiary and its parent – a more concrete example would be a bank subsidiary of a corporate entity, as e.g. often the case in the automotive industry – the ratings must be comparable as they are in certain cases either directly inherited or notched according to predefined rules. 2. Also the rating override process and respective policies are based on the master scale concept. Several parts (e.g. when it comes to notch downgrades or considerations of investment vs. non-investment grade) would need to be reworked from scratch when leaving or collapsing the master scale, with potential inconsistencies and reduced transparency being the result. 3. The concept of sovereign ceiling requires ratings of counterparties and their sovereign to be directly comparable and would hence not work without a master scale concept either. In addition to that, with respect to granularity of the rating/master scale it should be noted that risk differentiation between grades is not only based on default observations, but also other criteria impacting the risk profile like data availability (for example for listed counterparties much more information can flow into the assessment) and support considerations. Moreover, the conditions of paragraph 102b) and 103 cannot be fulfilled at the same time with sufficient significance, if buckets within rating grades are defined via thresholds on probabilities of default given by a risk differentiation model.	Drefahl, Christian	German Banking Industry Committee	Publish
25	Credit risk	5.1 Structure of PD models	113	98	Clarification	In order to improve its readability, we suggest to rephrase paragraph 113 in simplified language.		Drefahl, Christian	German Banking Industry Committee	Publish
26	Credit risk	5.2 PD risk quantification	122	100	Amendment	Paragraph 122 (d) - (f) should be adapted accordingly to EBA GL 2017/16.	According to paragraph 122 part e EGIM, the fact that certain debtors are not observable during the entire year should not play any role per se in the calculation of the one-year default rate. Therefore, there should also be no adjustments or deviations from the method used to calculate the one-year default rate. In our view, this contradicts the requirements in paragraph 80 part a of the EBA Guidelines on PD estimation, LGD estimation and treatment of defaulted exposures (EBA/GL/2017/16), according to which institutions must analyse possible distortions that may arise due to the proportion of short-term and terminated contracts that cannot be observed during the relevant one-year periods. According to paragraph 38 in conjunction with paragraph 37(ix) of the above EBA GL, this distortion should be corrected by an appropriate adjustment. We consider such an adjustment necessary as otherwise the LRA and the 1-year PD would be underestimated. Therefore, we believe that this bias should be corrected regardless of its cause. Since the EGIM requires that each observation be included in the denominator of the default rate, an adjustment would not be possible. In addition, we believe the requirements in paragraph 122(e) EGIM are inconsistent with the requirements in paragraph 122(f) EGIM, which outline how to deal with migrations out of the rating system during the year or the sale of exposures when determining the LRA.	Drefahl, Christian	German Banking Industry Committee	Publish
27	Credit risk	5.2 PD risk quantification	124	102	Clarification	The use of overlapping time windows should not be expected if any of the conditions a), b) or c) is fulfilled. We propose b) to be used in conjunction with a) and/or c).	The use of overlapping time windows leads to overweighting of snapshots in the middle of the observation period. Thus, overlapping time windows are likely to result in different average default rates than non-overlapping windows (i.e. condition b) in paragraph 124 would regularly be met) in any case.	Drefahl, Christian	German Banking Industry Committee	Publish

28	Credit risk	5.2 PD risk quantification	125	102	Clarification	The requirements around the use of external data in paragraph 125 are so complex that it seems inevitable from the start that there will be deviating/inconsistent assessments and findings.		Drefahl, Christian	German Banking Industry Committee	Publish
29	Credit risk	5.2 PD risk quantification	126	103	Amendment	For non-retail PD models, the requirements in paragraph 126 are hard to meet.	The prescribed analyses of potential biases are expected to be performed on internal data only. At the same time, it is stated that a lack of statistical evidence will not be accepted as a sufficient indication for the absence of biases. However, such a lack of statistical evidence could likely occur in case of scarce data, especially in case of broad confidence intervals for wholesale portfolios. It is unclear which alternative assessments instead of testing for statistical significance should be performed in those cases.	Drefahl, Christian	German Banking Industry Committee	Publish
30	Credit risk	5.2 PD risk quantification	126	103	Amendment	We suggest adapting the requirement to the effect that negative analysis results merely represent a strong indication of bias and should therefore trigger further, valid analyses. Remaining uncertainties can also be addressed by a category B MoC.	To assess whether the parameter estimates are biased in accordance with paragraph 38 of this chapter, paragraph 126 of the EGIM requires institutions to compare the LRA default rate with the average PD estimates. In the ECB's view, the estimates are biased if there are (a) material differences between the average of the two measures at the calibration segment level or (b) systematic differences at the class level. In this context, the finding of material differences in (a) or systematic differences in (b) should not be based on statistical significance alone. In particular, in the ECB's view, the lack of statistical evidence that a PD estimate and the corresponding LRA default rate are different based on internal data is not sufficient to conclude that there is no material difference. This is particularly true in cases where only limited data is available. In this regard, we would like to note, as we already did with regard to paragraph 38 EGIM, that a testing procedure that is independent of the statistical significance runs the risk of drawing overly simplistic conclusions. We therefore suggest adapting the requirement to the effect that negative analysis results merely represent a strong indication of bias and should therefore trigger further, valid analyses. Remaining uncertainties can also be addressed by a category B MoC. Especially in portfolios with few defaults, a single default event with closely related borrowers at the institution level may lead to artifacts that could only be cured by economically inappropriate risk differentiation or quantification. If a large number of tests with the same direction are carried out for sub-samples (i.e. for portfolios of institutions) on the basis of a limited database, individual institutions must become conspicuous for statistical reasons alone. On the one hand, such an approach would run counter to the objective of avoiding excessive overfitting in the models (see paragraph 95); on the other hand, it is precisely participation in a data pool that can help in the assessment of relevant issues. Moreover, it would counteract the overarching goal of avoiding RWA differences if such artifacts resulted in unjustified calibration differences across institutions. Such differentiations should therefore only be introduced if there is a sufficient data basis or a thorough root cause analysis.	Drefahl, Christian	German Banking Industry Committee	Publish
31	Credit risk	5.2 PD risk quantification	130 (a)	104	Deletion	This requirement goes well beyond the requirements of the Guidelines and should thus be dropped.	The requirement in point a) „that under no circumstances should an approach be adopted to overcome data scarcity at grade or pool level, lack of evidence of discriminatory capacity, homogeneity or heterogeneity across grades" makes the use of calibration segments virtually impossible, in particular for non-retail portfolios. In our view, data availability is one of the key criteria for choosing a calibration approach. If data availability is low, the calculation of LRA based on internal defaults usually cannot be done at the rating grade level. Moreover, according to paragraph 130, institutions that use the approach referred to in paragraph 92 (b) of the EBA Guidelines on PD and LGD for calibration should not only perform the calibration tests required therein but should also perform additional tests as part of the development and ongoing monitoring of their models to ensure that the final PDs (after calibration) reflect the LRA default rate of the individual classes.	Drefahl, Christian	German Banking Industry Committee	Publish

32	Credit risk	5.2 PD risk quantification	130 (b)	105	Deletion	In its current form, point b) effectively hampers sound risk management and should thus be dropped.	Point b) implies that long-term historical data is available for all relevant risk drivers. This appears to be inconsistent with the requirement to identify recent risk drivers and include them in scoring and rating methods, if relevant, like for instance ESG criteria. Relevant impacts of a changing environment, for example due to digitisation/ the use of AI, real world crises, changes in regulations, etc., can be reflected only very slowly and thus impair model accuracy.	Drefahl, Christian	German Banking Industry Committee	Publish
33	Credit risk	5.2 PD risk quantification	130 (c)	105	Amendment	We suggest the following amendments in paragraph 130 c): "[…], institutions should assess whether the use of the historical rating assignments based on previous versions of the assignment methodology would be adequate, **i.e. add more value as compared to the approximated ratings using the new rating assignment methodology in terms of calibration tests and likely range of variability assessment."** Moreover, we propose to leave the possibility not to use historical assignments to grades in case recalculation of historical ratings for the full historical observation period is impossible or too burdensome. Proposed addition to point c): **"If re-calculation of the historical rating assignments is not possible and the usage of the historical rating assignments is not adequate, appropriate adjustments for the long-run average default rate shall be made. They can be based on approximated ratings using the new (changed) assignment methodology. Calibration tests as mentioned in point (b) of the paragraph are then to be performed on a smaller sample where a re-calculation of the ratings is possible."**	The requirements with regard to the historical observation period in point c) appear to be in contrast with the usual approaches used in practice. In the specific case of changes in the method for assigning exposures to grades or pools, the requirement to make all reasonable efforts to recalculate the new assignment back through time is deemed fully reasonable. However, where the recalculation is not possible, we do not consider as appropriate practice to use the historical rating assignments based on previous versions of the assignment methodology. Analyses performed on these old rating assignments, such as e.g. - Representativeness of the likely range of variability - Calibration tests could be biased and therefore not conclusive.	Drefahl, Christian	German Banking Industry Committee	Publish
34	Credit risk	5.2 PD risk quantification	130 (e)	105	Clarification	The EGIM should not unnecessarily limit possible mitigations to upward shifts of default rates.	Point e) in paragraph 130 requires an upward adjustment to default rates if bad years are underrepresented in the available data. However, this issue could also be solved by other measures, such as the use of another year as replacement.	Drefahl, Christian	German Banking Industry Committee	Publish
35	Credit risk	5.2 PD risk quantification	131	106	Clarification	In contrast to the interpretation stated in para. 131, depending on the calibration approach, there might be deviations between average PDs and LRA default rates for some grade or pools. As far as those deviations do not affect a significant proportion of the relevant population and are not systematic, they should not be automatically regarded as violation of this paragraph.		Drefahl, Christian	German Banking Industry Committee	Publish
36	Credit risk	5.2 PD risk quantification	135	107	Clarification	The references in Section 5.2.3 to calibration tests would have to be re-formulated to allow conclusions based on single snapshots to be taken into account.	Even if a model is representative over the full time-horizon used for calibration and LRA DR calculation, the distribution of risk-drivers might change over time. This can cause goodness-of-fit problems on LR samples. Therefore, it makes sense to analyse the fit between probabilities and default rates not only on LR samples but also on single snapshots and conclude on both outcomes.	Drefahl, Christian	German Banking Industry Committee	Publish
37	Credit risk	5.2 PD risk quantification	136	108	Deletion	Paragraph 136 should be dropped	The cited paragraph 87 of the EBA Guidelines on PD and LGD provides enough guidance on the calibration to the LRA DR at both levels. The new requirements added in paragraph 136, namely to compare the average PD with the one-year default rates for each of the calculation dates, contradicts the expectation to maintain the TTC philosophy particularly in cases where the variability of the one-year default rates is high. Such a comparison is also not conclusive for years back in history where the re-calculation of rating assignments in case of changed methodology is impossible or not adequate (c.f. comment to paragraph 130 point c)). Moreover, it is unclear which actions should follow if for individual years the calibration tests are not passed. Since this is neither data scarcity nor an additional statistical uncertainty (as compared to a "normal" statistical uncertainty already captured by MoC-C), but something driven merely by the nature of the portfolio, appropriate adjustments and MoCs are not considered as a good measure to account for failed calibration tests. Excluding these years from the sample is also not an option and contradicts to the requirement to cover the likely range of variability of default rates.	Drefahl, Christian	German Banking Industry Committee	Publish
38	Credit risk	6.1 Realised LGD	153	116	Deletion	This requirement should be dropped.	Paragraph 153 requires institutions to take into account NPV reductions where institutions open new facilities to replace previously defaulted facilities as part of restructuring or for technical reasons. This contradicts both several paragraphs in the EBA GL (e.g. 132, 134, 137) and accounting principles and violates the level playing field with institutions outside the SSM (c.f. detailed comments on paragraph 77).	Drefahl, Christian	German Banking Industry Committee	Publish

39	Credit risk	6.2 LGD structure	173	121	Clarification	We suggest the following addition: "[…] Independent datasets should correspond not only to random sampling (out-ofsample), but also to different time periods (out-of-time) unless there are no sufficient data available for the training sample. **However, when performing out-of-time analysis, most recent time slices should not be omitted to prevent for a potential bias with effects stemming from open cases in the analysis."**	LGD development in recent time slices is highly affected by open cases for which LGD realisations depend on the assumption of future cashflows. Performing an out of time analysis by just omitting recent time slices would have a high impact on the ratio between open vs. closed cases which would bias the outcome of the analysis.	Drefahl, Christian	German Banking Industry Committee	Publish
40	Credit risk	7.1 Commitments, unadvised limits and scope of application	195	132	Clarification	We propose the following amendments to paragraph 195 (underlined): Conversion factor means the ratio of the currently undrawn amount of a commitment that could be drawn and that would therefore be outstanding at default to the currently undrawn amount of the commitment. The extent of the commitment is determined by the advised limit, unless the unadvised limit is higher. The exposure value for the items listed in Article 166(8) of the CRR must be calculated as the committed but undrawn amount multiplied by a CCF. To calculate the exposure value as required by Article 166(8) of the CRR, institutions should adopt the following approach. a) Treat a committed facility as an exposure from the earliest date after acceptance of the client at which the facility is recorded in the institution's systems in a way that would allow the obligor to make a drawing. An unadvised committed limit is any committed credit limit defined by the institution (i) that is above the committed advised limit the obligor has been informed of by the institution; and (ii) according to which additional drawings are possible, at least temporarily. This higher (unadvised) credit limit may be disregarded if its availability is subject to a further credit assessment by the institution. b) Consider as "commitment" any legally binding contractual arrangement that has been offered by the institution and accepted by the obligor to extend credit, purchase assets or issue credit substitutes. Only commitments qualify as regulatory off-balance sheet items. c) Consider as "conditionally cancellable commitment" any such arrangement that can be and will be cancelled by the institution if the obligor fails to meet conditions set out in the facility documentation, including conditions that must be met by the obligor prior to any initial or subsequent drawdown under the arrangement. d) Consider as "credit lines" all lines including products such as facilities granted for construction where the payments to the obligor are made according to the progress of the construction. Products such as guarantees are not, however, included in the concept of credit lines. e) Facilities which are not committed are not in scope for the exposure value calculation, i.e. do not qualify as regulatory off-balance sheet items.	We understand that only committed limits are considered to be regulatory off-balance sheet items in line with paragraph 195 point b) "consider as "commitment" any contractual arrangement that has been offered by the institution and accepted by the obligor to extend credit, purchase assets or issue credit substitutes." Therefore, uncommitted limits are not considered as regulatory off-balance sheet items since it is the institutions discretion whether it provides financing, e.g. in the form of a loan, or not, and these uncommitted limits do not establish a legally protected basis for the client's confidence in receiving financial support. Additionally, the institution would reduce or cancel such uncommitted limits, if the credit standing of the client deteriorates. With regard to committed limits, the nominal amount of the respective off-balance sheet item is determined as the advised limit, unless the unadvised limit is higher. However, this "higher (unadvised) credit limit may be disregarded if its availability is subject to a further credit assessment by the institution, as long as this additional assessment includes a re-rating or a confirmation of the rating of the obligor." In practice, an on-demand re-rating or an explicit confirmation of the rating of the obligor would be extremely onerous for many customer types and not feasible in a timely manner. This is because many rating methods have a certain amount of manual input (expert judgements) or allow manual overrides. Therefore, we propose to delete the condition "as long as this additional assessment includes a re-rating or a confirmation of the rating of the obligor". For this credit assessment, it should be sufficient if the institution approves each additional drawing by the obligor on an individual basis by, for example, assessing whether there are indications of deterioration of the obligor's creditworthiness. This would be in line with the EBA Q&A ID 2017_3246 since the EBA also uses the terms 'bank's approval' and 'creditworthiness' and does not require a re-rating or an explicit confirmation of the rating of the obligor: „As an illustration, framework arrangements would not give rise to off-balance sheet items if the institution needs not only to approve the initial and each subsequent drawdown by the client but it has also the complete discretion on whether to give its approval regardless of the fulfilment by the client of the conditions set out in the arrangement, since no drawdown would be possible without a prior and specific approval of the institution.[…]" As outlined above, we believe that this credit assessment prior to each drawdown by the obligor is only required for committed unadvised limits. If such a process exists, these higher committed unadvised limits can be disregarded.	Drefahl, Christian	German Banking Industry Committee	Publish

41	Credit risk	7.4 CCF risk quantification	204	137	Amendment	We propose to allow institutions to align the calculation of LRA CCFs to LGDs, i.e. consider all individual defaults from the observation period directly in the LRA CCF via a count weighted average. This treatment is consistent to the general alignment between LGD and CCF in terms of exposure (i.e. treatment of drawings after default), level of calculation, etc.	In our view, the requirement in paragraph 204 to first calculate the default weighted average CCF per year of default and then use a simple arithmetic average over these yearly observations can lead to a contradiction to Article 182 (1)(a) CRR, since it could introduce an unjustified weighting of the defaults depending on the year of default. Especially for LDPs, the CCF would become a function of a small number of defaults in each calendar year. Article 182 (1)(a) of CRR clarifies that *"institutions shall estimate conversion factors by facility grade or pool on the basis of the average realised conversion factors by facility grade or pool using the default weighted average resulting from all observed defaults within the data sources;"* Moreover, this approach would be neither in line with the calculation / aggregation of LRA LGD nor LRA PD and hence introduce a bias. Additionally, the choice of calendar year is fully arbitrary: there is absolutely no economic rationale for taking average from January to December compared to e.g. July to June. As justification for this EGIM interpretation typically Response 6 in the Responses to the public consultation on the draft ECB guide to internal is quoted, namely """The ECB's understanding is that Article 182(1)(a) of the CRR does not exclude the interpretation reflected in paragraph 134(c), i.e. the use of the arithmetic average of the yearly averages of realised CCF. The comparison with LGD is also not deemed a valid argument. The rationale for the use of a number-weighted average for LGD is that this parameter captures the losses across the recovery process, which covers multi-year periods""". Although we still disagree to the conceptual view outlined in this response, in this response, yearly average is seen as one, but not the only possible option. We, therefore, propose either to change the approach to overall count-weighted average or include respective clause to allow alternative way of calculating LRA CCF."	Drefahl, Christian	German Banking Industry Committee	Publish
42	Credit risk	7.4 CCF risk quantification	204	137	Deletion	We request that paragraph 204, point c) be deleted.	Paragraph 204 requires that the average CCF is calculated from the mean value over the annual averages of the realised CCFs. To ensure stable best estimates, the data bases of calculated averages should have an appropriate minimum size. According to CRR, Article 182 a), best estimates can be derived at facility levels or pools, thus limiting the minimum size to this level. If the best estimates are to be calculated as required in EGIM paragraph 204, point c), this is not only in some way a contradiction to CRR, Article 182 a), but also limits the minimum size to the level of the annual window. This in turn means that the facility tiers or pools must be cut correspondingly more coarsely, which consequently causes an inappropriate decrease in risk differentiation. When calculating the MoC of category C, the statistical uncertainty is quantified. Since the annual values of a facility level or pool have a greater statistical uncertainty than the total mean value of the facility level or pool, the required procedure unnecessarily increases the statistical uncertainty. Finally, it should be noted that the individual year slices (especially the bad ones) are taken into account when determining the downturn premiums and thus significantly determine the forecast to be applied. On the basis of the argumentation presented, paragraph 204, point c) entails a high risk of reducing the risk differentiation, but no added value for the CCF applied (incl. mark-ups).	Drefahl, Christian	German Banking Industry Committee	Publish
43	Credit risk	7.4 CCF risk quantification	204	137	Clarification	The answers to the Q&A (2020_5511 and 2020_5254) should be considered in the EGIM.	In our view, the procedure for determining the LRA-CCF described in paragraph 204 would result in the LRA-CCF no longer being number-weighted as required by the CRR, as the realized values from years with fewer observations would be given greater weight. To our knowledge, there are at least two Q&As pending with the EBA on this issue (2020_5511 and 2020_5254).	Drefahl, Christian	German Banking Industry Committee	Publish
44	Credit risk	7.4 CCF risk quantification	207	139	Amendment	According to paragraph 207 (b) (iii), institutions should apply a minimum CCF of 100% in the case of an expert-based estimate of the CCF. In our view, this appears to be inappropriately conservative, as there are products that justify a lower CCF due to internal bank processes (in particular, guarantees callable at any time).		Drefahl, Christian	German Banking Industry Committee	Publish

45	Credit risk	8.1 Relevant regulatory references	208	140	Clarification	It is not clear whether the whole paragraph refers only to PD.	In principle, section 8 should clarify which requirements should apply to which parameters (PD, LGD or CCF). For example, at one point in paragraph 208, the MoC is required to reflect uncertainty at the level of the final PD estimates.	Drefahl, Christian	German Banking Industry Committee	Publish
46	Credit risk	8.1 Relevant regulatory references	208	140	Amendment	Grade level MoCs should not be strictly required. Instead, flexibility is needed to enable institutions to calculate MoCs that are economically sensible in light of their individual business model and rating approach.	The requirement to assign MoCs at grade level will eventually result in various inconsistencies and undesirable consequences: - To begin with, a negative incentive towards risk differentiation will follow from this requirement. Ceteris paribus, the number of obligors per grade decreases with an increasing number of grades et vice versa. Therefore, models characterised by a high number of grades and thus a high degree of risk differentiation will be subject to a higher overall category C MoC. Viewed the other way around, reducing the number of grades would be beneficial with regard to the aggregate MoC level, while at the same time problematic with respect to ensuring homogeneity within grades. - Moreover, the number of obligors is not evenly distributed across grades. For instance, the highest grades may well contain significantly less obligors than subsequent grades. Hence, grade level MoCs will tend to be higher for higher grades. This will not only lead to a structural bias but potentially even a change in the rank ordering of obligors. - Last but not least, as PD estimation might not be based solely on grade level, grade level MoCs may not be sensible with regard to their interpretation in the first place. In particular since the risk-differentiation model is estimated on segment-level, it only makes sense to quantify MoC A related to that model on segment-level (e.g. for deficiencies such as partly missing risk-drivers). This also applies for deficiencies categorized under MoC B if these apply to the complete segment. - The EGIM proposes to base mean-PD estimates per grade solely on long-run default rates and derive MoC C accordingly. In case that a calibrated risk-differentiation model already is a per-client PD estimate based on risk-drivers, this does not make sense from a statistical standpoint. Assume e.g. that PD estimates for risk-differentiation are calculated using a logistic regression model which was calibrated on the long-run sample. A calculation of a mean-PD per grade based on these PD estimates would be far more accurate than the one proposed in EGIM, since information in the risk-drivers to quantify PDs would not be discarded. The EGIM in turn proposes to use client information only to pool clients, and discards of that information for calibration purposes. In practice, grade level MoCs do not allow banks to adhere to the principles of risk differentiation, monotonicity and interpretability at the same time.	Drefahl, Christian	German Banking Industry Committee	Publish
47	Credit risk	8.1 Relevant regulatory references	208	140	Clarification	It should be clarified in paragraph 208 that a "continuous" MoC calculated e.g. as a confidence interval of the estimation function is also allowed.	It is our understanding that, as long as continuous models are allowed under the prerequisites mentioned in paragraph 141, every PD estimate is to be understood as a separate grade or pool (CRR Art. 169(3)). Therefore, a "continuous" MoC calculated e.g. as a confidence interval is also allowed.	Drefahl, Christian	German Banking Industry Committee	Publish

48	Credit risk	8.1 Relevant regulatory references	208	140	Deletion	The requirements that that the MoC should not affect the rank ordering and that institutions should be able to ensure monotonicity in their final estimates while still reflecting the uncertainty at grade or pool level should therefore be deleted.	In the PD according to paragraph 62 EBA Guideline 2017/16, the rating of a third party in a rating system B can be transferred to another obligor in rating system A under certain conditions ("rating transfer") (a) or used as an input parameter (c). In our view, it is methodologically correct in these cases to take the uncertainty of the third-party rating (i.e. its MoC value) into account in the conservative PD estimate. According to paragraph 108 EGIM, this shall also be the case from the ECB's perspective in the case of a rating transfer according to paragraph 62 (a) of the EBA-GL 2017/16. However, this is contradicted by the requirement that the MoC must not change the rank ordering – especially in the case of contractual support of the obligor according to paragraph 62 (c) of EBA-GL 2016/17. If the MoC of the third-party rating from rating system B is taken into account, this generally changes the rank ordering. The requirements that that the MoC should not affect the rank ordering and that institutions should be able to ensure monotonicity in their final estimates while still reflecting the uncertainty at grade or pool level should therefore be deleted. On the one hand, it is very sweeping. For example, it is unclear whether the monotonicity is meant at the level of the rating system, the PD model, the calibration segment or the rating level, etc. On the other hand, the MoC is intended to reflect specific uncertainties. Depending on the situation, these can occur at one of the different levels, e.g. only a specific industry (within a calibration segment) could be affected by increased uncertainty. At the very least, it should be made clear that there may be constellations where a different approach is necessary.	Drefahl, Christian	German Banking Industry Committee	Publish
49	Credit risk	8.1 Relevant regulatory references	210	140	Deletion	The respective, newly added requirement should be dropped.	It is practically impossible to have the same statistical uncertainty at both calibration segment level and the grades or PD sub-ranges level as required in paragraph 210, because it depends on the number of observations in the sample.	Drefahl, Christian	German Banking Industry Committee	Publish
50	Counterparty credit risk	3.2 Principles for ECB Banking Supervision	26	226	Amendment	The list should be taken as guidance and banks should consider the line items that are applicable and meaningful for the particular use case.	The list provided is exhaustive and it is unlikely to be appropriate to consider each of the criteria for all counterparties across asset classes.	Drefahl, Christian	German Banking Industry Committee	Publish
51	Counterparty credit risk	9.2 Principles for ECB Banking Supervision	67, 68	243, 244	Clarification	The extent to which the use tests are performed should be decided by the respective firm based, amongst potential other criteria, on the IT system setup, the release and testing process as well as previous experience with releases of a given scale and complexity.	The periods required for parallel runs are considered very long. Each institution should perform use tests in the shape and form that provide the institution with sufficient confidence that the model change is working as intended in the production environment. Creating a disconnect between the systems/libraries employed for internal risk management and capital calculation would create a violation of Art. 289 CRR *"Institutions shall ensure that the distribution of exposures generated by the model used to calculate Effective EPE is closely integrated into the day-to-day CCR management process of the institution".*	Drefahl, Christian	German Banking Industry Committee	Publish

52	Counterparty credit risk	13.1 Relevant regulatory references	93	256	Clarification	The reference to CRR in paragraph 93 point u) is unfounded	The reference to CRR in paragraph 93 point u) is unfounded as Article 368(1)(b) CRR states: „*the institution shall have a risk control unit that is independent from business trading units and reports directly to senior management. The unit shall be responsible for designing and implementing any internal model used for purposes of this Chapter. The unit shall conduct the initial and on-going validation of any internal model used for purposes of this Chapter, being responsible for the overall risk management system. The unit shall produce and analyse daily reports on the output of any internal model used for calculating capital requirements for position risk, foreign exchange risk and commodities risk, and on the appropriate measures to be taken in terms of trading limits;*" The relevant chapter is "Chapter 5: Use of internal models to calculate own funds requirements"" which is included in " Title IV: OWN FUNDS REQUIREMENTS FOR MARKET RISK"", i.e. not relevant for CCR from a legal point of view. The RTS on assessment methodology refer to a single risk control unit that is both responsible for designing/implementing any internal model (1LoD) and validation (2LoD) which can only refer to RISK in total (i.e. does not distinguish between 1LoD and 2LoD).	Drefahl, Christian	German Banking Industry Committee	Publish
53	Counterparty credit risk	13.2 Principles for ECB banking supervision	96	259	Clarification	Clarification on the expected time lines of RNIEPE and the cashflow spikes being included in the EU legislation's refinement of the IMM provisions would be appreciated.		Drefahl, Christian	German Banking Industry Committee	Publish
54	Counterparty credit risk	13.2 Principles for ECB banking supervision	99, 104	260, 262	Deletion	We propose to delete the last subsentence of paragraph 99 and paragraph 104 b).	A back-testing of RniEPE will hardly be feasible in practice, as in the vast majority of cases, there is likely no observation to compare against, be it market observations or data provided by another party that allows for a like for like comparison given different approaches to the RNIEPE, portfolio compositions and other factors. Therefore, no respective requirement/ expectation should be included in the EGIM.	Drefahl, Christian	German Banking Industry Committee	Publish
55	Counterparty credit risk	13.2 Principles for ECB banking supervision	107 (b), 108 (c)	264	Deletion	The requirement to floor at netting set level should be removed.	While flooring an individual RNIEPE's impact on the portfolio level makes perfect sense, flooring the impact on a netting set level neglects the fact that an institution's business is usually diversified across different counterparties. The requirement to segregate, within a single netting set, trades impacted by an RNIEPE from the other ones introduces additional source of uncertainty, such as the generation of synthetic sub-netting sets, a split of collateral among those and potential modelling sets which are unlikely to increase the quality of the estimation of an RNIEPE's impact. Furthermore, the requirement directly contradicts the denominators specified in paragraphs 114 (a) and (b) and paragraph 105 stating "As identified RNIEPE are considered to be part of the IMM, the quantification of each RNIEPE should (to the extent possible) be methodologically similar to the respective exposure quantification in the IMM".	Drefahl, Christian	German Banking Industry Committee	Publish
56	Counterparty credit risk	13.2 Principles for ECB banking supervision	109	265	Clarification	The inclusion of cash flow spikes into the RNIEPE framework as prescribed in paragraph 109 b) is expected to replace any model limitations imposed by the supervisor. A respective confirmation would be appreciated. Also, the expected regulatory timing of formal incorporation of cash flows into RNIEPE should be specified.		Drefahl, Christian	German Banking Industry Committee	Publish
57	Counterparty credit risk	13.2 Principles for ECB banking supervision	114	266	Amendment	The denominators in (a) and (b) should be aligned with the ones in (c) and (d).	Capital overlays ultimately derived from RNIEPE impacts have to be reported in RWA, allowing firms to incorporate the different levels of risk weights for different counterparties. As a consequence, the industry would appreciate to be given freedom to choose between quantifying the RNIEPE items in EEPE or RWA. Cherry picking should of course not be allowed, so the choice needs to be consistent across a firm's RNIEPE items. The denominators in 114(a) and (b) require to calculate the impact on impacted netting sets only. This is potentially leading to cases where, from an overall portfolio point of view, a low materiality netting set incurs a significant relative impact from an RNIEPE, which on the portfolio scale would be low in relative and absolute terms.	Drefahl, Christian	German Banking Industry Committee	Publish

| 58 | Counterparty credit risk | 13.2 Principles for ECB banking supervision | 116 | 267 | Clarification | It should be clarified that threshold excesses in accordance with paragraph 116 c) should persist for two consecutive quarters before action is mandated in line with other CRR articles.
Moreover, capitalisation should be acceptable to reduce below overall thresholds. | | Drefahl, Christian | German Banking Industry Committee | Publish |