



EUROPEAN CENTRAL BANK
BANKING SUPERVISION

Template for comments

Public consultation on the revised ECB guide to internal models

Institution/Company

JPMSE

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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
1	Counterparty credit risk	3.2 Principles for ECB Banking Supervision	26	226	Amendment	<p>We would like to point out, that the list of attributes provided to be utilised in the identification of transactions and collateral positions which are concentrated, illiquid and/or hard-to-replace, is exhaustive. We fully appreciate the guidance provided by this list but on the other hand would like to bring a potential down-side of requiring the consideration of each line item to the ECB's attention. Not all features are applicable across all possible combinations of asset classes and counterparties. Another, not unlikely, challenge is likely posed by the availability and reliability of the data, such as market price observations.</p> <p>In our view, the provided list should serve a guidance and an institution should select the relevant items for which reliable market data is available. This can be achieved by rewording the paragraph to:</p> <p>"In establishing the definitions of the items mentioned in paragraph 25(a) to (c) above, along with the related processes, the ECB sees it as good practice if an institution considers, for each counterparty where appropriate, where appropriate, the following features and attributes of transactions and collateral: [...]"</p>	The list provided is exhaustive, but not every feature is applicable for every use case.
2	Counterparty credit risk	3.2 Principles for ECB Banking Supervision	29	228	Amendment	<p>Whilst we understand and appreciate the intention to harmonise the practices across the SSM regulated banks in the EU, it should be highlighted, that the rules outlined exceed the Basel as well as regulatory rules in other jurisdictions. The harmonisation within the EU would come at the cost of a divergence across regulatory regimes. We therefore ask the ECB to balance between harmonisation within the EU while ensuring not to create an imbalance on a global scale.</p>	Level of detail provided by regulators in different jurisdictions differs significantly and could potentially create regulatory imbalances for global institutions

3	Counterparty credit risk	9.2 Principles for ECB Banking Supervision	67	243	Amendment	<p>From our point of view the requirements with respect to parallel runs imposed by EGMA make perfect sense to ensure a meaningful impact estimation. The requirements imposed in paragraph 67, however, are considered problematic in more than one way. On the one hand, it will lead to a violation of CRR article 289: "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". On the other hand we are concerned about a potential excessive cost associated with expected very long parallel run periods. It should be in a firm's own interest to ensure that a model change undergoes sufficient testing to gain experience with the new setup. As procedures, systems and setups differ across different firms, we feel that an institution is best placed to assess how much testing of the different aspects of a change is necessary to gain this experience. For significant changes this testing plan should be discussed and agreed upon with the respective JST, as the JSTs usually possess some insight in the system and testing setup.</p> <p>We suggest rewording the paragraph to: "In accordance with the aim of Article 289(2) of the CRR regarding the upfront use of a new model, the ECB considers it good practice for an institution to start by testing the envisaged model changes for internal risk management purposes to acquire sufficient experience with the change or extension before it is fully implemented. This would apply in cases where the change needs to be investigated as set out in the ECB Guide on materiality assessment (EGMA). Therefore, the contemplated planning for tests and parallel run phases before the actual implementation of a material model change should be provided to the ECB for their investigation. This testing and parallel run phases should include at least a period of risk monitoring metrics computation and assessment prior to the activation, whether the internal limits need to be recalibrated to account for this model change if it is deemed relevant. For model extensions, the ECB considers it good practice to start applying the model extension for risk management purposes ahead of the implementation of the extension for EEPE computation. This upfront use should start no later than the application date (i.e. the date of the application letter) in the live production environment for exposure calculations for the purpose of risk management."</p>	System setups and release procedures differ from firm to firm. The detailed plans should be subject to agreement with the JST to ensure efficiency.
4	Counterparty credit risk	9.2 Principles for ECB Banking Supervision	68	244	Amendment	<p>As outlined in the comment for paragraph 67, the periods for parallel runs should be subject to discussion and agreement between an institution and the corresponding JST. To ensure a timely release into production upon regulatory approval, the paragraph could be adjusted as follows: "If an extension or a change affecting any of the above items (a) to (d) is classified as "to be investigated" by the EGMA, this upfront implementation should be completed within a sufficient time (recommended to be at least three months) before the date of the application letter. Where the institution notifies ex ante an extension or a change affecting any of the above items (a) to (d), the ECB sees it as best practice for the institution to first run a one-month use test (or non-live implementation) if there is a considerable impact on limit utilisation for certain transactions, netting sets or counterparties that are particularly affected by the change or extension owing to its nature. Implementation of material model changes and extensions to be investigated by ECB should be completed before the date of the application letter within a time coherent with EGMA prescriptions to assess impacts on own fund requirements."</p>	System setups and release procedures differ from firm to firm. The detailed plans should be subject to agreement with the JST to ensure efficiency.
6	Counterparty credit risk	13.2 Principles for ECB banking supervision	99	260	Amendment	<p>Performing regular ongoing model performance monitoring, such as back-testing, is one of the corner stones of internal models. However, for RNIEPE models, it is going to be an impossible challenge to perform back-testing. The main reason being that in order to back-test, there is an indisputable need for a 'true' realisation to compare forecasts or estimations to. Furthermore, even if back-testing was possible, provided that RNIEPE models are more simplistic than the EEPE model(s) and have to rely on stronger assumptions, it is questionable, if under the given constraints, meaningful actions could be derived from back-testing results or if those results would basically confirm under strong assumptions a meaningful interpretation of back-testing results is not possible.</p> <p>We consequently propose to reword paragraph 99 as follows: "In accordance with Article 287(2) of the CRR, the RNIEPE framework and methodologies should be subject to validation and independent review, as set out in further detail in Article 294(1)(d), (g), (k), (m), (n) and (o) of the CRR and Article 288 of the CRR respectively. In this context and where applicable, back-testing of RNIEPE add-ons is seen as beneficial."</p>	Backtesting of RNIEPEs is desirable, but not feasible due to a lack of 'true' data points to compare to.

7	Counterparty credit risk	13.2 Principles for ECB banking supervision	104(b)	262	Deletion	<p>Based on the arguments provided in the comment to paragraph 99 we propose to reword paragraph 104(b) in the same spirit: "The ECB considers that in order to ensure an accurate capture of risks, institutions should strive to identify and monitor⁶⁹ RNIEPE on a regular basis as part of the overall risk management framework. The ECB considers it best practice to use existing processes efficiently to identify RNIEPE. a) [...] b) back-testing as referred to in Article 294 of the CRR; c) [...]"</p>	Backtesting of RNIEPEs is desirable, but not feasible due to a lack of 'true' data points to compare to.
8	Counterparty credit risk	13.2 Principles for ECB banking supervision	107(b)	264	Deletion	<p>We acknowledge that the introduction of the RNIEPE framework is helpful in improving the resilience of the CCR capital estimation, but would like to highlight the concern, that prohibiting the netting of trades impacted by an RNIEPE and the remaining ones, is introducing a significant margin of conservatism into the estimation. While we understand that from a regulatory point of view as high as possible margins of conservatism are desirable one also needs to consider the flip side. The impact number will not inform about the estimated impact, but the impact plus a margin, that is varying depending on the netting set. It will therefore not allow to assess the impact correctly since there is no split between 'real' impact and additional margin of conservatism. We therefore suggest to remove paragraph's 107 sub-paragraph (b).</p>	Changes to the netting rules compared to the EEPE introduce a different "measure" making meaningful comparisons extremely difficult.
9	Counterparty credit risk	13.2 Principles for ECB banking supervision	108(c)	264	Amendment	<p>We would like to bring to the ECB's attention that by flooring the RNIEPE impacts on netting set level to zero the fact that institutions perform diversified business activities across different asset classes and counterparties is neglected. While we agree that in the assessment of the RNIEPE impact(s) diversification effects between different RNIEPEs should not be used to reduce the impact, we think that this requirement is not reflective of the way firms operate and control their business. Hence, we would like to propose the below rewording of the sub-paragraph: (c) The incremental exposure can be any positive or negative number. The calculation of the incremental exposure may result in a negative number if the incorporation of the RNIEPE has a risk-reducing effect. In that case, and in line with paragraph 105, the incremental exposure is set to zero for the respective netting set. For a given RNIEPE, the signed incremental exposures for the respective netting set is to be used in the RNIEPE add-on calculation, while flooring RNIEPE add-on at zero.</p>	Changes to the netting rules compared to the EEPE introduce a different "measure" making meaningful comparisons extremely difficult.
10	Counterparty credit risk	13.2 Principles for ECB banking supervision	113		Amendment	<p>We would like to draw the ECB's attention to the fact that RNIEPEs are, at least in some cases, likely to be burdensome calculations, be it from a technical or process point of view. While we agree to the fact that RNIEPEs need to be refreshed sufficiently often to provide meaningful information we would like to suggest splitting the RNIEPE population into the material items, the ones resulting into a capital overlay/add-on, and the non-material ones. For the material ones we propose an at least quarterly impact assessment, whereas for the non-material ones we propose to reassess the impact on an at least annual basis. The below rewording would incorporate this differentiation: "In accordance with Article 430 of the CRR in conjunction with Article 5(1) of the Commission Implementing Regulation on supervisory reporting, institutions must submit the information relating to own funds requirements with quarterly frequency. Therefore, the ECB considers that in order to assess the adequacy of own funds, institutions should quantify and monitor the RNIEPE and adjust their scope on a regular basis and should update the RNIEPE at least quarterly for any RNIEPE subject to a capital add-on (i.e. material RNIEPE) and annual monitoring for all other RNIEPEs (non-material). Upon supervisory approval, the quarterly update of RNIEPEs subject to a capital add-on could be proxied based on an annual quantification meeting the standard of EGIM section 13.2.3."</p>	The frequency for the re-assessment should distinguish between items resulting in a capital buffer and less material ones.
11	Counterparty credit risk	13.2 Principles for ECB banking supervision	114		Amendment	<p>There are two points to address regarding this paragraph. The first one being that from our point of view firms should be granted the possibility to decide whether they want to measure RNIEPEs in EPE or RWA. This would allow firms to benefit from cases where an RNIEPE mainly impacts transactions with low risk counterparties. This would harmonise the framework since capital overlays are ultimately measured in RWA. Secondly, the denominators of the formulas outlined in sub-paragraphs (a) and (b) may cause unwanted effects. A netting-set with, relative to the firm's EEPE, low materiality might incur a significant RNIEPE impact as the impact assessed only relative to this netting-set not incorporating its materiality relative to the entire portfolio. We would therefore recommend to align the denominators with the ones in (c) and (d) to calculate the impact relative to the materiality of all netting-sets, i.e. the entire portfolio.</p>	The formulas provided are not consistent and can cause significant misinterpretations of impact numbers.