



EUROPEAN CENTRAL BANK
BANKING SUPERVISION

Template for comments

Public consultation on the revised ECB guide to internal models

Institution/Company

Rabobank

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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	General topics	1.8 General principles on climate-related and environmental risks	25	12	Clarification	Last year, the EBA postponed guidance on where to include forward-looking climate and environmental risk in the capital framework (Pillar 1 or 2). This new version of the ECB guide to internal models, avoids explicit references to backward or forward looking climate and environmental risk, which creates ambiguity. The ECB guide should make explicit what is expected for forward looking elements of climate and environmental risk.	The ECB guide should make explicit what is expected for forward looking elements of climate and environmental risk.
2	General topics	1.8 General principles on climate-related and environmental risks	25	12	Clarification	Where climate and environmental risk is mentioned, it is usually accompanied by the guidance to consider it where relevant and material. However, the document does not offer further specification of relevance or materiality re climate and environmental risk. Although materiality is not a new, there are ample choices about its application such as the level (bank, portfolio or client) or abstraction (event, theme or even climate change as a whole). A clear definition would take away a lot of ambiguity and difference in application between banks	A clear definition would take away a lot of ambiguity and difference in application between banks
3	Credit risk	5.1 Structure of PD models	94	90	Clarification	If forward looking climate and environmental risk information should be included in models, there needs to be more guidance around how to include this in models. The forward-looking element is obviously the most important part of climate and environmental risk but there is an inherent potential conflict with the historical nature of the capital models, as the significance and parameter estimated of recent events may not reflect future risks. More specific/practical guidance on how to include forward looking elements in model development is needed.	More specific/practical guidance on how to include forward looking elements in model development is needed.
4	Credit risk	6.1 Realised LGD	143	113	Clarification	If forward looking climate and environmental risk information should be included in models, there needs to be more guidance around how to include this in models. The forward-looking element is obviously the most important part of climate and environmental risk but there is an inherent potential conflict with the historical nature of the capital models, as the significance and parameter estimated of recent events may not reflect future risks. More specific/practical guidance on how to include forward looking elements in model development is needed.	More specific/practical guidance on how to include forward looking elements in model development is needed.
5	General topics	2.6 Reversion to a less sophisticated approach	42	17	Clarification	A distinction should be made in case the ECB proposes or the institutions itself proposes to revert to a less sophisticated approach. Further instructions are needed to clarify ECB expectations regarding the definition and formalising of objectives and intuitive criteria to decide which of the different approaches should be used for the calculation of own funds requirements across the whole portfolio.	To reduce ambiguity
6	General topics	2.6 Reversion to a less sophisticated approach	45	19	Clarification	A distinction should be made in case the ECB proposes or the institutions itself proposes to revert to a SA for specialized lending exposures.	To reduce ambiguity

7	Credit risk	2.2.2	8		Clarification	<p>The paragraph mentions that when applying for a material model change:</p> <p>1) Evidence should be provided that new versions of the IT systems are ready to be put into production once the change is approved,</p> <p>2) The execution of the model and calculation of own funds requirements should be fully replicated in a non-live production environment,</p> <p>3) It should be demonstrated that an appropriate process has been set up to ensure that the full IT implementation will be completed successfully with regard to the date of the implementation of the changed model.</p> <p>Given the requirements in 2) and 3), it is not clear what sort of additional evidence is envisioned in item 1).</p>	If additional evidence is expected, this should be clearly stated.
8	Credit risk	3.1	7		Amendment	There is a typo in footnote 123: 7(a) is repeated twice.	Typo
9	Credit risk	3.7	33, 34		Amendment	There is a reference to non-existent paragraph 0 (used to be paragraph 30).	Error in reference
10	Credit risk	3.7	54		Clarification	Footnote 151 explains that recalibration using the combined default and loss data of the acquiring and acquired institutions is not immediately required if it can be proven that the models of the acquiring institution remain conservative when backtested on the combined historical data, where MoC and downturn adjustments should be excluded from the backtesting. This suggests that the backtesting should be performed based on model best estimates. Is immediate recalibration using the combined historical data of the acquiring and acquired institutions also required if the back testing shows statistically accurate model best estimates?	To reduce ambiguity
11	Credit risk	3.7	55		Clarification	The paragraph states that when the acquiring bank's workout processes are different from those of the acquired bank, the acquiring bank should apply paragraph 33 of EBA/GL/2017/16 for loss data. Paragraph 33 includes two subparagraphs, with only (b) applying specifically to loss data, and (a) rather to default data for PD estimation. If the acquiring bank is required to apply both paragraphs 33(a) and (b), then removing the explicit reference to loss data in paragraph 55 would be more clear than the current formulation. If the acquiring bank is only required to apply paragraph 33(b) on loss data and not paragraph 33(a), then explicitly referring to paragraph 33(b) in paragraph 55 would be more clear than the current reference to paragraph 33 as a whole.	To reduce ambiguity
12	Credit risk	4.2	N/A		Clarification	Prior to using the acquiring bank's models for the acquired bank, is there no need to prove representativeness of the acquiring bank's models with respect to the application portfolio of the acquired bank? Both with respect to risk differentiation and quantification, as would be required for model development by paragraphs 23 and 28 of EBA/GL/2017/16.	To reduce ambiguity
13	Credit risk	4.3	62		Clarification	<p>The paragraph states that when an obligor has exposures both within the ECB jurisdiction and other jurisdiction(s), where different materiality thresholds apply, default should be triggered whenever the materiality threshold is exceeded for 90 consecutive days in a jurisdiction. Moreover, institutions are expected to introduce unlikelihood to pay triggers to make the default status consistent across all jurisdictions. Suppose the definition of default applies on obligor level, and an obligor has exposures in multiple jurisdictions each of which applies a different materiality threshold.</p> <p>(a) In this situation, the criterion for the obligor to default if it is more than 90 consecutive days past due should be applied separately for each jurisdiction that has a different materiality threshold. For example, if the obligor has exposures in three jurisdictions that all apply different materiality thresholds, there should effectively be three default triggers for the past due criterion applicable to the obligor, which should ensure that the obligor is flagged as defaulted whenever it is materially past due for 90 consecutive days in any jurisdiction. Is this understanding correct?</p> <p>(b) Per jurisdiction, we understand that the application of the criteria for days past due default identification should incorporate the outstanding amount and arrears of the obligor from all jurisdictions. For example, if the obligor has arrears of EUR 50 on an exposure in jurisdiction A where the materiality threshold is EUR 100, but also has exposures with no arrears in jurisdiction B, where the materiality threshold is EUR 20, then counting of days past due for the obligor should be performed on the basis of the materiality threshold applicable in jurisdiction B, even though the arrears exist only in jurisdiction A. Is this understanding correct?</p>	Current text is not fully clear
14	Credit risk	4.5	70		Clarification	Why is there a reference to paragraphs 36 to 40 in the EBA Guidelines on DoD on the specific credit risk adjustment default trigger? The connection to write-offs being a potential indication of unlikelihood to pay is not clear.	Current text is not fully clear

15	Credit risk	5.1.1	83(a), 85(a)(b)	Clarification	<p>Paragraph 85(a) states that when distressed restructuring does not apply to a defaulted exposure, the exposure can be classified to non-defaulted status even if there are still past due amounts, provided the past due amounts are not material, or material but less than 90 days past due, and all other conditions of paragraph 71 of the EBA guidelines on DoD are met. Paragraph 85(b) states that when distressed restructuring applies to a defaulted exposure, one of the requirements to return to non-default status is that there are no past due amounts on the exposure according to the contractual agreement after the restructuring arrangements. Thus, a non-distressed exposure may return to non-default status with finite arrears, but a distressed exposure may not.</p> <p>Paragraph 83(a) clarifies that when the definition of default applies at obligor level, the conditions for reclassification to non-default status should be applied to each exposure of the obligor, and the obligor can only return to non-default status when all conditions are met for all exposures.</p> <p>Suppose the definition of default applies on obligor level, and that a given obligor with two exposures A and B is defaulted, with exposure A being non-distressed and exposure B distressed. Exposure B meets all the requirements of paragraph 73 of the EBA guidelines on DoD to return to non-default status, including having no past due obligation after the restructuring arrangement. Similarly exposure A meets all the requirements of paragraph 71, but does have finite past due amounts (material, or not material but less than 90 consecutive days past due, such that the mandatory default trigger is not applicable.) Consequently, the obligor has finite past due amounts through exposure A. Is the interpretation correct that this obligor is permitted to return to non-default status because the conditions of paragraph 71 are met for exposure A, and the conditions of paragraph 73 are met for exposure B simultaneously? Or, is this obligor not permitted to return to non-default status due to the obligor having past due amounts through exposure A, and the requirement of having no arrears due to exposure B being distressed?</p>	Current text is not fully clear
16	Credit risk	5.1.4	95, 173, 202	Clarification	<p>As per Par 95, 173 and 202, independent datasets for model development should correspond not only to random sampling (out-of-sample), but also to different time periods (out-of-time) unless there are no sufficient data available for the training sample.</p> <p>i) Given the phrasing of the above sentence, it seems that ECB considers the out-of-sample to be a higher priority compared to out-of-time for evaluating model overfitting. Clarification would be required if this is indeed ECB's view, or otherwise if rephrasing may be needed.</p> <p>ii) In ECB's view are both out-of-time and out-of-sample testing required in the case of data scarcity? From EBA's supervisory handbook for the validation of IRB models, performing tests on either one of them might be sufficient when data is scarce. However, the same is not explicitly prescribed or mentioned in this article.</p> <p>iii) Can additional guidelines be shared on quantification of data sufficiency; would an institution's independent analysis to prove data scarcity be sufficient in ECB's viewpoint?</p>	An implicit prioritization seems to be given, but it is not clear if that is the intention
17	Credit risk	5.2.2	109	Clarification	<p>Par 109 states that institutions should consider existence of third-party support as a potential relevant driver for risk differentiation when its used extensively for overrides. Can ECB provide further clarification or guidance on quantification of the extent of third-party support required/involved in order for the above to be effective? Is this subject to institution's own judgement and supporting evidence?</p>	Current text is not fully clear
18	Credit risk	5.2.2	122(b)	Clarification	<p>As per Par 122(b), a default on a joint obligor should be counted separately from defaults of individual obligors. Can ECB provide more comprehensive criteria or clarify using an example for the underlying facility structure or individual obligor to joint obligor relationship for an institution to be compliant with the above? For example, if an individual obligor has an underlying facility that is not jointly liable in a joint obligor structure, then that obligor should be counted separately as another Joint obligor. However, if the joint obligor structure has two individual obligors with only one underlying facility, should the Joint obligor default be treated as an additional default in ECB's viewpoint? Clarification required on any specific conditions that must be fulfilled in order to be counted separately. If no specific conditions apply, then a comprehensive example or illustration of this requirement would be beneficial for reference.</p>	Current text is not fully clear
19	Credit risk	5.2.3	122(d)(e)(f)	Clarification	<p>Par 122(d) and (e) states that to calculate ODR, obligors/facilities need to be included in the denominator and where relevant in numerator even when the obligor/facility cannot be observed (or cease to exist) in the observation period. Further 122(e) states that this does not automatically result in application of appropriate adjustments. However, Par 122(f) mentions that sale of credit obligations during the observation period leads to increased uncertainty and hence a MoC/appropriate adjustment need to be considered for the sold obligations.</p> <p>i) Purely from a data standpoint, sold credit obligations during observation would also "cease to exist" in the observation period. Hence, clarification required if 122(d) and (e) are applicable to sold obligations or not.</p> <p>ii) Par 122(d) and (e) seem to be contradictory unless the phrases "cease to exist" or "cannot be observed" does not encompass sold credit obligations in ECB's viewpoint. In other words, the above articles present different/contradictory prescriptions on how to deal with sold credit obligations and rephrasing required in case 122(d) and (e) does not include sold obligations; conversely clarification required if indeed sold credit obligations also fall under "cannot be observed" in historical period category in ECB's viewpoint.</p>	Current text is not fully clear
20	Credit risk	7.4	135	Clarification	<p>As per Par 135, to ensure there are no systematic deviations when comparing the estimated PDs with the LRA default rate of the grades; the direction of divergences across grades should be random regardless of the materiality or statistical significance of the deviations. While the randomness in divergence is understood, its not clear why the statistical significance should be ignored while performing this evaluation. Can ECB provide some more perspective on this?</p>	It is not clear why statistical significance should be ignored
21	Credit risk	8.1	207(b)(i)	Clarification	<p>Par 207 provides the compliance requirements for defining CCF values based on judgemental considerations. However, can ECB provide more comprehensive guidance on application and identification of 'non-material exposures' for application of CCFs since its not very clear from this article?</p>	Current text is not fully clear

22	Credit risk	6.1.3	208		Clarification	Par 108 states that MoC should not affect risk rank ordering & institutions should be able to ensure monotonicity in their final estimates while still reflecting the uncertainty at grade or pool level. Since this requires maintaining a fine balance between appropriate quantifying uncertainties via application of MoC while preserving risk differentiating ability of the model, further clarification is required regarding the level of evaluation of rank ordering for the model. Is it only applicable if MoC is applied at a grade level or also at the level of calibration segment? For example, a model with perfect rank ordering may be calibrated on multiple calibration segments; is the requirement of monotonicity (post MoC) applicable for each of the calibration segments individually or is it applicable at model/portfolio level?	Current text is not fully clear
23	Credit risk	6.1.5	150		Clarification	Par 150 states that institutions should define a proper methodology for the allocation of recoveries and costs to each individual facility in case this information is available only at an aggregated level. In cases where an appropriate allocation to facility level from aggregated level is not feasible, would this requirement be satisfied by application of MoC or appropriate adjustments?	Current text is not fully clear
24	Credit risk	1.8	160(c)		Clarification	Par 160(c) provides information on an institution's selection of a sufficiently long time since the massive disposal in accordance with CRR Art 500. Specifically the condition specified "most of the cases that were incomplete as of the date of the disposals have been closed" involves institution's own judgement and hence is subjective. Would a quantification of this w.r.t. average time of assets in default as of the date of the massive disposal and the MRP be sufficient in ECB's perspective? Further, does ECB require any representativeness analysis to be necessary to arrive at the sufficient time period for disposed vs non-disposed exposures in this context?	Current text is not fully clear
25	General topics	2.6	25		Clarification	The paragraph is a new addition requiring institutions to assess the materiality of climate and environment risks. The paragraph also suggests inclusion of risk drivers which are deemed relevant and material. In this regard, requesting clarification on the following - The data requirements as stated in EBA/GL/2017/16, Section 4.2 would be deemed applicable for such risk drivers? - Given that such data may not be present historically (less than 5 years), how would the requirements pertaining to historical data (cf CRR Art 180 h); 181 i); 182 2)) be applied in such scenarios?	Current text is not fully clear
26	General topics	5.2	42		Clarification	The paragraph is a new addition explaining scenarios leading to reversion to a less sophisticated approach. In this regard, requesting clarification on the following - Based on the Par 42(d)iii), it is expected that the reversion to a less sophisticated approach is not aimed at reduction of own funds requirements. What would be deemed as an appropriate threshold or benchmark for such an analysis? - What would be the expectations for the Internal validation function in this regard? Should it play a role in assessing these requirements in case of a reversion proposal?	Current text is not fully clear
27	General topics		92		Clarification	There is a change of wording in this paragraph that can be interpreted as the following. In case of material changes, the review from internal audit function can happen after the submission to the competent authority for approval. Is this understanding appropriate?	To avoid misinterpretation