EUROPEAN CENTRAL BANK

BANKING SUPERVISION

# Template for comments

## Public consultation on revisions to the ECB's policies concerning the exercise of Options and Discretions (O&Ds) in Union law

**Institution/Company**

AFME/ISDA

### Contact person

**Mr/Ms**

**First name**

**Surname**

**Email address**

**Telephone number**

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

**General comments**

AFME and ISDA have submitted a separate cover note with our general comments and appendices on the Trading Book and Article 49(1). Please refer to this.

# Template for comments

## Public consultation on revisions to the ECB's policies concerning the exercise of Options and Discretions (O&Ds) in Union law

### ECB Regulation on Options and Discretions under Union law

**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 article/chapter/paragraph, where appropriate;**
- **you indicate whether your comment is a proposed amendment, clarification or deletion.**

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| **Deadline:** | midnight CET on 25 January |

| ID | Section | Type of comment | Detailed comment | Concise statement as to why your comment should be taken on board | Name of commenter |
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| 1 | Transitional arrangements for ECAI credit assessments of institutions | Amendment | The industry welcomes the extension of the transition period up to July 26 provided for by the consultation. However, given the low availability of compliant ratings in the market, banks consider that ECB should be ready to extend this deadline until minimum 3 large agencies provide compliant ratings and this should be reflected in the recital of the regulation, especially given that in CRR3 there is a possibility for a deadline until 31 December 2029 to comply with this requirement, as is also foreseen in Basel. Furthermore, due to both the lack of available or forthcoming market solutions in compliance with the applicable Regulation (CRR3), and the fact banks cannot demand that ECAIs align with the aforementioned Regulation by the established deadline of the transitional period, we suggest the ECB also explores, together with ESMA, the possibility of alternatives to xgs ratings in the longer term – for instance Moody's Baseline Credit Assessment (BCA), the Stand Alone Credit Profile Rating (or "SACP"), or Fitch's Issuer Default rating (or "IDR").<br><br>It is important to allow the ESAs to conduct an ECAI mapping process and also allows CRAs such as S&P and Moodys to get their new rating product ready for market (we think that relying on a single rating would not only be problematic from the perspective of counterparty coverage but would also create issues over quality/ cost). Currently Fitch is the only rating agency that has developed a new XGS rating (our understanding is that other CRAs such as S&P are developing proxy step ratings - however it is not clear whether these will be compliant with the provisions of CRR3 Article 138(g), and therefore whether institutions will be able to use these with confidence. It should be noted that, while banks will make every effort to support and promote rating agencies and ESMA taking the necessary steps to develop the new ratings and undertake the requisite ECAI mapping process, it is not within the gift of banks to deliver this.<br><br>Further, ESMA has noted to industry the undesirability of market disruption in the rating space and the timeline for endorsing a new rating scale is expected to take up to 18 months. We would also highlight that the EBA's assumptions when providing Basel III policy advice on this matter: (i) there would be a transitional period; and (ii) the CRAs would be able to easily issue usable ratings. Both of these points are at risk now (refer to pages 41-43 of the EBA's policy advice). | | AFME/ISDA |

# Template for comments

## Public consultation on revisions to the ECB's policies concerning the exercise of Options and Discretions (O&Ds) in Union law

### ECB Guide on Options and Discretions under Union law

**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 article/chapter/paragraph, where appropriate;**
**- you indicate whether your comment is a proposed amendment, clarification or deletion.**

| **Deadline:** | midnight CET on 25 January |
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| 1 | Section 2, Chapter 1, Paragraph 15 | 23 | Deletion | Art. 24(2) CRR allows competent authorities to use IFRS for prudential purposes, including in cases where the national applicable accounting framework requires the use of n-GAAP. We welcome that the ECB basically maintains the decision not to exercise the option set out in Art. 24(2) CRR in a general manner. However, we disagree with the ECB's intention to consider exercising the option on a case-by-case basis (Par 15 subpara 2: "However, the ECB may consider exercising the option set out in Article 24(2) on a case-by-case basis, if duly justified from a supervisory perspective.").<br><br>Institutions for which the national applicable accounting framework requires the use of n-GAAP should continue to be allowed to use n-GAAP for prudential purposes, unless banks request the use of IFRS. The valuation of assets and off-balance-sheet items and the determination of own funds in accordance with IFRS is associated with high processual and IT costs. | It should be noted that some international banks would be required to follow three sets of accounting standards (e.g. US GAAP, IFRS, and n-GAAP), with substantial associated costs. Where the difference between accounting standards forms a material impediment for the benchmarking of peer banks for a particular regulatory issue or concern, a targeted, alternative solution should be explored rather than enforcing a full implementation of another accounting standard. | AFME/ISDA |
| 2 | Section 2, Chapter 1, Paragraph 5 | 27 | Amendment | The current ECB proposal entails to risk weight non-CET1 instruments issued by insurance sub. covered by 49(1).<br>This is a material change of the current framework which modifies the functioning of the Danish compromise set out in the level 1 text and contradicts Articles 49, 56 and 66 of CRR.<br>1. Art 49.1 allows, under certain circumstances, to risk weight own funds instead of deducting them but is relating to CET1 only. Indeed art 49 is part of Sub-section 2: “exemptions from and alternatives to deduction from Common Equity Tier 1 items” within Section 3 " Deductions from Common Equity Tier 1 items, exemptions and alternatives", within Part 2 “Own funds”.<br>2. It is further evidenced by the fact that Part 2 is followed by:<br>• Part 3 "Additional category 1 capital" where article 56 request to deduct AT1 subscribed by the bank<br>• And Chapter 4 for "Tier 2 capital" where article 66 requests to deduct T2 subscribed by the bank<br>We are of the view that ECB should not change the level 1 text application this way, which is only in the gift of co-legislators. Hence, Article 49.1 must not be extended to AT1 and T2. It would also be against the principle of Article 49.1, the last paragraph of which states that “The method chosen shall be applied in a consistent manner over time.”<br>It should be noted that, if such changes were to be made, Articles 56 and 66 would also have to be adapted to prevent unjustified cumulation of risk weighting and deduction on the same instrument, however this is also something which is not within the power of the ECB to do. We therefore recommend the ECB liaises with EC to ensure the consistency between the level 1 text and its implementation. Indeed, if the ECB proposals were to be carried forward it remains unclear how these could be operationalised, given banks would need sufficient time to adapt their structures. Further, had the banks had known (or even imagined such a possible treatment), they would probably have organized their issuances differently from the start.<br><br>Please refer to Appendix 2 in the cover note for the detailed analysis called "Detailed comment regarding the proposed implementation of Article 49(1) in the ECB OND guide". | Guide should be amended so that the permission only cover CET1 instruments. | AFME/ISDA |
| 3 | Section 2, Chapter 2, Paragraph 8 | 28 | Amendment | We would appreciate if the requirements and documents to be provided would be taken into account in a proportionate manner to the applied reduction in own funds. This means that in the case of very small amounts of applied reductions in own funds (e.g. with the effect on Capital Ratios <10bp), lower or graduated documentation should be required. This refers to the scope and as well to the recentness of the documents. In cases with very low materiality, it should also be possible for the ECB (the JST's) to make a decision solely on the basis of the ECB's already available information. We also understood from JSTs that this could make the process much easier for the ECB and Banks, without any additional risks.<br><br>In this respect the ECB may also want to introduce the same principle in section 3 on 104(4) regarding documentation ("For the purpose of assessing the request of the institution under Article 104(4) of the CRR, the ECB expects that the credit institution presenting the application submits the documents listed in points (i) to (x) below, unless they have already been provided to the ECB. In the latter case, banks should clearly set out the circumstances under which those documents have been provided."). | Operational burden for institutions and ECB (JSTs). | AFME/ISDA |
| 4 | Section 2, Chapter 2, Paragraph 9 | 29 | Amendment | This does not reflect the intention of the latest changes of the RTS on Own Funds (DR 2014/241) which was to reduce the burden for all parties involved in the approval process. Against this background, we would appreciate if the ECB (the JST) would be able to refrain from the requirement of new documents in the case of unchanged renewals of continuing general prior permission (same amount, small amount) on a case-by-case basis. In those cases it should also be able to make a decision on the basis of the already available information.<br><br>In this respect the ECB may also want to introduce the same principle in section 3 on 104(4) regarding documentation ("For the purpose of assessing the request of the institution under Article 104(4) of the CRR, the ECB expects that the credit institution presenting the application submits the documents listed in points (i) to (x) below, unless they have already been provided to the ECB. In the latter case, banks should clearly set out the circumstances under which those documents have been provided."). | Operational burden for institutions and ECB (JSTs). | AFME/ISDA |

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| 5 | Section 2, Chapter 2, Paragraph 15 | 31 | Deletion | There is a critical inconsistency between the ECB draft guidance in point 15 of the chapter on Own Funds and the amended Article 84 of CRR3 regarding the treatment of minority interests for subsidiaries in third countries:<br>Article 84 of CRR3 for Third-Country Subsidiaries:<br>The text specifies unambiguously that for third-country subsidiaries, the comparison mechanism should take the lower of:<br>(i) Local supervisory regulations applicable to the subsidiary (individual capital requirements).<br>(ii) Local supervisory regulations applicable to the subsidiary but on a consolidated basis (i.e., accounting for intragroup exposures).<br>This makes it clear that the comparison mechanism is entirely based on the local supervisory framework for third-country subsidiaries, without reference to CRR-specific capital requirements and without leaving this issue to the discretion of the supervisor. In contrast to this, what it is actually left to the supervisory discretion is the possibility for the competent authorities to allow the entities to choose either of the two options (no matter which is the lesser) "the competent authority may allow an institution to subtract either of the amounts referred to in point (a)(i) or (ii), once that institution has demonstrated to the satisfaction of the competent authority that the additional amount of minority interest is available to absorb losses at consolidated level".<br>However, the ECB guidance suggests applying the lower of:<br>(i) CRR requirements extended to the subsidiary at a consolidated level.<br>(ii) Local third-country supervisory requirements.<br><br>Thus, apart from the fact that the ECB has not been granted with the discretion to modify the methodology for calculating these minority interests, the ECB does it by deviating from the article 84 in the CRR text as it does introduce CRR-derived consolidated requirements into the comparison for non-EU subsidiaries which does create a disadvantage for non-EU subsidiaries. | The ECB makes an interpretation of Art. 84, which is not aligned with CRR text. Article 84 CRR3 establishes a mandatory methodology for calculating minority interests and does not grant discretion to supervisory authorities. Therefore, interpreting its provisions falls outside the stated purpose of the O&D Guide, which is to clarify the application of options and discretions available to supervisors. Also, the ECB text contradicts the intent of the revised CRR3, which explicitly restricts the comparison to the local regulatory framework. The ECB guidance effectively imposes CRR-level requirements on non-EU subsidiaries, which undermines the recognition of local supervisory regulations as independent and tailored to the jurisdictional risks. This creates an unnecessary and unwarranted disadvantage for non-EU subsidiaries by potentially undervaluing their minority capital contribution based on requirements not reflective of their local risk environment. | AFME/ISDA |
| 6 | Section 2, Chapter 2, Paragraph 16 | 31 | Amendment | Paragraph 16(1): Regulation 2024/1623 (“CRR3”) has in effect amended Art. 84 (1) CRR by adding a new subparagraph which provides that institutions may derogate from the "lower of the two requirements“-rule of Art. 84 (1) (a) CRR when calculating the amount of minority interest that is eligible for being recognised in the consolidated CET1 capital of the consolidated banking group:<br>“By way of derogation from point (a) of the first subparagraph, the competent authority may allow institutions to subtract either of the amounts referred to in point (i) or in point (ii), once the institution has demonstrated to the satisfaction of the competent authority that the additional amount of minority interest is available to absorb losses at consolidated level;”.<br>The revised ECB’s guide on options and discretions in chapter 16 (p. 31 et. seq.) establishes criteria to demonstrate loss absorbency on group level that in our view go significantly beyond the legal rationale of the CRR rules on minority interest recognition.<br>The ECB’s explanatory document introduces a new requirement for the automatic intragroup transfer of resources by stating the following:<br>“Since capital held by third-party investors covers the losses suffered by the issuing entity only, in order to make it possible for this capital to also absorb losses at consolidated level, an automatic intragroup transfer of resources would be needed.”<br>In our view, the requirement for an automatic intragroup transfer of resources to demonstrate loss absorbency for the additional amount of minority interest recognised is inconsistent with the current requirements for minority interests and not supported by the legal rationale of the CRR.<br>As articulated by the “Fiche on minority interest” deployed during the CRR 3 legislative process to support consensus between the legislators on this issue (and attached with our submission for reference), the current minority interests recognised are considered loss absorbent on group level although there is no automatic intragroup transfer. The reasoning of the Fiche acknowledges the economic and legal reality that a loss is absorbed in the subsidiary (where the minority interest originates) by the own funds of the subsidiary (and not by the own funds of other undertakings that belong to the same group). It is considered sufficient that there are regulatory capital requirements based on which the subsidiary will maintain the own funds needed to fulfil them. In the current rules, this is limited to the "lower of the two requirements“-rule of Art. 84 (1) (a) CRR. | General comment on why proposed requirement on automatic loss transfer are legally impossible to fulfil and not aligned with rationale of underlying CRR rules on minority interests (request for deletion of blanket automatic loss transfer requirements and replacement with adequate criteria on loss absorption). See also ID 10 regarding the provision of the legal opinion to support this point. | AFME/ISDA |
| | | | | In our view, the same definition of loss absorbency should also apply for the new derogation. I.e. the minority interest recognised can be considered loss absorbent at group level if the amount is limited to a capital requirement applicable to the subsidiary.<br>“In more practical terms this means, in case the subsidiary’s own funds instruments are written down or converted, the generated loss absorption is confined to the subsidiary. Therefore, the recognised minority interest is limited to the requirements applicable to the subsidiary”.<br>Note that for the new CRR 3 derogation from the "lower of the two requirements“-rule of Art. 84 (1) (a) CRR, this may also relate to the capital requirements that apply to the subsidiary on the consolidated level (under Art. 84 (1) (a) point (ii) CRR).<br>Under the CRR 3, deviations from the "lower of the two requirements“-rule of Art. 84 (1) (a) CRR are possible, provided sufficient loss absorbency of the additional amount (which is based on a regulatory requirement that applies to the subsidiary under Art. 84 (1) (a) point (i) or (ii) CRR) is demonstrated by the institution (e.g. that the subsidiary continuously steers its own funds above the capital requirements that apply to it on the consolidated level, and that the parent can ensure that the subsidiary meets its consolidated capital requirements, Art. 84 (1) (a) point (ii) CRR).<br>Therefore, we see no basis in the regulation for requiring an automatic intragroup transfer for the additional amount under the derogation introduced by the CRR 3.<br>Moreover, if loss absorbency would be defined such that an automatic intragroup transfer via the provisions of own funds instruments would be required, it would be impossible to fulfil such a requirement. Apart from legal impediments in corporate law of European countries, this is because any subsidiary that is subject to own funds requirements on a standalone basis would not be able to meet the requirement for provisions for automatic absorption of losses incurred by other group entities without violating the qualitative requirements for the recognition of the subsidiary’s own funds instruments under the CRR and IFR.<br>During the consultation process the ECB has indicated that the rules for the calculation of the minority interest are embedded in the Basel accord and the ECB must be compliant with the principle stipulated there. In this respect we would underline that the CRR3 is how the EU legislators have determined to apply the Basel accord and this is what should underpin the ECB's OND guide. We would note in any case, that the Basel text explanation of minority interests (Definition of capital in Basel III – Executive Summary) focuses on the concern that the subsidiary’s capital could be distributed to minority shareholders (“As surplus capital in the subsidiary, that is, more than the statutory minimum requirement, could be repaid to the holders of the non-controlling interest”). The necessity of an automatic loss transfer for the recognition of minority interests is not indicated in this text. | | |
| 7 | Section 2, Chapter 2, Paragraph 16 | 31 | Amendment | Paragraph 16(1): Specifically regarding the requirement “whether the provisions governing the instruments owned by persons other than the undertakings included in the consolidation […] include loss-absorption mechanisms that are automatically activated in the case of losses suffered by other undertakings included in the consolidation […] “. If loss absorbency were to be defined such that an automatic intragroup transfer would be required, it would be impossible to fulfil such a requirement. This is because a subsidiary that is subject to own funds requirements on a standalone basis would not be able to meet the requirement for the automatic absorption of losses incurred by other group entities without violating the qualitative requirements for the recognition of the subsidiaries’ own funds instruments under the CRR and IFR.<br>CET1 instruments by design absorb the losses of their issuer (e.g. the issuing institution), but not the losses of e.g. other subsidiaries of an ultimate parent.<br>In company law, stocks of stock corporations are part of share capital of the stock corporation that absorb the losses of the stock corporation, which is not liable for losses incurred by other entities in a wider or different consolidation circle of a group. The assessment of the eligibility of CET1 instruments under the CRR is also tied to a classification as stocks in the sense of the applicable national company law (see the EBA’s list of capital instruments that competent EU and EEA authorities have classified as CET1). Likewise, in respect of 3rd country subsidiaries, local boards typically have a responsibility (often even legal responsibility) to work in the best interests of their entity, and not in the best interests of the Group, so they could not agree to such a mechanism. Local regulators are unlikely to accept such a mechanism either.<br>Further, Art. 28 (1) (i) CRR on the loss absorbency of CET1 instruments requires that “compared to all the capital instruments issued by the institution, the instruments absorb the first and proportionately greatest share of losses as they occur, and each instrument absorbs losses to the same degree as all other Common Equity Tier 1 instruments”. | The requirement for automatic loss transfer is legally impossible to fulfil - a subsidiary that is subject to own funds requirements on a standalone basis would not be able to meet the requirement for the automatic absorption of losses incurred by other group entities without violating the qualitative requirements for the recognition of the subsidiaries’ own funds instruments under the CRR and IFR (request for deletion of blanket automatic loss transfer requirements and replacement with adequate criteria on loss absorption). | AFME/ISDA |

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| | | | | This requirement for instruments to absorb losses and to be transferred to other entities in a legally binding contractual way moreover causes the following issues:<br><br>•The creation of AT1/T2 instruments that absorb losses pari passu with CET1 instruments could endanger the CET1 instruments of the subsidiary. Moreover, it would be doubtful if CET1 instruments that designed to absorb losses of other group entities would still be available to absorb the losses of their issuer first, as required by Art. 28 (1) (i) CRR. The inclusion of mandatory distributions in the provision of the subsidiary's CET1 instruments to cover losses of other group undertakings would also violate the requirements for CET1 instruments, in this case Art. 28 (1) (h) CRR ("the conditions governing the instruments do not include any obligation for the institution to make distributions to their holders and the institution is not otherwise subject to such an obligation").<br>•For AT1/T2 instruments, it would not be aligned with the concepts of AT1/T2 loss absorption if the AT1/T2 instruments of a subsidiary would absorb the losses of its ultimate parent and of any "upstream" subsidiary of the parent. If e.g. the AT1 instruments of the subsidiary would be written down due to such losses, the requirement of Art. 54 (3) CRR (that the amount of instruments recognised in AT1 items is limited to the minimum amount of CET 1 items that would be generated if the principal amount of the AT1 instruments were fully written down or converted into CET1 instruments would no longer be met, since this relates to the subsidiary and not to the wider consolidated group of entities.<br>•If the subsidiary's own funds instruments (CET1/AT1/T2 instruments) would equally absorb losses (here: of other group entities), this could endanger their ranking.<br>•Permanence: CET1 eligibility criteria is standardised across the globe and most if not all jurisdictions require CET1 instruments to be perpetual without incentives to redeem. The request of the ECB would contravene the permanence of the instruments and render them ineligible locally. The requirement contravenes Basel III's emphasis the instrument is available to the issuer in perpetuity. | | |
| | | | | •Subordination: CET1 instruments or other non CET1 own funds instruments must absorb losses according to the hierarchy of losses and CET1 itself must be the most subordinated claim. A contract stipulating transfer of resources will inevitably disrupt the hierarchy and make the instruments ineligible.<br>•Preferential treatment: CET1 instruments cannot have features that enhance certain stakeholders at the expense of loss absorption<br>•Insolvency: the write down of the instruments will not support the solvency or financial stability of the issuer causing systemic and contagion risks in the region<br>•Going concern: CET1 instruments are meant to write down on a going concern basis and not in any other circumstances<br>•Market confidence: Third party investors will perceive these instruments as weaker or less loss absorbing potentially raising concerns about the credibility of the issuer.<br>•It would be highly impractical for banks to approach all 3rd party investors to change the terms and conditions of the instruments they are invested in to meet the ECB requirements.<br>•It could also have accounting or tax impacts for the holder of the instrument - including a clause in a new instrument, especially Tier 2, which goes beyond the statutory provisions is likely to fail the IFRS 9 Solely Payments of Principal and Interest (SPPI) test for the holder of the asset (the third party). The instrument would be initially recognised at fair value and would subsequently be classified and measured at Fair Value through Profit or Loss ('FVTPL'). It could be an issue also for existing instruments should a bank venture into changing the terms. The P&L volatility for the holder of the asset (third party) could exist also because there may be no accounting off-set (if the asset is funded by a liability at Amortised cost). It depends however on the accounting policy of the investor and whether the existing instrument would fail the SPPI test or not. The implication here is that the financial asset will likely be derecognised (held at amortised cost) and a new asset is recognised. The difference between the carrying amount of the old instrument (amortised cost) and the Fair Value of the newly recognised instrument will result in a P&L impact.<br>• When an issuer tries to change existing instruments (which will be the case for all banks), international law jurisdictions are stringent in what can be achieved and would require some sort of consent from the investor to changing the instrument. Moreover, such a material change in the terms and conditions of a pre-existing instrument would be considered as the issuance of a new instrument (see EBA Q&A 2013_16). An instrument could have multiple investors (AT1) and this becomes almost impossible to achieve i.e. tracing all investors for their consent. In some cases investors require the exchange of the instrument for another one with the modified T&C and require a fee to be paid which can be substantial. Moreover, investors could demand a premium on top of the normal yield paid if the clause provides for loss absorbing triggers beyond those of the entity itself (investor would have to absorb the risks of other entities in the group). This will inevitably have a cost of capital and be detrimental/too expensive to pursue.<br><br>Finally we would request the ECB clarify if this requirement is only characterising AT1 and Tier 2 instruments? CET1 instruments per se are inherently loss absorbing, thus the above does not make sense for CET1 instruments. | | |
| 8 | Section 2, Chapter 2, Paragraph 16 | 32 | Amendment | The Guide's requirements for an automatic intragroup transfer are especially unsuitable for cases where the stand-alone capital requirements of the subsidiary are lower (i.e. where the institution wants to apply Art. 84 (1) (a) point (ii) CRR instead) – as evidenced by The "Fiche on minority interest".<br><br>The "Fiche on minority interest" explains the rationale of the pre-CRR 3 „lower of the two requirements"-rule as follows: "to ensure that the risk and capital allocated to the subsidiary do not exceed those determined at the consolidated level" (see the part of the text starting with "however"):<br><br>"The rationale for limiting the recognition of minority interests is that only the amount of minority interests that would cover losses on consolidated level should be recognised at consolidated level. […]<br>In more practical terms this means, in case the subsidiary's own funds instruments are written down or converted, the generated loss absorption is confined to the subsidiary. Therefore, the recognised minority interest is limited to the requirements applicable to the subsidiary. However, to ensure that the risk and capital allocated to the subsidiary do not exceed those determined at the consolidated level, a second safeguard was introduced, which limits the recognition to the requirements on consolidated level. The lower of the two levels should be applicable, ensuring that only that part of own funds is recognised on a consolidated level, which would absorb losses attributable to the group."<br><br>The above explains that the cap at the capital requirement from a group perspective was deemed necessary to align the amount of minority interest recognised with the amount of risk considered, i.e. to cap the recognition of minority interest in cases where the group's consolidated capital requirement of the subsidiary is lower than the subsidiary's standalone capital requirement. This cap ensures the loss absorbency on group level, as it restricts the minority interests recognised on group level to the capital requirements applicable on group level for the subsidiary. | Current requirements on automatic loss transfer are legally impossible to fulfil and not aligned with rationale of underlying CRR rules on minority interests (request for deletion of blanket automatic loss transfer requirements and replacement with adequate criteria on loss absorption). | AFME/ISDA |
| | | | | The CRR3 allows to derogate from the currently irremovable constraint of "the lower of the two levels should be applicable" condition and it provides institutions with the opportunity to demonstrate to the competent authority that the higher amount would also be loss absorbent at group level. In order to recognise this additional amount of minority interest at group level, it is necessary to demonstrate that this amount is available to absorb losses at the consolidated level.<br><br>In this context it is important to distinguish the two possible scenarios with regards to minority interest recognition, namely<br>(a) a situation where the minimum capital requirement at the standalone subsidiary level is lower than the requirement from a group contributory perspective; and<br>(b) a situation where the standalone requirement is higher than the group contributory one;<br><br>In our view, to recognise an additional amount of minority interest at group level under the new CRR3 rules, in category (a) it must be demonstrated that there is sufficient capital in the subsidiary where the minority interest originates to cover the higher group requirements for the subsidiary. In this situation, loss absorbency on group level does not require that minority interests cover losses outside of the subsidiary where the minority interest originates. Instead, it is required to demonstrate that the subsidiary has sufficient capital to cover its higher capital requirement from a group perspective.<br><br>We therefore suggest to amend the O&D Guide accordingly and to differentiate the loss absorbency requirements for the recognition of additional amounts as minority interests in alignment with the legal rationale of the CRR. | | |
| 9 | Section 2, Chapter 2, Paragraph 16 | 32 | Amendment | Paragraph 16(1): Regarding the requirement "if those undertakings are subject to write-down or conversion of their capital instruments or eligible liabilities pursuant to Article 59 of the BRRD". This second criterion relates to "Article 84(1), point (a), of the CRR", i.e. the rules on the inclusion of certain CET1 items (such as CET1 instruments) of the subsidiary in the consolidated CET1 capital and refers to: "if those undertakings are subject to write-down or conversion of their capital instruments or eligible liabilities pursuant to Article 59 of the BRRD". It is not clear to us what is meant by "write-down or conversion" with respect to CET1 instruments and how this could be achieved for CET1 instruments.<br>We also note that it is unclear to which entity this requirement applies and under which circumstances the write-down of conversion must be triggered.<br>The wording "[…] loss-absorption mechanisms that are automatically activated in the case of losses suffered by other undertakings included in the consolidation […] or if those undertakings are subject to write-down or conversion of their capital instruments or eligible liabilities pursuant to Article 59 of the BRRD" suggests that the criterion applies to the undertaking that has incurred the loss. However, based on the context, we assume it applies to the subsidiary from which the minority interest originates.<br>We further assume that the write-down or conversion requirements apply to AT1 or T2 instruments issued by the subsidiary from which the minority interest originates, since a conversion of CET1 instruments would not make sense.<br>Equally, it is not clear under which circumstances the write-down or conversion must be triggered. In a SPE group, write-down or conversion will not be triggered automatically by the resolution authority for the own funds instruments of subsidiary A if another subsidiary B suffers losses (the idea would rather be that losses are effectively passed on to the resolution entity). | Lack of clarity of application on the write down criterion with regard to minority interests. Current requirements on automatic loss transfer are legally impossible to fulfil and not aligned with rationale of underlying CRR rules on minority interests (request for deletion of blanket automatic loss transfer requirements and replacement with adequate criteria on loss absorption). | AFME/ISDA |

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| 10 | Section 2, Chapter 2, Paragraph 16 | 33 | Amendment | Regarding "Documentation of the application of the derogation from Articles 84(1), point (a), 85(1), point (a), and 87(1), point (a), of the CRR" point (ii): In line with our comments on para 16(1), a leading international law firm has indicated that, based on the current drafting of the requirement for an opinion and the lack of clarity around the provisions of the loss-absorption mechanism (as discussed below), it would be challenging to issue an opinion which confirms that "the loss-absorption mechanisms referred to under point (1) above are automatic, effective and enforceable" if the instruments are subject to write-down.<br><br>Specifically, is not very clear to said legal firm what kind of automatically activated loss-absorption mechanisms would be required to be included in the provisions governing instruments issued by a subsidiary where the instruments are not subject to write-down.. Specifically, they raise the following queries:<br>•What type or scale of loss must be suffered by a group company in order to trigger the mechanism (at the moment, there is simply a generic term of “losses” used which seems to be quite a low bar); how this would be determined (and by whom).<br>•What mechanism could be included in the terms of the instruments where the instruments issued by the subsidiary are shares constituting CET1 at the subsidiary level or are Additional Tier 1 instruments already accounted for as equity on a consolidated basis (for example, for an English company which is a subsidiary of an EU bank, including a clause which effects a cancellation of ordinary shares in pre-defined circumstances would be very problematic, due to the restrictions on reductions of capital under English company law and similar restrictions may exist under other corporate law regimes);<br>•a loss-absorption mechanism in CET1 instruments is likely to cut across the CET1 eligibility requirements in CRR Art 28(1)(f) and (g), noting that the clarifications included within CRR Art 28(2) would not extend to such loss-absorption mechanism unless it is executed within a resolution procedure or at the direction of a resolution authority;<br>•or how any requirement to transfer resources to or directly absorb losses of other group companies (if this is required) would be compatible with the conditions that must be met in order for the instruments to qualify as regulatory capital of the subsidiary. In this respect, we would draw a comparison with the approach taken to Profit and Loss Transfer Agreements, which are incompatible with the eligibility requirements for CET1 instruments (as per the EBA Q&A 2018_3675). Depending on how it is structured, there are elements of the automatic loss transfer mechanism discussed here that could be similar in nature to a Profit and Loss Transfer Agreement – e.g. if another subsidiary in the group were suffering losses, the CET1 instruments of the other subsidiary would be written-down and there could then be an obligation to transfer the resources generated by such write-down to the parent/subsidiary suffering losses. In that scenario, we would assume that the EBA applies the same analysis to the automatic loss transfer mechanism as it does to Profit and Loss Transfer Agreements, vis-à-vis CET eligibility.<br>From the industry's perspective, the latter is not possible - the common stocks of the subsidiary that foresee an automatic loss absorption in case of losses of any other subsidiary of the ultimate parent would no longer qualify as CET1 instruments. | Based on feedback from an international law firm, the current drafting of 16(1) (See ID 6 and 7), and the lack of any materiality test in relation to covering any obstacles contained within "legally binding arrangements", it will be challenge for a legal firm to provide such an opinion. | AFME/ISDA |
| | | | | Moreover, the legal firm notes that in any event, legal opinions on the provisions of instruments do not generally comment on whether a provision is 'automatic' or 'effective' as they are usually restricted to whether the provision is enforceable under the relevant governing law (and would be subject to customary qualifications, e.g., as to the effects of insolvency laws). Such a mechanism would also be novel in the market and would therefore need to be acceptable to external investors in the instruments – there are, therefore, commercial implications that need to be considered Indeed, from the industry's perspective we do not see a situation in which an investor to want to invest in stocks that do not only cover the losses of their issuer, but also of any other company in the same banking group, including unforeseeable further changes to the group structure (on top of which the investor has zero influence).<br>The legal firm also shared more fundamental concerns with the requirement for that the opinion confirm that "there are no obstacles to the prompt transfer of resources resulting from either applicable legislative or regulatory acts (including fiscal legislation) or legally binding agreements" and address whether there are obstacles to the transfer of "resources generated through the activation of the loss-absorption mechanisms under point (1)". It is unclear what this means because it is unclear what type of loss-absorption mechanism will satisfy the requirements of point (1). However, if the mechanism in question is a write-down mechanism for obligations accounted for as liabilities, then the activation of the write-down will not 'generate resources' as such but will rather result in a reduction of liabilities and an increase in reserves. The opinion wording normally addresses the ability to transfer assets, normally by paying a dividend to the parent company, but it would not be possible to identify whether the cash or other assets transferred by way of dividend is any way attributable to or connected with the write-down. Again, the legal firm believes that a requirement to transfer resources to other group companies could certainly be incompatible with the instruments being classified as regulatory capital of the subsidiary.<br><br>For background, undertakings included in the consolidation that have issued relevant instruments will normally be:<br>§ companies subject to restrictions under company law on the payment of dividends or making other distributions (e.g., requiring them to have adequate distributable reserves, to comply with requirements for creditor protection in relation to reductions of capital and requiring directors to consider the interests of the company and possibly other stakeholders when making distributions); and<br>§ regulated entities subject to solo or sub-consolidated minimum regulatory capital requirements and buffer rules that effectively restrict the payment of dividends or making of distributions and which may require consent for the reduction or early repayment of capital instruments held by the parent undertaking (and regulators may have powers to intervene and restrict the payment of dividends or making of distributions).<br><br>Regarding the requirement for the opinion to cover any obstacles contained within “legally binding arrangements” – as no materiality test is applied to this assessment, this is likely to involve a detailed due diligence review by an external counsel of all legal arrangements that the subsidiary in question (and potentially other entities in the group) has signed up to. This could prove to be a prohibitive exercise for a banking group to undertake. | | |
| 11 | Section 2, Chapter 2, Paragraph 16 | 33 | Amendment | Regarding "Documentation of the application of the derogation from Articles 84(1), point (a), 85(1), point (a), and 87(1), point (a), of the CRR": point (ii) The ECB requires firms to get a legal opinion from a firm an external third party "established in the EU" to support the requirements in para 16(1). This is disproportionate and out of line with the requirements for other existing legal opinions in the ECB's guide, which do not require the legal opinion to be established in the EU (they only require a legal opinion to be issued by "an external independent third party or by an internal legal department"). No lawyer can/will give a legal opinion on a jurisdiction for which he/she is not qualified. For the case at hand, the necessary qualification would encompass not only banking regulation, but also national company law etc. | If there is to be a requirement to get a legal opinion then it should not be limited to a legal firm established in the EU. | AFME/ISDA |
| 12 | Section 2, Chapter 3, Paragraph 3 | 33-34 | Clarification | The text requires additional clarification where it states "The ECB is of the view that, for instruments listed in Article 104(3) of the CRR, where there is a potential overlap with Article 104(2), points (d) to (i), of the CRR, Article 104(4) of the CRR does not apply and the relevant positions must be assigned to the non-trading book".<br><br>The guide implies that if there is a borderline case when deciding between the trading book and non-trading book, the institution should opt for the non-trading book classification. This would imply that if, for example, an institution has a TRS or CIU with a basket of equity with some underliers unlisted, that the institution would have to put the entire amount under the non-trading book, even if there are mitigating actions. This example does not make sense from a risk management perspective. | The guide does not take account of materiality of the position or the quality of the mitigating actions. See ISDA white paper on CIUs (https://www.isda.org/2024/12/13/frtb-implementation-challenges-capitalization-of-funds/), which offers a recommendation to introduce a materiality threshold that would allow CIUs to remain in the trading book if their banking book holdings are immaterial. | AFME/ISDA |
| 13 | Section 2, Chapter 3 | 33-34 | Clarification | This comment pertains to the scope of the guide. Given the proposed framework does not refer to internal hedges, it is assumed to apply exclusively to external transactions. | The guide refers to Article 104(2)(d), which deals with the classification of instruments. Under IFRS, internal trades are removed. | AFME/ISDA |
| 14 | Section 2, Chapter 3, Paragraph 3 | 33 | Clarification | The text states "The ECB understands that any position in an instrument referred to in points (d) to (i) in Article 104(2) of the CRR should be designated as a trading book instrument when it is first recognised on the books of an institution, unless the institution has been granted an approval from the ECB to include such positions in the non-trading book upon the position being recognised on the books of the institution for the first time."<br><br>Article 104 should be used in the context of the classification of a position (i.e., the initial recognition of the position on the books of an institution), while Article 104a should be used in the context of reclassification (i.e., after the initial recognition of the position on the books of an institution). See comment 26 as an example of where classification and reclassification are being mixed up. | Since there is no provision in the CCR3 text for grandfathering and to avoid any confusion, the industry seeks confirmation that this requirement in Article 104(4) applies only to new positions in the context of their classification (and not to existing positions for which Article 104a conditions for reclassification would apply). | AFME/ISDA |

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| 15 | Section 2, Chapter 3, Paragraph 3 | 33 | Clarification | The ECB states that instruments listed in CRR Article 104(2)(d)-(i) should be designated as a trading book instrument when it is first recognized on the books of an institution.<br><br>However, the ECB then states that for instruments listed in Article 104(3) of the CRR, where there is a potential overlap with Article 104(2), points (d) to (i), of the CRR, Article 104(4) of the CRR does not apply and the relevant positions must be assigned to the non-trading book. For example, this would be the case for an unlisted equity that resulted from market-making activity. The ECB Guide would indicate that, due to the market-making an entity must allocate initially to the trading book, but then redesignate to the banking book due to the instrument being an unlisted equity.<br><br>We do not expect that it is the ECB's intention to force firms to initially recognise such a position in the trading book, and then immediately reclassify it to the non-trading book. Therefore, it would make it far clearer if the ECB were to clarify that the hierarchy is rather:<br><br>1. Any position in an instrument referred to in Article 104(3) of the CRR should be designated as a non-trading book instrument when it is first recognised;<br><br>2. Any position in an instrument referred to in points (d) to (i) in Article 104(2) of the CRR, but not referred to in Article 104(3) of the CRR, should be designated as a trading book instrument when it is first recognised. | The wording is currently inconsistent, which could lead to misinterpretation from users of the ECB Guide. Amending the wording as suggested would reduce this ambiguity. | AFME/ISDA |
| 16 | Section 2, Chapter 3, Paragraph 3(iii) and (v) | 34 | Deletion | Paragraph 3(iii) and (v) both address the demonstration of trading intent, which is an example of the complexity and redundancy of the proposed framework. | The starting point of asking for derogation is the demonstration of no trading intent. | AFME/ISDA |
| 17 | Section 2, Chapter 3, Paragraph 3(ii)(a) and (iii)(a) | 35-36 | Clarification | The guide should comply with CRR3 and clarify that Article 104(2)(d):<br>• Covers transactions where the business or activity model corresponds to a trading purpose, resulting in their classification as FVP&L; and<br>• Excludes items classified as Fair Value through Profit and Loss (FVP&L) when the business or activity model does not correspond to a trading purpose, particularly derivatives that mitigate IRRBB and are included in the IRRBB (or FXRBB) management framework, consistent with EBA Guidelines on IRRBB and FXRBB.<br><br>The ECB should delete sections, (ii) and (iii)(a) on page 35 of the guide related to Article 104(2)(d) that are irrelevant and replace them with clarifications that:<br>• Transactions not recognized as FVP&L are classified in the prudential Banking Book, including derivatives accounted for under hedge accounting;<br>• Transactions recognized as FVP&L are included in the prudential Banking Book when they fall under the IRRBB framework or in FXRBB framework;<br>• Other transactions that align with a trading purpose, including hedging transactions with a trading purpose that are accounted for as FVP&L in the prudential Trading Book.<br>Note that since Article 104(2)(d) targets transactions aligned with a trading purpose, these transactions cannot be classified in the prudential Banking Book and hence are not subject to exemption requests. | The Trading Book Classification Exemptions section is not consistent with the Level 1 text. This misalignment would lead to a dramatic and unjustified broadening of the scope of transactions subject to supervisory pre-approval, extending beyond the commonly understood analysis of Level 1 text. It would also introduce overly prescriptive technical requirements on instruments included in the scope of the exemption request, creating additional administrative burden and supervisory uncertainty. At a time when there is a push for regulatory simplification in Europe, these requirements would lead to unnecessary overcomplexity and misalignment with CRR3 and the European regulatory framework.<br><br>For a more detailed analysis, please refer to the cover note that is accompanying this spreadsheet. | AFME/ISDA |
| 18 | Section 2, Chapter 3, Paragraph 3(ii)(a) and (iii)(a) | 35 | Deletion | The text for (ii)(a) states "if the scope of application covers Article 104(2), point (d), of the CRR and the business objective is the hedging of banking book positions, the internal classification of derivative instruments as hedging instruments throughout their lifetime".<br><br>The text for (iii)(a) states "if the scope of application covers Article 104(2), point (d), of the CRR and the business objective is the hedging of banking book positions, the monitoring should include the hedge effectiveness and hedge relationship between hedged positions and derivative instruments, the identification of the hedging instrument, the hedged position or risk being hedged and how the credit institution will assess whether the hedging relationship meets the hedge effectiveness as specified in the internal policies of the credit institution".<br><br>Paragraph 3(iii)(a) references "hedge effectiveness and hedge relationship". While the term "hedge effectiveness" is recognized under IFRS, it cannot apply here because any derivative designated as an effective hedging instrument under IFRS does not qualify as a derivative under IFRS and is therefore not subject to the presumed trading book allocation in CRR Article 104(2)(d). Demonstrating "hedge effectiveness" should be permissible based on different concepts, such as the CRR credit risk mitigation framework for RWA hedges in the banking book, economic hedging for non-RWA hedges, the IRRBB framework for IRRBB hedges, or the mandate of the ALM function of the bank. Moreover, "throughout the lifetime" and "discontinued" are IFRS accounting terminology, but should not be applied in the guide pertaining to what happens after the initial classification of a position. | Derivatives from the banking book intended for hedging exposures, without trading intent and initiated outside of the trading desk, should naturally be classified under the banking book. Requiring individual or group derogations for these types of products would impose an unnecessary operational burden. | AFME/ISDA |
| 19 | Section 2, Chapter 3, Paragraph 3(viii) | 35 | Clarification | Section 3 paragraph 5(viii) requires banks to define actions, which are envisaged for positions that no longer meet the conditions and may not be known at inception. Even if these actions are known at inception, this requirement implies that the bank would be bound to those predefined actions. If that is the case, it unnecessarily restricts the bank's discretion. | The guide should focus on initial assignment and not cover any actions after the initial assignment. | AFME/ISDA |
| 20 | Section 2, Chapter 3, Paragraph 3(ii)(b) | 35 | | Paragraph 3(ii)(b) stipulates that the hedging derivative instrument must be terminated if the hedged instrument expires, is sold, terminated, or exercised. In addition to discontinuing the hedge, credit- or equity-related derivatives would also fall under the mandatory trading book allocation as per CRR Article 104(2)(b) and could transition to the trading book. Additionally, documentation confirming the discontinuation of the hedging derivative is required. Since this discontinuation occurs after ECB approval to assign the derivative to the banking book, it remains unclear whether additional information is needed to provide to the ECB once the derivative is discontinued. | The guide should focus on initial assignment and not cover any actions after the initial assignment. | AFME/ISDA |
| 21 | Section 2, Chapter 3 | 35 | Clarification | The draft guide effectively describes several examples of what the ECB will consider for specific types of positions under Article 104(2). We note that the Basel Framework RBC25.9 Footnote 3 offers the following additional guidance:<br>"Subject to supervisory review, certain listed equities may be excluded from the market risk framework. Examples of equities that may be excluded include, but are not limited to, equity positions arising from deferred compensation plans, convertible debt securities, loan products with interest paid in the form of "equity kickers", equities taken as a debt previously contracted, bank-owned life insurance products, and legislated programmes. The set of listed equities that the bank wishes to exclude from the market risk framework should be made available to, and discussed with, the national supervisor and should be managed by a desk that is separate from desks for proprietary or short-term buy/sell instruments."<br>We recommend that a similar consideration be incorporated into the ECB guide. | We recommend aligning with Basel to provide non-exhaustive examples of what may qualify for exemption to provide further clarity. For example, listed equity positions arising from deferred compensation plans over prolonged periods are driven in part by regulatory guidance to defer variable remuneration as set out in Article 92(2) and Article 94 of the CRD and should not be subject to trading book treatment. | AFME/ISDA |
| 22 | Section 2, Chapter 3, Paragraph 3 (ii)(a), (ii)(b), and (iii)(a) | 35 | Clarification | Section 2, Chapter 3, Paragraph 3, second sub-paragraph, items (ii)(a), (ii)(b), and (iii)(a) of the guide seem to suggest that derivatives used for hedging banking book items fall under the scope of CRR Article 104(2)(d), meaning they are classified unambiguously as having a trading purpose under the accounting framework applicable to the institution. Consequently, these derivatives can only be assigned to the banking book if the ECB approves a derogation request filed by the bank.<br><br>Under IFRS 9, derivatives are automatically classified as Fair Value through Profit and Loss (FVPL) if a hedge accounting relationship cannot be documented, regardless of whether they pertain to a financial asset (IFRS 9 4.1.4) or to a financial liability (IFRS 9 4.2.1). The IFRS accounting classification of derivatives does not depend on the trading purpose criteria; in IFRS 9, the concept of held for trading (HFT) constitutes a business model rather than a specific accounting category. Therefore, derivatives are not classified unambiguously as having a trading purpose if the accounting framework applicable to the institution is IFRS. For institutions subject to IFRS, our interpretation of CRR3 is that derivatives are not automatically classified in the trading book under CRR Article 104(2)(d).<br><br>As a result, when a bank adheres to IFRS, derivatives used for hedging banking book items do not fall into either the trading book or the banking book. Thus, they should be classified in the banking book since they lack trading intent and do not hedge a position with trading intent. | The ECB should clarify that when a bank follows IFRS, derivatives used for hedging banking book items are to be directly assigned to the banking book without the need for any derogation. Section 2, Chapter 3, Paragraph 3, second sub-paragraph items (ii)(a), (ii)(b) and (iii)(a) of the guide are not applicable to banks that apply IFRS. | AFME/ISDA |
| 23 | Section 2, Chapter 3, Paragraph 4 | 36-38 | Clarification | It is unclear whether these conditions apply specifically to the direct holding of hedge fund shares or to all types of exposures, including derivatives. | A clarification of the scope is needed and whether it applies to the direct holding of hedge fund shares, or whether it extends to other exposures. | AFME/ISDA |
| 24 | Section 2, Chapter 3, Paragraph 4 | 36 | Deletion | The text states "The ECB is of the view that separate requests should be submitted for each hedge fund".<br><br>The conditions for classifying exposures to hedge funds should align with those applied to Collective Investment Undertakings (CIUs) under Article 104(8). Special care should be taken in classifying these products, particularly those developed in the US. The proposed US draft text does not impose any constraints on the classification of hedge funds exposures, which could create an unlevel playing field for EU banks operating in the US market. | This request is not aligned with the time-to-market of the activity and would also be quite burdensome to implement from an operational perspective. | AFME/ISDA |
| 25 | Section 2, Chapter 3, Paragraph 3(vii) | 36 | Deletion | Paragraph 3(vii) is redundant to (x), as the lack of trading intent is the justification for banking book assignment in both cases. | | AFME/ISDA |

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| 26 | Section 2, Chapter 3, Paragraph 3(iv)-(vi) | 36 | Amendment | According to CRR Article 104(4), the ECB is responsible for approving a derogatory classification in the banking book when the institution has effectively demonstrated the absence of trading intent or hedging of a position with trading intent.<br><br>Items (iv), (v) and (vi) from the second sub-paragraph indicate that banks should submit:<br>(iv) an impact assessment on own fund requirements<br>(v) the intended accounting treatment and estimate of the account value<br>(vi) the expected position size and impact on risk metrics<br><br>Apart from the intended account treatment mentioned in item (v), the other items are not relevant to the required demonstration. Furthermore, this may suggest that two requests with similar rationales but different impacts or metrics could be treated differently, contradicting the Level 1 text. Finally, providing such metrics and impact assessments is quite burdensome and, as mentioned previously, offers limited added value in processing these requests. | | AFME/ISDA |
| 27 | Section 2, Chapter 3, Paragraph 4(ii) | 37 | Deletion | The text for (ii) states that "the hedge fund does not have features that might obstruct the tradability of such instruments (e.g. lock-up periods, cases involving redemption allowances where only specific time frames for periodic redemptions are possible – weekly, monthly, quarterly, yearly – or cases with redemption closings during volatile market periods);"<br><br>This appears to limit the possibility of derogation to daily NAV hedge funds, which is overly restrictive. The conditions for classifying exposures to hedge fund should align with those applied to Collective Investment Undertakings (CIUs) under Article 104(8). Special care should be taken in classifying these products, particularly those developed in the US. The proposed US draft text does not impose any constraints on the classification of hedge funds exposures, which could create an unlevel playing field for EU banks operating in the US market. | This appears to limit the possibility of derogation to daily NAV hedge funds, which is overly restrictive. | AFME/ISDA |
| 28 | Section 2, Chapter 3, Paragraph 4(iii) | 37 | Deletion | The text for (iii) states that "the hedge fund is listed".<br><br>This condition is overly restrictive. The conditions for classifying exposures to hedge fund should align with those applied to Collective Investment Undertakings (CIUs) under Article 104(8). Special care should be taken in classifying these products, particularly those developed in the US. The proposed US draft text does not impose any constraints on the classification of hedge funds exposures, which could create an unlevel playing field for EU banks operating in the US market. | This condition is overly restrictive. | AFME/ISDA |
| 29 | Section 2, Chapter 3, Paragraph 4(v) | 37 | Clarification | The text for (v) states "how the institution ensures that relevant positions under the discretion provided for in Article 104(4) of the CRR are managed by units responsible for non-trading book management which are separate from units responsible for trading book management".<br><br>It appears to be a typographical error. The text should clarify how the institution ensures that the relevant positions, as outlined in CRR Article 104(5) of the CRR, are managed by units responsible for trading book management, which operate independently from those responsible for non-trading books. | This point needs further clarification and there appears to be a typographical error. | AFME/ISDA |
| 30 | Section 2, Chapter 3 (N/A paragraph has been deleted) | 41 | Clarification | We welcome the removal from the Guide of the reference to Art 162 of CRR regarding the maturity of exposures falling under the F-IRB approach. We believe the CRR3's updated text is sufficiently clear regarding this point and that this provision does not require further supervisory clarification. | | AFME/ISDA |
| 31 | Section 2, Chapter 3, Paragraph 6 | 42 | Amendment | To assess whether some equity can be risk weighted at 100%, the ECB has expanded the conditions in CRR by requiring a subsidy. This is not stipulated in the level 1 text. | The reference to subsidies should be deleted. | AFME/ISDA |
| 32 | Section 2, Chapter 3, Paragraph 8 | 42 | Clarification | We note that the ECB intends to apply the recommendation issued by the EBA in its 2020 report on SRT without indicating it as a reference in its guide. As regard to the CRT test that the ECB propose to introduce in its guide, we would like to underline that ECB doesn't seem to distinguish between the requirements of Article 244/245.2 and those of Article 244/245.3: Indeed Article 244/245.3 indicates that, in case a bank doesn't meet the quantitative SRT tests of Art. 244/245.2 a bank can recognise the SRT if it demonstrates to the competent authority that the risk transferred is proportionate to the RWA relief provided by the securitisation - the demonstration is to be made by the bank. Instead, in case the transaction meets Art.244/245.2 it's for the ECB to demonstrate that the risk transfer is not commensurate to the RWA relief. The proposal made in the ECB guide (that reflects indeed the current ECB practice) is that banks should demonstrate that there is commensurateness of risk transfer in all cases, and in particular even if the mechanical tests of Art.244/245.2 are met. This therefore goes beyond CRR requirements.<br><br>In general, we would like to note that the EBA report, from which the ECB has taken different recommendations, is not a guideline and that these recommendations have not been tested by the EBA on real transactions and banks observe that some of these recommendations need to be adapted. In particular the hypothesis to be used for the CRT test needs to be reviewed, of which the basis for the calibration of the EL and UL, but also that banks should have the ability to define alternative scenarios when they are more fitted to the nature of the underlying securitised asset.<br><br>Furthermore, fundamentally the CRT test does not appear to effectively evaluate the commensurateness quality of a risk transfer, aiming merely to meet an adequate minimum. Instead, it rather ensures that the risk transfer recognized by regulation is assessed more stringently than through a more "economic" risk transfer measurement methods. The actual risk transfer might be minimal, yet the test could still yield a positive result in certain scenarios (and a high level of risk transferred could also lead to a negative result of the test).<br><br>In regard to specific points subjects to the comprehensive review by the ECB:<br>"iv) whether the cost of credit protection for synthetic securitisation is so too high that it would undermine the transfer of credit risk;" - We observe that the ECB is using the recommendation of EBA 2020 report. However as explained above, the recommendations of this report have not been extensively tested and typically the proposals made by the EBA show severe drawbacks, even for largely placed transactions executed in an historically low spread market.<br><br>"(vii) whether, where the originator uses the Securitisation External Ratings - Based Approach (SEC-ERBA) as provided for in Article 254 of the CRR, to calculate capital requirements on the retained securitisation positions, the chosen external credit assessment institution (ECAI) has appropriate experience and expertise in the asset class being rated."<br><br>We believe this statement goes beyond the ECB's powers. First, we would like to note that, if CRR Article 254.4 grants the right to the Competent authority to prohibit, on a case by case basis, the usage of the SEC-SA this right doesn't exist for the SEC-ERBA. Secondly, the appropriate experience and expertise of an ECAI in the rating of an asset class is made by the EBA under the mandate granted under CRR article 270e. We therefore ask the ECB to remove this statement. | Clarification to align with what is required by the CRR. | AFME/ISDA |
| | | | | Overall, we regret that the supervisory framework of SRT transactions is becoming increasingly mechanistic and rigid, based on assessment approaches that have not been sufficiently tested and that prove unfit for some types of transactions. The creation of an ECB central "horizontal team", while aiming for more coordination across JSTs, is actually diminishing the dialogue between banks and supervisors, since the decision is ultimately made by the central team which has no interaction with banks and often does not provide timely feedback. This increasing disconnect between market timing and supervisory assessment is concerning at a time where the EU intends to scale up the SRT market. | | |
| 33 | Section 2, Chapter 3, Paragraph 11 | 45 | Deletion | Regarding chapter 3 paragraph 11: Both conditions included for Article 314(3), point (c) introduce the operational risk loss element as a requisite to approve the separate ILDC calculation. CRR3 disregards operational risk loss data for the calculation of own funds requirements for operational risk in the EU as it is put forward in the preamble of the regulation: "To ensure a level playing field within the Union and to simplify the calculation of own funds requirements for operational risk, that discretion should be exercised in a harmonised manner for the minimum own funds requirements by disregarding historical operational loss data for all institutions."<br>Additionally, the condition on point (c) i) replicates in its entirety the ILM proposed in the Basel framework, by considering historical operational loss data and multiplying it by 15. Once again, the ILM was purposefully disregarded by the legislator when deliberating the new regulation. Therefore, by including operational losses as a qualifier for operational risk capital calculation, the ECB is going against the intention of the EU legislator and going beyond the supervisory discretion allowed in the CRR.<br>Conditions included by the EU legislator in the CRR 3 for approval of the separate ILDC are almost identical than the conditions required in CRR 2 for the Alternative Standard Approach (ASA). If the additional conditions included in the ECB Guide were included in CRR, those geographies with an ASA approval wouldn't qualify for the same treatment under CRR3.<br>In our opinion, the way in which the ECB should assess the appropriateness for a group to calculate a separate ILDC for a specific subsidiary to fulfil condition for Article 314.3 (c), should be to confirm whether the NIM profile of the solicitant subsidiary is of a different nature than the profile of its banking group and therefore it distorts the Group's ILDC calculation, which leads to an overestimation of its operational risk consolidated capital requirements. This approach is supported by the consultative document on operational risk issued by the Basel Committee in October 2014, where it observed that bank business models and jurisdictions emphasize varying NIM profiles and, as a result of this, in some cases the Business Indicator may not be a proper proxy for operational risk exposure. To address this issue, it introduced the ASA which applies a "cap" to the NIM in Basel II operational risk framework. Therefore, by analogy with the problem of calculating operational risk at a consolidated level in the case of banking groups with different NIM profiles under Basel II and the introduction of the separated ILDC to solve this problem in CRR3, competent authorities should assess whether the NIM profile of the subsidiary which applies for the separated ILDC is different from the rest of the Group's profile and not the group's loss component. By doing so, the assessment of whether the use of this derogation provides an appropriate basis for calculating the EU parent institution's own funds requirement for operational risk would be well founded. In any case, if the supervisor imposes any additional conditions to ensure that the capital requirements resulting from the application of this treatment are adequate to cover the operational losses of the subsidiary, the appropriate approach would be to use the credit institution's ratio of operational losses to operational risk capital requirements. Comparing this ratio calculated for the subsidiary with the one resulting at the Group level makes little sense and could lead to undesirable situations where this treatment could only be applied in Groups with a very high level of operational losses. | The conditions detailed in the guide do not align with the regulator's intent regarding Article 314.3. The separate ILDC were included in CRR to avoid distortions in the Group's ILDC calculation when the NIM profile of the solicitant subsidiary is of a different nature than the profile of its banking group and therefore leads to an overestimation of its operational risk consolidated capital requirements. The separate ILDC was included in the CRR to prevent distortions in the Group's ILDC calculation when the NIM profile of the requesting subsidiary differs significantly from that of its banking group. This discrepancy could otherwise result in an overestimation of the consolidated capital requirements for operational risk. | AFME/ISDA |

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| 34 | Section 2, Chapter 3, Paragraph 11 | 45 | Amendment | 314(3)(b)<br>The current proposal defines "high PDs" by comparing the credit risk exposures of the retail/commercial banking subsidiary to the PDs of "similar loans" of the parent credit institution without defining the notion of "similar loans".<br>Therefore, we propose the below amendments:<br>- The PDs of at least 50% of the subsidiary's combined retail and commercial credit risk exposures, measured by taking Stage 1 IFRS 9 PDs over the last five years, are at least twice as high as the Stage 1 IFRS 9 PDs of similar loans within the same exposure class of the parent credit institution measured on an individual basis over the same period.<br><br>314(3)(c)<br>As the exemption will modify the business indicator and will not impact the losses, we propose the below amendments to the wording:<br>- (i) the credit institution's loss component calculated on a consolidated basis before the application of the derogation or due to the derogation does not exceed its business indicator component calculated on a consolidated basis before the application of the derogation or due to the derogation (for this purpose, its loss component should be calculated by multiplying its average annual operational risk losses over the last five years by 15); | Using the well-defined "exposure class" concept poses less interpretation risk than the notion of "similar loan". | AFME/ISDA |
| 35 | Section 2, Chapter 3, Paragraph 12(3) | 46 | Clarification | Paragraph 12(3) requires maintaining a comprehensive list of instruments. Additionally, Paragraph 13(8) mandates a similar inventory but with alternative definitions. The ECB should clarify that the inventory in Paragraph 12(3) should not include any information already provided in another section of the guide, such as Paragraph 13(8), to avoid repetition and redundancy. | The preference is that banks not be required to maintain the inventories mentioned in Paragraph 12(3) and 13(8). If that is not acceptable, then it should not be required that the two inventories be linked.<br><br>We would point out that Paragraph 12(3)(ii) mandates the inclusion of "pricing models/methodologies used to calculate sensitivities" in the inventory, which appears redundant with Paragraph 13(8). | AFME/ISDA |
| 36 | Section 2, Chapter 3, Paragraph 12(10) | 48 | Amendment | The industry recommends the following amendments to Paragraph 12(10):<br>"For the purpose of the assessment of compliance with the specifications in Article 325c ... it is expected that the credit institution submits the following information to the ECB:<br>(i) ...<br>(ii) an audit report, signed by the head of the internal audit function of the institution and approved by the management body, describing the main outcomes of the SAQ, a summary of the findings identified, including their severity, and a corresponding remediation plan~~, including, where applicable, the follow-up on the remedial actions derived from previous independent reviews. U~~pon request from the competent authority, the institution shall provide the follow-up on the remedial actions derived from previous independent reviews." | Mandating that each annual internal review includes documentation of follow-ups of previous findings imposes an unnecessary and redundant operational burden. Institutions generally have robust internal processes to monitor the remediation of all market risk-related findings (e.g., such as those from internal audit, model validation, and findings from competent authorities), which are regularly reported to senior management. Furthermore, the status of outstanding findings is a common topic of discussion in the dialogues between institutions and the competent authority.<br><br>Instead, the industry recommends that institutions provide this information upon request of the competent authority. | AFME/ISDA |
| 37 | Section 2, Chapter 3, Paragraph 13 | 49-51 | Amendment | This is a general comment on paragraph 13: there seems to be a misconception that alternative sensitivities are entirely new, isolated measures requiring separate control and monitoring tools, along with detailed documentation. However, sensitivities are derived from pricing models, which are already expected to comply with existing documentation and control requirements. | The industry recommends that ECB review the requirements related to sensitivities in the context of pricing models and allow banks to leverage existing controls and documentation. There should not be a requirement to create new inventories or processes that isolate sensitivities from the broader framework of pricing model management. | AFME/ISDA |
| 38 | Section 2, Chapter 3, Paragraph 13(1) | 49 | Amendment | The ECB's criteria for the qualitative assessment of alternative sensitivities currently focus on aligning more closely with industry practices and ensuring appropriate risk measurement. However, the guidelines lack clarity on whether an alternative definition, such as using hazard rates instead of credit spreads, can be considered non-material. Hazard rates provide a more rigorous approach to defining credit spreads, help avoid pricing failures, and do not result in significant quantitative differences. The ECB should consider expanding the scope to include the possibility of such alternative definitions being evaluated alongside regulatory-defined sensitivities.<br><br>While the ECB's guidance addresses variations in shock size and direction, it does not differentiate between multiplicative and additive shocks in sensitivity calculations. For example, a sensitivity like vega can be calculated as an additive shock under an alternative definition, whereas it is treated as a multiplicative shock according to the regulatory definition. Furthermore, the CRR3 vega definition does not align with industry practices or other jurisdictions. In the Basel framework, vega is defined separately, with sensitivity being the product of vega and volatility. In contrast, CRR3 incorporates volatility directly into the sensitivity formula, leaving no room for a separate vega definition. This discrepancy should be considered non-material. The ECB should explicitly address differences of this type to clarify any uncertainties.<br><br>The guide text should be amended as follows:<br>"... For example, the bump sizes could be set at different levels, and instead of one-sided bumps, two-sided bumps could be applied, or analytical derivatives could be used, or hazard rates instead of credit spreads could be used, or multiplicative / additive shocks could be used if this results in a more appropriate risk measurement for the credit institution's trading portfolio." | The qualitative criterion in Paragraph 13(1) should expand the scope to classify more rigorously defined alternative sensitivity definitions such as hazard rate as non-material. Hazard rates serve as inputs for calculating credit spreads. Therefore, adjusting hazard rates effectively translates to adjusting credit spread, albeit with different tweak sizes.<br><br>The qualitative criterion in Paragraph 13(1) should expand the scope to include variations such as multiplicative or additive shocks as non-material. Absolute vega sensitivities, when multiplied by the implied volatility, align with the definition already accepted under CRR2 and conform to all other FRTB regulations, including those established by Basel, the US, and the UK. | AFME/ISDA |
| 39 | Section 2, Chapter 3, Paragraph 13(3) | 50 | Clarification | The ECB should clarify that if "already approved applications remain valid", **any conditions or restrictions that were set at the time of the original approval will no longer be applicable** with the publication of this revised EGOD. In particular, qualitative justifications should suffice for such usage.<br><br>The industry seeks confirmation that the guide supersedes all previous obligations, which varied across banks. Firms should have the option to independently decide to adopt qualitative criteria and discontinue their quantitative processes, provided they have assessed and confirmed that their inventory of alternative definitions and justifications is adequately prepared. | In a number of cases, when the ECB approved the use of alternative sensitivities, it did so under certain conditions that varied between banks (for example, by imposing certain obligations on the monitoring process). Therefore, it is necessary to explicitly mention that these conditions are no longer in effect. | AFME/ISDA |
| 40 | Section 2, Chapter 3, Paragraph 13(5) | 50 | Amendment | In Paragraph 13(5)(iii)(c), documentation requires a mention of whether the alternative sensitivity definition is "owned" by an independent risk unit. It has not been clarified what is meant by "owned". As per Article 325t(a) and (b), reference is made to independent risk control unit in terms of usage for reporting profits and losses to senior management. Having alternative sensitivity ownership managed by an independent risk unit has not been included in CRR Article 325(t) and would introduce additional requirements beyond CRR Article 325(t)(1).<br><br>Paragraph 13(5)(iii)(c) should be amended to:<br>(c) ~~owned~~ used by an independent risk unit | | AFME/ISDA |
| 41 | Section 2, Chapter 3, Paragraph 13(6) | 50 | Deletion | The meaning of validation that covers "the definition of alternative sensitivities" is ambiguous. According to the guide, alternative sensitivities are deemed valid if they (i) are not materially different from the regulatory ones and (ii) are more appropriate from a qualitative point of view. The guide should specify whether the validation function is expected to merely confirm (i) and (ii), and if so, that there is no need to reassess this validation periodically. We suggest to add text that clarifies that the validation of "implementation" may be part of the normal process of pricing model validation that banks should have in place and are, therefore, not a separate validation workflow. | Paragraph 13(6) should be deleted on the grounds that it is already covered by the "appropriateness" criteria. | AFME/ISDA |
| 42 | Section 2, Chapter 3, Paragraph 13(7) | 51 | Amendment | Point 13(7) seems to contradict the notion of a qualitative assessment referred to in sections 13(1) and 13(2). This section should clarify that banks are not required to create a distinct monitoring process for alternative sensitivities if they already have processes in place to monitor the performance and adequacy of their pricing models generally. | The industry recommends that ECB should amend this section to provide clarification and allow for broader options to achieve the intended objective.<br><br>The current reference to "regulatory non-compliance" is too broad. The suggested reference is CRR Article 325(t)(5) and (6). | AFME/ISDA |
| 43 | Section 2, Chapter 3, Paragraph 13(8) | 51 | Clarification | According to paragraph 13(8), the ECB has outlined a list of documents required for assessment under Article 325t(5) and (6). However, the specific procedure for this assessment has not been detailed. | The ECB should clarify that, when referring to an "assessment", it refers to the assessment of the initial application, as it is understood by the industry. | AFME/ISDA |
| 44 | Section 2, Chapter 3, Paragraph 13(8)(i)(b) | 51 | Deletion | The text says "(8)(i)(b)<br>the current and last three relevant risk management and P&L reports (daily, monthly, quarterly);"<br><br>We see limited added value for providing P&L reports for the alternative sensitivity use case and therefore, we recommend deleting the relevant guide. | | AFME/ISDA |

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| 45 | Section 2, Chapter 3, Paragraph 13(5), (8)(ii) | 51 | Amendment | To prevent excessive documentation efforts, it should be acknowledged that banks may already have sufficient documentation regarding their pricing models (from which alternative sensitivities are derived) that can be provided to the ECB. There is no need to set up and maintain a complex inventory to demonstrate the appropriateness of the sensitivities used.<br><br>Similarly, internal audits should be decoupled from the ongoing monitoring activity since these could operate at different frequencies. Furthermore, we propose removing the requirements outlined in (8)(ii), as they would fall under the supervision of the regular internal audit as described in Chapter 3, Section 12 on Internal Review. | The requirement for a specific inventory of sensitivities should be replaced by a requirement of "auditability" of the calculation and appropriateness of these sensitivities. | AFME/ISDA |
| 46 | Section 2, Chapter 3, Paragraph 16 | 52 | Amendment | The ECB lists two conditions for approving the fallback on internal ratings: "(i) an internal ratings-based (IRB) model approved by the supervisor for the same counterparties is in place; (ii) the JST does not have concerns related to that approved IRB model, substantiated by high severity findings that have resulted in the imposition of limitations or conditions that are still unresolved."<br><br>On the first condition, we urge the ECB to maintain flexibility in approving alternative methodologies for counterparties that are not covered by an IRB model or for firms that do not have an IRB model. We propose that the ECB allow firms to develop their own methodologies for determining the IG vs Non-IG determination, subject to ECB's satisfaction. For instance, due diligence of external ratings is required per CRD Article 79(b) / CRR Article 113(1) which mandates non-IRB firms to develop internal rating methodologies. This methodology relies on the internal assessment of counterparty creditworthiness which can be leveraged and fine-tuned to determine IG vs HY criteria for CVA. Allowing banks to use their own methodologies would also be consistent with the EBA Stress Test methodology which requires banks to break down CVA positions into investment and non-investment grade for the types of counterparties using their normal approach to distinguishing investment grade according to external ratings or, for counterparties with no external rating, according to an internal methodology if applicable. Banks should be encouraged to use the same internal methodology to determine IG vs Non-IG criteria (EBA's methodological notes for 2025 EU-Wide Stress Test - paragraph 294).<br><br>Where an IRB model approved for the same counterparties exists, the second condition may be overly conservative. The use case for probability of default (PD) models in the context of CVA is much simpler than the original use case for IRB risk weights, as PD models will only be used to determine whether a counterparty falls into the broader investment grade (IG) or non-investment grade (Non-IG) categories. There are cases where a model may encounter high severity findings accompanied by open limitations and conditions in the context of IRB risk weights, yet still effectively distinguishes between IG and non-IG counterparties. For example, if the ECB imposes a floor or add-on for certain rating grades. While this may render the model overly lenient for IRB purposes, if these grades still classify as IG, banks should be able to utilize them for calculating CVA RWAs.<br><br>Furthermore, the CVA use case closely resembles the transitional arrangement outlined in the output floor (CRR Article 465.3), which permits EU banks to assign a lower risk weight to unrated corporates classified as IG when assigned a PD less than or equal to 0.05%. This approach does not require approval from the ECB and is not bound by the same constraints. | We suggest the following amendment to the ECB guide text:<br><br>"The ECB is of the view that the use of internal ratings for the determination of credit quality steps should be approved only under the following conditions: (i) an internal ratings-based (IRB) model approved by the supervisor for the same counterparties is in place or a model for using internal ratings for CVA is applied for by the institution and approved by the supervisor; (ii) the JST does not have concerns related to that approved IRB model and its performance to differentiate between counterparties deemed to be investment grade (i.e. mapped to a credit quality step 1 to 3 ) and those deemed to be non-investment grade (i.e. mapped to a credit quality step 4 to 6)~~, substantiated by high severity findings that have resulted in the imposition of limitations or conditions that are still unresolved.~~" | AFME/ISDA |
| 47 | Section 2, Chapter 3, Paragraph 16 | 52 | Clarification | New paragraph should be inserted to handle applications submitted prior to the publication of the final version of the guide. | It should be clarified that already approved applications will remain valid. | AFME/ISDA |

# Template for comments

## Public consultation on revisions to the ECB's policies concerning the exercise of Options and Discretions (O&Ds) in Union law

### ECB Recommendation on Options and Discretions under Union law

**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 article/chapter/paragraph, where appropriate;**
- **you indicate whether your comment is a proposed amendment, clarification or deletion.**

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| **Deadline:** | midnight CET on 25 January |

| ID | Section | Type of comment | Detailed comment | Concise statement as to why your comment should be taken on board | Name of commenter |
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# Template for comments

## Public consultation on revisions to the ECB's policies concerning the exercise of Options and Discretions (O&Ds) in Union law

### ECB Guideline on Options and Discretions under Union law

**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 article/chapter/paragraph, where appropriate;**
- **you indicate whether your comment is a proposed amendment, clarification or deletion.**

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| **Deadline:** | midnight CET on 25 January |

| ID | Section | Type of comment | Detailed comment | Concise statement as to why your comment should be taken on board | Name of commenter |
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