EUROPEAN CENTRAL BANK

BANKING SUPERVISION

Template for comments

Public consultation on the revised ECB guide to internal models

Institution/Company

BBVA Group

Contact person

Mr/Mrs

[redacted]

First name

[redacted]

Surname

[redacted]

Email address

[redacted]

Telephone number

[redacted]

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General comments

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

Deadline: 15 September 2023

ID	Chapter	Section	Paragraph	Page	Type of comment	Detailed comment	Concise statement as to why your comment should be incorporated
1	General topics	1.8 General principles on climate-related and environmental risks	25	12	Clarification	This section should be more general, targeting the inclusion of any relevant driver not observed in the past, this may include the effects of climate change, new environmental factors, the social trends, high inflation and interest rates and others deemed relevant. Additional quantitative guidance on how define the "relevant" and "material" concepts would be helpful. Having said this, even if considered of "relevant and material" nature, their final inclusion as risk drivers should be conditioned to their statistical contribution to the performance of the model, as any other potential risk driver. The fact of not having historical information for these variables is a challenge in itself to prove their statistical relevance. Forcing their inclusion without an statistical-based ground can constitute a potential source for credit risk management deterioration (e.g.risk differentiation and quantification)	Consistency with the modelling approach for the rest of potential risk drivers
2	Credit risk	2.2 IT systems: infrastructure and implementation testing	7.d	61	Amendment	The requirement of "the institution is able to submit the respective COREP reporting (Article 144(1)(g) of the CRR" by the initial model approval or roll-out, seems to collide with the provision in paragraph 26 of General Topics chapter /1.9 section (page 12) of the EGIM where it is stated that :"The ECB generally expects this time frame to be no longer than three months from the date of the notification". Also, there is a risk that the initial model approval or roll-out request could eventually not be approved by ECB. In such case, undoing the COREP processes to the previous set up would be unduly burdensome for the institution. Alternative proposal: to reword the requirement as "is able to evidence the readiness to implement the respective COREP reporting in a time frame no longer than three months from the date of notification"	Consistency with other provision in the EGIM
3	Credit risk	2.2 IT systems: infrastructure and implementation testing	7.e	61	Clarification	Further clarity on the definition of the "internal risk measurement and management purposes" term would be appreciated Our understanding of the requirement of "is able to use the model for internal risk measurement and management purposes" when referred to estimation of risk parameters is that it would be met if there are previous versions in place for internal risk management. In other words, the requirement should not mandatorily demand having new versions of Economic Capital and IFRS 9 risk parameters calibrated by the time of the application submission. The grounds for such understanding is that Economic Capital and IFRS 9 models are not covered by the IRB regulation	Consistency with the scope of IRB regulation
4	Credit risk	4.3 Days past due criterion	69	81	Amendment	The requirement to convert past due amounts into EUR on a daily basis, could potentially lead to undesired distorsion in the counting of days past due, especially in non SSM geographies. This could eventually cause a deterioration of the ability to effectively anticipate risk management mitigating actions. It is proposed to introduce the possibility to apply a less frequent exchange rate conversion provided it can be grounded on convincing supporting analyses.	Prudent Risk Management

5	Credit risk	4.7 Adjustments to risk estimates in the case of changes to the definition of default	92	88	Clarification	The requirement to retrospectively assess the impact of the change in the definition of default (i.e. 2 years backwards) should be regarded on the best reasonable effort basis (i.e use of proxies if need be) Especially in the cases where the change is triggered by the remedial efforts stemming from a supervisory finding/obligation, the retrospective assessment should not prevail over the timeliness of such remediation, nor constitute a source or additional penalisation if proxies are used.	Consistency with the supervisory request for the timely remediation of obligations Commensuration of prudential requirements
6	Credit risk	5.2 PD risk quantification	130 (c)	105	Clarification	The paragraph states that cases where it is not possible to backwards recalculate the assignment of exposures in the likely range of variability period, it should be duly justified and documented. In this context, a best reasonable effort basis (e.g. use of proxies if need be) should be deemed sufficient. Especially in the cases where the change is triggered by the remedial efforts stemming from a supervisory finding/obligation, the retrospective assessment should not prevail over the timeliness of such remediation	Consistency with the supervisory request for the timely remediation of obligations
7	Credit risk	8 Model-related MoC	208	140	Clarification	The requirement to calculate MoC C at grade at both calibration and segment levels leads to excessive conservatism on capital requirements beyond the actual uncertainty. More guidance on the flexibility in the interpretation of the requirement would be appreciated (e.g. to apply the distribution of the MoC at grade level, but not necessarily its calculation)	Commensuration of prudential requirements
8	Market risk	6 Methodology for IRC models focusing on default risk	158	197	Deletion	In article 158, it is stated that institutions should analyse any observed differences between these estimates and estimates that are derived in combination with current market prices where the relevant corrections were performed to obtain real-world PDs. This is an additional burden that is not explicit in the regulation. The obtention of real world PDs from CDS spread quotes will rely inevitably on strong assumptions. Moreover CDS market quotes have relevant liquidity and market risk components which contaminate real world PDs. Furthermore, long run PDs should be used as input in order to not double count the effect of the economic cycle, ad obtaining this from volatile CDS quotes is very difficult. We are honestly not sure what the reason for this requirement is since the ECB is in other contexts looking to homogenize PD estimations across IRC, IRB, accounting and so forth, and the use of implied data is not used for PD estimation in general. It also goes against previous requirements since the EBA guidelines on IRC (paragraph B.12.3) imply the opposite and only allow banks to use implied data if they can show it compares well against the historical record. Perhaps the ECB has misunderstood the requirement from the CRR that the data on which PDs based should be up to date since this only means that historical series underlying PD estimation should be up to date.	Unrealistic and burdensome expectation with no added value to model
9	Market risk	6.5 Ratings, probabilities of default and recovery rate assumptions	160	198	Clarification	It is typically the case that extrapolation of sovereign PDs to high investment grades lead to PDs of less than 1 basis point for several rating grades. We would therefore request clarification that the requirement of differentiation of risk applies to the model before the artificial application of the 1 basis point floor. Otherwise, artificially increasing the PDs for high rated sovereigns will lead to a slower rate of PD increase with rating downgrades for investment grade sovereigns with the possibility of a PD ratio when moving to Non-investment grade that is then considered an "outlier". We therefore also request that the determination of what PD ratio would be considered an "outlier" be based on the model before applying any PD floor.	To avoid any misinterpretations regarding the supervisory expectation.
10	Counterparty credit risk	3.2 Principles for ECB Banking Supervision	25	226	Clarification	We would ask that it be clarified that IM or other types of over-collateralization should not be included in the determinant for MPoR increases. The MPoR is linked to VM interchange and it does not make sense that additional collateral should penalize the MPoR and possibly lead to a higher capital charge. Note that due to IM thresholds (typically 50 million per counterparty) the actual amount of interchanged IM may be small as compared to the overall exposure and an increase in MPoR may lead to higher exposure amount due to the addition of IM.	To avoid disincentivizing sound risk management.
11	Counterparty credit risk	3.2 Principles for ECB Banking Supervision	25	226	Amendment	The threshold for when to consider a netting set as illiquid based on "one or more trades" seems overly restrictive and some type of materiality criteria would be needed. We would like the paragraph to substitute "one or more trades" for "material trades". Materiality could be defined in terms of, for example, NPV sensitivities, trade-level EAD, or some other metric.	To avoid disincentivizing sound risk management.
12	Counterparty credit risk	13 Risks not in effective expected positive exposure	92-125	255-269	Amendment	The new RNIEPE framework will be extremely burdensome, and apart from the spike AddOn, is not really needed since model deficiencies are already captured in increases in the alpha parameter, and they are already captured through existing backtesting frameworks, periodic model validation etc. In CCR it is very complicated and costly to estimate RNIEPE. Much more so than in other risk types. For these reasons we suggest that the part of the RNIEEPE framework not related to cash flow spikes be removed.	To avoid a complicated, overy conservative and overly burdensome new framework

13	Counterparty credit risk	13 Risks not in effective expected positive exposure	109	265	Amendment	The definition of delta tk in paragraph 109 (b)(iii) does not seem correct. The paragraph states that it "denote the time period inside the MPOR during which the cash flow payments described in point (ii) above are possible". But this is different than the meaning of delta t_k in Article 284(6) of the CRR. If the definition used in paragraph 109 is used the resulting ERE AddOn will depend on the number of timesteps. It makes more sense if delta t_k adopts the definition of Article 284(6), since the "time period inside the MPOR during which the cash flow payments are possible" is reflected in the exposure increase itself, and therefore captured in the ESE_t_k terms.	Clarification on definition of time differentials in spike formula