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FBF RESPONSE TO THE EBA CONSULTATION PAPER ON GUIDELINES ON CONNECTED CLIENTS (EBA/CP/2016/09)

The French Banking Federation (FBF) represents the interests of the banking industry in France. Its membership is composed of all credit institutions authorized as banks and doing business in France, i.e. more than 370 commercial, cooperative and mutual banks. FBF member banks have more than 37,500 permanent branches in France. They employ 370,000 people in France and around the world, and service 48 million customers.

The FBF welcomes the opportunity to share its comments on the EBA Consultation on connected clients. Please find our main comments below and our detailed feedback to the different questions raised in the consultative paper.

I- General comments

We welcome the efforts made by the EBA to help financial institutions in getting a better understanding of the definition of "connected clients", and the opportunity to answer this consultation. The challenge faced by the industry is not new, and we handle it with the seriousness it deserves.

However, we consider that the top priority is to address the main objectives of the regulation, and not to get more complex definitions which could in certain cases become non applicable. Actually, some provisions of the guidelines are relative to the clustering rules for exposures to central governments, while the sovereign risk framework is still under deep discussions. In addition the guidelines refer to the Basel Committee's Step-in proposed framework to help identifying economic dependency, while like sovereign risk it is still being discussed and not yet finalised.

Similarly, we are surprised that discussions on the rules of default contagion are not linked to this consultation. Furthermore, we are very much concerned that those guidelines will eventually lead to a higher level of complexity in the Large Exposures Reports, in particular for the "economic dependency" topic (although economic dependency is used for defining financial interconnectedness between clients, it is presently one element of the assessment process, and not based on systematic criteria). A broader application of this criteria would involve a significant operational effort by banks, and without any obvious upward on the quality of the assessment.

Subsequently, we ask the EBA to perform a cost analysis because the proposed broad criteria may lead to costly IT changes / evolution. What's more, these criteria will have to be periodically reassessed, which will lead to redhibitory costs given the enlarged definition of economic dependency.

Also, we would like to point out that applying systematic large triggers may lead institutions to connect some counterparties at such a point that the large exposure limits may be systematically reached.

Accordingly the FBF sees no added-value by issuing these revised guidelines, rather we expect the framework to be more complex. Besides we are not in favour of anticipating any current discussion at the international level.

Should the guidelines be revised and published anyway, the FBF asked the EBA to envisage sufficient time for allowing banks to implement any revised framework, at least 18 months after publication.

II- Answer to questions related to the consultation

Question 01: Are you aware of any situations where the existence of a control relationship among clients does not lead to a 'single risk'?

Yes. It is typically the case in jurisdictions where banking structural reforms were adopted. In France, the law for regulation and segregation of banking activities provides that trading entities must be segregated and subject to individual capital and liquidity requirements, while the parent company has to apply the Large Exposure regime to its trading subsidiary. Albeit there is still a control relationship between these entities, there is no economic risk anymore and no existence of a "single risk".

Moreover this might be the case in few situations, in particular for major international Groups acting among several business lines or for specialised lending involving non-recourse debts; even if a control relationship exists, a specific analysis can demonstrate that no single risk exists.

For FBF members, it is important that the internal analysis according to experts can still be considered in the revised guidelines, and that internal risk management practices do not have to be reconsidered.

Question 02: What is the likely impact of the clarification of having an exceptional case when the existence of a control relationship does not lead to a 'single risk'? Please provide an estimation of the associated quantitative costs.

FBF members see no significant impact expected as their internal procedures already specify the need of specific analysis and documentation of the conclusion in such cases.

Question 03: Do you see a need for further clarification of the accounting provisions which are relevant for large exposures purposes? If yes, please point out the exact indicator of control according to the Directive 2013/34/EU or Regulation (EC) No 1606/2002 which should be clarified with respect to the large exposures regime.

No.

Question 04: Are there any other indicators of control in the case of a similar relationship which are useful to add to this list of indicators?

No.

Question 05: What would be the cost of the assessment of the existence of control relationships in the case of subsidiaries exempted from accounting consolidation? Please provide an estimation of quantitative costs.

In your experience, how significant are these cases?

We do not estimate any significant additional costs as our internal procedures to identify individual customers for clustering purposes already require such assessment and documentation (in particular for significant informal groups).

Question 06: Is the guidance provided in section 5. 'Alternative approach for exposures to central governments' clear? If not, please provide concrete suggestions.

Yes. However we are very much concerned by the potential impact that such an alternative approach would have on the bank's sovereign exposures amounts should this be applied. The "assimilated" Sovereign exposure definition is neither defined at the EU level nor at the international level. The FBF is not in favour of such an approach and ask the EBA to wait for new insights at the international level as regards sovereign risk.

Question 07: What is the likely impact of considering that clients are connected as soon as the failure of a client would lead to 'repayment difficulties' of another client? Please provide an estimation of any associated quantitative costs.

Banks in general will have to face a major problem of feasibility and we fear that, as a result, the clustering will not be homogenously implemented among banks. Moreover, banks will face the risk of misguided assessments over some groups, leading to non-desirable impacts over the delegation levels and the limit consumptions. Therefore, in order to ensure the feasibility, coherence and comparability among European financial institutions, we suggest that either BCE/EBA or NCAs provide the list of such customer connections.

In addition, we are using this opportunity to draw attention to the need of expending the use of the global Legal Entity Identifier (LEI) to all financial markets (and not limiting its application to specific market segments). We consider such improvement as a major prerequisite for ensuring the consistency of the Large Exposures framework implementation within Europe. In this perspective, we very much welcome the opinion drawn by the ECB on the 12 September 2016 on the proposal for a Regulation amending Regulation (EU) No 345/2013 and Regulation (EU) No 346/2013, standing that "ECB strongly supports the use of internationally agreed standards, such as the International Securities Identification Number (ISIN) and the global Legal Entity Identifier (LEI), as unique identifiers to meet reporting requirements on the securities markets. (…) The ECB is accordingly of the view that, where appropriate and to the extent possible, other legislative changes underpinning the CMU should also establish the mandatory reporting of unique identifiers".

Question 08: Are the situations described in the list in paragraph 23 as constituting economic dependency clear? If not, provide concrete suggestions. In particular, do you have any comments regarding the introduction of the threshold of 'at least 50%' in points c), d), f) and g)?

In the assessments of situations where economic dependencies may exist, it is indicated that the institutions should automatically cluster customers together if one of criteria is met without taking into account the expert analysis. The proposed mechanism does not seem right as, firstly, they are not sufficient on a stand-alone basis to systematically justify a grouping, and secondly, such a systematic process will not consider the dynamic aspect of the economic dependencies. Therefore, automatic criteria will produce misleading results. For example, in point h), the situation where two companies have the same customer base don't systematically lead to a connection because if one company lose a client, this same client could be retrieve by the other company due to the limited possibility to find new customer. In this case, the expert analysis could be crucial to decide if the connection is relevant. Consequently, we believe that criteria c/, d/ and h/ may be proposed as an element of the assessment but not as systematic triggers of connection.

In our opinion the guidelines should be modified to indicate that the listed criteria should be considered in the assessment process, but without any systematic grouping.

We propose to amend the guidelines par. 23 in the following way:

~~"institutions should deem, […]"~~ by "institutions may consider, in particular […]". This will leave the flexibility for banks to assess whether the criteria characterises a real situation of economic dependency or not.

Question 09: Are you aware of any other situations that should be added to the list of situations that constitute economic dependency? In relation to the situation described above, would you treat these exposures as connected? Please explain.

No. We remind that these criteria should not lead to automatic grouping of clients. An internal expert analysis should remain the basis for assessing such connectedness.

Question 10: Is the guidance in section 7. 'Relation between interconnectedness through control and interconnectedness through economic dependency' clear? If not, please provide concrete suggestions.

What is the likely impact of this guidance? Please provide an estimation of the associated quantitative costs.

Yes. However we consider it regrettable that this consultation is performed without being linked to the on-going discussions relative to the default contagion rules.