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DEUTSCHER FACTORING VERBAND E.V.

Secretariat of the
Basel Committee on Banking Supervision
Bank for International Settlements
CH-4002 Basel
Switzerland

Operational risk: Revisions to the simpler approaches
Comments on consultative document

Berlin, 5th of January 2015

Dear Madam or Sir,

As representatives of the German factoring industry, we thank you for giving us the opportunity to express our views on the planned revisions to the simpler approaches for measuring operational risk capital.

Our association currently represents 24 factoring companies which stand for more than 90% of the annual factoring turnover in Germany (2013: 171 billion Euro), the large majority of which are classified as financial service institutions ("Finanzdienstleistungsinstitute") according to the German Banking Act ("Kreditwesengesetz"), while approximately a third of our members have a banking license and are therefore classified and regulated directly as banks. Therefore, **all our members as well as over 180 other factoring companies are subject to strict supervision and regulation by the German financial supervisory authority BaFin** (Bundesanstalt für Finanzdienstleistungsaufsicht). Moreover, out of the large majority of our members which are considered to be financial service institutions, more than 60% are part of a consolidated banking group, thereby (at least indirectly) falling within the scope of application of many supervisory provisions and prerequisites which otherwise only apply to credit institutions. However, **factoring is not the same nor can it be compared to credit transactions performed by credit institutions or banks**: In contrast to a bank loan, factoring companies offer **funding by paying the purchase price for the purchase of receivables**, resulting from the delivery of goods or services rendered.

The planned replacement of Gross Income (GI) by the Business Indicator (BI) as the new proxy indicator for operational risk exposure in the new and revised Standardised Approach (SA) may address and remedy certain weaknesses in the current approaches and thereby generally improve the estimation of capital requirements for operational risks, but in our view, this overall improvement only applies to credit institutions with clear emphasis on what can be described as "traditional" lines of banking business.

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However, the planned revisions do not generally improve the estimation of capital requirements for operational risks of banks which have specialized in certain forms of financing such as e.g. factoring. For these specialized banks, the revised SA and, more specifically, the BI does not accurately capture their operational risk profiles, but it rather presents a distorted picture and hence leads to disproportionate and inadequate capital requirements for the operational risks of such specialized banks.

Factoring companies provide working capital funding and financing solutions to businesses, particularly SMEs, based upon the accounts receivables created by the factoring client company. With a factoring solution, receivables are purchased by and assigned to a factoring company, in return for the payment of the purchase price for these receivables. If default or credit protection is part of the agreement, it is referred to as "non recourse factoring". In Germany, this is the predominant form of factoring, whereas factoring agreements where the risk of default of the debtor remains with the factoring client as seller and assignor of the receivable ("factoring with recourse") are less widely used. The factoring company will often also undertake all credit management and collections work for the factoring client. For its services, the factoring company receives a fee, and there is a discount charge for finance provided to the factoring client in advance of collections. Considering this, factoring is a form of financing which is predominantly fee-based but which also has a relatively strong interest component. Moreover, factoring is connected only to a limited number of operational risks, again in contrast to traditional banks.

It is therefore our view that these specificities need to be taken into consideration more in the works on the revised SA, just as this is mentioned in the principles of the revised SA, which state that the revised SA "should be calibrated according to the operational risk profile of a large number of banks of different size and business models" and that "it should be suitable for implementation across a wide range of ... banks" (cf. p. 7 of the consultative document "Operational risk - Revisions to the simpler approaches", October 2014).

Unless the operational risk exposure of banks specialized in factoring is captured more accurately, the capital requirements for operational risks for banks specialized in factoring will increase substantially although their operational risk situation has largely remained unchanged. This also applies to the implications the revised SA would have on the calculation of the risk bearing ability, where a similar substantial increase in the required covering would follow, should the planned revised SA be adopted in its current form, i.e. without adaptations for banks specializing in certain forms of financing such as factoring.

Please do not hesitate to contact us should you require clarifications regarding our comments and views. Also, we would be happy to provide you with more information about the factoring industry in Germany should you require this.

With kind regards,
Deutscher Factoring-Verband e.V.

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