

**ABI comments on
BCBS Consultative Document
“Review of the Credit Valuation
Adjustment Risk Framework”**

October 2015

Preliminary remarks

The Italian Banking Association (ABI) welcomes the opportunity to comment on the Consultative Document “Review of the Credit Valuation Adjustment Risk Framework”.

ABI shares the objectives pursued by the Committee and, in particular, the alignment of the CVA regulatory framework with accounting and risk management practices and with the upcoming new market risk framework. In that respect, ABI acknowledges that the BCBS proposal represents a fundamental step forward.

In order to avoid unintended consequences, ABI recommends that the results of the QIS currently in progress be given careful consideration in view of the final calibration of the framework. In fact, initial evidence gathered from members shows that the tentative calibration proposed in the Consultative Document results in a capital charge that is several times higher than the current level and does not fairly reflect the underlying risks. ABI elaborates further on this point below.

Moreover, the implementation of the reform would entail a major organisational and IT effort, and enormous operating costs, on the part of the banks. ABI would like to emphasise that the scope of these impacts will be strongly affected by the timing of the reform. In the Consultative Document, the Committee does not explicitly cite an expected date for the entry into force of the new framework. It is of the utmost importance that the date be set while taking into account that, at present, banks are already facing complexity and costs stemming from the multitude of imminent regulatory reforms (relating to derivatives and other fields).

In the following section, some observations on specific aspects of the proposed framework are illustrated.

Specific comments

Scope of application of the CVA capital charge

The scope envisaged in the present Consultative Document, in line with the scope of the current BCBS Basel III capital standards¹, encompasses all

¹ Basel Committee on Banking Supervision, *Basel III: A global regulatory framework for more resilient banks and banking systems - revised version*, June 2011.

derivatives except those cleared through a qualified central counterparty². The EU discipline³, instead, sets a stricter definition of the scope, excluding dealings with some counterparties (above all sovereigns and a high percentage of non-financial counterparties). The definition of the scope of the CVA capital charge adopted in the EU Regulation appears preferable because it excludes transactions that are not likely to give rise to systemic risk. In addition, including these transactions in the scope of the CVA would increase their cost for non-financial counterparties, and thus in the end discourage them from hedging risks.

Applicable approach

The Committee proposes two frameworks, a so-called “FRTB-CVA framework” and a “Basic CVA Framework”, the latter intended as a “residual” option for banks not willing or able to adopt the former. In ABI’s opinion, there is a need to better specify the eligibility requirements for the authorisation to use the FRTB-CVA framework. In the current draft (Annex 1, B.1.(a) and Annex 1, B.3.(a)) they seem very stringent – requiring for example an internal model for exposures – for both the options that constitute the FRTB-CVA framework, i.e. the IMA-CVA and the SA-CVA. Therefore, under the proposed framework, almost all Italian banks would apply the Basic Approach.

Furthermore, it is not clarified whether the adoption of advanced methods will be mandatory under certain conditions, as in the current CVA framework (where banks cannot choose between the standard and the advanced approach: if both the relevant VaR and IMM models are approved, the bank must use the Advanced Method).

Calibration of the new framework

As outlined above, initial exercises assessing the impact of the new framework under the proposed calibration gave rise to serious concerns. In particular, for the banks that carried out the simulation, the Basic Approach yielded a much higher capital charge than under the current rules (4-5 times or more) and is therefore very unfavourable.

The main driver of the impact seems to lie in the risk weights (Annex 1, C.2.(b)), where a more equitable calibration, in absolute terms and among the risk buckets, would be necessary. In fact, the risk weights of the

² Fair-valued securities financial transactions would be included as well.

³ Regulation (EU) N. 575/2013, art. 382.

“financials” and “sovereigns” risk buckets appear prejudicial, in particular when compared to the risk weights of the other risk buckets.

Moreover, the impact of the proposed calibration should be combined with the effects of the new counterparty credit risk standardised regulatory framework (so called SA-CCR). In fact, it is likely that a vast majority of the banks that would apply the Basic CVA Approach will use the SA-CCR as well.

Technical issues

In the FRTB-CVA approach, the Committee proposes two options for exposure calculation (Annex 1, B.1.(d) and (e); Q5). In ABI's opinion, given that one of the goals of the reform is to align the regulatory framework with accounting practices, Option A – accounting-based CVA - is preferable.

Finally, in ABI's opinion a more precise definition of the risk buckets (table on page 30 of the Consultative Document) would be useful, in order to avoid the risk of errors in the classification and the risk that different banks might apply different prudential treatments to the same instrument, due to different interpretations of the boundaries of the buckets.