Barclays Bank PLC
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28th February 2014

IVSC
1 King Street
London
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Dear Sirs,

Exposure Draft – Credit and Debit Valuation Adjustments

Thank you for the opportunity to comment on the Exposure Draft (ED), Credit and Debit Valuation Adjustments (CVA / DVA). Our overall observations are set out below and our detailed responses to the questions are included as an Appendix.

We are very supportive of the IVSC's initiative to provide information and guidance around complex and current valuation topics such as CVA and DVA. The ED is a high quality document but we suggest some amendments that will improve it further.

We consider the target audience of the ED is currently somewhat unclear, i.e. who it is aimed at. The general drafting seems to be geared towards large entities in the financial services industry, which may be inconsistent with one of the stated objectives of the paper to "aid professionals who are not specialists in understanding the principles". It is therefore important that the target audience is clarified, feedback obtained from a broad group of potential users and the document updated accordingly.

It is not entirely clear how the guidance in the ED should be applied, for example whether it advocates specific modelling techniques in preference to other possible alternative approaches. We therefore recommend to either clarify the objective of the paper as providing guidance and an overview of market practice, or to be more explicit about which techniques are considered examples of best practice.

For those unfamiliar with mathematical notation, the ED could be very technical and some of the expected models and applications may seem complex. A comment to the effect that the application would need to be scaled to the sophistication of the entity and the financial instruments it holds, might be useful. Additionally some simple worked examples on how to calculate CVA / DVA for medium and smaller entities could be included to provide further guidance, perhaps as an appendix to the paper.

Lastly, the paper refers to Funding Valuation Adjustments (FVA) in the section on current issues. We would like to highlight that this is a topic where there is presently no industry consensus on the application and definition of FVA. There are different viewpoints in the market which are evolving as discussions between peers and other experts continue. We believe the developing nature of the topic should be addressed in the paper and any observations caveated accordingly.

If you would like to discuss our response in more detail, please contact Vikas Karlekar, Global Head Product Control Valuations, (vikas.karlekar@barclays.com) or David Bradbery, Managing Director, Technical Accounting Group (david.bradbery@barclays.com).

Yours faithfully,

David Bradbery

Managing Director, Finance

Specific comments on questions in the ED

Question 1: Do you agree that the proposed scope is appropriate? If you disagree, please indicate changes that you would recommend.

We would like to highlight that the current drafting of the document appears to be focussed on IFRS users. However in the purpose section (paragraph 4) the ED makes reference to US GAAP, but then does not refer to it again. It would be good to balance the document so that it relates to both IFRS and US GAAP users unless it is specifically tailored to IFRS users in which case that should be made clear from the outset.

The target audience of the ED is currently unclear i.e. who is it aimed at. The general drafting seems to be geared towards large entities in the financial services industry, which could be inconsistent with one of the stated objectives of the paper to "aid professionals who are not specialists in understanding the principles". It is therefore important that the target audience is clarified and feedback obtained from a broad group of potential users.

Question 2: Do you agree with the definitions? If you consider an alternative or additional definition is appropriate then please provide this in your response.

The ED provides definitions of market value and fair value in paragraph 8 which are not obviously consistent with each other. It might therefore be worth explaining what the differences are and how to align the two concepts for IFRS users. Furthermore the market value definition refers to "parties acting knowledgeably, prudently and without compulsion". The term prudently or prudence has particular connotations for both accounting, valuation and regulatory purposes which might be confusing to readers when used in this context.

The ED refers in several sections to larger financial entities without defining what such entities are. In paragraph 40 for example it states that the historical method of calculating exposures would be considered insufficiently sophisticated for larger financial entities. We believe a definition of a larger financial entity should be provided or alternatively a different wording could be used such as the description in paragraph 85.

Question 3: Do you believe that other methods should be considered in addition to the Monte Carlo such as binomial and trinomial trees?

We believe that the modelling section (paragraphs 51 and following) is not comprehensive enough to provide detailed guidance on the modelling topics it raises, yet at the same time is still very technical. We would recommend to keep the discussion on a more general level, highlighting the principles that underpin the valuation approach, and provide references for further reading for those users that require comprehensive information.

For those unfamiliar with mathematical notation, the document is in a number of places very technical and some of the expected models and applications are complex. For example, the Monte Carlo method whilst relatively simple in concept may be complex and costly to apply, and may therefore not be suitable for use by all entities. It might therefore be worth further expanding in the practical section appropriate methods for entities with less sophisticated systems and volumes of derivative holdings.

Paragraphs 61 to 74 contain some general statements about how different risk factors might be modelled, however there is not sufficient detail to aid users on what method to implement. Additionally, the information included in these paragraphs is not necessarily a reflection of approaches that are universally applied. We would suggest for the section to be shortened and made more general.

We are not sure what value the reproduction of the Black-Scholes formula in paragraph 92 provides for the users as there is no further explanation on the application of the formula. We would suggest to either delete the formulaic example or provide further guidance of the valuation drivers and their relevance to CVA / DVA.

Lastly, it is unclear in the ED how the guidance should be applied, for example whether the ED prefers specific modelling techniques or whether it believes that specific techniques should not be applied. We therefore recommend to either clarify the objective of the paper as providing guidance and an overview of general market practice or to be more explicit about which techniques the IVSC considers examples of best practice.

Question 4: Do you believe that netting sets have been discussed to an appropriate level?

Yes, we believe they have been addressed at an appropriate level.

Question 5: Do you consider that there is a need for the IVSC to augment the Code of Ethical Principles for Professional Valuers with more specific guidance on governance and controls in the financial sector?

See our response to question 6.

Question 6: Do you consider that there is a particular issue or issues that arise when considering a suitable governance and control protocol for calculating CVA or DVA that does not otherwise give rise to concern?

Addressing both questions 5 and 6, we believe that detailed discussions around the governance and control principles in the IVSC framework are outside the scope of this ED. Any enhancements or changes to that framework should be addressed in a consultation paper and put through the required due process.

In general, we believe that the control framework needs to be appropriate for the risk of the entity and the derivative holding.

Question 7: Do you agree that it is appropriate to suggest that entities with less complex or smaller derivative holdings in relation to their overall business should adopt less complex methodology, or instead should all entities be expected to implement equally rigorous methodology?

The document could be considered by those unfamiliar with mathematical notation to be very technical and some of the expected models and applications could seem complex. Further comment that the application should be scaled to the sophistication of the entity and the financial instruments it holds would be a useful clarification.

Especially smaller companies would struggle to implement highly complex solutions and the cost benefit analysis of such a solution is unlikely to be positive. It would be unfortunate if the ED gave rise to an expectation that such entities should adopt unnecessarily complex solutions for computing CVA / DVA.

We therefore suggest that in paragraphs 85 to 96 further consideration is given to what distinguishes an entity between the three approaches and more guidance is provided on the simpler approaches either in an appendix or in the body of the document to allow entities to understand their situation. This should reflect additional feedback obtained from less complex / less sophisticated entities.

We would suggest to include examples on how to calculate CVA / DVA under the guidance in paragraphs 93 to 96 for medium and smaller entities perhaps as an appendix to the paper.

Question 8: Does the discussion about the cost of funding contribute to the objectives of the TIP outlined in the "Scope and Purpose" section on p3?

Yes, as the cost of funding discussion is an inherent part of CVA / DVA it is appropriate that it is included in the ED. However we would like to highlight that practice around the inclusion and calculation of FVA is evolving and there is currently no industry consensus. We therefore believe that the ED should be careful not to pre-empt industry decisions and be mindful of the evolving nature of this topic.

Question 9: Given the current debate in this area do you believe it is appropriate for this TIP to outline the main issue around FVA or should this be removed altogether until there is greater consensus?

We agree that the discussion about the cost of funding contribute to the objectives of the TIP.

However we believe that the depth of discussion depends on the ultimate purpose of the document and whether it will be primarily used for guidance or information. If the document is primarily used for information purposes, then a detailed debate of the main issues around FVA is appropriate. On the other hand however, if the document is primarily supposed to provide high level guidance then the inclusion of such a discussion might create confusion among the users.

Question 10: Are there any key principles that have been omitted or not fully explained?

A large section of the document is referring only to CVA and not to DVA. If it is considered that the statements made for CVA could be equally applied for DVA then a statement to that effect should be made.

Additionally, the paper specifically references many Basel III terms which might be confusing for non-financial services entities. While we appreciate the references and the consideration of the regulatory environment that banks operate in, these considerations might be dealt with better in a separate chapter or an appendix.