

## EBA CP 2013-05 : DRAFT IMPLEMENTING TECHNICAL STANDARDS ON ASSET ENCUMBRANCE REPORTING

### RESPONSE FROM THE BUILDING SOCIETIES ASSOCIATION (UK)

#### INTRODUCTION

The Building Societies Association (BSA) represents mutual lenders and deposit takers in the UK including all 46 UK building societies. Mutual lenders and deposit takers have total assets of over £375 billion and, together with their subsidiaries, hold residential mortgages of £245 billion, 20% of the total outstanding in the UK. They hold more than £250 billion of retail deposits, accounting for 22% of all such deposits in the UK. Mutual deposit takers account for 31% of cash ISA balances. They employ approximately 50,000 full and part-time staff and operate through approximately 2,000 branches.

The BSA is pleased to have had the opportunity both to respond to this consultation, and to attend the EBA's public hearing on these ITS on 2 May. The BSA welcomes the EBA's readiness, both stated in the CP, and expressed at the public hearing, to make these ITS proportionate.

#### GENERAL COMMENTS

The BSA agrees with some of the EBA's analysis, in section 6.1 of the CP, regarding the risks posed by high levels of asset encumbrance at banks. BSA members are predominantly retail deposit-based, and have not traditionally resorted to secured funding on any significant scale. But access to secured funding remains an important part of their resilience under stress, and - as we explain below - not all encumbrance is harmful.

As mutuals, the interests of our individual customers come first; the BSA therefore agrees that the structural subordination of retail depositors at banks is of concern. The BSA itself advocates retail depositor preference, but this benefit- even if accepted - can be nullified by excessive asset encumbrance. Retail depositors are unable directly to demand, take or use collateral even if it were available; high levels of encumbrance therefore systematically privilege those secured wholesale creditors over retail depositors.

#### PROPORTIONALITY

We also agree with the EBA that the negative aspects of high levels of asset encumbrance can constitute a threat to the regulatory objectives of financial stability, depositor protection, and reduction of systemic risk. And it is the systemic dimension to the encumbrance problem that makes it essential that measures such as reporting are *proportionate*, and sensibly targeted at the largest institutions, and those with the very highest levels of encumbrance.

Not all encumbrance is harmful, however - indeed, moderate levels are considered beneficial by the market and credit rating agencies, and in some instances it is positively required by other EU legislation. The central clearing of OTC derivatives requires the posting of margin collateral, and even bilateral contracts will have to be collateralised under EMIR. Routine access to central bank facilities is available only against collateral, so as to protect the central bank from an accumulation of credit risk to the banking sector. Deposit-takers will use repo when necessary to realise cash from securities held as liquid assets.

Access to secured funding remains an important part of resilience against both idiosyncratic and market-wide stresses. In anticipation of this, our larger members may retain on balance sheet a stock of self-issued eligible securities that have been pre-packaged for use during a stress. Furthermore, broad access to secured funding is a crucial component of a fully developed and diversified wholesale funding platform for our larger members. Finally, specific Government financing interventions, such as the UK's Funding for Lending scheme, typically operate only on a collateralised basis.

Many BSA members have practically no other source of regular encumbrance than those officially required or sanctioned examples given above, and their aggregate level of encumbrance is modest. We therefore think it would be a mistake, and not supported by any cost-benefit consideration, to require full scale reporting of encumbrance in these cases. We note the EBA's commitment to proportionality, but we consider that some of the suggested thresholds need adjusting. To do so in the way we suggest below will also restore some practical but modest incentives to institutions to moderate their normal encumbrance levels – so leading to practical risk reduction, as well as avoiding unnecessary compliance costs.

#### SPECIFIC COMMENTS

The BSA is content with the proposed threshold of € 30 billion above which institutions, being regarded as systemic, are required to complete the most detailed reporting regardless of their actual level of encumbrance.

We note that the most detailed reporting – using the Advanced Templates - is also to be required from *smaller* institutions if their level of encumbrance exceeds 5%. This level is too low, and moreover the CP itself suggests that the final figure will need to be calibrated after a data collection exercise.

The BSA strongly urges that institutions below € 30 billion should not be required to complete Advanced Templates unless their level of encumbrance regularly exceeds **20%**. Concentrating reporting and supervisory attention on the largest institutions, and on those medium sized institutions with the very highest levels of encumbrance, is clearly the smart way forward – and delivers sufficient coverage of the risk areas without wasteful and misplaced compliance burdens.

The EBA also suggests the very sensible idea of an even lower size threshold - € 1 billion - below which reporting would be further cut back. The BSA strongly supports this approach, but considers that a threshold of **€ 3 billion** (i.e. 1/10 of the higher size threshold) would be more appropriate. For those institutions below € 3 billion, but with encumbrance levels higher than **20%**, quarterly completion of the main template (only) would be sufficient. But for institutions which are below € 3 billion and whose level of encumbrance is below 20 %, the BSA proposes that **annual** completion of the main template (only) should be sufficient.

#### CONCLUSION

Other industry bodies, such as the International Capital Markets Association, are best placed to contribute detailed technical comments on the templates themselves, including on some of the practical and systems issues highlighted at the public hearing. The BSA's principal concern is to see the reporting requirements tailored in a proportionate way.

27 June 2013