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European Banking Federation response to EBA consultation paper on draft implementing technical standards on supervisory reporting requirements for the leverage ratio (EBA/CP/2012/06)

The European Banking Federation (EBF) welcomes the opportunity to respond to the EBA consultation paper on Implementing Technical standards (ITS) regarding supervisory reporting requirements for the leverage ratio.

1. Overarching Comments in relation to the Supervisory Reporting Framework within which the proposed ITS will be integrated

We note that CP 2012/06 is meant to supplement the EBA Consultation Paper CP50 on supervisory reporting for institutions, published on 20 December 2011.

Leverage Ratio reporting will be implemented together with COREP and FINREP and other reporting streams, such as Large Exposures Reporting and Liquidity Coverage and Stable Funding reporting, which will need to be coordinated and analysed to avoid unintended consequences, duplications and where possible to exploit any synergies in data mining and management.

The EBF would, therefore, like to refer to the comments that we have jointly submitted in response to the CP50 as several of those comments are also relevant within the context of CP 2012/06.

- As we strongly support the European Commission's aim to achieve a Single rulebook, we welcome the proposals made in CP 2012/06 aimed at introducing uniform requirements.
- As firms will implement the proposals made in CP 2012/06 together with those made concerning the other reporting work streams mentioned above, the comments made as to the magnitude of the proposed new framework are also relevant within the context of CP 2012/06. From a practical point of view, the timing which is being proposed is unrealistic. Even if firms had unlimited resources to try and make the proposed overhaul happen, this cannot possibly be implemented as planned by the Authorities as introducing the required changes inevitably takes time. It is a strong possibility that data quality could suffer if such ambitious timelines are adhered to.

- As a consequence, the date of the first-time application of the Framework which is being proposed in CP50 needs to be postponed until 1 January 2014, at the very least. In this regard the EBF welcomes the announcement by EBA on 31 July 2012 that the finalisation and publication of the EBA draft Implementing Technical Standards (ITS) on supervisory reporting requirements for institutions has been pushed back pending the adoption by the EU legislators of the Capital Requirements Regulation (CRR). We appreciate the acknowledgement that some flexibility will need to be given through phase-in provisions or on the implementation date of the new requirements.
- Our comments below provide additional arguments explaining in particular why implementing the proposed Leverage Ratio Reporting prior to 1 January 2014 cannot possibly be envisaged.

2. General remarks on CP 2012/06

Overall EBF considers the leverage ratio to be insensitive to risk as it ignores the quality of the assets and therefore it is a very simplistic measure. The introduction of a leverage ratio as a supplementary measure will increase the complexity of the regulatory capital framework as several measures must be managed simultaneously.

Sufficient implementation time

In EBF's view this Consultation Paper is premature, as the final CRD IV/CRR text has been delayed and most likely will not be finalised until late autumn 2012. Given the uncertainty EBF thinks that the consultation should have awaited the final legislation, which will need to address the implementation timetable. The delay in the final legislation will also delay the alignment of the leverage ratio reporting requirements and the final reporting templates to be used for this purpose.

This delay presents difficulties in terms of implementation as institutions will not have enough time to adjust to the rather substantial final leverage ratio reporting requirements within the current implementation deadline of 1 January 2013. Therefore, as noted in the overarching comments, EBF strongly recommends that the implementation date for the reporting requirements for the leverage ratio is deferred until 1 January 2014, at the least.

A holistic review of all supervisory reporting ITS

EBF finds it important to note that while improved information will help supervisors and financial markets, the accumulation of several reporting requirements while lacking a common data definition and the relevant mapping with other requests might result in multiplication of the same or similar data in several templates and excessive reconciliation /validation efforts. Consequently, EBF suggests that EBA performs a holistic review of the overall reporting requirements once the final rules enter into force, carries out a single data definition and elimination of any duplicative templates and then proposes the final ITS.

Further alleviation of the leverage ratio reporting burden

Regardless of the likely delay in implementation, but the uncertainty over that makes it an imperative, EBF thinks that all non-essential data items not required by the level 1 text for the

calculation of the leverage ratio should be removed. In particular, the templates LR3, LR6 and LR8 should be excluded (see question 1).

To further alleviate the reporting burden and in order to align the leverage ratio reporting with COREP (and FINREP), EBF proposes that quarterly calculations of the leverage ratio is used instead of monthly calculations over the quarter and that the leverage ratio reporting be required on a consolidated level only - not on an individual level. As a minimum, EBF suggests that EBA introduces a grace period for solo basis reporting till for example the end of calibration and that solo basis is interpreted in accordance with COREP definitions. Finally, the remittance date for the leverage ratio reporting should be set after the COREP remittance date.

Continuous consultation with the industry in the test period

As the current Consultation Paper is based on the original CRD IV/CRR proposal from the European Commission, it is very important that further consultation with the industry will be undertaken once the CRD IV/CRR proposal has been finalised, in order to ensure quality and consistency in reporting and that institutions are not overburdened by the final leverage ratio reporting requirements.

Similarly it should be ensured that the observation period for the leverage ratio is used to assess and implement any identified refinements and corrections to the leverage ratio reporting requirements in continuous dialogue with the industry.

3. EBF responses to consultation questions

Questions from the ITS:

Q1: Do institutions agree with the use of existing and prudential measures? Is there additional ways to alleviate the implementation burden?

EBF welcomes that the leverage ratio reporting template is developed with the aim of using existing and prudential measures, i.e. alignment with the COREP framework, in order to avoid overburdening institutions by introducing additional templates. Furthermore, EBF supports the adaption of the template to the Basel QIS template as it ensures international consistency.

However, EBF finds that more could - and should - be done to alleviate the implementation burden of the leverage ratio reporting requirements.

First, the proposal of a monthly calculated leverage ratio over the quarter will be very demanding for the institutions and the cost of monthly calculation would outweigh the relevance of a leverage ratio as long as it remains an additional measure. In addition, potential synergies of including the leverage reporting as part of the COREP framework will be lost. For example, it will not be possible to balance the Tier 1 capital (the numerator in the leverage ratio) with the Tier 1 number used in the quarterly solvency reporting, nor will it be possible to balance the exposures figure across risk weights in LR3 and IRB and SA categories in LR6. That notwithstanding, EBA refers to the specific cells in the COREP solvency reporting templates that the figures in the leverage reporting should be based on.

A main objective of the leverage ratio is to have an easy obtainable and objective non-risk measure that can be compared to the quarterly RWA calculations. To have the ratio based on average of

monthly data would make the analysis less simple to do for an external party and hence part of the motivation for the ratio would be lost.

Therefore, in order to alleviate the reporting burden, **EBF proposes to let the leverage ratio reporting requirement be based on quarterly reporting instead of quarterly averages of monthly data.** This possibility already exists in CRR article 475 (3) as a derogation whereby supervisors can allow institutions to calculate their leverage ratio quarterly instead of on a monthly basis. EBF finds that this derogation should be made general and permanent for all institutions.

EBF is aware that the monthly calculation requirement is a level 1 requirement and EBF has therefore addressed the relevant policy makers on the issue. However, EBF finds it important to flag this concern in the consultation so EBA can carry on the message in discussion with policy makers.

Second, to further alleviate the reporting burden EBF proposes **that QIS reporting on the leverage ratio be stopped** as soon as the EBA leverage reporting tests are started, in order to avoid double-reporting.

Third, EBF furthermore suggests **excluding memorandum items that are not used in the actual leverage ratio calculation** (of the 134 items required by the templates, only 10 are mandated by the level 1 text and used to calculate the leverage ratio). The most burdensome demands for banks do not seem to arise from the components used in the actual calculation of the leverage ratio, but from all the additional specifications and breakdowns.

- In particular LR2 puts higher demands on IRB banks, not using the CCFs used in the standardised approach.
- Furthermore LR6 introduces a new break down of the exposures that in several areas is not in line with the break downs in the COREP report and which is not required by the Level 1 text. Any RWA breakdowns in the standardised or the IRB approaches are already provided by COREP so there is no need to introduce a new alternative analysis. **In consequence EBF suggests that LR6 be excluded.**
- The same is true for the template LR3 as this breakdown of exposures according to their risk weights is already available in the COREP templates and is not useful in the framework of a non-sensitive risk measure like the leverage ratio. **Hence EBF suggests that LR3 be excluded.**
- The LR 8 template is also particularly onerous, as it risks inconsistencies in reporting. For example asset encumbrance reporting needs very clear definitions, particularly so that institutions can understand how the items relate to IFRS and liquidity reporting requirements. EBF cannot see the relevance of the LR8 template within the framework of the ITS on the leverage ratio as such information is not required for the actual leverage ratio calculation and furthermore it relates primarily to liquidity. **EBF therefore finds that the LR8 template should be excluded.**

Q2: Do institutions already have the data required for reporting under this proposal available on a monthly basis? If so, is the data of the required standard similar to other data reported to supervisory authorities?

Currently, not all institutions have the data required under this proposal available on a monthly basis. Some - but far from all - institutions would be able to provide (average) monthly data based upon COREP but of a less detailed nature and of less quality. To provide the level of detail on a monthly basis that is proposed in the Consultation Paper would require a considerable amount of extra work for institutions.

Such a requirement would have quite an impact on the reporting process as it requires involvement of different functions in the bank in terms of accounting data (balance sheet data), group credit data (provisions for shortfall calculation in the capital base) as well as capital adequacy data (derivative and SFT exposure). It is time consuming to process the figures since the existing IT-infrastructure has not been configured to these requirements. Moreover, implementations of updates within the IT-systems are performed during the in-between-quarter months, not to put to risk the system during the reporting period. A monthly reporting frequency takes away that possibility, and therefore increases operational risk.

Therefore, as stated in Q1, EBF proposes the use of quarterly data instead of monthly data. At present more detailed information - of better quality - is available on a quarterly basis even though this is still complex and for some institutions it would require some manual effort to adapt the financial data to regulatory reporting.

Q3: The same timelines are proposed for reporting on a consolidated level as well as on an individual level, is this seen as problematic? If so, would you propose a different timeline for reporting on a consolidated level?

EBF strongly supports the view that the leverage ratio should only be reported on a consolidated level – not on an individual level. This makes sense as institutions are managed at a consolidated level. Furthermore, the leverage ratio - while being a crude measure not based on risk - will however hit in particular those parts of a banking group that are engaged in traditional (retail) banking activities which are safe – unless the ratio is monitored on a consolidated level. Reporting on a consolidated level allows for banks with for example, un-recognised low risk weighted products on a leverage basis, e.g. residential mortgages, to balance these with higher risk weighted products.

Furthermore, the leverage ratio is linked to accounting data, i.e. FINREP, which banks need to report on a consolidated level only. Therefore, in order to create internal consistency in reporting requirements, this – i.e. reporting on consolidated level only – should also be the case for the leverage ratio.

In addition, there can be deviations between the accounting regulations on consolidated level compared to individual level, since EU IFRS is applicable on group level for listed companies while the legal entities usually report in accordance with the local GAAP. This can cause differences if leverage ratio for entity levels should be reported.

EBF is aware that, as is the case with the reporting frequency, the reporting level is also a level 1 issue that requires dialogue with policymakers, but EBF finds it necessary to flag it to EBA as well.

However, should the reporting of the leverage ratio on both levels remain, EBF finds that:

- EBA should introduce a grace period in which institutions are allowed to report their leverage ratio on a consolidated basis only so that they can achieve a certain level of industrialization of this reporting, for instance till the calibration is completed.
- EBA should clarify the meaning of the requirement for individual level reporting for this ITS as this is not clear from the CRR text. EBF strongly supports that the understanding of the individual level should not diverge from the level of application of COREP, neither should it be required for all legal entities but only for significant subsidiaries. It is impossible for some institutions to produce this reporting for every single legal entity. Applying the same level of application as COREP will improve consistency between regulatory reporting.
- Banking groups should not be required to deliver data at a solo level before those which need to be delivered at a consolidated level. In reality, most data comes from consolidated level first, so banks need to have the consolidated data to achieve the individual data.

In any case it would reduce the reporting burdens if the remittance date for reporting the leverage ratio could be set after the capital adequacy reporting.

Q4: What additional costs do you envisage from the proposed approach to reporting the leverage ratio in order to fulfill the requirements of the CRR outlined in this ITS?

If a monthly calculation of the leverage ratio is required this will have an extremely high impact on costs as it involves several functions within an institution such as accounting, group credit and capital adequacy. Adequate lead time and internal resources for such systems changes are needed. A requirement for reporting on the leverage ratio from 1 January 2013, on a basis which will not be finalised until autumn 2012 at the earliest, is at this stage almost impossible with a lead time of 6 - 9 months as basic for systems changes.

Furthermore, as already mentioned, while the data needed for the calculation of the actual leverage ratio requirement is ok, providing the additional memorandum items will be very time consuming for institutions, and should therefore be excluded.

In addition, double reporting of derivative exposures will be needed for those banks with an internal models approach (IMM) approval for derivatives for capital adequacy purposes due to the fact that the mark-to-market method for derivatives is proposed here.

Questions from Annex II:

A. Derivatives share threshold in template LR1 and LR2

Q5: Is the calculation of the derivatives share threshold sufficiently clear?

The calculation of the derivatives share threshold is as such clear.

However, it should be noted that:

- The formula for calculating the total exposure measure in paragraph 13 (page 2, annex II) seems to not be entirely correct and should be carefully re-examined. For example {LR2; 070; 5} is deducted twice.
- In the total exposure measure formula the link is unclear regarding 20% and 50% CCF as only 10% CCF is applied. It should be clarified why the split between the standardised approach CCF classes is needed if not separately considered in the calculation of the total exposure measure in the leverage ratio.

As a specific observation, EBF does not see the relevance in Template LR2 of lines 080 and 100. These are both drawn amounts yet under the heading of ‘off balance sheet items’. The heading does not suggest on and off balance sheet items should be combined here.

Q6: *Do you believe this method captures institutions derivatives exposure in a sensible way?*

EBF finds it reasonable to net derivatives instead of taking the gross value.

Q7: *Does the reduction of fields to be reported in a given period by institutions that do not exceed the threshold value in that period, lead to a significant reduction in administrative burden?*

In EBF’s view the introduction of a derivatives share threshold does not reduce the reporting burden significantly as an institution would still have to calculate the absolute value and the threshold value to determine if it was below the threshold. Furthermore, as already mentioned, some of the other templates are still quite burdensome for the institutions to fill in, especially LR6.

Q8: *Preliminary internal calculations by supervisors suggest that a threshold value should be in the range of 0.5% to 2%. Would you suggest a different threshold level, if yes, please justify this?*

EBF supports the use of a fixed materiality threshold for the derivatives share threshold but it should be higher than the proposed level.

B. Nominal amount threshold in template LR4

Q9: *Is the calculation of the nominal amount threshold sufficiently clear?*

EBF understands that the threshold should be set relative to the sum of the notional amount of all credit derivatives, i.e. purchased and sold credit derivatives. However, it is not clear whether netting of two offsetting credit derivative contracts can be treated on a net basis as a closure of a contract or whether it will count as two contracts. EBF assumes - and supports - a netting approach.

However, as mentioned in relation to the derivatives share threshold, the nominal amount threshold does not really present a burden relief either as institutions would still have to calculate the figure to determine their position. Therefore the calculation will be required for all, despite the threshold.

Q10: *Preliminary internal calculations by supervisors suggest that the nominal threshold value should be in the range of 200 to 500 million. €. Would you suggest a different threshold level, if yes, please justify this?*

In EBF’s view the nominal threshold value should be set on the basis of an institutions’ balance sheet size; it should not be a fixed amount. For example, the threshold level could be the sum of notional amount of credit derivatives in relation to the institutions total exposure measure.

Q11: *Is the term “reference name” and the distinction from “reference obligation” sufficiently clear?*

EBF understands "reference name" to refer to an underlying legal entity and thereby to be broader in scope than "reference obligation" which we interpret to refer to specific obligations of the reference name. However, further clarification would be welcome, as more interpretations have been raised among the EBF membership.

Q12: *Is the treatment of credit derivatives referring to indices and baskets sufficiently clear?*

Yes, this is clear.

Q13: *Which additional contractual features should be taken into consideration when assessing offsetting of written and purchased credit derivatives? How would this add to complexity and reporting burden?*

No comments at this point.

Q14: *Is the classification used in template LR6 sufficiently clear?*

As commented in EBF's response to Q1 the provision of the data requested in LR6 would be a quite burdensome add-on for institutions as it introduces an alternative breakdown not in line with COREP reporting. Much of the information required by LR6 will already be part of the future COREP and can be found in these reports. Hence, in order to avoid any double reporting, LR6 should be excluded. Accordingly, EBF has no comments in regard to the clarity of classification in LR6.

However, it should be noted that the mixture of financial and then regulatory reporting in one table - LR6 - is unusual.

Q15: *Do you believe the current split, which is predominantly based on the exposure classes for institutions using the standard method are appropriate or would you suggest an alternative split?*

EBF supports that the leverage ratio reporting be aligned with the data breakdown and definitions used in the COREP framework. This is not the case for the current split in LR6. Using another approach as basis for exposure class distribution, other than that used in the capital adequacy reporting, will increase the reporting burden substantially. Therefore, as mentioned above in Q14, LR6 should be excluded.

The breakdown in the current LR6 into groups that are not at all used in COREP, such as row 020, 030, 040, 050, 090, 110, 140 among others, is seen as particularly onerous, as it demands the adjustments and analysis regarding the COREP report to be made on a much more detailed level. In some areas this also puts additional requirement on data delivery as well as on the applications and processes used, which in turn are connected to a higher implementation cost.

Also the mix of two different approaches in LR6 - some rows have different requirements for institutions using the IRB method and for institutions using the standardised method – can make the analysis very complex for IRB institutions that also use some standardised exposure classes.

Finally it should also be kept in mind that, as separate documentation for standardised and IRB approaches will be required as mentioned in the Consultation Paper, this will further add to the reporting burden, although the aim is not to do so.

Q16: *Is the classification used in template LR7 sufficiently clear?*

Yes, these are standard classifications.