

Set up in 1960, the European Banking Federation is the voice of the European banking sector (European Union & European Free Trade Association countries). The EBF represents the interests of some 5000 European banks: large and small, wholesale and retail, local and cross-border financial institutions. The EBF is committed to supporting EU policies to promote the single market in financial services in general and in banking activities in particular. It advocates free and fair competition in the EU and world markets and supports the banks' efforts to increase their efficiency and competitiveness.

EBF COMMENTS ON THE EBA CONSULTATION PAPER ON DRAFT IMPLEMENTING TECHNICAL STANDARDS ON DISCLOSURE FOR OWN FUNDS BY INSTITUTIONS

KEY POINTS

- The objective of achieving enhanced transparency is supported.
- The proposed templates need to be brought in line with the expectations expressed by the users' community.
- EU Authorities should increase their efforts to convince international institutions to adopt an integrated approach to reporting requirements on a global level.
- Disclosures regarding significant subsidiaries should be required in exceptional circumstances only.
- The consultation on the proposed common templates did not duly observe Better Regulation Principles.
- The common templates should aim to achieve a minimum level of standardisation to satisfy the expectation of consistency, with flexibility allowed at institutional level to promote an enhanced disclosure with quality narratives to assist users in making informed decisions.
- The Capital Requirements Regulation, as proposed by the European Commission, does not provide the EBA with a legal mandate to prepare technical standards to impose disclosures requiring an accounting/prudential reconciliation of the whole balance sheet nor to impose templates which institutions are required to use when disclosing their capital situation during the transition phase.

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GENERAL COMMENTS

1. The Objective of Achieving Enhanced Transparency is supported

The EBF supports the consultation paper's overall thrust toward the development of comprehensive, transparent disclosures which meet the needs of market participants.

It has, however, strong reservations over the approach proposed to meet this objective and, moreover, on the process.

Although we note that the EBA Consultation is not seeking comments on the common templates that the draft ITS proposes to introduce, the EBF remains convinced that they are not meeting the expectations of the users' community. The EBF, therefore, strongly suggests amending them along the lines indicated in the comments made below.

Finally, we note that there are several references made in the Consultation Paper to documentation which has still to come. For example, page 4 of the consultation refers to "Further consultation papers on the remaining RTS on own funds in the CRR are expected to be published later in 2012". There is also reference to major changes proposed by the revised texts produced by the EU Council and Parliament, yet an acknowledgement that the final text of the CRR may still change. We are also told that the EBA will adapt the draft ITS according to the final version of CRR/ CRD IV, before submitting it to the European Commission for adoption (page 5). Whilst the EBF understands the constraints with which the EBA is faced, it is concerned about the piecemeal approach that is being adopted concerning the RTS on Own Funds as it does not allow stakeholders to examine if the various ITS are indeed internally consistent. Our expectation is, at the very least, that the EBA would re-consult with industry and users if once all any major changes appear, either in later planned consultations or in the final draft.

2. Need for an Integrated Approach to Reporting and Disclosure Requirements

The European Central Bank highlighted in its response to the Basel Committee's consultation, that it would have been preferable for the proposed common templates to be linked to the supervisory reporting requirements because such an approach would have minimised the administrative reporting burden of institutions.

Whilst we understand why it was not possible for the Basel Committee to take that suggestion on board, we nevertheless regret that the Committee did not consider ways to address the basic concern which the European Central Bank had raised, i.e. the need to avoid duplication of work. We note, in particular, that the proposed capital disclosure templates duplicate to a large extent disclosures which are currently already required under Pillar 3 (e.g. scope of consolidation, differences to the accounting scope of consolidation). Our understanding is that institutions will be authorised to make a reference to the capital disclosure templates to satisfy the corresponding Pillar III requirements. It may be useful for the forthcoming draft Technical standard to include a recital confirming this.

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Adopting a more holistic view, we note a substantial increase in various types of regulatory reporting requirements which result in multiplication of same or similar data in several templates and reconciliation/validation efforts and, therefore, create significant implementation and operating burdens on European institutions. We believe that the EU supervisory community can play a key role in convincing their peers at the Basel Committee that the time has come for the global supervisory community to prepare for adopting an integrated approach to reporting requirements in a near future. If not, the Basel Committee will be repeating the basic mistake which the EU supervisory community has been making in a recent past, i.e. to oblige cross-border banks to conform to a range of differing sets or reporting requirements which often aim at collecting identical data.

Against this backdrop, we would like to suggest that the EBA would – either in the final document or, possibly, in its feedback statement – include wording which would amount to recognising that the proposed templates duplicate existing requirements to some extent, and include a strong, formal recommendation to EU Authorities to use their influence to convince the Basel Committee that it needs to take initiatives to move towards integrated reporting.

3. Disclosures on Significant Subsidiaries

We note the provisions in Article 12, referenced in the consultation, which require disclosure by significant subsidiaries on an individual or sub-consolidated basis.

We recognise that users may need further information on significant subsidiaries, a point which has been addressed by IFRS 12, which requires additional disclosures. However, while acknowledging that EBA must operate within the confines of the Regulation text, additional regulatory disclosures need to be appropriately defined and managed to avoid confusion. Therefore we recommend that guidance is provided that such disclosures should be required only in exceptional circumstances, i.e. bearing in mind the overarching requirement to convey the risk profile to market participants.

4. EU Better Regulation Principles have not been observed

Better Regulation Principles impose on EU Authorities an obligation (i) to consult widely before proposing legislation, and (ii) to examine what is the best way to ensure that all interests have been taken into account.

We are not convinced that the process which has been adopted in producing the present consultation does meet those minimal standards.

- (i) The EBA Consultation needs to be understood against the backdrop of an initiative which has been taken by the Basel Committee aiming at requiring banks that are internationally-active across Basel member jurisdictions to publish their capital positions according to common templates.

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It has been confirmed during bilateral conversations which some of our members have held with their supervisors that, as a consequence, there is no leeway whatsoever left to the various member jurisdictions to depart from the common templates that have been agreed upon within the Basel Committee because comparability across jurisdictions would otherwise be jeopardised. We note, in any event, that the questions for consultation do not invite respondents to comment on the templates themselves. This means that the outcome of the EBA consultation process is already far progressed, regardless of the comments that stakeholders may make on the proposed templates.

We note, in particular, that the EBA has taken the initiative of consulting stakeholders only after the Basel Committee had launched its consultation and taken a decision. Our impression is that the Better Regulation Principles, to which the EU is committed, imply that the EBA should have launched its consultation whilst the Basel Committee was still in a process of preparing its decision. This would have allowed the representatives from EU Member States to take the views of EU stakeholders into account when negotiating with their peers on what the Basel Committee was going to propose.

It may be useful highlighting that the European Commission had adopted such an approach in respect of Basel III in 2010: it organised a consultation amongst EU stakeholders in parallel with the Basel Committee consultation.

- (ii) The International Banking Federation – of which the EBF is a member – had commented on the Basel Committee’s consultation in observing that the proposed common templates were substantially driven by supervisors’ assessment that the informational interests of market participants closely match their own. It had questioned, in particular, if the granularity of the data requested met the information needs of market participants. The IBFed had, therefore, welcomed in particular the invitation which the Basel Committee had specifically made to investors, analysts, rating agencies and other users of data disclosed by banks to provide feedback on the proposed templates.

An analysis of the responses received from the user community reveals that a majority of respondents to the Basel Committee consultation representing the user community concurred with the view held by IBFed.

- The **Association of British Insurers** commented, amongst others, as follows:

“ As regards regulatory capital the key objective is to understand how this data reconciles back to the reported shareholders’ equity amounts in the financial statements. We think there is probably scope for simplification of Annex 2 in a way that would achieve this with greater clarity. (...) (W)e think there is some scope for simplification of the proposed data in order to ensure an appropriate balance between the costs to preparers and the needs of investors, and indeed to avoid information overload for users. “

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- The **Corporate Reporting Users' Forum** commented, amongst others, as follows:

“ The proposed templates would take an important step toward bridging what we view as a significant disconnect between reported equity and regulatory capital, as not all banks reconcile the two, and certainly not in a comprehensive and consistent way. We offer several suggestions as to how (...) potentially to simplify Annex 2 to focus directly on the difference in equity between the consolidated financial statements and the regulatory basis of consolidation.”
- **Deutsche Börse Group** commented, amongst others, as follows:

“(I)n our view, the combined table contains all necessary details and that a step-by-step publication (...) would result in an information overload. Furthermore, the decreased readability of the information would potentially discourage receivers of the information to further use it.”
- **Fitch Rating** commented, amongst others, as follows:

“ Therefore, the proposal for banks to provide a detailed reconciliation of all regulatory capital elements back to published financial statements is welcomed by Fitch. The step by step approach detailed in the Consultative Document would provide a user-friendly tool, but we question whether the work involved in producing such a comprehensive reconciliation of the balance sheet would be justified by its usefulness. It is unlikely that many analysts would find much use for most of the line-by-line balance sheet items set out in Annex 2 for most banks. “ We have not quite understood what the Basel Committee thinks such a detailed comparison would achieve. Investors and analysts would need some of this information to understand the common equity data in lines 1 to 6 of Annex 1, but total assets and total equity comparison would present this in most cases and give an indication of whether the differences were material enough to warrant further explanation.

“ The difference, as we understand it, would be the scope of consolidation. Investors and analysts will focus on material items only, and as long as investors and analysts have an understanding of 80-90% of the reconciliation, they do not need greater detail. We would therefore urge consideration of a materiality test for the balance sheet reconciliation.”
- **The Institute of Chartered Accountants in England and Wales** commented, amongst others, as follows:

“ (W)e question the merits of requiring a detailed balance sheet comparison as set out in Annex 2.

“ We understand that the proposed balance sheet comparison in Annex 2 aims to provide information to assist users in comparing accounting and regulatory capital. Following consultation with users, our view is that the Annex 2 requirements are too detailed and may not provide the clearest information”; The

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proposals as currently drafted are too prescriptive and detailed, and will require information to be reported which may be of little interest to many stakeholders.”

- **The Higher School of Economics** (Russia) commented, amongst others, as follows:

“ (It’s important to deliver the disclosed information in a format that is less detailed and sophisticated but is easier to interpret and to incorporate into decision-making.”

Adopting a more high-level approach to all the responses that the Basel Committee received from the user community, we believe that their main thrust can be summarised as follows:

- a three-stage reconciliation of the full balance sheet is too much information, and the focus should be on the capital account;
- they would favour simplification and the application of reasonable materiality thresholds, for instance in the analysis within regulatory capital of the impact of interests in associates and unconsolidated investments;
- they would prefer, instead of data volume, helpful explanation of the key differences between the financial accounting and regulatory consolidations and the resulting capital numbers.

We were surprised to note that the Basel Committee did not follow up to their comments and, moreover, and probably more importantly, did not even go through the effort of explaining why. This is another flaw in the process.

Our understanding is that the EBA will explain – either in the final version of the technical standard or in its feedback statement - why the supervisory community believed it to be appropriate to overlook the views held by a significant part of the user community.

SPECIFIC COMMENTS

1. Common Templates

The supervisory community takes the view that common disclosure templates are needed in order to improve comparability of disclosure information.

Although we understand this objective, we would like to point out that there are good reasons for institutions to determine the scope and the level of detail of the disclosure information on their own. This approach is based on the idea that due to market discipline, an institution is able to find a suitable solution commensurate with the complexity and scale of its business. Hereby individual specifics of an institution can be considered adequately.

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Anyway, based on the feedback provided by the user community, we believe that consistency, usefulness and user friendliness are the most valued attributes of information for disclosure purposes. Excessive level of detailed, high volume information, combined with complex technical calculation, is likely to obscure any key information presented, especially for large and diverse institutions. Hence, it will reduce the usefulness and user friendliness of the disclosures provided.

We therefore, propose a minimum level of standardisation to satisfy the expectation of consistency, with flexibility allowed at institutional level to promote an enhanced disclosure with quality narratives to assist users in making informed decisions.

2. Reconciliation of the Regulatory Versus Accounting Consolidation

- The EBA technical standards cannot possibly go beyond the mandate which the EU legislative framework confers to it.

Article 424 CRR – which is the legal basis of the proposed technical standard – states the following:

“Institutions shall disclose (...) a full reconciliation of Common Equity Tier 1 items, Additional Tier 1 items, Tier 2 items and filters and deductions applied pursuant to Articles 29 to 32, 33, 53, 63 and 74 to own funds of the institution and the balance sheet in the audited financial statements of the institution.”

Clearly, this provision does NOT require institutions to undertake an accounting/prudential reconciliation of the whole balance sheet. It only requires a full reconciliation in respect of the own fund components.

The template, as proposed, lacks, therefore, a sufficient legal basis.

- We do not consider that the objectives of transparency and comparability would be best served by the use of the common template proposed in Annex I. We note, as mentioned above, that a majority within the users’ community has expressed a similar opinion.

The proposed reconciliation template takes a tabular numeric approach to setting out every item that may differ, between accounting and regulatory records. The reasons for many of these items will be highly technical, and a simple comparison of individual values could lead to misunderstanding by less skilled analysts, when the items are taken in isolation. Our belief is that, especially for larger, complex banking groups - those in which the market may be particularly interested - the output of this particular exercise may more likely confuse users than enlighten them. This is because the resulting template would itself be complex, with a large number of 'many-to-many' linkages between the accounting and regulatory balance sheets, including a lack of one-to-one correlation in many instances. The effort expended in preparing this template would therefore be disproportionate to the value added.

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Furthermore, as the responses to the Basel Committee's consultation have amply demonstrated, investors are not so much interested in high volumes of data per se as in high quality, summarised information that is immediately relevant and understandable. The end-objective should not be to provide a mathematical 'reconciliation' as such, but to illuminate the differences between the accounting and regulatory balance sheets. We suggest that more helpful to most users from the outset would be:

- a) to provide figures for the principal differences, both in terms of material amounts and significant topics that we know to be of interest to investors, and
 - b) narrative to explain that data meaningfully to them.
- If the comments made above would not be accepted, we would like to strongly suggest that the example which is provided in Annex A be substantially amended and that the reconciliation requirement be limited to balance sheet totals only.

More particularly, the proposed reconciliation requirement should aim at explaining the major differences, in broad terms, between the Total Assets published in the financial statements and the Total Assets included in the regulatory balance sheet. This should include particular emphasis on assets which are treated differently within the scope of the Regulatory framework, with indication of the reasons underlying the major discrepancies, including discrepancies in consolidation criteria and differing valuation rules.

In tabular form this might look as follows:

Total assets published in the financial statements.	
+/- Major differences between Finance and Risk (financial statements vs regulatory totals) e.g.:	
<ul style="list-style-type: none">• Differences because of consolidation criteria• Differences in valuation• Different treatment of derivatives• Differences re netting of balances	
Total assets included in regulatory reporting	

3. Disclosure Template During the Transition Phase

The transition period will increase the complexity of the capital position of banks. We, therefore, understand the importance of banks providing appropriate disclosure during this time. Nevertheless, we do hold certain concerns over the content of the proposed disclosure.

- Article 470 CRR sets out the Own Funds disclosures which institutions are required to make from 1 January 2013 to 31 December 2021. Those required disclosures will further increase complexity, and, to be useful, will certainly require more detailed supplementary

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explanation of the figures shown, including of the care needing to be exercised in interpreting these for the purpose of projecting future capital levels.

- Article 470 CRR does not confer any mandate whatsoever to the EBA to prepare technical standards in this respect. The proposed Transitional Own Funds Disclosure Template therefore lacks any legal basis.
- It needs to be added, moreover, that the proposed transitional template apparently presumes that the figures which will be disclosed across different jurisdictions and institutions will be perfectly comparable.

This might have been true if all jurisdictions would have decided to phase-in the transitional arrangements in conformity with what has agreed in Basel III. Unfortunately, however, this will not happen. Whilst the US appears to be determined to observe the Basel III transitional arrangements, some EU Member States are contemplating accelerating the transitional arrangements, without the CRR objecting to such an approach. Furthermore, definitions which have been harmonised at a global level are missing, which may result in making comparisons an illusionary exercise.

The transitional templates cannot, therefore, be reconciled with the overarching objective which the proposed common templates aim to achieve, i.e. to allow making (faithful) comparisons between institutions across jurisdictions.

We continue to believe, moreover, that it would be inappropriate for EU banks to complete the transitional own funds disclosure template as proposed.

- Such a requirement is inconsistent with the transitional arrangements defined in the Basel III standards. The very introduction of transitional arrangements implies *ipso facto* that the disclosures about the composition of capital which Paragraph 93 of the Basel III Resilience Framework imposes only need to be made in line with the gradual time-frame which it proposes.
- Moreover, the proposed template makes it extremely easy to derive the full Basel 3 figures. As a result, markets might recklessly simulate the full Basel 3 figures and reach a random conclusion on whether the institution might - or might not - be Basel 3 compliant at the 2018 horizon – notwithstanding that there are a whole range of other parameters that may come into play until 2018 which banks may be planning to influence? It is precisely this possibility which explains why a phased-in approach has been opted for.
- Furthermore, those transitional arrangements have been introduced to allow banks to implement the new framework “*through reasonable earnings retention and capital raising, while still supporting lending to the economy*”. They aim to ensure that increasing the resilience of institutions does not unduly affect lending to the real economy and without putting a lot of pressure on capital markets.
- Finally, disclosures of all regulatory adjustments under the full terms and conditions of Basel III may provide market participants with access to additional information that could be detrimental to the publishing institutions, for instance with respect to external growth operations.

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