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FEEDBACK TO THE CONSULTATION ON THE APPLICATION OF THE SUPERVISORY REVIEW PROCESS UNDER PILLAR 2 (CPO3 REVISED)

1. In May 2004, CEBS published a consultation paper on the application of the supervisory review process under Pillar 2 (CP03). A revised version of that paper was submitted for a second round of public consultation in June 2005. The paper included amendments to take feedback received in the first round of consultation into account, and was also expanded to reflect additional work carried out in the interim. The second consultation period ended on 21 October 2005. Seventeen responses were received, all but one of which are available on the CEBS website (one respondent asked that its comments be treated confidentially).
2. This paper presents a summary of the major points raised in the second round of consultation and the changes made to address them. Several common themes emerged from the comments; they related to internal governance, the scope of application of the revised CPO3, concerns about what respondents perceived as the overly detailed and prescriptive nature of the guidelines, the link between SREP and ICAAP and proportionality and the application of the guidelines to smaller and less complex institutions. Some comments referred to the interplay with other consultation papers.
3. The Annex provides a detailed description of the comments received and CEBS' response to them.

INTERNAL GOVERNANCE

Detail and prescription

4. The revised consultation paper included a new section on internal governance and asked respondents whether there was agreement that this area should be a key focus of the evaluation of the ICAAP. While there was general agreement that internal governance is an essential part of risk management, many respondents expressed concern about the scope of the requirements and suggested that CEBS' guidance should be confined to key basic principles and aspects of direct relevance to Pillar 2. Several respondents did not see the need to issue any guidance on this subject. Some respondents noted that the consultation paper on the validation of advanced modelling approaches (CP10) also contains draft guidance on internal governance, and suggested that it would be useful for CEBS to centralise all of its internal governance guidance in a single document. CEBS believes that its draft guidelines on the supervisory review process are a useful complement to the guidelines in CP10. The CRD is more granular in its model validation provisions than in the Pillar 2 section, and hence more detailed guidelines are necessary in CP10. However, CEBS recognises that more emphasis should be placed on the nature of the guidelines, explaining that they represent a common understanding of

supervisors clarifying their expectations for internal governance, rather than prescriptive rules to be complied with.

5. Many respondents also indicated that the guidelines on internal governance are excessively detailed and prescriptive, and in some cases are not consistent with the governance and organisational structures actually used by institutions. They requested greater flexibility in the allocation of responsibilities, which would make it easier to comply with the legal frameworks in different Member States and minimise any negative impact of the guidelines on institutions' organisational structures. It was not CEBS' intention to establish overly prescriptive guidelines, and CEBS agrees that there should be flexibility in how the guidelines can be met. To avoid confusion the guidelines have been amended to adopt a higher level perspective. Moreover, the definition of 'management body' has been changed slightly and placed more prominently in the guidelines with the definition of 'internal governance' in the 'Key Components' section of the guidelines.

Redundant guidelines

6. Some respondents suggested that the current scale of the proposed guidelines on internal governance is not required by the CRD. In their opinion, the provisions of the CRD (Article 22 and Annex V) are sufficient in themselves, and do not require additional guidelines. They felt that imposing additional requirements represented a significant deviation from the limits on responsibilities envisaged by the Lamfalussy process, and could trigger a debate on the consistency of CEBS' guidelines with the framework of the CRD. CEBS considers that its draft guidance on internal governance is neither inconsistent with the CRD nor goes beyond the mandate of Level 3 Committees to promote convergence in supervisory practices. Internal governance is an important concept in the CRD, and in order to foster convergence in approaches, supervisors need to clarify their common understanding of the Directive's provisions.

SCOPE OF APPLICATION

Calls for application on a consolidated basis only

7. Many respondents, while acknowledging that the provisions of the CRD explicitly envisage pillar 2 to be carried out on a solo and sub-consolidated level, called for it to be applied, as far as possible, at the group level. These respondents felt that the home supervisor should assume a strong coordinating role in the SRP dialogue with the group as a whole, and they argued that the final document should recommend a substantially reduced ICAAP and SREP at the subsidiary or subgroup level, compensated by an enhanced dialogue between home and host regulators. Although this topic is addressed in CEBS' draft guidelines for cooperation between consolidating supervisors and host supervisors (CP09), some respondents suggested that these principles should be developed further in CP03. Their main arguments were:
 - Separate Pillar 2 processes for each solo entity could lead to overcapitalization on a consolidated level.

- A SREP conducted at the level of a subsidiary alone could give misleading results, since internationally active institutions typically focus their internal capital efforts on the group level, using centralised treasury and risk-management functions.
 - Separate national processes could lead to contradictory requirements and interpretations.
 - Formal requirements for ICAAP/SREP at the subsidiary level should be minimised and generous allowance made for central control and analytical functions.
8. CEBS recognises the importance of this issue and is seeking to enhance home-host coordination. CEBS notes, however, that this is a legal matter. The guidelines must clearly and unequivocally reflect the framework established in the Directive. The CRD requires that the ICAAP be applied at the (sub)consolidated level in a Member State and at the individual level if the credit institution which is neither a subsidiary in the Member State where it is authorised and supervised, nor a parent undertaking, or if the credit institution is not included in the consolidation. The guidelines have been amended - see 'Key Considerations' - to provide a more detailed explanation on this subject.

PRESCRIPTIVENESS AND THE LINK BETWEEN ICAAP-SREP

Too prescriptive?

9. Respondents generally welcomed the additional emphasis that CEBS has placed on the dialogue between institutions and supervisors. However, some respondents suggested that the overall tone of the guidelines had changed from high-level principles to a more rigid supervisory 'checklist,' which they felt could weaken the quality of the dialogue and lead to an excessive reliance on additional capital requirements. They expressed their concern that the revised guidelines placed less emphasis on the two-way nature of the dialogue, and asked CEBS to revert to the language of the earlier draft wherever possible. Similarly, many respondents did not consider the image of a 'building block' approach appropriate for the issues treated under Pillar 2. While they agreed that some degree of prescription is needed for convergence to have any substance, many respondents felt that the guidelines were overly prescriptive and would lead to automatic capital add-ons.
10. CEBS finds some merit in these suggestions. Accordingly, the guidelines have been amended to better reflect the notion that capital is not the only corrective measure, and to stress the pragmatic and qualitative approach that EU supervisors will take to Pillar 2. Some wording changes have also been made throughout the document in order to avoid the erroneous perception of prescription and to achieve a more balanced approach

Flexibility

11. Some respondents stressed that the dialogue between institutions and supervisors will be more effective if the guiding principle is that 'one size cannot fit all.' They felt that the dialogue should encourage and reinforce senior

management's ownership of its ICAAP and its responsibility for the definition of appropriate capital levels. The industry believes that there could be a very fine line between a regulator assessing an institution's decisions and actions, and engaging in a form of shadow management. CEBS agrees with this comment and understands that the dialogue should reflect how a business is managed and organised in practice, rather than imposing an approach which merely fulfils a regulatory requirement. The guidelines have been amended - see 'Key Considerations' - to include this concept explicitly.

12. Other respondents emphasised the level of trust and confidence between institutions and supervisors as the basis for the dialogue. In order to encourage institutions to participate freely in the dialogue, some respondents stressed that supervisors should provide clear feedback to institutions on how they evaluate ICAAPs, should supply timely and reasonable explanations as to why requests are made or actions are taken, and should ensure confidentiality of the entire information exchange process. Some respondents sought clarification on two aspects that they felt remained ambiguous: how the dialogue will be conducted in practice (e.g., who will bear the burden of proof?), and what the role of the peer group review will be. CEBS believes that the answers to these questions will emerge as implementation plans develop. It is important to be conscious of the need to be flexible in the approaches to avoid being overly prescriptive.

SMALLER-LESS COMPLEX INSTITUTIONS/ PROPORTIONALITY

Less guidance?

13. CP03 asked whether smaller, less complex institutions would find additional optional guidance on the ICAAP helpful, and, if so, what such guidance might cover. Many respondents saw no need for further guidance, over and above the concept of proportionality. Most felt that information on which areas of the ICAAP are considered less important for small and less complex institutions would be more helpful than additional guidance. A few respondents stated that some additional guidance would make it easier for small institutions to implement Pillar 2, and suggested that such guidelines should cover generic tools and principles.
14. CEBS carefully considered the arguments raised in the consultation, and concluded that no specific guidance should be issued at this stage. It is important to note, however, that while all of the guidance is relevant to smaller and less complex institutions, supervisors and institutions should take full account of the principle of proportionality when applying the SREP/ICAAP.

Proportionality

15. In general, there was strong support for the emphasis that CEBS placed on the importance of proportionality, and many respondents considered that the current flexibility was appropriate. They also agreed that the proportionality principle should relate both to the specific features of the institutions (size, complexity) and to the intensity of the dialogue between institutions and supervisors.

16. However, some respondents were concerned about the removal of references to the principle of proportionality from the text, and requested that this important point should be re-inserted in the IG, ICAAP, SREP, and RAS principles. Others thought that the guidelines were sufficiently clear. CEBS acknowledges that the absence of specific references to proportionality in the IG, ICAAP, SREP, and RAS principles may have generated some confusion. After the first round of consultation, CEBS decided to remove these *repeated* references to proportionality in the paper, and to highlight the general principle of proportionality in both the executive summary and the key considerations. This was never intended to dilute the importance attached to this concept or to diminish its scope. To avoid confusion and to reinforce this principle, a footnote has been added at the beginning of every chapter stating that the key components and considerations, including those on proportionality, apply to every chapter in full. Moreover, for those IG guidelines where the possibility for misunderstanding was significant, specific mention of the principle of proportionality has been added
17. Respondents also sought clarification on the application of internal governance principles to both smaller institutions and complex institutions. The industry was concerned about the ability of smaller institutions to fulfil all of the requirements set out in the internal governance section. The industry also recommended that the guidelines should explicitly state that proportionality should take into account not only of the limited resources of smaller institutions but also the expectation of a greater degree of delegation of duties in more complex institutions. CEBS acknowledges that proportionality is an important issue for smaller institutions, but does not expect greater delegation in larger and more complex institutions.
18. Some respondents requested that the intensity of the dialogue should be significantly scaled down in certain circumstances, such as when an entity is a small institution within a larger group, when an entity uses the Standardised Approach, when capital is readily available from a parent company, or when capital is maintained at significantly higher levels than the 8 percent minimum as a result of large exposure constraints. CEBS maintains its position that the main concern for supervisors is ensuring that institutions adequately identify, measure, aggregate, and monitor their risks and – where appropriate – allocate capital to them

Materiality

19. Some respondents also indicated that CEBS should acknowledge 'materiality' (as one aspect of proportionality) as fundamental to 'better regulation,' and should include it uniformly in the guidelines. CEBS considers that this concept is already clear in the paper insofar as materiality is not directly linked to the issue of proportionality and concludes there is no need to make further changes in this respect. However CEBS agrees to clarify the guidelines and to note that institutions should identify and assess all material risks in their ICAAPs
20. The attached annex summarises the main comments and concerns raised during the consultation exercise, CEBS' analysis, and the decisions taken on them. The changes in the text have also been incorporated in CEBS' final Guidelines on The Application of the Supervisory Review Process under Pillar 2.

Analysis of responses to CP03 (rev)

Supervisory Review Process

Draft Text CP03 rev	Received Comments	CEBS DRAFT Analysis	New text (proposal)
	General issues		
	<p>Some respondents asked clarification about the status of CEBS guidelines and their interaction with other texts in place, especially guidelines in force at the national level</p> <p>It seems not clear whether CEBS intends its guidelines to be considered as strict requirements or rather as examples.</p>	<p>The CEBS Charter refers to the legal quality of CEBS' tools and products states in its Article 4.3 that "[...] the members will introduce [guidelines, recommendations and standards] in their regulatory / supervisory practices on a voluntary basis."</p> <p>Further clarification is provided by the Lamfalussy report where it is written that "the outcome of this work would be non-binding although clearly it would carry considerable authority."</p>	N/R
	Respondents needed to know whether, or to what extent, and from which date the guidelines in this paper will or may come into force in the relevant	Criteria and methodologies related to Pillar II will formally take effect in each jurisdiction to coincide with the	N/R

	jurisdictions.	relevant implementation dates set out in the Capital Requirements Directive. Moreover, according to article 144 of the CRD and CEBS guidelines on Supervisory disclosure those criteria and methodologies will have to be disclosed by year end 2006.	
	Some respondents asked regulators to be mindful of the manner in which supervisor implement the pillar 2 regime could increase the cost base of the regulated firms. Higher costs will be passed on to end users and could lead to decreased efficiency in the system.	Supervisors recognize the need to avoid imposing unnecessary costs on institutions. As such, they are committed to applying a proportionate and coordinated approach, while encouraging institutions to develop more advanced risk management approaches.	N/R
	It was pointed out that the CEBS document formally applies to banks and investment firms only. However, the further integration of risk management functions in financial conglomerates should not be impeded by these rules.	Agree but CEBS formal remit does not extend to conglomerates.	N/R
	CEBS should provide more information on how they will strive for convergence and consistency of approach, whilst ensuring that the individual needs of firms are respected.	The ICAAP guidelines have been kept deliberately high level so as to respect the individual needs and responsibilities of the institutions and allow maximum flexibility. However, CEBS will undertake more work in 2006 on achieving an appropriate degree of convergence and consistency of approach	N/R
"Principal aims of Pillar 2" "Institutions should themselves develop sound risk	Respondents consider that most banks (particularly small and medium-sized institutions) are not in a position at present to aggregate all risks and arrive at	CEBS believe that all institutions must be able to present an ICAAP. However, supervisors will take a pragmatic approach, making	N/R

<p>management processes that measure, aggregate and monitor their risks</p>	<p>a single risk number.</p>	<p>allowance for the challenges posed, especially for small to medium sized institutions. It is not expected that small institutions need to undertake complex aggregation calculations in order to arrive at their capital assessment.</p>	
<p>Relation to Pillar 1 "Institutions are expected to operate above the minimum capital requirements set under Pillar 1.</p>	<p>The following comments were pointed out:</p> <ul style="list-style-type: none"> -The statement states in the paper is against the rule that capital is not always the best way to mitigating risk. -CEBS should explicitly clarify that supervisors will impose no capital requirements going beyond those under Pillar 1 if the ICAAP is judged to be "fully satisfactory" -Capital is no the first tool to be used as a typical means to address a "not fully satisfactory ICAAP process". Only in exceptional circumstances should additional capital be required under Pillar 2 -The distinction between the "quantitative" first pillar and the "qualitative" second pillar should be made very clearly throughout the paper. 	<p>The statement referred to is taken verbatim from the Basel Framework document and there is no conflict between this and the reference to capital not always being the best way of mitigating risks.</p> <p>Each supervisory authority will decide how to give effect to this principle</p> <p>CEBS agrees that a range of mitigants can be acceptable, of which capital is only one, albeit an important one.</p> <p>Pillar 1 should not be considered as purely quantitative in nature.</p> <p>Nevertheless some modifications have been introduced in the text to reinforce the balance required between quantitative and qualitative measures</p>	
	<p>One respondents stressed the existing divergence between minimum regulatory capital and economic capital and its allocation:</p> <p>(i) For credit risk, economic capital is expected to be</p>	<p>The minimum regulatory capital requirement under Pillar 1 has been calibrated by Basel on the basis of a well diversified internationally active</p>	<p>N/R</p>

	<p>lower than the minimum regulatory capital, due to the more conservative assumptions underlying the Pillar 1 framework for credit risk</p> <p>(ii) Economic capital is allocated to business lines or business units, regulatory capital must be allocated to legal entities</p> <p>(iii) The regulatory definition of available capital (Tier 1, 2 and 3 capital) differs from the definition of economic capital that bank themselves think they should hold and</p> <p>(iv) Some institutions' economic capital framework includes risks in entities that are not covered under the CRD (i.e. insurance risks in entities that do not fall in the scope of application of the CRD).</p>	<p>bank.</p> <p>It is recognised, at the same time, that economic capital serves different objectives, uses a different definition of capital, applies different correlation assumptions, and may encompass entities not covered by CRD. Additionally banks' ICAAPs should include ALL material risks, not just credit risk or pillar one risks</p> <p>For these reasons, it is inevitable that there could be divergences between the regulatory approach and economic capital modelling. Furthermore it is important that banks are able to explain and discuss such differences, in the supervisory dialogue.</p>	
	<p>Some respondents expressed that some terms such as "internal capital", "regulatory capital", "economic capital" and "own funds" were not used consistently throughout the paper.</p>	<p>CEBS has introduced some changes in the paper to be consistent</p>	
<p>Principal aims of Pillar 2 " The dialogue should embrace all aspects of business risk and control risk, including risk management systems, internal control systems and internal governance</p>	<p>Some respondents requested clarification and greater precision on how these terms and in particular "control risk" are being used and are to be understood.</p>		

	Complaint mechanisms for banks should be elaborated at European level. Divergence in this field, in particular if efficient dispute settlement procedures are established in some countries only, could seriously affect the aim of a level playing-field.	CEBS might investigate the concept of mediation mechanisms to find out if it could be used in the banking sector.	
	One respondent pointed out that the adopted CRD has dropped any direct reference to the BCBS's February 2003 Sound Practices for the Management and Supervision of Operational Risk and the BCBS's Pillar 2 guidance suggesting that banks should possess operational risk frameworks. If these omissions are not addressed by CEBS, the treatment of a credit institution or investment firm's operational risk framework might become a source of supervisory divergence.	CEBS follows Basel good agreed papers and good practices. Not necessary for CEBS to replicate work done in other fora.	
	Some respondents urged CEBS to continue to refine its guidance and work with its sister committees (and in particular CESR) to ensure that its Pillar 2 guidance accommodates those credit institutions and investment firms adopting a holistic approach to their business and control risks (MiFID)	CEBS continues its work with the other level 3 committees to promote consistency.	
Relation to Pillar 1 "..... supervisory authorities will focus on own funds in the ICAAP-SREP dialogue.	Some respondents were critical of the fact that evaluation with regard to regulatory capital was to be carried out only by supervisors. This will lead to difficulties in determining what may be deemed an appropriate level of capital. It is the responsibility of the management board, not supervisors, to determine what operating variables are to be regarded internally as optimum/adequate.	ICAAP 10 requires institutions to explain to the supervisor's satisfaction the similarities and differences between its ICAAP and its own funds requirements. Furthermore the supervisor has the responsibility to satisfy himself that an institution holds adequate regulatory capital	
	Many respondents mention that CEBS document does not sufficiently stress the confidentiality of the SRP which should be a bilateral process between bank and supervisor and where supervisors have access to a very large amount of sensitive data and confidential	CEBS considers that no changes are required. It is acknowledged that the SRP is primarily a bilateral process. Confidentiality will be respected in accordance with European and	N/R

	information.	national legal provisions.	
	<p>Many respondents found it crucial to extend supervisory cooperation and convergence on Pillar 2 to non-EU regulators as well.</p> <p>CEBS should take the international dimension into account, both in working with the AIG and in developing guidance for supervisors. In a longer timeframe, it will be desirable for the EU authorities, including CEBS, to develop more formal relationships for cross border implementation of Pillar 2.</p>	<p>CEBS hopes that its proposals for home/host cooperation can influence the wider international debate as to how Pillar 2 should be conducted on a cross-border basis.</p>	
	Scope of application (Home/host)		
	<p>Several respondents called for Pillar 2 to be applied as far as possible, at the group level. They stressed that home supervisor should take on a strong coordinating role in the SRP dialogue with the institution.</p> <p>The main arguments were that separate Pillar2 processes on each solo entity level could lead to:</p> <ul style="list-style-type: none"> • overcapitalization on a consolidated level. • misleading results as internationally active banks typically focus their internal capital efforts on the group level, using centralized treasury and risk management functions. • contradictory, or even mutually exclusive, requirements and interpretations <p>The supervisory effort needed to be able to assemble information from all parts of the group and determine whether the individual legal entities are receiving the</p>	<p>CEBS fully recognises the importance of this matter and is making an effort to enhance home host coordination. Nevertheless, CEBS also notes that this is a legal issue and the guidelines should reflect the framework established in the Directive.</p> <p>A key purpose of CEBS guidelines is to lay the foundation for common understandings and convergent practices which should better facilitate the recognition of group functions</p> <p>The guidelines have been amended - see 'key considerations' - to give a more detailed explanation on this subject.</p>	<p>See new text in the guidelines</p>

	<p>support that is required.</p> <p>Based on strong dialogue between home and host regulators formal requirements for ICAAP/SREP at the subsidiary level should be minimized and generous allowance made for central control and analytical functions.</p> <p>Although this topic is handled in CPO9, respondents requested that should be also developed in CP03 stressing among others the following features; the consolidating supervisor role in coordinating the SREP and its recognition by all the host supervisors on a multilateral basis, the importance of the degree of integration of the banking group and its internal organisation in the SREP, the importance of two-way exchange of information and mutual recognition between consolidating and host supervisors, the fully recognition by the host supervisor of the SREP conclusions and the decisions of the consolidating supervisor, the fully integration of the local SREP in the evaluation of the whole banking group...</p>		
	Prescription		
	<p>Most of respondents found that the principles and guidelines contained in the revised CEBS paper are too prescriptive and rigid mainly the section relating to internal governance</p> <p>Overall respondents welcomed the additional importance laid on the dialogue between institutions and supervisors. However, some respondents suggested that the overall 'tone' of the guidelines had moved from high level principles to a rigid supervisory checklist which could weaken the quality of the dialogue and lead to a generally additive</p>	<p>CEBS realises that some presentational and /or languages issues could be misinterpreted. Accordingly the guidelines have been amended to better reflect the CEBS intention.</p>	<p>See changes through the paper</p>

	<p>approach to capital.</p> <p>They argued that there is less emphasis than before on the two-way nature of the dialogue, which would be a retrograde step.</p> <p>Many respondents did not find the image of a “building block” approach appropriate for the issues treated under Pillar 2.</p> <p>They requested for a reversion to the language of the earlier drafting wherever possible.</p>		
	Supervisory disclosure		
	<p>Respondents argued that in the revised version of CP 03, compared to the initial version, the obligation to disclose the supervisory criteria has been removed or relaxed. In addition, these are issues not covered by the disclosure requirements included in CP 05.</p> <p>They also expected that national supervisors fully disclose their national RAS in a manner that is accessible to all practitioners.</p> <p>They consider supervisory disclosure as essential to the development of a Pillar 2 framework and therefore they asked that this information be provided by CEBS before the CRD’s transposition.</p> <p>CP03 Revised should confirm that the supervisory disclosures concern only the criteria and methodologies used by the supervisors, and not information about a specific institution</p>	<p>The CRD requires competent authorities to disclose the general criteria and methodologies they use in the review and evaluation of the SREP. CEBS guidelines on Supervisory disclosure do cover the disclosure requirements of article 144 1 C) and set out how this will be disclosed by the CAs.</p> <p>The SDF will be implemented by year end 2006 as a target date for qualitative information, and by mid 2008 for the statistical data, recognising that some of the intended content may not yet be available at the time.</p> <p>An earlier implementation target date, in the middle of the implementation of the CRD itself, might lead to unnecessary confusion and prove</p>	N/R

		burdensome.	
	Material risks		
	Taking into account that materiality is one aspect of proportionality, some respondents noted that the CEBS paper demands that firms carry out an assessment of ALL risks which is practically impossible. The effective risk assessment should only be concentrated on assessing the impact of the material risks.	CEBS considers that materiality is not directly linked to the issue of proportionality. However CEBS agrees to clarify the guidelines and to note that institutions should identify and assess all material risks in their ICAAPs	
	Guidelines for institutions		
	Guidelines on Internal governance		
	Many comments reflected a general agreement on the importance of internal governance as an essential part for appropriate risk management. However on balance this section was not supported by the majority of respondents which considered that it was duplicative, detail, prescriptive and redundant. Moreover they stressed that the concept of proportionality was not properly considered in this section and asked CEBS to be mindful of including any detail which could be perceived as interfering in the organization of banking groups.	CEBS accommodates these comments by including some changes in the final guidelines.	
	IG 2/IG7/IG8		
	Flexible allocation of responsibilities would make it possible to comply with the different frameworks set	CEBS agrees that there should be flexibility in how responsibilities are	

	by member states' national legal regimes.	distributed and performed, but ultimately this should not detract from where ultimate responsibilities lie.	
	IG 3		
<p>IG3</p> <p>a).....institutions should establish risk management function to cover each material business line</p> <p>b).... it typically focuses on maximising the risk/ return trade.....Risk management includes ongoing identification, measurement and assessment of all risks.....</p>	<p>To ask for a separate risk control function within each material business line is considered a too detailed requirement.</p> <p>Risk management should take place at each level of the organisation with the central function setting risk management policy and monitoring risk management.</p> <p>There is a confusion of Risk Management and managing risks. The risk/ return trade off is a decision for the management function (managing director) not the risk management function. Furthermore some business models are based on maximizing customer use not on maximum return.</p> <p>Risk management functions generally attempt to deal with material risks instead of all risks.</p>	<p>Proposed changes:</p> <ul style="list-style-type: none"> - In the last sentence replace the word "should" by "could consider" -Delete "it typically focuses on maximising the risk/ return trade-off...." -change the wording to all material risks 	<p>IG3 a).....institutions could consider establishing risk management function to cover each material business line</p> <p>b) Risk management includes ongoing identification, measurement and assessment of all material risks.....</p>
	IG 4		
<p>IG 4 They should include setting the institution's business objectives, risk strategies and risk profile, and adopting the policies needed to achieve these</p>	<p>IG 4 should be read at level of the subsidiary as « They should include that the local management body is fully aware of the business objectives, risk strategies, risk profile and policies defined by the banking group and that the local management is fully responsible for the appropriate implementation in the subsidiary »</p>	<p>CEBS has added a fourth sub-paragraph to describe the responsibilities of the management body of a subsidiary.</p> <p>CEBS believes that it would be useful and easier to follow-up if they are in</p>	<p>IG4 d) In the case of subsidiaries, the responsibilities of the management body (..) should acknowledge the business objectives, risk profile and policies defined by the management body of the parent institution. It</p>

objectives. IG4 c) Documentation should include the essential duties and working procedures...	It is too far reaching to require that the management body's duties and working procedures should be required in writing	writing	should also be clearly stated in written documentation that the management body in the subsidiary is responsible for the appropriate implementation of the strategies and policies set by the parent institution (including.....) within the subsidiary consistent with their own local obligations
	IG 6		
	In order to reduce the level of detail in the IG guidelines one respondent proposed to replace IG1-10 by IG6. IG 6 is considered sufficiently high level	CEBS considers that this change is not appropriate	
	IG 8		
	Proportionality should be addressed in this IG	Proportionality is addressed in the key considerations chapter. No specific mention is necessary in this case	
	IG 9		
IG9 a).....regarding both internal and regulatory capital are both.... Documentation should.....types of regulatory capital may be used. Furthermore, the distribution of	Principle IG9 refers to "own fund" in the title and to "regulatory capital in the following text. These terms should be used consistently throughout the document. The term "on-going basis" should be clarified to avoid misinterpretation. It is too hash to require an institution to allocate capital over and above of the legal requirements for a	Proposed changes: replace the word regulatory capital by own funds.. Delete "capital should be allocated where the risks are" (paragraph a)	IG9 a).....regarding both internal capital and own funds are both.... Documentation should.....types of own funds may be used (primary and supplementary capital) Furthermore, the distribution of own funds

<p>regulatory capital within a groupallocation of capital to subsidiaries (i.e capital should be allocated where the risks are)</p> <p>b).....purposes, but here too the supervisor will expect the institution to allocate capital where the risks are.</p>	<p>subsidiary of a group. An institution must be free to allocate capital where there are business opportunities, once they have met the legal capital requirements</p>	<p>Delete "but here too the supervisor will expect the institution to allocate capital where the risks are." (in paragraph b)</p> <p>-"on going basis" is the wording used by the CRD.</p>	<p>within a groupallocation of capital to subsidiaries</p> <p>b).....purposes.</p>
	<p>IG 11</p>		
<p>IG 11 a).....This is particularly important when there may be conflicts of interest with other stakeholders, or within a group</p>	<p>There is a conflict between the content of IG11 and the Commission Recommendation 2005/162/EC on the role of non-executive directors or supervisory directors.</p> <p>It was questioned whether it makes any sense at all to apply the internal governance standards to non-executive members of the management body. Their tasks are definitely different from those of the executive directors.</p> <p>Delete the last sentence in paragraph a</p>	<p>CEBS does not see that there is a conflict between the two. On the contrary we think that they are more or less in line with each other.</p> <p>Delete the last sentence in paragraph a</p>	
	<p>The management body of a subsidiary will not (and should not) be completely independent from the directions given by the management body of the parent institution.</p>	<p>CEBS has added a sentence to this effect.</p>	<p>11.c While it is acknowledge that the management body(..) of a subsidiary is also expected to observe and implement the business objectives, risk profile</p>

			and policies defined by the management body(..) of the parent institution, this has to be consistent with their own local obligations (including....).
	IG 12		
IG 12 The management body should have policies for selecting compensating monitoring and planning the succession of Key executives	<p>Respondents asked CEBS to delete this principle; It would be problematic when it comes to selecting senior executives where considerations going beyond the purely objective. Furthermore, IG12 has been introduced without any reference to the CRD.</p> <p>Such standards should not be required for smaller banks at all</p>	<p>CEBS believes that this principle is rooted in CRD (article 22).</p> <p>Furthermore it is fully consistent with the Basel document on corporate governance and Basel guidance relative to internal control (1998)</p> <p>CEBS believes that all firms should have a properly documented approach for senior executive remuneration and succession planning.</p>	N/R
	IG 13		
IG13 The management body should promote high ethical and professional standards and internal control culture	<p>Respondents asked CEBS to delete this principle because it was introduced without any reference to the CRD.</p>	<p>CEBS believes that this principle is rooted in CRD (article 22)</p>	N/R
	IG 14		
	<p>Respondents argued that IG14 was too prescriptive and it confused organization with governance.</p>	<p>CEBS has introduced some amendments to address these</p>	<p>Istitutions should establish, making adequate allowance for</p>

	<p>Proportionality should be addressed in this IG</p>	<p>comments.</p> <p>Although the proportionality concept applies to all guidelines as it is states in the key consideration section, the IG 14 heading has been amended and a new paragraph introduced to reinforce it in this case.</p>	<p>the principle of proportionality,.....</p> <p>b.....The control function is organisationally separate from the activities it is assigned to monitor..... The head of the control function to a person who has no responsibilities for managing the activities....”</p> <p>IG14 c. These internal control functions (i.e. risk control, compliance and internal audit) should.....</p> <p>Furthermore, it is the responsibility of the management body to ensure that the risk control function, the compliance function and the internal audit function all have sufficient resources (well-qualified and experienced staff, as well as a sufficient number of staff) at their disposal</p> <p>d) It may not practical for smaller institutions to meetmitigated.</p>
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IG 15			
<p>IG 15 a).....Control activities should be defined at every business level.</p> <p>b)...In large....should be established to monitor each of the material risks (in material business) to which.....Senior management should</p>	<p>It is going too far to require control activities at every business level.</p> <p>IG 15 refers to 'material risks' (in material business lines) but provides no indication as to whether 'control risks' are included under this term.</p>	<p>Proposed changes:</p> <p>Delete "at every business level" and "in material business"</p>	<p>"Control activities should be defined at the appropriate level."</p> <p>"In large....should be established to monitor each of the material risks to which.....The management function should continuously...."</p>
IG 16			
<p>IG 16. The compliance function should identify and assess compliance risks</p>	<p>Respondents expressed the following concerns:</p> <ul style="list-style-type: none"> -The definition of the compliance was much larger than what is generally accepted in most European countries. The tasks of the compliance function should be limited to the possible. -there might not be such a clear distinction between risk control and compliance. -Rather than doing the reporting themselves, the compliance function should have in place processes to ensure deviations get reported -Remove the words "fully" " and future' from principle 16 c) 	<p>CEBS has rewritten the text in order to be line with the final version of the BCBS document on compliance.</p>	<p>See new IG16 text in the guidelines</p>

	IG 17		
	<p>Some respondents considered this principle over prescriptive and proposed to change the wording.</p> <p>Audit recommendations should be followed up by management, but an equal obligation is warranted for Risk and Compliance recommendations.</p> <p>The final sentence of IG 17b is redundant and should therefore be deleted</p>	<p>CEBS shares industry points.</p> <p>Proposed changes:</p> <ul style="list-style-type: none"> -new paragraph (IG17a) -In IG 17 b the wording where this is a different function and the final sentence have been deleted 	<p>New IG 17 a The management body(...)is responsible for establishing the internal control framework in compliance with regulatory requirements. The internal audit function is responsible for the assessment of the adequacy of internal controls and should report its findings to the management body (...)"</p>
	IG 18		
	<p>One respondent believed that the bank itself should have had the possibility to define the term "significant" in more detail</p>		N/R
	IG 19		
	<p>Some respondents noted that IG 19 about an internal alert process is not based on the CRD and It should be deleted.</p> <p>One respondent stressed that IG19 should also be applied to a firm's internal capital adequacy assessment process (ICAAP).</p>	<p>CEBS believes that this principle is rooted in CRD (article 22).</p>	N/R
	IG 20		
IG 20: Institutions should aim for the highest standards of	<p>Some respondents noted that IG 20 about disclosure and transparency is not based on the CRD and</p>	<p>CEBS believes that this principle is rooted in CRD (article 22).</p>	<p>IG 20: Institutions should meet the generally agreed transparent</p>

<p>transparency in the conduct of their business.</p> <p>a. Institutions should consider public disclosure going beyond regulatory requirements as a way of reinforcing their internal governance.</p>	<p>redundant. Therefore they should be deleted.</p> <p>Others considered that this guideline should be much shorter and not so far reaching. Any form of disclosure to the outside world on the outcome of the supervisory review or any concrete prudential measures taken by a supervisor is undesirable.</p>	<p>Proposed changes:</p> <p>The headline has been amended in line with the industry request</p> <p>The first sentence has also been deleted</p>	<p>requirements in the conduct of their business</p>
	<p>IG 21</p>		
<p>IG 21 c).... Including, in particular, the content of any corporate governance code or policy and the process by which it is implemented.</p>	<p>Some respondents noted that IG 21 about disclosure and transparency is not based on the CRD and It should be deleted.</p> <p>Others stressed that this guidelines went to far and should be reduced</p>	<p>CEBS believes that this principle is rooted in CRD (article 22).</p> <p>IG 21 c. Last sentence has been deleted</p>	<p>N/R</p>
	<p>ICAAP general</p>		
	<p>The figures of the Pillar 2 adequate capital and the internal economic capital could be identical. So long that the bank is "ongoing" and that the two first principles are applied, no supervisory add-on or floors will jeopardise the equivalence of the figures of economic capital and P2 adequate capital.</p> <p>Centrally managed and centrally calculated economic capital, which integrates the diversification, should be</p>	<p>Economic capital and own funds serve two different purposes. Institutions are likely to conduct their ICAAP with reference to internal capital. Supervisors will review this as part of the SREP, in order to reach a view of the adequacy of own funds. Institutions should be able to explain how the ICAAP outcome relates to regulatory capital requirements (as</p>	

	<p>allowed. No local calculation will be required.</p> <p>“apportion” the consolidated economic capital to the legal entities following their “own” top-down risk-sensitive system of allocation should be allowed.</p> <p>Risk-mitigating effects not yet recognised by supervisors under Pillar 1 (for instance diversification) could result in capital relief which may be offset against additional risks under Pillar 2.</p> <p>Additional guidance from the supervisors could also prove useful in connection with the treatment of some risks within the ICAAP</p>	<p>per ICAAP 10),</p> <p>What institutions do for their internal purposes is for them to decide., but the supervisor may require additional calculations. Supervisors do not dictate the ICAAP, but institutions should be able to defend the calculations.</p> <p>See forthcoming papers on concentration risk, interest rate risk in the banking book...</p>	
	ICAAP 3		
<p>ICCAP 3 b.</p> <p>ICAAP 3 c.</p>	<p>Flexible allocation of responsibilities would make it possible to comply with the different frameworks set by member states’ national legal regimes.</p> <p>Full documentation of the capital policy is too extensive. Adequate documentation should be sufficient.</p>	<p>CEBS considers that IT and other systems need to be fully and formally documented.</p>	
	ICAAP 4		
	<p>An ICAAP for a subsidiary entity will likely be a completely separate process designed primarily to meet local governance and regulatory requirements. Often, at the level of an individual subsidiary capital is driven not by the risks inherent in the business conducted by the entity but rather by the need to hold capital at a particular level so as not to breach regulator-imposed exposure limits, particularly in respect of intra-group transactions.</p>	<p>Supervisors must strike a reasonable balance given that solo entities are required to meet their minimum standards.</p> <p>Further, there is the cross-border question, where host supervisors have to meet their local responsibilities for subsidiaries but within the context of the parent group through the</p>	

		home/host relationship.	
	<p>This principle should be clarified to stress that the ICAAP in more complex institutions will largely be built on the institution's existing practices and structures, which are already designed to cope with a complex risk environment.</p> <p>The requirement in paragraph a) "institutions should completely integrate the ICAAP into their management processes" is not appropriate and is too far-reaching, particularly in view of the fact that supervisors use regulatory capital as a basis.</p> <p>The term "on-going basis" in paragraph b could lead to misunderstandings. It would be preferable to use the expression "as often as is deemed necessary".</p>		4 a. The ICAAP should form an integral part of Institution's management processes so as to enable the management body (...) to assess, on an going basis, the risks that are inherent in their activities and material to the institutions...
	it is debatable whether ICAAP should be used in "the individual credit decision process".	Up to institution to decide, but the ICAAP should reflect the reality of the institution's risk management processes.	
	ICAAP 5		
5. aThis review should take place at least annually	Clarify that a review once a year as part of the annual audit satisfies the requirement for regular review of the ICAAP by the institution.	The institution's management should review and the audit checks it independently	N/R
5.b The ICAAP and its review process should be subject to independent internal review	<p>This requirement is already covered by the internal governance principles. It should e deleted</p> <p>Clarify that the institution may also arrange for an independent external agency to carry out the review process.</p>		
	ICAAP 6		

6. a... Institutions should set capital targets which are consistent with their risk profile and operating environment	Risk appetite should be included as a forward-looking element.		
	It is not realistic, nor would it be efficient, to expect that subsidiaries be capitalized on the basis of ICAAP measures as if they were freestanding banks. ICAAP6 should be made clearer on this point.	Already commented	
6. d. Less sophisticated institutions that take a Pillar 1 approach as the starting point for the ICAAP should also begin to develop a fully risk-based approach.....	This paragraph requires clarification as it may not be correctly interpreted. Can supervisors impose an advanced approach for an ICAAP under Pillar II at some point? what is meant by a "fully risk based approach".	The intention is to encourage institutions to continue to develop and enhance their risk management processes, but not to impose advanced ICAAP approaches on banks that do not have the capability to use them.	6.e Institutions that take a Pillar 1 approach as the starting point for the ICAAP may also consider developing a fully risk based approach.....
ICAAP 7			
7b.Risks not fully captured under Pillar 1.	As a result of recent amendments stressed LGDs are entirely included in the first pillar and they should be removed from Pillar 2. The wording may lead the reader to interpret its meaning to be that simpler approaches are not acceptable for use in the ICAAP. This would appear to contradict the principle of proportionality.	No change needed (see Basel text Guidance on paragraph 468 of the framework)	See ICAAP 7 in the guidelines
7b. Pillar 2 risks.	As well as having to take into account concentration risks in their ICAAP, institutions should also be able to factor in diversification effects if they can soundly justify the reasons for doing so and methodologies used. The exclusion of diversification effects will lead	Institutions are free to develop their own internal approaches. From the supervisory perspective, the approach to diversification is currently under consideration, although this presents	

	<p>to unnecessarily high capital levels.</p> <p>A number of Pillar 2 risk types that are mentioned in the text such as reputation risk or settlement risk are not really Pillar 2 risk types. Due to their nature cannot be covered by regulatory capital and should be deleted from the document</p> <p>Settlement risk is already included in Pillar 1 (unsettled and failed transactions)</p>	<p>some difficulties given that Pillar 1, which does allow for diversification, has already been calibrated on a well-diversified internationally-active bank</p> <p>Actually as CEBS acknowledges not all risks are best mitigated by capital.</p> <p>Settlement risk has been deleted</p>	
7b Risk factors external to the institution	<p>Quite apart from the fact that the text gives no indication of exactly what kind of risks are meant here, this goes far beyond what is required under the new CRD. This bullet point should therefore be deleted.</p>	<p>The directive requires institutions to consider in their ICAAP "the risks to which they are or might not be exposed" – it does not exclude external risks. Furthermore, external risks are mentioned in the Basel documents.</p>	
	<p>For those risks which are more qualitative in nature there are no assessment criteria which can be regarded as market standards. Information about the expectations of the supervisors would be useful for market participants.</p>		
	ICAAP 8		
	<p>The requirements of ICAAP 8 regarding a detailed capital plan for a longer time horizon and with regard to stress-testing are too demanding for smaller banks.</p>	<p>The principle of proportionality should be applied here. However institutions should consider their future needs and stress scenarios.</p>	N/R
8b the plan should also lay out how the institutions will comply capital requirements in the	<p>This requirement is excessively demanding and no needed</p>	<p>Banks need to consider how their capital needs will evolve over the coming years, and will need to make sure that they have sufficient capital to avoid breaching regulatory requirements. The level of detailed</p>	

future....		should be proportionate	
8c.Institutions should conduct appropriate stress tests which.....	<p>It should be made clear in the text that stress test results should not generally lead to additional regulatory capital, especially given that Pillar 1 is already stressed.</p> <p>The discussion of stress testing now contained in CP3 revised could lead to inappropriate supervisory use of stress test results, perhaps penalizing good risk management in the broader sense.</p>	If the stress test results are already factored adequately into Pillar 1 then the outcome in Pillar 2 should be correspondingly less. They should not double-count for the same thing. However, Pillar 2 stresses cover more than just Pillar 1 and take a holistic view of the capital plan through a cycle.	
	ICAAP 9		
9d.....Supervisors would expect the institution to demonstrate that it had analysed all risks outside Pillar 1 and found them to be absent, not material, or covered by a simple cushion over the Pillar 1 minimum	the option of adding a cushion over the Pillar 1 minimum is just one option at the disposal of the smaller institutions, as opposed to a choice for the supervisor, a systematic application of this approach would not be in line with the spirit of Pillar 2.	institutions are required to operate above the Pillar 1 minimum, and they need to ensure that they do not risk breaching this minimum. Whether this is set by supervisors or by institutions depends on each country.	N/R
9f....Institutions not rely on quantitative methods alone to assess their capital adequacy but include an element of qualitative assessment.	Against this background, the example of a "building block" approach given in paragraph d could be misleading and in contradiction to the core idea of Pillar 2, to deliver a broader understanding of banks' risks.	CEBS has included some changes to reinforce the balance required between quantitative and qualitative measures.	
	ICAAP 10		

	Firms do not seek guidance from regulators on the relationship between own funds and internal capital. Firms are not comfortable with the "building block" approach that is advocated. Furthermore, it is not apparent to firms that "benchmarking" between firms in the field of their models for internal capital is realistic, feasible or appropriate.	Institutions will define their internal capital and will discuss this with their supervisors.	N/R
10a The ICAAP should produce a reasonable overall capital number and assessment	Many institutions, especially smaller ones, are not currently in a position to calculate a single capital number. This is not made sufficiently clear by the term "a reasonable capital number".	According to article 123 it is a legal obligation. Smaller institutions are not expected to conduct complex aggregations.	
10b Institutions might be encouraged to make greater disclosures of information which is not proprietary or confidential.	If an institution chooses not to disclose additional information above the amount that is strictly required, there should be no negative Pillar II consequence for this institution.	Agree	
Guidelines for supervisory authorities			
	For larger, more complex institutions, SREP's function mainly lies in the assessment and review of institutions' ICAAPs rather than in supervisors' own assessment of institutions' risk profile.	The SREP will focus on the ICAAP and to this extent the dialogue is key. However supervisors have the responsibility to perform their own assessments of the institution's risk profile. The extent to which they will rely on the institution's ICAAP as an input to their assessment will depend on the quality of that ICAAP and the processes surrounding it.	

	Supervisors should be committed to explore the use of other measures available to them before taking recourse to capital add-ons. By applying add-ons, supervisors would essentially be treating the potential disease rather than the early symptoms.	Already commented	
	Support CEBS' commitment to achieve convergence of supervisory practices.	CEBS is committed to this	
	Clarification for the term significant (SREP3, SREP9, SREP10)		
	SREP 4		
4b. The evaluation of control.....and internal audit and compliance functions.	In the interest of completeness and consistency, the risk function should be subject to the same audit.		
	SREP 7		
	This seems to be an extremely broad brief and one that would be difficult to achieve in the context of a supervisory review.		
7. This process will enable supervisory authority.....and provide incentives for institutions to improve their risk management systems'.	How supervisors will do it should be clarified	The intention is to encourage institutions to improve their risk management systems.	7. This process will enable supervisory authority.....and encourage institutions to improve their risk management systems'.
	SREP 8		

8...For example where there is an imbalance between business and control risks, the supervisor...	This sentence does not seem to make sense. Perhaps 'imbalance between business and risk controls' was intended.	Agree	
	RAS 1		
	Under principle RAS 1 CEBS should not only include risks and controls, but also mitigants.		N/R
1a.Supervisory authorities should have individual ratings for risks and controls	This should be made less stringent; a scoring procedure should be permitted if necessary. The guideline should avoid using the expression "rating" since the CRD uses this term in a different context.		N/R
	Is it envisaged that regulators would share the risk ranking with the institution?		N/R
1d. It may be useful to set a default score or rating.	Default ratings would not be a useful concept. Ratings should always reflect reality.		N/R
	RAS 2		
	In RAS2, the list of control functions is different from the one given in IG14.		N/R
	when dealing with "groups and major institutions" versus "smaller institutions" one should try to avoid effects on competition.		N/R
	RAS 3		

	The texts for RAS3 and RAS4 seem to have been exchanged.		N/R
	THE SREP-ICAAP INTERACTION AND PRUDENTIAL MEASURES		
	Does the output of the ICAAP once agreed with the regulator, constitute the regulatory capital?	Not necessarily, although in some countries/cases this approach may be taken, if the outcome is above pillar one.	N/R
Diagram 1 page 8	The upper part of the diagram should be identified as the application of the two SRP first principles and the lower part as the application of principle 4.		See diagram 1
	Overall respondents welcomed the additional importance laid on the dialogue between institutions and supervisors. However, some respondents suggested that the overall 'tone' of the guidelines had moved from high level principles to a rigid supervisory checklist which could weaken the quality of the dialogue and lead to a generally additive approach to capital.	The guidelines have been amended to better reflect the notion that capital is not the only corrective measure and to stress the pragmatic, flexible and qualitative approach that EU supervisors will take to Pillar 2. some wording changes have also been included throughout the paper to avoid the wrong perception of prescriptiveness and to achieve a more balanced approach.	
	DIALOGUE 2		
2. the structure of the dialogue should be based on a 'building block approach'	Many respondents did not support the "building block" analysis and noted that a prescriptive set of risk buckets within Pillar 2 was inappropriate and will not drive consistency. A more fluid concept such as "streams" of risks was necessary to discourage any tendency towards a purely additive approach to capital.	CEBS has included a new paragraph and amendments to diagram 2 to address these concerns.	2c. It is important to stress that these elements should not be interpreted as resulting in automatic capital additions. Supervisors will apply judgment when considering the relationship between

The "building block approach" will result in

- (a) an inflexible categorization of risks,
- (b) cumulative aggregation and
- (c) too great a focus on the individual "blocks", thus losing sight of the "big picture".

The building blocks are concentrated solely on business risk and make no mention of control risks and the control risk function. (The connection between diagram 2 and diagram 1 should be specified). We ask for further clarity on the type of controls to be recognized under the building block approach.

qualitative and quantitative components, making due allowance for qualitative measures which may be effective mitigants on their own or in combination with capital. Moreover, it is not a question of simply aggregating risks and the capital which may be attributed to them. There may be good reasons why the total amount of capital allocated may be less than the sum of the individual risk elements; however these would

need to be assessed within the context of an holistic approach which would have to be sufficiently robust

			<p>need to be assessed within the context of an holistic approach which would have to be sufficiently robust</p>
	<p>Reputation risk and settlement risk are not really Pillar 2 risk types. Due to their nature cannot be covered by regulatory capital.</p> <p>Securitisation risk is basically a Pillar 1 issue.</p> <p>External factors should be deleted</p> <p>it would probably be useful if supervisors would define the major parameters of the scenarios for stress tests under Pillar 2 thereby avoiding that entities come to asymmetric results</p>	<p>Already commented (see ICAAP 7)</p> <p>Stress-tests will be based on institution-specific scenarios, which clearly cannot be defined by the supervisor</p>	
	<p>A clear line should be drawn between the risks</p>		

	affecting the institution's solvency, which capital may be, at least partially, an answer for, and the risks impacting the shareholders' value, which are clearly beyond capital adequacy issues.		
	In Dialog2, on the diagram, legal and compliance risk are not included into operational risk, which is not consistent with the generally accepted definition of operational risk given in page 40.	Amend to reputation and strategic risk	See diagram 2
	Many respondents noted that beyond the basic risk types -credit, market and operational- any risk taxonomy was hazardous and requests, at least, a thorough consultation, which has not taken place. Banks urged CEBS not to act hastily on this very difficult matter; they would not like to divert scarce resources that are currently focused on building a reliable and timely Pillar 1 capital requirements reporting.	Reflects the Basel documentation	
	Mitigation factors should be mentioned under principle Dialogue 2.		
	In the case of banks reporting according to IFRS, provisioning is not a supervisory outcome or prudential measure anymore	The possibility to require institutions to apply a specific provisioning policy is set out in Article 136 of the CRD	
	This block description should be included in the ICAAP guidelines. The diagram does not mention regulatory capital and a final outcome.	Disagree.	
	DIALOGUE 3		
	This process should be two way, with the firm expecting to have to explain its rationale, and outcome of its own process to the regulator and the regulator to expect that the firm might challenge the regulatory interpretation and stand ready to justify	Dialogue aims at challenging the institution and its assumptions.	

	the approach that has been taken.		
	DIALOGUE 4		
	More detail is required on how peer groups are to be determined by national regulators and how such a subjective question is to be considered in a pan European context	How the dialogue will be performed in practice and the role and the determination of peer group should emerge as implementation plans develop. This said, supervisors are conscious of the need to be flexible in their approaches so as to avoid being overly-prescriptive.	See dialogue 4
	MEASURES 1		
	<p>-Capital is not the only answer: regulators should focus on risk management and mitigation processes, rather than setting ever higher capital levels</p> <p>-The first bullet point in paragraph b should be placed at the end of the list of available measures to underscore the statement made at the beginning of the paper that capital add-ons are to be considered a means of last resort.</p> <p>-The economic capital of « Advanced » institutions will be above the Pillar 1 minimum required capital, not because it is a regulatory requirement, but because Pillar 2 covers all risks and aims at a higher protection</p> <p>It is important to explicitly state that it is possible for the result of the SRP, and Pillar 2 in its entirety, to be zero.</p> <p>The links between measures and outputs of the SREP and RAS should be explicitly addressed.</p>	Already discussed.	

	There should be no explicit or implicit assumption that Pillar 2 requires capital in Tier 1 form.		
	CP03 Revised should include a chapter explaining the link between Pillar 1 minimum required capital, Pillar 2 adequate capital and own funds. Institutions should explain the consistent application of those three capital approaches. They will not have to reconcile the final figures.		
	Regulators must take account the consequence of requiring a firm to hold additional capital when exercising their powers in this field – including the costs that must be borne by the firm in raising additional capital.		