



FEDERATION
BANCAIRE
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*Banking supervision
And Accounting issues Unit*

The Director

Paris, June 24th 2013

FBF Response - EBA Consultation Paper on Draft Implementing Technical Standards on Asset Encumbrance Reporting under article 95a of the draft Capital Requirements Regulation (CRR).

Dear Madam,

The French Banking Federation (FBF) is the professional body representing over 450 commercial, cooperative and mutual banks operating in France. It includes both French and foreign-based organizations.

The FBF is pleased to take this opportunity to comment on the proposed ITS on Asset Encumbrance. The FBF appreciates the EBA's efforts to determine a harmonized European framework for reporting and determining the level of asset encumbrance, in line with the recommendations of ESRB issued in December 2012. This will help ensure consistency at supervisors and possibly other stakeholders' level when assessing the asset encumbrance of financial institutions.

Moreover, we recognize that the quality of the work already accomplished on the proposed reporting framework is sufficient to enable a good assessment of the asset encumbrance situation of the different institutions.

However, we would like to draw the EBA's attention on the following **high-level points regarding this draft ITS**.

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Objective of the reporting on asset encumbrance

We fully recognize the usefulness of reporting on asset encumbrance in order to assess banks reliance on secured funding and the degree of structural subordination of unsecured creditors and depositors. However we consider that the second objective (assess the ability to handle funding stress) is already covered by the other liquidity reporting LCR, NSFR or Additional Monitoring tools. Notably, some tables (B, C and D) are indeed redundant with the liquidity ITS. We recommend the EBA to remove these tables from the Asset Encumbrance reporting and focus on the first objective.

Complexity of the reporting

The granularity of the reporting templates is such that their production will be highly complex and hard to achieve. It will generate significant costs in terms of both implementation of the required IT systems and on-going production.

Indeed, producing these reporting represents a significant challenge:

- One of the most difficult points in the reporting framework proposed by the EBA is the necessity to cross information that is currently lodged in different information systems in banks (accounting on the one hand, management data on the other hand) or that is currently not linked within the information systems of the banks. For example, the link to make between encumbered assets and the corresponding liabilities may prove burdensome and costly to implement. It will be a challenge to collect all these data resulting from different IT tools. It will already be a challenge to cross accounting and management data on macro aggregates and ensure consistency at that level. Requiring a deeper level of details to carry through both systems is clearly not feasible and will drive to implement counterproductive shortcuts which will not make sense. Hence we urge the EBA to limit the level of detail requested in the different tables.
- Another challenge is the need to consolidate the data on asset encumbrance, which can be rather complicated, depending on the structure and the relationship between the different entities of a Group.
- The on-going production of these reporting on a recurrent basis will require additional staff to ensure the accuracy of the reported figures both at local level and Head Office level, what will induce additional costs for banks and Financial Institutions overall.

As mentioned in the consultation paper, one of the aims of the EBA is to propose reporting which implementation cost is proportional to the added value of the collected information. We consider that as-is, the reporting framework is overly complex and does not reach this goal. A simplification of the reporting framework could be done without damaging the ability of the stakeholders to appreciate the situation of the institutions as far as asset encumbrance is concerned. Detailed comments on this subject are provided below.

Date of the first reporting

We do not find in the consultation paper any input concerning the date of 1st reporting for asset encumbrance. Meanwhile, we observe that the implementation date for the CRD-CRR will most probably be the 1st July 2014. Should this implementation date be retained, the banks will only have a few months to develop and to test the required IT systems. **This is not feasible.**

As a general rule and based on past experiences, in order for banks to put in place that kind of reporting with good quality, a minimum of eighteen months should be given between the final version of the templates and the date of first production.

Perimeter - level of production to define

The perimeter of application of the reporting on asset encumbrance is not clearly stated in the consultation paper.

We understand that the reporting will have to be supplied both on an individual and consolidated basis. However, we draw the attention of the EBA on several aspects that are important as far as perimeter is concerned:

- It makes more sense to consider entities which are globally integrated into the prudential consolidation perimeter rather than entities which are accounted for by the equity method which should be excluded from the consolidation perimeter.
- Depending on how the groups are constituted, it makes more sense to report only a consolidated level. This is especially the case for cooperative banks, where the relationships between the central institution and the local banks can be rather complex, including as far as asset encumbrance is concerned. However, the rules concerning this issue are not clearly stated and we do not know under which conditions a waiver on asset encumbrance reporting could be granted.
- However, it does not make much sense to produce the reporting specific to covered bonds on a consolidated basis (Part D); the risk taken on covered bonds is a risk that should be appreciated for each vehicle separately, which should already be the case in the NSFR.
- On the general principle of a due reporting on an individual and consolidated basis, and regardless of the threshold which will be eventually retained, we have also the following remarks:
- Stand-alone basis: only entities which are currently subject to COREP will be required to submit EBA reports on asset encumbrance.
- Consolidated basis: we would appreciate the EBA sets up some objective criteria to exempt or/and to lighten some local entities in the production of these reporting aimed at feeding the reporting at the consolidated basis.

Accounting values – IFRS or local GAAP

A lot of accounting values must be supplied for the reporting on asset encumbrance. However, it is not clearly stated which accounting values can be used, when local GAAP are used to produce the individual accounting, and IFRS are used to produce the consolidated figures. We consider that this issue should be left at the hand of institutions potentially mitigating the cost of implementation.

Investors' relations

It is worth noticing that asset encumbrance is an issue on which investors and stakeholders expect the institutions to disclose more public information. Asset encumbrance is one of the aspects the EDTF discussed in its paper on public disclosure published in October 2012, and on which it issued a specific recommendation. Meanwhile, we observe that the Basel Committee is also working on disclosure requirements as far as liquidity is concerned.

We think that these initiatives would benefit from a concerted coordination effort so as to limit the increase in reporting burden for the institutions.

Definition of the asset encumbrance ratio in Annex II

(Instructions - 1.6. Proportionality p.4).

We believe that the formula of the definition of the asset encumbrance ratio presented in the Instructions contains some mistakes, to be replaced by the row number highlighted in bold as specified below:

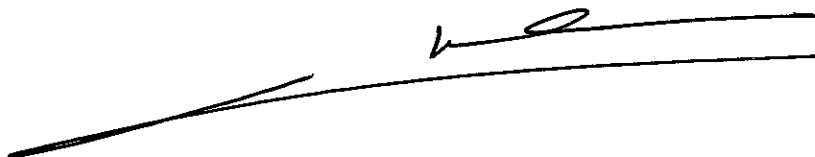
Carrying amount of encumbered assets = {AE-Assets; 010; 010} + {AE-Collateral; 130; 010}.

- Total assets = {AE-Assets;010;010} + {AE-Assets;010;060}+{AE-Collateral;**130**;010}+{AE-Collateral;**130**;040}.
- Asset encumbrance ratio = (Carrying amount of encumbered assets) / (Total assets)

You will find in the appendices specific remarks or questions on the different tools mentioned by the EBA and our answers to the questions raised in the Consultation Paper.

We thank you for your consideration of our remarks and remain at your disposal for any questions or additional information you might have.

Yours sincerely,



Jean-Paul Caudal

Appendix I: Specific remarks or questions on the different tools mentioned by the EBA.

Part A: Encumbrance overview

General remark: this part is, according to us, the most useful as far as asset encumbrance is concerned. It allows determining a ratio of asset encumbrance in a rather consistent manner.

However, as-is, it is excessively complex and should be simplified.

- **AE-Assets**

Even though this type of information will be needed for consolidation purposes, we do not see the need in this specific reporting to report the column "of which: issued by other entities of the group".

Beside we question the interest of the column "of which central bank's eligible" given that other liquidity reporting already provide information on the capability to pledge assets and obtain further liquidity (Refer notably to the Additional Monitoring Tools reporting on counterbalancing capacity). This kind of detail doesn't serve the objective on structural subordination. Similarly we question the interest of the lines "of which xxx" as examples of details which do not provide information on balance sheet subordination and are already provided in other liquidity reporting.

Furthermore, and in line with a comment made above, it would make sense to only report accounting values, and not also fair values at the exclusion of any other valuation metric without the loss of any precision, given the fact that most encumbered securities are likely to be accounted for at their fair value.

In avoidance of doubt, we believe as a general principle that the asset encumbrance disclosure reporting is much more a matter of liquidity than accounting, and therefore fair value makes sense for securities transactions and accounting values make sense for loans. One additional remark: row '070 of which: issued by general government': does it include public company and supranational securities, US GSE/GSA securities?

- **AE-Collateral**

Even though this type of information will be needed for consolidation purposes, we do not see the need in this specific reporting to report the column "of which: issued by other entities of the group".

We question the relevance of adding the column "of which central bank eligible" and the lines "of which xxx", that are redundant with other liquidity reporting (see above).

For the sake of simplification, we think that only one type of value should be reported in each row: either fair value or nominal. Fair value makes sense for securities, nominal for the other types of instruments (loans...).

- **AE-Not pledged. Own covered bond and ABS issued and not yet pledged**

The last column "Nominal of own debt securities issued not available for encumbrance" of the template does not seem to be useful; it doesn't bring any complementary information for the capacity of encumbrance.

The column "Carrying amount of the underlying pool of assets" has no interest since these assets are already reported in the template AE-Assets.

Regarding ABS, the split between “Senior”, “Mezzanine” and “First Loss” categories of the underlying pool of assets does not make sense since there is no clear split within the pledged pool of assets.

We also believe that there is not any need to distinguish specifically self-detained covered bonds and ABS and hence that the section AE-Not pledged should be folded back in the AE-Collateral section (should it be estimated necessary, the corresponding information could be isolated in a row of this last section).

- AE-Sources of encumbrance

There is presently only very limited information carried in the institutions accounting systems that connect a pledged asset to the liability requiring the pledging. Under the framework of the Asset Encumbrance reporting, we see no rationale to formalise such connection, notably as this part of the reporting will prove extremely difficult and very costly to implement. Hence, we propose to limit this section to the column “matching liabilities, contingent liabilities or securities lent”.

In the same vein, we see even less interest in reporting within the corresponding assets and collateral those which are collateral received and re-used and those which are own debt securities encumbered.

Even though this type of information will be needed for consolidation purposes, we do not see the need in this specific reporting to report the column “of which: issued by other entities of the group”.

It does not make sense to report information on the “% in market” of debt securities issued. Indeed, at the individual level, these debts should be reported. At the consolidated level, they are eliminated so that the reporting supplied based on accounting values provides already all the necessary information.

Other remark: What is the difference between the row ‘040 Deposits’ (which are implicitly ‘collateralized deposits’) and the row ‘070 Collateralized deposits other than repurchase agreements’?

Part B: Maturity data

The objective and added-value of this reporting is questionable and proves redundant with the information already supplied in the NSFR and additional monitoring tools framework such as it is.

Part C: Contingent encumbrance

The liquidity stress scenarios to assess contingent encumbrance have been defined by the CRR after a long period of discussion and have been voted. We are concerned that the EBA goes beyond its mandate when introducing new scenarios, which may prove inconsistent with the CRR. As a consequence we demand the EBA to stick with the already defined scenario and remove this template from the Asset Encumbrance reporting.

In addition, the projected reporting would be complex and prove highly difficult to automatize and make reliable without long and costly developments that may not even settle all exhaustiveness and reliability problems.

To illustrate the risk of inconsistency, we can highlight the scenario 1. We wonder what the basis is for the 30% decrease of the fair value of encumbered assets and what sense it makes for loans.

Part D: Covered Bonds

- AE-CB Issuance

The present value of the cover pool and of the covered bond liabilities may not be calculated and are not useful to assess the risk generated by the vehicle. Thus, we recommend suppressing these values from the reporting.

We have the same remark concerning the asset-specific value of the cover pool.

- AE-CB Eligible Assets

We draw the attention of the EBA that there is a specific perimeter problem on this particular template. Indeed, unencumbered assets eligible for cover pool may not be directly held by the covered bond issuing vehicle. Thus, considering this reporting in isolation with the previous one makes no sense.

In this part, we think only the nominal amount needs to be reported. Present value and Asset-specific value are not useful.

Part E: Advanced data

The difficulty outlined in our comment regarding the AE-Sources of encumbrance table applies in full to this section of the reporting. The complexity of establishing connections between the pledged assets and the corresponding liabilities will prove extremely difficult and very costly to implement. This is all the more true as this template requires even more details about the source of encumbrance and about the collateral type compared to the template in Part A.

Moreover, the added connections made by this reporting between the encumbered assets and the corresponding liabilities do not meaningfully enhance the information already reported in part A.

Accordingly, we think it should be removed from the reporting framework.

Appendix II: Answer to specific questions.

Q1: Is the definition of asset encumbrance sufficiently clear?

The definition of asset encumbrance given in the consultation paper is the following:

“For the purpose of this Regulation an asset is considered encumbered if it has been pledged or if it is subject to any form of arrangement to secure, collateralise or credit enhance any transaction from which it cannot be freely withdrawn”.

We consider this definition to be reasonably clear; we would however appreciate further clarification regarding some of its aspects.

First, we feel that the term “freely withdrawn” is open to interpretation and could gain from being illustrated with examples provided in the explanatory text. Indeed, it is not really clear how excess collateral must be treated in terms of encumbrance. This is especially important in the case of covered bonds: should the collateral in a covered bond cover pool in excess of the amount required to maintain a given rating be considered unencumbered? Should the excess amount above the required amount given the covered bond statutory regime be considered unencumbered? We think that it is worth mentioning under which conditions exactly the cover pool amount in excess of minimum coverage requirement can be considered encumbered or unencumbered, and how the minimum requirement should be calculated.

For the sake of clarity, we propose that the definition be amended the following way: “For the purpose of this Regulation an asset is considered encumbered if it has been pledged or if it is subject to any form of arrangement to secure, collateralize or credit enhance any transaction from which it cannot be freely withdrawn without requiring replacement or agreement by one or more of the transaction counterparties”.

Second, we think that the treatment of assets that are collateralized in pools that are not fully used should be clarified and reviewed. As a general rule, and consistently with rules currently being adopted in the LCR framework, we think that to determine the assets that are encumbered the same waterfall as for LCR, NSFR and additional monitoring tools should be defined. For example, in pools combining private claims and securities (such as the ones used to obtain central bank refinancing), private claims should be assumed to be encumbered first. It is our opinion that a waterfall model that would take into account asset classes and potential haircuts would be preferable than the pro-rata approach that is proposed. In addition, we believe that the pro-rata approach is contradictory to the encumbrance sequence as requested by the NSFR, which is based on the RSF rate, from the highest to the lowest rate.

Third, should a pro-rata approach be applied, it is not really clear how to calculate it. If the collateral provided contains several asset classes (for instance securities and loans) where there is no common measure of the value of the collateral, should the reference measure always be the accounting carrying amount of the collateral? If varying haircuts apply depending on the nature of the collateral, should those haircuts be considered in the pro-rata allocation of encumbrance? An example would help institutions and ensure a common understanding of the framework.

Furthermore, we have one remark in the wording of the definition itself on p.9 of the Consultation Paper: we are questioning the relevance of ‘**reverse repurchase**’ in the definition of asset encumbrance, insofar as a security received through a reverse repurchase transaction is not encumbered.

Q2: Do you agree with the decision to follow the level of application as set out for prudential requirements? If not, what other level of application would be appropriate?

The perimeter of application of the reporting on asset encumbrance could be more clearly stated in the consultation paper.

We understand that the reporting will have to be supplied both on an individual and consolidated basis. However, we draw the attention of the EBA on several aspects that are important as far as perimeter is concerned:

- It makes more sense to consider entities which are globally integrated into the prudential consolidation perimeter rather than entities which are accounted for by equity method which should be excluded from the consolidation perimeter.
- Depending on how the groups are constituted, it makes more sense to report only a consolidated level. This is especially the case for cooperative banks, where the relationships between the central institution and the local banks can be rather complex, including as far as asset encumbrance is concerned. However, the rules concerning this issue are not clearly stated and we do not know under which conditions a waiver on asset encumbrance reporting could be granted.
- However, it does not make much sense to produce the reporting specific to covered bonds on a consolidated basis (Part D); the risk taken on covered bonds is a risk that should be appreciated for each vehicle separately, which should already be the case in the NSFR.

The rationale for reporting only on a consolidated basis is based on the complexity and the diversity of funding business models among European banking groups. For instance, assets pledged to the cover pool of a covered bond can be pledged from one entity to another inside the same banking group before finally guaranteeing the covered bonds issued by a specialised subsidiary. Another example would be the case where securities from securitisation structures are issued by one entity but detained by another entity of the same group. Without being exhaustive with these examples, if these entities were to exceed the reporting thresholds outlined in Article XX (page 10 of the Consultation Paper), they would end up reporting a distorted level of asset encumbrance that would reflect neither the entity health, nor its ability to shift to secure funding in case of stress. The individual reporting would not either help assess the banking group level of encumbrance or the secured part of its funding model.

Q3: Do you believe the chosen definition of asset encumbrance ratio is appropriate? If not, would you prefer a measure that is based solely on on-balance sheet activities (collateral received and re-used, for instance from derivatives transactions would not be included) or a liability?

We believe that globally, the chosen definition is indeed appropriate (including off-balance sheet and not based on liabilities).

We also share the EBA opinion that this ratio should only be used to define a reporting threshold given the unfeasibility of establishing an individual optimal level of asset encumbrance if national, market and business model specificities have to be taken into account.

We suppose however that the ratio formula page 4 of annex II –Reporting on Asset Encumbrance- is not well specified: we believe that {AE-Collateral;130;010}+{AE-Collateral;130;040} should replace {AE-Collateral;010;010}+{AE-Collateral;010;040} in the Total assets formula to be consistent with the definition reported on page 11 of the Consultation Paper.

Q4: Do you agree with the thresholds of respectively 30 bn. € in total assets or material asset encumbrance as defined as 5% of on- and off-balance sheet assets encumbered? If not, why are the levels not appropriate and what would be an appropriate level? Should additional proportionality criteria be introduced for the smallest institutions?

The principle of threshold based on total assets and % of on and off balance sheet seems consistent to us. However, we think that the conditions should not be cumulative: institutions fulfilling one of the conditions should be granted the waiver.

Furthermore, we think the waiver should concern Part A and Part D as well as Part B, C and E, as it does not make sense to report on asset encumbrance for very small institutions or institutions that do not encumber their assets. Another choice would lead to a very important number of non-significant reportings to be produced, making it likely that they are never exploited and lowering the visibility of the important reportings.

Also, we think that like other thresholds in the prudential regulation (such as the one million threshold applying to define the retail exposure class in solvability and in liquidity), they should be reviewed on a regular basis to adjust for inflation or other developments.

Finally, consistently with one of the comment made in the part dedicated to general comments, we think that the reporting on asset encumbrance is sometimes likely to make more sense on a consolidated basis depending on the organization of the groups.

Q5: Under what circumstances might unencumbered assets of the types of loans on demand, equity instruments, debt securities and loans and advances other than loans on demand not be available for encumbrance?

Given the diversity of European regulations and private contractual terms resulting in encumbrance according to the definition specified in this Consultation Paper we believe that the answer to that question would be highly specific not only to a given jurisdiction but also to the business model of each institution and would not help to assess in a better way the appreciation of a given institution to shift to secured funding under stress. We reiterate our recommendations not to disclose the liquidity of the assets because it is not part of the asset encumbrance objective. However, if it was to be maintained, the central bank eligibility would be easier to implement;

Q6: What additional sources of material asset encumbrance beyond the one listed in rows 20 to 110 and 130 to 150 in template AE-Source do you see?

No additional sources have been detected.

Q7: Do you believe the central bank repo eligibility criteria is an appropriate marketability criteria or should other criteria, such as risk weights, be used? If other criteria should be used, what could be the alternative?

As stated before, if the objective is to assess access to secured funding under stress, then already requested liquidity reporting (LCR, NSFR and Additional monitoring tools) are more accurate. Otherwise, to capture structural balance sheet subordination this criterion is not appropriate and will just create a bias any way.

Nevertheless, the central bank repo eligibility criterion is a good marketability criterion given its objectivity and the relative ease with which it can be appreciated. However, it should be extended to all central banks, not only the local Central Bank. Indeed, the aim is to identify the securities that are marketable and not those which are pledgeable at the local central bank.

Q8: Do you believe the chosen scenarios are appropriately defined? What alternative definitions would you apply?

The liquidity stress scenarios to assess contingent encumbrance have been defined by the CRR after a long period of discussion and have been voted. We are concerned that EBA goes beyond its mandate when introducing new scenarios, which may prove inconsistent with the CRR. As a consequence we demand EBA to stick with the already defined scenario and remove this template from the Asset Encumbrance reporting. Moreover, the percentage chosen (30% decrease in value) is extreme and doesn't make sense for loans

Q9: Does the instructions provide a clear description of the reporting framework? If not, which parts should be clarified?

The instructions are generally clear. However, the objectives presented in the consultation paper are an extensive interpretation of article 95 of the CRR and overlap objective pursued by other liquidity reporting. Thus some of the required tables are redundant with liquidity reporting and sometimes in contradiction with the CRR prescriptions. In Part A, concerning the self-issued ABS, the detailed rows "Senior", "Mezzanine" and "First Loss" make no sense for the underlying pool of assets (since there is no clear split within the pool of assets that is pledged).

The way the depreciation of significant currencies should be tested in part C is not clear: should the depreciation tested be compared to the reporting currency? In the same reporting and scenario, the amounts to be reported should be net of the hedge, should a hedging relationship be documented. This should be clarified in the instructions and will surely bring a lot of complexity to this reporting while redundant with LCR and Additional monitoring tools which already highlights FX issues.

We also expect clarification on the reporting framework: confirmation that the Asset Encumbrance reporting is part of the Corep package under a prudential scope, and also clarification on the remittance delay, etc.

Q10: Do you identify any overlaps with the existing reporting framework, which could be

We identify obvious overlap with the data reported in the LCR and NSFR framework, as well as in the on-going consultation paper on additional monitoring tools, but with an added level of complexity imposing heavy implementation costs and increased reporting burden on the institutions.

We urge to avoid having to produce several sets of reporting on the very same issue of asset encumbrance. There must be room for rationalization that could be expected from EBA since it has an overview of all the required reportings.

We appreciate that the EBA has removed asset encumbrance table (LR6) from leverage ratio reporting.