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Finance for Europe

Association for Financial Markets in Europe

Consultation Paper Response

Draft Implementing Technical Standards on Asset Encumbrance Reporting under Article 95a of the draft Capital Requirements Regulation ('CRR')

20 June 2013

The Association for Financial Markets in Europe (AFME) welcomes the opportunity to comment on the EBA's recent consultation paper on Draft Implementing Technical Standards on Asset Encumbrance Reporting under Article 95a of the draft Capital Requirements Regulation ('CRR'). AFME represents a broad array of European and global participants in the wholesale financial markets. Its members comprise pan-EU and global banks as well as key regional banks, brokers, law firms, investors and other financial market participants. We advocate stable, competitive, sustainable European financial markets that support economic growth and benefit society.

AFME is the European member of the Global Financial Markets Association (GFMA) a global alliance with the Securities Industry and Financial Markets Association (SIFMA) in the US, and the Asia Securities Industry and Financial Markets Association (ASIFMA) in Asia.

AFME is listed on the EU Register of Interest Representatives, registration number 65110063986-76.

We summarise below our over-arching response to the discussion paper, which is followed by a section with more detailed thinking around some of the main topics and questions asked.

Over-arching Comments

AFME and its members agree in principle with the reporting of asset encumbrance and are supportive of the work the EBA is undertaking in this area. The proposed reporting requirements are generally straight-forward but we have noted more widely that it is not clear what the EBA is seeking to achieve from the templates which appear a mix of reporting on balance sheet sub-ordination and liquidity. We consider that reporting on liquidity risk is covered through the reporting firms will need to complete in relation to the LCR, NSFR and additional monitoring measures, and we would recommend therefore that the EBA should focus on balance sheet subordination only. AFME and its members have reservations also as to the value that will be provided from reporting on the suggested scope of consolidation if it is intended to provide a gauge to liquidity risk.

More detailed considerations/responses to questions

Question 1

Is the definition of asset encumbrance sufficiently clear?

AFME and its members consider that the definition is clear. As a general principle, we consider that to the extent possible the definitions and treatments should be consistent with the approaches taken under the liquidity reporting framework.

Question 2

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?

We understand from the recent EBA Public Hearing that the scope of application will follow the approach to COREP reporting and that all entities subject to COREP will therefore be required to report on asset encumbrance. AFME and its members would, however, reiterate our view that the EBA needs to be clear as to the intended use of the data it plans to capture – If for instance, the EBA is seeking to gauge a firm's ability to raise additional funding through encumbering assets then it would not be meaningful to collect data on a consolidated basis unless assets can be freely transferred between different entities and across different jurisdictions. Focussing on a figure at a regional, sub-consolidated level may also be misleading and result in non-comparable data – for example, global groups may issue a higher proportion of their unsecured debt outside of EU entities in the scope of the EBA's reporting and the ratio for the entities or sub-consolidated groups within the scope of CRDIV may therefore be unrepresentative of the group's encumbrance, when compared to group's which are headquartered in the EU and fully in the scope of the EBA's proposals.

As mentioned previously, we would recommend that the EBA should seek to assess balance sheet subordination only through the templates proposed.

Question 3

Do you believe the chosen definition of the 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 are generally supportive of a ratio which includes off balance sheet collateral received and rehypothecated or available for rehypothecation as it gives a total measure of encumbrance. We share the EBA view also that the ratio should be used only to define a reporting threshold given the unfeasibility of establishing optimal levels of asset encumbrance if national, market and business model specificities have to be taken into account.

Question 4

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 sheets 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?

AFME and its members have noted that institutions would need to invest significantly in preparing for the new reporting requirements to be able to identify with certainty whether they exceeded an encumbrance ratio of 5%. We would therefore suggest the use of the total assets measure is preferable and that if levels of encumbrance are needed as a trigger for the reporting requirement, then a simplified measure should be considered.

AFME considers also that further thought is needed around how a firm is considered to have exceeded a threshold – By way of illustration, as it is currently written a one-off spike in a firm's activities could cause it to exceed the threshold and trigger reporting when in reality for most of the time the firm's encumbrance might be negligible. We would suggest therefore that consideration is given to the need for firms to exceed the thresholds consistently over a period of time, for example a quarter, and/or for forms of averaging to be applied.

Question 5

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?

We consider that there are few restrictions other than through third parties' willingness to accept particular asset types as, for most assets, even if legal title could not be transferred, a floating charge over the asset could be granted, which would appear to meet the definition of encumbrance. We therefore have no specific examples of where such assets could not be available for encumbrance.

In addition, given the diversity of European regulations and private contractual terms resulting in encumbrance, any possible answers to this question following the definition of encumbrance provided in this consultation would lead to highly specific answers, not only in relation to different jurisdictions but also in relation to different business models. In our view any such answers would not assist in assessing in any meaningful way the extent to which institutions could move to increased secured funding in the event of a stress.

Question 6

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

No additional sources have been identified.

Question 7

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?

The repo market represents the most expedient way of raising cash, and, as a result, is generally firms' first choice for generating liquidity when required. In particular, the eligibility of a particular asset for repo with a central bank may serve as an appropriate measure for 'extremely high' liquidity. However, assets that are not eligible for repo with central banks are also often highly marketable and can be tested against other metrics to gauge the extent to which they exhibit 'high' liquidity. We would reiterate our comment, however, that the EBA should not seek to assess liquidity risk through the templates set out in this consultation but should focus more specifically on balance sheet encumbrance.

We understand that the EBA is intends as a separate area of work to conduct a comprehensive review of asset classes in order to determine their potential eligibility for inclusion in the liquid assets buffer under the liquidity coverage ratio. AFME has provided a detailed response to the EBA's discussion paper on this topic and we refer to the feedback we gave on the proposed liquidity metrics together with the additional metrics and explanatory characteristics we proposed. Appropriate combinations of these measures can be used to assess the marketability of particular assets and we would be pleased to engage further with the EBA on this topic.

Question 8

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

AFME and its members have noted the overlap with the stress testing performed under the liquidity coverage ratio and with the testing required under the Pillar 2 framework and firms' recovery and resolution planning. In particular, we would note that the liquidity stress scenario to assess contingent encumbrance have been defined in the CRR after a long period of discussion and political agreement, and we are concerned that new scenarios may be inconsistent with the CRR.

Additional questions in Annex II:

Question 9

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

AFME and its members have noted that the current instructions do not provide guidance on the treatment of pooled collateral and that throughout the requirements it is assumed that one piece of collateral is assigned to one asset. There appears also no consideration of the treatment of tri-party repos.

Question 10

Do you identify any overlaps with the existing reporting framework, which could be mitigated?

As mentioned throughout, we have identified an overlap with information reported under the liquidity framework and we would prefer an approach which avoids the need to produce several sets of reports on the same issue.