

# POSITION PAPER



## **WSBI-ESBG response to the BCBS consultation on Pillar 3 Disclosure Requirements**

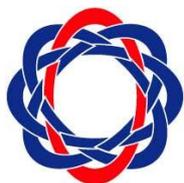
**WSBI (World Savings and Retail Banking Group)**

**ESBG (European Savings and Retail Banking Group)**

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ESBG Transparency Register ID: 8765978796-80

10 June 2016



**WSBI**



**ESBG**



Dear Sir/Madam,

Thank you for the opportunity to comment on the Basel Committee on Banking Supervision (BCBS) Consultation on Pillar 3 Disclosure Requirements. While the work of the BCBS on the Pillar 3 Disclosure Requirements is appreciated by members, increasing the coherence of the Pillar 3 framework and improving the comparability of information, there have been concerns raised in a number of areas which are detailed below. Our response to this consultation will first detail some general concerns before referring to specific issues with the suggested templates and tables.

### **General comments**

As stated above, while WSBI-ESBG members are appreciative of the work done by the BCBS they are of the opinion that the scope of the information to be disclosed has increased significantly and that the level of granularity in information suggested to be disclosed is overwhelming. Members are unsure whether the current draft of the disclosure requirements meets the needs of the addressees, in particular small and medium banks. A discussion on what is really meaningful and appropriate to disclose to investors rather than merely reporting the information to relevant authorities is called for. When harmonising the Pillar 3 disclosure requirements the Basel committee should avoid introducing definitions and information not required by the regulations themselves. When figures are calculated and defined differently in Pillar 3 than in other reporting it adds to the burden of disclosure and reporting for banks.

Further concerns have been raised regarding the proposal to require publication of standardised methods to benchmark internally modelled capital requirements. Non-risk based capital requirements may give misleading information to investors and other stakeholders about the riskiness of different banks and this must surely not be the intention of the committee.

The review of many of the Basel standards is still ongoing and hence the proposed Pillar 3 framework is based on “moving targets” such as Basel proposals for changes on calculating capital requirements for credit risk (both standardised methods and IRB), CVA risk, Operational risk and the Leverage ratio. It is therefore difficult to know how to interpret or comment upon the disclosure proposals where the substance is not yet settled. A final assessment of the feasibility and appropriateness of the Pillar 3 framework can only be made when the changes to the Basel standards have been finalised. The fact that the proposed Pillar 3 framework is based on standards not yet finalised also has important implications for implementation. For example, the consequences of the proposals can only be evaluated when the requirements are finalised thus pushing forward the date when banks will be able to comply with the new requirements. With this in mind the proposed implementation date of the end of 2017 for certain templates is very ambitious.

With all new requirements the concepts of proportionality and materiality are of paramount importance. The information required must be relevant, it must be clarified that the templates need only be filled with essential information, to the extent that there should be a provision for reporting institutions to shorten mandatory templates to just those lines that need to be filled. The proposed volume of additional disclosure will also place a significant strain on banks' ability to meet the external reporting timelines required by investors and securities regulators. The suggestion that the Pillar 3 report be published concurrently with the financial reports for the corresponding period exacerbates this challenge. Additional costs (e.g. for information technology) may also be incurred as a result of the more rigorous internal review required for publicly disclosed information and the need to enable the necessary information to be captured for fixed-format templates. For this reason, too, we request greater flexibility



in the application of the templates so that reporting deadlines can be met and added value can be delivered to users. Hence WSBI-ESBG urge the Basel Committee to re-evaluate its stance on this item.

There is an impression that the proposed level of detail and frequency of disclosures are geared primarily to users of Pillar 3 reporting by publicly traded companies. Non-publicly traded small and medium-sized banks would also be affected by the requirements, however. Much of the required information will change only insignificantly over time so it makes little sense, from a relevance perspective, to issue disclosures more frequently than once a year. This also applies to institutions which publish quarterly financial reports. Moreover, quarterly reports are prepared in a much tighter time frame than is the year-end report. Given that regulatory reporting information only has to be submitted to supervisors after 30 working days, we believe it would be inappropriate to require banks to publish some of the data ahead of this deadline in the context of Pillar 3 disclosures. We therefore urge the Basel Committee to allow all templates and tables to be disclosed on an annual basis.

In addition to the above general comments members would also like to highlight some specific challenges arising from the proposed templates and tables.

### **Template Specific Comments**

#### **Part 1: Proposals for revised and new disclosure requirements**

In view of disclosure requirements relating to upcoming regulatory changes (new OpRisk SMA, FRTB) the implementation dates of the disclosure requirements in relation to these new regulatory requirements should be strictly aligned with the material implementation dates of the proposed changes. Members deem it appropriate to implement the changes step-wise, depending on the finalization of the different review projects. As a general rule the new disclosure requirements should not get into force earlier than the material changes itself.

##### **Point 1.1 Proposal for a dashboard of key regulatory metrics:**

Even if the marginal costs for banks, as set out in the documents, seem to be rather low and these figures seem to be existing already in the public domain, it needs to be emphasised that this is an additional requirement, which needs additional efforts, additional check-routines, and it is information already in existence, so it is duplication of information. The regulator must very carefully assess if this additional disclosure requirement is really necessary.

To ensure proportionality, it should be considered, that the dashboard of key regulatory metrics is the only disclosure requirement for non-publicly traded small and medium-sized banks. The Basel Committee must comply with the principle of proportionality to actively reduce regulatory burden for those institutions.

##### **Point 1.2 Use of standardized approaches to benchmark internally modelled capital requirements:**

It is the view of members that the use of the word “opacity” in view of data generated based on IRB- or MR-models does not really seem to be appropriate, as this data is being scrutinized and validated by several internal and external parties. Disclosing STA figures does not change much in view of the strengthening of the interpretation of the IRB- or MRM-figures as these figures are based on another methodology. The risk of misinterpretation and misunderstanding increases if these figures are being made directly comparable without detailed information/explanation, because not every reader will be



an expert in the field of RWA-computation. It can also be questioned if this really is useful information to be provided to the market.

## **Part 2: Overview of risk management, key prudential metrics and RWA**

### **Templates HYP1 and HYP2:**

From the instructions it remains unclear where to report exposures in permanent or temporary partial use, meaning that for these exposures RWA are already calculated in Standardised Approach. For the sake of comparability either these exposures should be excluded from both columns or included in both columns. What should be avoided is, to in-/exclude it from one column but at the same time not in-/exclude it from the other.

The proposal to require publication of standardized methods to benchmark internally modelled capital requirements has been deemed flawed by WSBI-ESBG members. Non-risk based capital requirements will give misleading information to investors and other stakeholders about the riskiness of different banks which surely was not the intention of the committee. Members are also of the opinion that this information probably would not add much value if a permanent floor, based on the Standardised Approach, should be implemented for internal bank models by the BCBS.

### **Template KM1: Key metrics (at consolidated group level)**

Banks are expected to supplement the template with a narrative commentary to explain any significant change in each metric value compared with previous quarters. Clarity is needed on whether it is expected that the narrative commentaries would need to be included in upcoming publications as the significant change from one quarter to the next until they are phased out after T-4. Disclosing commentary only on changes compared to the previous quarter (T-1) is suggested.

### **Template OV1: Overview of RWA**

Page 23: Definitions and instructions – Equity: Breakdown according to "Equity investments" is difficult to assess as it refers to Basel framework still to be finalised.

WSBI-ESBG members have also suggested that it is unclear how banks should publish Pillar 2 requirements. It is important that it is possible to distinguish between formally decided Pillar 2 capital requirements and informally reached requirements in Pillar 2. If this is unclear then it will be difficult for investors and other stakeholders to compare banks with their peers where Pillar 2 requirements are in some jurisdictions reached by formal decisions and in other through informally reached agreements. One example that should be clarified in the templates is the Floor adjustment in the template OV1. In the note to the template OV1, page 23, it is stated that "Pillar 2 adjustments applied do not need to be disclosed".

## **Part 3: Linkages between financial statements and regulatory exposures**

### **Template PV1: Prudent valuation adjustments**

Disclosures on the split into trading and banking book should be aligned with the revised version of the capital requirements for market risk framework expected to come into force in 2019. Implementation in EU regulation might prolong the implementation further.

The suggested Pillar 3 disclosure of prudent valuation adjustments is in another format when compared to proposed regulatory reporting requirements in the EU. Introducing different varieties of reporting or disclosures will lead to unnecessary reporting burden on banks and increased complexity for investors and other stakeholders



The template could be adapted to the EU proposal making the following adaptations:

- Market Price Uncertainty should not be included within the Close Out Cost;
- The committee needs to clarify the area “Other”.

#### **Part 4: Composition of capital**

##### **Point 4(c) Step 1**

According to accounting, IFRS, and regulatory requirements there is no obligation to disclose the scope of consolidation on entity level. Therefore, any list of entities which show the difference between the two scopes does not add any value for external readers.

##### **Template CC1**

For entities applying the phase in requirements until 2018 this template is not relevant.

The provisions on TLAC holdings will need to be adjusted for the final TLAC holdings rules (lines 52-55 and footnote 34). The present versions do not reflect necessary changes recommended in industry comments on the TLAC holdings proposals.

In line 64, the definition of the buffer requirement is not appropriate: “*Institution specific buffer requirement (minimum CET1 requirement plus capital conservation buffer plus countercyclical buffer requirements plus D-SIB buffer requirement, expressed as a percentage of risk weighted assets)*”. It should be restricted to the components of the combined buffer. The minimum CET1 requirement should be excluded.

Legal basis for information to be disclosed (Basel standard or local regulation) should be clearly stated. The EU implementation of global TLAC requirement in parallel with the implementation of the bank specific MREL as outlined in the BRRD will further increase risk for confusion among investors.

How should banks disclose additional firm-specific external TLAC requirements? This is important especially in the context of MREL requirements in the European Union. Depending on the design, MREL requirements could be regarded as such as additional firm-specific TLAC requirements. Otherwise comparability will be suffering.

##### **Template CC2**

The CC2 template does not correspond to the currently valid FINREP structure and should be adapted to the balance sheet structure which is in accordance with IFRS 9. This standard will enter into force on 01 January 2018.

As credit institutions have to disclose their balance sheet according to IFRS and analysts and investors are familiar with this structure, the Pillar 3 structure should be in line with IFRS. A creation of a new balance sheet structure will not enable reconciliation between IFRS and regulatory requirements. Thus, unification between the IFRS balance sheet and the regulatory publication should be guaranteed.

##### **Template CCA**

It is not clear whether this table is intended to be at the group consolidated level or not. It is also not clear whether it excludes internal TLAC. The working assumption is that it applies to external issuances only, but this needs to be confirmed.

Given the ongoing discussions about expanding the TLAC regulatory reporting requirements to MREL, members would like to highlight the following regarding the KM2 and CCA templates:



### **Template KM2**

KM2 is required on a quarterly basis, which is out of sync with other TLAC templates, required on a semi-annual basis. KM2 should therefore be put on a consistent basis with the other TLAC templates. There is no obvious value added from the quarterly frequency of KM2. MPE banks have multiple resolution groups and the proposal would result in frequent, extensive disclosure under KM2. It is suggested that only material resolution groups (with appropriate narrative on the basis on which such groups are selected) be disclosed and only on a semi-annual basis

### **Template CCA**

Line 34a appears to require an instrument-by-instrument response where the applicable types of subordination differ. Reasonable aggregation should be allowed. More generally, as Table CCA is required for each instrument, the reporting volume will be a concern to users as well as issuers. The volume will be substantially greater than for Tier 2. It would be very useful to introduce a materiality threshold for CCA reporting (or include only benchmark issuances). Transactions below a threshold could be aggregated.

Private Placements (both for subordinated and senior debt) should be aggregated, both to manage down the volume of disclosures and to provide reasonable confidentiality, both as to the firm's financing strategy and for lenders. The principles of aggregation need to be discussed, but reasonable aggregation should allow other lenders to see the general position of private placements in the stack. Private-placement lenders are presumably in a position to negotiate comprehensive disclosure of their exposures as part of the placement process and so would not need to rely on public disclosures to ascertain their own exposures to bail-in.

The frequency requirement of Table CCA is that "Table CCA should be updated on a bank's website whenever the bank issues or repays a capital or TLAC instrument or whenever there is a redemption, conversion, write down or other material change in the nature of an existing instrument." Given that Table CCA requires the inclusion of "the main features of a bank's regulatory capital instruments and other TLAC-eligible instruments," the frequency requirement would amount to daily or near daily updating of public disclosure. This would surely be burdensome and it is difficult to see any value added for investors, while the complexity of website disclosure would increase substantially, which should be taken into account. This is especially the case for debt redemption at contractual or expected maturities. Except for material and extraordinary events that would have to be disclosed in any case under other bodies of regulation and law, it should be entirely sufficient to provide the CCA disclosures on a semi-annual basis consistently with the bulk of Pillar 3 as proposed. The Basel Committee should consider going even further for institutions which are not capital market orientated and non-publicly traded. For these institutions an annual disclosure would be sufficient.

In row 3a, it is required to disclose "other TLAC-eligible instruments governed by foreign law". To be noted is that in the EU implementation of TLAC, the governing law could be the law of an EU country other than the home jurisdiction of the bank. This approach has been chosen for the MREL as outlined in the BRRD. If this approach is chosen also in the EU implementation of TLAC, then the TLAC-eligible instruments governed by the law of non-EU countries should be disclosed in this row.

Members have indicated that they find it difficult to opine on the templates related to TLAC disclosure as the final scope and form of the TLAC holdings proposals are still outstanding. It would be preferable to review a final set of disclosure templates on TLAC once all outstanding questions on TLAC definition and TLAC holdings have been settled.



## Template TLAC2

In the EU implementation of TLAC, it is suggested that the 28 Member States are to be regarded as one jurisdiction. In that case, only subsidiaries in non-EU countries can be regarded as material subsidiaries for which the disclosure of TLAC2 would be relevant.

## Part 7: Liquidity

### Table LIQA – Liquidity risk management

The qualitative and quantitative disclosure examples are largely covered by the information provided already today so the proposal appears reasonable. The suggested flexibility giving banks the opportunity to assess what information is the most relevant to publish, even though this might reduce comparability is appreciated by members.

### Template LIQ1 – Liquidity Coverage Ratio (LCR)

The banks in the EU are obliged to calculate and submit the LCR based on the Delegated Act (Commission Delegated Regulation (EU) 2015/61 of 10 October 2014) to the local regulators on a monthly basis. The daily reporting is only required if the limit on the LCR is breached or is expected to be breached in the near future. Therefore, the proposal on the quarterly publishing of the LCR, based on the latest BCBS regulation (<http://www.bis.org/publ/bcbs238.pdf>), as an average of the daily ratios on both, solo and consolidated level, would require significant additional effort from the banks.

Moreover, as the calculation methodology for the Basel III LCR and LCR, based on the Delegated Act, are different (especially in the classification of the HQLA assets, but also in the definition of stable retail deposits and of deposits with operational relationships, as well as the treatment of less stable deposits, contingent liabilities other than committed credit and liquidity facilities etc.), the disclosure of the Basel III LCR for the EU banks could lead to misleading conclusions from investors and clients, as the EU banks focus on the steering of the LCR based on the Delegated Act. Therefore, a situation can occur, where a bank complies with the EU regulations and limits, but its Basel III LCR would be significantly lower than 100%, which could raise doubts about the soundness of its liquidity risk exposure. This possibility would force these banks to focus also on the steering of the Basel III LCR figures parallel to the one based on the Delegated Act, which is hopefully not desired by the EU regulators.

### Template LIQ2 – Net Stable Funding Ratio (NSFR)

On the proposals regarding the (i) postponement of the implementation of the NSFR disclosure requirements until the final European Regulation and the related ITS are implemented, or the (ii) disclosure of the quarterly NSFR on a semi-annual basis based on the CRR and the EBA template using the latest Basel III NSFR weighting factors:

The banks in the EU are obliged to fill and submit the NSFR template from EBA based on the CRR (Regulation (EU) No 575/2013 of the European Parliament and of the Council of 26 June 2013) to the local regulators on a quarterly basis. Members have highlighted this as a concern as:

- The calculation methodology and the template structure for the Basel III NSFR (acc. to <http://www.bis.org/bcbs/publ/d295.pdf>) and NSFR based on the CRR and the EBA template are largely different (especially in the classification of the HQLA assets);
- There is no final regulation how exactly to calculate the NSFR in the EU (there are no prescribed weighting factors in the EBA template);
- The limit on NSFR is not expected to be implemented before 2018.



There is currently less focus on the steering of this ratio compared to the LCR. Therefore, the proposed regulation on the NSFR Pillar 3 disclosure would force the EU banks to implement a new NSFR report by the end of the half of 2018, which will be most probably replaced by the final EBA template for NSFR calculation. To avoid the cost for this temporary solution, some members have proposed that:

- The implementation of the NSFR disclosure requirements is postponed until the final European regulation and the related ITS are implemented; or
- A disclosure of the quarterly NSFR on a semi-annual basis based on the existing rules (here: CRR and the EBA template using the latest Basel III NSFR weighting factors) is allowed.

## **Part 11: Market Risk**

### **Table MRA: General qualitative disclosure requirements related to market risk**

The need to disclose information on desk structure as well as an exhaustive list of desks under the IMA, instead of a general description can be questioned as the information is of proprietary nature. It should be sufficient to report the information to the relevant authorities.

In section A point a) it is required that “policies for determining whether a position is designated as trading, including the definition of stale positions, the market value of stale positions, and the nominal value of stale positions” is to be disclosed. It is, however, unclear what the term “stale position” refers to.

### **Template MR1: Market risk under SA**

The information required is far too granular. Disclosing Delta, Vega and Curvature would give competitors too much information and hence this information should only be reported to relevant authorities. Capital charge in SA by asset class should be sufficient in terms of public disclosure so as to provide investors with a good understanding of the risk taken. Such an approach would also avoid a situation with information overload.

Further, in the accompanying narrative banks are required to disclose position specific information. This does not provide any additional value to users unless detailed information is disclosed, e.g. counterparty names. In that case however the information is of confidential nature. It could be considered instead to disclose total amount per category.

To keep a position in the trading or banking book in contradiction to general presumptions of the boundary requires FSA approval or could be conducted upon supervisory request. It is questionable whether such a disclosure would add value to users.

### **Table MRB: Qualitative disclosures for banks using the IMA**

In section A point b) it is required that “Soundness criteria on which internal capital adequacy assessment is based on” is disclosed. The reason for requiring disclosure of the soundness specifically for the market risk Expected Shortfall models, but not for credit risk or liquidity risk models should be clarified.

In section A point c) the reference to “the range of values used for the n-business days factors” needs to be clarified, since the revised version of the capital requirements for market risk frameworks requires banks to use regulatory number of business days. Also further clarification on the level of detail expected when describing the difference between the reduced set of risk factors and the full set of risk factors should be provided. A high level description should suffice.



### **Table MRC: The structure of desks for banks using IMA**

It is not appropriate to disclose information on desk structure as the information is sensitive and of proprietary nature. This information should only be provided to relevant authorities.

### **Template MR2: Market risk IMA per desk**

It is not appropriate to disclose information on capital levels and back-testing results on desk level as the information is sensitive and of proprietary nature. This information should only be provided to relevant authorities. Disclosure on asset class level is sufficiently granular from the investors' point of view.

The actual standalone desk level numbers might be interpreted inappropriately as they do not take into account the diversification benefit at bank wide level, i.e. two desks might look very capital consuming on a standalone basis, but when aggregating them together due to opposite risk profiles, the picture could look very different.

### **Template MR4: RWA Flow Statement:**

The separation of Market Risk RWA into the categories 2-7 is ambiguous due to the non-additive nature of IMA-models. Providing a qualitative description of the major changes that impact the RWAs would be recommended. Additionally it may be prudent to set the frequency to semi-annual (in alignment with the frequency for the other detailed templates).

## **Part 12: Operational Risk**

It is challenging to assess the implication of the proposal as the Pillar 3 disclosure requirement is to change as the Standardised Measurement Approach (SMA), currently under consultation, is finalised.

### **Table ORA – General qualitative information about operational risk management**

Further information on the qualitative disclosures, especially in point c (operational risk measurement system) and e (risk mitigation and risk transfer used in the management of operational risk) is called for.

The time periods applied in Template OR1 (Historical losses used for SMA calculation) and Template OR3 (Historical losses) should be harmonised. This could be done by aligning the period to the one suggested in the SMA consultation: having a 5 year period initially, while gradually moving to a 10 year period. On the other hand, internal loss data for a shorter period of e.g. five years would be more relevant and better linked to banks' current business activities, as it gives more weight to recent organisational changes and M&A activity, as well as being more related to future vulnerabilities. The two templates (OR1 and OR3) could also be merged if the time periods applied are harmonised.

Additionally, the degree of detail of the business indicator is far from being relevant for the public, as it includes intermediate accounting data that entities manage internally (memory, audit, etc.). In fact, the detail asked for could be compared to publishing the current C16 of capital consume.

## **Part 14: Remuneration**

It is appreciated that name specific information is not requested in the proposed Pillar 3 disclosure framework. In addition, it would be advisable to require disclosure only if there is, for example, four or more employees in a specific category, so as to further protect the individuals. Also, members who have begun to implement the template for Remuneration have encountered an issue with Template REM3.



### **Template REM3 – Deferred remuneration**

Row 6 of this template refers to “Material risk takers” – this is not consistent with Template REM2 which refers to “Other material risk takers”. In order to maintain consistency and for this template to make sense Row 6 should be corrected to read “**Other** material risk takers”.

### **Conclusion**

As previously mentioned WSBI-ESBG members appreciate the work done so far by the BCBS in this area but, as with all requirements, there is a need to ensure the principles of proportionality and materiality are maintained. We greatly appreciate the opportunity to put forward our views on this consultation and hope that the points made above will prove useful going forward.



## About WSBI (World Savings and Retail Banking Institute)

WSBI brings together savings and retail banks in all continents and represents the interest of circa 6,000 financial institutions with total assets of USD 14 trillion and serving some 1 billion customers in 80 countries worldwide (2013 figures). As a global institution, WSBI focuses on international regulatory issues that affect the savings and retail banking industry. It supports the aims of the G20 in achieving sustainable, inclusive and balanced growth and job creation around the world, whether in industrialised or less developed countries. WSBI favours an inclusive form of globalization that is just and fair, supporting international efforts to advance financial access and financial usage for everyone. It supports a diversified range of financial services that meet customers' transaction, savings and borrowing needs responsibly. To these ends, WSBI recognizes that there are always lessons to be learned from savings and retail banks from different environments and economic circumstances. It therefore fosters the exchange of experience and best practices among its members and supports their advancement as sound, well-governed and inclusive financial institutions.



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## About ESBG (European Savings and Retail Banking Group)

### ESBG – The Voice of Savings and Retail Banking in Europe

ESBG brings together nearly 1000 savings and retail banks in 20 European countries that believe in a common identity for European policies. ESBG members represent one of the largest European retail banking networks, comprising one-third of the retail banking market in Europe, with 190 million customers, more than 60,000 outlets, total assets of €7.1 trillion, non-bank deposits of €3.5 trillion, and non-bank loans of €3.7 trillion. ESBG members come together to agree on and promote common positions on relevant regulatory or supervisory matters.



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Published by WSBI-ESBG. March 2016.