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STANDARD
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Basel Committee on Banking Supervision
Bank for International Settlements
CH-4002 Basel
Switzerland

By e-mail: baselcommittee@bis.org

February 20, 2012

Dear Sir / Madam

Consultative document - definition of capital disclosure requirements

Standard & Poor's Ratings Services ("Standard & Poor's") appreciates the opportunity to provide the Basel Committee on Banking Supervision (the Basel Committee) comments on its *Consultative document – definition of capital disclosure requirements* (the "CD") issued in December 2011 The views expressed in this letter are Standard & Poor's and do not necessarily represent those of any other entity to whom it may be affiliated. We intend our comments to address the analytical needs and expectations of our credit analysts[1]. In our view credit analysts are among the most frequent users of banks' financial information, particularly with regard to financial information regarding capital.

Standard & Poor's Supports The Basel Committee's Proposals To Improve Banks' Definition of Capital Disclosure Requirements

We broadly support the Basel Committee's proposals as set out in the CD, as we believe that they will contribute significantly to enhancing users' understanding of the capital composition of banks.

We strongly support the CD's proposal for the use of common templates as we believe that this will greatly enhance market understanding and allow greater comparability across banks. Similarly, we note that the European Banking Authority (EBA) proposes a template approach to achieve a high level of harmonization and strong convergence in common regulatory reporting requirements (COREP) across Europe.

We encourage the Basel Committee to develop common templates for disclosures about banks' capital requirements, as the proposals tentatively suggest, as soon as possible. High quality, comparable disclosures using common templates would, in our opinion, strongly enhance clarity

[1] The opinions stated herein are intended to represent Standard & Poor's Ratings Services' views on the potential changes set out in the CD. Our current ratings criteria are not affected by our comments on the CD.

and consistency in this area, and would avoid some of the shortcomings that limit the usefulness of Pillar 3 reports.

We would suggest that the template approach is not diluted, as we believe this would undermine the rationale for mandating templates (which, as we understand it, is to enhance comparability and reduce complexity). Therefore, we think that the scope for preparers to amend the templates should be appropriately limited or eliminated. At the same time, in order to avoid the risk of a mechanical, tick-box approach when banks complete the templates, we think that the proposals should include an overarching requirement to provide additional disclosures where necessary for a proper understanding of the bank's capital position.

We agree that the disclosure templates should be published with the same frequency as banks' financial reports. We also believe that the timeliness of the templates is at least as important as their frequency and that the Basel Committee should take this into consideration in the finalized requirements. Given that Pillar 3 reports are generally only published annually and often quite some time after the end of the period to which they relate, we do not consider Pillar 3 reports to be currently the appropriate vehicle for these templates.

We set out more detail to some of the above comments in the rest of this letter.

Drawbacks To The Current Pillar 3 Disclosures

Pillar 3 disclosures under Basel II have since 2009 been an important input to our analysis. Nevertheless, we have observed a number of drawbacks to the current Pillar 3 disclosures. We believe that avoiding these drawbacks in the disclosure requirements would be beneficial for market participants. In our experience with Pillar 3, we consider that the following weaknesses have often limited users' ability to take full advantage of the additional disclosure:

- the insufficient timeliness of Pillar 3 reports, which may in some instances be released several weeks or months after financial statements;
- the absence of quarterly or semi-annual disclosure in some jurisdictions;
- the variations existing between preparers regarding the definition of the data items that are disclosed (for instance, definition of exposures);
- the aggregation of information according to different classification by preparers (for instance definition of regions for geographic breakdowns);
- the scarcity of narrative information to support quantitative disclosure, and
- the lack of common templates which market participants can use in an efficient manner (as opposed to COREP for instance).

Standard & Poor's Welcomes The Use Of Standardized Templates

One of the key elements of useful disclosure in our opinion is comparability, both across banks and over time. We consider that comparability becomes more difficult when the underlying subject matter is inherently complex, as in the case of banks' capital. We welcome the proposals in the CD to mandate the use of standardized templates, because we believe this approach could help to mitigate complexity and enhance comparability.

We also believe that in order for the template approach to be most effective, **the scope for preparers to amend the templates (for example, by combining or omitting lines in the templates, perhaps on the basis of their materiality assessments) should be appropriately limited or eliminated.** In our view, it would be far more difficult – if not impossible – to make

comparisons across shorter, but non-identical, "summarized" templates than it would be to make comparisons across identical templates, even though these may be longer. In other words, we believe that the use of summarized templates would undermine the rationale for mandating templates.

That said, we consider it important that the template approach does not preclude preparers from providing additional disclosure where necessary; preparers should not be led to take a "tick-box" approach to completing the templates. That is why we think that **the proposals should include an explicit, overarching requirement to provide additional disclosure where that is necessary for a proper understanding of a bank's capital position**.

We understand that it is sometimes appropriate for individual jurisdictions to add items to the templates to reflect circumstances specific to those jurisdictions. However this raises the concern that individual jurisdictions differ in their approaches to adding similar items, which in our view creates an added layer of complexity that is not helpful. We therefore consider that it would be better, on balance, if the Basel Committee mandated the data items to be included in the templates, rather than this being done at a jurisdictional level.

Similarly, inconsistent interpretation and application of the templates by banks would undermine comparability. Although the explanations for each row that are provided in the CD are helpful, we do not believe that they will be sufficient in ensuring consistent interpretation and application. We recommend that the Basel Committee establishes a central process to address technical queries in a consistent manner and publishes its responses to common queries to further promote consistent interpretation and application of the templates.

Data Items In The Templates

We broadly agree with the data items that the Basel Committee proposes to include in the templates and, in particular, we consider that the approach proposed for the transitional period to 2018 will provide users with relevant information in a clear and comparable format.

We also agree with the introduction of a "main features template," as outlined in Annex 3 of the CD.

Paragraph 32 of the CD sets out a list of data items that the Basel Committee decided not to include in the templates. The rationale for excluding these items is not clear to us. Whilst it can be argued that the information that would be provided by these items is already publicly available, we think that the items are part of the basic information set that is necessary for any form of analysis and understanding of bank capital. We would use the information listed in paragraph 32 in order either to inform our classification of a hybrid capital instrument based on its degree of equity content or to inform our rating of the instrument, or both. Other features that we view as relevant in our analysis include the currency of the instrument and the exchange rate retained in regulatory ratios (for example, whether the initial exchange rate or the exchange rate as at the closing date is used), or the fact that an instrument were subscribed to by governments.

Based on the experience of recent years, in our view the conditions under which coupon or dividend payments can be suspended or cancelled is also very relevant. However, item 16 of the main features template (in Annex 3 of the CD), which requires the coupon or dividend payment to be classified as either 'fully discretionary,' 'partially discretionary' or 'mandatory,' will not provide a sufficient basis to assess these conditions. A number of factors can have a significant

impact on whether the coupon or dividend must be paid and the template should require these to be described clearly. They include the following:

- look-back or dividend pusher periods;
- clauses that link deferability or cancelability to payments made on one or more pari passu instruments;
- clauses that require coupons to be paid if the issuer has sufficient distributable reserves or meets minimum regulatory capital requirements, and
- clauses that require nonpayment if the issuer reports a loss in a particular accounting period.

Furthermore, we believe that the templates should also apply to all capital instruments, i.e. including common equity.

Frequency, Location And Timeliness Of Disclosures
An up-to-date understanding of a bank's capital position is an important element in assessing its financial position and risk profile. That is why we agree with the proposal in the CD that banks should publish both the post 1 January 2018 template and the template proposed for the transitional period to 2018 (the disclosure templates) as frequently as they publish their periodic financial statements.

We do not have a strong view as to whether these templates should be included as part of banks' periodic financial reports; however we do consider that **the timeliness of the templates is at least as important as their frequency. We encourage the Basel Committee to take this into consideration in the finalized requirements**, particularly if those requirements do not ultimately include publication of the disclosure templates as part of the periodic financial reports. We also agree that banks should make available on their websites an archive of templates from prior periods and an up-to-date version of the main features template.

Because of the importance of both the frequency and timeliness in publishing the disclosure templates as proposed in the CD, and because of the drawbacks to Pillar 3 reports which we noted earlier, we do not believe that Pillar 3 reports would currently be the appropriate vehicle for the templates.

We thank you for the opportunity to comment on the CD. We would be pleased to discuss our views with the Basel Committee. If you have any questions or require additional information, please contact Arnaud de Toytot (arnaud_detoytot@standardandpoors.com / +33-1-4420-6692).

Yours sincerely,

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