2018.05.25

FRENCH BANKING FEDERATION RESPONSE TO THE BCBS CONSULTATIVE DOCUMENT ON PILLAR 3 DISCLOSURE REQUIREMENTS – UPDATED FRAMEWORK.

The French Banking Federation (FBF) represents the interests of the banking industry in France. Its membership is composed of all credit institutions authorized as banks and doing business in France, i.e. more than 390 commercial, cooperative and mutual banks. FBF member banks have more than 38,000 permanent branches in France. They employ 370,000 people in France and around the world, and service 48 million customers.

The FBF welcomes the opportunity to share its comments on the BCBS Consultative Document on Pillar 3 disclosure requirements – updated framework.

Key messages :

- **Internally modelled capital requirements should not be publicly benchmarked to standardised approach.**

Disclosures comparing the internal models based results with the standardized measures could **wrongly lead investors to consider standardised approach as necessarily the "correct measure and benchmark", undermining the conceptual basis of the risk-based approach. This could have the same effect than a floor calibrated at 100%.**
If there are significant differences between RWA SA and RWA IRB, market participants excessively may rely on RWA SA and may distrust RWA IRB without fully understanding the underlying rationales used in IRB.

In addition, detailed disclosures by type of risks or type of assets could alter the gain from the phasing of the output floor until 2027. They **will encourage market expectations of full floor by 2022.**

The detailed disclosures could also undermine the BCBS principle of a floor at an aggregated level, as they provide enough granularity to simulate the phased-in or full floor at category level or asset class level.

As a result, these detailed public disclosures will represent negative unintended consequences on the market, without providing any true base for risk comparability between banks.

- **Public information should be limited to meaningful and readable information to users.**

While we support the aim of transparent information to users, **we question the balance between transparency and efficiency for end-users**. We question both the **increasing volume and the increasing detailed technicity** of disclosures creating complexity for end users: at best, they do not use it, at worst they can misinterpret it..

In addition, we do not believe that all the proposed information required within the consultation paper will be meaningful to readers and that it will contribute to a relevant comprehensive view of the banks' risk profile.

Further, as already experienced by banks, users, whichever their category (rating agencies, investors, asset managers or analysts) do not show very broad interest to Pillar 3 disclosures.

As regarding information requested specifically by rating agencies, while rating agencies advocate for the most complete information disclosure possible, they already exchange regularly with financial institutions. Their ability to question banks on data available largely surpasses the ability of other Pillar 3 users (investors ...). As a result, the risk of misinterpretation by actors who do not have the capacity to request clarification from the institutions increases as more complex information is published.

In addition, the European supervisor has chosen to base the information to be published in Pillar 3 on the regulatory templates (Corep and Finrep). The set of templates has a global consistency, not very compatible with the addition of requests according to specific focuses sometimes complex and time-consuming to produce.

Finally, **Pillar 3 should remain simple and efficient for all types of end-users**. **There is no need to complexify Pillar 3 disclosures for sophisticated users, such as rating agencies, as they have the possibility to obtain additional granular information directly from banks, via due diligences for instance.**

- **Proprietary and confidential information should be taken into consideration.**

In some circumstances, the level of the granularity of the information requested is overwhelming. It leads the banks to disclose proprietary and confidential information that may have competitive implications. Even if the banks are allowed not to disclose such information, they are required to provide specific mention explaining why they are not reporting this information, which contradicts the above mentioned confidentiality principle.

As acknowledged by the Committee, **an appropriate balance should be sought between the need for meaningful disclosures to the market and the protection of proprietary and confidential information**. Therefore, **a distinction should be made between detailed qualitative and quantitative information to be provided for the only use of supervisors and appropriate aggregated information to be provided to the investors**.

The section 5.1.5. *" Proprietary and confidential information"* is unchanged from the previous version of Pillar 3, whereas the new version of Pillar 3 added disclosure requirements at a much more granular level raising challenging issues of proprietary and confidential information, especially for CVA calculations and Operational Risk items. If requirements on those topics remain as granular as proposed, therefore the "exceptional cases" qualification should be removed from the final version of the Section 5.1.5 and the text should clearly stipulate that only the "more general information" should be disclosed.

Question 1: What are respondents' views on the proposed disclosure requirements set out within the Consultative Document?

- **Revised and additional disclosure requirements for credit risk**

Implementation of the additional requirement regarding NPLs and forbearance exposures will go against the level playing field at the expense of the EU. Indeed, European Union authorities have already issued similar requirements. The template EU CR1-E of the EBA guidelines (EBA GL 2016/11) regarding NPLs and forbearance had entry into force in December 2017 and apply to G-SII and O-SII entities. Thus, we question the use of common and consistent definitions regarding NPLs and forbearance within the Basel proposal but also with the other regulatory requirements.

Besides, an option is given to the national supervisors. In the case of NPLs and forbearance information, the BCBS allows an option to that could jeopardize the objective pursued of comparative information between entities.

Recommendation.

As flexibility is proposed for the format of the non-performing and forborne exposures table , we recommend **to clarify that the format of this table should be aligned with the format requested by local jurisdictions when those jurisdictions have similar requirements mandatory to banks.**

- **Revised disclosure requirements for operational risk**

Regarding OR1, given that **different banks are at different levels as to the quality and quantity of their loss information,** the extent to which the data is meaningful and comparable remains in question. The bald information required could lead to **wrong conclusions** and therefore establish an unlevel playing field and may actually result in raising more questions.
In addition **it is not clear how external parties can interpret a total loss figure in order to conclude on the quality of OR risk management** as this figure covers very different aspects of the evolution of the loss (additional losses on past incidents, new losses, recoveries, adjustment of provisions …)

Recommendation

In preference to the current proposal**, it would be more informative** of a bank's actual risk management and operational risk to **break down operational losses by categories, in percentage values, rather than providing absolute amounts**. Many members believe **percentages and trends, rather than absolute amounts, would be more useful** and less likely to raise problems of confidentiality.
In any case there is the concern that some operational risk losses notably such as **pending litigations and settlements may be subject to confidentiality** and a specific mention allowing not reporting these incidents (including the ones for which exclusion is requested) should be provided.

The detailed qualitative and quantitative information about losses should be provided to European Supervisors only.

- **Revised disclosure requirements for leverage ratio**

We **support the semi-annual disclosure of LR1 and LR2 as opposed to quarterly**. A semi-annual disclosure would provide sufficient useful information for the users. Moreover, a semi-annual frequency would be aligned with that of CC1 and CC2 and that would make more sense.
Besides, it should be noted that, at the European level, the European Banking Authority advises to disclose full information on leverage ratio semi-annually.

Besides we question the relevance of a double set of leverage ratios, one for the purpose of Pillar 1 requirements and the other one to meet Pillar 3 requirements (Template LR2). We believe that it does not enhance information as it leads to focus on temporary exemptions that are already disclosed in the Template LR1.

Recommendation

The leverage ratio calculation should be limited to Pillar 1 requirements. Pillar 3 disclosures shall focus on the summary comparison of accounting assets vs leverage exposure measure (Template LR1). In addition, we agree that the national minimum leverage requirement according to Pillar 1 shall be disclosed.

- **Revised disclosure requirements for credit valuation adjustments (CVA)**

Following the finalised Basel III framework and the development of two approaches, - the standardised approach (SA-CVA) and the basic approach (BA-CVA), the Committee has extended the disclosure requirements for a better understanding of the banks' CVA capital charge and the strategies and processes on that matter.

However, the level of the detailed description of the regulatory CVA calculations – i.e. notably, exhaustive list of the inputs used in the calculation, description of the proxy spread, - as required in table CVAB raise main concerns. It could imply to disclose information that is confidential and sensitive. Such information should not be shared with the market, but should rather be only disclosed to supervisors. Even if paragraph 5.1.5 in the consultation aims to allow banks not to publicly disclose any confidential information, it requires banks to provide public explanation, which is totally in contradiction with the BCBS confidentiality principle.

Recommendation

We suggest to **reduce the number of data so that to provide meaningful information to readers and to avoid publicly disclosing confidential information. If need be, such information should be reported to supervisors only.**

- **New disclosure requirements for standardised approach RWA to benchmark internally modelled capital requirements.**

We would like to recall our concerns raised in the second phase of the Pillar 3 review's consultation regarding disclosures comparing the internal models based results with the standardized approach - templates BEN 1 and BEN 2.
We do not believe that the proposed disclosure will help at all investors in their analysis. On the contrary, **the proposed disclosure could misleadingly establish the Standardised Approach as the true capital requirement**. It will wrongly lead investors to consider standardised approach as necessarily the "correct measure and benchmark", given that it is a much rougher and less-risk sensitive measure. We fully disagree with the BCBS proposal.

With the benchmarking of internal models against the standardised approach, **market expectations would be permanent,** creating undesirable incentives and negative externalities (e.g. on financial stability and credit supply). On top of that, such a disclosure will endanger level playing field since it would push some banks using standardised approach to optimize their exposures with more risky assets, whereas that would not the case for banks using mostly internal models.

In addition, disclosures by type of risks or type of assets could alter the gain from the phasing of the output floor until 2027. With such disclosures, starting 2022, the users will be able to compare and restate the capital requirements of the banks that are using internal models into standardized approach. **This would undermine the 72.5% floor calibration, the phase-in period till 2027 and the aggregated level of application of the floor.**

Moreover, Hypothetical RWA under standardised approach would provide neither more transparency on internal models nor more understanding of internal models. **It would not reflect the risk profile of bank** using internally modelled RWA. To provide information on hypothetical RWA under standardised approach would bring more complexity in reading the Pillar 3 data. It would be difficult for users to understand the relevance of the standard RWA compared to internal models based RWA.

The conversion of all risks under SA will enable only a partial or wrong comparability between banks and, more generally, between jurisdictions. **A true comparability of risk should be based on a comprehensive quantitative and qualitative information both on banks themselves and on jurisdictions market specificities**.
For instance, a deep understanding of the differences of RWA for mortgage loans, between US banks and EU banks cannot be simply provided by the conversion in Standard Approach. The true comparison would need to take into account the type of loans (Junior lien and revolving home equity loans in the US vs First lien mortgages in Europe), the probability of default ranges and the recourse frameworks (dual recourse in France vs no-recourse in the US).

Recommendation.

For all these reasons, we fully disagree with the BCBS proposed requirement to disclose standardised RWA to benchmark internally modelled RWA.

If granular information requirement was to be maintained, it should be for supervisory benchmarking purposes only; **we urge the BCBS to circumvent such data to the sole supervisory reporting remit and not to extend it to public disclosure**.

- **Revised disclosure requirements on overview of risk management, key prudential metrics and RWA.**

We have so specific comments.

- **New disclosure requirements on asset encumbrance.**

Asset encumbrance disclosure requirements will have the effect of disclosing sensitive information, even though at the discretion of the jurisdiction. Such optionality will imply divergent practices and put into question level playing field between EU and non-EU banks. Moreover, EU banks would be submitted to two different requirements as the EBA issued its own standard on asset encumbrance disclosures.

Besides, template ENC includes an optional requirement regarding central bank facilities that may be included at the discretion of the jurisdiction. As acknowledged in the Basel consultation paper, the information related to amount of assets used in central bank facilities is sensitive and may be viewed as confidential. Therefore, we recommend to delete this information.

- **New disclosure requirements on capital distribution constraints (CDC)**

The purpose of the CDC template is difficult to understand. We assume it would be to clarify the staking order of capital layers and MDA triggers.
From our perspective, it is premature to include Pillar 2 elements at this stage. The BCBS is reviewing the different Pillar 2 practices and approaches among jurisdictions,
In Europe, the pillar 2 framework is still under negociation. Due to the sensitivity of information, all the jurisdictions do not require to disclose the Pillar 2 Guidance. Accordingly, banks in these jurisdictions should not be obliged to disclose this information.

Moreover, information required in line 3 is already included as part of the leverage ratio requirements for European banks. Therefore, we see no reasons, for banks to disclose capital distribution constraints separately as part of Pillar 3.
Besides, giving an additional option to the national supervisors to require the template would not promote a level playing field across EU banks and non-EU banks.

Recommendation.

We would suggest deleting the template CDC as the information related to Pillar 2 and capital distribution constraints is already available and as it is considered sensitive information. Alternatively, banks should provide narrative information as ot the nature of capital ratios that would trigger restrictions on distributions in times of stress. The narrative information should complement KM1 and KM2 templates.

Question 2: What are respondents' views on the advantages and disadvantages of expanding the scope of application of Template CC1 to resolution groups, relative to retaining its current scope of application to the consolidated group?

- **Amendments to the scope of application of disclosures on the composition of regulatory capital**

The scope of application of regulatory capital requirements and TLAC requirements are different. Namely, regulatory capital requirements currently apply on a group consolidated basis whilst TLAC requirements apply on a resolution entity or group basis. Moreover, resolution regime is driven at local level and varies across jurisdictions. Common disclosures will create undue complexity and confusion, may prove more difficult to adapt and are more prone to errors.
Accordingly, **we believe that regulatory capital disclosures should be made at a group consolidated level and should be kept separate from TLAC disclosures**. TLAC disclosures should only be provided at resolution level with a focus on the risk profile of the resolution group and subject to a materiality threshold.