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Secretariat of the Basel Committee on Banking Supervision
Bank for International Settlements
CH-4002 Basel
Switzerland
baselcommittee@bis.org

May 25, 2018

Dear Sir/Madam:

Re: *Pillar 3 disclosure requirements – updated framework*

The IBFed[1] appreciates this opportunity to comment on the Basel Committee on Banking Supervision (BCBS) proposal to revise the Basel Pillar 3 disclosure requirements and share with you our views on this issue.

The Basel Committee issued revised Pillar 3 disclosure requirements in 2015. This was followed in March 2017 by the second phase of the review. Lying before us, is the third phase of the review of the Pillar 3 framework.

IBFED supports the aim of transparency that should be accomplished by means of Pillar 3 disclosures requirements. However, we have concerns with the proposed disclosure of certain sensitive or proprietary information in phase three as described below.

At the same time, we want to emphasize that the focus must be on disclosures that are relevant for users. From the experience of banking organizations that have provided Pilar 3 disclosures for years, very few users seem to be interested in consulting Pillar 3 disclosures. Moreover, financial analysts rarely raise questions on such data.

The proposed amount of information to be disclosed increases the risk of misinformation and reduces comparability. This would be counterproductive. Examples to illustrate these concerns are provided below.

[1] The International Banking Federation (IBFed) was formed in 2004 to represent the combined views of our national banking associations. The IBFed collectively represents more than 18,000 banks, including more than two thirds of the largest 1000 banks in the world. IBFed member banks play a crucial role in supporting and promoting economic growth by managing worldwide assets of over 75 trillion Euros, by extending consumer and business credit of over 40 trillion Euros across the globe, and by collectively employing over 6 million people. The IBFed represents every major financial centre and its members' activities take place globally. This worldwide reach enables the IBFed to function as a key international forum for considering regulatory and other issues of interest to the global banking industry. For more information visit: www.ibfed.org

- We anticipate that the phase-in period including the output floor will de facto be shortened substantially due to market expectations penalising any deviations from the proposed requirements well in advance. This should not be the case. We believe there should be consistent implementation timing for the Basel III reforms globally.
- We are concerned about introducing the Standardised Approach as a benchmark for risk-weighted assets because this would erroneously lead investors to consider it to be the “correct and benchmark measure”.
- With respect to operational risk the disclosure of detailed qualitative and quantitative information about losses as proposed would not be appropriate. Disclosure would lead to undesirable consequences especially for ongoing litigation events. Also, the disclosures would compromise the confidential nature of certain losses. The detailed level of disclosure regarding the Credit Valuation Adjustments, notably the exhaustive list of the inputs used in the calculation, description of the proxy spread etc., stands in stark contradiction to the notion of confidentiality and risks the exposure of sensitive information.

We have provided more detailed comments on the proposal below. We thank you for taking our comments into consideration, and we look forward to future discussions on these issues.

Yours sincerely,

Ms Hedwige Nuyens
Managing Director
IBFed

Deborah K. Crossman

Ms. Debbie Crossman
Chair of the Prudential Supervision Working Group
IBFed

Part 1: Revisions and additions to the Pillar 3 framework arising from finalisation of the Basel III post-crisis regulatory reforms

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

The comprehensive scope of the underlying requirements may be questioned as several indices are not meaningful to readers and are not conducive to providing a valuable overview.

We consider the overall usage of Pillar III information to be low, particularly with the largest share of users being rating agencies who are already in possession of the information. Hence, it is not clear that this depth of information is needed. In addition, regulators should await the industry's response to the experiences from implementation of Expected Credit Loss Accounting (IFRS9 internationally and ASU 2016-13 in the US) before proceeding with the introduction of new requirements in this respect.

We question the need for disclosing capital distribution constraints in jurisdictions where Pillar 2 disclosures are not required as this is sensitive information, as noted in the framework. We believe sufficient information is already disclosed by those banks to allow stakeholders to determine the risk of coupon cancellations. We were pleased to learn from the Working Group on Disclosure at the outreach meeting in London that this template is not mandatory, and we request that this be reflected in the final standard.

The compromises reached on the Basel III reform package envisage that the new output floor requirements will be phased in through 2027. Given the proposed disclosures, however, there is danger that market expectations will make this phasing-in period much shorter in practice. Information in proposed Template BEN2, would make it possible to gauge the difference in many single asset classes between the risk-weighted assets calculated using an internal model and the Standardized Approach. Experience with phasing-in capital requirements under Basel III demonstrated that, regardless of transitional arrangements, the market penalizes divergence from the final target level and expects future requirements to be met from the outset. It can therefore be assumed that these disclosures would also have the effect of bringing forward the impact on regulatory capital of the final level of the floor.

<u>1.1 Revised disclosure requirements for credit risk</u>

With respect to Template CRB-A, the European Banking Authority issued template EU CR1-E with information about non-performing loans and forbearance exposures within its guidelines (EBA GL-2016/11), which had entry into force in December 2017. G-SII and O-SII entities are all required to disclose template EU CR1-E from that reporting date. U.S. banking organizations similarly already disclose extensive information on these matters in regulatory filings that are made public. However, we object to a requirement to make public the confidential and proprietary information called for in this template.

<u>1.2 Revised disclosure requirements for operational risk</u>

Given significant differences in the ways that different banks calculate granular loss information as envisioned, the extent to which the data are meaningful and comparable remains in question. The divergence would likely lead to wrong conclusions. Most significantly, this may lead to unfair and undesirable consequences from public exposure of confidential information on ongoing litigation events. Such disclosures may also be challenging for banks that may not have the data.

In addition, it is not clear how external parties can interpret a total loss figure in order to conclude on the quality of operational 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…).

Suggestions

- Annual disclosure of loss data also does not provide sufficient time to complete the internal loss data reporting and attestation process. We recommend that a one quarter lag be allowed for the calculation and reporting of the data and capital. Such a lag would allow the banks to complete their reconciliation processes.
- Table ORA: We request clarification of the term "operational risk measurement system"? Is this about any specific tools such as RCSAs, KRIs, KRMs, top and emerging risks, risk appetite, etc.?

Template OR1:

- As per section 5.1.5 of the consultative document, if a bank, concerned with proprietary and confidential information, does not disclose all the losses that drive the operational risk capital calculation, the disclosed information would give an incomplete view of its loss profile. This would impair the ability to interpret the information disclosed. As such, we question the need for disclosing historical losses under OR1 and recommend removing columns 'a' to 'j' at minimum and keeping column k along with rows 9 to 11.
- We recommend further clarification/guidance for template OR1. For example:
  - How should the number of operational losses for loss events that span across accounting years be reported?
  - What takes precedent: accounting standards vs. the Basel Committee's loss collection standards, etc.?
- We are concerned with the thresholds in the template and broad scope of operational losses that banks would be required to disclose that would not be material.

Template OR2:

We request confirmation that the "Financial Component" (amounts reported in lines 3, 3a, and 3b) follows Basel Committee reporting rather than financial reporting.

1.3 Revised disclosure requirement for leverage ratio

We have reservations about the clarity of the Business Indicator Component (BIC) calculation and advise to provide better formatting in line with balance sheet items.

1.4 Revised disclosure for credit valuation adjustment (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.

The detailed description of regulatory CVA calculations – notably the exhaustive list of the inputs used in the calculation and description of proxy spread in table CVAB would require disclosing information that is confidential and sensitive. Even if paragraph 5.1.5 in the consultation aims to allow banks not to publicly disclose confidential information, requiring banks to provide a public explanation in effect contradicts confidentiality.

Recommendation:
The granularity of inputs required for several templates would not provide meaningful information to readers. The IBFED recommends reduction of the scope and detail of quantitative CVA disclosures.

Table CVAA
Due to proprietary reasons, we request that the Basel Committee removes the requirement for banks to disclose their strategic objectives and strategies for monitoring hedge effectiveness.

1.5 New disclosure requirements to benchmark the risk-weighted asset (RWA) outcome of banks' models with RWA calculated according to the standardised approach

As proposed, institutions authorized to use internal models, would be required to publish the hypothetical risk-weighted exposure amounts under the applicable standardized approach. Inevitably, readers of Pillar 3 disclosures would see the standardized approach as a benchmark. In that point of internal models is better measurements of true risk exposures, setting the standardized approach as a standard would result in misleading interpretation of the entities' level of risk.

Overall, we have serious reservations about direct comparisons between internal model results and those under prudential standardised approaches. Internal model approaches are much more risk sensitive than standardised approaches, so it is only logical that there will be differences. A direct comparison, however, would suggest that the standardised figures are the "right" ones, especially if the internal model results produce lower risk-weighted asset figures. The evident focus in the two templates on the figures calculated under the standardized approach could lead users of the Pillar 3 report to regard these figures as the more relevant and accurate, with the result that less attention would be paid to internally modelled results.

In addition, disclosures by type of risk or type of asset would undermine the intent of phasing in the output floor until 2027. With such disclosures, starting in 2022, analysts and rating agencies would be able to compare and restate the capital requirements of the banks that are using internal models into the standardised approach values, without any floor. Judging by past experience, market pressure would force the banks to forego phase-in and implement immediately.

Suggestions:

- We have serious doubts about the need for these disclosures. We question the need for A-IRB banks to disclose standardised risk-weighted assets, which would distract from internally modelled values. We do not believe that A-IRB banks should be compared against standardised approach values.
- The disclosure should not enable the standardised approach to serve as a benchmark, and de facto a floor for capital.
- If the Basel Committee decides to introduce templates BEN 1 and BEN2, we suggest the following amendment from the perspective of practice.

Template BEN1:

- We suggest insertion in column heading d the requirement that the column equal row b + c to support understandability.
- For Operational Risk risk-weighted assets benchmarking, we understand that "Actual RWA calculated under standardised approaches" (6c) and "RWA under full standardised

approach for benchmarking" (6d) will have the same amounts as internal model, are no longer applicable. Please confirm.

Template BEN2:

- We suggest insertion in column heading d requirement that the column equals row b + c to support understandability.
- Linkage to template BEN1 should be required to avoid confusion of the placement of Equity investment in funds in row 7 of that template and not as credit risk.

1.6 Revised disclosure requirements for overview templates on risk management, RWA and key prudential metrics

Suggestion:

- Template OV1: Row 26 should include reference to the fact that it is a percentage.

Part 2: New disclosure requirements on asset encumbrance

We are concerned about the asset encumbrance disclosure requirements in the sense that the information, albeit optional, is sensitive and may very well hamper the level playing field in some jurisdictions, e.g. non-EU banks. If asset encumbrance disclosure is considered necessary, we believe it important to have a clear and standardized format that is consistent with the EDTF recommendations.

We appreciate the flexibility in the proposed Template ENC: Asset encumbrance that provides supervisors with latitude, for example, on whether or not to require certain columns.

Part 3: New disclosure requirements on capital distribution constraints

We were pleased to learn from the Working Group on Disclosure at the outreach meeting that the CDC template is not mandatory and we request that this be reflected in the final standard.

Given the sensitivity of Pillar 2 information, we agree that this template should not be required in jurisdictions where Pillar 2 disclosure is not required. Since banks already disclose required minimum capital ratios under Pillar 1 this additional level of disclosure would be discussed as part of their qualitative discussion on capital management.

Suggestion:

- In Europe, we recommend the margin of discretion should solely apply to the ECB in lieu of national supervisors for purposes of comparability and in order to achieve the fulfilment of a level playing field.
- There is no reason for disclosure of capital distribution constraints separately. In Europe, banks are required to disclose in contrast to other banks, and we therefore have severe concerns that the level playing field will be at risk in a requirement for disclosing sensitive information. Further, the complication of implementing a template that is not applicable globally would mean disclosures that cannot be compared across all disclosing institutions. The information is only relevant and meaningful to supervisors in the face of major threat, and in these situations s in which the information would be required by them on an ad-hoc basis.
- If this disclosure is pursued, we recommend that additional capital rows be inserted to highlight the required frameworks for which additional capital is required to be held (e.g.

jurisdictions where Pillar 2 G-SIB loss absorbency requirements and G-SIB leverage requirements are disclosed) for ease of transparency and reader understandability

Part 4: Amendments to the scope of application on the composition of regulatory capital

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?

We believe that reopening issues that have already been decided does not set a good precedent for future discussions, as it raises concerns about the stability of the decisions already taken and creates regulatory uncertainty.

We agree with the Basel Committee that requiring a resolution group to disclose Template CC1 would be "artificial", as no regulatory capital requirement is applied at that level. The CET1 rules are designed for the prudential world. The CC1 template requires a breakdown of the constituent elements of a bank´s capital. Regulatory capital is designed under specific prudential rules with a different scope, nature and perimeter than those that govern the resolution requirements. Some examples are:

- Some instruments do not count towards TLAC/MREL as they do towards capital, and vice versa.
- The excess of provisions that can count towards T2 is determined according to the prudential perimeter, which is not the same as the resolution one;
- The equity holdings of the subsidiaries are weighted according to the capital rules while the treatment differs in TLAC/MREL.

National capital requirements are set according to local rules. Even under Basel III local rules differ among members. Requiring capital composition disclosure at the resolution group level risks misunderstanding that such disclosure is a minimum requirement. Usually, disclosure requirements are built on prudential requirements already established. However, in this case, a disclosure is being discussed with no prudential requirement behind it, which confuse interpretation. Investors could understand this as a requirement and apply the same interpretation rules as when analysing the CC1 template at the consolidated level.

Given that only Multi Point of Entry (MPE) groups would face this requirement this would lead to a situation where Single Point of Entry (SPE) banks provide one single template and MPE banks provide several templates, although only the consolidated version would correspond to a prudential requirement. The rest would be merely an artificial concept built on many hypotheses, which could be misinterpreted by the market as an assessment of the capital position of the resolution group where there is no such capital position.

Furthermore, investors already have all the information they need in this regard. The TLAC/MREL1 template provides broad details of the composition of TLAC/MREL at the resolution group level. This template comprises regulatory and non-regulatory capital elements. In addition, the regulatory capital item includes the most important determinants of its composition: CET1, AT1 and T2. This is the information that investors need. A further breakdown of CET1 does not help investors to better understand the capital position of the resolution group. On the contrary, as stated above, it increases confusion.

MPE banks have regulatory capital but not TLAC/MREL requirements at the consolidated group level. A different perimeter applies with regard to TLAC/MREL and capital requirements. Combining the two of them, CC1 and TLAC/MREL1, at resolution group level would be particularly confusing for investors.

According to the BIS (Pillar 3 consultation), the consolidation perimeter of a resolution group may not coincide with that applied to banking groups under the Basel framework, particularly in terms of the coverage of group entities (which applies to both MPE and SPE), given the different treatment of insurance subsidiaries in both frameworks.

Additionally, the BIS (Pillar 3 consultation) states that disclosure of requirements at the resolution group level could lead to a greater disclosure burden for G-SIIs with an MPE resolution strategy putting them at a clear disadvantage compared to SPE banks. Not only would MPE banks have to cope with greater disclosure requirements, they would also have to face an increase in administrative costs in order to start reporting data at a new level of consolidation.

All in all, the prudential and the resolution frameworks share more differences than similarities:

- Their objectives are different
- There are differences in the scope of application of both frameworks. In principle, those subsidiaries that would be liquidated are excluded from the resolution perimeter, and.
- The TLAC/MREL term sheet does not apply at the solo-level but to the resolution group levels which responds to specific sub-consolidated units that do not always correspond to the capital disclosure units.