24 June 2009

Follow-up review of banks' transparency in their 2008 audited annual reports

Executive summary

This report provides an overview of the outcome of the monitoring work that CEBS has carried out with respect to banks' transparency. It follows a series of efforts that CEBS has carried out in the past as part of the work the EU institutions agreed to carry out in response to the November G20 Declaration and that have led to the publication of CEBS's good practices in June 2008 and two related follow-up assessments.

The present report assesses the 2008 year-end disclosures of a sample of EU (and to a lesser extent of non-EU) banks and reveals that the CEBS June 2008 good practices have been covered quite extensively in many cases. As previously the disclosures vary to some extent in terms of the level of detail but generally the granularity seems to be in line with the way banks have been affected by the crisis.

The report nevertheless identifies a number of areas within the CEBS June 2008 good practices where disclosures could be improved. These are notably disclosures on:

- fair value measurement; more particularly disclosures on valuation models and on the underlying assumptions and adjustments could be further improved;
- methodologies used to determine the impact of own credit spreads and to account for day one differences; and
- disclosures on consolidated and in particular derecognised entities and related exposures;

Overall, the disclosures of EU banks are very similar to those of their non-EU peers. Where diversity has been observed, it can often be related to differences in disclosure requirements.

The development of the crisis also led CEBS to look beyond its June 2008 good practices to identify[1] a number of areas that institutions should pay particular attention to in order to ensure that their disclosures reflect the most recent developments, in particular:

- impairment of financial instruments and of goodwill;
- disclosures on 'new' areas or exposures affected by crisis.

[1] Annex 1 sets out the good practices identified in the CEBS June 2008 report and highlights items that have been included to address the financial crisis.

CEBS observed that some banks' disclosures were not developed enough to highlight the impact of the crisis. In addition, it is felt that in some cases the disclosures have not been sufficiently adapted to reflect the spreading out of the crisis to other markets and activities.

As expected there has been a significant increase of disclosures compared to previous analyses. While CEBS does not advocate that disclosures in those reports are as comprehensive as those provided in annual reports, the findings of the present report could assist banks in assessing whether their quarterly and interim disclosures provide room for improvements.

Some banks should also consider the need for efforts to ensure that disclosures are provided on a timely basis and, if necessary, outside the usual publication schedule.

The report also raises a number of issues with regard to the presentation and structure of disclosures that could assist banks in improving the quality of their disclosures.

Prior to the publication CEBS 'tested' its findings of the report(s) with the industry at a public hearing. On the whole, the findings did not give rise to major objections from the side of participants.

Rather than preparing a new assessment, CEBS will, as a next step, develop a set of high-level disclosure principles to help banks prepare disclosures covering areas or activities that warrant particular attention.

The development of such high-level principles based on the good practices published in June 2008 and on the findings of this and previous follow-up assessments, is considered to provide a helpful tool to guide banks in providing adequate disclosures to the markets on areas or activities under stress.

The high-level principles are intended to be fully compatible and consistent with disclosure requirements developed by other fora or set out in prudential regulations (notably Pillar 3) and in accounting standards. This should help address concerns expressed by industry representatives on how CEBS's June 2008 good practices and related follow-up findings interact with other initiatives and existing disclosure requirements.

The development of these high-level principles will be submitted to the usual CEBS due process, which foresees a public consultation.

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I. Introduction

The present report provides an overview of the outcome of the additional monitoring work that CEBS has carried out with respect to banks' transparency.

Past efforts resulted in i) CEBS Report on banks' transparency on activities and products affected by the recent market turmoil published on 18 June 2008, ii) the related follow-up report published in October 2008 assessing how the good practices identified in CEBS's June 2008 report had been implemented, and lastly iii) the Follow-up review of banks' transparency in their 2008 4th quarter and preliminary year-end results published in March 2009.

This work is part of the work the EU institutions agreed to carry out in response to the November G20 Declaration and also reflects a commitment made in CEBS's October 2008 report to analyse banks' 2008 year-end disclosures.

Recent developments in the area of accounting – in particular the changes in the reclassification requirements in IAS 39 – and the generalisation of the crisis, led CEBS to look not only how banks' disclosures addressed the elements included in the CEBS June 2008 good practices but also to look at disclosures on areas that have been affected by more recent developments of the crisis.

The present report provides the final outcome of this work. In line with the July 2008 ECOFIN conclusions CEBS also analysed the disclosures provided under Pillar 3.[2] The outcome of that analysis is included in a separate report (published simultaneously).

II. Background

CEBS's June 2008 report encompassed not only disclosures on the impacts of the market turmoil on exposures levels and on results (as in the Financial Stability Forum (FSF) recommendations), but also information on business models, risk management practices and accounting and valuation practices.

The main findings of that report highlighted a number of weaknesses in the disclosures made by banks, particularly with regard to business models, risk management practices and accounting and valuation practices. This led CEBS to identify a set of good practices for these areas, which have been used as a benchmark for this report.

In the follow-up report published in October 2008, CEBS concluded that the banks' interim disclosures in 2008 on the impact of the market turmoil and on exposure levels had improved to reach a generally satisfactory level. By contrast, disclosures on business models and, to a lesser extent, disclosures on risk management and on accounting and valuation practices still had scope for significant improvements.

The March 2009 CEBS report concluded that banks' transparency in their 2008 last quarter and preliminary year-end results did not show significant improvements.

[2] The July 2008 ECOFIN conclusions set out ' It [the Council] looks forward to the review by CEBS of its recommendations on banks' disclosure in 2009 within the scope of pillar III of the Capital Requirements Directive.'

The findings revealed that as regards quantitative disclosures – on impacts and exposure levels – banks continue to provide satisfactory information. For qualitative disclosures – on business models and risk management – there is still room for improvement.

CEBS also expressed the view that, especially for qualitative disclosures, further progress needs to be made. This is deemed increasingly important for business models, which often are directly impacted by the financial crisis. The findings also underline the importance of disclosures on risks and risk management, as the crisis has raised some questions on whether institutions had sufficient command over the risks they engaged in, especially under these adverse conditions.

However, the 2008 last quarter and preliminary year-end reports generally contain more limited disclosures than other reports. In order to provide a comprehensive assessment, it was deemed necessary to complement the analysis of the 2008 last quarter and preliminary year-end disclosures with an analysis of the disclosures provided in the 2008 annual reports (AR), which is the subject of this report.

III. Objective and methodological remarks

The objective of this report is to assess how the good practices put forward in CEBS's June 2008 report have been implemented in banks' audited 2008 annual reports and how they compare to previous disclosures, particularly with regard to areas that, in CEBS's October 2008 report, were identified as providing scope for improvement.

The analysis first addresses the CEBS June 2008 good practices dealing primarily with sub-prime related activities and exposures. In addition, given the wider nature of the crisis the analysis looks also at the disclosures that have been made to cover new areas affected by the crisis and the impact these had on banks' performances and exposures.

As a result of these developments the discussion addresses issues such as liquidity risk management, state interventions and other measures such as recapitalisations, but also disclosures relating to recent changes in accounting such as the reclassification amendments in IAS 39 and related changes in IFRS 7 requirements.

The analysis is based on the same approach that was applied in previous reports – i.e. the disclosures of a sample of banks were compared against the good practices set out in CEBS's June 2008 report. To reflect the expanded scope as set out above the table in Annex 1, which reproduces the good practices, has been amended.[3]

To ensure comparability with the previous exercises, this analysis relies largely on the sample of banks that was used previously[4]. The report has been based on the

[3] Amendments to the tables have been underlined in the annex

[4] The list of banks has been included in annex 2. The sample changed in comparison to the previous assessment because four banks, which had been analysed in a previous assessment of the annual reports, did not provide last quarter or preliminary year-end report. There have also been changes as a result of mergers and acquisitions or other structural changes. The sample furthermore includes two additional non-EU banks in order to be in a better position to situate the disclosures of the EU institutions.

2008 annual reports of 23 (previously 19) large banks with cross-border activities, 18 of which (previously 14) have their headquarters in the EU. The findings cover all the institutions irrespective of their geographical origin but address, where relevant, differences that have been observed between EU banks and their non-EU counterparts.

The nature of the exercise and the analysis, where individual supervisors reviewed the disclosures of certain banks against a common benchmark example – implies a certain amount of judgement. To address this, the analysis of the individual assessments has been centralised and verified through cross-checks with members providing the input. In addition supervisors had been asked to check the individual assessments with the institutions included in the sample to ensure that CEBS's view of the disclosures is in line with that of the institution's own perception.

Additionally, for a number of significant issues CEBS cross-analysed the disclosures of a representative cross-section of institutions to ensure that the findings are pertinent and to allow the identification of best practice examples.

IV. Main findings of the analysis of the audited annual reports

The following paragraphs discuss the main observations stemming from the analysis of the disclosures of the banks included in the sample and identify areas for which disclosures could be enhanced.

In addition the discussion provides, for certain areas, disclosures that are being considered as best practice examples. For many banks these could serve as useful guidance to increase the usefulness of their disclosures.

i) Impact of the market turmoil

a) Assessment of CEBS good practices

As regards the disclosures on the impact of the market turmoil the findings can be summarised in the following table:

Level of detail (in general) of disclosures	High	Satisfactory	Low
% of banks	70%	24%	4%
Compared to previous AR, the disclosures are	Improved	Similar	Less detailed
% of banks	32%	59%	9%

The description of results and in particular losses (both in quantitative and qualitative terms), the related reasons and factors responsible for the incurred impact, and related breakdowns have been well disclosed.

For a number of banks further progress could be made in the following areas:

- Disclosures on the impact of credit spreads on own liabilities: In some cases the level of detail of disclosures regarding the methodology used to determine the impact of credit spreads on own liabilities could improve.

  Moreover, even if it is not explicitly required by IFRS 7, banks could disclose the sources of inputs used in the valuation. Indeed, the IASB Expert Advisory panel measuring and disclosing fair value of financial instruments in markets that are no longer active (October 2008) notes: "given the scrutiny applied to the movements in the fair value of liabilities due to changes in an entity's own credit risk, in addition to the required disclosures of how the amount was calculated, disclosing the source of inputs used to calculate the movement provides transparency about the uncertainty of that amount". In addition, according to IAS 1, entities shall disclose the significant accounting policies and the major sources of estimation uncertainty.

  CEBS already mentioned in its report on valuation of illiquid assets (June 2008) the fact "that institutions shall create awareness in the market that in the event of an improvement in market conditions previously recorded gains stemming from financial liabilities (…) will be absorbed by corresponding loss".

  As best practice example CEBS has identified the following disclosure that:

  - *provides detailed information on valuation methodology of own debt*
  - *explicitly mentions that "gains and losses arising from changes in the credit spread of liabilities issued by the institutions reverse over the contractual life of the debt, provided that the debt is not repaid early".*

  Finally, IFRS 7 paragraph 10 requires disclosure of the cumulative amount of fair value change that is attributable to changes in the entity's own credit for instruments designated at fair value through profit or loss. This has not been systematically disclosed

- More generally, disclosures on the impacts of the crisis between periods could be provided more systematically together with distinctions between realised and unrealised losses. This information, although not required by IFRS 7, has been observed in a number of cases and provides helpful insight on how the situation of institutions has developed between two reporting periods and how exposures or risks have changed as a result of asset sales, transfers, write-downs or write-offs. Ideally, disclosures would explain how these changes have affected results (with a breakdown of whether the impacts are related to valuation differences or write-downs – i.e. unrealised – or the result of a write-off or a sale (or transfer) of assets – i.e. realised.

- Similarly, information on potential future losses (in case of a further downturn) or the effect of a market recovery could be provided more systematically in order to allow for an assessment of an institution's future performance. Some institutions have provided this information by including a sensitivity or scenario analysis or by means of qualitative information.

b. Other issues

Moreover, CEBS considers that, with the wider scope of the crisis, banks' disclosures could be further improved beyond what is covered by the CEBS June 2008 good practices to provide:

- Detailed data on types of sensitive exposures beyond the initial exposures affected by the sub-prime crisis (such as, for example, hedge funds, Corporate Collateralised Debt Oobligations (CDOs), Collateralised Loan Obligations (CLOs) etc) or on new areas of concern such as impairment or exposures to other guarantors than monoline insurers such as Credit Default Protection Corporates (CDPC), in order to ensure that disclosures adequately reflect the spreading out of the crisis to other markets and activities.
- For available for sale instruments, a breakdown of unrealised gains and losses by asset category (equity, debt instruments, loans) to allow users to assess the evolution of the value of these instruments.

ii) Exposure levels and types

a) Assessment of CEBS good practices

As regards the disclosures on the exposure levels and types the findings can be summarised in the following table:

Level of detail (in general) of disclosures	High	Satisfactory	Low
% of banks	57%	39%	4%
Compared to previous AR, the disclosures are	Improved	Similar	Less detailed
% of banks	32%	59%	9%

The situation described under i) is very similar for the level of detail observed on exposure levels and types.

Most areas covered in the CEBS good practices have been covered reasonably well although the levels of detail and the focus of the information differs in accordance with the size of the impact.

In some cases, the disclosures could be further developed in a number of areas. These include:

- The level of detail of information on exposures for instruments that are not consolidated (or that have been derecognised).

  CEBS has noted some best practice disclosures, with comprehensive information on consolidation criteria and quantitative information on consolidated and not consolidated Special Purpose Entities (SPEs).

  In this context, it has been observed that the disclosures of non-EU banks were more detailed that those of their EU counterparts. It is deemed that this difference is mainly related to the fact that local disclosure requirements on structured entities are very detailed.

- Disclosures on the nominal and fair value of the assets underlying the structured products (as well as on their characteristics) in order to enable users to assess the sources and potential for future risks.
- The level of detail as regard information relating to guarantors. While exposures to monoline insurers have been properly disclosed, exposures relating to Credit Derivative Product Company (CDPC) for instance have not been provided systematically.

As best practice example CEBS has identified the following disclosures which provide:

- o *an explanation of the CDPCs function and the risks involved;*
- o *notional and fair value as well as amounts of credit risk adjustments.*

b) Other issues

Moreover CEBS considers that, with the wider scope of the crisis, banks' disclosures could be further improved beyond what is covered in the scope of the CEBS good practices to include exposures to areas and businesses that have been affected by the crisis indirectly or with recent effect. Banks should provide adequate insight on some areas or type of transactions that have more recently been affected by the crisis (e.g. emerging markets, investment and hedge funds).

iii) Accounting policies: valuation, impairment and reclassification issues

The introduction of some of the accounting changes in the course of the crisis led CEBS to cover the related disclosures in its analysis. In particular CEBS analysed institutions' disclosures with respect to the changes in IAS 39 and IFRS 7 regarding reclassification.

With the development of the crisis, increased focus has also been put on impairment issues. These points have been addressed in addition to the accounting related points already covered in the CEBS good practices.

a) Valuation and related issues

As regards the disclosures on valuation and other issues the findings can be summarised in the table below:

Level of detail (in general) of disclosures	High	Satisfactory	Low
% of banks	61%	35%	4%
Compared to previous AR, the disclosures are	Improved	Similar	Less detailed
% of banks	36%	64%	0%

Most areas covered in the CEBS June 2008 good practices have been covered reasonably by the banks.

There are however a number of areas where further improvements could be made:

- Disclosures on valuation uncertainty:
    - Disclosures on modeling techniques (for different instruments) could be improved in some cases; in particular the main conceptual/theoretical foundations on which the models are designed, its underlying assumptions and the adjustments made to fair values. With regard to the latter it would be particularly informative to get an idea of their magnitude. To the extent that uncertainties associated with the use of model-based valuation (both level 2 and 3), which are predominantly addressed through use of model reserves, are material, quantitative and qualitative information on those reserves would be useful.
    - Sensitivity analyses for level 3 fair values have been provided in a number of cases, although the disclosure was often limited to the impact on total assets and liabilities. Also the assumptions underlying the different scenarios were not always specific enough (or the basis for using the assumptions and inputs). For example, some banks have provided the potential effect of a change of specific valuation assumptions whereas others have referred to “a reasonable change in assumptions”.

      As best practice examples CEBS has identified the following disclosures of a number of banks which provide:

        - *relevant description of valuation techniques for instruments classified in level 2 and 3 of the fair value hierarchy;*
        - *significant information on valuation assumptions similar to a glossary to help understand the impact of changes in significant inputs (volatility, correlation, spreads to discount rates); and*
        - *pertinent disclosures of underlying macroeconomic scenarios*.

      It is worth noting in this context that the disclosures on sensitivity analyses of EU banks were in general more detailed than those of their non-EU peers (notably for exposures directly affected by the crisis).
- Disclosures on fair value hierarchy: a number of banks provide quantitative information on the three levels of the fair value hierarchy for instruments measured at fair value through profit or loss, even if it is not mandatory under IFRS for year-end 2008. In addition, bank could provide information on the policy for classifying financial instruments in the different level of the fair value hierarchy.
- Level of granularity regarding the use of the fair value hierarchy levels for different financial instruments categories and migration between fair value levels.

As best practice examples CEBS has identified the following disclosures provided by a number of banks:

- *a table with a breakdown of financial instruments under level , including comparative information;*
- *a breakdown of the fair value hierarchy by types of instruments;*
- *migrations between the levels 2 and 3 of the fair value hierarchy (even though this information was not yet mandatory in 2008)*

Some of the non-EU banks provided very granular information on the distribution of financial instruments by fair value levels (with a special focus on level 3) and detailed descriptions of valuation methodologies. This can be explained by the fact that these entities are subject to very specific disclosure requirements set out in the accounting standards.

- Policies for the recognition of day one differences, where material: For some banks this information is entirely missing although it provides helpful insight to users.

Best practice examples provide explanations on how the current market situation (unobservable parameters due to the lack of liquidity) impacts the recognition of day one differences, information on the policies and the controls that are in place and on how practices change when input becomes observable.

b) Impairment

- Disclosure on methodology (and assumptions) used to determine collective provisions under the IAS 39 impairment rules could be provided in a more detailed manner.
- Disclosures on the methodology for impairment on equity instruments is not sufficiently detailed; it appears notably that many banks do not provide the quantitative criteria used to determine whether there is an objective evidence of impairment for quoted equity instruments (notably the quantitative triggers used to qualify the significant or prolonged decline of an equity instrument below its cost).
- Institutions could improve their disclosures on the methodology and the assumptions used for the impairment test for goodwill. This information is relevant in the current context given the significant increase in 2008 of the amount of impaired goodwill. Banks could provide more detailed information about the key assumptions used to determine the future cash flows of the cash generating units (notably as regards the actuarial rate in use).

c) Reclassification issues

As regards the disclosures on the reclassification of assets in application of the recent amendments to IAS 39 it appears that 20 out of 23 banks made use of these provisions and at the same time provided detailed disclosures in that respect. The three (EU) institutions that they did not make use of the reclassification provisions explicitly disclosed that fact.

Generally speaking banks followed the disclosure requirements made in IFRS 7. However, the presentation of the impact of the reclassifications was not homogenous between banks, with some banks presenting the impacts including interest gains and others only disclosing the impact relating to changes in fair value of reclassified assets.

CEBS observed that in some cases banks went beyond the minimum requirements and identified a number of practices that could be used more widely, such as:

- Information on the capacity and intent to keep reclassified instruments until maturity or in the foreseeable future. Even though this is not explicitly required under IFRS 7, this information is helpful to assess whether reclassifications are justified.
- Detailed description of the type and nature of the reclassified assets (and the related granularity) in order to ensure clarity about the assets that were subject to the reclassifications.
- Although this information is currently not required under IFRS 7 a few banks have provided specific information on the impairment amount recognised on transferred assets. This disclosure is meaningful for users to obtain knowledge regarding the evolution of reclassified assets.

Among the non-EU banks there are three banks that made reclassifications in line with the provisions of local GAAP and provided (except for one) detailed disclosures.

iv) Business models

a) Assessment of CEBS good practices

As regards the disclosures on business models the findings can be summarised in the following table:

Level of detail (in general) of disclosures	High	Satisfactory	Low
% of banks	35%	57%	9%
Compared to previous AR, the disclosures are	Improved	Similar	Less detailed
% of banks	23%	77%	0%

Banks' annual reports disclosures covered the description of the business models and related changes as a result of the crisis relatively well. A similar observation can be made for the description of the banks' strategy and objectives. Banks also provided generally speaking good or adequate disclosures on the link between the business model and the degree of vulnerability to or the impact of the crisis.

Further progress should be made with respect to the following:

- Disclosures on activity changes or reorientations could at times be explained or justified more clearly.

  CEBS noted in that context some best practice examples, where banks clearly isolated the impact of ceased activities which could be meaningful for users to assess the result of continuing activities and future cash flows.

- Description of the type of activities and their importance for and contribution to business. The information was sometimes very generic without providing sufficient clarity on how activities contribute to the bank's business and revenues, and how revenues are generated, which is particularly relevant for the exposures that contributed to the problems.

It has also been observed that for some of the non-EU banks the discussion on business models appeared less detailed than for EU banks.

b) Other issues

Moreover CEBS considers that, with the wider scope of the crisis, disclosures could be improved by providing:

- Disclosures on the strategies and role taken with regard to SPEs and the reasons leading banks to support (and consolidate or not) some of these entities could be developed.
- Sufficient explanations on the rationale and the effects of that exposures reductions and/or transfers.
- Information on new products that have been developed during the crisis. In that context, one example that has been identified provided information on new instruments (such as unemployment insurances) to ensure that users have sufficient information on related exposures and risks.

v) Risks and risk management

a) Assessment of CEBS good practices

As regards the disclosures on risks and risk management the findings can be summarised in the following table:

Level of detail (in general) of disclosures	High	Satisfactory	Low
% of banks	65%	35%	0%
Compared to previous AR, the disclosures are	Improved	Similar	Less detailed
% of banks	59%	41%	0%

As regards the level of disclosures in the area of risks and risk management, most banks covered the elements included in the CEBS good practices reasonably well. In a number of cases banks enhanced their disclosures on risk management (notably on liquidity risk). CEBS notes and welcomes that in a number of cases institutions included a discussion of management of interest rate risk and currency risk, which is possibly related to the first delivery of the Pillar 3 disclosure requirement (which are subject to a dedicated analysis).

Further progress could however be made with respect to the following items:

- For all the different risks banks could enhance their disclosures (in particular qualitative information) on applicable limits and related breaches and supplement them with the relevant explanations. Furthermore the disclosures on stress testing could be developed. In case this disclosure (especially quantitative information) is of proprietary nature, there should be at least sufficient qualitative explanations to allow users to gain sufficient understanding.
- Further progress could also be made regarding the disclosures of liquidity risk management. While most institutions include a discussion of the methods used to assess and manage liquidity risk, there was little information on liquidity risk position and breakdown of funding sources, and other indicators used to manage this risk (such as basic qualitative information on liquidity buffers and survival periods).
- In line with IFRS 7, many banks already provide quantitative disclosures on the contractual maturities of assets and liabilities. In that regard CEBS noted that some banks have provided information on maturity buckets with duration under three months such as demand liabilities and with duration under one month. In some cases quantitative information could be supplemented with information on underlying assumptions (including the treatment of liabilities that have no contractual maturities, the treatment of derivatives).

In the area of disclosures on liquidity risk, it is deemed that some EU banks provided more detailed information than non-EU peers.

b) Other issues

Moreover CEBS considers that, with the wider scope of the crisis, disclosures could be further improved by providing more detailed information on risk profiles of certain portfolios or exposures (e.g. on credit card exposures, hedge funds, which are some of the areas that have more recently been affected by the crisis).

vi) Other disclosure issues

a) State interventions and recapitalisation measures

In 2008, with the exacerbation of the financial crisis, many governments set up national schemes or measures to provide either direct (through capital injections or asset transfer schemes) or indirect (by issuing guarantees) support to ailing banks or to financial system in general. Other banks tried to recapitalise in the market. Given the importance of some of the interventions and the need for related transparency it was deemed appropriate to review in the analysis the disclosures that banks made in that respect.

The analysis shows that 17 institutions (out of 23) benefited from state interventions. In most cases (10) related disclosures were very detailed. 5 banks explicitly mentioned that they did not resort to state interventions, whereas in one case the disclosures were not conclusive.

The situation is similar as regards recapitalisations, where 16 institutions (out of 23) have been recapitalised and provided in the majority of cases (9) very detailed disclosures. One bank has only mentioned recapitalisation measures but did not provide any elaborations. Five banks explicitly mentioned that they did not resort to such measures.

Although for many banks disclosures were rather explicit, the information could in some cases be more focused on describing the interventions and measures in more detail.

Additionally disclosures could in some cases have been clearer on whether the stabilising measures are conditional to specific commitments (regarding compensation and benefits, governance or distribution of credit).

Also, it is not always clear whether as a result of the support, in particular in the case of transfers of toxic asset to dedicated funds, whether the institution bears any residual risks in relation to the transferred assets.

b) Remuneration issues

In many cases, banks provided detailed information on compensation or remuneration schemes and related changes. Often the information was however focused on key management personnel and did not deal with operational staff (and in particular members of the trading desks). CEBS considers that it is important that these topics are adequately covered by banks' disclosures. This is in line with the CEBS's principles on remuneration published in April 2009, and in particular with general principle ii. stipulating that *'The remuneration policy should be transparent internally and adequately disclosed externally.'*

vii) Presentation issues

As regards presentational and structural aspects of the disclosures CEBS made the following observations, which could assist banks in improving the quality of the information they provide:

a) Description of disclosure policy and principle

13 out of 23 banks provide information, with varying level of detail, on the disclosure policy and principles. This information should be systematically provided for all institutions.

b) Structure of the disclosures

In most cases disclosures relevant for the CEBS good practices are provided in various parts of the reports. It can be observed for example that information on the business model is often included in the strategic part, whereas information on impacts and on exposures is disclosed in the performance discussion. Often the exposures and information on write-downs are also given in the risk and risk management disclosures and in the notes to the financial statements. Other banks discuss most of the aspects (with the logical exception of the accounting policies) in one section dedicated to the financial crisis.

CEBS does not want to advocate one specific presentation (disclosures included in one dedicated section or in various parts of the reports) as long as the information is clearly traceable and adequately cross-referenced. This was a problem in a few cases, where disclosures lacked structure and were difficult to follow.

In one case the disclosures in the financial statements were not entirely in line with the discussions provided in the business, performance and /or risk sections (notably as regards changes in business activities and instruments).

It is therefore suggested that banks take extra care to ensure that the different parts of their reports are clear and consistent and allow readers to find easily the information they are interested in. For that purpose it might be worthwhile including a guide to disclosures dealing more specifically with crisis-related issues.

c) Clarity of disclosures

Most banks' disclosures are appropriately balanced between narrative disclosures and are supplemented by clear and comprehensible tables or graphs. There are however cases where the disclosures provide some room for improvement in terms of clarity. This is especially the case where much of the quantitative information is provided in narrative form.

In most cases the disclosures are supplemented with clear explanations for the terminology used. In a few limited examples specific glossaries have been provided. There are however also a few instances where there was lack of clarity regarding the terminology used.

Annex 1 – June 2008 CEBS's good practices (adapted)

CEBS good practices *	**Level of detail of disclosures**	**Comparison to previous**	**Observations/ Comments**
Business model **<u>(for activities affected by the financial crisis)</u>** • Description of the business model (i.e. of the reasons for engaging in activities and of the contribution to value creation process) and, if applicable of any changes made (e.g. as a result of crisis). • <u>Link between business model and degree of vulnerability to the crisis (in relation with the changes in operating income and in net income)</u> • Description of strategies and objectives. • Description of importance of activities and contribution to business (including a discussion in quantitative terms). • Description on the type of activities including a description of the instruments as well as of their functioning and qualifying criteria that products/ investments have to meet. • Description of the role and the extent of involvement of the institution, i.e. commitments and obligations.			
Risks and risk management **<u>(for activities affected by the financial crisis)</u>** • Description of the nature and extent of risks incurred in relation to the activities and instruments <u>/ coverage of credit risk, market risk, operational risk</u> • Description of risk management practices of relevance to the activities, of any identified weaknesses of any corrective measures that have been taken to address these. • In the current crisis, particular attention should be given to liquidity risk, <u>including:</u> • <u>qualitative description of risk management practices for liquidity risk (internal governance, systems, internal controls, expertise of personnel, internal methodologies…)</u> • <u>quantitative information on risk management practices for liquidity risk (contractual and expected maturities…)</u> • <u>qualitative information on liquidity management in periods of stress conditions (liquidity stress-testing, survival periods if no access to the markets, contingency funding…)</u>			

CEBS good practices *	Level of detail of disclosures	Comparison to previous	Observations/ Comments
Impact of the crisis on results <u>(for activities affected by the financial crisis)</u> • Qualitative and quantitative description of results, with a focus on losses (where applicable) and write-downs impacting the results. • Breakdown of the write-downs/losses by types of products and instruments affected by the crisis <u>(reduced)</u>. • Description of the reasons and factors responsible for the impact incurred. • Comparison of i) impacts between (relevant) periods and of ii) income statement balances before and after the impact of the crisis. • Distinction of write-downs between realised and unrealised amounts. • Description of the influence the crisis had on the firm's share price. • Disclosure of maximum loss risk and description how the institution's situation could be affected by a further downturn or by a market recovery. • Disclosure of impact of credit spread movements for own liabilities on results and on the methods used to determine this impact.			

CEBS good practices *	**Level of detail of disclosures**	**Comparison to previous**	**Observations/ Comments**
Exposure levels and types **<u>(for activities affected by the financial crisis)</u>** • Nominal amount (or amortised cost) and fair values of outstanding exposures. • Information on credit protection (e.g. through credit default swaps) and its effect on exposures. • Information on the products. • Granular disclosures of exposures with different breakdowns provided;(level of seniority and/ or quality, geographic origin, type of exposures, product characteristics; <u>(reduced)</u> • Movement schedules of exposures between relevant reporting periods and the underlying reasons (sales, disposals, purchases etc.). • Discussion of exposures that have not been consolidated (or that have been recognised in the course of the crisis) and the related reasons. • <u>Exposure related to a deterioration of the guarantee received (credit quality of monoline insurers and others, changes in real estate market price:</u>			

CEBS good practices *	Level of detail of disclosures	Comparison to previous	Observations/ Comments
Accounting policies and valuation issues (for activities affected by the financial crisis) • Classification of the transactions for accounting purposes and the related accounting treatment. • Detailed disclosures on fair values of financial instruments (financial instruments to which fair values are applied; fair value hierarchy; treatment of day one differences; use of the fair value option and related amounts). • Disclosures on the modelling techniques used for the valuation of financial instruments, (description of modelling techniques and of the instruments to which they are applied; description of valuation processes, type of adjustments applied to reflect model risk and other valuation uncertainties; sensitivity of fair values; and stress scenarios). • Disclosures on consolidation of SPEs and other vehicles (such as VIEs) and relationship with unconsolidated SPEs (nature of involvement, level of exposure, reasons for not consolidating…). • Description of the approach retained for the impairment of financial instruments (notably for the collective and individual impairment of loans, and the impairment of equity instruments) • Description of the approach retained for the impairment of goodwill.			
Reclassification of financial instruments • Clear information on the reasons for reclassification • Clear information on the nature of financial instruments reclassified • Impact on results with the distinction between the changes in fair value that would have been recognised if the reclassification has not been made and the interest income (or other incomes and expenses) that has been recognised and would not have been if the reclassification has not been made.			
Other disclosure aspects • Description of government interventions e.g. by means of capital injections, asset sell-offs or other state support (such as guarantees) or interventions (such as nationalisations) • Disclosures on recapitalisations			

CEBS good practices *	**Level of detail of disclosures**	**Comparison to previous**	**Observations/ Comments**
Presentation issues • Description of disclosure policies and of the principles that are used for disclosures and financial reporting. • Relevant disclosures for the understanding of an institution's involvement in a certain activity should as far as possible be provided in one place. • Where information is spread between different parts or sources clear cross-references should be provided to allow the interested reader to navigate between the parts. • Narrative disclosures should to the largest extent possible be supplemented with illustrative tables and overviews to improve the clarity. • Institutions should ensure that the terminology used to describe complex financial instruments and transactions is accompanied by clear and adequate explanations.			
<u>Overall assessment</u>			

Annex 2 - Banks covered in the survey

Banco Santander

Bank of America

Barclays

BBVA

Citi

Commerzbank

Credit Agricole

Credit Suisse

Deutsche Bank

Dexia

Erste Bank

HSBC

ING

Intesa SanPaolo

JP Morgan

Nordea

Rabobank RBS

RBS

RZB

SEB

Société Générale

UBS

Unicredit Group