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8<sup>th</sup> July 2005

Dear Sirs

## **CEBS Consultation on financial reporting (CP06)**

The British Bankers' Association (BBA), the International Swaps and Derivatives Association (ISDA) and the London Investment Banking Association (LIBA) welcome the opportunity to comment on the proposed consolidated financial reporting framework (the framework) as outlined in CP06. In general our Members support the concept of harmonisation and convergence as a means of reducing the regulatory burden and creating a level playing field across the EU and support CEBS in this general objective. Our Members accept that regulators need financial information for supervisory purposes and understand why, particularly in certain jurisdictions, they may wish to receive it in a particular format. Our Members consider that this is a useful contribution to the debate and that there are important lessons to be learned from the process. However, they think that the reporting requirements set out in IAS/IFRS, in accordance with Regulation EC 1606/2002 (the International Accounting Standards (IAS) Regulation), already represent an extensive set of common reporting requirements and therefore our Members do not consider the more detailed proposals set out in CP06 to be appropriate.

## **Key issues**

Our Members have five key concerns regarding the framework:

- The IAS Regulation requires the reporting of consolidated financial information for listed groups on the basis of IAS/International Financial Reporting Standards (IFRS) requirements – no more, no less. The disclosures resulting from IAS/IFRS already represent an extensive set of common reporting requirements. As such, requirements which exceed, or are even at odds with these disclosures should have no place in harmonised financial reporting. Additional supervisory disclosures, which are justified for prudential reasons, should be captured in the solvency reporting package. National authorities are, of course, at liberty to ask for explanation of particular financial reporting disclosures where a supervisory need arises and our Members are

happy to provide that explanation. Our Members consider that such a risk based approach is more appropriate and would impose a lower burden both on regulators and the industry.

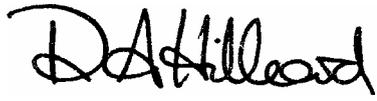
- The additional information required has not been justified by an impact analysis. It is unclear to our Members the purpose for which the additional information is required and therefore the benefit derived. Furthermore, on the cost side, not all of the additional data required will be available on firms' systems. Firms would need to invest in system development at a time when they are already heavily involved in other regulatory and accounting initiatives, thereby diverting limited resource away from those important projects. Therefore our Members consider that the proposals are counter to the principle of better regulation in the Commission's Green Paper on Financial Services Policy (2005 – 2010). In particular we would cite the commitment to 'convincing economic impact assessments before launching a proposal' and to 'ex-post evaluation' to ensure that the benefits sought are actually derived.
- The framework is unlikely to deliver common reporting. Given the non-mandatory nature of the proposals, regulators will be able to pick from, and supplement, the menu of possible reporting requirements included within the proposal. Additionally the framework will only apply to a sub-set of institutions. The UK, for example, is not proposing to implement IAS/IFRS on a mandatory basis beyond the requirements of the IAS regulation, although other groups may choose to implement if they so wish. Therefore there will still be divergence between jurisdictions and within jurisdictions.
- As a result of the additional reporting burden the framework may provide a disincentive for groups who are considering moving to IAS/IFRS on a voluntary basis if it is intended that such groups should be covered by these proposals.
- Our Members believe that use of XBRL itself may deliver some of the commonality of reporting that CEBS is seeking. Reporting using XBRL will provide a common platform for other users of this information. As IAS/IFRS reporting evolves using this protocol, common reporting frameworks are likely to evolve. However our Members would want to see the move toward this protocol achieved over a reasonable timeframe because of the systems implications of its introduction.

Responses to the questions posed within the CP are contained in Annex 1 and other issues raised by our Members are contained in Annex 2.

We understand that some national regulators are keen for CEBS to produce guidance of this nature. If, on balance, CEBS decides to proceed with the framework as outlined, our Members consider that it is important, in line with the non-mandatory nature of the proposals, to allow those regulators who propose to rely on published financial statements alone to continue to do so.

We look forward to working with CEBS further on this issue. Please contact Diane Hilleard ([diane.hilleard@liba.org.uk](mailto:diane.hilleard@liba.org.uk)), Paul Chisnall ([paul.chisnall@bba.org.uk](mailto:paul.chisnall@bba.org.uk)) and Ed Duncan ([eduncan@isda.org](mailto:eduncan@isda.org)) if you would like to discuss any of the issues raised in this letter or on future proposals in this area.

Yours faithfully,



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## Annex 1 - Responses to questions

### **Q1 Do respondents agree that the reporting framework is IAS/IFRS consistent? Please indicate where you believe that this is not the case.**

To the extent that the framework reproduces the reporting requirements that are within IAS/IFRS we agree that it is consistent. However, the framework goes far beyond the requirements in IAS/IFRS. It is not clear to us why the additional information is necessary.

Examples of where our Members consider that the framework is not consistent are as follows:

- ? Reporting is required on the basis of explanations/definitions or general requirements within IAS/IFRS rather than specific reporting requirements. Many of the references made to IFRS do not contain any disclosure requirement at all (such as references made to IAS 39, which is a measurement standard and does not refer to reporting requirements). For example the references to IAS 39.7 and ED7.
- ? The framework appears to limit some of the options available to firms in IAS/IFRS. This is not compatible with a framework that is supposed to be consistent with IAS/IFRS. For example, the explanatory guidance in Annex 2 requires separate reporting of accrued interest whereas under IFRS you can choose whether to offset it against the instrument.
- ? In some areas reporting is required on the basis of exposure classifications within the Internal Ratings Based Approach (IRB) contained within the draft Capital Requirements Directive (CRD). The classifications in Article 86 are not reporting requirements. Additionally the IRB approach will not necessarily be used by all firms. The Standardised Approach contains additional categorisations and there may be subtle differences between similar classifications in the IRB and under the Standardised Approach. Also these categorisations also do not represent a faithful transposition of the classifications outlined in the CRD. For example, there is not a 'non credit institution' category in the draft CRD.
- ? Additional disclosures for derivatives held for trading are required, beyond those required by IFRS, where these are broken down by both "nature" (interest rate, equity, currency, etc), and by "type" (FRA, Forward, interest rate swap, etc).
- ? All references made to "Common Practice" go beyond the reporting requirements of IFRS/IAS and are therefore not consistent with IFRS/IAS.

### **Q2 Do respondents believe that the use of Common Practice (CP) is appropriate? Please indicate where you believe this is not the case.**

No. Our Members consider that it is inappropriate for CEBS to require enhanced disclosure within a consultation on proposals to standardise financial reporting consistent with IAS/IFRS. Where such additional information is required for supervisory purposes, this should be considered for inclusion within the proposals for common reporting of the solvency ratio.

**Q3 Do respondents believe that the data contained in the reporting framework are available within the reporting entity? Please indicate where you believe that this is not the case.**

To the extent that information is required for the purposes of IAS/IFRS reporting requirements the data will be available in the reporting entity, but only within the timeframe for implementing, the as yet unpublished, IFRS 7 (although early adoption is encouraged, it is likely the majority of our members will not comply with IFRS 7 much before annual periods beginning on or after January 2007). Additional information will not necessarily be available. Some of the additional information requested will also be available as a result of the requirements to produce solvency ratio reporting, but not necessarily on the same basis/systems as collated for accounting purposes. As stated earlier, our Members believe that prudential reporting should only be considered as part of the solvency ratio reporting.

**Q4 What additional steps do respondents think CEBS should take to promote further convergence towards a system of regular supervisory reporting that strikes a proper balance on the degree of detail of the information requested?**

Our Members consider that common reporting should focus on minimum harmonisation based only upon the requirements of IAS/IFRS and that these should be allowed to evolve over time. Firms think that common reporting formats should be global rather than purely EU based and a natural evolution approach would allow this to happen. In the intervening period, we would support a risk based approach to reporting whereby firms discuss with national authorities the areas of their financial reporting on which supervisors need additional information. This can be supplemented with management information as appropriate. Common solvency reporting should be tackled as part of the work on CP04.

If CEBS intends to continue with the approach as outlined, then the issue of home/host reporting needs further consideration. We recommend that firms are permitted to use the home supervisor's reporting requirements.

**Q5 Do respondents believe that the guidance provided in Annex 2 is appropriate in all respects? We particularly welcome comments on the first chapter of the explanatory guidance.**

While securing a common understanding is obviously a desirable objective, our Members do not believe that the guidance is appropriate in all respects. Our Members do not believe that it is possible to provide guidance on presentational issues without impacting recognition and measurement. For example the requirements for accrued interest to be reported separately directly impacts the options available under IFRS to either report separately or report net against the financial instruments to which it relates; and the framework also prescribes a particular methodology for the impairment of financial assets that fall within the available for sale methodology which is not required by IFRS.

## **Annex 2 - Other issues**

As mentioned above, our Members have a number of other issues associated with the proposals for the framework. These are outlined below:

- ? The framework, as proposed, represents maximum harmonisation of all possible regulatory requirements and allows national authorities to pick from that list. Our Members consider that CEBS should seek to converge on minimum requirements as a general principle. We would cite the proposals for supervisory disclosure contained in CP05 as a good example of a more proportionate approach to reporting.
- ? Firms are in favour of global rather than EU harmonisation, but think that standard presentation should be allowed to evolve as IAS/IFRS become embedded worldwide. If regulators have determined that other information is necessary to provide a true and fair view they should work with other global regulators and feed their conclusions into the IAS/IFRS process. On this issue we would also note that significant steps are being taken in convergence between IFRS and US GAAP, and that over time, as differences between the two standards are eradicated, users of accounts will naturally benefit from receiving more and more comparable information.
- ? There is a lack of clarity as to the scope of these proposals. For example it is not clear how the proposals would apply to groups comprised of both banks and investment firms; and to groups that operate across EU jurisdictions - in particular, whether sub-consolidation would be required at a national level; whether the reporting can be completed on the basis of the home supervisor's requirements and the status of firms with the consolidating parents outside the EU?
- ? The frequency of reporting expected is unclear. Our Members consider that this should be no more frequent than the financial reporting requirements.
- ? The extent of validation required is unclear. If supervisors expect that these reports to be subject to audit and audit committee review, this will increase the direct cost to firms of producing financial information and additionally increase the risks to banks and their auditors. For entities subject to US regulation the requirements of Sarbanes Oxley will apply and we are aware of the proposals to bring in similar requirements in the EU.