Brussels, 29 April 2005

EAPB Position on the CEBS Consultation Paper on the New Solvency Ratio: Towards a Common Reporting Framework (CP04)

The European Association of Public Banks (EAPB) represents the interests of 19 public banks, funding agencies and associations of public banks throughout Europe, which together represent some 100 public financial institutions with a combined balance sheet total of EUR 3,000 billion and over 170,000 employees, i.e. representing a European market share of approximately 15%.

The EAPB would like to thank CEBS for the opportunity to comment on the above mentioned consultation paper. Prior to the comments on the consultation paper, the EAPB wants to welcome that CEBS is endeavouring to consult such an important issue closely with market participants and the industry. The EAPB would very much appreciate CEBS considering these comments and taking them into account.

We strongly support CEBS's aims of moving towards a level playing field in Europe and reducing the reporting burden on the banks. The solvency framework's key underlying principles of flexibility, consistency and standardisation are appropriate, in our view.

In our view the draft templates themselves are too extensive and too detailed, thus making the overall framework highly complex and unclear. The consultation paper argues that the draft represents the "highest common denominator" and that national supervisors, under the principle of flexibility, can opt for a lower degree of detail. In our opinion this is no justification for such an excessive volume of reporting requirements. Banks operating across borders, which had invested particularly high expectations in the CEBS initiative, may find themselves having to bear the implementation costs for the "maximum draft" and may thus be unable to concentrate only on possibly less extensive national requirements. We therefore urge that the final version reflects the concept of harmonisation not only in a standardisation of formats, but also in a substantial reduction of the data to be reported. Furthermore, we believe it would be beneficial if, for groups operating throughout the EU, the principle of

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home country supervision would apply to the solvency reports submitted by all units. This is the only way to ensure that reporting requirements for cross-border institutions will be consistent throughout the group.

A regulatory solvency reporting framework should give supervisors a clear idea about a bank's risk situation and the adequacy of its own funds. In addition, the reporting burden on the banks should be kept within limits. For these reasons, the information in the templates should be confined to that which is necessary to calculate capital requirements. This can be adequately achieved by a presentation of the bank's exposures broken down into several risk classes, its risk-weighted assets and corresponding capital requirements. We reject any information going beyond the above since the additional costs involved would be out of all proportion to the additional insight for supervisors.

The draft often requests data whose information value, in our view, lies only in checking the plausibility of the reported figures or the bank's calculations. This applies, for example, to much of the CRM templates, to the request for exposures to be broken down by credit conversion factors on the SA templates and for the numerous Pillar II elements. The accuracy of calculations must be checked during the approval process, however, not by means of a standardised report submitted several times a year.

In light of our views expressed above, we reject all the "other information" (OTH) templates.

We reject the proposed mapping of the 16 standard approach classes to the seven IRB classes. Although we welcome the objective of achieving greater clarity by reducing the number of reported classes, we believe the associated implementation costs will outweigh the benefits. All banks which calculate part of their portfolio under the standard approach will have to carry out the granular division into 16 classes. Due to the unsystematic recognition of physical collateral in the standard approach, it will not be possible to map the 16 classes to seven just by aggregating several standard approach classes into one IRB class. Mapping will therefore have to take place by reassigning each individual exposure to one of the IRB classes. This will necessitate two separate allocation processes for standard approach portfolio exposures: one to comply with the requirements of the standard approach and one for reporting purposes. Allocating the individual standard approach exposures to the 16 classes would therefore not merely be only an "interim calculation step" for reporting, but

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would have no function whatsoever. For this reason, we call on CEBS to modify the structure of the standard approach templates proposed in the draft.

To the individual templates we want to make the following explanatory notes:

- CA

The requested information on regulatory capital is too detailed and should therefore be tightened.

- CA IAS

According to the explanatory notes, the aim of this template is to provide comprehensive information related to the effects of IFRS on regulatory capital. The effects of adapting IFRS accounting data for regulatory purposes are to be quantified and presented as clearly as possible by means of "prudential filters". CEBS announced the adoption of these filters and of further guidelines for calculating regulatory capital on the basis of IFRS group accounts in a press release issued on 21 December 2004. In principle, we consider the idea of using CEBS's prudential filters for regulatory reporting purposes to be appropriate. We believe it is questionable, however, whether the template in its present form is a suitable means of implementing these guidelines correctly. It is not clear how the prudential filters recommended by CEBS are incorporated into the template. All in all, we consider the selected matrix presentation as being highly complex, detailed and unclear. We believe a fundamental simplification and explanation of the template is needed to ensure that the effects of the prudential filters will be calculated accurately. It is particularly important, moreover, that the prudential filters are clearly indicated in the template.

- SA

In our view, reporting should be confined to columns 4, 9, 10 and 11.

- SA SEC 1 and SA SEC 2

All the securitisation templates request extremely detailed information on securitised transactions and, in particular, require a number of interim calculation steps to be shown. The requested level of detail far exceeds what is needed. Dividing the templates into true sale and synthetic is unnecessary from a risk angle since the only difference lies in the credit

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protection to the underlying assets. We therefore recommend consolidating the two templates.

In terms of "Investors" the proposed breakdown into three different classes and rated/unrated tranches is largely unnecessary. Rank plays no role whatsoever in calculating capital requirements for rated securitised positions in the standard approach. As for unrated positions, rank is relevant only if the method of calculating capital requirements for securitised positions in an ABCP programme described in Annex IX, part 4, paragraph 12 is applied. Such positions must be at least second loss. In contrast to the Basel capital adequacy framework, application of the look-through approach (Annex IX, part 4, paragraph 11) is not confined to the most senior-ranked positions. It is therefore sufficient to differentiate between rated and unrated positions.

Column 6 is not necessary for calculating capital requirements and may be deleted: Regarding to column 7 we would point out that credit risk mitigation techniques do not always lead to a reduction in the exposure value. This is normally only the case with funded securitisation. With unfunded securitisation, the risk mitigation effect is taken into account by adjusting the risk weight, and the transaction is recorded under the risk class to which the protection provider belongs.

Columns 15 and 16 can be deleted. The information in row 15 already has to be entered in aggregated form in row 78 of the CA template. Positions deducted from Tier 1 are to be entered in column 16. The draft directive allows banks the option of either assigning securitised positions with a 1250% risk weighting to the weighted risk assets or deducting them from the components of non-consolidated own funds. A capital deduction of securitised items from core capital only is not envisaged in the directive. Instead, it follows the Basel approach, under which 50% of securitised positions are deducted from Tier 1 and 50% from Tier 2 capital.

In principle, exposures retained or repurchased by originators should be reported using the same system as that for investors. The above comments therefore also apply here.

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- IRB

Under the IRB approach, capital requirements (column 11) and risk-weighted assets (column 10) are calculated by applying the PD, LGD, EAD and (if necessary) M risk parameters in the respective capital function. With this in mind, we consider it sufficient to indicate these parameters only (PD (column 4), LGD (column 8), EAD (column 7) and, if necessary, M (column 9)). In addition, we would appreciate clarification that the scaling factor (currently 1.06) should be reflected in column 10.

We do not believe it would serve any useful purpose to report EL and LGD in columns 13 and 8 respectively for loans drawn and open lines (on-balance and off-balance transactions). This would not deliver any meaningful information.

- IRB EQU 1

We believe it would make good sense to confine reporting to columns 4, 5, 8, 9, 10 and 11. Reporting the average LGDs in column 7 would provide no information of relevance to supervisors since the weighted LGDs involved are only those prescribed by supervisors. Columns 8 and 9 already request allocation to the two possible alternatives.

- IRB EQU 3

Only columns 1, 4 and 5 should have to be reported. Column 3 contains the same data as column 4 multiplied by 12.5. Reporting these figures will therefore deliver no added value.

- IRB SEC 1 and SEC 2

It is true that, when calculating capital requirements for securitised positions under the IRB approach, it is necessary to distinguish between rated and unrated items and between different ranks. These distinctions should not, however, be made as proposed in the template. With *rated* positions, special risk weights apply under the IRB approach for the most senior tranches. It therefore makes good sense to distinguish between "normal" and senior positions in these cases. *Unrated* positions must be deducted from capital regardless of their rank unless the SF is applied to them. When applying the SF, however, no distinction needs to be made on the basis of rank. Although rank certainly plays a role in the SF, this is reflected in the credit enhancement level (L), which is determined by calculating the ratio of junior positions to the total securitisation volume. A distinction between most senior and other tranches can therefore be dispensed with for unrated positions.

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For the originators, no amounts can be entered in the two columns for the internal ratings based approach (28 and 29). Since the internal ratings based approach is also to be applicable to balance sheet items, we consider that it must also be possible with originators to calculate on-balance sheet positions in ABCP securitisations under the IRB approach and enter these on the template.

Rows 26 and 27 are for entering the exposure values or “average risk weights” calculated by applying a look-through approach under Annex IX, part 4, paragraphs 11, 12 and 14. We would point out that these rules apply only to the standard approach.

- SA CRM

We would like to make the general point that the structure of all the CRM templates is highly complex, which undermines their information value. Sufficient information about the transfer of risk between the approaches and about credit risk mitigation is provided by columns 3, 4, 5, 6, 7, 8, 9, 14, 19, 20, 21 and 26. The remaining columns, particularly those for the memorandum item (22-25), show individual calculation steps, whose accuracy should be monitored in the approval process.

- FIRB CRM

For the same reasons as those outlined above, we also consider this template as being too complex and reject the requirement to show interim calculation steps. We therefore suggest limiting the content of the template to columns 1, 2, 3, 4, 5, 6, 11, 19, 20, 21, 22, 28, 30 and 32. The requested information about the distribution of LGD estimates in columns 33 and 34 will not serve any useful purpose, in our view, since we are dealing here exclusively with LGDs prescribed by supervisors.

- AIRB CRM

Reporting should be confined to columns 1, 2, 3, 4, 5, 6, 11 and 19 for the reasons outlined above in our comments on the FIRB CRM template.

- CRM I-O

We totally reject these templates since we fail to see how the observation of flows of collateral between the segments can assist in evaluating a bank’s risk profile. In our view, the insight provided by such an approach is more of an academic nature.

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- MKR-IM Daily

This template does not appear to offer supervisors any additional information value. Authorisation and testing procedures already provide supervisors with sufficient information about the specifics of the banks' models and the suitability of any subsequent significant changes to the models also has to be confirmed by the competent authorities.

- OPR

If the AMA is applied, reporting requirements should be confined to that which is necessary to allow supervisors to evaluate whether the bank is complying with the rules. If a bank wants to reduce capital requirements for operational risk on the grounds that EL is covered by alternative means, Annex X, part 3, paragraph 8 of the draft directive amending Directive 2000/12/EC merely requires it to demonstrate that appropriate measures are in place. An obligation to report a concrete amount cannot be inferred. This requirement is therefore to be rejected. Furthermore, the precise distinction between the reporting fields "of which: due to expected loss" and "expected loss captured in business practice excluded from capital requirements" is not clear. We interpret the item "of which: due to expected loss" to be a statistical measurement of the AMA model and "expected loss captured in business practice excluded from capital requirements" as the expected loss measured in terms of value adjustments and budgeting. We do not consider such a comparison appropriate. Current accounting practices do not make it possible to build up adequate provisions for the expected loss from operational risk. A comparison with the quantitative risk measurement would therefore not be justified.

- OPR LOSS

According to Annex X, part 3 paragraph 14 of the draft directive amending Directive 2000/12/EC, the reporting of the losses shown in the business-line/event-type matrix has to be submitted to the competent authorities only on request. If the template is intended as a basis for regular mandatory reporting, therefore, it must be rejected. Should the template, however, be intended as a basis for information which may, under certain circumstances, be requested by the authorities, it should first be clarified that presentation in this form could only become necessary under the AMA. In addition, the requirement to indicate the highest single loss and the number of losses for each business-line/event-type must be deleted.

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The draft directive envisages no such requirements; nor would they provide supervisors with any discernable information value.

- MRK SA TDI, MRK SA EQU, MRK SA FX, MRK SA COM

The approach of requiring interest rate risk and currency risk positions to be reported for all currencies needs to be modified, in our view. We believe it would be sufficient to concentrate on the five most important international currencies (euro, US dollar, Swiss franc, pound sterling and yen) and report the rest under a collective item “other currencies”. Similarly, the reporting of market risk from equities by country of origin should be confined to a few core regions (e.g. USA, Japan, EU).

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