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Objet Response of Crédit Agricole on the FinRep project

Jose Maria Roldan
Chairman
Committee of European
Banking Supervisors
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Dear Sir,

Thank you for allowing us to submit our comments on the FinRep project concerning a consolidated financial reporting framework under International Financial Reporting Standards (IFRS).

We also enclose our answers to the questions raised in the consultation, to which the following remarks relate.

In adopting IFRS and making them mandatory for listed companies, the European Union (EU) has chosen a single set of accounting standards in order to facilitate comparison of financial statements, at a time when financial markets are becoming increasingly integrated. But paradoxically, as the Committee of European Banking Supervisors (CEBS) itself has pointed out, IFRS neither imposes nor proposes a standard reporting format. Had this shortcoming not been remedied, the goal of comparability would not have been fully achieved.

Crédit Agricole therefore welcomes CEBS' approach, which seeks to fill this gap by providing credit institutions with a standardised, IFRS-consistent consolidated reporting format. That said, the initiative would stand a much better chance of succeeding – and of satisfying the concern for consistency, uniformity and simplicity – if the proposed statements were not designed solely with CEBS in mind but could also be used by banks to make their own financial disclosures.

We therefore feel that the CEBS project only partially meets the need for financial statements that are prepared on a common basis, accepted by the vast majority of users, and useful to banking supervisors and credit institutions alike.

There are several reasons for that judgement. First, the FinRep project is too complex. To accommodate the diverse approaches of CEBS member authorities, the project incorporates every single requirement, down to the finest level of detail. As a result, the financial statements are unnecessarily unwieldy and the information they contain is often redundant. Moreover, it may be questioned whether some of the new informational requirements are relevant.

Second, since national supervisors would be allowed to demand some or all of the information in the proposed financial statements for their own purposes and to ask for supplemental statements, there would automatically be as many reporting formats as there are supervisors. This would eventually undermine the legitimacy of the system, which should be common and unique. Implementing such a system would therefore be seen as an additional administrative constraint imposed by a virtual supranational organisation whose purpose remains a mystery.

If the FinRep project were to be confirmed in its present state, it would add to the administrative burden of cross-border banking groups such as ours. It would prevent us from rationalising our IT systems by forcing us to supply diverse data that vary according to the countries in which we operate and the supervisory authorities that oversee them.

In our view, to arrive at a genuinely uniform reporting system, member states' authorities should standardise their approaches to, and practical arrangements for, supervision before seeking to harmonise financial statements.

Once this preliminary phase is complete, a European working group composed of credit institutions and CEBS representatives should be set up to analyse these statements and prepare a truly coherent and uniform project that is accepted by the largest number of market participants.

Examining the FinRep project in detail, we note that its informational requirements exceed the basic IFRS disclosures. Only some of the regulatory references used to support each detailed demand are derived from the IFRS chapter on mandatory disclosures. Instead, many of the references come from draft standards, proposals for directives, or "Common Practice". This approach is not shocking in itself, but it must nevertheless be shared.

We also note that the current version of the FinRep framework chooses the most detailed of the IFRS options. For example, it breaks out two balance-sheet captions, "Accrued income from financial instruments" and "Accrued expenses from financial instruments", whereas, under IFRS, these items can be allocated to the financial instruments in question.

As regards this question of presentation, which will have a bearing on the complexity of future updates to management and accounting systems, we would remind you that listed credit institutions adopted IFRS on 1 January 2005. Consequently, they were obliged to present their financial statements under IFRS as from the first quarter of 2005, at a time when no European mechanism existed. To that end, France's national accounting board, the CNC, published a recommendation along with a proposed reporting format back in 2004. That recommendation resulted from a year-long process of cooperation between the parties concerned, including credit institutions, the French banking supervisor and securities regulator, auditors, and so on. We began to modify our management and accounting systems in the light of the CNC recommendation, which adopted certain options. The options taken up in the FinRep framework, which are apparently not the same as those chosen in the standard statements recommended in France, have obviously affected those modifications.

Leaving aside the valid question as to whether the new choices are relevant, we will still need additional time to implement the changes resulting from them. In their present form, credit institutions' accounting systems cannot be used to prepare financial statements that are identical in format but that may have substantially different content, depending on the country for which they are intended. Moreover, the deadlines for producing these statements are increasingly tight.

We are now experiencing the changeover to IFRS on a daily basis, and we wish to draw your attention to the drastic changes we are having to make, both to our accounting systems and to our management systems. In consequence, the workload of the teams responsible for making these changes has obviously risen considerably. While we understand the demands of banking supervision at European level, we considerate it vital in the current context of slimmer banking margins and cost reductions – yet another demand of banking supervisors – to confine additional disclosure requirements to the bare minimum. Moreover, the information thus disclosed should be consistent with that chosen by the majority of credit institutions. Last, the changes should be spread over a reasonable period of time and should be implemented only after in-depth discussions with the banking industry.

Please feel free to contact us if you require any further information.

Yours truly,

G. Couvidoux
Head of Standards and Procedures

ANNEX

Question 1 : Do respondents agree that the reporting framework is IAS/IFRS consistent? Please indicate where you believe this is not the case.

As we pointed out in our general comments, the proposed consolidated reporting framework has adopted a number of presentational options, thus automatically excluding the alternatives available under IFRS. The most striking example is the method of recognising changes in assets and liabilities at fair value through profit or loss. Since IAS/IFRS say nothing on this subject, it is possible to account for these changes entirely as "net gains or losses on financial instruments at fair value through profit or loss". CEBS requires that the share of unpaid accrued interest be recorded as interest margin. This raises major operational problems for institutions that did not choose this option at the outset.

Furthermore, we do not believe that it falls within CEBS' remit to impose accounting practices by making presentational options mandatory.

In addition, the proposed consolidated reporting framework does not rely solely on existing standards. Many of the disclosure demands are based on Exposure Draft 7. In our view, it is ill-advised to propose a reporting framework based partially on draft standards, which by definition are subject to change before the final version and which, more importantly, have not yet been approved by the relevant European authorities.

Question 2 : Do respondents believe that the use of Common Practice (CP) is appropriate ? Please indicate where you believe this is not the case.

To be truly appropriate, Common Practice must genuinely correspond to procedures used regularly by credit institutions in all CEBS member states. This is the case when these procedures result from the requirements of the 1986 EU directive. Furthermore, CP should fill a gap in the procedures used to meet IFRS disclosure requirements.

Consequently, when CP results from a collection of national practices, or when the disclosures arising from CP are overlaid on those required under IFRS and are not needed to ensure informational consistency, then the use of CP is inappropriate, in our view.

Question 3 : Do respondents believe that the data contained in the reporting framework are available within the reporting entity ? Please indicate for which data you believe this is not the case.

In its consultation paper, CEBS assumes that the data contained in the proposed reporting framework are already available in entities' information systems.

In practice, however, this is certainly not the case. The data required in the framework go well beyond what is strictly required under IAS/IFRS:

- the reporting requirement may result from an interpretation of IFRS, although the information demanded is not explicitly required under those standards ;

- the requirements may be included in the explanatory guidance and thus be omitted from the actual standards themselves ;

- they can refer to draft standards (ED7) that have yet to be approved ;

- by definition, the requested analyses are based on the prudential categories set forth in the Capital Requirements Directive (CRD) and therefore are not IAS-mandated data as such.

Accordingly, the major drawback with the reporting framework as it stands is the cross-referencing of data, i.e. breakdown by category of financial instrument and then by nature of instrument, and finally by type of counterparties, pursuant to the draft CRD. It is not possible to report information in this level of detail – and on a consolidated basis, to boot – using today's IT systems. Consolidation tools are generally off-the-peg applications that are not designed specifically for the banking industry and therefore cannot cope with such a wealth of data.

Question 4 : 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.

As mentioned in our general comments, achieving genuine convergence in supervisory reporting systems demands preliminary discussions about harmonising the way in which CEBS member authorities conduct supervision.

The sole condition for introducing a harmonised and IFRS-compliant supervisory reporting system in the near future would be to design financial statements that are based solely on the information required by IFRS, which have been approved by the European Parliament, and that leave open all the options provided for under those standards.

The project would subsequently be developed and expanded in the light of accumulated experience.

Question 5 : 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.

The guidance in Annex 2 is welcome insofar as it provides detailed explanations about the FinRep project. In terms of substance, however, several remarks are called for :

- The Explanatory Guidance explicitly sets forth the presentational choices that have been made, particularly as regards accrued income and expenses (see general remarks). In practice, this amounts to denying the alternative options provided for under IFRS and hence challenging any divergent choices made by credit institutions. It must be stressed that these presentational choices have no impact on net worth or on profit and loss. So why not leave credit institutions free to choose – witness the proposal concerning the choice between the trade date and the settlement date, which is provided for elsewhere in the text ?

- In the Allocations section, the guidance mentions the choice of breaking counterparties down into the same economic categories as those chosen for the draft CRD. Making such a breakdown for consolidated financial statements is technically complex. It is systematically requested and cross-referenced to other criteria, but does it really meet a recognised supervisory need ?

- As mentioned above, CEBS assumes from the outset that all the data it requests are available in reporting entities' IT systems. We note, however, the acknowledgment that information on repos may not be readily available in accounting systems but is more likely to be found in front-office databases. There are several such inconsistencies.