

ZENTRALER KREDITAUSSCHUSS

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Consultation paper on Financial Reporting (FINREP) Comments of the Zentraler Kreditausschuss

Dear Madam, dear Sir,

The Zentraler Kreditausschuss¹ would like to thank CEBS for the opportunity to comment on the consultation paper. We should like to begin by making a few general points, which will be expanded and supplemented in our replies to the specific questions in the consultation document.

I. General remarks

In principle, we support pan-European harmonisation of financial reporting requirements on the basis of IFRS consolidated accounts. The aim of such a project is to increase the comparability

¹ The ZKA is a joint committee operated by the central associations of the German banking industry. These associations are the Bundesverband der Deutschen Volksbanken und Raiffeisenbanken (BVR), for the cooperative banks, the Bundesverband deutscher Banken (BdB), for the private commercial banks, the Bundesverband Öffentlicher Banken Deutschlands (VÖB), for the public-sector banks, the Deutscher Sparkassen- und Giroverband (DSGV), for the savings banks financial group, and the Verband deutscher Hypothekenbanken (VdH), for the mortgage banks. Collectively, they represent more than 2,300 banks.

of the reported data and thus ensure a level playing field in the European internal market for financial services. There is a need to reduce substantially the number of different reporting requirements currently existing in member states and streamline reporting processes.

In our view, however, the approach adopted in the consultation paper will not succeed in harmonising financial reporting for prudential purposes along the lines outlined above. The draft first sets out an extensive and highly-detailed definition of items to be reported, which, moreover include numerous national specificities. Each supervisory authority will then be able to determine which of these items have to be reported by the banks in its member state. It will also be possible to set additional reporting requirements over and above those in the already extensive framework. This will result in the large number of diverging national reporting requirements remaining. Both banks and supervisory authorities in the European Union will thus continue to have to contend with a whole host of different reporting requirements. This undermines the creation of a level playing field and places a heavy burden on the banks concerned, which will be made still more onerous in the event of cross-border consolidation. In order to ensure that reporting requirements are consistent at least for banks operating across borders, the principle of home country supervision, and thus the rules of the parent company's member state, should apply to all units of a group.

Overall, however, we believe there is an urgent need for the proposed approach to be thoroughly reviewed and not adopted in this form. It is not a suitable means of bringing about harmonisation. In our opinion, financial reporting can only be truly harmonised on the basis of rules which already apply in equal measure to all banks in the European Union and are not supplemented or modified by numerous additional requirements and national specificities. Such a basis is provided by IFRS disclosure requirements.

As we see it, moreover, the proposed requirements are blatantly at odds with CEBS's stated aim of refraining from establishing additional reporting obligations and bringing about a "potential reduction of administrative burden". The type and extent of the envisaged information to be reported, especially the high degree of detail and resulting complexity, will, in our view, preclude any possibility of meaningful analysis or assessment.

On examining the proposed items to be reported more closely, we noted that a considerable number of them go beyond the already extensive disclosure required under IFRS and would sometimes restrict accounting options. This is inappropriate and unreasonable, in our view. Given that IFRS already constitute a comprehensive and internationally recognised set of rules,

the disclosure requirements they contain must also serve as a benchmark for harmonised financial reporting for prudential purposes. It should be borne in mind that the Regulation on the application of international accounting standards makes the use of IFRS mandatory for the consolidated accounts of all EU listed companies from 2005 or 2007. We reject any requirements for harmonised financial reporting at EU level which exceed or are even at odds with IFRS disclosure.

The banks' annual reports are already compiled using a transparent and IFRS-compliant reporting format, which, however, differs sometimes considerably from the draft framework. We see a danger that, in their present form, the templates might have a certain prejudicial effect on accounting, which we firmly reject. The IASB alone has the authority to set internationally recognised group accounting standards, also for EU member states (Regulation (EC) 1606/2002). An endorsement process then makes the standards legally binding. This procedure would be seriously undermined if other institutions such as CEBS established a parallel set of rules.

Furthermore, some of the proposed data is not readily available in the banks' IT systems. Reporting these items would therefore create an additional administrative burden out of all proportion to the additional information value. The same would doubtless apply to the processing by supervisors of such a large number of highly detailed, quantitative reporting requirements. There would be a real risk of information overload, undermining the desired prudential transparency and potentially leading to the wrong conclusions being drawn. A harmonised financial reporting system for prudential purposes should therefore be developed with cost/benefit considerations first and foremost in mind.

As well as addressing the content of the items to be reported, the consultation paper recommends using the eXtensible Business Reporting Language (XBRL) as a standard transmission technology. While we basically support investigating the idea of introducing a standard data exchange format, we should like to point out that financial reporting cannot be harmonised by prescribing a particular transmission technology such as XBRL. The first step must be to clarify the numerous open questions relating to the content of the reporting requirements and their national implementation before discussing the issue of a standard data exchange format.

II. Specific comments

Our replies to the specific questions in the consultation paper are as follows:

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

In principle, we welcome CEBS's aim of developing an IFRS-consistent reporting format. To achieve the greatest possible degree of consistency, we believe it is essential to use the IFRS disclosure requirements as a benchmark for the standardised financial reporting framework. The reporting proposed in the consultation paper far exceeds that required in the context of IFRS disclosure, however. For example: the templates include frequent references to IAS 39.9, which contains no disclosure requirements, but merely definitions of various categories of financial instruments. Similar reservations apply to numerous other references to IFRS which deal with recognition and measurement rules or with definitions, not reporting requirements (e.g. the IAS/IFRS references in various templates to IAS 39.37; IAS 39.86-89; IAS 39 AG 15 ; IAS 32.11 and many others).

We also noted instances where reference is made to IFRS disclosure requirements which are not consistent with the information requested in the templates. ED 7.21, for example, envisages that realised gains and losses should be broken down by certain categories of financial instruments and disclosed on a net basis. The template for the income statement, however, requests gains and losses to be divided into groups of financial instruments and reported on a gross basis. This approach reflects neither the requirements of ED 7.21 nor normal banking practice and is therefore inappropriate, in our view. The same applies, for example, to several of the numerous and highly detailed reporting requirements in the templates for the cash flow statement and the statement of changes in equity, which go far beyond the disclosure currently required under IFRS (especially IAS 7.20 and IAS 1.97).

Furthermore, it is not always clear what, in concrete terms, has to be reported. The template for the balance sheet, for example, requires the reporting of issued subordinated liabilities which are held for trading. In our view, these items cannot exist. This also applies to the "financial liabilities held for trading – debt to credit institutions" which are mentioned in Template 18.

In some templates, the reference column indicates supervisory rules that have not yet been adopted, such as Article 86 of the Capital Requirements Directive. In these cases, the Directive's envisaged rules on exposure grouping are intermingled in the templates with certain product categorisations and accounting rules. This combination creates new reporting requirements which reflect neither accounting nor supervisory disclosure rules and request information which is not available in this form in the banks' IT systems (see also our reply to question 3).

We are, moreover, highly critical of the fact that the standardisation in the templates sometimes has the effect of restricting existing accounting options. We reject any such restrictions on IAS/IFRS for prudential considerations alone. One example is the treatment of interest income and interest expenses from trading transactions. IFRS allow these to be allocated to either the interest result or the trading result. The template for the income statement, in contrast, requires mandatory reporting under interest result. As a result, prudential reporting requirements will influence how certain accounting options are exercised. This is unacceptable (see also our reply to question 5). It is not, in our view, the task of CEBS to restrict or interpret existing accounting standards. This is the responsibility of accounting standard setters and their interpretation committees.

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

We believe the whole concept of referencing "Common Practice" is problematic since a number of the reporting requirements supposedly covered by this term exist only in a few member states and so by no means reflect normal reporting and disclosure practices throughout the EU. Yet harmonisation of financial reporting can only be achieved on the basis of rules that apply equally to all banks in the European Union and require no further interpretation by national supervisory authorities. Only IFRS can provide such a basis since they will become mandatory for all EU-listed companies from 2005 or 2007. As already mentioned in our general remarks, requirements which exceed or are even at odds with IFRS should have no place in harmonised financial reporting at EU level. In consequence, we consider that the proposed reporting requirements in accordance with so-called "Common Practice" are inappropriate and should be dispensed with.

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.

Since numerous CEBS reporting requirements exceed the existing IFRS rules in terms of both form and content and contain national specificities, some of the requested data is not readily available in the banks' IT systems. This applies, for example, to some of the extensive information on repos and reverse repos (Template 43). It will also be highly problematic to comply with the requirements under the "layered approach" to balance sheet and profit and loss data. Balance sheet data, for example, is first to be presented by category of financial instrument (held for trading, available for sale, held to maturity, designated at fair value through p & l, etc.). These categories must then be broken down according to certain product groups (equity instruments, debt instruments, derivatives, etc.) and sometimes further subdivided according to counterparty or prudential exposure class (e.g. public sector, banks, corporate, retail, etc.).

This convoluted approach ultimately produces a combination of accounting disclosure requirements, various CEBS-specific product categorisations and prudential exposure classifications which is not available in the banks' databases in this form. This also applies to some of the requested breakdowns of profit and loss items (e.g. the detailed subdivision of interest income and interest expense by certain groups of financial instruments or the breakdown of the trading result by product categories specified by CEBS, etc.) and to numerous other templates (e.g. the requested product breakdown for derivatives held for trading and used for hedging in Templates 4 and 9, the detailed subdivisions for finance and operating lease in the columns in Templates 11, 12 and 13, and many others). Much of the data could, if available at all, only be accessed manually in individual sub ledgers (this applies, for example, to numerous details on derivatives and hedge accounting in Templates 4, 9 and many others). This would require extensive input from individual group subsidiaries, which would then have to be consolidated by the parent company in a time-consuming and labour-intensive process. Such complex breakdowns provide little meaningful information, however, and are to be rejected for cost/benefit reasons.

We therefore consider it essential for the CEBS reporting framework to confine itself to the data which is already held in the banks' IT systems for the purposes of complying with IFRS disclosure requirements. This would also have the advantage that the data could be

taken directly and in automated form from the group's consolidated accounts (general ledger).

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 pointed out above, financial reporting can only be successfully harmonised if it is based on IFRS disclosure requirements, since these will apply equally to all listed companies in the European Union. We therefore believe there is an urgent need to revise the requirements proposed in the templates with this in mind. Steps should be taken to reduce the high volume and level of detail and achieve as much consistency as possible with the information-oriented disclosure required under IFRS. We are, moreover, of the opinion that when developing and reviewing reporting requirements the principle of home country supervision, and thus the rules of the parent company's member state, should apply to all units of a group. This will ensure that reporting requirements for banks operating across borders are consistent.

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 objective of the explanatory guidance is to clarify the structure and content of some of the extensive reporting requirements. CEBS asserts that the guidance is confined solely to presentational matters; it will not affect recognition and measurement in any way or the correct application of accounting standards. It is not possible, however, to view IFRS recognition and measurement rules and CEBS reporting requirements in complete isolation from one another. Some of the options permitted under IFRS, for example, would be restricted by certain standardised CEBS reporting requirements (see also our reply to question 1).

This is illustrated by the treatment of accrued interest recommended in the explanatory guidance. The IFRS permit both separate reporting in the balance sheet or offsetting against the financial instruments to which the accrued interest relates. The explanatory guidance, however, makes it mandatory to report accrued interest as a separate item under information on the balance sheet. It is highly probable that CEBS rules on presentation will

rapidly establish themselves as criteria for exercising IFRS options. We do not consider this appropriate. To prevent accounting options from being influenced or restricted, it should be left to the banks to decide whether or not to exercise them, also in the context of financial reporting for prudential purposes.

This also applies to the treatment of certain items such as the impairment of financial assets in the available for sale category. Chapter II of the explanatory guidance sets out a detailed method of posting such impairment which reflects neither a specific IFRS rule nor common practice in the banks. We do not consider it appropriate for CEBS to prescribe a rule in this way.

In contrast, we warmly welcome the fact that the existing IFRS option allowing financial instruments to be accounted for on either the trade date or the settlement date has also been adopted by CEBS in its financial reporting requirements.

We should be happy to discuss the above matters with you further at any time.

Yours sincerely
on behalf of the Zentraler Kreditausschuss,
Bundesverband deutscher Banken



Katrin Burkhardt



Antje Böttcher