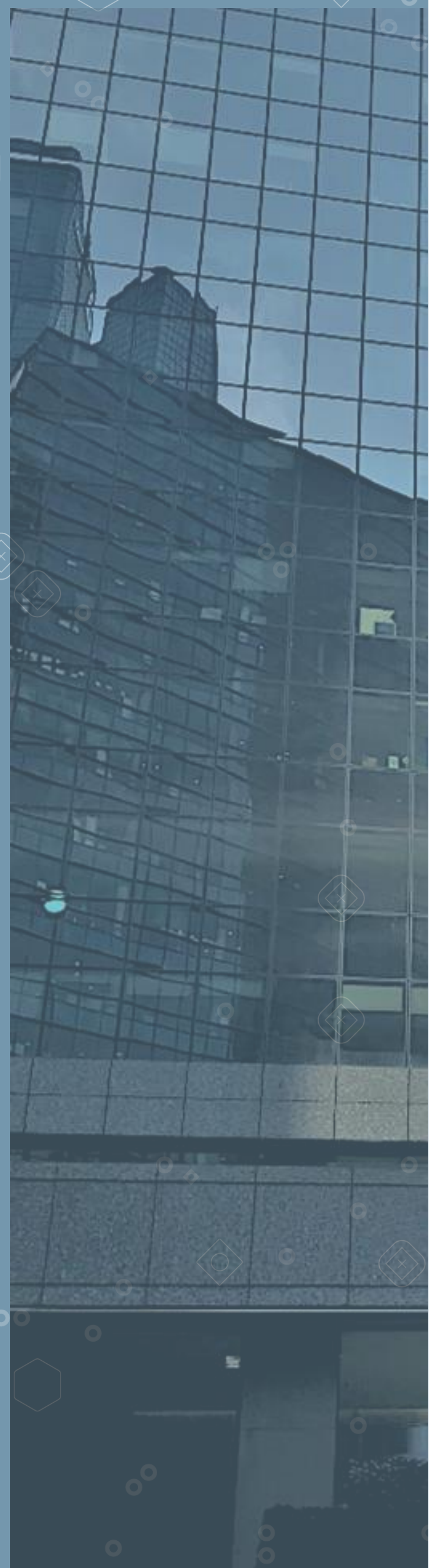
European Banking Authority

REPORT ON CONVERGENCE OF SUPERVISORY PRACTICES IN 2023

EBA/REP/2024/13

JULY 2024



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Abbreviations

AML/CFT	anti-money laundering / countering the financing of terrorism
BIS	Bank for International Settlements
CA	competent authority
COREP	common reporting
CRD	Capital Requirements Directive
CRR	Capital Requirements Regulation
CSRBB	credit spread risk in the banking book
CVA	credit valuation adjustment
DPM	data point model
EBA	European Banking Authority
ECB	European Central Bank
ECL	expected credit loss
EEA	European Economic Area
ESAs	European Supervisory Authorities
ESEP	European Supervisory Examination Programme
ESG	environmental, social and corporate governance
EU	European Union
EVE	economic value of equity
FINREP	reporting of financial information
FLI	forward-looking information
FX	foreign exchange
GL	Guideline
HII	Herfindahl-Hirschman Index
ICAAP	internal capital adequacy assessment process
ICT	information and communications technology
IFRS	International Financial Reporting Standard
ILAAP	internal liquidity adequacy assessment process
IMV	initial market valuation
IPU	intermediate parent undertaking
IQD	interquartile dispersion
IRB	internal ratings based
IRRBB	interest rate risk in the banking book
ITS	Implementing Technical Standards
JD	joint decision
KPI	key performance indicator
ML/TF	money laundering / terrorist financing
MREL	minimum requirement for own funds and eligible liabilities
NII	net interest income
NPE	non-performing exposure
NPL	non-performing loan

OFR	own funds requirements
ORC	overall recovery capacity
PD	probability of default
P2G	Pillar 2 Guidance
P2R	Pillar 2 Requirement
RTS	Regulatory Technical Standards
SEP	Supervisory Examination Programme
SICR	significant increase in credit risk
SOT	supervisory outlier test
SREP	supervisory review and evaluation process
sVaR	stressed value at risk
TSCR	total SREP capital requirement
VaR	value at risk

Executive Summary

One of the EBA's key objectives, in line with its legal mandate[1], is to enhance supervisory convergence across the internal market. In accordance with Article 107 of the Capital Requirements Directive (CRD), the EBA reports annually to the European Parliament and Council on the degree of convergence of supervisory practices. The EBA is deploying various tools to facilitate, ensure and assess convergence in supervisory practices; the conclusions of this assessment are described in the current Report: the level of implementation of the key topics identified in the EBA's 2023 European Supervisory Examination Programme (ESEP)[2], analysis of the convergence of supervisory practices in the context of Pillar 2 and liquidity measures, the outcome of peer reviews and benchmarking exercises, the EBA's conclusions on the functioning and performance of closely monitored colleges, the EBA's most relevant policy developments, and training activities.

The key topics identified for supervisory attention in 2023 were adequately included by most competent authorities, but there is still disparity on the implementation of risk areas like ESG and data aggregation capabilities in the supervisory processes.

The four key topics identified for supervisory attention in the 2023 ESEP, being 1) macroeconomic and geopolitical risks, 2) operational and financial resilience, 3) transition risks and 4) ML/TF risks in the SREP and internal controls and governance, were adequately included by most CAs in their supervisory priorities for 2023. They were also included in the work plans of the supervisory colleges closely monitored by the EBA.

Macroeconomic and geopolitical risk was a key area for CAs in the context of the continuing Russian aggression in Ukraine, the interest rate rises and persistent high inflation in most Member States in 2023. Especially the risk related to interest rates and inflation was deemed to be increasing, as was the supervisory attention paid to these risks.

The resilience of institutions on an operational and financial level has various elements, most of which were assessed by CAs in the context of the SREP. Although the risks analysed were on average deemed stable, there were concerns related to information security management and the implementation of the IFRS 9 standard by institutions. On data aggregation capabilities, a few CAs are still in the process of incorporating this element into their supervisory work.

Transitions related to digitalisation and ESG were given supervisory attention by most CAs. CAs have stepped up their attention to these risks in the past year, although a small minority are still working on including ESG risk in their supervisory approach. While ESG risk was mainly investigated and assessed via off-site analyses and questionnaires, the most broadly used tool for risks related to the digital transformation was exchanges with institutions' senior management.

[1] Article 1(5)(g) of the EBA's founding regulation (Regulation (EU) No 1093/2010).

[2] EBA ESEP Rep 2022 28 - 2023 priorities.pdf (europa.eu).

The final key topic, the assessment of ML/TF risks in the SREP and regarding internal governance, was especially assessed in the context of the sanctions against Russia and Belarus. CAs found that the risk was on average stable, but there was relatively wide disparity among CAs. Most of the authorities have included the ML/TF risks in the SREP assessment and noted that institutions have strengthened internal controls and governance to implement and monitor the sanctions.

There is still room for further convergence in the consistent identification and treatment of risks covered by P2R across the EU.

The 2023 survey[3] outcomes indicate that the application of P2R is a common and well-established practice, with all CAs utilising P2R to address risks not covered or not sufficiently covered by Pillar 1. The P2G setting framework has notably improved since the last survey in 2021, with nearly all authorities having a methodology in place, often aligning with the updated SREP GLs. Regarding the overall P2R amount, the survey shows some dispersion around the EU average (2.8%), with instances of a higher average amount (above 4%) observed in some jurisdictions.

Authorities have been increasing the frequency of monitoring liquidity and funding risk in recent years. While the current framework is generally satisfactory, there are targeted areas where it could be improved, particularly in reporting frequency and deposit origination.

The implementation of CRR III / CRD VI and the subsequent review of the SREP GLs are expected to increase convergence in the implementation of the framework, helping authorities to achieve greater consistency in the supervisory outcome in the context of setting Pillar 2.

The EBA peer reviews and benchmarking exercises provided further support for supervisory convergence and for addressing deficiencies identified as raising prudential concerns.

The peer review found that the CAs fully implemented the relevant section of the EBA's SREP Guidelines in the context of CVA risk, and that the actual approaches employed by CAs towards the supervision of CVA risk satisfy the regulatory requirements and are consistent with those Guidelines. Nevertheless, the peer review suggested some follow-up measures for CAs to address some deficiencies and strengthen supervision.

The 2023 Market Risk Benchmarking exercise shows positive results in term of disparity for the internal model and FRTB standardised approach, but supervisory attention is still needed for potential issues linked to specific aspects of the exercise. The respective Credit Risk Benchmarking Exercise highlights the ongoing need for continuous monitoring of potential undue variability in own funds requirements across institutions, particularly concerning the adoption of the IRB roadmap[4].

[3] The 2023 survey covered data as of December 2022 (corresponding to previous SREP cycles). Given that the updated EBA SREP Guidelines had an application date as of 1 January 2023, the survey confirmed that most competent authorities anticipated their compliance with the updated EBA SREP Guidelines.

[4] The annual EBA benchmarking exercises contribute to improving the regulatory framework, increasing convergence of supervisory practices and, thus, restoring confidence in internal models. For credit risk internal models, the EBA has followed its roadmap for the implementation of the regulatory review of internal models. The EBA roadmap to repair IRB models is a key component of the review of the IRB framework, along with the enhancements brought by the final

According to the 2023 IFRS 9 monitoring report, while significant progress has been generally observed in the implementation of the expected credit loss (ECL) impairment models, latest investigations have revealed diverse approaches adopted by institutions for estimating ECLs. Importantly, analyses have confirmed that many institutions have yet to address practices previously identified as raising prudential concerns, such as those related to significant increases in credit risk (SICR), PD modelling, overlays and forward-looking information (FLI) incorporation processes within the IFRS 9 framework.

The EBA's monitoring of supervisory colleges has confirmed that the annual college cycle is functioning well.

The EBA has developed key performance indicators (KPIs) for all supervisory colleges for implementation in the 2023 supervisory cycle (and beyond). Most of the measurement points in relation to these KPIs were achieved to a great extent for the majority of colleges; for the ones where room for improvement was identified, colleges were requested to take appropriate steps to improve their functioning. The quality of the key college deliverables is deemed to have improved significantly and is at a good level. While the consolidating supervisors prepare and facilitate the college meetings well, information sharing could still be enhanced, in particular information on early warning signs, potential risks and vulnerabilities. Joint supervisory activities are sometimes limited to the organisation of the annual college meeting, failing to explore further opportunities of joint work that is especially warranted to consolidate robustness in uncertain times.

Targeted policy developments support and promote further convergence in prudential supervision.

In 2023, the EBA revised its technical standards on supervisory colleges, aiming to improve further this common EU framework for college functioning, facilitating more efficient and effective supervision of cross-border banking groups. Furthermore, the EBA harmonised the observed practices on ORC determination and assessment, to improve the usability of recovery plans and make crisis preparedness more effective.

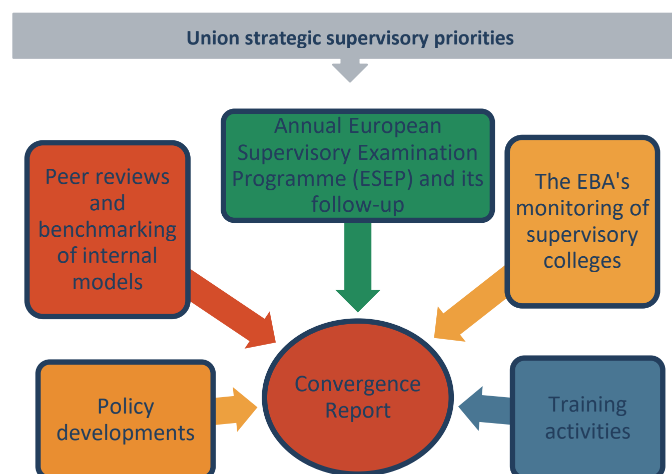
Basel III framework, assessed by the EBA in a set of recommendations issued in response to the call for advice from the Commission.

Background and introduction

1. In line with Article 1(5)(g) of its founding regulation[5], the EBA is required to foster and promote supervisory convergence across the European Union (EU). Specifically in the context of the supervisory review and evaluation process (SREP) that forms an integral part of the prudential supervision conducted by CAs, the EBA is required, i) to develop common procedures and methodologies for the supervisory review, and ii) to report annually on the degree of convergence of supervisory practices to the European Parliament and the Council[6].

2. The EBA Report on convergence of supervisory practices in 2023 (Report) summarises i) how the EBA pursued supervisory convergence in 2023 in the context of the SREP and ongoing supervision via various convergence tools at its disposal, and ii) the EBA's main observations on the respective developments and conclusions.

Figure 1: Supervisory convergence tools



3. Section 1 of this Report analyses the degree of progress in the convergence of supervisory methodologies and measures, including the use of proportionality, achieved through the implementation of the 2023 ESEP by the CAs. This section includes the main outcomes of the CAs' assessments of the ESEP 2023 selected key topics, gathered through the structured information collection from CAs, and the EBA observations stemming from colleges' monitoring activities, as well EBA's analysis of the convergence of supervisory practices in the context of Pillar 2 and liquidity measures. Section 2 of the Report explains how convergence in the context of supervisory colleges evolved, focusing on the closely monitored colleges. Section 3 describes the policy developments concerning supervisory colleges and crisis preparedness. The EBA's training activities supporting supervisory convergence are listed in Section 4 of the Report.

[5] Article 1(5)(g) of the EBA's founding regulation (Regulation (EU) No 1093/2010).

[6] Article 107 of the CRD.

1. Supervisory convergence in the SREP and ongoing supervision

1.1 Implementation and results of the 2023 ESEP

Most CAs adequately incorporated the topics identified for supervisory attention into their priorities for 2023.

The areas where most CAs together observed increasing risk concern interest rate risks, inflation and related asset price correction risks.

There is still disparity among CAs on the implementation of risk areas like ESG and data aggregation capabilities in the supervisory processes.

4. The EBA drives supervisory convergence[7], among other things, by annually setting out key topics for supervisory attention. This informs the CAs' processes for selecting supervisory priorities and influences supervisory practices on the selected topics.

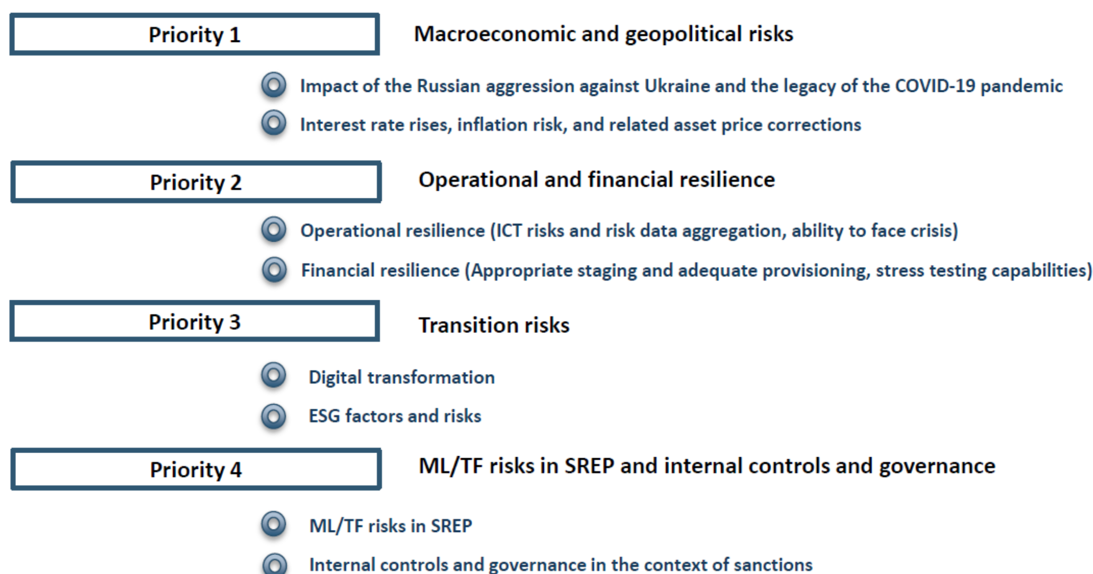
5. The European Supervisory Examination Programme (ESEP) for 2023 was sent to CAs and published in October 2022 to allow CAs to take the topics into account in planning their 2023 supervisory activities (Figure 2).

6. A survey was launched at the end of 2023 to follow up on the 2023 ESEP. The main goal of this survey was to see whether and how the topics identified in the ESEP were considered in the supervisory work performed by CAs during the year.

7. In addition, the implementation of the key topics of the ESEP in the Supervisory Examination Programmes (SEPs) of the closely monitored colleges was followed up by the EBA. In its analysis the EBA took into account the discussions within the college, the interactions with the institutions and the supervisory assessments carried out.

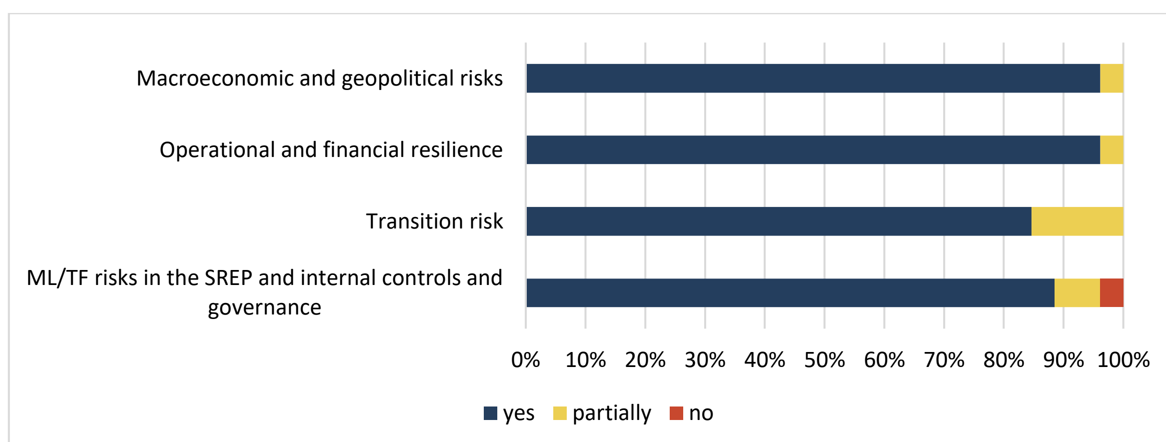
[7] Supervisory convergence is defined by the EBA as follows: a process for achieving comparable supervisory practices in Member States which is based on compliance with the EU rules, and which leads to consistent supervisory outcomes.

Figure 2: Overview of the four key topics and corresponding focus areas of the 2023 ESEP



8. The outcome of the survey among CAs indicates that almost all 2023 ESEP key topics were taken into account by CAs in setting their priorities. Figure 3 shows that three of the four topics were considered by all CAs (either in full or partially). For one topic, *'ML/TF risks in the SREP and internal controls and governance'*, one CA did not include this topic in its supervisory priorities, but decided to focus on other risk areas, based on its assessment of which risks are most relevant in the national context.

Figure 3: Key topics incorporated into CAs' supervisory priorities in 2023 (% of CAs)



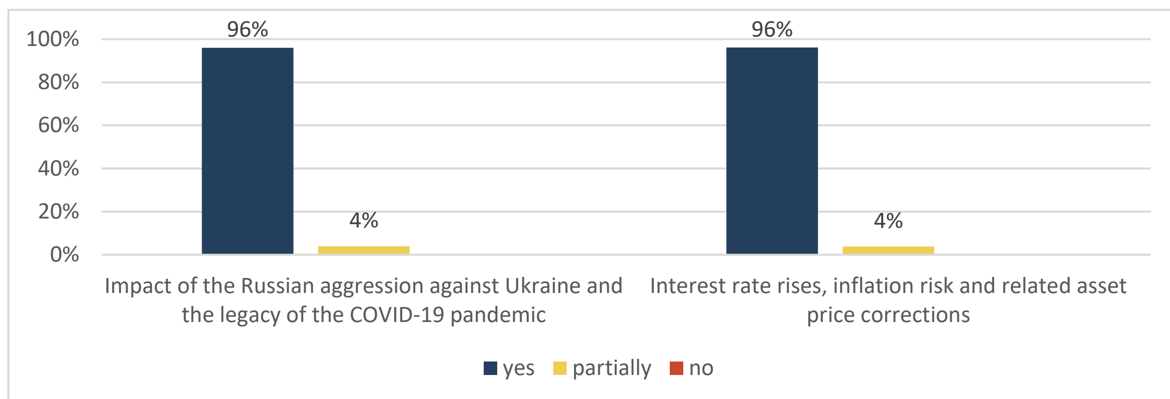
1.1.1 Macroeconomic and geopolitical risks

9. The impact of the Russian aggression against Ukraine was in 2023 one of the most prominent geopolitical risks. The aggression led to sanctions on Russia-based banks, companies and individuals, impacting institutions with participations in Russia, Belarus and/or Ukraine. As a second order effect, energy prices increased due to the sanctions, making banks more

vulnerable to defaults of indebted households as well as energy intensive corporates, of which some were just recovering from the COVID-19 crisis.

10. Figure 4 shows that all CAs took the relevant aspects of this key topic into account in 2023, while one CA did this partially, and focussed only on some aspects of the two focus areas.

Figure 4: Level of attention paid to focus areas under macroeconomic and geopolitical risks (% of CAs)



11. One of the outcomes of the analysis of CAs on this key topic was that the risk related to the Russian aggression and corresponding change in energy prices is overall stable (Figure 5), while the number of CAs which observed decreasing risk outnumbered the CAs which observed increasing risk. This could potentially be linked to the evolvement of energy prices which, after peaking at the end of 2022, in general declined, thereby potentially decreasing this risk for institutions. However, energy prices are in most Member States not back at pre-2022 levels and combined with the indebtedness of households and corporates after the COVID-19 pandemic could still lead to difficulties. Most banks with links to Russia decreased these links during 2022 and 2023 by following exit strategies, also potentially explaining the stable/decreased risk.

12. With regard to interest rates, inflation and asset price corrections, most CAs found that this risk was increasing during 2023 (Figure 5). This led to increased supervisory attention during the year for most CAs (Figure 6). This outcome tallies with the continuous interest rate hikes which occurred during 2023. Asset markets also remained volatile in 2023, especially after the banking stress in the United States and Switzerland in March 2023.

Figure 5: Outcome of risk assessments of CAs in relation to the macroeconomic and geopolitical risks (% of CAs)

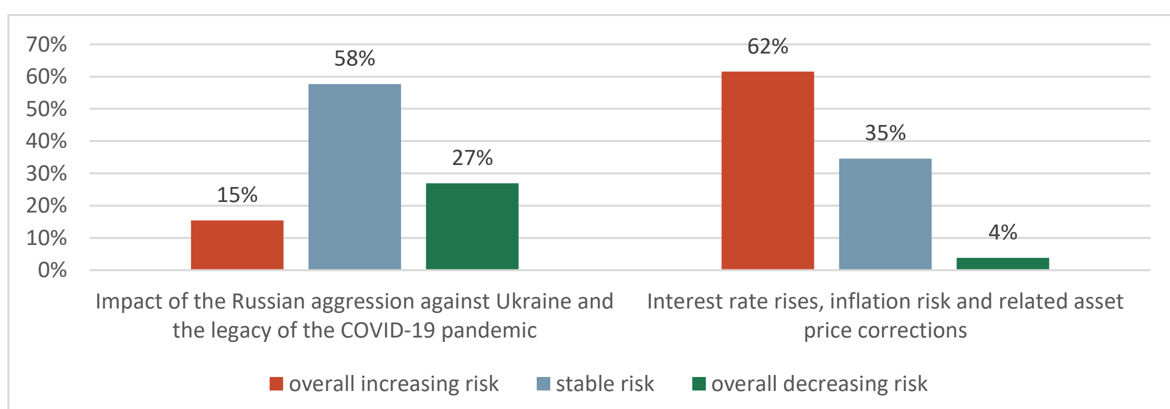
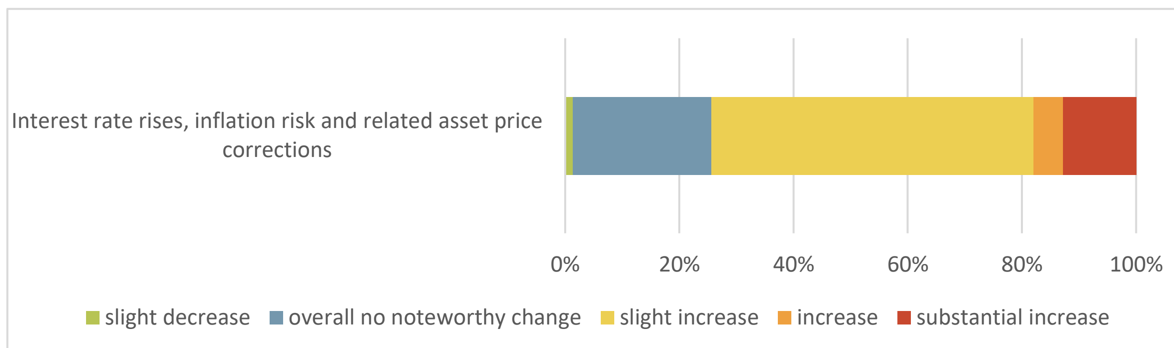


Figure 6: Change in level of attention paid to specific aspects of the macro and geopolitical risks and operational and financial resilience (% of CAs)



13. In analysing the management and impact of the geopolitical and macroeconomic risk at banks, supervisory authorities reported the following tools (listed in order of popularity):
    a) meetings with staff and management of institutions, either ad hoc or embedded in regular assessments;
    b) off-site analyses, either institution-specific or in the context of thematic reviews;
    c) additional reporting on the topic by means of e.g. a specific questionnaire/survey;
    d) on-site assessments of the risk.

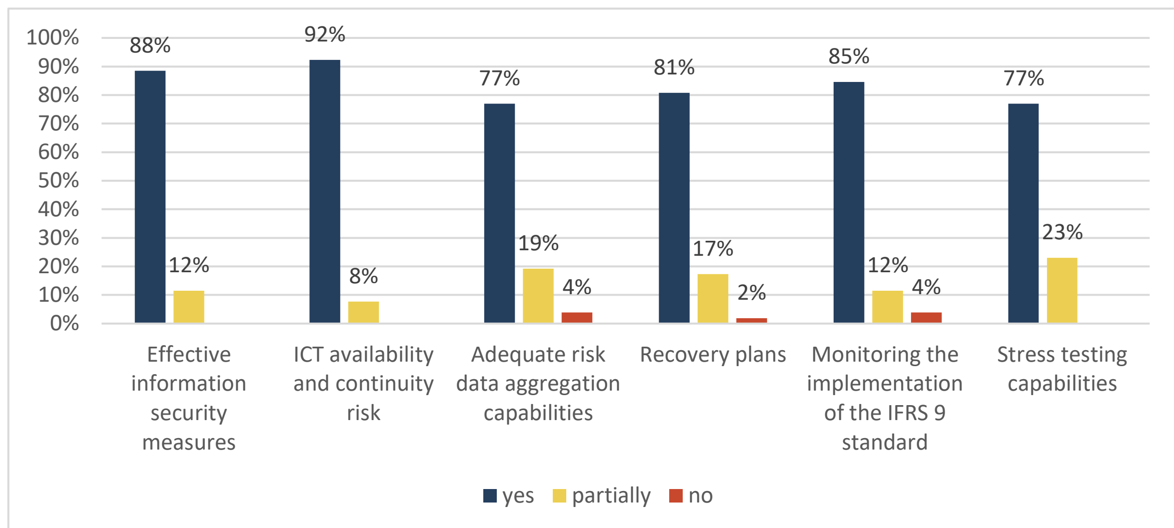
14. Throughout 2023, macroeconomic and geopolitical risk management and the impact at banks were consistently monitored by colleges. While the Russian portfolio still represents a significant downside risk for some banking groups, the majority of institutions notably decreased their presence in Russia. With regard to the interest rate hikes, banking groups demonstrated that they have proactive IRRBB management by employing hedging strategies and conducting backtesting. All in all, for most colleges the geopolitical and macroeconomic risk remains relatively stable, although continued vigilance and robust risk management remain important.

1.1.2 Operational and financial resilience

15. The second 2023 ESEP key topic is the resilience of institutions, both operationally and financially. Operational resilience is increasingly relevant since the expanded use of online channels after the pandemic. The stress observed in recent years also demonstrated the importance for banks to be able to produce trustworthy supervisory data in a short timeframe, an important part of operational resilience. Recent years also lead to valuable lessons learned, which should feed into the recovery planning of institutions. Finally, besides operation resilience, the COVID-19 crisis and the banking stress of March last year also showed the need for financial resilience in terms of capital and liquidity.

16. Based on the survey, most of the expectations regarding operational and financial resilience were taken into account by CAs (Figure 7). For three expectations, a small number of CAs did not reflect on them in their supervisory work, due to the (im)materiality of the risk or the composition of institutions' balance sheets or because the CA put the emphasis on other areas it deemed relevant.

Figure 7: Level of attention paid to the focal points under operational and financial resilience (% of CAs)



17. The outcome of CAs' risk assessments shows that for most focal points connected with operational and financial resilience, the risk is assessed as currently stable (Figure 8). The expectation of '*effective information security measures*' stands out, as more than one-third of CAs found that this risk is increasing. This is also linked to the increased geopolitical risk in recent years. Some CAs mentioned that the improvements in security measures of recent years were offset by the increased threat landscape. Although on average institutions demonstrate adequate resilience against cyber and operational threats, the inherent risk remains elevated. On ICT availability, CAs found that most institutions are compliant with the existing regulation, but with room for improvement. Risks related to ICT have increased and the increased outsourcing of ICT services complicates the risk even further.

18. Data aggregation capabilities received increased attention from CAs. Overall capabilities have in general increased in recent years, but a significant proportion of banks have not reached full compliance with supervisory expectations. A few CAs are still in the process of developing supervisory activities in this area.

19. On recovery planning, most CAs noted improvements to the content of the plans, including the scenarios used by institutions. The plans are on average credible, but there is room for improvement with regard to the number of institutions performing exercises and dry runs to test the recovery plans.

20. On the financial resilience risks, some authorities mentioned that the monitoring of the IFRS 9 standard was not relevant for some of the institutions (i.e. the ones using nGAAP). Also divergent practices among institutions were noted with regard to the implementation of the standard, which is in line with the outcome of the EBA monitoring report on the implementation of the IFRS 9 standard[8]. The attention paid by CAs to the implementation of IFRS 9 remained relatively stable over the year, with more authorities increasing the attention paid to this during the year compared to authorities decreasing it (Figure 9). Finally, on stress

[8] EBA/Rep/2023/36: IFRS 9 implementation by EU institutions, monitoring report, November 2023.

testing capabilities, CAs noted that the frameworks have been strengthened over the years and that results are in general reliable.

Figure 8: Outcome of risk assessments of CAs in relation to operational and financial resilience (% of CAs)

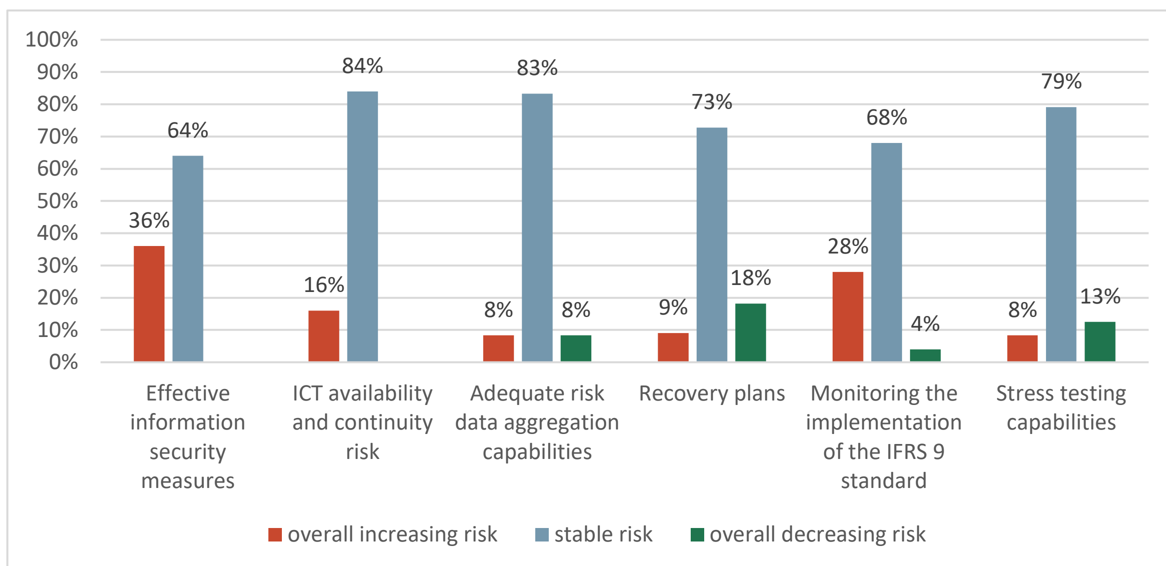
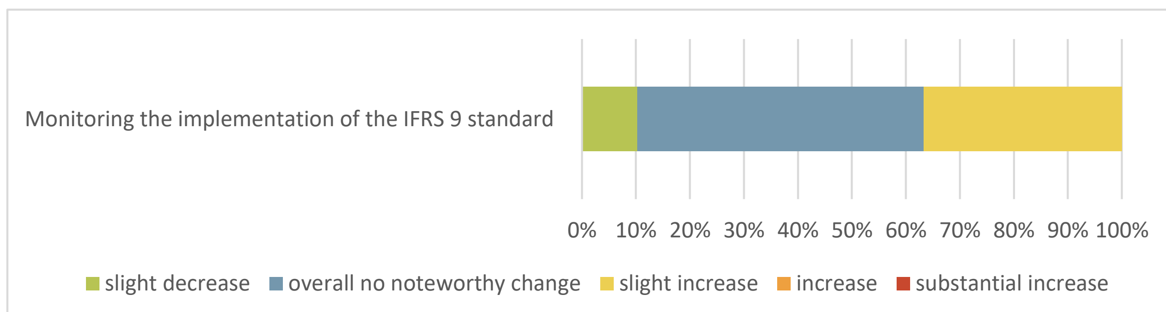


Figure 9: Change in level of attention paid to the implementation of the IFRS 9 standard during the year (% of CAs)



21. In the context of colleges' monitoring, the EBA confirmed that operational and financial resilience has been a focal point in supervisory risk assessments and college discussions, albeit with variations in coverage across the six identified focus areas.

1.1.3 Transition risk (digital transformation and ESG risk considerations)

22. Major transitions currently impacting the banking sector are the digital transformation and the increasing importance of taking ESG factors and ESG risks into account.

23. The digital transformation, with the transition to digital banking services instead of a branch network, poses challenges to institutions. It requires changes in IT systems and new investments, as well as an alteration of the cost structure. It could also impact the business model of institutions and require a better analysis and management of the risks related to ICT.

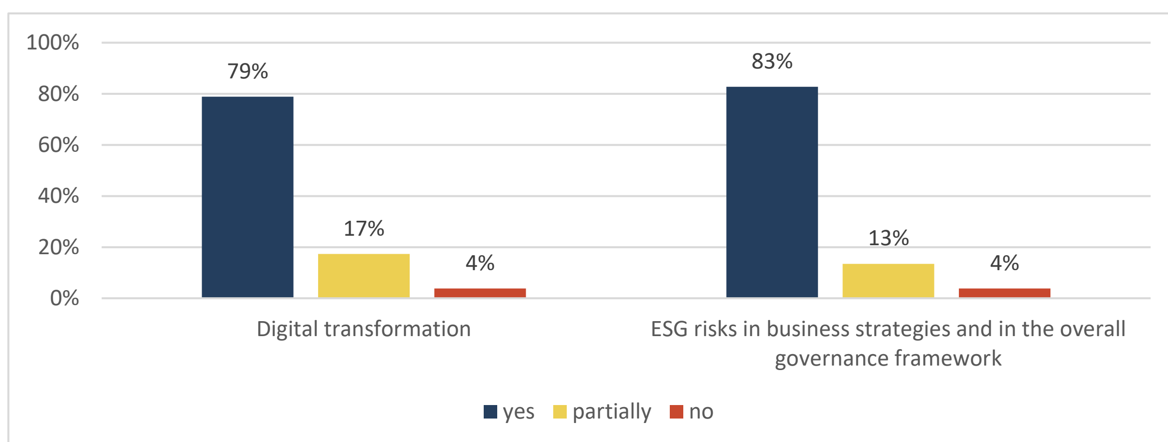
24. The specific ESEP expectations regarding the digital transformation which CAs were asked to assess were related to the suitability of the management function to drive and implement the digital strategy and of the supervisory function to monitor, challenge and assess the

transformation. CAs were also requested to assess the impact of the transformation on the business model and risk profile of the institutions.

25. The second transition risk, ESG, is also becoming more and more relevant and is connected to all risks a bank faces, as it impacts for example the business model, but also credit risk and market risk. The 2023 ESEP provides for specific expectations regarding ESG. CAs should analyse whether institutions are able to identify ESG risks and reflect them in their risk appetite and in their risk management framework, both for financial and non-financial risks. More specifically, the credit strategy of the bank should be fully aligned and reflect underlying ESG risk appetite.

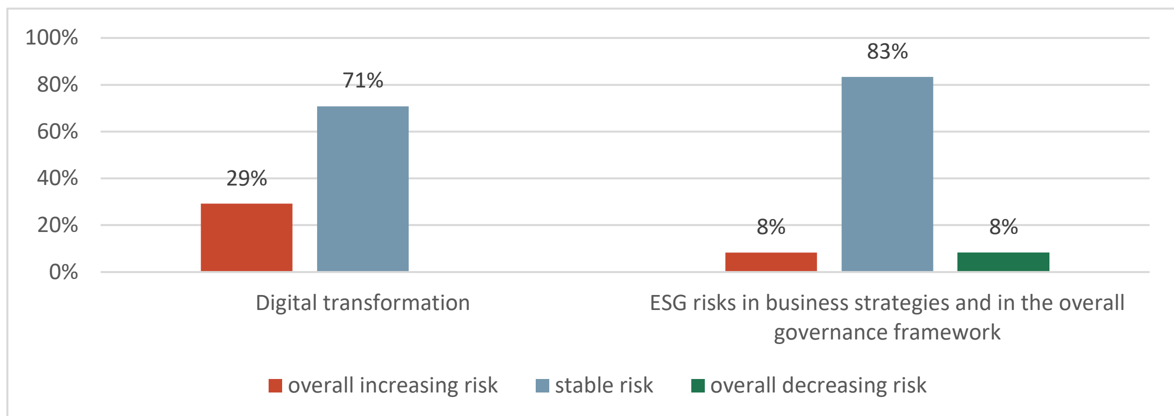
26. As for the previous key topics, most CAs included the two specific transition risks fully or partially in their activities for 2023.

Figure 10: Level of attention paid to the focal points under transition risk (% of CAs)



27. The outcome of the analysis of CAs regarding transition risks shows that both elements of this risk are considered to be stable overall, but a significant proportion of CAs (almost one-third) observed an increase in the risks related to the digital transformation (Figure 11). CAs acknowledge that the digital transformation is a necessity to remain competitive. An area of improvement for institutions is the competencies of board members regarding digital topics and the monitoring of the success of the digital transformation (e.g. by setting and monitoring a clear set of KPIs regarding the digital transformation). On the CAs side, the increasing focus on IT risks requires the hiring of supervisors with IT skills. On the ESG transition, CAs noted that the expectations of CAs regarding institutions are increasing and, although institutions are improving their efforts to comply with these expectations, they need to step up their efforts.

Figure 11: Outcome of risk assessments of CAs in relation to transition risk (% of CAs)



28. Regarding ESG risks, several authorities have formalised the expectations towards institutions and incorporated this into the supervisory process (e.g. the ECB Guide on climate-related and environmental risks for banks). Tools widely used among CAs to analyse ESG risk were off-site analyses, questionnaires (incl. self-assessments) and thematic reviews, thereby focusing on the materiality of the transition risk and the adherence to supervisory expectations.

29. In the context of colleges' monitoring, the EBA confirmed that supervisors within supervisory colleges discussed the two focal points of transition risk, although the alignment of institutions' credit risk strategy with ESG risk appetite was not fully integrated into assessments or college discussions by most supervisory colleges.

1.1.4 ML/FT risks in the SREP and internal controls and governance

30. ML/FT risks could have a detrimental impact on the institution's financial soundness and could also impair the viability and sustainability of the business model. Attention to this risk has been stepped up over recent years but increased attention from CAs is still necessary.

31. The 2023 ESEP suggested that CAs assess ML/TF risk in the context of the SREP[9]. ML/TF risks should be integrated into the relevant SREP areas, especially regarding the prudential implications linked to (changes in) the business model and regarding the compliance of the internal governance framework with applicable ML/FT requirements. This also includes an assessment of the responsibilities of the management body regarding ML/TF risks.

32. A specific part of ML/TF risks in the context of the 2023 ESEP is the implementation of the sanctions regarding Russia and Belarus. Prudential supervisors should, according to the ESEP, verify whether the internal control and governance frameworks are sufficient to do so, and whether they facilitate the timely implementation of such restrictive measures.

33. All CAs devoted attention to ML/FT risks during 2023 (Figure 12), while some did so partially by only focusing on specific institutions on a case-by-case basis (e.g. institutions with an exposure

[9] Since 2022 the updated SREP Guidelines have provided common guidance on how to factor the aspects relating to anti-money laundering and countering the financing of terrorism (AML/CFT) into the SREP and to cooperate with the authorities and bodies responsible for ensuring compliance with AML/CFT requirements.

to Russia). The outcome of CAs' assessments is that both the ML/TF risks in the SREP and the risk related to the internal controls and governance in the context of sanctions are stable, although slightly more authorities noticed a decrease compared to an increase in these risks (Figure 13). With regard to the risk related to the implementation and monitoring of the sanctions, there are two main drivers moving in opposite directions. On the one hand, institutions in general decreased their Russian exposure, thereby limiting the risk, but on the other hand the number of persons and firms sanctioned is still increasing, thereby potentially leading to increased risk for institutions in managing and adhering to the sanctions.

Figure 12: Level of attention paid to the focal points under ML/TF risks in the SREP and internal controls and governance (% of CAs)

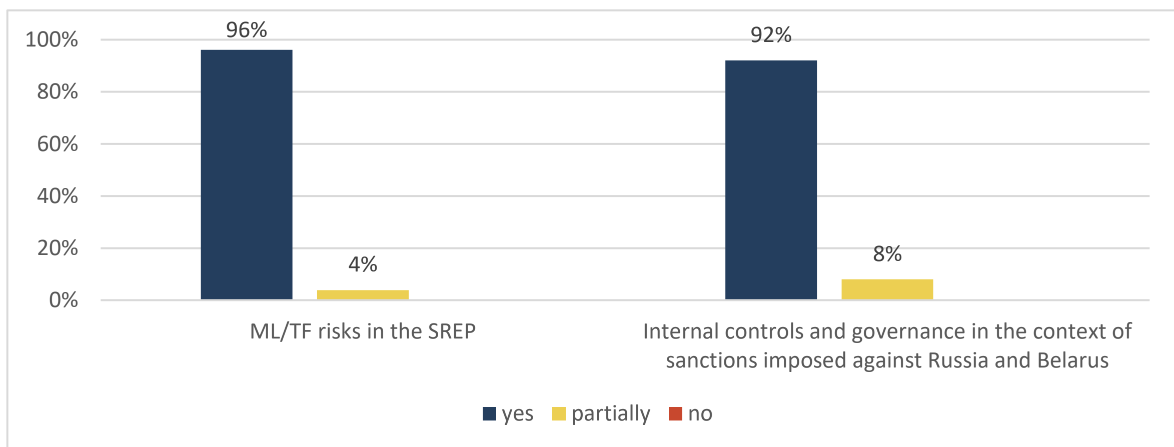
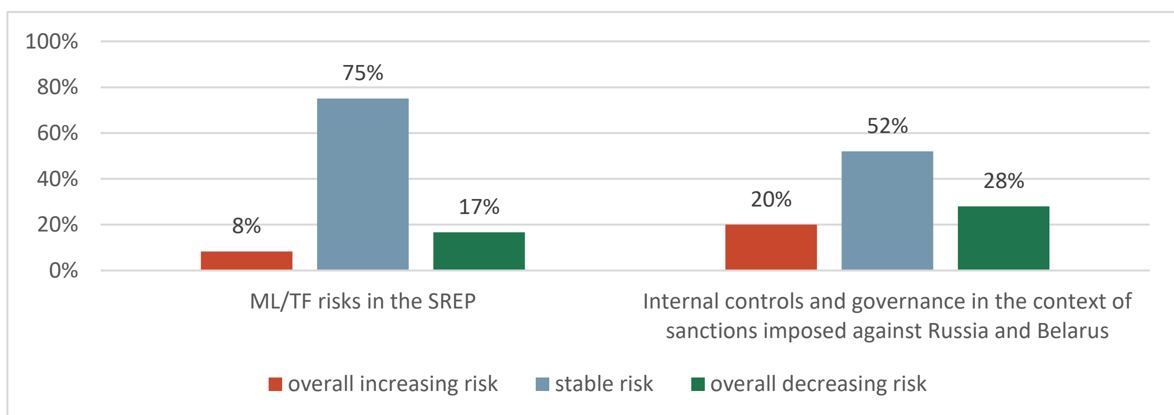


Figure 13: Outcome of risk assessments of CAs in relation to ML/TF risks in the SREP and internal controls and governance (% of CAs)



34. The analysis of ML/FT risks is for most CAs part of the SREP assessment. This is supplemented with a combination of off-site reviews, meetings with the institution and on-site inspections. Specifically, regarding the sanctions imposed on Russia and Belarus, CAs noted that institutions strengthened internal controls and governance to be able to implement and monitor the sanctions. Additional efforts were made regarding institutions with close links to Russia, in terms of business model or structure.

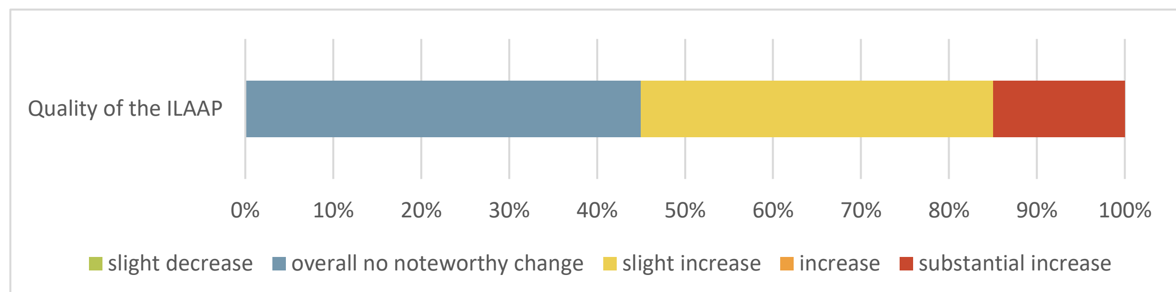
35. Supervisors have continued integrating the ML/TF risks into relevant SREP areas. The outcome of this assessment was discussed in some college meetings jointly held with AML supervisors, as confirmed by the EBA in the context of colleges' monitoring. These meetings aimed to facilitate the consideration of relevant information on AML/CFT risks within the supervisory colleges and have revealed that concerns persist regarding the adequacy of governance frameworks in addressing AML/CFT risks.

1.1.5 Other risks: ILAAP

36. The 2022 EBA convergence report concluded that in several instances supervisors requested improvements in some areas of the ILAAP. In 2023 this topic was still one of the key priorities for institutions. The ILAAP is also covered in the survey on Pillar 2 and liquidity (Section 1.2 of the current Report), confirming the findings of the ESEP questionnaire.

37. In terms of the role of the ILAAP in the monitoring of the liquidity and funding profile, this was generally deemed to be a relevant managerial tool used by institutions and very helpful for supervisors in supporting their ongoing assessment of liquidity and funding risks. The majority of CAs stepped up the attention they paid to the quality of the ILAAP during 2023 (Figure 14). Most probably this was related to the banking stress in March 2023 and the lessons learned from this period.

Figure 14: Change in level of attention paid to the quality of the ILAAP (% of CAs)



38. Regarding actions taken by CAs in the context of the ILAAP, some authorities highlighted this area in general during the SREP dialogue and addressed the ILAAP deficiencies in the SREP decision. Others focused more on specific parts of the ILAAP, e.g. behavioural models, withdrawal rates and contingency funding plans. Some CAs set specific expectations for banks regarding the quality and content of the ILAAP, e.g. on the ILAAP's better integration with the ICAAP / capital management / risk appetite frameworks and recovery planning as well as increasing the severity of the liquidity stress scenarios.

1.2 Convergence of supervisory practices in the context of Pillar 2 and liquidity measures

While a certain dispersion of supervisory decision-making is consistent with the need to take into account local market specificities and idiosyncratic situations, the analysis shows that there is still room for further consistency in the identification and treatment of risks covered by P2R across the EU.

The P2G setting framework has notably improved since the last survey in 2021, with nearly all authorities having a methodology in place, often aligning with the updated SREP GLs.

Authorities have been increasing the frequency of the monitoring of liquidity and funding risk in recent years. While the current framework is generally satisfactory, there are targeted areas where it could be improved, particularly in reporting frequency and deposit origination.

The implementation of CRR III / CRD VI and the subsequent review of the SREP GLs are expected to increase the convergence in the implementation of the framework, helping authorities to achieve greater consistency in the supervisory outcome in the context of setting Pillar 2.

1.2.1 Background

39. The analysis of the approaches employed by competent authorities (CAs) as a result of their SREP review (commonly known as 'Pillar 2') stands as a core element in the EBA's efforts to bolster supervisory convergence, consistent with its mandate in this area. The outcomes of this analysis also serve as an informative feedback loop for the EBA's future policy work in this domain. Specifically, they shed light on potential areas within the EBA SREP Guidelines that might necessitate clarifications or potential amendments based on the evolving practices observed.

40. Aligned with similar exercises conducted in 2019 and 2021[10], this analysis focuses on key supervisory areas, including the establishment of Pillar 2 Requirements (P2R) and Pillar 2 Guidance (P2G). With CRD V also introducing the possibility of setting Pillar 2 Requirements and Pillar 2 Guidance for the leverage ratio (referred to as P2R-LR and P2G-LR respectively), the analysis also assesses whether, and to what extent, CAs have implemented these measures. Additionally, given the insights revealed by the crisis events in spring 2023, particular attention was paid to supervisory approaches to liquidity and funding risk, as well as to institutions' risk management practices in these areas, and the taking up of supervisory measures.

41. To conduct the analysis, the EBA launched a survey to gather data[11] from CAs, the results of which are presented in this Report. The data collection involved obtaining detailed information at institution level, covering both quantitative and qualitative aspects. This included information concerning business model, SREP category, overall and risk-specific SREP scores, risk-by-risk P2R decomposition, P2G levels and their respective setting methodologies. A

[10] See the EBA Report on convergence of supervisory practices in 2021 and EBA Report on convergence of supervisory practices in 2019 for further details.

[11] The 2023 exercise collected data for end 2022. Based on the specific SREP calendar followed by CAs, data could reflect different SREP cycles.

specific questionnaire was designed to understand the approach of CAs to liquidity and funding risk supervision, incorporating focus areas and actions undertaken, if any, in response to the events of spring 2023.

42. As illustrated in the next section, while the coverage in terms of assets is exhaustive and could allow for general conclusions for large institutions at EU level (thanks to the contribution to the total assets of Significant Institutions – SIs directly supervised by the ECB), in the case of Less Significant Institutions (LSIs) directly supervised by national CAs, the limited sample size compared to the overall large number of LSIs, especially in some jurisdictions, might not necessarily lead to draw general conclusions or fully represent the entirety of the CAs' practices.

1.2.2 Data analysed

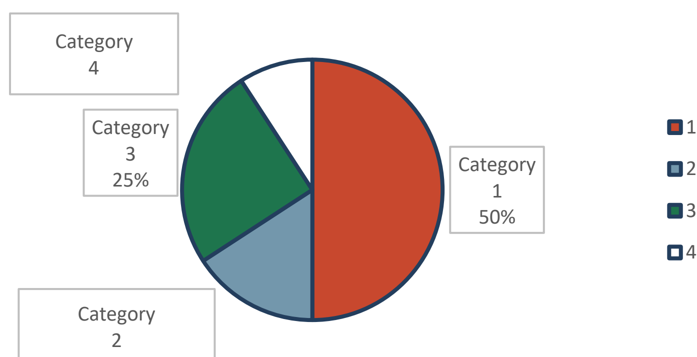
43. The sample utilised in the data collection comprises 194[12] banks under the direct supervision of 25 competent authorities from 26 EEA countries, representing 74% (84% when considering the data provided on an aggregate basis) of the European banking sector's assets. CAs were requested to provide data for institutions falling within their jurisdiction based on the following criteria:

   a. up to four 'Large' institutions – significant institutions established in a Member State;

   b. up to six between 'Medium' – total value of consolidated assets between EUR 5 billion and 30 billion – and 'Small' institutions – 'small and non-complex institutions' under CRR II – established in a Member State.

44. In detail, the sample is composed of 70 'Large' institutions, 54 'Medium' institutions and 70 'Small' institutions. In terms of SREP categorisation, the sample is mostly composed of category 1 institutions (50%), with a good proportion and representation of banks with a lower categorisation (respectively 16% belonging to category 2 and 34% to categories 3 and 4).

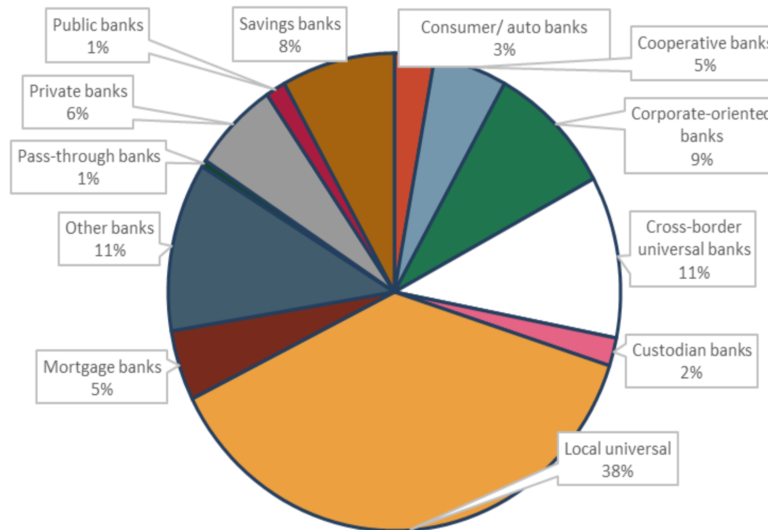
Figure 15: Distribution of SREP categorisation



[12] One authority submitted aggregated data for the medium and small institutions in its remit.

45. In terms of business model, the majority of the banks are classified as local universal. All business models are represented in the sample, with at least one bank falling into each category.

Figure 16: Distribution per business model category

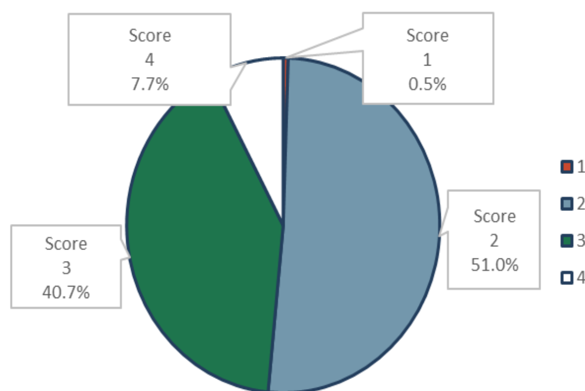


1.2.3 Overall SREP score and P2R

46. Considering the relevance of the SREP scores as a summary indicator of the overall risk to the institution's viability according to the SREP assessment, a focused explorative analysis has been conducted on both the assignment of these scores and their interplay with the setting of P2R.

47. In terms of the distribution of the overall SREP scores, Figure 17 illustrates that most of the institutions in the sample (more than 90%) have been assigned 'intermediate' scores of '2' and '3'. Score '4' was assigned to approximately 8% of the sample, while the least risky score ('1') was assigned to only one bank, equivalent to 0.5% of the overall sample. Notably, no institution in the sample was categorised as 'failing or likely to fail', hence no SREP score of 'F' was recorded. While it is acknowledged that intermediate and more granular scores, for instance via the so-called qualifiers (+ or – or +/- 0.5), with respect to the general ones listed in the EBA SREP Guidelines are employed by some CAs, in order to ensure the consistent treatment of the banks across jurisdictions SREP scores in the survey were requested as integers from 1 to 4. This could result in a more concentrated representation of the scores compared to the actual ones, due to the lower number of scores considered.

Figure 17: Distribution of the overall SREP score



48. To analyse the evolution of the overall SREP scores over time, a comparative analysis has been conducted between the distribution of scores from the previous assessment (carried out in 2022 with data from the end of 2020) and the current exercise. Only institutions included in both samples were considered. The majority of institutions present in both samples maintained their score, accounting for around 84%. Additionally, 8% improved their score, while an equal 8% experienced a decline in their scores. Overall, the scores exhibited high stability within each grade over time. Figure 18 provides a detailed breakdown of the transition across the scores observed between the two samples.

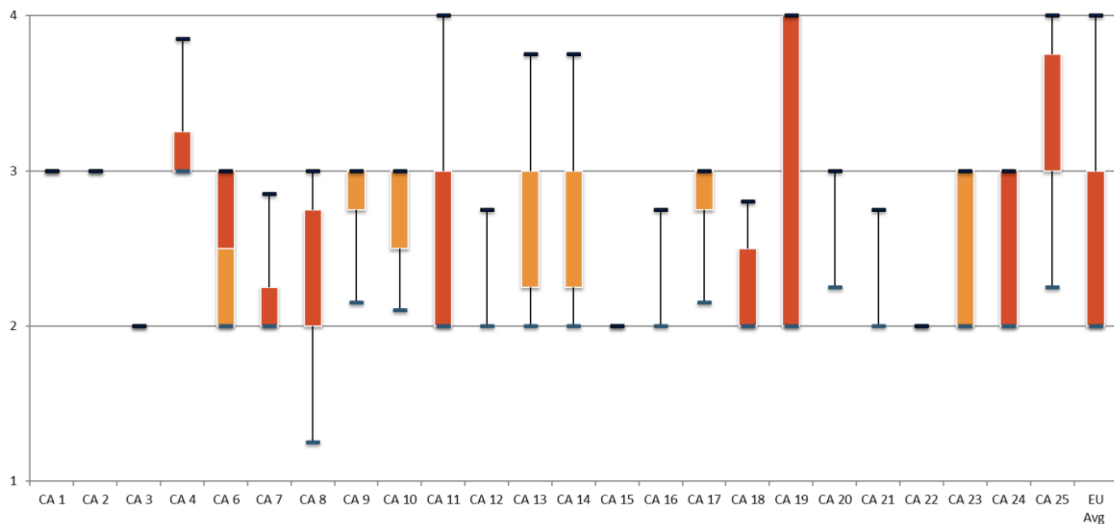
Figure 18: Distribution of the overall SREP score

Transition matrix	Scores 2022		
Scores 2020	**2**	**3**	**4**
2	**84%**	18%	0%
3	14%	**82%**	13%
4	2%	0%	**88%**
Total	100%	100%	100%

Sum of the percentages done by column

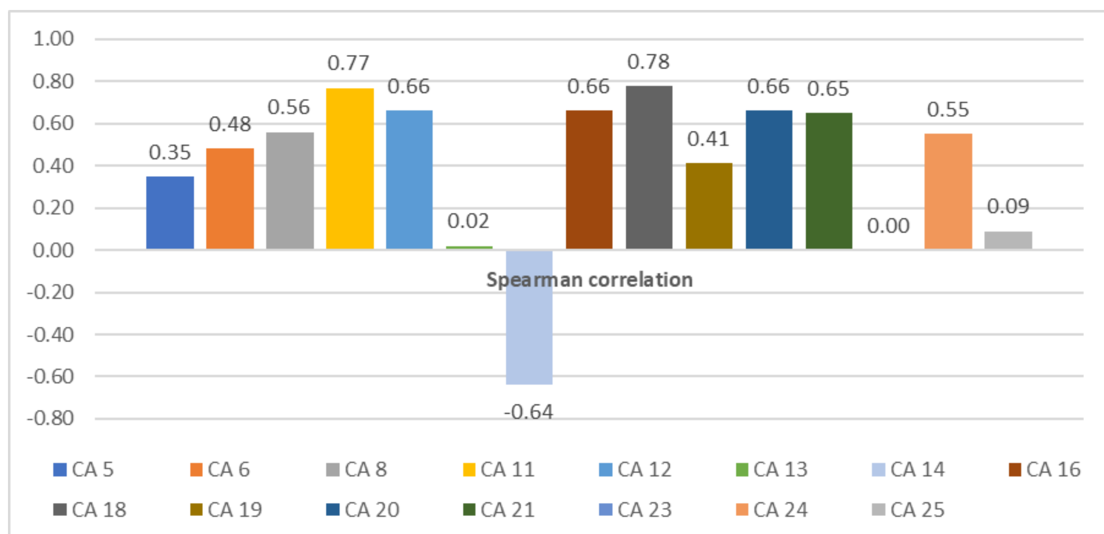
49. The stability of the scores and the predominant assignment of intermediate scores '2' and '3' have been observed not only over time but also across jurisdictions. When evaluating the dispersion of the SREP scores within and across CAs (Figure 19), the data confirms the previously highlighted general evidence, demonstrating an overall common trend across CAs.

Figure 19: SREP scores dispersion



50. To conclude the analysis on the overall SREP score, its relationship with P2R setting has been assessed through correlation analysis. Although the EBA SREP Guidelines do not prescribe a specific or automatic methodology to set the additional own funds requirements, exploring the relationship between additional own funds requirements and the scores could provide useful insights into the approaches taken by CAs, such as using the SREP score as an 'anchor point' for P2R. Data[13] shows a positive correlation between overall SREP score and the amount of P2R (Figure 20). Instances of a limited or negative relationship arise from some specificities of the institutions' business model (including impact of low-density RWAs) and the significance of concentration risk as a key P2R component (see also Figure 22).

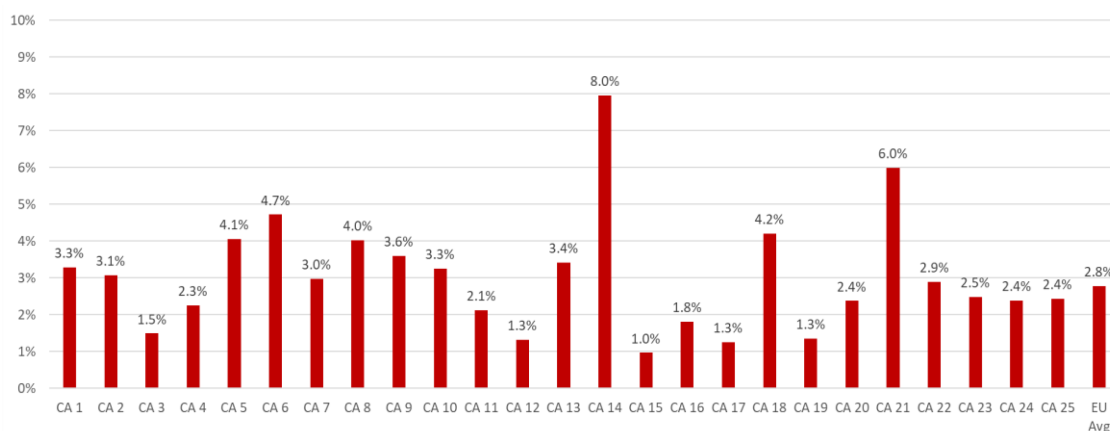
Figure 20: Correlation between overall SREP scores and P2R across CAs



[13] Data is reported if at least five observations per CA are available and co-movements between P2R and overall SREP scores have been observed (i.e. at least two different SREP scores are assigned to the institutions in the sample). Thus, some CAs are excluded from the correlation analysis as all the institutions submitted in the survey have the same SREP score (hence, a correlation cannot be calculated due to the absence of variability).

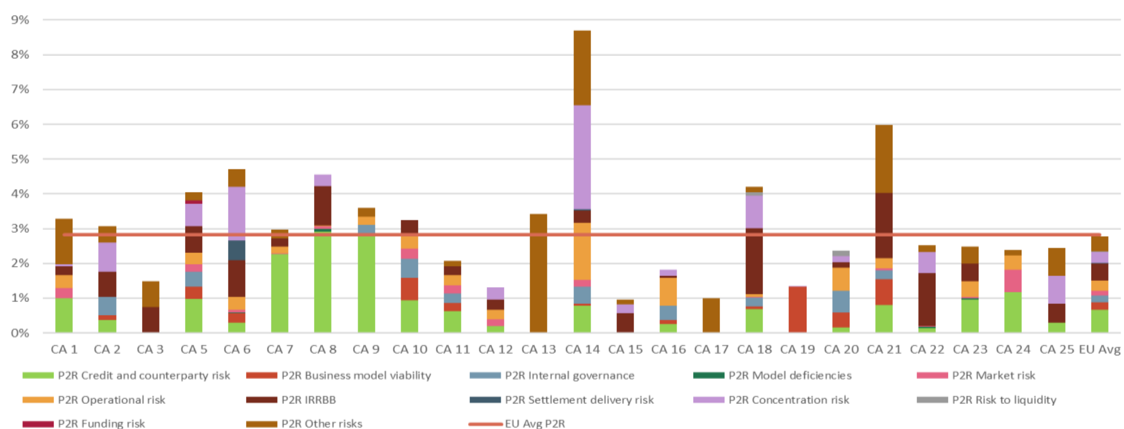
51. Shifting the focus to the analysis of the P2R add-ons, the survey outcomes indicate that the application of P2R is a common and well-established practice among all CAs. In both the previous and current data collection periods, all CAs utilised P2R to address risks not covered or not sufficiently covered by Pillar 1. Figure 21 illustrates the overall P2R amount by CA. Overall, there is some dispersion around the EU average (2.8%), with instances of a higher average amount (above 4%) observed in some jurisdictions. From the qualitative information collected on the methodology adopted to set P2R, higher values are in some cases associated with the relevant adjustment of the institutions' ICAAP figures and with the use of internal supervisory benchmarks. In some instances, high P2R add-ons were specifically associated with the specific concentration and business-model-specific risks (including impact of low-density RWAs) of the institutions.

Figure 21: Average P2R by CA (simple average)



52. To delve deeper into the composition and the amount of P2R across authorities, the risk-by-risk breakdown of P2R has been considered. It is evident that higher P2R add-ons typically correspond to cases where concentration risk, IRRBB and more generally 'other risks' are identified and deemed material by CAs, or in instances of low RWA density business models.

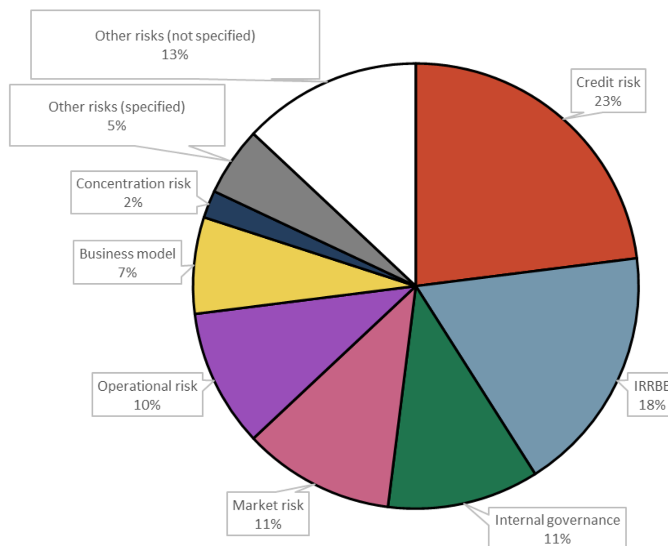
Figure 22: Average P2R risk-by-risk decomposition by CA (simple average)



53. Focusing on the risk-specific contributions to the overall setting of P2R at EU level, further broken down in Figure 23, it can be observed that risks already (but not sufficiently) covered by Pillar 1, such as credit and counterparty risk, market risk and operational risk, account for 44%

of P2R. Other significant areas are IRRBB, internal governance, business model and 'other risks'. At an aggregated level, concentration risk plays a limited role (circa 2%), while model risk for regulatory approved internal models is slightly above 0% and therefore not included in the pie chart below.

Figure 23: Average contribution to P2R by risk (weighted average by total assets)

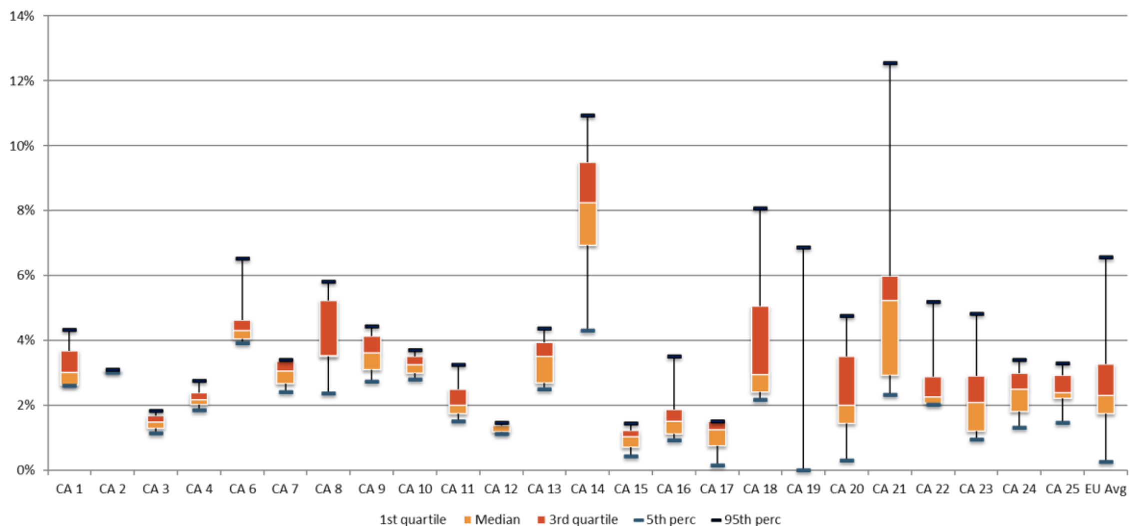


54. Due to the material impact of the 'other risks' category on the setting of P2R, a more detailed focus on its composition has been provided. The specified other risks relate to NPE coverage shortfall, commercial real estate risk weights, customer behaviour, ownership risk, CSRBB, pension risk, holistic risk and other individual add-ons (e.g. based on on-site findings). The data reveals that, in certain instances, 'other risks' can be classified within existing risk categories, while in the majority of the cases CAs did not offer additional specification regarding the nature of these 'other risks'.

55. In light of the insights gleaned from the in-depth examination of 'other risks', coupled with their observed materiality in shaping P2R and their dispersion across CAs, it is worth recalling the work performed at EBA level concerning the development of a Supervisory Risk Taxonomy. The aim of this effort was to foster a shared understanding of risks and their categorisation (including a mapping with the FINREP/COREP reporting), thereby enhancing convergence in risk identification and assessment and promoting consistent determination of capital requirements. Based on the findings, the EBA believes that there is still room for further convergence in the identification of risks and wider adoption of the Supervisory Risk Taxonomy. This would aim to mitigate excessive reliance on ambiguously defined risk categories as highlighted by the outcome of this analysis, and can contribute, instead, to a consistent identification and reporting of risks.

56. To conclude the analysis of P2R, the dispersion of P2R add-ons within and across CAs has been reported. Figure 24 shows that in certain jurisdictions P2R add-ons exhibit greater dispersion across institutions compared to others where add-ons tend to be more concentrated and less volatile around the median.

Figure 24: P2R dispersion within and across CAs



57. While the dispersion within the same CA might be fully justified by the specific risk profile of the institutions in scope of the supervisory review, the difference observed across authorities could also more generally reflect different approaches in place. Looking at the methodologies employed by CAs[14], the following common features have been observed:

   a. Eight CAs explicitly mention the use of the SREP scores (taking into account both the inherent risk and the risk control components) as the base for P2R determination. Others granted a greater role to the ICAAP calculations (where reliable), especially for those risks included in the institutions' ICAAP and not explicitly covered by the own funds requirements.

   b. For the setting ofP2R for risks not covered by own funds requirements, authorities generally relied on internally developed methodologies and benchmarks. With specific regard to the IRRBB, some authorities mentioned the use of the supervisory outlier test (SOT) as the starting point for P2R, taking into account the worse impact from the economic value of equity (EVE) SOTs and the net interest income (NII) SOT. Another recurring methodology is the use of the Herfindahl-Hirschman Index (HHI) to determine the P2R add-on for concentration risk (single-name, sectoral, geographical concentrations), in line with the provisions set out in the EBA SREP Guidelines. Application of P2R was limited or absent for addressing liquidity shortcomings. The few cases observed relate to the coverage of the FX liquidity risk.

58. Generally looking at the collected data and the analysis conducted on the SREP scores and P2R, some P2R dispersion is still observed across authorities, with some CAs displaying limited discrimination across institutions in their remit and others with a more dispersed P2R. In limited instances, the risk-by-risk decomposition of P2R is taking place ex post or not at all, which is not in line with the EBA SREP Guidelines.

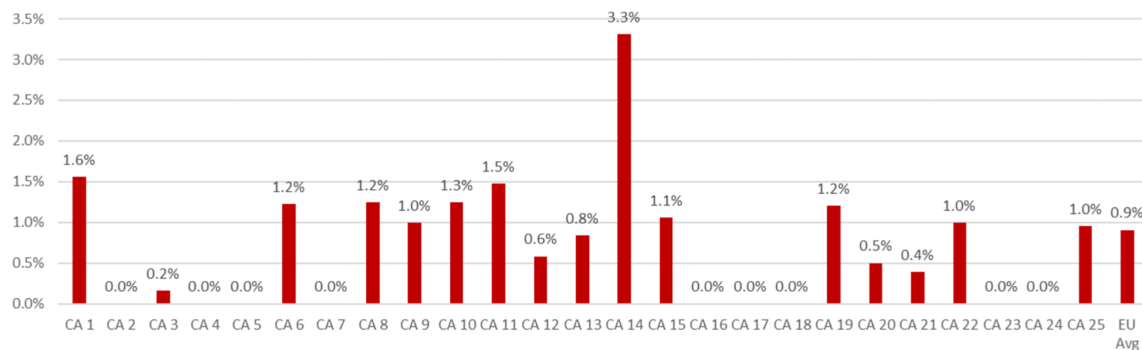
[14] It is to be noted that, while the coverage in terms of assets is exhaustive and could allow for general conclusions especially for large institutions, the elevated number of LSIs within some jurisdictions means that selecting six institutions for this category may not fully represent the entirety of the CAs' practices.

59. Regarding the setting of the P2R-LR, only one authority already set it as of the end of 2022 reference date. Upcoming trends in this area, including as a result of the implementation of the revised EBA SREP Guidelines started in the 2023 SREP cycle, will be assessed as part of the future monitoring exercises of supervisory convergence.

1.2.4 Pillar 2 Guidance

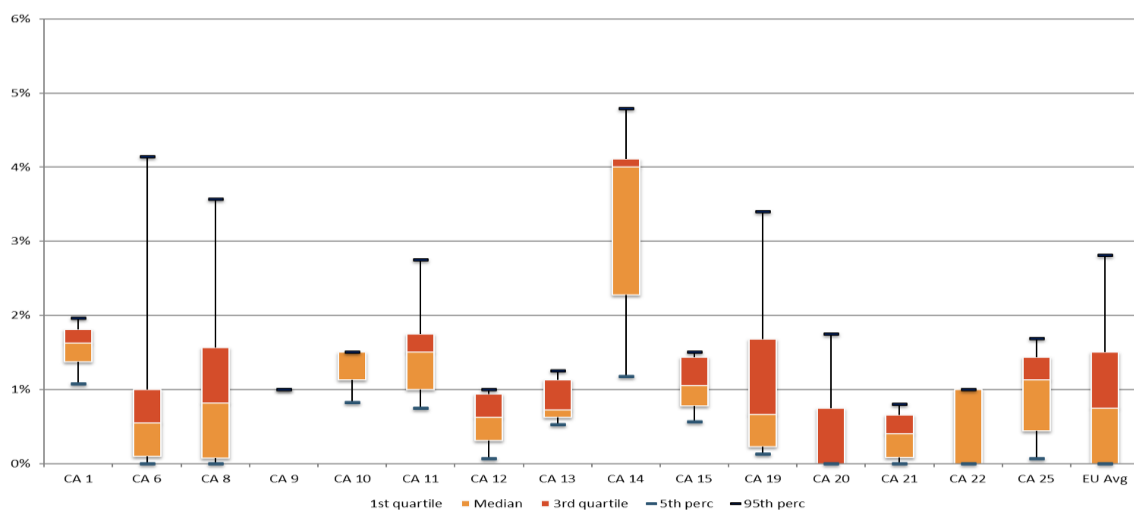
60. While in 2019 only 12 out of 22 CAs were applying P2G, and in 2021 20 of the 27 CAs implemented P2G, all authorities in the sample have now developed an internal methodology to set P2G. However, despite this undeniable positive development, Figure 25 shows that limited divergence in the P2G levels among those authorities remains.

Figure 25: Average P2G by CA (simple average)



61. This evidence is also confirmed by Figure 26 below, where, in a similar way to what has been observed in the P2R dispersion analysis, the P2G set by some CAs exhibits greater dispersion, while in other instances P2G is more concentrated around the median. As with P2R, low RWA density business models would also impact the P2G dispersion.

Figure 26: P2G dispersion within and across CAs



62. Based on the collected data on the approaches followed by CAs in the setting of P2G, the dispersion could be explained by the different methodologies used for determining P2G. Different calculation methods were noted, especially regarding the following aspects:

a. Use of a P2G ceiling (a small number of authorities mentioned different thresholds, such as 3.5%, 4.5%, 5% and 10%) and hurdle rates (mostly corresponding to the breach of the overall capital requirement, OCR, or total SREP capital requirement, TSCR, by the institutions' capital requirement in case of stress) to set P2G has been observed. The application of the hurdle rates is the main reason for the zero P2G set by some authorities.

b. Use of the bucketing approach as the starting point for the setting of P2G. While it has been observed that several CAs are already using the bucketing approach – as envisaged by the revised EBA SREP Guidelines that entered into force from the 2023 SREP cycle – others did not employ this methodology. Further progress in this space can therefore be expected as a result of the full implementation of the aforementioned revised Guidelines and could be appreciated in a future monitoring exercise in this area.

63. In terms of P2G's scope of application, all institutions – including Less Significant Institutions – are part of the P2G setting exercise. The updating frequency by CAs is usually aligned with the supervisory stress test and based on the SREP engagement model, usually referring to the following timeframes: e.g. category 1 institutions – at least annually; category 2 institutions – at least every two years; category 3 and 4 institutions – at least every three years.

64. As far as the setting of P2G-LR is concerned, similar observations to those on P2R-LR can be made. In fact, only one authority already set P2G-LR as of the end of 2022 reference date. The evolution of practices in this respect might be appraised in the future, as its application by CAs could become more widespread.

1.2.5 Supervision of liquidity

65. In the wake of the crisis events in 2023 and the heightened awareness they brought regarding the significance of monitoring liquidity and funding risks, as well as the supervisory capacity to implement effective corrective measures for problematic institutions, the survey has been expanded to encompass – primarily at a qualitative level – the strategies adopted by CAs in overseeing these risks and, more broadly, in issuing qualitative supervisory measures. For these specific topics, the most recently available information (including, where available, 2023 evidence) and approaches were requested from CAs.

66. Starting from the liquidity and funding risks, CAs have systematically increased the monitoring frequency of institutions' liquidity and funding profile, leaving enhanced and more in-depth interaction to treatment on a case-by-case basis in line with the specific institution risk profile. The most common focus areas during 2023 were:

a. funding plans, cost of funds and interest rate pass-through from the assets to the liabilities side;

b. liquidity stress testing;

c. content/quality of the liquidity buffer;

d. use of online deposit platforms and more general deposit behaviour.

67. Some authorities performed dedicated impact assessment analysis following the Russian invasion of Ukraine or the 2023 spring crisis events, testing the sensitivity of the institutions to a scenario similar to the Silicon Valley Bank case. Other CAs are planning to launch dedicated thematic and horizontal reviews of institutions' liquidity and funding plans. Several authorities prioritised monitoring of liquidity and funding as key priorities for the coming years, in line with the supervisory priorities set out in the 2024 EBA ESEP[15].

68. In addition, the type of liquidity and funding-related supervisory measures has been analysed. Sixteen authorities have institutions in their remit with qualitative and/or quantitative measures in place, stemming from the inherent liquidity and funding risk or the related risk management framework. These requirements are mostly institution-specific and mainly resulted in:

    a. setting higher liquidity buffers mandatorily prescribed for individual banks (including a minimum FX LCR as well as a minimum survival period);

    b. setting higher outflows for a specific part of funding and requiring a minimum survival period based on those higher outflows;

    c. imposing limits on asset encumbrance;

    d. asking for a targeted update of funding plans to address the TLTRO repayment;

    e. asking for an adjustment of the internal limits adopted in institutions' risk appetite framework.

69. A couple of authorities used more general measures applicable to all LSIs in terms of a survival period (at least six months) or an additional requirement for LCR for deposit concentration introduced on a sector level for level playing field reasons.

70. To conclude the deep dive on this topic, CAs were asked to provide their views on the adequacy of the current liquidity reporting framework. Overall, the current framework is considered sound, but some improvements are needed to improve the ability of CAs to proactively monitor a fast-moving risk like liquidity and enhance the harmonisation of reporting practices. Suggested targeted areas of improvement concern:

    a. increasing the reporting frequency (mainly for maturity ladder and asset encumbrance);

    b. origination of deposits (e.g. online accounts, which may have an impact on the mobility of cash funds);

    c. higher granularity for behavioural cash flows, downgrade triggers, short-term buckets;

    d. inventory of where collateral is held;

    e. breakdown of central-bank-eligible assets mobilised/non-mobilised;

    f. net liabilities of assets from correlated clients/groups;

    g. accounting treatment of the assets in the liquidity buffer.

[15] See the EUROPEAN SUPERVISORY EXAMINATION PROGRAMME FOR 2024 for further details.

1.2.6 Qualitative measures

71. In terms of the more general qualitative supervisory measures, an overall convergence across authorities has been observed with regard to the most common areas which are most usually subject to this kind of supervisory action. In more detail, several CAs flagged the following ones as the most frequently recurring: i) governance and internal control framework; ii) business model; iii) credit risk management; and iv) operational risk and ICT risk/resilience aspects.

72. From those authorities that provided a split between the liquidity and funding-related measures and the other type of supervisory measures, it proved that the former accounted for around 10% to 15% of the overall supervisory measures in 2023.

1.3 Results of peer reviews and benchmarking exercises

1.3.1 Peer review on credit valuation adjustment risk

73. The peer review on credit valuation adjustment (CVA) risk[16] analysed the effectiveness of the supervisory practices of a specific set of CAs regarding their assessment of CVA risk of the institutions under their supervision, with a view to strengthening consistency and effectiveness of supervision in this area. In particular, it focused on the practices employed for the supervision of the application of Commission Delegated Regulation (EU) 2018/728, which specifies the procedures for excluding transactions with non-financial counterparties established in a third country from the own funds requirements for CVA risk.

74. The peer review found that the CAs fully implemented the relevant section of the EBA's SREP Guidelines in the context of CVA risk, and that the actual approaches employed by CAs towards the supervision of CVA risk satisfy the regulatory requirements and are consistent with those Guidelines. Nevertheless, the peer review suggested some follow-up measures for CAs to address some deficiencies and strengthen supervision. These include, inter alia, a review of the resources allocated to the supervision of CVA risk, the performance of CVA risk assessments also on smaller institutions, the monitoring of the CVA risk of transactions excluded from the own funds requirements for CVA risk, and a review of compliance with the requirements of Commission Delegated Regulation (EU) 2018/728.

75. Finally, the peer review also identified some best practices related to the supervision of CVA risk, that may be of benefit for other CAs to adopt. These include keeping institutions informed regarding supervisory expectations and actions to address deficiencies on CVA risk, and the supervision of CVA risk which ensures a holistic view that takes into account risks of a similar nature, such as market and counterparty credit risk, and interaction with valuation practices, accounting rules and other types of adjustments.

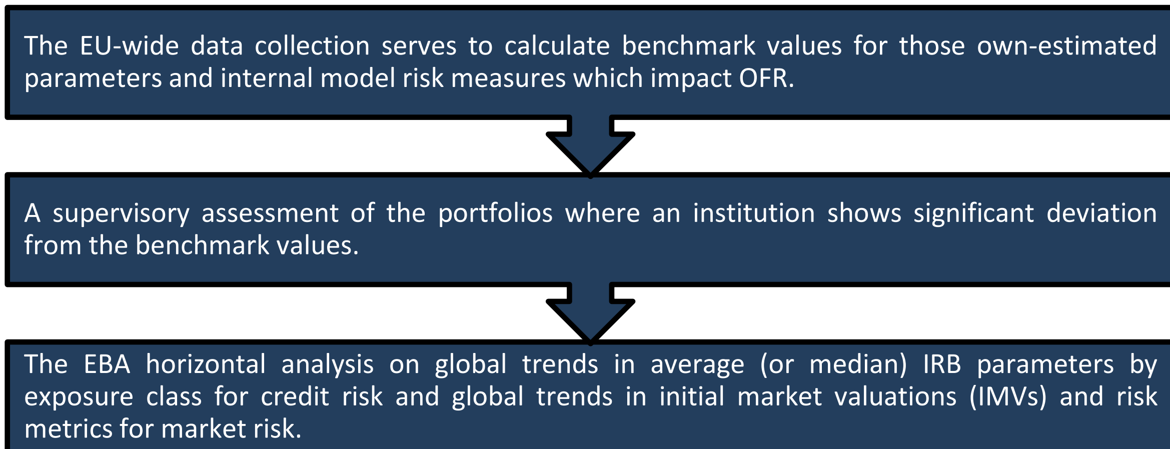
1.3.2 Benchmarking of internal models

76. Since 2015, the EBA has been conducting an annual EU-wide supervisory benchmarking exercise for credit and market risk models, in accordance with Article 78 of the CRD. This article requires, inter alia, that i) CAs conduct an annual assessment of the quality of internal models; and ii) the EBA produces reports to assist CAs in this assessment. This regular benchmarking exercise covers the entire population of institutions authorised to use internal models for calculating own funds requirements (OFR). The exercise is based on granular data collection, which allows the EBA to provide the supervisors with a statistical tool to compare results produced by the banks' internal models. While no perfect alignment of the results is expected, significant divergent results are brought to the attention of supervisors. These significant outliers are analysed and explained by supervisors where appropriate. Based on these data collections and follow-up analysis, the EBA publishes two horizontal reports on the outcomes

[16] Peer Review Report on credit valuation adjustment (CVA) risk (EBA/REP/2023/15).

of the yearly benchmarking exercises[17], one with respect to credit risk and another one for market risk.

Figure 27: The three pillars of the 2023 market and credit risk benchmarking exercise



The 2023 Market Risk Benchmarking Exercise shows positive results in term of dispersion for the internal model and FRTB standardised approach, but supervisory attention is still needed for potential issues linked to specific aspects of the exercise.

77. The report summarises the data submission collected from the end of 2022 until September 2023; the 2023 results show a significant reduction in the dispersion of the initial market valuation (IMV) versus the 2022 exercise regarding the equity and interest rates asset classes. The credit spread and commodity asset classes remained stable versus the 2022 dispersion. Nonetheless, for the FX asset class average interquartile dispersion (IQD) increased significantly (8% vs 3% in 2023). Excluding the problematic instruments, the average IQD of the FX asset class is 2%, which is in line with the submissions for the previous exercises. The commodity asset class remains a very high IQD asset class (14% vs 24% in 2022).

78. From a risk factor perspective, FX portfolios exhibit a lower level of dispersion than the other asset classes. In general, variability is substantially lower than in the previous exercise. This is likely due to an improvement in the data submission, which decreased the dispersion of the risk measures in general.

79. Regarding the single risk measures, across all asset classes except for commodities the overall variability for value at risk (VaR) is lower than the observed variability for stressed VaR (sVaR) (16% and 21%, compared to 21% and 28% in the 2022 exercise, with 27% and 31% in 2021 and with 18% and 29% in 2020). More complex measures, such as the incremental risk charge (IRC), show a higher level of dispersion (42%, compared to 45% in the 2022 exercise, with 43% in 2021 and 49% in 2020).

80. Positive results are also shown in the reporting of the FRTB ASA's own funds requirements dispersion for the 2023 exercise, which is generally lower than the internal model results, even

[17] EBA publishes annual assessment of banks' internal approaches for the calculation of capital requirements | European Banking Authority (europa.eu).

if some specific portfolios showed unexpectedly high dispersion, which the supervisors need to examine attentively.

The 2023 Credit Risk Benchmarking Exercise highlights the ongoing need for continuous monitoring of potential undue variability in own funds requirements across institutions, particularly concerning the adoption of the IRB roadmap.

81. The reference date for data collection for the credit risk exercise was 31 December 2022 and institutions submitted data between April and September 2023.

82. The credit risk report outlines the evolution of the variability of the risk parameters over the period 2015-2023. This helps supervisors assess progress in achieving consistent risk assessments. In particular, regarding the PD parameter, the corporate asset class exhibits a reduction in variability during the period under consideration, whereas for the other asset classes the variability seems more stable. As far as LGD is concerned, the variability remains quite stable across all asset classes during the period considered, with some minor exceptions, such as in the case of SME corporate, where more noticeable fluctuations in the coefficient of variation[18] are observed in the first four years of observation (2015-2019).

83. Furthermore, for the first time the report analyses the impact of prudential adjustments on the estimated PD, providing evidence that such adjustments could explain part of the variability. In addition, a specific analysis has been conducted on the LGD of the 'other retail' portfolio, identifying some possible drivers of the variability in the estimated LGD and showing the role that the type and degree of coverage of the guarantees can play in explaining the variability of the LGD. The results of these horizontal analyses are expected to support supervisory reviews to identify areas requiring further convergence efforts.

84. The report also tracks the adoption rate of the IRB roadmap across EU institutions. The increasing share of material model changes that have been approved for all asset classes suggests that banks are making progress in implementing the IRB roadmap, a key initiative for supervisory convergence. Such conclusions encourage supervisors to prioritise their review activities to ensure banks are on track with IRB roadmap implementation.

85. Going forward, the EBA expects that the harmonisation of terminology and concepts set out in the products of the IRB roadmap and the ongoing monitoring and study of potential determinants of the variability of risk parameters would support supervisory convergence.

1.3.3 IFRS 9 implementation monitoring report

86. Since the publication of the first IFRS 9 monitoring report[19] in November 2021 and following the staggered approach agreed in the 2019 IFRS 9 roadmap[20], the EBA has continued its monitoring of IFRS 9 implementation across EU institutions. The IFRS 9 benchmarking reporting

[18] The variability of both PDs and LGDs reported by the institutions (EAD-weighted average at asset class level) is represented in terms of the coefficient of variation (standard deviation divided by the average).

[19] IFRS 9 2021 monitoring report (europa.eu).

[20] EBA publishes its roadmap on IFRS 9 deliverables and launches IFRS 9 benchmarking exercise | European Banking Authority (europa.eu).

has been expanded to encompass additional portfolios, notably the high default portfolios, included in the scope of the ITS on supervisory benchmarking. Following the launch of a new ad hoc data collection (the 'third ad hoc data collection'), a second IFRS 9 monitoring report was published in November 2023[21]. This report summarises the key findings from the EBA's analysis of IFRS 9 benchmarking data and information collected and follows up on previous findings aiming to assess any improvements made by banks to their expected credit loss (ECL) models to address supervisory concerns.

87. According to the 2023 report, while significant progress has been generally observed in the implementation of ECL impairment models, latest investigations have revealed diverse approaches adopted by institutions for estimating ECLs. This heterogeneity may account for part of the variability observed on final ECL figures among institutions and resulting impacts on prudential metrics. Importantly, analyses have confirmed that many institutions have yet to address practices previously identified as raising prudential concerns, such as those related to significant increases in credit risk (SICR), PD modelling, overlays and forward-looking information (FLI) incorporation processes within the IFRS 9 framework. Additionally, a varying degree of implementation of backtesting methodologies on ECL models was noted, with some institutions lagging behind their peers, and, more worryingly, a very limited use of backtesting analysis for the periodic review of IFRS 9 models. Given the important implications that ECL figures have for the consistent application of the regulatory capital standards and for the ultimate building of appropriate levels of provisioning, the EBA has consequently urged institutions to address in a more definitive manner the identified areas of improvement.

88. The EBA will continue monitoring and promoting the consistent application of IFRS 9 going forward, with the benchmarking exercise serving as a primary monitoring tool. Supervisory oversight is also expected to play an increasingly crucial role, with heightened scrutiny and follow-up on key findings highlighted in the EBA IFRS 9 monitoring reports.

[21] IFRS 9 2023 monitoring report (europa.eu).

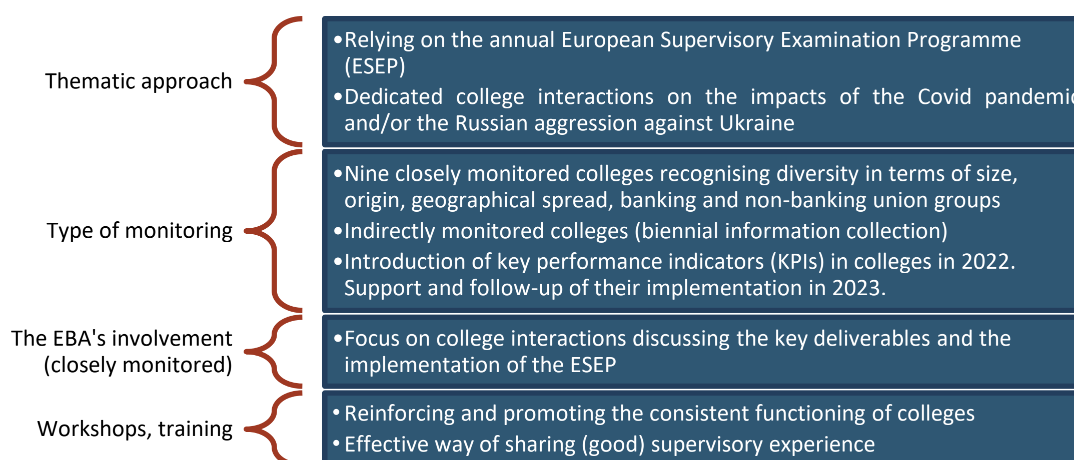
2. Convergence in supervisory colleges

2.1 Background

89. Colleges are a permanent and essential feature of the cross-border supervisory landscape. The EBA is required to promote the efficient and effective functioning of colleges of supervisors for cross-border institutions across the Union, including in times of turbulence[22]. The EBA's supervisory college monitoring approach, by which the EBA facilitates and assesses the implementation of EU regulation and various EBA policy products, has continuously adapted to the increasing experience supervisory colleges have gained in recent years. As colleges became more experienced in operating according to the delegated and implementing regulation[23], the focus of the EBA's monitoring has shifted towards the key college deliverables.

90. For the 2021-2023 college monitoring approach (Figure 28), the EBA monitored closely a limited number of colleges, which were nevertheless diverse in terms of business model, origin, geographical spread and size, the so-called *'closely monitored colleges'*. The EBA's involvement in these colleges encompassed attendance at college meetings, following the group risk assessment and joint decisions on capital and liquidity processes, as well as the process for the assessment of the group recovery plan and the relevant joint decision. A key feature of the approach was the introduction of key performance indicators (KPIs) for enhancing and assessing the effectiveness of college activities. Aiming to share supervisory experience and best practice and enhance supervisory convergence, the EBA also organised workshops on the various aspects of the supervisory cycles, including processes around the joint decisions and the respective group risk assessments.

Figure 28: The EBA's 2021-2023 college monitoring approach



[22] Articles 8(1)(i) and 21 of the EBA's founding regulation (Regulation (EU) No 1093/2010).

[23] Commission Delegated Regulation (EU) 2016/98 and Commission Implementing Regulation (EU) 2016/99.

91. In 2022 four qualitative key performance indicators (KPIs) were introduced for supervisory colleges. Competent authorities that participate in colleges are expected to consider these qualitative KPIs and the respective measurement points[24] in their activities and in the context of organising the key deliverables[25] of the college. The focus in this year's Report is on the outcome of the monitoring of the implementation of the KPIs in colleges.

2.2 Outcome of the EBA key performance indicators stocktake exercise

92. In autumn 2023, the EBA ran a stocktake exercise seeking college members' input on the self-assessment of the implementation of the KPIs. The high-level overall conclusions are:

The 'annual' college cycle is functioning well. Most of the measurement points in relation to the KPIs were achieved to a great extent for the majority of colleges.

The quality of the key deliverables is deemed to have improved significantly and is at a good level.

The consolidating supervisors prepare and facilitate the college meetings well.

Information sharing could still be enhanced, in particular information on early warning signs, potential risks and vulnerabilities.

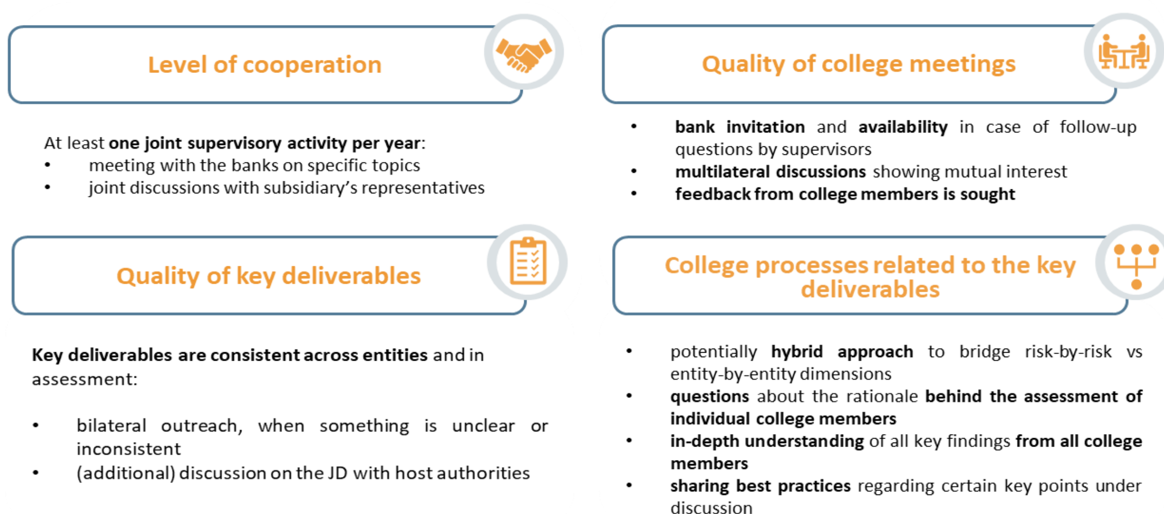
Joint supervisory activities are sometimes limited to the organisation of the annual college meeting, failing to explore further opportunities of joint work in particular in light of uncertain times where collective approaches enhance robustness.

93. The good practices (Figure 29) identified while assessing the implementation of the KPIs were shared with all supervisory colleges.

[24] A measurement point is a specific aspect that contributes to the evaluation of the KPI, the implementation of which facilitate a more efficient and effective college operation. Details of the measurement points by KPI are provided along with the charts presenting the outcome of the EBA's key performance indicators exercise.

[25] Group risk / liquidity risk assessment, joint decision (JD) on capital, on liquidity and on the group recovery plan as well as the group recovery plan assessment.

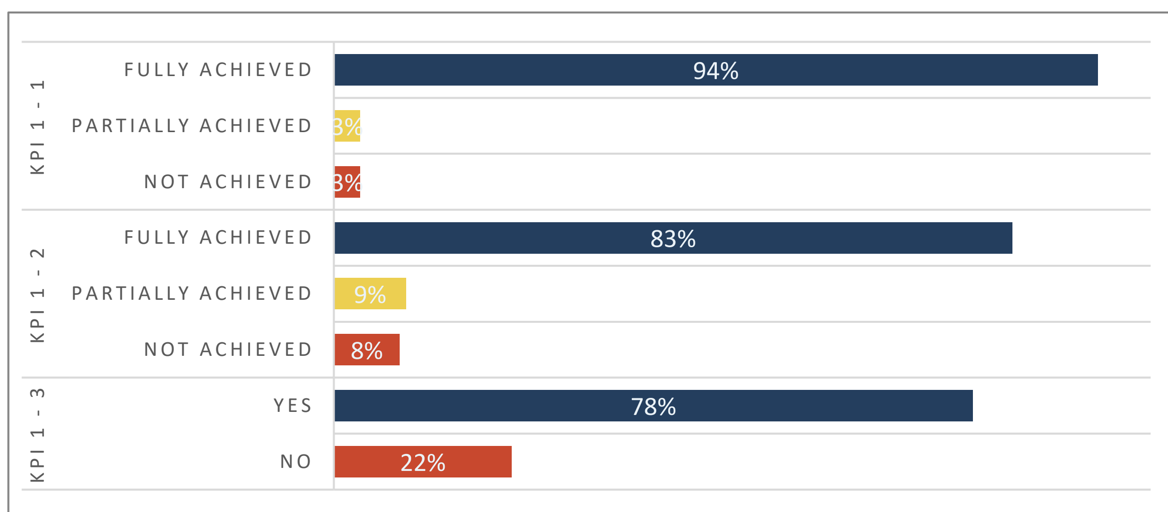
Figure 29: Good practices identified



94. The good practices collected emphasise the proactive approach of colleges in fostering and facilitating information sharing and actively promoting discussions among members. Such practices serve as a benchmark for encouraging comprehensive understanding, knowledge sharing and robust collaboration.

95. Despite the overall good results, there are still some specific elements in college cooperation to be strengthened. The following paragraphs illustrate the collective view of the consolidating supervisor and other college members and observers regarding the four KPIs, highlighting in particular the areas where improvements are expected.

Figure 30: KPI 1 – Level of cooperation

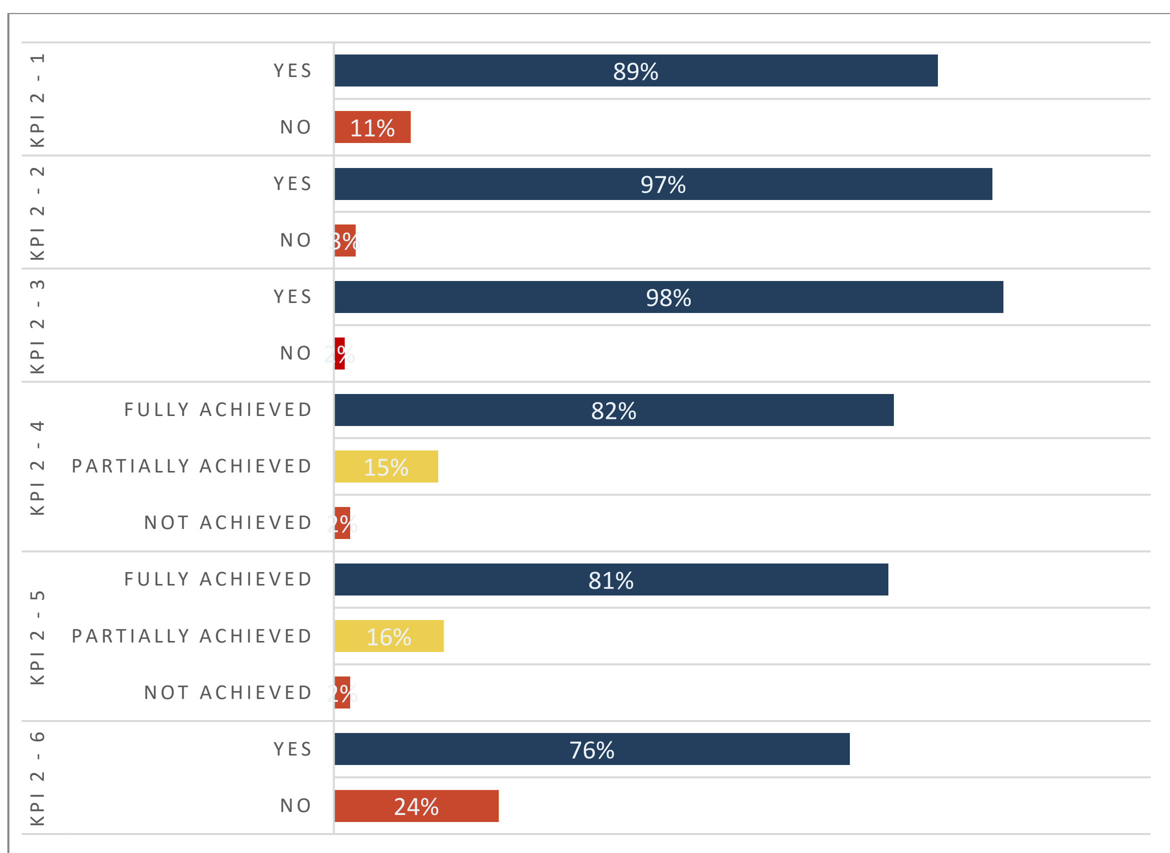


Note: KPI 1-(1) Proactive sharing of information, KPI 1-(2) Identification of early warning signs is effective, KPI 1-(3) At least one joint supervisory activity per year

96. In relation to KPI 1 concerning the level of cooperation (Figure 30), information sharing could still be enhanced, in particular information on early warning signs, potential risks and

vulnerabilities. Most colleges ensured an environment of open communication, showing the effort towards shared objectives and mutual understanding. Several colleges showed willingness and commitment to organise joint supervisory activities and involve members and observers in workshops with a thematic focus, meetings with the supervised entity, and on-site and off-site examinations. Notwithstanding that information flows throughout the year, some colleges limited the joint supervisory activities to the organisation of the annual college meeting, failing to explore further opportunities of joint work. Colleges are thus expected to strengthen their commitment to identifying and organising more joint supervisory activities including meetings with the bank, thematic reviews, joint on-site examinations or joint off-site work.

Figure 31: KPI 2 – Quality of college meetings

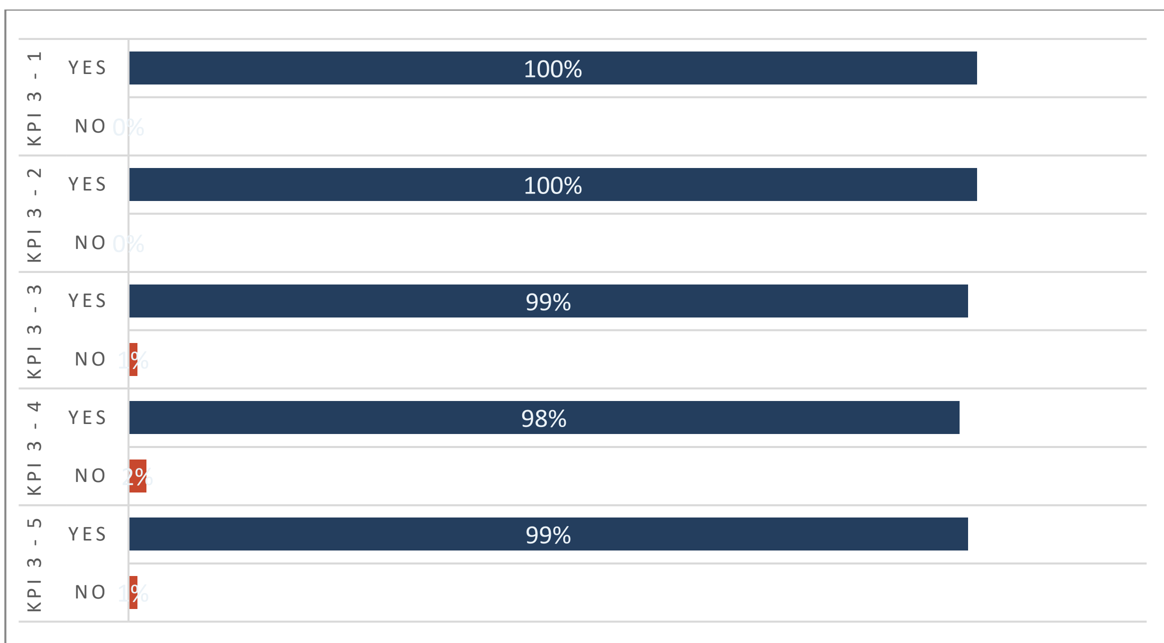


Note: KPI 2-(1) The bank is invited for relevant issues, KPI 2-(2) Expectations on host CAs' contribution are clear and timely, KPI 2-(3) Consolidating supervisor facilitates discussion, KPI 2-(4) College members are active and willing to share information, KPI 2-(5) Multilateral discussions showing mutual interest, KPI 2-(6) Feedback from college members is sought

97. Regarding KPI 2 on the quality of college meetings (Figure 31), most colleges enhanced communication and information sharing by engaging the supervised institution and requesting focused updates on relevant topics of supervisory interest. While in the majority of colleges post-meeting feedback was sought, approximately 24% of them reported a lack of structured feedback collection from college members. Nonetheless, during college meetings host authorities are usually requested to provide insights and feedback on specific processes as well as on the overall cooperation. The active involvement and willingness to share information

among host supervisors can be improved. It is expected that all members of the colleges actively participate and share a mutual interest in each other's supervisory concerns.

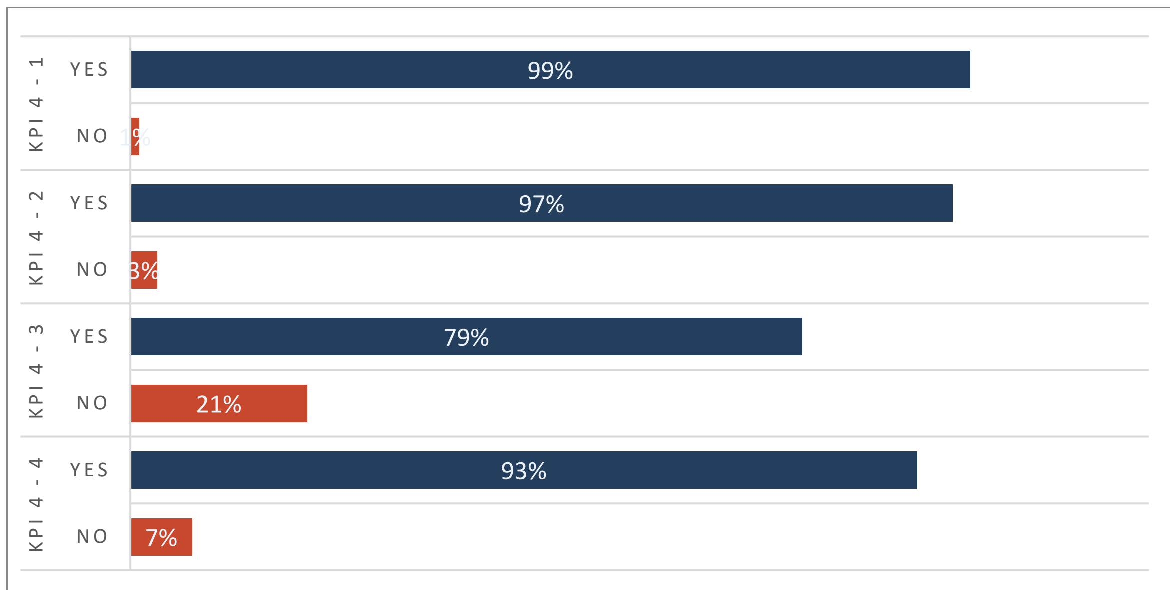
Figure 32: KPI 3 – Quality of key deliverables



Note: KPI 3-(1) Key deliverables are complete, KPI 3-(2) Key deliverables are detailed enough and well reasoned, KPI 3-(3) Key deliverables are clear and coherent, KPI 3-(4) Key deliverables are in line with legal requirements, KPI 3-(5) Key deliverables are consistent across entities and in assessment/measures

98. The positive outcomes presented in Figure 32 regarding the level of implementation of KPI 3 on the quality of key deliverables are largely attributable to the effective adherence to Level 1 and 2 EU regulations, and the experience built up by college members in organising and delivering in an efficient and effective manner college outcomes (e.g. group risk assessments, joint decisions, group recovery plans).

Figure 33: KPI 4 – Colleges' processes related to key deliverables



Note: KPI 4-(1) Joint decision timeline is prepared in timely fashion, KPI 4-(2) Key deliverables are shared well in advance of discussions, KPI 4-(3) Risk-driven discussions, KPI 4-(4) Healthy level of mutual challenge exists

99. Finally, in terms of the colleges' processes related to the key deliverables (Figure 33), most colleges organised the discussions around the group risk assessment according to risk drivers or based on a hybrid approach which bridges a risk-by-risk versus an entity-by-entity approach, showcasing adaptability. When an entity-by-entity approach is followed, colleges are expected to seek a risk-driven discussion. Most colleges reported a healthy level of mutual challenge, actively promoting an environment of open communication and cooperation. Consolidating supervisors gather insights from all members, emphasising the rationale behind individual assessments to minimise discrepancies and foster comprehensive understanding and knowledge sharing. A constructive level of mutual challenge is maintained. Nevertheless, encouraging host supervisors to strive for a better understanding of the risk assessments conducted by their counterparts would contribute to a more comprehensive exchange of insights.

100. In 2023 the EBA provided feedback on the KPI exercise to all individual colleges in the form of an individual benchmark analysis, shared good practices and selected a small sample of colleges that were expected to set up an action plan[26] for improvements. Consolidating supervisors were requested to introduce and settle any improvements needed during the period 2024-2026.

[26] Requests for action plans were communicated for colleges where the implementation of KPIs was not fully achieved and adjustments were deemed necessary.

101. During the 2024-2026 period, the EBA will continue to closely monitor supervisory colleges, including the newly established colleges set up in line with Article 116(1a) of the CRD[27] and the ones established based on the intermediate parent undertaking (IPU) regime.

[27] Article 116(1a) of Directive 2013/36/EU states that a college should be set up also where all the cross-border subsidiaries of an institution are authorised in third countries, to coordinate information sharing and supervisory activities in going concern and emergency situations.

3. EBA policy work supporting supervisory convergence

The EBA further improves the common EU framework for colleges of supervisors and promotes a more efficient and effective supervision of cross-border banking groups.

Type of product: RTS and ITS | **Publication date: January 2024**

102. The technical standards on supervisory colleges, adopted in 2015[28], have been updated[29] to reflect the new requirements laid down in CRD V and CRR II, as well as to reflect on the EBA's ongoing college monitoring activity and the lessons learned from the implementation of the standards. The updated standards aim at ensuring a common EU framework for colleges of supervisors and promoting a more efficient and effective supervision of cross-border banking groups.

103. The key amendments include:

i. enhanced information exchange within the college, as well as with observers, in going concern and in emergency situations;

ii. effective identification of emerging risks in the case of an event of adverse material impact on the risk profile of the group or its entities;

iii. appropriate use of the possibility for 'entrustment of tasks and delegation of responsibility', when it facilitates the efficient and effective supervision of cross-border banking groups.

The EBA harmonises the observed practices on ORC determination and assessment, to improve the usability of recovery plans and make crisis preparedness more effective.

Type of product: Guidelines | **Publication date: July 2023**

104. EBA Guidelines on the overall recovery capacity (ORC) in recovery planning[30] establish a consistent framework for the determination of the ORC by institutions in their recovery plans and the respective assessment by competent authorities, and aim at strengthening institutions' effective crisis preparedness.

[28] In view of the considerable changes, the current RTS and ITS on colleges of supervisors, adopted by the Commission in 2015, will be repealed as soon as the updated ones are adopted.

[29] Final Report on RTS and ITS on supervisory colleges.pdf (europa.eu) (see also Annex I and Annex II to the Report here).

[30] Final Report on GLs on overall recovery capacity in recovery planning.pdf (europa.eu).

105. The objective of the ORC is to provide a summary of the overall capability of the institution to restore its financial position after a significant deterioration by implementing suitable recovery options. The assessment by competent authorities of an institution's overall recovery capacity allows them to understand to what extent an institution would be able to recover from a range of potential crisis situations.

106. The Guidelines are composed of two sections. The first section, addressed to institutions, aims at providing guidance on the relevant steps to set up a reliable ORC framework. The second section, addressed to competent authorities, complements the framework by harmonising the core elements of the competent authorities' assessment of the ORC from both a quantitative and qualitative perspective.

4. Training as a convergence tool

107. The EBA delivered a wide range of virtual and in-person training, workshops and e-learning to stakeholders in 2023, covering various topics related to banking regulation, supervision and innovation. Twenty-four (24) training events were delivered to 4,694 participants (Annex II).

Virtual and physical seminars

108. The EBA training events provided a balanced mix of theory and practice with updated content and methodology to reflect the latest regulatory developments and the emerging challenges in the banking sector, to foster interaction and engagement among the participants. Some of the topics covered by the EBA in 2023 were: Basel III monitoring exercise, internal model under FRTB, SupTech tools, climate risk stress testing, supervisory colleges, non-performing loans, MREL and TLAC, DPM refit, consumer education on sustainability and greenwashing, and major incident reporting under PSD2. Feedback reflected high satisfaction rates and appreciation for the quality and relevance of the training courses and workshops as a convergence tool. Suggestions for improvement included extending the duration of some courses, providing additional practical examples and case studies, and offering more opportunities for information exchange and networking.

Online training

109. The EBA's Learning Hub was an integral tool in the online flagship project, EU Supervisory Digital Finance Academy with the Commission, DG Reform and the European Supervisory Authorities (ESAs), in enhancing supervisors' knowledge and expertise in digital finance and sustainability issues to further achieve supervisory convergence. The six training events delivered covered topics such as MiCA, DORA, RegTech and global regulatory cooperation.

110. Furthermore, two online training events were delivered in 2023, namely on supervisory reporting (FINREP and COREP) and on loss absorption capacity (MREL and TLAC). This online training consisted of self-paced e-learning materials and live seminars. Participants benefited from the comprehensive and updated content with support and guidance from the EBA experts. 90% of the participants expressed their overall satisfaction and would recommend them to other colleagues.

111. Training was provided in collaboration with the BIS on Basel III implementation, ESG risk and climate change scenarios, and in collaboration with the ESE on recovery plan assessment, while the JC consumer education initiatives tackled sustainability and greenwashing.

112. The EBA will continue to update its content and methodology to reflect the latest regulatory developments and the emerging challenges in the banking sector, as well as continuing to meet the expectations and needs of its stakeholders.

Annexes

Annex I – List of supervisory colleges

EEA home country	Name of cross-border banking group
AT	Addiko Bank
AT	Bausparkasse Wüstenrot
AT	Erste Group
AT	Porsche Bank Group
AT	Raiffeisen Bank International AG
BE	KBC Group
BE	FinAx Group
CZ	J&T Finance Group
DE	Clearstream Financial Holding Group
DE	Deutsche Bank
DE	Commerzbank AG
DE	DZ Bank AG Deutsche Zentral-Genossenschaftsbank
DE	ProCredit Group
DK	Danske Bank
DK	Saxo Bank A/S
EL	Alpha Bank, S.A.
EL	National Bank of Greece
ES	BBVA
ES	Banco de Sabadell, S.A.
ES	Grupo Santander
FI	Nordea
FR	BNP Paribas
FR	Crédit Agricole S.A.
FR	Société Générale
FR	ODDO ET CIE
FR	RCI Banque SA
FR	Dexia Group

EEA home country	Name of cross-border banking group
HU	OTP Bank Nyrt
IE	Allied Irish Banks plc
IE	Bank of Ireland Group plc
IT	Intesa Sanpaolo SPA
IT	UniCredit Group
LI	Liechtensteinische Landesbank Group
LI	VPB Group
LU	Bank of China
LU	Havilland S.A.
LU	Precision Capital S.A.
NL	Adyen N.V.
NL	Citco Bank Nederland N.V. (CBN)
NL	ING Groep N.V.
NL	Rabobank
NL	Triodos Bank
NO	DNB ASA Group
PT	Banco Comercial Português, SA
SE	Handelsbanken
SE	Skandinaviska Enskilda Banken (SEB)
SE	Klarna
SE	Swedbank
SI	Nova Ljubljanska Banka (NLB)
49	**Total number of colleges for EEA banking groups**

Name of third-country banking groups
Citibank Europe plc (CEP)
1 college for third-country banking groups

European Banking Authority

Annex II – Overview of the training events the EBA provided to EU competent authorities in 2023

	Title	Date	Format	Participants
1	TFIS virtual seminar on Basel III monitoring exercise	25-26 January 2023	Live seminar	688
2	In-person workshop – Internal model under FRTB	31 January – 2 February 2023	In-person training	50
3	SupTech (social) media monitoring tools	8 February 2023	Live seminar	305
4	Climate risk stress testing	8-9 February 2023	Live seminar	757
5	KPIs in supervisory colleges	15 February 2023	Live seminar	96
6	In-person workshop – Internal model under FRTB in Stockholm (rerun)	28 February – 1 March 2023	In-person training in Stockholm	50
7	EU-SDFA MiCA Advanced Course (1st edition)	20-31 March 2023	E-learning and live seminar	108
8	NPLs	22 March 2023	Live seminar	272
9	SGIA SupTech workshop – Complaints handling tool	20 April 2023	Live seminar	147
10	EU-SDFA Advanced Courses Global Regulatory Cooperation: Overview and New Frontiers	24 April – 8 May 2023	E-learning and live seminar	69
11	EBA/BIS – Recent regulatory developments in Europe	25-26 April 2023	Live seminar	135
12	In-person workshop – Internal model under FRTB in Frankfurt (rerun for ECB staff)	25-27 April 2023	In-person training	37
13	EBA/ESE joint training – Current and best practices in recovery plan assessment	10-11 May 2023	Live seminar	92
14	EU-SDFA MiCA Advanced Course (2nd edition)	22 May – 2 June 2023	E-learning and live seminar	105
15	EU-SDFA EBA workshop on RegTech	31 May – 1 June 2023	In-person training	50
16	EU-SDFA DORA Advanced Course	19-30 June 2023	E-learning and live seminar	105
17	Workshop on SupTech – Lessons learned from SupTech development and adoption	21 June 2023	Live seminar	192
18	Leveraging EUCLID	21-22 June 2023	Live seminar	337
19	Industry workshop major incident reporting under PSDs	4 July 2023	In-person training	109
20	Supervisory reporting FINREP/COREP	4-20 October 2023	E-learning and live seminar	219
21	Introductory session – Supervisory reporting – hands-on workshop on DPM refit	10 October 2023	Live seminar	534
22	JC workshop on consumer education initiatives on sustainability and greenwashing	14 November 2023	In-person training	46
23	Update – e-learning on MREL	27 November – 5 December 2023	E-learning and live seminars	123
24	EU-SDFA Advanced Courses Global Regulation and Cooperation in Digital Finance	6-27 November 2023	E-learning and live seminars	68
Total				**4 694**

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