Public hearing on the draft CEBS Disclosure Guidelines: Lessons learnt form the financial crisis (CP30)

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Outline

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Background

- CP 30 comprises a set of principles extracted from CEBS’s observations on disclosures banks made during the financial crisis
- Intended to help institutions to improve their risk disclosure in **stressed situations**
- High-level principles, not intended to amend, duplicate or add to existing disclosure requirements
- Aim to address ways of improving the form and content of disclosures irrespective of their context (IFRS, Pillar 3, listing rules or others)

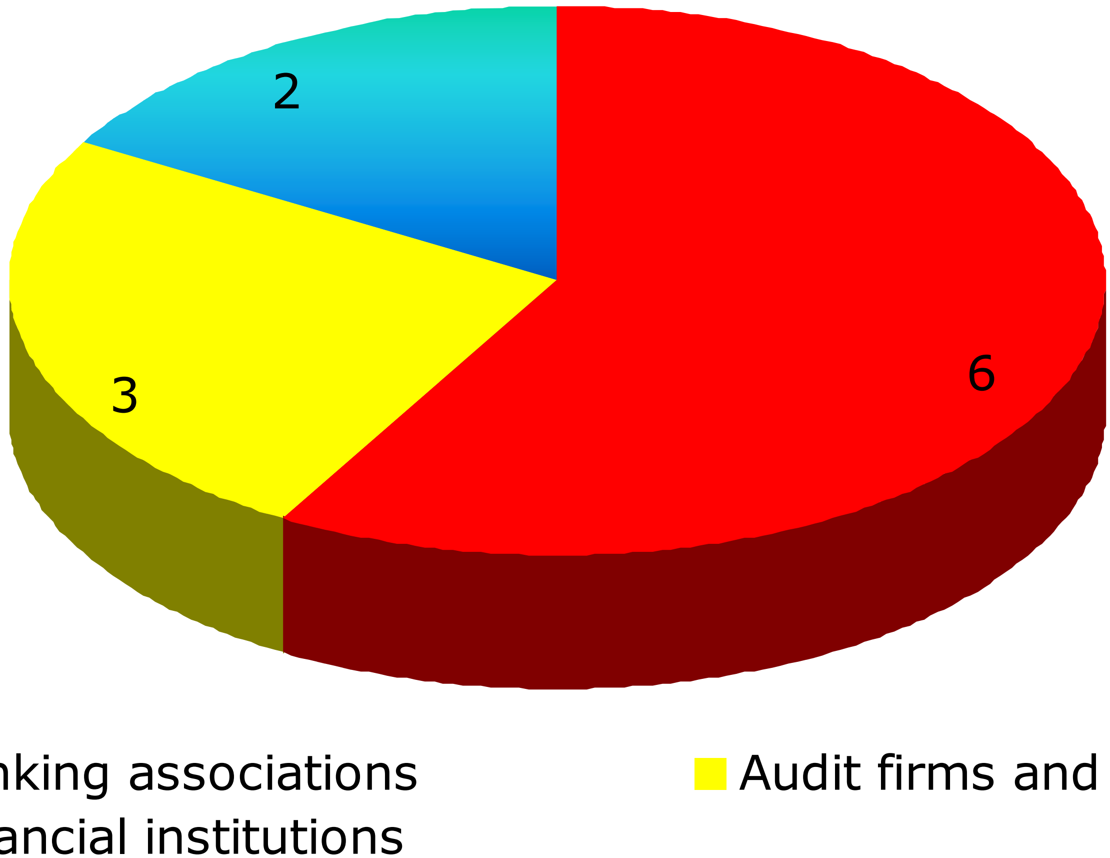
Background

- 16 principles divided into three different parts, discussing respectively:
  - general principles to be applied to high quality disclosures;
  - principles dealing with the content of disclosures on areas or activities under stress, in particular for disclosures on business models, impacts on results and risk exposures, impacts on financial positions, risk management and sensitive accounting issues;
  - guidance on presentational aspects of disclosures.

Background

- Draft guidelines published in October 2009 for a 3-month consultation period ending 15 January 2010
- Comments sought on all aspects of the proposed guidelines (CP30). In particular CEBS asked:
  - Are the proposed guidelines helpful in achieving better disclosures?
  - Are the guidelines comprehensive and sufficiently clear?
  - Do the proposed guidelines raise any concerns in terms of a level-playing field?
- 11 responses received

Responses received



General comments

Most respondents are supportive of CEBS's endeavours to help financial institutions improve their risk disclosures.

In particular, some welcome use of high-level principles / good practice disclosure and that principles are not compulsory.

BUT:

- Concerns that guidelines are too detailed and increase the already significantly large amount of disclosures
- Need for clarification as to:
  - and how the guidelines interact with other disclosure requirements,
  - the scope and objective of the guidelines and what is considered a situation of "stress".

General comments

Risk of information overload

- Some respondents point out the current wealth of information and on the risk that CEBS's guidelines may lead to expand disclosure requirements.
- The guidelines come within the scope of existing requirements. They aim at organising and presenting the requested information in a way that would enhance the clarity of the message passed on to users in times of stress.
- The principles referring to comprehensiveness and granularity of the information are underpinned by existing requirements.

General comments

<u>Interaction with other requirements</u>

- Some respondents question how the guidelines relate to other requirements.
- Guidelines not particularly aimed at IFRS-related disclosure or information provided under Pillar 3. The principles are high-level and should be considered in conjunction with other requirements.
- Guidelines should not be considered as additional disclosure requirements but are fundamentally intended to guide financial institutions in providing adequate disclosures in times of stress.
- Guidelines intend <u>to promote and enhance transparency principles anchored in other relevant disclosures requirements</u>.

General comments

<u>What are stressed circumstances</u>

- The question of the scope and objective of the guidelines was raised by several respondents. It calls for clarification as to what is considered a situation of stress.
- During its initial discussion leading up to the CP, CEBS decided not to define a situation of stress. Given the comments received, this will have to be further considered in order to clarify the scope of the guidelines.

<u>Other general comments</u>:

- Initiative should be coordinated on a global level
- Disclosures need to be adapted to audience
- Question about enforcement of principles?

Comments on Section I: General principles

Principle 1: Financial institutions should provide timely and up to date information irrespective of the timing of their normal publication calendar

- A few respondents see this principle as a new requirement engaging not only a bank's responsibility but also implying costs. Some also related this to higher publication frequencies.
- Due to its importance for users, principle has been added to the guidelines with a view to emphasise the need for timely information in times of stress.
- CEBS could clarify principle to say that publication calendar should be such as to ensure timely and up-to-date information.

Comments on Section I: General principles

Principle 2: In order to enhance the quality of information, financial institutions should provide adequate information on areas of uncertainty

- A few respondents are concerned about a possible excessive expansion of information on sensitivity analyses. They question value for the users of financial statements. Also: How to accomplish in practice?
- Suggestion to differentiate between reported data and forward-looking statements.
- Strive to find the right balance between sufficiently complete and yet not too detailed information. To this end, information could be critically reviewed regarding their benefits for decision-making.

Comments on Section I: General principles

Principle 3: Financial institutions should provide comprehensive and meaningful information that fully describes their financial situation

- Some concerns about coordination with competent authorities and/or for continued compliance with relevant disclosure obligations in case a bank would be confronted with sensitive information in stressed circumstances.

- Actual disclosure is matter of management discretion and judgement (as regards level of detail). In contrast: Demand for criteria about omissions.

Comments on Section I: General principles

Principle 4: Disclosures should allow for comparisons over time and between institutions

- One respondent is concerned by the fact that this would increase the scope of the varying disclosure formats and the flood of information provided.
- CEBS agrees that attention must be paid not to increase the quantity of information already required but it also believes that it must be done on the criteria of usefulness which undoubtedly is satisfied in the case of comparative information.
- A few respondents advocate against the use of uniform formats - which is not CEBS's intention -, although it was also noted that the issue may be alleviated by generalised use of XBRL reporting format.

Comments on Section I: General principles

Principle 5: Financial institutions should seek to early adopt new disclosure standards and best practice recommendations from standard-setters and regulators

- A few respondents explicitly support the principle to seek early adoption, although some stress that regulators should not interpret IFRS standards.
- A few respondents point out possible risks of early adoption to quality and the practical difficulties (notably the upgrading of IT systems)
- One respondent mentions the importance of the iterative process that is used to set up new disclosure processes
- CEBS believes that early adoption is desirable and that banks should made their best efforts to meet this principle without compromising quality.

Comments on Section I: General principles

Principle 6: Financial institutions should specify whether and to what extent information has been verified by external auditors

- Some respondents asked for guidance how principle should be applied in practice.
- One respondent suggests that financial institutions provide insight on their internal monitoring / assurance processes (organisational independence, coverage of audit plan, oversight of the internal audit function)
- CEBS considers it good practice for financial institutions to address in their disclosures the question of the verification of information. CEBS does NOT require verification.

Comments on Section II: Content

Principle 7: Financial institutions should elaborate on the position and importance of the activities under stress within their business model

- Some respondents question the form that information on business model should take: interaction with management commentary, appropriate level of details, extent of forward-looking information (if any), location…

- Information on business model has to be tailored to each particular situation but need also to be sufficiently detailed to allow external users to gain sufficient insight on the overall situation of the financial institution.

- CEBS has no strong views where information is provided.

Comments on Section II: Content

Principle 8: Disclosures should include clear and accurate information on the impacts on results and on risk exposures of the activities under stress

- Several respondents are concerned by the request for forward-looking information: may raise legal issues, requires extensive preparatory and verification work, is subjective and may be misinterpreted.
- CESB believes that forward-looking information provide useful insights to users especially in stress situations.
- Yet, CEBS recognises that care needs to be taken about verifiability and legal liability of forward-looking information.
- Besides, caveats would also be needed about the limits of the exercise.

Comments on Section II: Content

Principle 9: Disclosures should also include information regarding the impacts on the institution's financial position

- One respondent noted that IFRS 7 contains already sufficient disclosure requirements about liquidity risk.
- Quantitative information in IFRS 7 is very limited.
- No other specific comment received beyond those mentioned in general comments – except for reiterations of previous comments regarding forward-looking information

Comments on Section II: Content

Principle 10: Financial institutions should communicate: appropriately on the management of risk to activities under stress

- One respondent cautions against the possibility of creating "self-fulfilling prophecies"
- The principle is not intended to impose on banks artificial corrective measures but only suggests a description of the measures effectively taken or underway to enhance risk management processes.

Comments on Section II: Content

Principle 11: Financial institutions should be as specific as possible with regard to sensitive accounting issues

- One respondent cautions against the risk of extensive scenario disclosures around sensitive accounting issues which could lead to undermining the quality of financial reprting

- CEBS considers that by nature sensitive accounting issues require special care. Yet, high quality disclosure does not depend on the amount of information disclosed.

Comments on Section III: Presentational issues

Principle 12: Disclosure should as far as possible be provided in one place with appropriate cross-references where necessary

- Some respondents tend to consider that it is up to each financial institution to decide how to present information.
- CEBS agrees with this principle but encourages financial institution to consider the users' benefits to provide in one place all information relating to the SAME stressed circumstances. The principle does not intend to regroup disclosures from various regulations / standards in one document.
- Some respondents note that cross-references should be at management's discretion and could raise issues between audited / non-audited information.
- Relationship between audited / non-audited information not affected by cross-references. Only intended to guide users.

Comments on Section III: Presentational issues

Principle 13: Disclosure should be provided at an appropriate level of granularity of transparency

- One respondent point out the risk of the principle leading to an even greater information overload.
- Already addressed during general comments
- Another respondent mentions that the level of granularity must be weighted against the length of the remittance periods.
- CEBS agrees and believes once again that it is up to the financial institution to strike the right balance between timeliness and the right level of detail.

Comments on Section III: Presentational issues

Principle 14: Financial institutions should seek an appropriate balance between quantitative and narrative information

- Only supportive comment received

Comments on Section III: Presentational issues

Principle 15: Financial institutions should continue to develop an educational approach

- One respondent argues that education not primary goal of financial statements and that executive summaries may distract users from a full reading of financial statements.
- Other respondents welcome the suggestion to institutions to consider the inclusion of executive summaries and to “tell a story” about their activities.
- CEBS feels that right balance should be sought between too long educational developments and clear disclosures for non-expert users. CEBS also insists on the need to look for consistency throughout the report.
- One respondent notes the that Pillar 3 is a point in time picture of risks.
- CEBS sees no contradiction

Comments on Section III: Presentational issues

Principle 16: Financial institutions which are not exposed to the activities under stress should clearly specify that fact when it is likely to provide useful information for users in their decision-making

- A few respondents are concerned that a positive statement on the absence of involvement from the financial institution may have adverse effects on readers (i.e. could create suspicion – in particular in situations where the going concern is at stake – or result in manipulations) and may involve the legal responsibility of the institution.

- CEBS agrees that this principle requires management judgment as to when an explicit statement of non-involvement – or low-involvement - is needed in order to prevent the effectiveness of the disclosure being undermined by unnecessary “noise”.

Questions

- Do participants have other comments on the draft guidelines?
- How should CEBS take the draft guidelines forward?
- What would the impact be in terms of cost? Benefits?
- Other considerations?

Next steps

- CEBS will prepare a feedback document (within 3 months after the consultation period ends) discussing the comments and CEBS's reactions.
- Impact assessment.
- Follow-up proposal to be submitted to CEBS.