

EBA

European
Banking
Authority

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Annual Report | 2011

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Executive summary

The 2011 Annual Report of the European Banking Authority (EBA) provides an account of the activities and achievements of the Authority in its first year of existence. The EBA was established on 1 January 2011 in response to a call for a more integrated regulatory and supervisory framework in the European Union. The EBA, together with the national supervisory authorities, the other two European Supervisory Authorities (ESAs), EIOPA and ESMA, the Joint Committee and the European Systemic Risk Board (ESRB), is part of the new European System of Financial Supervision (ESFS).

The Regulation establishing the EBA entrusted the Authority with a wide range of tasks in addition to the ones inherited from its predecessor, the Committee of European Banking Supervisors (CEBS), all ultimately aiming at preserving financial stability and ensuring confidence in the financial system as a whole, and providing protection for the customers of financial services.

The EBA started its activity at full speed. As its Chairman pointed in his introductory remarks, the EBA “started out in a pretty rough and difficult market environment with a number of key challenges to be faced immediately. It was not easy to focus on building a new organisation while having at the same time to deal with major challenges to the stability of the banking sector”.

The priorities and the activities of the EBA, set out in its 2011 Work Programme, covered three main areas: **Regulation**, **Risk Analysis** and **Operations**, with the aim to set up the **Consumer Protection** function of the Authority.

In its regulatory efforts, the EBA focused its work on laying the foundation for the so called European Single Rulebook, a common set of fully harmonised rules that will be binding and directly enforceable in all EU Member States. This is a substantial task, as more than 100 binding technical standards are due to be finalised in the next few years and approximately 40 standards are expected to be issued by 1 January 2013. Throughout 2011, the EBA prepared the ground for the development of several binding technical standards on key areas such as own funds and liquidity on the basis of the European Commission’s proposals on CRDIV/CRR of July 2011. Besides this preparatory work on the binding standards, the EBA continued the drafting of guidelines covering different aspects of the CRDIII such as internal governance, extensions and changes to the Advanced Measurement Approach (AMA), remuneration data collection exercises, Stressed Value at Risk (Stressed VaR), and Incremental Default and Migration Risk Charge (IRC).

In the Risk Analysis area, the priorities mainly focussed on the challenges raised by the deterioration of the financial market environment in Europe. In addition, the EBA continued its regular monitoring, assessment and analysis of risks and vulnerabilities in the EU banking sector. Furthermore, the EBA stepped up its efforts to promote effective and efficient cooperation between national supervisory authorities in the field of banking supervision, by means of policy work and active participation in colleges of supervisors.

A key component of the Risk Analysis activities in 2011 was the EU-wide stress test exercise which was performed on a sample of 91 banks using a single adverse scenario and consistent methodology. This exercise has proven to be a very strong incentive for the banks involved as they took considerable actions to avoid falling below the benchmark of 5% CT1 and raised some EUR 50 bn in fresh capital in the first four months of 2011 in anticipation of meeting the commonly agreed capital threshold. Despite its success also in terms of great disclosure and quality assurance, the main objective of restoring confidence in the European banking sector was not achieved, as the sovereign debt crisis extended to more countries. Furthermore, many EU banks, especially in countries under stress, experienced significant funding challenges. Following the indications of the International Monetary Fund and the European Systemic Risk Board, the EBA proposed measures, as part of a package agreed at European level, to strengthen the banks' level of capitalisation and to encourage a return to more relaxed conditions on the funding market. A formal Recommendation was then approved, requiring banks to form a capital buffer so as to reach a capitalisation coefficient of 9% in terms of highest quality capital (CT1), by the end of June 2012, after prudent valuation of the banks' exposure to Member States of the European Union.



In Consumer Protection, the EBA focused its work mostly on mortgages and other forms of consumer lending and surveyed concerns in areas such as the role of credit intermediaries, transparency and clarity of pre-contractual information provided to consumers, and creditworthiness assessments.

When the three European Supervisory Authorities were established, a Joint Committee was also created for regular cooperation. The Joint Committee frequently discussed sector and cross-sector risk assessment reports, and possible policy options in the light of market developments. These policy options fell in the areas of supervision of financial conglomerates, accounting and auditing, micro-prudential analysis of cross-sectoral developments, risks and vulnerabilities of the financial system, measures combating money laundering, and consumer protection. In 2011, the first joint risk reports were presented to the European policy-makers.

Finally, strengthening the EBA's Operations and enhancing its institutional capabilities have played a crucial role in the first year of the Authority. During 2011, the EBA made significant progress in bringing its financial and human resources management, procurement processes, IT infrastructure and communication activities in line with the requirements of relevant EU Regulations and best practices.

Foreword by the Chairman

It is a great honour and privilege for me to present the first Annual Report of the European Banking Authority (EBA) which summarises the activities performed by the Authority over its first year of existence.

The establishment of the EBA on 1 January 2011 marked a major change in the institutional set-up as it responded to an urgent call for visible progress towards a more integrated regulatory and supervisory framework in the European Union (EU). The EBA's predecessor, the Committee of European Banking Supervisors (CEBS), had already put a lot of effort into achieving more convergence, but its limited mandate prevented the Committee from having a noticeable impact on the day-to-day practices of the national authorities. Indeed, one of the major weaknesses before the establishment of the EBA was the inability of the Committee to decide and coordinate policy actions within the European Union. And the need for a step change towards a greater and more effective integration of financial markets in the EU became even more relevant with the emergence and escalation of the crisis in Europe.

The Regulation establishing the EBA entrusted the Authority with a wide range of tasks in addition to the ones inherited from the CEBS, all ultimately aimed at preserving financial stability and ensuring confidence in the financial system as a whole and providing sufficient protection for the customers of financial services.

We started out in a pretty rough and difficult market environment with a number of key challenges to be faced immediately. It was not easy to focus on building a new organisation while having at the same time to deal with major challenges to the stability of the banking sector. Market pressure for coordinated action to restore confidence in the resilience of EU banks has constantly been extremely high. The very first challenge for us was the Europe-wide stress test, carried out jointly with national supervisors in order to assess the resilience of a large sample of 90 banks across 21 countries against an adverse but plausible scenario. The publication of the results in July 2011 provided the market with unprecedented transparency and disclosure – some 3,200 data points for each bank – thus helping to assuage investors' concerns about banks' exposure to risks. The stress test has proven to be a very strong incentive for the banks involved, as they made considerable efforts to avoid falling below the benchmark set in the exercise (a ratio of Core Tier 1 – CT1 – to risk-weighted assets higher than 5%) and increased their aggregate CT1 by EUR 50bn in the first four months of 2011. The stress test was run in a very rigorous way, achieving consistent results and implementation of the agreed methodology thanks to three rounds of peer review.

It is, however, fair to admit that due to the unfolding of the sovereign debt crisis in the euro area, the stress test failed to restore confidence in the resilience of EU banks. The financial crisis entered a new phase in August, when growing concerns about the sustainability of the public debt in some countries in the euro area generated a major dry-up of the market for bank medium and long-term funding. Investors began to assess the strength of European banks on the basis of the credit quality of the sovereign providing them with their

Andrea Enria



safety nets; the banks' capital position was measured valuing their sovereign exposures at market value, irrespective of the accounting book where they were located. An adverse feedback loop was looming: the deterioration of the sovereigns was driving a funding squeeze on banks, which was triggering a disordered deleveraging process potentially affecting growth prospects, with adverse effects on the fiscal position of the sovereigns. In response also to the recommendations of the International Monetary Fund and the European Systemic Risk Board, we proposed measures, as part of a package agreed at European level, to strengthen the banks' level of capitalisation and encourage a return to more relaxed conditions on the funding market. After prudent valuation of the banks' exposure to the Member States of the European Union we approved a Recommendation requiring banks to form a capital buffer so as to reach a capitalisation coefficient of 9% in terms of highest quality capital (CT1), by the end of June 2012.



On the regulatory front, the EBA was given a central role in establishing the so called European Single Rulebook, a common set of fully harmonised rules that will be binding and directly enforceable in all EU Member States. With the unfolding of the crisis, the project of the Single Rulebook, launched by the de Larosière Group, has proven even more vital to the strengthening and consolidation of the Single Market. Experience in the first months of operations of the EBA has shown that very significant differences still characterise the regulatory frameworks of EU countries, thus leading to a fragmented and unlevel playing field. The new regulatory framework to implement the reforms endorsed by the G20 provides us with a major opportunity to move towards the establishment of the Single Rulebook. In line with the proposal for a Directive and a Regulation on capital requirements – the so called CRD4-CRR – we have begun the preparatory work to draft 'binding technical standards' that will define and specify the content of European legislation in a truly uniform fashion through a Regulation directly applicable throughout the Single Market. This is a substantial task, as more than 100 binding technical standards are due to be finalised in the next few years. Approximately 40 standards should be issued by 1 January 2013. The most important objectives of this first set of standards are to complete the technical aspects of the definition of capital and to make arrangements for monitoring the introduction of the liquidity coverage ratio.

The path ahead of us is still very challenging, but I am confident that we can build on the achievements of this first year of work to deliver further progress. Since the very first months of activity we have indeed taken decisions in areas where there was no consensus and we have given evidence of a truly European approach. Success does not come automatically. It requires substantial efforts and the will of many persons and institutions. And I would like to take this opportunity to thank all the national supervisory authorities and members of our Board of Supervisors for their continued support, even when we have had to deal with very controversial issues. The work we developed on the stress test, in our regular risk assessments and in the drafting of regulatory and implementing standards would not have been possible without the cooperation and the contribution of experts from the national authorities.

I firmly believe that the success of the EBA and of the new institutional framework going forward depends very much on our ability to work as a 'system' in conjunction with national supervisors.

Interview with the Executive Director

One year has passed since the establishment of the EBA. Could you identify the key operational challenges you have had to grapple with and the progress achieved so far?

The start-up phase of the EBA in early 2011 was a highly challenging period. Considering the increasingly adverse conditions in the financial markets and the amount of tasks to be carried out under the EBA's mandate, the newly-born Authority had to be up and running at close to full speed from the very first day of existence.

Although when established, the EBA could rely on approximately thirty highly motivated staff members inherited from its predecessor, the CEBS, the changeover as well as the first

operational decisions took place without the EBA's Top Management in place. Becoming a European public body also meant familiarising ourselves with EU administrative rules, which brought about major changes to the day-to-day operations, functioning and administration of the Authority compared with the former CEBS' administrative arrangements. But the enthusiasm and great dedication of our staff have proven to be fundamental in navigating through these months. By the end of 2011 the EBA had doubled its headcount, stabilised its IT operational environment, expanded its office space, adopted the vast majority of rules and procedures required by the various EU regulations, and most importantly, it successfully carried out a Europe-wide stress test and, subsequently, a bank recapitalisation exercise.

Adam Farkas



In terms of budget and resources, how do you intend to adjust the establishment plan to cater for the increased and demanding tasks the Authority has been entrusted with?

If we look at the work plan of the EBA, which is still being shaped by upcoming legislative proposals, more than 200 deliverables are expected from the EBA's staff in the coming years, many stemming from the implementation of the new CRR/CRD IV package. The most critical period from a human resources perspective will be the second half of 2012 and the first half of 2013, when a very high number of deliverables are due, mainly in the form of draft binding technical standards and guidelines. The establishment plan was approved in late 2010, but the amount of tasks and their timing have changed since then. We have therefore requested changes in the amount of resources that are available to the EBA in line with the changes to our mandate. One positive development is

that the new CRD/CRR legislative proposal was accompanied by a proposed legislative statement providing for an additional 9 staff members, and the corresponding budgetary resources in response to these requests. In general, we have to use our resources in the most efficient way, and communicate clearly when adjustments in resources are needed in the light of future proposals which can change our tasks significantly.

The EBA is part of the new European System of Financial Supervision. How is coordination and cooperation with the national supervisory authorities and the other European supervisory authorities (ESAs)?

When the EBA and the other two European micro-prudential authorities (ESAs) were established on 1 January 2011, an institutional framework, known as the Joint Committee was also created for regular cooperation among the three supervisory authorities. Its main objective is to address cross-sectoral supervisory issues, and to ensure consistency in the ESAs' practices both in policy-making and operations. The key policy areas for coordination are the supervision of financial conglomerates, accounting and auditing, micro-prudential analysis of cross-sectoral developments, the risks to and vulnerabilities of the financial system, measures to combat money laundering, and consumer protection. In 2011, the EBA's Chairperson served as the first Chair of the Joint Committee, the chairmanship of which is held on a rotating basis for one year. The first joint risk reports were produced and presented to European policy-makers in the course of 2011, and the respective sub-committees embarked on a number of joint initiatives in all the other key policy areas. On the operations side, close cooperation is crucial to ensure alignment of the Authorities' respective internal rules of procedures as well as a consistent interpretation of the respective internal bylaws, budgetary processes and IT solutions. Besides the Joint Committee, senior representatives of the three Authorities participate as observers in each others' Board of Supervisors' meetings.

With respect to the EBA's cooperation with the national supervisory authorities (NSAs), our Founding Regulation states that the European System of Financial Supervision must be an integrated network of national and EU supervisory authorities, leaving the day-to-day supervision of individual institutions at national level. In addition, our main decision-making body is comprised of the heads of the NSAs. National experts are also involved in the activities of the EBA standing

committees, sub-groups and task forces as well as through the provision of temporary staff to work on ad-hoc projects such as the stress test exercise. Thus, the EBA and the NSAs work very closely at all levels on a continuous basis, and our success depends to a great extent on the quality of this cooperation. The experience of 2011 demonstrated that the new architecture and the engagement of national supervisors with the EBA can deliver superior results in harmonising rules as well as risk assessment and supervisory practices across Europe.

How has the EBA engaged and interacted with external stakeholders?

To help facilitate consultation with stakeholders in areas relevant to the tasks of the EBA a Banking Stakeholder Group (BSG) has been established. It is composed of thirty members appointed to represent in balanced proportions credit and investment institutions operating in the EU, their employees' representatives as well as consumers, users of financial services and representatives of SMEs. The active discussions with the BSG provide key inputs to the EBA's work. In addition, the EBA, in line with its obligation to follow due process, is organising open consultations on all the technical standards and guidelines that are being drafted to ensure that input and comments are gathered from all interested parties. Finally, the Authority has also engaged in regular contacts with different industry and consumer organisations, as well as with supervisory authorities in third countries, think tanks, and International Financial Institutions.



The EBA's profile: mandate, tasks and priorities

The EBA's mandate

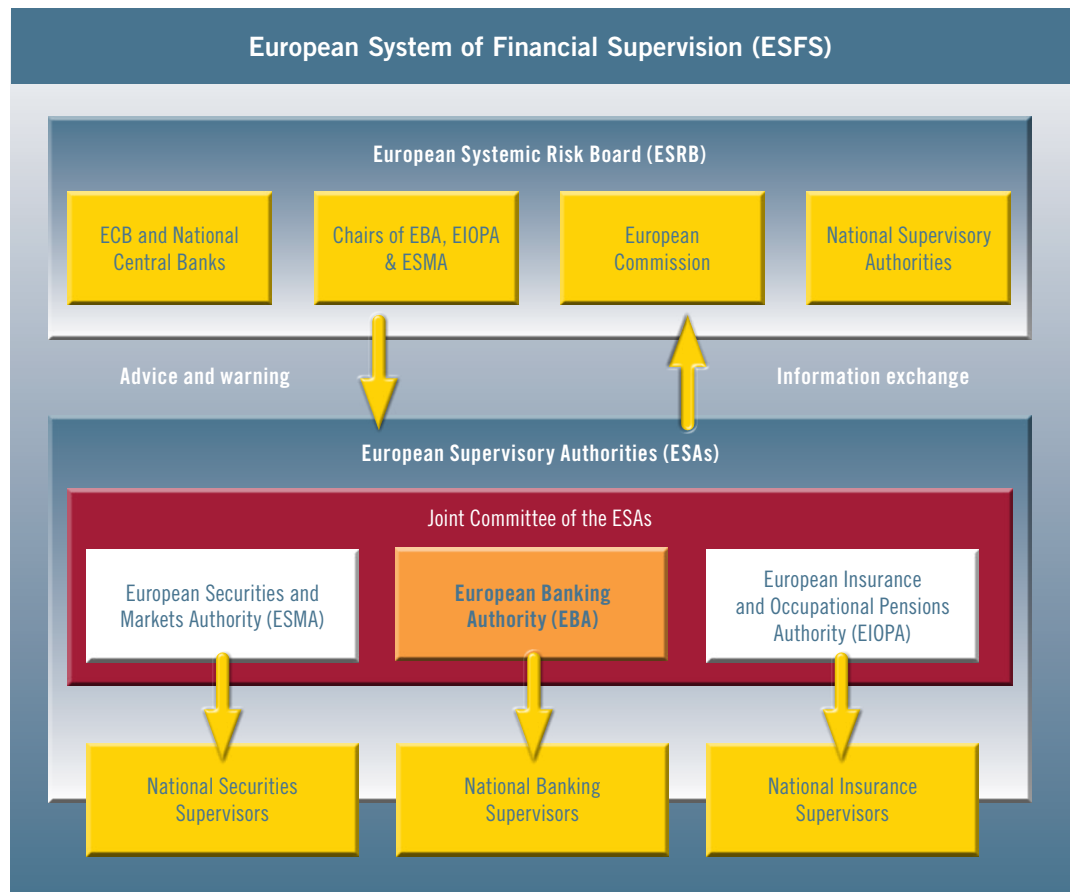
The European Banking Authority (EBA) is one of the three European Supervisory Authorities (ESAs) that together with the European Systemic Risk Board (ESRB) make up the new European architecture for financial supervision created in response to the financial crisis that hit the world in 2008. Together with the national supervisory authorities, the ESAs, the EBA's Joint Committee and the ESRB represent the new European System of Financial Supervision (ESFS). The EBA officially came into being on 1 January 2011. In addition to the new mandate derived from its Founding Regulation, the Authority has taken over all existing and ongoing tasks and responsibilities from the Committee of European Banking Supervisors (CEBS).

The EBA acts as a hub-and-spoke network comprising EU and national bodies safeguarding public values such as the stability of the financial system, the transparency of markets and financial products and the protection of depositors and investors.

The EBA has a broad remit, including preventing regulatory arbitrage, guaranteeing a level playing field, strengthening international supervisory coordination, promoting supervisory convergence and providing advice to EU institutions in the areas of banking, payments and e-money regulation, as well as on issues related to corporate governance, auditing and financial reporting.

The European System of Financial Supervision

In November 2008, while the world financial crisis was still evolving, the European Commission tasked a High Level Group chaired by Mr. Jacques de Larosière with the challenging task of providing recommendations on the future of European financial regulation and supervision. This led to the presentation, on 25 February 2009, of a comprehensive report in which the de Larosière Group analysed the causes of the crisis, and identified serious shortcomings in the existing financial supervision system of the EU, before acknowledging that crisis management by Member States and the EU regulatory and supervision system had not been satisfactory. The de Larosière Group made 31 recommendations, in particular in connection with setting up a stronger European system of supervision and better crisis management to ensure that all the relevant actors and all types of financial instruments were subject to appropriate regulation and oversight. At the core of this report were proposals to strengthen cooperation and coordination between national supervisors in order to improve financial market regulation and to remove national exemptions. The new European System of Financial Supervision (ESFS) was therefore called upon to foster harmonised rules as well as coherent supervisory practice and enforcement with the ultimate goal of ensuring financial stability at the level of individual financial companies and of protecting the customers of the financial services industry.



The EBA's tasks

The tasks set out in the EBA's mandate include, among other things:

- ✓ Developing draft regulatory and implementing technical standards on EU banking legislation aimed at establishing a set of harmonised rules, the so-called 'Single Rulebook';
- ✓ Issuing guidelines and recommendations to both the competent authorities and financial institutions aimed at establishing consistent, efficient and effective supervisory practices within the ESFS;
- ✓ Investigating alleged incorrect or insufficient application of EU law by national authorities and issuing recommendations in specific cases where a competent authority is in breach of EU law;
- ✓ Taking decisions directed at individual competent authorities or financial institutions in emergency situations;
- ✓ Mediating or issuing binding determinations to resolve disagreements between competent authorities in cross-border situations;
- ✓ Issuing decisions addressed to individual financial institutions in exceptional circumstances if EU law is directly applicable and the competent authorities have persistently failed to act;
- ✓ Acting as an independent advisory body and issuing opinions to the European Parliament, the Council or the Commission;
- ✓ Ensuring proper follow-up of warnings and recommendations issued by the ESRB;
- ✓ Taking a leading role in promoting transparency, simplicity and fairness in the market for consumer financial products or services across the internal market.



The EBA's governance

1. The Board of Supervisors

The Board of Supervisors, the main decision-making body of the EBA, met sixteen times in 2011. Ten of these sixteen meetings took place via conference call.

According to the EBA Regulation, the Chairperson and the Executive Director of the EBA are appointed by the Board of Supervisors. On 12 January 2012, Mr Andrea Enria was elected as Chairperson of the EBA and confirmed by the European Parliament on 3 February 2012. He took up office on 1 March 2011. Mr Adam Farkas was elected as Executive Director by the Board of Supervisors on 2 March 2011. He took up office on 16 April 2011.

During 2011, the Board of Supervisors discussed and enacted decisions on certain issues related to the core functions of the EBA, which are laid down in the EBA Regulation, such as items related to Regulation, Oversight and Consumer Protection. Some noteworthy decisions adopted by the Board of Supervisors in 2011 were, inter alia: the publication of the recapitalisation exercise, EBA consultation papers on guidelines on the Incremental Default and Migration Risk Charge (IRC) and on guidelines on Stressed Value at Risk (Stressed VaR), the consultation paper on draft Implementing Technical Standards (ITS) on supervisory reporting requirements, the publication of the compliance table regarding Guidelines on Internal Governance (GL44), the publication of a recommendation and the final results of the bank recapitalisation plan as part of a set of co-ordinated measures to restore confidence in the banking sector.

2. The Management Board

The Management Board ensures that the EBA carries out its mission and performs the tasks assigned to it in accordance with the EBA Regulation. Acting within this scope, the

Management Board met thirteen times in 2011, either physically or via conference calls.

During 2011, the Management Board accomplished the tasks allocated to it by the EBA Regulation, such as: key EBA priorities and the EBA 2012 Work Programme, provisions related to access to documents, the publication of its minutes, the EBA Budget 2011-2012 and accompanying financial decisions, supplementary rules of procedure for the selection of the Chairperson and Executive Director, procedural decisions, personnel planning, planning regarding the EBA's premises, planning regarding a common supervisory culture, the allocation of the work programme to member organisations, the Chairmanship of EBA Standing Committees, the Financial Rules of the EBA, Implementing Rules for the EU Staff Regulations and the Conditions of employment of other servants of the European Union (CEOS), Rules of Procedure, the Code of Good Administrative Behaviour, and the EBA's IT project.

As stipulated in the EBA Regulation, the Management Board is made up of the Chairperson of the EBA, six other members of the Board of Supervisors and a representative from the European Commission. Other than the Chairperson, each member of the Management Board has an alternate who may replace him/her if he/she is prevented from attending. The term of office of the members elected by the Board of Supervisors is 2 ½ years, with a possibility of being extended once.

3. The Banking Stakeholder Group

The EBA's Banking Stakeholder Group (BSG) was established on 18 March 2011 to help facilitate consultation with stakeholders in areas relevant to the tasks of the EBA.

In particular, the Group shall be consulted on actions concerning regulatory technical standards and implementing technical standards and guidelines and recommendations, to the extent that these do not concern individual financial institutions. The Group may also submit opinions and advice to the Authority on any issue related to the tasks of the Authority, with particular focus on a common supervisory culture, peer reviews of competent authorities and assessment of market developments.

The Group may also submit a request to the Authority, as appropriate, to investigate an alleged breach or non-application of EU law.

It is composed of 30 members appointed to represent in balanced proportions credit and investment institutions operating in the EU, their

employees' representatives as well as consumers, the users of financial services and representatives of SMEs.

On 5 July 2011, the BSG members appointed Sony Kapoor as Chair of the BSG and David T Llewellyn as Vice Chair.

The Group held four meetings in 2011, and the minutes of its meetings can be found on the EBA's [website](#).

4. The Board of Appeal

Articles 58 and 59 of the EBA, EIOPA and ESMA Regulations provide for the establishment of a Joint Board of Appeal of the three Authorities. The Board is responsible for deciding on appeals against certain individual decisions of the Authorities. Its decisions can themselves be appealed before the Court of Justice of the European Union.

The Joint Board of Appeal is composed of six members and six alternates, who must be individuals of high repute with a proven record of relevant knowledge and professional experience, including supervisory experience, to a sufficiently high level in the fields of banking, insurance, occupational pensions, securities markets or other financial services. Current staff of the competent authorities, or other national, or EU institutions, involved in the activities of those authorities are excluded from the Joint Board.

In 2011, following a public call for expressions of interest published in the Official Journal of the European Union on 19 January 2011 (C17/2), and after consultation with the ESAs' Board of Supervisors, the EBA, ESMA and EIOPA respectively appointed the members and alternates to their joint Board of Appeal.

The Board of Appeal comprises **six members and six alternates**¹, who are individuals of high repute with a proven record of relevant knowledge and professional experience in the fields of banking, insurance, occupational pensions, securities markets or other financial services.

The inaugural Board of Appeal meeting took place in December 2011, when the Board of Appeal held a preliminary discussion on its Rules of Procedure.

¹The members and alternates of the joint Board of Appeal are: for the **EBA**, William Blair (Member, UK), High Court Judge, Queen's Bench Division; Giuseppe Godano (Alternate, IT), Retired, formerly a lecturer in International and EU law, Universities of Rome and Cassino; Katalin Mero (Member, HU), Associate professor, Department of Finance and Accounting, International Business School, Budapest; Pat McArdle (Alternate, IE), Adviser to the Independent Review Panel of the Irish Department of Finance; for **ESMA**, Arthur Docters van Leeuwen (Member, NL), Chairman of the Advisory Board, Independent Risk Solutions; formerly Chairman of the Committee of European Securities Regulators and of the Netherlands Authority for Financial Markets; Juan Fernandez-Armesto (Member, ES), Arbitrator, formerly Chairman of the Spanish Securities and Exchange Commission; Gerard Rameix (Alternate, FR), Mediator for Credit to Enterprises; Lars Afrell (Alternate, SE), Senior Vice President, Swedish Securities Dealers Association; for **EIOPA**, Noel Guibert (Member, FR), Retired, formerly International Director of the Autorité de Contrôle des Assurances et des Mutuelles (ACAM); Anna Konstantinou (Alternate, GR), Legal Adviser and General Director of the Motor Insurers' Bureau of Greece; Beata Maria Mrozowska (Member, PL), Legal Counsel, Hogan Lovells; Bob Wessels (Alternate, NL), Professor of International Insolvency Law, Leiden University.





The EBA's priorities for 2011

The EBA's priorities for 2011 were set out in its 2011 Work Programme and were organised under three organisational clusters: Regulation, Oversight and Operations.

The set of main priorities identified under Regulation included:

- **Binding Technical Standards related to the CRD III and CRD IV proposal:** initiating a review of a substantial number of existing guidelines that will need to be transformed into Binding Technical Standards (BTS) by 1 January 2014, as mandated by the Omnibus Directive. The focus of these standards will be on: hybrid instruments; securitisation retention clauses; some aspects of the Large Exposures Regime; ECAI assessment; uniform formats and frequencies for liquidity risk reporting, including IT solutions; the joint decision process for the identification of liquidity sub-groups and the specification of requirements for the Leverage Coverage Ratio (LCR); criteria to determine the appropriate ratios between fixed and variable remuneration; specification of the classes of instruments eligible as part of variable remuneration.
- **CRD guidelines:** taking over from the work carried out by the CEBS on several sets of guidelines as mandated in the CRD III review which are due by the end of 2011 and preparing for the new mandates in the context of the CRD IV review to implement Basel III.
- **Remuneration:** Following-up work related to the implementation of CRD III and publication of guidelines on remuneration; developing reporting and benchmarking criteria following the public consultation.
- **Policy analysis and coordination:** establishing a policy analysis and coordination unit to coordinate the EBA's position and role vis-à-vis

the EBC, FSC, EFC, European Commission, European Parliament and the ESRB.

- **Joint Committee work under EBA chairmanship:** chairing the Joint Committee for its first year of operations. In this respect, starting work on some of the Omnibus proposals for cross-sector directives, in particular, in relation to the Financial Conglomerates Directive; undertaking coordinated risk assessment exercises and producing a number of regular reports.

The set of main priorities identified in Oversight included:

- **Binding Technical Standards in reporting frameworks:** working on reporting frameworks, continuing the revision of the COREP and FINREP and developing BTS.
- **Risk dashboard:** developing a Risk Dashboard to identify and measure systemic risk, including work with the ESRB on systemic risk measures.
- **Risk assessments:** providing assessments to the European Parliament, the Council, the Commission and the ESRB of trends, potential risks and vulnerabilities in its area of competence.
- **Stress testing:** conducting the 2011 EU-wide stress test.
- **Home-host support:** Following-up and monitoring the implementation of college-related guidelines issued in 2010 on the operational functioning of colleges and on joint assessment and joint decisions on risk-based capital adequacy.

The priorities identified in the two core clusters will be achieved through the support of **Operations which identified a range of procedural issues to be addressed, including:**

- **Transitional set-up and governance:** defining the EBA's role in its new tasks and assuring that the new governance structure operates well.
- **Staffing:** ensuring that the executive team and the core staffing complement are built up; monitoring the appointment of the EBA's middle management and ensuring a full complement of staff during the year.
- **Budgeting:** implementing the European Commissions' budgeting procedure.
- **Training:** developing a training programme for 2011 aimed at its members.
- **IT:** continuing the work on the implementation of its new IT system.
- **Procurement processes:** setting in train procurement processes for several important expenditures, notably with reference to the EBA's planning for future premises.

The main priorities identified in the area of **Consumer Protection and Financial Innovation included:**

- **Consumer Protection:** identifying and analysing issues and potential concerns related to retail banking customers, where consumer detriment may result from certain retail banking products or services, especially those of an innovative character, and taking (or recommending) further action if deemed necessary.
- **Financial Innovation:** identifying potentially harmful financial innovations, analysing such innovative products or financial activities in depth and assessing their prudential and/or systemic risks, as well as any potential detrimental effects for consumers, and taking (or recommending) further action if deemed necessary.
- **Liaising with stakeholders:** liaising pro-actively with external stakeholders in this new domain of work for the EBA, i.e. European consumer organisations, the EBA Banking Stakeholder Group, the European Commission, and the consumer protection units of the other two ESA's, ESMA and EIOPA.

In addition, the priorities identified by the EBA's Legal Counsel Unit will be to further consolidate the basis of its activities by continuous work on the EBA's legal framework and ensuring the proper functioning of the Authority's Governing Bodies, namely the Board of Supervisors and the Management Board. Other priorities relate to further ex ante legal verification of EBA decisions, opinions and positions. The unit will also strive to ensure a legally sound environment for the EBA, identify possible legal problems associated with the EBA's activities and provide constant monitoring and implementation of laws applicable to the Authority to prevent it from incurring legal risks and will develop solutions for them. Additional support will be allocated in order to ensure that resolutions reached within the structures of the Authority are in conformity with the regulations that govern the EBA.

Regulation



Introduction to EBA's Regulatory Function

In line with the EBA's Founding Regulation, the regulatory function of the Authority has as its main objectives contributing to (i) improving the functioning of the internal market, including, in particular, a sound, effective and consistent level of regulation and supervision; (ii) ensuring that the taking of credit and other risks are appropriately regulated and supervised; and (iii) preventing regulatory arbitrage and promoting equal conditions of competition.

To achieve these overarching objectives, the EBA's regulatory function is responsible for contributing to (i) the establishment of high-quality common regulatory and supervisory standards and practices, in particular by providing opinions to EU institutions and by developing guidelines, recommendations, and draft regulatory and implementing technical standards; and (ii) the consistent application of legally binding EU acts, in particular by contributing to a common supervisory culture, ensuring consistent, efficient and effective application of the acts within the EBA's scope of action.

Recognising that the main scope of action for the EBA relates to the consistent application of the Capital Requirement Directive (CRD) across Member States, the above-mentioned tasks were translated into two main strands of work in 2011: the development of non-binding guidelines for the consistent application of CRD III across the EU, and the preparatory work for the development of a first set of binding technical standards for the

harmonised application of the proposed CRD IV/ CRR.

The non-binding guidelines covered different aspects of CRD III, such as internal governance, extensions and changes to the Advanced Measurement Approach (AMA), remuneration data collection exercises, Stressed Value at Risk (Stressed VaR), and the Incremental Default and Migration Risk Charge (IRC).

The EBA's preparatory work for the development of several binding technical standards (e.g. on such key areas as own funds and liquidity standards) was carried out on the basis of the European Commission's proposals on CRD IV/ CRR of July 2011. This preparatory work was challenging given the unavailability of a final CRD/ CRR text, but essential to ensure that the EBA will be able to deliver high-quality technical standards in time.

The following sections will provide further details on the work developed under the EBA's regulatory function.

2

Building up the Single Rulebook

a) Own funds

The work performed by the EBA in the area of own funds will contribute to the establishment of a Single Rulebook with the particular aim of strengthening the quality of capital and enhancing the transparency of regulatory own funds.

In 2011, the EBA started working intensively on the mandates given by the draft CRR in the area of own funds.

According to the July 2011 European Commission proposal for a Capital Requirements Regulation (CRR), approximately 20 draft technical standards shall be submitted by the EBA to the European Commission, the vast majority of them before 1 January 2013.

On the basis of the European Commission's proposed draft CRR, published on 20 July 2011, the EBA started preparatory work on a consultation paper aimed at setting out the first set of draft regulatory technical standards on own funds.

The proposed standards will cover all areas of own funds, from the features of instruments of the highest quality (Common Equity Tier 1 instruments) to those of instruments of a lower quality (Tier 2 instruments).

The standards will elaborate on the positive elements of own funds – i.e. the characteristics of the instruments themselves – as well as on deductions to be operated from own funds. It is in fact crucial to ensure that there is a uniform approach concerning the deduction from own funds of certain items like losses for the current financial year, deferred tax assets that rely on future profitability and defined benefit pension fund assets. It is also necessary to ensure that, where exemptions from and alternatives to deductions are provided, sufficiently prudent requirements are applied.

Various provisions of the draft technical standards will help to increase the permanence of capital instruments more generally through specification of the features of the instruments and through the specification of provisions relating to supervisory consent for reducing own funds. The draft standards will also increase the loss absorbency features of hybrid instruments.

The EBA Sub-group on Own Funds had already started to carry out an on-going assessment of the features of hybrid instruments issued by EU institutions, namely for the purpose of the 2011 EU-wide stress test and the subsequent capital exercise. This collective analysis promotes transparency, fosters convergence in the features of issuances and leads, where appropriate, to modifications in the terms and conditions of the instruments before they are issued.

Next Steps

The consultation paper on the first set of draft regulatory standards on own funds will be published in the first half of 2012.

Given the sensitive nature of this topic, the consultation process will allow a sufficiently long time so that all interested stakeholders will be able to provide their comments.

Further consultations on the remaining draft technical standards will be released later in 2012. Taking into account the final CRR text as well as the responses to the successive consultations, the EBA expects to finalise the largest part of the technical standards on own funds and to transmit them to the European Commission by the end of 2012.

Under the current draft CRR text, the EBA will monitor the quality of own funds instruments issued by institutions across the EU and must notify the European Commission immediately where there is significant evidence of material deterioration in the quality of those instruments.

This empowerment is particularly crucial as an on-going review of the quality of own funds will be a very useful complement to the establishment of the Single Rulebook, and will enable the Single Rulebook to be alive and effective in the area of own funds. Furthermore, it will ensure that appropriate recommendations for amendments and/or improvements to this Single Rulebook can be proposed.

b) Liquidity

The Commission proposal of 20 July 2011 for CRD IV and a Regulation also transposes the Basel III liquidity rules into European legislation. The proposal includes the introduction of liquidity reporting, which will allow an analysis of the impact of introducing a Liquidity Coverage Ratio (LCR) proposed by the Basel Committee on Banking Supervision. The reporting requirement also focuses on structural longer-term liquidity components, which will enable the EBA to assess the impact and the consequences of introducing the Net Stable Funding Ratio (NSFR) also

proposed by the Basel Committee. The proposal for a regulation includes a number of tasks for the EBA, inter alia to (i) develop reporting formats for the two ratios and additional monitoring metrics, (ii) to propose a uniform definition of assets of high and high liquidity and credit quality under qualitative and quantitative criteria, (iii) to prepare the ground for legislation on the LCR and calibration by a comprehensive impact assessment and, (iv) develop several binding technical standards.

The EBA's liquidity sub-group is in charge of the accomplishment of these tasks. In order to facilitate a smooth transposition to Basel III-compliant liquidity risk reporting, towards the end of 2011 the Board of Supervisors gave its approval to launching a voluntary monitoring exercise nearly one year ahead of the regulatory deadline in order to help banks best assess the potential impact. The sub-group on liquidity provided the national competent authorities with a set of templates for LCR reporting which will be rolled out in spring 2012. In parallel, work continued on a BTS on liquidity risk reporting, which is due to the EU Commission by 1 January 2013 and for which a consultation will be launched in the first half of 2012.

Next Steps

The EBA will use the information gathered during the observation period to inform its report to the Commission on the potential impacts of an LCR and NSFR. With reference to the LCR, there will be a particular focus on the criteria for liquid assets, the identification of retail deposits subject to higher outflows and the likelihood that they will lead to outflows. The observation period for the NSFR will be used to analyse the impact of a structural ratio on provision of long-term credit to the real economy.

c) Internal governance

The Guidelines on Internal Governance were published on 27 September 2011 aiming at strengthening risk management in financial institutions, increasing the stability of the financial sector and re-establishing trust in the banking system, which is crucial if the banking system as a whole is to operate well.

Article 22 of Directive 2006/48/EC requires 'that every credit institution have robust governance arrangements, which include a clear organisational structure with well-defined, transparent and consistent lines of responsibility, effective processes to identify, manage, monitor and report the risks it is or might be exposed to,

adequate internal control mechanisms, including sound administrative and accounting procedures, and remuneration policies and practices that are consistent with and promote sound and effective risk management'. Effective internal governance arrangements are fundamental if institutions, individually, and the banking system as a whole, are to operate well.

In its guidelines the EBA consolidated and updated its former guidelines on internal governance to remedy weaknesses which had been identified as the underlying causes of the financial crisis. Besides other enhancements, new chapters on the transparency of corporate structures, the role, tasks and responsibilities of the supervisory function and on IT systems and business continuity management were added.

In particular, inadequate oversight by and challenge from the supervisory function of management bodies are widely acknowledged to have been the underlying causes of the financial crisis. Therefore, in 2011, the EBA worked intensively on further guidelines in the area of internal governance, further improving and harmonising the assessment of the suitability of members of management bodies and key function holders.

Next Steps

A consultation on the assessment of the suitability of all members of management bodies and of key function holders, both in terms of repute and sufficient experience will be launched in the first half of 2012.

Such an assessment is crucial for the proper functioning of a credit institution. The guidelines will require credit institutions to assess the suitability of members of management bodies and key function holders prior to or immediately after their appointment. The competent authorities will themselves assess the suitability of proposed or appointed members of management bodies based on notifications received from credit institutions. The guidelines will set out several criteria which should be considered in this assessment both by credit institutions and competent authorities.

d) Market risk and securitisation

The CRD III trading book amendments, which entered into force on 31 December 2011, included the requirement of Stressed Value at Risk ('VaR') and Incremental Default and Migration Risk Charge ('IRC') modelling for the calculation of the regulatory capital for market risk in the trading book for credit institutions using the Internal Model Approach ('IMA').

The European Banking Authority was mandated to monitor the range of practices in this area and to provide guidelines on Stressed VaR and IRC modelling.

The objectives of these guidelines are: i) to achieve a common understanding among the competent authorities across the EU on Stressed VaR and IRC modelling in order to enhance convergence of supervisory practices; ii) to create more transparency for institutions when implementing Stressed VaR and IRC into the calculation of the required capital for market risk in the trading book and into their risk management practices; and iii) to create a level playing field among institutions in this area.

After a monitoring period, the EBA started drafting the guidelines and published consultation papers on Stressed VaR and IRC on 30 November 2011 and held a public hearing with market participants on 13 December 2011.

On 31 December 2010, the CEBS published the guidelines on Article 122a of the CRD on the securitisation retention rules, due diligence and disclosure requirements.

Following the publication of the guidelines the EBA received a substantial number of questions from market participants for further clarification on how the guidelines should be interpreted. This resulted in the publication of a Q&A document on 29 September 2011 providing answers to technical and interpretive questions raised by market participants.

The EBA believes the publication of the Q&A paper on the guidelines on Article 122a will further encourage market participants to create a more transparent and uniform securitisation market going forward and will enable more convergence of supervisory practices across Europe with regard to Article 122a.

Next Steps

Following the end of the public consultation period on 15 January 2012, the EBA expects to publish the final guidelines on Stressed VaR and IRC in the first half of 2012.

e) Operational risk

In 2011, the EBA finalised its work on the guidelines on AMA extension and changes. Credit institutions need prior approval to be allowed to use an internal model (referred to as an Advanced Measurement Approach (AMA)) to calculate their capital requirement for operational risk. This AMA, should, at all times, be tailored to the specific characteristics of an institution, so that its actual operational risk profile is effectively covered. Therefore institutions need to review, change and may extend the AMA as appropriate. Changes to the AMA can have a considerable impact on the quality and reliability of the AMA and an institution's capital requirements. It is therefore necessary to involve the competent authority prior to the implementation of any extensions and changes.

The guidelines will harmonise the situations in which institutions should communicate AMA extensions and changes to the competent authorities and will provide guidance to institutions on how to define internal policies for AMA extensions and changes (AMA Change Policy) in line with supervisory expectations. According to these guidelines, changes will have to be categorised according to their materiality. For extensions and significant changes, prior approval by the competent authorities will be required, while major and minor changes will only need to be notified. Supervisors will review the AMA change policies and ultimately either approve or object to any proposed change or extension.

Next Steps

The EBA will publish guidelines on AMA extension and changes at the beginning of 2012. Based on the experience gained through the implementation of these guidelines, the EBA will develop further regulatory standards regarding model changes as required in the proposals of the European Commission for a Regulation on prudential requirements for credit institutions and investment firms.

3

Enhancing regulatory tools for crisis times

a) Remuneration

The guidelines on remuneration policies and practices, published on 10 December 2010, were to be implemented by 1 January 2011. The EBA Task Force on Remuneration performed a comprehensive implementation study on its guidelines in the 4th quarter of 2011. The results of this were published in April 2012 and showed good and convergent implementation of the qualitative policies, while on the quantitative side, there was divergence and poor extension.

Two other tasks for the EBA stemming from CRD III are the collection and disclosure of information on staff earning EUR 1 million or more p.a., and benchmarking remuneration trends and practices at EU level based on quantitative information on remuneration by business areas pursuant to Point 15(f) of Part 2 of Annex XII of the CRD. The Task Force developed two guidelines to facilitate these exercises and ensure a homogeneous approach to data collection at EU level. A public consultation was held in August/September. Eleven parties responded, offering mainly technical comments, for instance on the scope of application, level of consolidation, award period and date of first remittance. The Task Force has revisited the guidelines and broadly accommodated comments as appropriate.

Next Steps

The final guidelines will be published in the first half of 2012. Later, in mid-2012, the EBA will also issue two guidelines on (i) data collection on remuneration for high earners (individuals earning at least 1 million Euro p.a.) and quantitative information on remuneration by business areas pursuant to Point 15(f) of Part 2 of Annex XII of the CRD and (ii) data collection for the benchmarking study. The EBA will also disclose aggregate information on high earners and benchmark the quantitative information received in the second half of 2012.

b) Banks' recovery and resolution

Article 25 of Regulation (EU) 1093/2010 (the EBA Regulation) assigns to the EBA the task of participating actively in the development and coordination of effective and consistent recovery and resolution plans, procedures in emergency situations and preventive measures to minimise the systemic impact of any failure. In particular, the article provides that the EBA may identify best practices at facilitating the resolution of failing institutions, and develop regulatory and implementing technical standards with the same regard. The forthcoming European Commission proposal for establishing a framework for the recovery and resolution of credit institutions and investment firms is expected to further detail the nature and content of recovery and resolution plans, as well as the role of the EBA.

Besides Article 25, a number of other articles of the EBA Regulation assign the Authority powers which are relevant to crisis management and resolution situations. These powers relate notably to action in emergency situations (Article 18), settlement of disagreements (Article 19) and stress-testing exercises (Articles 21 and 32).

The importance of an adequate European framework for crisis management and resolution, and the role that the EBA should play within this context, is also underlined by the Conclusions of the Council of the European Union on Crisis Prevention, Management and Resolution of 18 May and of 7 December 2010.

In line with these provisions, and following previous communications on the same topic issued in 2010, in January 2011 the European Commission published a consultation document on 'Technical details of a possible European crisis management framework'. The analysis carried out in the consultation was broken down into the following main areas: scope of application; competent authorities; recovery and resolution plans (RRPs); early intervention measures; resolution tools; group treatment; financing arrangements. As regards the role of the EBA, the Commission's consultation document underlined the contribution the Authority could give to ensure uniform and consistent application of the new framework across the EU through EBA guidelines and draft technical standards on a number of crucial issues, such those regarding: drafting of RRPs and their assessment; definition of resolution tools and conditions for their application; and, finally, financing arrangements. Moreover, the Commission's consultation emphasises the mediation role that the EBA could play with regard to cross-border groups, to facilitate the application of early intervention

measures and resolution tools in a coordinated way among the competent national authorities.

The EBA replied to the consultation providing its views on issues of particular relevance for supervisory purposes through an opinion based on Article 34(1) of the EBA Regulation, issued on 3 March 2011 and published on the EBA website. Further technical advice was provided in the second half of 2011 to the Commission's services by the EBA's staff as regards following-up working documents dealing with the technical issues of the forthcoming legislative proposal.

Considering the G20/FSB decisions adopted in 2011 – asking the 29 global systemically relevant banks (G-SIBs, of which 15 are European) to meet the resolution planning requirements by the end of 2012 – and the ECOFIN conclusions of 7 December 2010 – asking for the execution of crisis simulation exercises within Cross Border Stability Groups (CBSGs) by mid-2012 -, in the second half of 2011 the Authority prioritised its work, focusing on the criteria for drafting and assessing RRP. The aim is to identify best practices through the work carried out in conjunction with the national supervisory authorities as well as to promote convergence on these best standards across the EU. Within this context, the Authority has started a stock-taking exercise on the different national experiences so far carried out on RRP, highlighting the areas where further work is needed, and worked on a EU common template to provide guidance on drafting recovery plans.

The EBA worked in conjunction with the other ESAs under the auspices of the Joint Committee to clarify the main legal questions related to the interpretation of Article 19 (actions in emergency situations) and set up a common operational framework to cater for possible emergency situations.

Finally, coordinated work across the ESAs was also carried out to set up an institutional framework to carry out the ESAs' mediation role, which represents an important aspect for the purposes of crisis management and resolution as highlighted above.

Next Steps

The EBA expects to publish a discussion paper proposing a template for recovery plans in the first half of 2012.



Plans for 2012

In 2011 the main focus of work of EBA's regulatory function was two-fold: on the one hand, it was aimed at developing non-binding guidelines for the consistent application of CRD III, and on the other hand, at preparing the ground for the development of a first set of binding technical standards in accordance with the mandates set out in the draft CRD IV.

In 2012, regulatory work will be even more intense on the development of the Single Rulebook in banking and the harmonised application of CRD IV. Most of the efforts will be concentrated on preparing and delivering sets of binding technical standards on key aspects of CRD IV. These aspects include Basel III topics like own funds (e.g. Common Equity Tier 1, Additional Tier 1, deductions from Common Equity Tier 1 and from own funds in general, transitional provisions on grandfathering, disclosure by institutions), liquidity standards (e.g. a reporting template for the LCR) and leverage ratio (e.g. a reporting template for monitoring), as well as other topics such as gain on sale of securitised assets, and credit value adjustments. In addition, jointly or in consultation with the ESMA and EIOPA, the EBA will prepare the technical standards to ensure that Central Counterparties in Clearing, Payments & Settlements are safer, as required in the European Market Infrastructure Regulation (EMIR). In parallel, monitoring of the effective implementation of regulations is developing in order to impose consistent pan-EU banking regulatory standards.



Chart 01: Timeline for CRD IV/CRR²

²This graph is based on the ECOFIN CRD IV/CRR compromise proposal, agreed on 15 May 2012, which is now currently under discussion with the European Parliament. As a result of these negotiations, the proposal may consequently change.

Oversight



Introduction to the EBA's bank oversight and key developments in 2011

a) The EBA's response to developments in the banking sector

The EBA's work on oversight is focused on ensuring the efficient functioning of colleges of supervisors, vital for the effective oversight of cross-border banking groups, and on undertaking risk assessments, including stress tests, of the EU banking system. In 2011, the priorities of the EBA had to be focused on the challenges raised by the deterioration of the financial market environment, whilst simultaneously building the risk infrastructure needed for effective oversight.

A key component of the oversight activities in 2011 was the EU-wide stress test exercise. The stress test, run on 91 banks with a single adverse scenario and consistent methodology, saw banks raise some EUR 50 bn in fresh capital in the first four months of 2011 in anticipation of meeting the commonly agreed capital threshold, which anticipated many aspects of the new Basel standards. The stress test was accompanied by a comprehensive peer review process, which ensured consistency of the exercise across the Single Market, notwithstanding the many differences in national regulatory frameworks. The exercise also included an unprecedented disclosure of data (more than 3 200 data points for each bank), including, among other things, detailed information on sovereign holdings.

However, the progress of the stress test was tracked by a significant further deterioration in the external environment. The main objective of restoring confidence in the European banking sector was not achieved, as the sovereign debt crisis extended to more countries and many EU banks, especially in countries under stress, experienced significant funding challenges.

In this context, the International Monetary Fund (IMF) and the European Systemic Risk Board (ESRB) called for further coordinated policy action. The EBA's risk assessments identified a need for action on both the funding and the capitalisation side. While underlining the need for the establishment of an EU-wide funding guarantee scheme, the EBA focused its efforts on further strengthening bank capitalisation. The EBA's Board of Supervisors subsequently agreed that a further recapitalisation effort was required and asked banks to reach a higher, 9%, capital ratio after taking into account sovereign buffers. The progress of the recapitalisation was discussed and monitored by colleges of supervisors.

b) The EBA's oversight responsibilities

As part of its overall responsibilities, the EBA is in charge of both (i) the monitoring, assessment and analysis of risks and vulnerabilities in the EU banking sector; and (ii) of ensuring effective and efficient cooperation between national supervisory authorities in the field of banking supervision, by means of policy work and active participation in the colleges of supervisors. The following sections describe how these tasks are pursued by the EBA.

2

Building the risk analysis infrastructure

One of the fundamental responsibilities of the EBA, as set out in its Founding Regulation, is to ensure the orderly functioning and integrity of financial markets and the stability of the financial system in the EU. To this end, the EBA is mandated to monitor and assess market developments as well as to identify trends and potential risks and vulnerabilities in the banking system. To achieve these objectives, the EBA started building a risk assessment and analysis infrastructure, focusing on a number of monitoring tools to carry out micro-prudential risk assessments (see Chart 02).

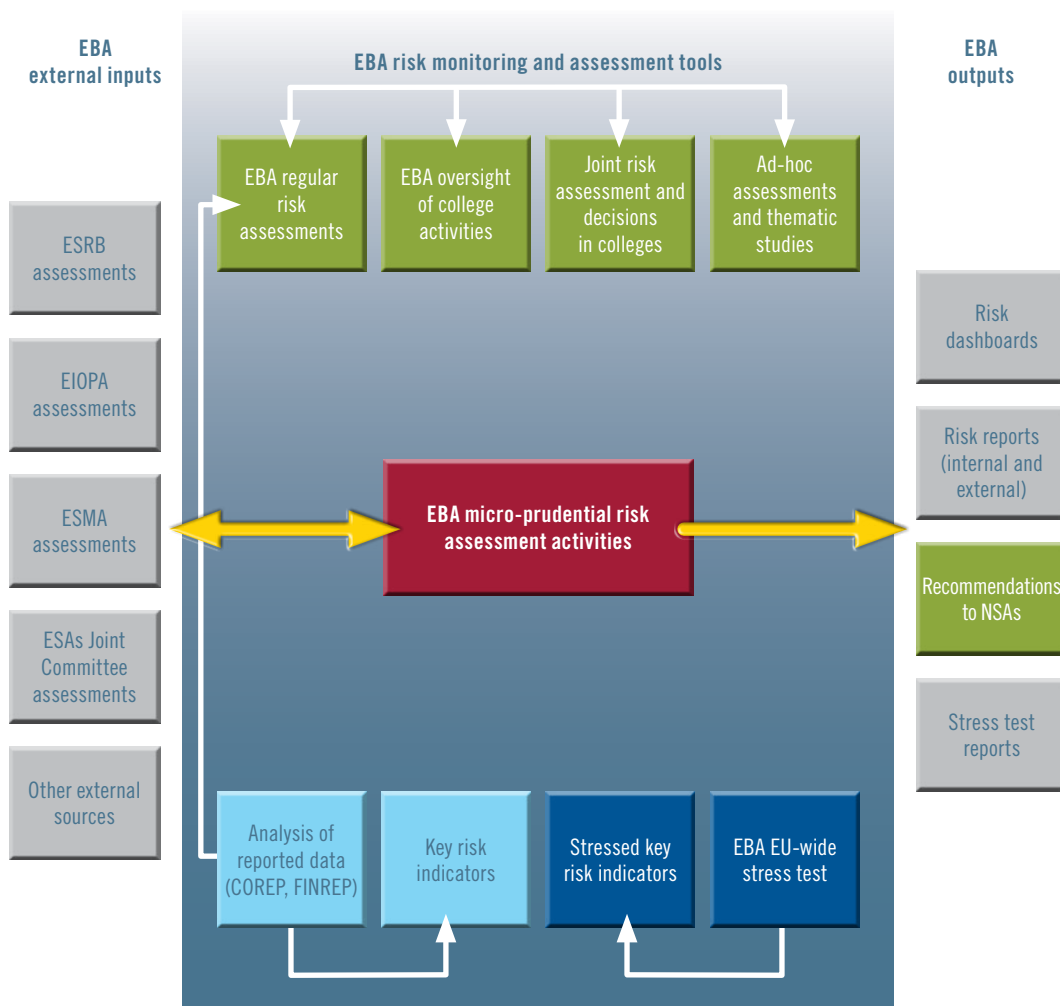


Chart 02: The EBA micro-prudential risk analysis framework for the EU banking sector

The key tools employed for the EBA's analysis of risks are (i) monitoring and analysis of financial and non-financial data through the collection of Key Risk Indicators (KRIs), market data, supervisory and market intelligence, (ii) regular bottom-up assessment of risks and vulnerabilities for the largest EU cross-border banking groups and (iii) EU-wide stress tests. The other inputs for risk assessments are the information shared by the other ESAs and the ESRB as well as information gathered from the NSAs within the scope of home and host cooperation and participation in the colleges of supervisors. Collectively, KRI data, stress testing data, and qualitative and quantitative information deriving from the work of the colleges of supervisors (notably joint risk assessment reports produced by the colleges) facilitate the creation of risk dashboards.

a) Quantitative data and common supervisory reporting

The quality of the EBA's work on risk analysis and assessment relies hugely on consistent micro-prudential financial and non-financial information. In 2011, the EBA devoted significant resources to the establishment of a framework for gathering such information, covering both regular and ad-hoc data collections. In close cooperation with national experts, the EBA defined its data requirements and established an IT infrastructure for reporting.

The EBA currently collects a core set of KRIs, which provide early warning signals of potential risk events. The KRIs are reported quarterly by the national authorities and cover 57 banks from 20 EEA countries. In terms of coverage, the banks in the sample represent at least 50% of each national banking sector and the time-series have been collected, on a best efforts basis, since the last quarter of 2008.

The definitions of KRIs are consistent with the COREP and the FINREP frameworks. For jurisdictions where these standards have not been implemented, the authorities have been encouraged to map local reporting standards to the common EU frameworks, thus highlighting the importance of increasing the consistency of supervisory reporting ensuring harmonisation and comparability of data.

Common European supervisory reporting – FINREP and COREP

To enhance comparability in the EU, in 2005, the Committee of European Banking Supervisors (CEBS) – the EBA's predecessor – published a standardised financial reporting framework (FINREP) for reporting the consolidated financial accounts of EU credit institutions using IFRS. The common framework (COREP) for reporting capital adequacy data for supervisory purposes was published in early 2006.

From a micro-prudential standpoint, the comparability of data across intermediaries is an essential feature, since it is the precondition for carrying out peer analyses and benchmarking exercises. To ensure this, the EBA is strongly committed to delivering a truly European reporting framework in 2012 by developing draft technical standards on supervisory reporting. These standards, which were published for consultation in December 2011, will cover reporting of capital adequacy, financial information, liquidity, large exposures and leverage ratio and they will specify uniform data elements, frequencies and remittance dates as well as the IT solutions to be applied by credit institutions and investment firms in Europe.³

b) Regular risk assessment and analysis

For the purposes of risk assessment and analysis, the EBA's work draws on quantitative information from supervisory reporting data (above) and from ad hoc data surveys as well as on detailed information from the NSAs and colleges of supervisors of the largest cross-border banking groups.⁴ In addition, market information and other external sources are used. The EBA's risk assessment activities also benefit from the joint assessments of risks performed by the colleges of supervisors in order to reach a shared decision on institution-specific Pillar 2 capital requirements. This demonstrates the important role of qualitative information in fine-tuning risk assessments and interpreting the results of the quantitative data.

The EBA's risk assessment and analysis activities have led to a production of various internal (aimed at its Board of Supervisors and NSAs, in general), and external risk reports. In 2011, the EBA submitted regular reports on risks and vulnerabilities in the EU banking sector to the Board of Supervisors, to the Economic and Financial Committee (EFC), and to the ESRB General Board.

³ A consultation paper on draft Implementing Technical Standards (ITS) on supervisory reporting requirements for institutions (CP50) is available on the EBA website: <http://eba.europa.eu/Publications/Consultation-Papers/All-consultations/CP41-CP50/CP50.aspx>

⁴ In 2011, the sample of banks covered by the EBA's micro-prudential risk assessment covered the 30 largest cross-border banks. For the 2012 risk assessment cycle, the sample will be expanded and harmonised with the list of banks monitored for all EBA bank oversight work.

The information collected for risk assessment and analysis purposes is also used to produce risk dashboards for the EU banking sector, which assist in prioritising risks and observing how those risks change over time. The EBA started developing these risk dashboards in 2011 and despite their embryonic status, they already form an integral part of the EBA's risk assessment toolkit.

Finally, in addition to the regular banking risk assessments, the EBA conducts thematic risk analyses on specific themes of supervisory concerns based on the collection and analysis of quantitative and qualitative information from the NSAs. In 2011, the focus of such data collections and subsequent analysis was on loan restructuring and modifications, forbearance and deleveraging.

Next Steps

In 2012, the EBA, in addition to delivering its regular risk reports to the ESRB and Council, will start to deliver an annual 'risks and vulnerabilities' report to the EU Parliament.

EBA risk assessments in the ESFS context

Being an integral part of the ESFS, in its risk analysis and assessment activities the EBA actively cooperates with the other ESAs and the ESRB. In addition to the regular reporting to the ESRB of its micro-prudential view on systemic risk, the EBA also looks at how macro-prudential risks and vulnerabilities identified by the ESRB affect individual institutions, bridging the gap between macro- and micro-prudential supervision and bringing a supervisory perspective to the EU policy debate; in short, helping to ensure that there is better informed decision-making.

Another important aspect in the EBA's risk assessment work is to ensure cross-sectoral coverage. This is achieved through close cooperation with other ESAs by means of the ESA's Joint Committee which aims at capturing cross-sectoral risks, their interaction and spill-over effects.

⁵The stress test was conducted on a sample of 91 banks, but the results have been released for 90 banks.

⁶In some exceptional cases, national supervisors calculated the impact of the EU-wide stress test on the solvency of banks (mainly applicable to small banks).

c) EU-wide stress testing

Articles 21 and 32 of the EBA Regulation give the EBA powers to initiate and coordinate EU-wide stress tests, in cooperation with the ESRB. The aim of such tests is to assess the resilience of financial institutions to adverse market developments, as well as to contribute to the overall assessment of systemic risk in the EU financial system. Stress tests are one of the primary components of the EBA's supervisory coordination toolkit.

The aim of the EBA 2011 EU-wide stress test was to assess the resilience of 91⁵ participating banks from 21 EEA countries against an adverse, but plausible macro-economic scenario.

In 2011, an EU-wide stress test was coordinated by the EBA in a constrained bottom-up fashion, using consistent methodologies, scenarios and key assumptions developed by the EBA in cooperation with the ESRB, the ECB and the European Commission. The banks were provided with a common scenario and requested to calculate its impact on their solvency levels using their own models,⁶ but applying the binding and consistent methodology set out by the EBA. This implied that banks were requested to undertake the analysis on a static balance sheet, precluding any mitigating management actions such as shrinking their balance sheets. Banks also had to adopt conservative approaches to market risk and securitisation. Although the test focused on credit and market risks it also, in recognition of the risks that subsequently crystallised, incorporated sensitivity to movements in funding costs and an assessment of credit risk in sovereign portfolios.

A key feature of the 2011 EU-wide stress test was a comprehensive quality assurance and peer review process, where the preliminary results of the stress tests were compared against a set of benchmarks, including the results of the top-down stress tests performed by the ESRB.

Next Steps

In 2012, the EBA will continue building its analytical capacity and working on the methodologies for EU-wide stress testing, whilst the next actual exercise will be undertaken in 2013.

Results of the 2011 stress test

The aggregate Core Tier 1 (CT1) ratio of the 90 banks that published information in the 2011 EBA stress test decreased from 8.9% to 7.7% after two years of stress. The largest driver was impairment charges which led to a CT1 decrease of 3.6 percentage points (see charts 03 and 04).

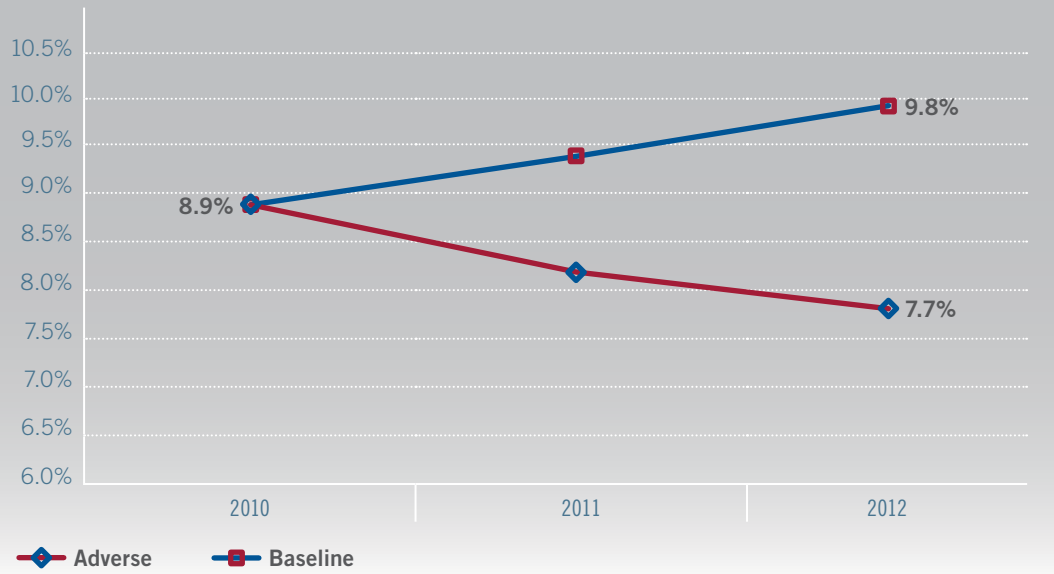
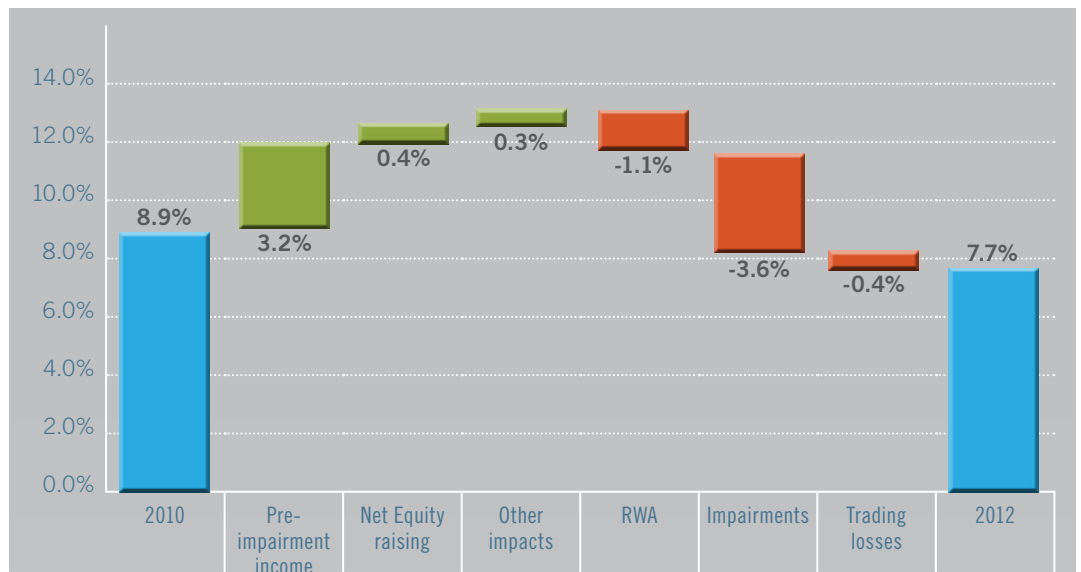


Chart 03: Evolution of aggregate CT1 ratio (baseline and adverse scenarios)



Despite the significant capital raising in anticipation of the EBA stress test, the post stress capital ratios of eight banks fell below the capital threshold set at the level of 5% CT1. In addition, 16 banks displayed post stress CT1 ratios between 5 and 6% after the application of the adverse scenario over the two-year time horizon. The results of the 2011 EU-wide stress test published in July 2011 were accompanied by unprecedented bank-by-bank disclosure of banks' sovereign and credit exposures as well as by details on capital movements and planned mitigating measures.⁷

On the basis of the results of the stress test, the EBA issued its first formal recommendation addressed to national supervisory authorities, requiring them to take appropriate remedial actions for the banks whose CT1 ratios under the adverse scenario fell below the 5% threshold set up for the exercise.⁸ This recommendation was designed to strengthen the capital position of the banks in the sample in a consistent way across banks, but was not a substitute for the idiosyncratic monitoring of asset quality, capital and liquidity that was undertaken by the supervisory authorities under the auspices of the colleges of supervisors.

Chart 04: Drivers of the CT1 ratio under the adverse scenario

⁷ More detailed information regarding 2011 EU-wide stress test, including methodology, scenarios, results and individual disclosures is available on the EBA website: <http://www.eba.europa.eu/EU-wide-stress-testing/2011/2011-EU-wide-stress-test-results.aspx>

⁸ The EBA Recommendation on remedial actions after the results of the 2011 stress tests is incorporated into the Aggregate report on the results of the 2011 EU-wide stress tests: http://stress-test.eba.europa.eu/pdf/EBA_ST_2011_Summary_Report_v6.pdf

d) 2011 Capitalisation exercise

Following the escalation of the sovereign debt crisis in Europe in Autumn 2011, which led to serious disruption and instability in the banking system, the EBA, as part of a broader European stability package agreed by the ECOFIN in November 2011,⁹ conducted a capital exercise among 71 banks aiming at assessing their capital needs and restoring confidence in the markets. Following the assessment of capital needs, the EBA issued a second formal recommendation in order to ensure that all 71 banks covered by the analysis built a temporary capital buffer to reach a 9% CT1 ratio by 30 June 2012, following a prudent valuation of sovereign debt holdings reflecting market prices as of 30 September 2011.¹⁰

Pursuant to this Recommendation, the EBA set up a series of follow-up steps requiring banks with a capital shortfall (see chart 05 for distribution of the shortfall by country) to present their capital plans (to be finally approved by the respective NSAs) outlining the measures they plan to take in order to meet the 9% CT1 capital threshold by 30 June 2012. These capital plans have been reviewed by the respective consolidating national supervisory authorities in close cooperation with the colleges of supervisors and the EBA.

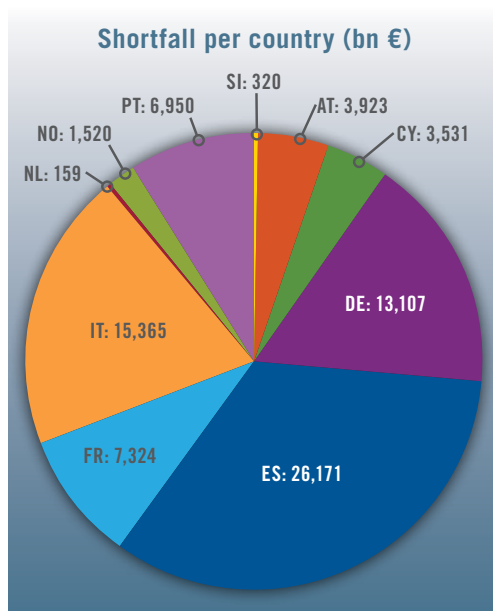


Chart 05: Distribution of capital shortfall by country

⁹ See ECOFIN Council conclusions of 8 November 2011 (http://www.consilium.europa.eu/uedocs/cms_data/docs/pressdata/en/ecofin/125976.pdf)

¹⁰ The EBA Recommendation on the creation and supervisory oversight of temporary capital buffers to restore market confidence (<http://www.eba.europa.eu/capitalexercise/2011/2011-EU-Capital-Exercise.aspx>)

The EBA Recommendation on the recapitalisation of banks led to significant efforts from banks to strengthen their capital positions without disrupting lending into the real economy. Since the submission of the capital plans in early 2012, the EBA's intensive monitoring of the process shows that 96% of the shortfall identified was expected to be met by actions with a direct capital impact, with the overall impact of capital plans amounting to EUR 98 bn against the original shortfall of EUR 78 bn (see chart 06).

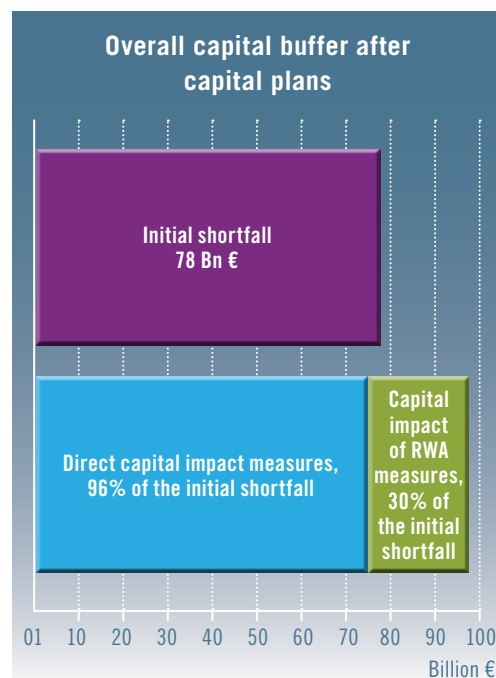


Chart 06: Aggregate impact of capital plans against the capital shortfall

Next Steps

An important task for the EBA in 2012 will be to closely monitor the fulfilment of capital plans put forward by banks with a capital shortfall, ensuring that they do not cause disorderly and excessive deleveraging and do not lead to significant constraints on the credit flow to the real economy.



3

Colleges of supervisors

a) Colleges as an effective tool for cross-border supervision

Enhanced cooperation between supervisory authorities both at EU and global level is the key to strengthening the supervision of cross-border banking groups. The vehicles for the coordination of supervisory activities are the colleges of supervisors. Under EU law, such colleges have to be established for EEA banks with subsidiaries or significant branches in other EEA countries. They may include supervisors in non-EEA countries, where relevant. When they function at their best, the colleges allow supervisory authorities to join forces, share knowledge and use skills and resources more effectively and efficiently, regardless of their individual jurisdiction. This requires determination and significant efforts to prompt coordinated approaches among competent authorities.

To assist in developing a consistent and effective college framework, the EBA's predecessor, the CEBS, published guidelines (i) on the operational functioning of colleges and (ii) on the joint assessment of banks' risks, and joint decisions on the adequacy of cross-border banks' capital within a college setting.¹¹

Since 2009, the national supervisory authorities within the EEA have set up more than 100

Colleges of supervisors as a cooperation structure

The colleges of supervisors are permanent, although flexible, coordination structures that bring together competent authorities involved in the supervision of a banking group.

In practice, the colleges are a mechanism for the exchange of information between home and host authorities, for the planning and performance of key supervisory tasks in a coordinated manner or jointly, including all aspects of ongoing supervision, and also for the preparation for and the handling of emergency situations. As of 2011, one of the fundamental tasks for supervisory authorities as members of colleges is reaching joint decisions on the risk-based capital adequacy of cross-border groups and their EEA subsidiaries.

colleges. Some of them consist of two authorities only, whereas others comprise 20 or more authorities from all parts of the world. The frequency and intensity of college activities can differ significantly depending on the size and complexity of the institutions.

b) EBA support and monitoring of college activities

Out of the more than 100 supervisory colleges that are established in the EEA, the EBA focuses its monitoring activities on 44 'priority' colleges established for the supervision of the largest cross-border groups (see Chart 07).

¹¹ CEBS Guidelines on the Operational functioning of Colleges (GL34) and CEBS Guidelines for the joint assessment of the elements covered by the Supervisory Review and Evaluation Process (SREP) and the joint decision regarding the capital adequacy of cross border groups (GL39).

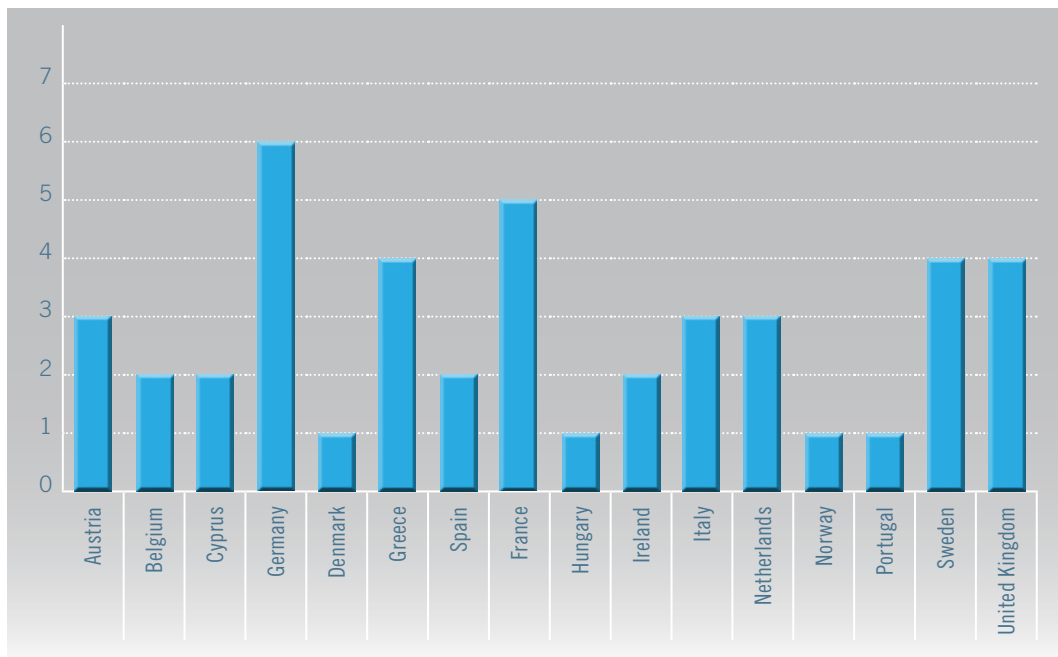


Chart 07: Distribution of 'priority' colleges per country

During 2011, the college activities of 44 of the largest banking groups were closely monitored by the EBA as a priority. Among its tasks were: (i) EBA staff participation in all aspects of college work, (ii) provision of guidance and tools to assist in fostering a common supervisory culture; and (iii) assessing and ensuring the colleges' adherence to the 2011 EBA action plan, which was based on the key deliverables outlined above and on the college-related guidelines. The aim of EBA staff participation and monitoring was to oversee the effective functioning of the colleges of the largest cross-border banking groups and their compliance with legal requirements (see Chart 08).

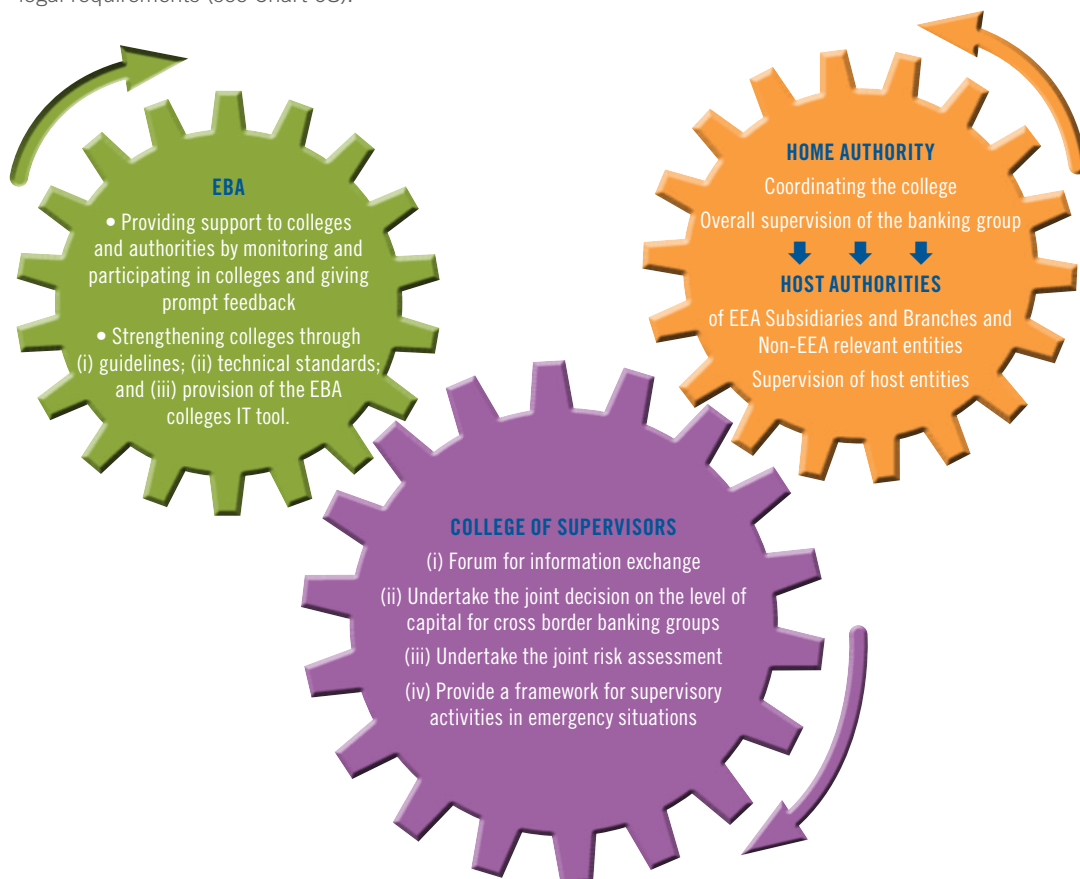


Chart 08: Interaction between the colleges and the EBA in the supervision of cross-border banks

2011 was an important milestone for the European colleges of supervisors as it was the first year that colleges legally had to reach joint decisions on the level of risk-based capital adequacy for cross-border banking groups, both on consolidated and individual entity levels. Such joint decisions based on the joint risk assessments conducted by the college members (commonly referred to as joint risk assessment and decisions – JRAD) form an integral part of the supervisory cycle for cross-border banks (see Chart 09).

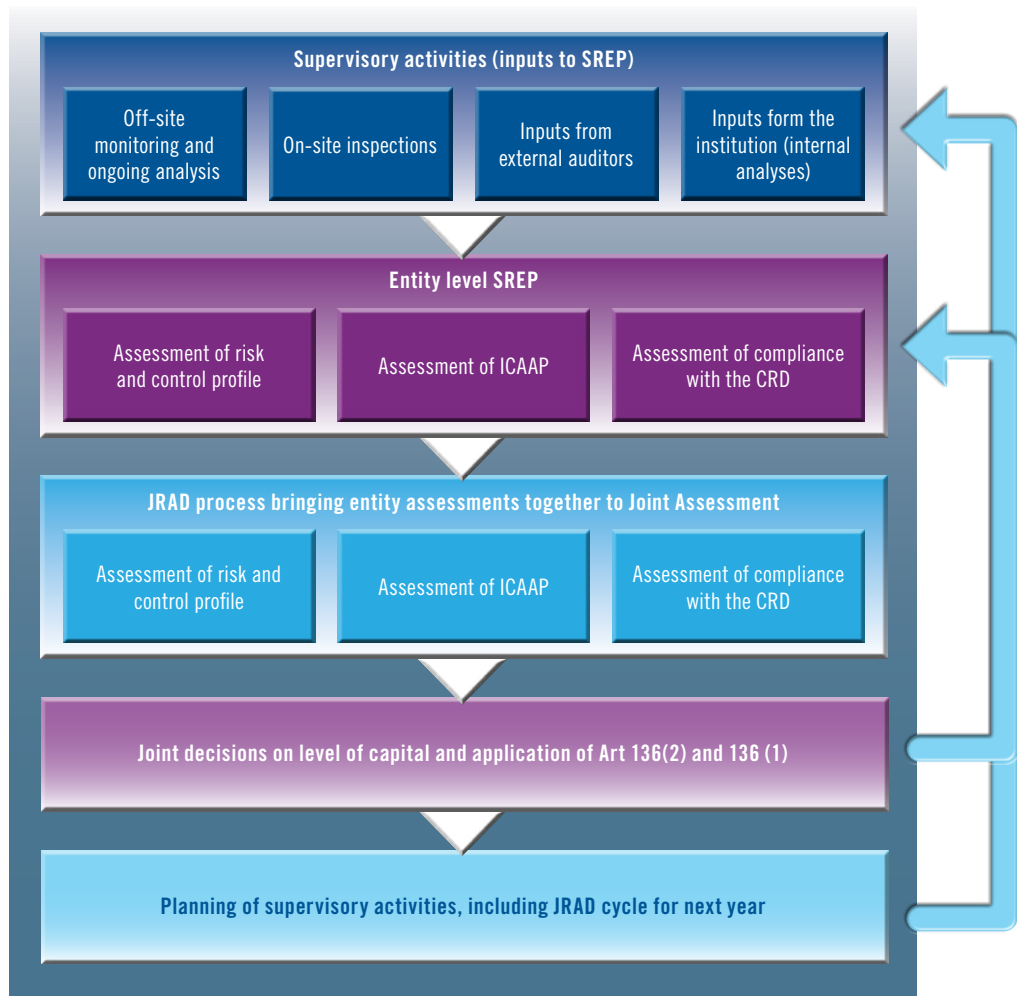


Chart 09: Joint decision as an integral part of the supervisory cycle for cross border banks

As an active member of the colleges, the EBA, drawing on experience gained from attendance across the EU (thus promoting convergence of practices across the colleges) and the EBA's more general work on assessing risk in the EU banking sector, made efforts to contribute to their consistent and coherent functioning. The involvement of the EBA in colleges has also helped the EBA to identify where further support, guidance and tools should be provided for use by competent authorities.

The EBA's initial findings from college participation and monitoring in 2011 indicated that the practices of colleges varied. The EBA's experience

was that effective planning of meetings, conference calls and sharing of risk information are essential for the coordinated performance of supervisory activities, an integrated joint risk assessment cycle, and a meaningful joint decision. In such cases it is noticeable that NSAs have perceived the benefits of increased collaboration and have made colleges an integral part of their supervisory approach. Conversely, where contacts and exchanges are irregular, the lack of coordination worsens under stressed conditions, and discussions on the joint risk assessment did not always cover all material risks in great depth.

Next Steps

When drafting binding technical standards, the EBA will continue to build on the aforementioned areas through its policy work and practical guidance and tools, such as its secure internet tool, for exchanging information (below), in 2012.

Further work is required for the colleges to be effective and efficient vehicles for the supervision of EEA cross-border banking groups. Therefore, a priority for the EBA in 2012 will be the strengthening of the colleges, with continued active EBA staff participation, support and monitoring. The EBA will take a broad view on all colleges, with special attention paid to banking groups covered by all Oversight work (both risk assessment and home-host work).

A significant improvement is envisaged in the EBA's support to the colleges' infrastructure through the EBA IT collaboration tool, a web-based secure platform developed by the EBA in 2011, allowing colleges to exchange information securely and providing web collaboration facilities. Currently the tool is used by 7 colleges and will be used by at least a further 6 in 2012. Going forward, this collaboration tool will be used by the EBA as a means to communicate securely with national supervisors and vice versa.

The legislative proposals for revision of the CRD (CRR/CRD IV package) mandates the EBA with the development of binding technical standards in areas related to home-host issues and functioning of colleges of supervisors. The need for the development of a coherent framework setting the rules and principles of home-host cooperation comes partly as a response to failings in the cooperation and exchange of information among national supervisory authorities that were identified during the crisis. At the end of 2011, the EBA started work on the development of draft regulatory and implementing technical standards (passport notifications, information exchange, colleges of supervisors, joint decisions) and this work will be an important part of the EBA's policy work on colleges in 2012, and in the following years up to 2015.

c) The role of colleges in the 2011 capital exercise

Colleges of supervisors played an important role in the EBA's capital exercise launched in 2011 (see above) by ensuring a coordinated approach to implementing the capital plans and allowing all relevant host authorities to be involved and kept up to date. The consolidating supervisory authorities are responsible for communicating their views on the capital plans taking into account the views expressed by host supervisors in college discussions.

Next Steps

In 2012, the colleges will provide a fundamental basis for discussions and will provide the opportunity for host authorities to better understand the measures outlined in the plans and the implications for the markets in their countries.

d) The role of colleges in crisis management

The importance of robust crisis management procedures has become evident in the turmoil of financial markets in recent years. Proper crisis management is complicated at a domestic level and even more complex where cross-border banking groups are involved. To address this aspect of risk management, the EBA has been mandated to contribute to, and to actively participate in, the development of effective and consistent recovery and resolution plans in the EU.

In 2011, the EBA began attending crisis management groups (CMGs)/cross-border stability groups (CBSGs) for some of the major banking groups with the objective of facilitating the development of best practices in this important area.

Next Steps

In 2012, it is expected that the European Commission will publish its Draft Directive on Bank Recovery and Resolution which will set out the proposed regime for Crisis Management in Europe. It is expected that this Directive will enhance and expand the EBA's role in this area.

In 2012, the EBA will develop common structures/templates for the preparation of Recovery and Resolution Plans by cross-border banking groups. This will be carried out with inputs from national supervisory authorities through the EBA appropriate sub-structures.

In 2012, the EBA expects to become more actively involved in a broader range of CMG activities to facilitate the development of robust crisis management measures in at least all systemically important European cross-border banking groups.

Joint Committee

1

Scope and objectives

The Joint Committee is a forum for cooperation that was established on 1st January 2011 with the goal of strengthening cooperation between the European Banking Authority (EBA), the European Securities and Markets Authority (ESMA) and the European Insurance and Occupational Pensions Authority (EIOPA), collectively known as the three European Supervisory Authorities (ESAs).

The three ESAs cooperate regularly and closely through the Joint Committee and ensure consistency in their practices. In particular, the Joint Committee works in the areas of supervision of financial conglomerates, accounting and auditing, micro-prudential analyses of cross-sectoral developments, risks and vulnerabilities for financial stability, retail investment products and measures combating money laundering.

In addition to being a forum for cooperation, the Joint Committee also plays an important role in the exchange of information with the European Systemic Risk Board (ESRB) and in developing the relationship between the ESRB and the ESAs.

2

Activities

The Joint Committee was successfully established in 2011. It has frequently discussed sector, cross-sector and joint risk assessments, and possible policy options in the light of market developments.

It has established four Sub-Committees:

- **The Sub-Committee on Financial Conglomerates**, which is preparing the ESAs response to the EC's Call for Advice (April 2011), as part of the EC's fundamental review of the Financial Conglomerates Directive (FICOD), in assessing the scope of application, internal governance, and supervisory empowerment and sanctions issues contained in the FICOD. Further the EBA, EIOPA and ESMA have published, under the Joint Committee section, on their respective websites, a list of identified Financial Conglomerates, and their identified relevant competent authorities, as required under the FICOD. Also, the Sub-Committee is developing Technical Standards in relation to the methods of consolidation of Own Funds under the FICOD.
- **The Sub-Committee on Cross-Sectoral Developments, Risks and Vulnerabilities**, which has produced cross-sector risk reports for the EFC-FST meetings in March and September, and contributed to the half yearly ESAs risk assessment reports provided to the ESRB.
- **The Sub-Committee on Anti Money Laundering**, which has identified differences in Member supervisory practices in relation to the

Ultimate Beneficial Owner (UBO) in a business relationship and the application of Simplified Due Diligence (SDD) measures under the 3rd Money Laundering Directive (AML). These differences may create gaps in the EU's AML/ counter terrorist financing (CFT) regime.

- **The Sub Committee on Consumer Protection and Financial Innovation**, which is in the process of being set up to work on consumer protection and financial innovation issues at a cross-sectoral level, for example financial literacy and education initiatives, in order to ensure cross-sector consistency.

In 2011, as required under the Commission's regime for ESAs, the ESAs developed an updated manual on training which was submitted to the

Joint Committee in November 2011. The objective of the manual is to ensure delivery of a successful European supervisory training programme for national supervisors and to provide practical guidance to the NSAs for the organisation and hosting of training events.

The changing regulatory environment and the delay in related legislation resulted in a number of challenges to and modifications to the training programme. The ESAs co-operated in the development of a common questionnaire aimed at assessing the demand for training needs in 2012 and to identify volunteers to host and organise seminars.

The cross-sector training programme for 2011 included the following seminars:

No.	Name of the seminar	Date & Location	Host	Number of participants
1	Reducing systemic risks in markets: a new parameter for overseers and supervisors	31 May- 1 June, Frankfurt	Bafin –Deutsche Bundesbank	50
2	Supervisory Colleges: dealing with cross sector aspects in supervisory colleges	21-22 March	ISVAP, Italy	39
3	New European Regulatory and Supervisory Structure: functioning and impact on national supervisors	7-8 June	Frankfurt, EIOPA	40
4	Operational Risk Management	17 October	Frankfurt, EIOPA	27
5	IT assessment	3-5 October	Madrid	31
6	Risk assessment	19-21 October	Banca d'Italia, Rome	57
In total				244

The ESAs decided to provide financial support for Authorities with financial constraints partly due to the difficult economic situation of some Member States. This facility was used only by a few Member States.

The effort devoted to training staff of EU supervisory and regulatory authorities on a cross-sector basis during 2011 resulted in around 350 supervisors being trained, which means a further strengthening of our common supervisory culture.

Finally, the formation of the **Impact Assessment Network** was initiated, which aims at assisting the ESAs in their consideration and drafting of Technical Standards, Guidelines and Recommendations for Consultations.

Consumer Protection and Financial Innovation



Scope and objectives

In accordance with Article 9(1) of its Founding Regulation, the EBA plays an important role in promoting transparency, simplicity and fairness in the market for consumer financial products or services across the internal market. To this end, the EBA is responsible for:

- Collecting, analysing and reporting on consumer trends;
- Reviewing and coordinating financial literacy and education initiatives by the competent authorities, such as national supervisory authorities;
- Developing training standards for the industry;
- Contributing to the development of common disclosure rules.

In May 2011, the EBA established a Standing Committee on Financial Innovation (SCFI). The SCFI brings together all relevant competent national supervisory authorities with the aim of assisting the EBA in fulfilling its mandate in the areas of consumer protection and financial innovation. The Standing Committee is, in turn, divided into two separate sub-groups, one on Consumer Protection and the other one on Innovative Products. The activities of both sub-groups include:

- a) Monitoring new and existing financial activities with a view to promoting the safety and soundness of markets and convergence of regulatory practices (with potential for adopting Guidelines and Recommendations);

- b) Safeguarding the objectives of Article 1(5) of the Regulation establishing the EBA as against potentially harmful innovative practices and activities, and achieving a coordinated approach to the regulatory and supervisory treatment of new and innovative financial activities;
- c) Developing common methodologies for assessing the effect of product characteristics and distribution processes on the financial position of institutions and on consumer protection (Article 8(2)(i) of the Regulation establishing the EBA).

2

Activities

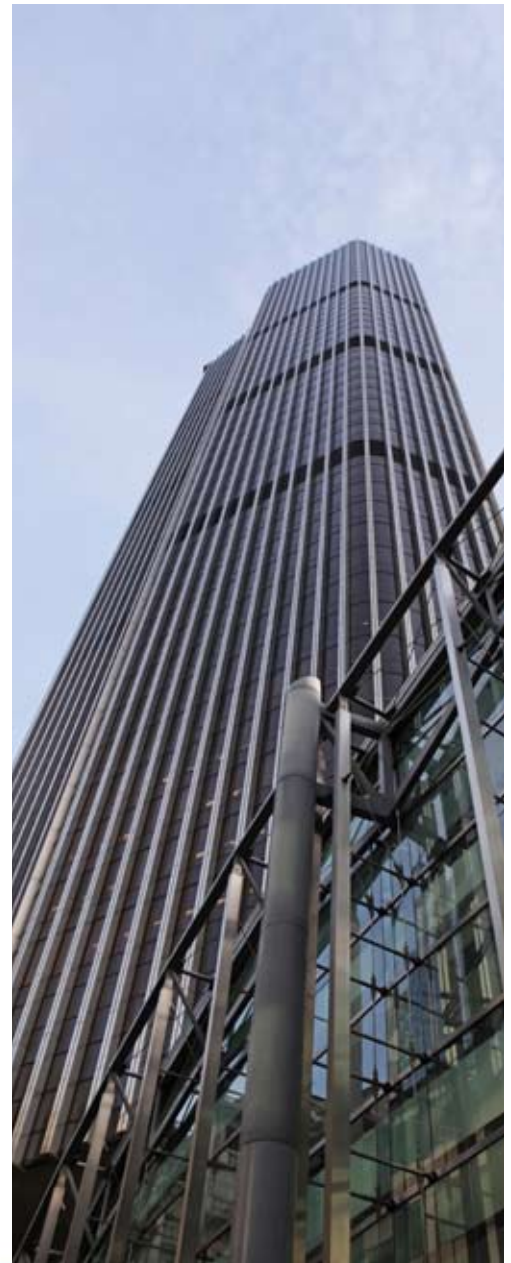
In 2011, the EBA undertook a first survey of national competent authorities to identify the key issues related to consumer protection in the banking sector. The survey suggested that over-indebtedness and responsible lending are still the top critical issues in the European Union. Therefore, in 2011, the EBA focused its work mostly on mortgages and other types of consumer lending and surveyed concerns in areas such as the role of credit intermediaries, transparency and clarity of pre-contractual information provided to consumers, and creditworthiness assessments. In compliance with the draft directive on credit agreements relating to residential property which stipulates that the EBA should define technical standards for professional indemnity insurance for credit intermediaries, the EBA also commenced preparatory work in this area.

In terms of innovative products, the EBA's work in 2011 was aimed at identifying potentially harmful financial innovations, not only from a consumer protection perspective, but also for credit institutions, or the banking system and financial markets as a whole. The so called exchange traded funds (ETFs), contracts for difference (CFDs), and structured products (securities with a pay-off based on structured derivatives) were identified as types of instrument that the EBA should analyse in greater depth, assess the risks they pose and, if deemed necessary, take or recommend further action.

The outcomes of the two surveys – in the area of consumer protection and financial innovation – together with more details of the SCFI's work in 2011 are summarised in '[An overview of the objectives and work of the EBA's Standing Committee on Financial Innovation \(SCFI\) in 2011 – 2012](#)'.

Next Steps

During 2012, the EBA will continue monitoring and analysing potential consumer detriment in the context of the mortgage market and other indebtedness issues (including aspects such as responsible lending, underwriting standards, arrears handling and forbearance) and will be providing guidance for credit institutions where appropriate. Finally, the EBA also will identify and analyse innovative products (or products whose use is innovative and/or rapidly growing) and might issue guidance or propose other measures where appropriate. Closer cooperation with the EIOPA and ESMA through the Joint Committee of the three ESAs will also strengthen the protection of consumers. The EBA's activities will be publicly presented during an EBA's Consumer Day which is planned for the second half of 2012.



Operations

The activities carried out by Operations played a crucial role in the first year of existence of the Authority as they were aimed at establishing its internal organisational structure and ensuring the performance of the two core clusters, Regulation and Oversight.

During 2011 the EBA made significant progress in establishing its internal organisation and operational procedures related to (i) financial management, (ii) human resources, (iii) procurement and (iv) information technologies and communication.

1

Financial Management

In the area of financial management, internal workflows and procedures have been implemented in line with the European Commissions' policies and principles for Financial Regulations and, in May 2011, the EBA was connected to the accrual-based accounting and asset management system provided by the European Commission. This marked an important milestone in implementing the principles of effectiveness, efficiency and sound financial management at the EBA.

2

Human Resources

2011 was crucial in setting up and extending the human resources team in order to adequately source the new functions and tasks of the EBA. In total 33 recruitment procedures have been conducted and the EBA's staff increased from 31 to 52 between 1 January and 31 December 2011. The EBA staff represents 19 nationalities. A more detailed breakdown is provided in Chart 10.

3

Procurement

In 2011, a number of procurement procedures for goods and services were initiated. Due to the significant increase of its headcount, the EBA had to run a tender procedure for the selection of a property advisor which was successfully concluded in December 2011. The EBA has furthermore made use of existing European Commission framework contracts, especially in the IT area, where it deployed a number of internal IT systems, such as email and an intranet, as well as an IT platform for collecting and analysing data from NSAs.

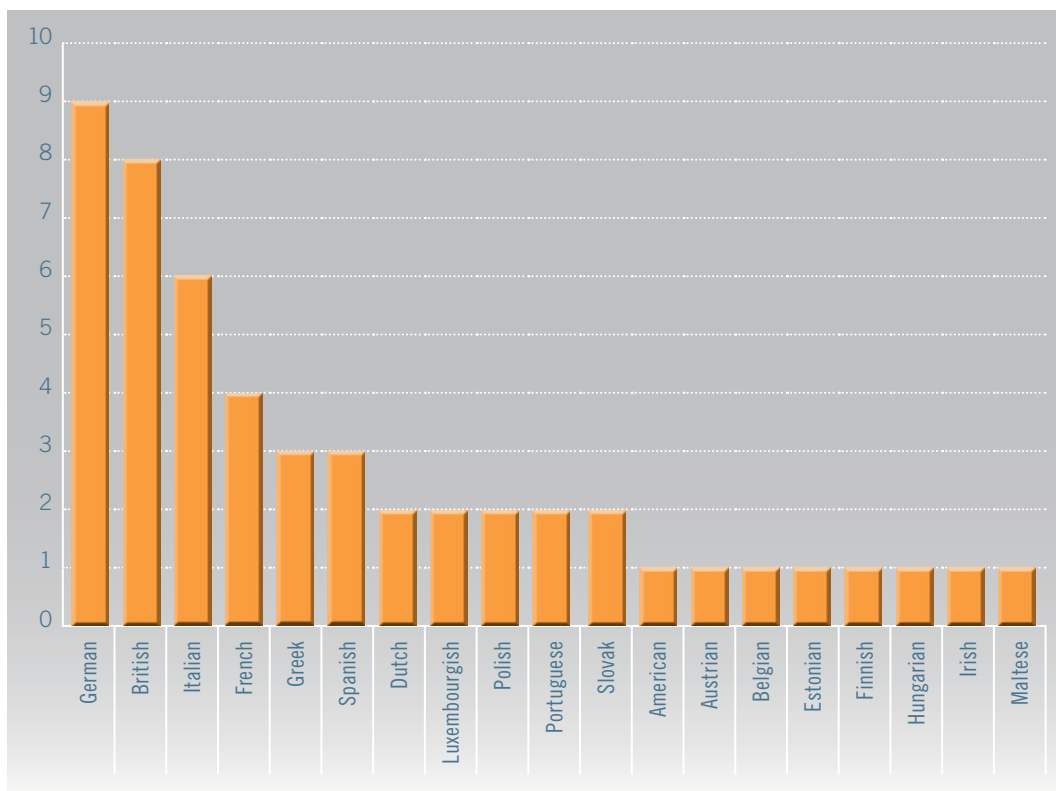


Chart 10: Breakdown of EBA staff by country

4

Information Technologies

The EBA inherited a number of IT service contracts from its predecessor organisation the CEBS. This enabled the EBA IT Team to rapidly deploy a number of horizontal IT systems such as email, mobile devices, an intranet as well as an IT platform for the data exchange, analysis and reporting of Key Risk Indicators. For the coordination of pan-European IT activities the IT-Sounding Board (ITSB) has been continued from the predecessor organisation CEBS.

5

Communication

Besides building the image and reputation of the new Authority, the main challenge in terms of external communication in 2011 was to reach and explain to the appropriate audiences the

EBA's work against a backdrop of the recent developments in the markets, namely the pan-European stress test and the recapitalisation exercise. Throughout 2011, with the support of external contractors for the 2011 EU-wide stress test, the main focus was placed on strengthening relations with the international and financial press and analysts. Some specific actions were also organised in several EU Member States with the help of the network of press officers in the national supervisory authorities, coordinated by the Communications Team. In this respect, the annual meeting of the network was organised in Frankfurt in May, together with the other European Supervisory Authorities. The team also worked on the development of new instruments both for external communication – a tender was launched in December 2011 for the redesign of the EBA website to be carried out in 2012 – and internal communication – i.e. the creation of an intranet platform. In 2011, the Communications Team was expanded with a new communications officer who joined on 1 October. It now consists of two people.

Legal Counsel

Key deliverables in 2011 were the drafting of the Authority's legal framework and the provision of legal advice pertaining to fields across the newly established EBA directorates and units. The unit also oversaw the setting up of the EBA's first Board of Supervisors and Management Board, and is responsible for the administration and functioning of these two governing bodies.

Resources in the unit were also allocated to the provision of legal advice related to the EBA's Founding Regulation and institutional matters, and the drafting and interpretation of implementing rules, rules of procedure, agreements and other undertakings, together with the drafting of numerous decisions taken by the Board of Supervisors, the Management Board, the Chairperson and the Executive Director in order for the Authority to fulfil its duties as intended in its Founding Regulation.

The unit oversaw issues related to public access to documents, interpretation of the Staff Regulations and the CEOS, and the handling of complaints. The unit liaised with other EU bodies such as the European Data Protection Supervisor (EDPS), the European Ombudsman, and other EU agencies, and also engaged in relations with the host state regarding the Seat Agreement.

One of the key challenges in 2011 was related to the proactive contribution to the further development of the EBA's legal framework, as the unit advises on any internal issues which could potentially give rise to litigation, providing legal advice and assistance on, and managing cases of litigation at both administrative and judicial level and representing the EBA in legal disputes before the ESA's Joint Board of Appeal, the European Civil Service Tribunal, the General Court of the European Union and the European Court of Justice.

Next Steps

The legal counsel unit will further consolidate the basis of its activities by continuous work on the EBA's legal framework. The unit will also continue to ensure a legally sound environment for the EBA, identify possible legal problems associated with the EBA's activities, and provide constant monitoring and implementation of laws applicable to the Authority to prevent it from incurring legal risks and will develop solutions for them.

The EBA's priorities for 2012

The year of 2012 will be only the second year of operation for the EBA as a fully-fledged EU Authority in the new European System of Financial Supervision (ESFS). There is therefore still a need to concentrate on the overall development and strengthening of the EBA's institutional capabilities. In addition, there are significant new legislative proposals in European banking regulation on the EU's agenda, some of which have already been published but not yet adopted, and some are expected to be published in the near future, but all having a major impact on the amount and priorities of specific tasks of the EBA in 2012 and thereafter.

The 2012 work programme identifies four areas of the EBA's activities. For the first three areas, **Regulation**, **Oversight**, and **Consumer Protection**, which represent the core functions of the EBA, a detailed list of tasks including a breakdown of deliverables is also provided on the EBA's website.

- The main objective of the EBA in the **regulatory policy area** is to play a leading role in the creation of the **Single Rulebook for the EU banking system**. The EBA is to play a crucial role in the technical implementation and application of this new set of regulatory rules, and will therefore focus its work in this context on accomplishing the drafting of binding technical standards under the new CRD IV/ CRR framework. The legislative proposals are expected to be adopted in mid-2012, and thus the ambitious timeline for implementation poses the biggest challenge for the EBA's organisation.
- The main objectives of the EBA's **regulatory oversight activities** in 2012 will be to (i) deliver independent and **high quality analysis of EU banks and the EU banking sector** in a way that adds value to the work of the NSAs, the ESRB

and EU policy making bodies, and leads to concerted policy responses, and to (ii) promote **supervisory convergence** and assist the NSAs to ensure that the colleges are run consistently and efficiently with substantive discussions leading to material decisions being taken which strengthen the resilience of EU cross-border banks and prepare them better for crises.

- The main tasks of the EBA's **Consumer Protection** work will be the collection, analysis and reporting on consumer trends; the review and coordination process of financial literacy and education initiatives by the competent authorities; the development of training standards and common disclosure rules for the industry; monitoring of new and existing financial activities and where appropriate, preparing guidelines and recommendations with a view to promoting the safety and soundness of markets and convergence of regulatory practice.
- On the **Operations front**, the overall objective of the EBA in 2012 will be the completion and further enhancement of the internal control environment in a period of intensive build-up and growth of the Authority. Internal controls will be improved on the basis of continuous self-assessment against targets and a timeline, as well as on the basis of the findings of the first audit from the Court of Auditors in 2011. Full implementation and standard operation of the EU Internal Control Standards has to be completed in 2012.

Annexes



Declaration of Assurance from the Authorising Officer

I, the undersigned, Adam Farkas, Executive Director of the European Banking Authority, in my capacity as Authorising officer,

- Declare that the information contained in this report gives a true and fair view.¹²
- State that I have reasonable assurance that the resources assigned to the activities described in this report have been used for their intended purpose and in accordance with the principle of sound financial management, and that the control procedures put in place give the necessary guarantees concerning the legality and regularity of the underlying transactions.

This reasonable assurance is based on my own judgement and on the information at my disposal such as the results of ex- ante and ex-post control verifications performed during the year.

- Confirm that I am not aware of anything not reported which could harm the interests of the European Banking Authority.

London, 15th June 2012

Adam Farkas,
Executive Director of the European Banking Authority

¹² True and fair view in this context means a reliable, complete and correct picture of the state of affairs.



Budget

The EBA's financial performance in 2011¹³

The annual accounts of the EBA have been established in accordance with the EBA's Financial Regulation adopted by the EBA's Board of Supervisors, as well as with the 'Framework Financial Regulation' (Commission Regulation (EC, EURATOM) No 652/2008 of July 2008 amending Regulation (EC, EURATOM) No 2343/2002 on the framework Financial Regulation for the bodies referred to in Article 185 of Council Regulation (EC, EURATOM) No 1605/2002 on the Financial Regulation applicable to the general budget of the European Communities).

The accounting rules, methods and guidelines are those adopted and provided by the Accounting Officer of the European Commission.

1. BUDGETARY OUTTURN ACCOUNT FOR 2011

The budgetary accounts below give a detailed picture of the implementation of the Budget in 2011. They are based on the modified cash accounting principle.

REVENUE		
Balancing Commission subsidy	+	5,073,000
Contributions from National Supervisory Authorities	+	7,413,000
Contributions from Observers	+	199,000
Other income	+	
Total Revenue		(a) 12,685,000
EXPENDITURE		
Title I: Staff		
Payments	-	5,308,649
Appropriations carried over	-	501,809
Title II: Administrative Expenditure		
Payments	-	1,400,590
Appropriations carried over	-	458,729
Title III: Operating Expenditure		
Payments	-	726,978
Appropriations carried over	-	657,275
Total Expenditure		(b) 9,054,030
Outturn for the financial year a-b		3,630,970
Cancellation of unused payment appropriations carried over from previous year	+	
Adjustment for carry-over from the previous year of appropriations available at 31.12 arising from assigned revenue	+	
Exchange differences for the year (gain + / loss -)	+/-	(51,109)
Balance of the Outturn Account for the financial year		3,579,861
Balance year N-1	+/-	
Previous balance from year N-1 reimbursed in year N to the Commission	-	
Result used for determining amounts in general accounting		3,579,861
Commission subsidy – agency registers accrued revenue and Commission accrued expense		1,493,139
Pre-financing remaining open to be reimbursed by agency to Commission in year N+1		3,579,861

¹³ The preliminary report from the European Court of Auditors on the EBA 2011 accounts is expected to be received in June 2012.

In 2011 the EBA used only non-differentiated appropriations. The total consumption of commitment appropriations reached EUR 9,054,030, of which EUR 7,436,217 have been paid and EUR 1,617,813 were automatically carried over as per Article 10 of the EBA's Financial Regulation.

2. BUDGET IMPLEMENTATION IN 2011

The table below shows the status of commitments and payments as of 31 December 2011, together with the amounts carried over to financial year 2012.

Title	Appropriations (1)	Committed (2)	% Committed (3) = (2)/(1)	Paid (4)	% Paid (5) = (4)/(1)	Carried Forward (6)	Appropriations cancelled (7) = (1)-(4)-(6)
Title 1 – Staff expenditure	6,407,650	5,810,459	91%	5,308,649	83%	501,809	597,191
Title 2 – Administrative expenditure	3,252,000	1,859,319	57%	1,400,590	43%	458,729	1,392,681
Title 3 – Operational expenditure	3,023,350	1,384,252	46%	726,978	24%	657,275	1,639,098
GRAND TOTAL	12,683,000	9,054,030	71%	7,436,217	59%	1,617,813	3,628,970

For the first year of activity of the EBA, the overall budget execution rate reached 71% in terms of commitments and 59% in terms of payments.

3. ECONOMIC OUTTURN ACCOUNT FOR 2011

The financial statements below show all charges and income for the financial year based on the accrual accounting rules complying with the European Commission's accounting rules.

2011	
OPERATING REVENUE	
Contribution from the Member States	7,413,000
Contribution from EFTA countries	199,000
EU Subsidy	1,493,139
Foreign currency conversion gains	124,415
Total Operating Revenue	9,229,554
OPERATING EXPENSES	
Staff expenses	5,359,276
Building and related expenses	864,118
Other expenses	2,538,050
Fixed asset related expenses	449,258
Foreign currency conversion losses	175,525
Total Operating Expenses	9,386,227
Surplus (Deficit) from Operating Activities	(156,673)
NON OPERATING REVENUES (EXPENSES)	
Financial expenses	(2,862)
Surplus/(Deficit) from Non-Operating Activities	(2,862)
Surplus/(Deficit) from Ordinary Activities	(159,535)
Surplus/(Deficit) from Extraordinary Items	–
ECONOMIC OUTTURN FOR THE YEAR	(159,535)

4. BALANCE SHEET

The balance sheet provides the financial position of the EBA as at 1.01.2011 and 31.12.2011

ASSETS	31.12.2011	01.01.2011
NON-CURRENT ASSETS		
Tangible fixed assets		
Computer Hardware	74,815	64,127
Furniture	84,247	108,347
Other fixtures and fittings	418,310	486,932
Total	577,372	659,406
CURRENT ASSETS		
Current receivables	170,754	223,486
Sundry receivables	206,683	
Prepaid expenses	66,360	194,129
EU entities	–	740,375
Cash and cash equivalents	6,378,023	2,756,875
Total	6,821,820	3,914,866
TOTAL ASSETS	7,399,192	4,574,272
LIABILITIES		
NON-CURRENT LIABILITIES		
Provision for risks and charges	784,316	0
Total	784,316	0
CURRENT LIABILITIES		
Current payables	2,319,492	3,117,509
Deferred revenues	–	580,000
Sundry payables	4,569	63,524
EU entities	3,637,111	0
Total	5,961,172	3,761,033
TOTAL LIABILITIES	6,745,488	3,761,033
NET ASSETS		
Accumulated results from previous years	813,239	813,239
Economic outturn for the financial year – profit/(loss)	(159,535)	0
TOTAL NET ASSETS	653,704	813,239



Glossary and abbreviations

- AMA** Advanced Measurement Approach
- AML** Anti Money Laundering
- BSG** Banking Stakeholder Group
- BTS** Binding Technical Standards
- CBSGs** Cross Border Stability Groups
- CCP** Central Counterparty
- CEBS** Committee of European Banking Supervisors
- CEOS** Staff Regulations and Conditions of Employment of other servants
- CFDs** Contracts for difference
- CFT** Counter terrorist financing regime
- CMGs** Crisis management groups
- COREP** Guidelines on Common Reporting
- CRD** Capital Requirements Directive (refers collectively to both 2006/48/EC and 2006/49/EC)
- CRD II** Commission Directive 2009/111/EC of the European Parliament and of the Council of 16 September 2009 amending Directives 2006/48/EC, 2006/49/EC and 2007/64/EC as regards banks affiliated to central institutions, certain own funds items, large exposures, supervisory arrangements and crisis management
- CRD III** Proposal for a Directive of the European Parliament and of the Council amending Directives 2006/48/EC and 2006/49/EC as regards capital requirements for the trading book and for resecuritisations, and the supervisory review of remuneration policies
- CRD IV** Proposal for a Directive of the European Parliament and of the Council amending Directives 2006/48/EC and 2006/49/EC as regards liquidity standards, definition of capital, leverage ratio, counterparty credit risk, counter-cyclical measures including through-the-cycle provisioning for expected credit losses, systemically important financial institutions and a single Rulebook for banking
- CRR** Proposal for a Regulation on prudential requirements for credit institutions and investment firms, also called Capital Requirements Regulation
- DGS** Deposit Guarantee Schemes
- EBA** European Banking Authority
- EC** European Commission
- ECOFIN** Economic and Financial Council
- EDPS** European Data Protection Supervisor
- EEA** European Economic Area
- EFC** Economic and Financial Committee
- EFC-FST** Economic and Financial Committee – Financial Stability Table
- EIOPA** European Insurance and Occupational Pensions Authority
- EMIR** European Market Infrastructure Regulation
- ESAs** European Supervisory Authorities
- ESFS** European System of Financial Supervisors
- ESMA** European Securities and Markets Authority
- ESRB** European Systemic Risk Board
- EU** European Union
- FICOD** Financial Conglomerates Directive (Directive 2002/87/EC of the European Parliament and of the Council of 16 December 2002 on the supplementary supervision of credit institutions, insurance undertakings and investment firms in a financial conglomerate and amending Council Directives 73/239/EEC, 79/267/EEC, 92/49/EEC, 92/96/EEC, 93/6/EEC and 93/22/EEC, and Directives 98/78/EC and 2000/12/EC of the European Parliament and of the Council, OJ L 35 of 11.2.2003)
- FINREP** Standardised framework for consolidated financial reporting for credit institutions (Financial Reporting)
- FSB** Financial Stability Board
- FSC** Financial Services Committee
- G20** Group of Twenty
- G-SIBS** Globally Systemically Important Banks
- IFRS** International Financial Reporting Standards
- IMA** Internal Model Approach
- IMF** International Monetary Fund
- IRB** Internal Ratings Based Approach
- IRC** Incremental Default and Migration Risk Charge
- ITS** Implementing Technical Standards
- ITSB** IT-Sounding Board of the European Banking Authority
- KRIs** Key Risk Indicators
- NSFR** Net Stable Funding Ratio
- SCFI** Standing Committee on Financial Innovation
- SDD** Simplified Due Diligence
- SREP** Supervisory Review and Evaluation Process
- Stressed VaR** Stressed Value at Risk
- UBO** Ultimate Beneficial Owners
- XBRL** Extensible Business Reporting Language



Statistics on disclosure requests

One request for information was received by CEBS Secretariat Ltd and the information was subsequently released by the EBA.

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