German Banking Industry Committee

Die Deutsche Kreditwirtschaft

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here: GBIC comments

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Enclosure

Comments of the German Banking Industry Committee

Dear Madam, Sir,

The German Banking Industry Committee (GBIC) very much appreciates the opportunity to comment on the above mentioned Consultation Paper.

Please find enclosed our response to this consultation.

We hope you will find these comments helpful and would be happy to discuss these with you.

Yours sincerely,
on behalf of the German Banking Industry Committee,
Association of German Banks

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German Banking Industry Committee

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Comments

EBA Consultation paper (EBA/CP/2016/06) "Draft Guidelines on LCR disclosure to complement the disclosure of liquidity risk management under Article 435 of Regulation (EU) No 575/2013"

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The German Banking Industry Committee is the joint committee operated by the central associations of the German banking industry. These associations are the Bundesverband der Deutschen Volksbanken und Raiffeisenbanken (BVR), for the cooperative banks, the Bundesverband deutscher Banken (BdB), for the private commercial banks, the Bundesverband Öffentlicher Banken Deutschlands (VÖB), for the public banks, the Deutscher Sparkassen- und Giroverband (DSGV), for the savings banks finance group, and the Verband deutscher Pfandbriefbanken (vdp), for the Pfandbrief banks. Collectively, they represent approximately 1,700 banks.

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Comments EBA Consultation **paper (EBA/CP/2016/06)**

General remarks

The consultation paper mentions, that the EBA has no specific mandate to elaborate Guidelines on the LCR or on liquidity risk in general terms. Nevertheless, the EBA takes the view that article 435 (1) (f) of the CRR is as a legal foundation sufficient for Guidelines to harmonise the specifications. We strongly disagree with this assessment and believe that EBA Guidelines are not the appropriate legislative level. In order to accomplish a solid legal basis, an amendment of the CRR would be necessary.
The annexes referred to should be checked again, as they correspond in part to the final EBA ITS rather than the version published in the EU Official Journal.

Question 1: Do respondents have any comment to the scope of application of the draft guidelines?

Based on Para 7 of the GL, Art. 6(1) and (3) and Art. 13 CRR we understand that the LCR Disclosure GL will apply only for credit institutions that are not part of a group (on solo level) and for EU parent institutions (on consolidated level). Significant institutions of EU parent institutions will not be subject to the LCR Disclosure GL, as according to Art. 13/1 CRR they are subject to Part 8 of CRR (disclosure) only to a limited extent, with liquidity risk being excluded. This should be clarified in the LCR Disclosure GL. Art 7 of the GL in combination with the explanatory text for consultation purposes (which makes repeated reference to the broad scope and level of application of the Delegated Act LCR) leaves some uncertainties in this respect. Credit institutions that have been waived or otherwise excluded from the LCR reporting requirement should also be excluded from the requirement to comply with the guidelines. Special requirements set by supervisors, such as the formation of a subgroup, should not be taken into account for disclosure, as information in this respect does not deliver any added value for market participants.

Most of the aspects regulated by the Guidelines are based on requirements of the Basel standards, which are not intended to be observed by smaller or internationally not active banks. The Guidelines do not properly respect the principle of proportionality of the CRR from our point of view. Therefore we suggest to limit the disclosure requirements for all banks to the disclosure of nominator, denominator and the ratio itself; this is not only for proportionality reasons, but rather for confidentiality and privacy reasons (see answer to question 8 and 14).

Question 2: As currently foreseen, the application date will be in June 2017. Do respondents find the date of application of the guidelines appropriate?

<u>First-time application (paragraph 10)</u>
The LCR disclosure requirements have to be applied two months after their publication in the EU Official Journal. Currently, the EBA is anticipating the application by June 2017 at the earliest. However, the consultation on LCR disclosure runs until August 2016. As further editing of the LCR disclosure requirements is likely once the consultation period ends, we believe that an application by June 2017 is too ambitious. First-time application of the LCR disclosure requirements by 1 January 2018 would be more appropriate in our view. This is especially important for institutes which are not directly supervised by the ECB.

We are seriously concerned about the effort that has to be done to implement the proposed calculation of the LCR as a daily average amount. This implies that all other related values have to be calculated on a daily basis, too. As mentioned below in further detail, for institutes such calculations are very burdensome.

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Question 3: Do respondents consider that the transitional period is sufficiently clear?

We understand the transitional period to be the period following final publication of the guidelines in the EU Official Journal, as only then will it be clear to institutions what they will actually have to disclose, on what scale, and how frequently. Only once the guidelines have been published in the Official Journal their implementation is feasible, since the EBA's final draft may differ from the European Commission's version (as the additional liquidity monitoring metrics already showed). In addition, we are of the opinion that a retroactive disclosure of values belonging to the transitional period is out of scope. In case supervisors should regard retroactive reporting as essentially, institutions should be allowed to disclose averaged values of the monthly reported LCR.

Question 4: Do respondents have any comment relative to the proposed LCR related items prone to rapid change?
No.

Question 5: Do respondents have any comment relative to the content of the table in Annex I of the draft guidelines and the way to display it?

We understand this to be a requirement with respect to the content of information called for by Article 435 (1) of the CRR. The consultation paper does not stipulate any specific form in which such information is to be provided nor is it given in a 'combined text'. This information may be included in the institution's financial statement or risk report. In this context, we believe that reference to other documents in the table is sufficient.

The table in Annex I requires institutions to disclose key ratios and figures other than those already captured. If these figures are based on the internal model of each bank, the information given will not be comparable across different banks, as the figures are highly dependent on internal model approaches. Due to the lack of comparability in determination of these items, their disclosure should, in our view, be voluntary. In addition, the request of including additional ratios (besides LCR, NSFR) as stated in the paper should be applied in a proportionate manner.

Concerning the qualitative disclosure information we recommend that they will be a subset of the proposed internal liquidity adequacy assessment process (ILAAP) documentation items. Pillar 3 should not require additional information items. A close integration of pillar 2 and 3 enhances consistency and reduces the additional operational efforts in our institutions.

Question 6: Do respondents have any comment on the content of the LCR disclosure template in Annex II?

The LCR is a very volatile ratio compared to other prudential liquidity ratios (such as the German LiqV), as it is designed to ensure that financial institutions have the necessary assets at their disposal to face a severe short-term liquidity disruptions over a 30-day period. This volatility results essentially from the variation in some of its components due to their very nature, which, if misunderstood by stakeholders, may have a detrimental impact on the real liquidity situation of an institution.

With this in mind, we question whether the level of granularity proposed would be more significant or meaningful to investors than simplified disclosure based only on the ratio itself at a group consolidated

level, the numerator and the denominator. In this regard, we note that for supervisory purposes banks must comply with a ratio and not with any sub-ratios, values or variation limits of the LCR components.

In our opinion, if such detailed granularity is maintained, it may not only lead to information overload for investors but would also harbour potential for disruption at banks driven by a "self-fulfilling prophecy" situation.

Furthermore, the additions to the EU-specific information in the LCR disclosure template may lead to serious misinterpretation at international level. These items are unknown internationally. It must be assumed that countries lack the required background knowledge to understand what these items mean. What is more, these items are usually of no great significance for the resulting ratio. This EU-specific information should therefore be omitted.

To avoid any misunderstandings, the designation for row 19 in the proposed reporting template should be altered to read "*Other cash inflows (fully performing)*". The current wording could create the impression that liquidity inflows from non-performing exposures have to be entered here. Alternatively, the designation for row 18 could be modified accordingly.

Furthermore, the requirement to report average daily figures is not operationally feasible. This applies especially to smaller institutions that have access to fewer resources within their reporting units than larger institutions. In most banks, the reported LCR is based on balance-sheet data that is partly only available on a monthly basis.

The table requires daily averages, which obviously only works if processes allow calculation of all required line items in that frequency. An alternative could be merely reporting the monthly figures and adding a statement confirming that, based on approximated daily figures derived from a liquidity management system, the reporting institution never violated the minimum regulatory LCR requirement (or if it did, on how many days within the reporting period). See also reply to question 11.

Question 7: Do respondents have any comment relative to the content of the template on qualitative information on LCR?

In this context, internal models are more meaningful than the LCR. An example is foreign exchange LCR disclosure, which has no clear-cut benchmarks.

We understand this to be a requirement with respect to the content of information called for by Article 435 (1) of the CRR. The consultation paper does not stipulate any specific form in which such information is to be provided nor is it given in a 'combined text'. This information may be included in the institution's financial statement or risk report.

Paragraph 18, row 1: "*Concentration of funding and liquidity sources*"
No direct connection with the LCR is recognisable here, as considering only funding sources that will be due in the next 30 days does not appear appropriate. This information is connected more with the additional liquidity monitoring metrics (ALMMs). What is more, this item is implicitly included in the qualitative information in the table in paragraph 16. For this reason, we believe that this item should be dropped here.

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Mandatory qualitative explanation (paragraph 18)
We see a benefit in institutions explaining the LCR they disclose in more detail where required. This may also be in their own interest, e.g. to explain an unusual business situation or if the current LCR differs significantly from that in the preceding period. In such cases, a qualitative explanation makes sense in our view. However, we see no benefit in a mandatory qualitative explanation if the institution itself sees no need for one. We should, in addition, like to point out that the Basel Committee on Banking Supervision also allows institution-specific interpretation and application of the requirements. The Basel Committee's disclosure requirements provided for disclosure in accordance with paragraph 15 only *"(...) where significant for the LCR (...)"*. This ought to have allowed institutions sufficient discretion in accordance with Article 432 (1) of the CRR.

We take an extremely critical view of items 1 – 4 of the qualitative disclosure requirements. The LCR disclosed is intended to give other market participants an idea of an institution's liquidity situation. The information proposed here could, however, allow a much deeper insight into an institution's business strategy.

It is, moreover, unclear what information supervisors specifically expect, as detailed descriptions or examples of the qualitative information to be provided are missing in Annex III – particularly as, according to the guidelines, quantitative explanations or results are not called for in this part of the report.

As regards the qualitative information in Annex I and Annex II, we do not believe that the guidelines on LCR disclosure are the right place to address these requirements, also because they are already mentioned in Article 435 (1) of the CRR.

Paragraph 18, row 3: "*Currency mismatch in the LCR*"
We take a critical view of the designation "*Currency mismatch in the LCR*". Since, given the large number of currency pairs, actual presentation of currency mismatches is too complex, this item should be renamed "*Liquidity position in significant currencies*".

Paragraph 18, row 4: "*A description of the degree of centralisation of liquidity management and interaction between the group's units*"
This item is already a mandatory part of the information called for in row 2 of the table in paragraph 16. To avoid any duplication and keep disclosure as consistent and concise as possible, this item should be deleted from paragraph 18.

Paragraph 18, row 5: "*Other inflows and outflows in the LCR calculation that are not captured in the LCR common template but which the institution considers to be relevant for its liquidity profile*"
This row is inappropriate. In accordance with Commission Delegated Regulation (EU) No 2015/61 of 10 October 2014, in conjunction with Regulation (EU) No 575/2013 of the European Parliament and of the Council of 26 June 2013, the LCR is designed to ensure a comprehensive picture of an institution's liquidity situation within the next 30 days under assumed stress conditions. Consequently, all the facts of significance for this picture have to be taken into account in the LCR. There cannot therefore be any other significant inflows/outflows that are not taken into account. For this reason, the item should be deleted from paragraph 18.

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Question 8: What information from Annex II, if any, would respondents consider irrelevant for LCR disclosure purposes?

All EU-specific information in the LCR disclosure template (see question 6) is irrelevant in our view.

Relationship between materiality, business secrecy and Article 432 of the CRR (paragraph 18)
We take an extremely critical view of items 1 – 4 of the qualitative disclosure requirements. The LCR disclosed is intended to give other market participants an idea of an institution's liquidity situation. The information proposed here could, however, allow a much deeper insight into an institution's business strategy.

We generally question whether public disclosure of such information is consistent with the confidentiality and privacy of a bank's business operations. Granular information on items may be misused in the marketplace to attack a bank's business model for improper reasons. We instead take the view that compliance with well-known and understood regulatory ratios reviewed and regularly audited by an authorized supervisory body should enable a third party to rely on an institution having a sustainable liquidity and funding position. This was a primary objective of aiming for standardized and harmonized liquidity ratios in Pillar I. Disclosure of the three main components – HQLA, outflows and capped inflows – plus the LCR ratio, should therefore provide sufficient information balancing the interests of all parties involved.

Regarding the qualitative information in Annex I and Annex II, we do not believe that the guidelines on LCR disclosure are the right place to address these requirements, also because they are already mentioned in Article 435 (1) of the CRR.

We should, in addition, like to point out that alignment of disclosure with new reporting standards (correction of the LCR is already planned) also requires a transitional period and should not be allowed to call for retroactive correction of values; such alignment should only be allowed to apply to future time periods. In addition, it would – as explained above – make sense to gear disclosure solely to HQLA, outflows as well as capped inflows and the reported LCR ratio.

Question 9: What information would respondents like to see added to the LCR disclosure requirements?

We do not believe that there is any additional information that needs to be publicly disclosed. Optionally, banks could be allowed to also disclose their current LCR rather than only historical values. Investors may be interested also in the most recent ratio reflecting the liquidity and funding status of the bank. For the bank itself, it may be helpful, where it has recovered from low ratios reported in recent quarters, to demonstrate to the market that its liquidity and funding status has improved.

Question 10: Do respondents find the general instructions in Annex III sufficiently clear for the development of the disclosure template?
Yes.

Question 11: In accordance with Article 4 of Commission Delegated Regulation (EU) 2015/61, the LCR needs to be met at any time whereas Article 15(1) of Commission Implementing Regulation (EU) No 680/2014 requires a monthly frequency of LCR reporting. The suggested approach for the LCR disclosure template is based on averaged values over daily observations

based on the reporting templates. Particularly considering that the most recent data needed would be from the quarter prior to the disclosure date, do respondents consider that this approach is, from a practical point of view, operationally feasible meaning that the accuracy of the daily reporting observations for the calculation of the averages can be ensured? Do respondents consider that this operational feasibility could depend on the size of the credit institution or could be different in the case of solo or consolidated data?

Calculation of the LCR ratio on a daily basis for disclosure purposes would, firstly, impose a disproportionately heavy burden on institutions' reporting unit resources. Secondly, the gain in information is limited, in our view, if an institution has, for example, internal controls that ensure that the LCR does not drop below a certain internal minimum ratio. Application of an above-mentioned simplified approach that may be used on a monthly basis for disclosure purposes can, in our view, ensure an optimal balance between the burden on reporting institutions and added value for interested, external third parties. This would be a pragmatic solution particularly for smaller institutions that automatically have less reporting unit resources.

Calculation of the LCR ratio on a daily basis is not feasible from a **practical point of view**. It will not only substantially increase the amount of work performed by institutions but also dramatically increase the costs resulting from the need for IT upgrades and better information storage capabilities. In most banks, the reported LCR is based on balance-sheet data that is partly only available on a monthly basis.

The bigger a group is, the more complex operational feasibility is. Particularly calculation of the daily LCR on a consolidated basis is extremely time-consuming, as the LCR has to be calculated in subsidiaries and then consolidated in the parent institution. It cannot therefore be assumed that institutions have already implemented such a process and that calculation of the LCR on a daily basis does not impose any additional workload as the ratio is already available.

For larger institutions which base their regulatory reporting framework on financial data warehouses to ensure consistency with audited balance sheet figures, calculation of the LCR on a daily basis for steering purposes may be based on processes which are better suited to day-to-day management. Such figures may deviate to some extent but serve in principle as a good approximation where the LCR materializes on a daily basis. Such approximations should be allowed, given that the supervisors have sufficient confidence in the process designed to ensure the similarity of both calculations.

See also reply to question 6.

From a **conceptual point of view,** we cannot agree that a higher calculation frequency than that called for by supervisors (monthly, according to Commission Implementing Regulation (EU) No 680/2014) is required for public disclosure purposes.

Additionally, all prudential ratios (capital, liquidity, leverage) are met at any time by institutions. This does not mean that, for public disclosure purposes, they should have to be calculated on a daily basis

Calculation approach (paragraph 19 in conjunction with the disclosure template in Annex II)
In the event that an institution falls below the current minimum LCR, the requirements of the LCR Delegated Regulation and the CRR stipulate that it must be able to calculate an LCR and report it to the competent supervisory authority on a daily basis (cf. Article 4, sentence 3 of the LCR Delegated Regulation in conjunction with Article 414, sentences 1 and 2 of the CRR). The current Basel liquidity

framework BCBS 238 (cf. paragraph 162) also requires banks to hold capacities allowing them to calculate the LCR on a daily basis in stress situations. This basic daily reporting requirement is being implemented in systems, and capacities and processes are being held to deal with stress situations.

The requirement in paragraph 19 of the consultation paper goes well beyond this requirement set for extreme situations. The guidelines provide for mandatory calculation of the LCR on a daily basis without any transitional period, as this is included in averaging of the disclosed LCR.

The consultation paper itself notes on page 19 that potentially different approaches to calculation of the LCR on a daily and monthly basis may lead to inconsistencies between an LCR computed on the basis of the disclosure template values and the disclosed LCR.

We share this view and are therefore strictly opposed to the approach proposed here for calculating an average LCR on a daily basis. The purpose of LCR disclosure it to create a better understanding of an institution's liquidity situation among other market participants by disclosing an average LCR. In our view, the general requirement for all institutions to compute quarterly LCR values on the basis of daily observed LCR data goes too far in this context. We believe that producing averages based on less data would also be feasible and in fact more appropriate. In view of the above-mentioned inconsistencies and potential deviations between the average LCR and the LCR to be reported (on a monthly basis) for prudential purposes, market participants might be unsure about how to assess these disclosed LCRs. Fluctuations in these LCRs could be primarily data-related and fail to reflect economic reality at institutions. To avoid this negative effect, institutions would be compelled to permanently tie up considerable resources also outside liquidity stress situations in order to maintain the high quality standards for both calculation of the LCR and for actual disclosure.

We propose a different approach to LCR disclosure: calculation of an average LCR via the LCR actually already established for prudential purposes covering the period prior to the respective reporting date.

Example: reporting date 30 June
LCR (April, May, June) / 3 = ø LCR disclosed in reporting on 30 June.

Question 12: Do respondents find the specific instructions in Annex III sufficiently clear for the development of the LCR disclosure template and the template on qualitative information on LCR in Annex II?
Yes

Question 13: In the elaboration of this CP, the EBA has considered several policy options under three main areas: a proportionality approach in the scope of application, items for a higher disclosure frequency and methodology for the calculation of the disclosures. Do respondents have any particular view on the assessment conducted on these policy options?

a. General assessment
No options are presented in connection with the cost-benefit analysis. Without any closer analysis of the estimated burden on institutions, the consultation paper assumes that there will be no significant additional workload. At the same time, on the cost side, the consultation paper explicitly lists which data collection, data processing, control system and monitoring costs institutions would face. The argument that the benefits of the guidelines outweigh these costs is therefore puzzling; in particular, it is not clear how risk appetite is supposed to be reduced in this way. Additional costs actually increase the pressure on

institutions to earn income. Particularly in the current market environment, the search for earnings is accompanied by a higher risk appetite.

Besides implementation of processes for computing the LCR on a daily basis across an entire group, formal aspects also need to be taken into account which, for compliance reasons, mean the introduction of additional key controls and documentation measures for institutions. What is more, the complex disclosure will impose an additional auditing burden both internally and externally.

b. Assessment of the policy options
As regards proportionality, we are in principle in favour of adopting option 1A. A simplified approach to LCR disclosure for smaller institutions ensures that these institutions can deliver key information quickly and in good quality. The information that would have to be disclosed through a simplified disclosure template and a non-simplified disclosure template would, in our view, generally be mutually comparable for interested, external third parties. The key information would be identical.

As regards frequency, we prefer option 2B for disclosure more frequently than annually, as it ensures better harmonisation and comparability. In addition, it is then easier for institutions to prepare the figures for annual disclosure, since the templates for more frequent disclosure can be aggregated. Special templates would not therefore make things easier for institutions.

There is an area of conflict as far as the calculation methodology is concerned. In our view, accuracy is increased by fewer data items, as the quality of these is higher thanks to longer validation. Daily values would, on the other hand, tend to be inaccurate. We regard the argument in option 3B that calculation of averages based on daily values would be highly data-intensive and burdensome as both very serious and correct. Generally speaking, the feasibility of option 3A is questionable and the averages produced would not match the quality of reported values.

We are therefore in favour of option 3B, as we believe that less frequent data observations allow more reliable and accurate calculation of averages and that, given the considerable implementation burden, weekly values, for example, would be an acceptable solution for institutions.

Furthermore, the cost of implementing option 3A is in no proportion to any potential gain in information that could be obtained through calculation of the LCR on a daily basis rather than its calculation on the basis of averages on the reporting dates. This argument would be particularly true if supervisors were to decide not to introduce any simplified reporting template for smaller institutions.

We refer once again in this context to our reply to question 8.

Question 14: The provisions of Regulation (EU) 575/2013, including the disclosure requirements in its Part Eight, respect the principle of proportionality having regard, in particular, to the diversity in size and scale of operations and to the range of activities of institutions. A less complex, low risk institution will have to disclose less than a more complex, higher risk institution. In addition, specific waivers for disclosure exist in case of non-materiality of information, and the EBA has issued Guidelines to specify the cases where such waivers are used. The EBA intends to conduct further work on the application of the principle of proportionality to regulatory requirements, including the disclosure requirements. As a result, should a specific approach be needed as regards the implementation of the Guidelines on liquidity disclosures in a proportionate manner, this approach will be consistent with the

EBA general approach as regards proportionality. In the meantime, users are invited to express their views on the following questions, whose answers will inform the future work of the EBA. Any potential solution suggested by respondents will have its feasibility assessed considering the applicable disclosure framework.

Do respondents think that the opportunity of having a simplified disclosure template for smaller credit institutions should be assessed? This simplified LCR disclosure template could comprise for example the ratio itself, the numerator and the denominator as key ratios and figures of the LCR, in the sense of Article 435 (1) (f) CRR. What arguments could respondents provide to justify that the LCR ratio itself, its numerator and its denominator are the only key ratios and figures of the LCR which are required to be disclosed by smaller credit institutions?

More generally please provide any argument in favour or against a simplified template, and if you believe a simplified template for LCR disclosures is relevant, please indicate which type of information you would like to have disclosed in that template.

What specific criteria would respondents suggest to identify those smaller institutions for which a simplified disclosure template could potentially be disclosed?

We believe it is important to ensure comparability in the marketplace. The information that would have to be disclosed through a simplified disclosure template and a non-simplified disclosure template would, in our view, generally be mutually comparable for interested, external third parties. The key information (numerator, denominator, ratio) would be identical.

At the same time, however, the templates for solo and group level should be uniform, as this makes it easier for groups to consolidate their individual subsidiaries and complete the group templates.

In line with our reply to question 8, we regard the disclosure of nominator, denominator and the ratio itself as appropriate for ALL banks; this is not only for proportionality reasons, but for confidentiality and privacy reasons.

At least for proportionality reasons, a disclosure of key information – as mentioned above – is sufficient for smaller and not internationally active banks from our point of view.