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EBF RESPONSE TO EBA CONSULTATION PAPER ON THE IMPLEMENTING TECHNICAL STANDARDS ON SUPERVISORY REPORTING CONCERNING OPERATIONAL RISK

The European Banking Federation (EBF) welcomes the opportunity to put forward our comments on the EBA Consultation Paper. The EBF response to the consultation represents the consolidated view from all EBF members i.e., 33 national banking associations from across Europe representing in total about 3,500 banks.

While we appreciate these technical standards as a first overview of the Pillar 3 templates required from 2025, we see general critical aspects mainly related to:

- The short time range between the availability of final instructions (in 2nd half of 2024) and the first official notification (referred to 31st March 2025). According to this short timeline, banks are forced to start IT projects and implementation according to the instructions reported in this Consultation Paper.

- The timeline for reporting under the new framework.

  - The consultation paper does not specify the initial dates for reporting under the new framework:

    The methodology of the new Business Indicator approach and the corresponding reporting template C16.02 require the computation of the business indicator and the preparation of the detailed reporting template C16.02 for each of the last three financial year-ends. This implies in our understanding that for the first reporting deadline of March 31, 2025, data for the year-ends of 2024, 2023, and 2022 must be recalculated. To this end, please clarify whether the March, June and September reports are based on the Y-1, Y-2 and Y-3 reference year-end dates and whether the only changes expected for these reports are related to scope adjustments in the event of disposals/acquisitions during year Y. Further, please note that even if FINREP reports exist for these dates, the level of detail needed for form C16.02 is not available. Any discrepancies from current FINREP reporting, as most certainly in the case of mergers and acquisitions adjustments, the retroactive data gathering will be exceedingly challenging.

  - The reference dates used for reporting quarterly BI calculation on template C 16.02:

    Respondents raise difficulties and inconsistencies in the proposed framework for the reporting of the full set of information on the Business Indicator as of 31/12/N at the Q4 remittance date. The draft RTS on the adjustments to the Business Indicator requires to calculate and to report information based on audited financial figures. However, it will be not feasible to use the 31/12/N data, as these audited financial figures are not available when producing and publishing the Q4 COREP.

- The provisions in Annex II, Chapter 4.1.3, regarding handling unavailable historical data, appear to be only partially applicable for transitioning to the new methodology. We believe it is critical to implement facilitations during the initial two-year phase-in period following the implementation of CRR III, specifically:

  - A waiver of retroactive adjustments of the FINREP figures for YE 2023 and YE 2022 with regard to M&A transactions should be granted. It should be possible to refrain from collecting and preparing data for M&A transactions which took place in the longer past.

  - As outlined in Annex II, Chapter 4.1.3, Text 149, when specific breakdowns cannot be derived from FINREP reports, they may be approximated on a best-effort basis. For instance, breakdowns within the trading or banking book can be estimated if not available.

- Additional general comments on track changes Final draft ITS.

  - We noticed that when final versions of ITSs are published on the EBA's website the track changes versions of the templates (Excel) and instructions (Word) provided are the ones between the former ITSs and the amended ITSs. No track changes versions of templates / instructions are provided between draft ITSs consultation and final draft ITSs. In this sense, to ease the comparison between the consultation versions and the final amended versions, we find important that the EBA continues providing:

    - the track changes versions of templates/disclosures between the current ITSs in application and the amended ITSs to be applied (as is currently the case) and
    - the track changes versions of templates and instructions between draft ITSs submit to consultation and final draft ITSs.

RESPONSES TO QUESTIONS LISTED IN THE CONSULTATION PAPER

Question 1: Are the instructions and templates clear to the respondents?

- TEMPLATE C16.02

  We noted a mismatch between the required items and the ones reported in the ITS on the business indicator. Another mapping would be needed to fill in the template C16.02.

  With specific reference to lines 0350 and 0380 of Template C16.02, the ITS on the mapping to supervisory reporting under Article 314(7) of the CRR include in the calculation of the BI items related to F.22, not declined in the C16.02 (see annex 1) which include F.02 items. Please clarify whether the composition/content is the same and harmonize referring only to F.02.

  By comparing the list of items as for Draft RTS "on the components of the BI under Art. 314(6) of the CRR", Art. 7 with the list of items as for Draft ITS "on the mapping of the BI components with corresponding supervisory reporting under Art. 314(7) of the CRR" we noticed that RTS list does not include the item "fee and commission income from loan commitments given" (which is included in the ITS list, mapped with F22.01r0200_c0010 FINREP item). Please clarify whether this item should also be included within the RTS list.

- TEMPLATE C16.03

  In our view the one potential source is the operational risk losses database, but there is a need for considerable effort to precisely link losses to the individual single lines of the template.

  It is difficult to understand the purpose of this new COREP map, since it establishes the reporting of a detail of accounting costs that seems irrelevant:

  a) Certainly, for the OR capital requirements (since the ILM will be =1 and, even if it wasn't, only the total amount of losses would be relevant), and
  b) In our view, for the characterization of the nature and breakdown of losses (already provided, to a greater/better extent, by the basically unchanged maps C17.01 and C17.02).

  Also, since data for 2024, 2023 and 2022 is required (in retrospect), it is possible for many institutions to encounter great difficulty in providing the break down at stake, even if, for example, the nature of the amounts to fill in this template was purely of "Operational losses" (and not "Accounting amounts").

  Given these reasons, we suggest this template to be non-mandatory or required on a 'best effort' basis, at least until the calculation at 31/12/2027.

- ARTICLE 314.7b final text of CRR3 reports:

  "*For the purposes of point (d), the losses, expenses, provisions, and other financial impacts due to operational risk events shall not be net of any related payments received from insurance or reinsurance policies purchased*".

Please confirm that it's possible to carry out the netting of the rest of the payments, that is, payments that are different from the ones received from insurance or reinsurance policies purchased.

- OTHER OPERATING INCOME

  With reference to the calculation of the Other Operating Income, both Article 5 of the RTS and in the ITS included annex, do not explicitly exclude from the calculation of the Business Indicator recoveries of expenses on behalf of customers (stamp duty, substitute tax and other recoveries), although Article 314 para. 5 let. d) provides for such exclusion. We urge to see article 5 of ITS amended, because in certain jurisdictions exclusion has a material effect on BIC.

  In case the institution does not opt for any derogation stated in Art. 314 paragraphs 2a nor 2b of the CRR3, please clarify whether it is necessary to fill in the template C16.04.

- TEMPLATES C17.01 and C17.02

  Regarding the templates C17.01 and C17.02, what does this minor amendment "Reporting as a group -> Losses caused by a common operational risk event or by multiple events linked to an initial operational risk event generating events or losses. With CRR3 this has changed -> losses will no longer be grouped but reported following the impact in accounting." mean? Some examples would be appreciated.

- RTS ON BI ITEMS

  Aligning Business Indicator Calculations with FINREP Templates as per the RTS on BI Items (pp. 33-38)

  Please enhance the clarity of the linkage between business indicator calculation elements and corresponding entries in the FINREP templates. The goal should be to avoid uncertainties, thus fostering a higher degree of consistency and harmonization across financial institutions.

  - There is a need to check for double counting. The row "profits from leased assets, including gains from lease modifications" and "losses form leased assets including losses from lease modifications" are mapped to:

    (i) F02.00_r0425_c0010 (only from leased assets) and
    (ii) F45.3_r0040_c00010/c0020 (only from leased assets).

    Regarding F02.00_r0425_c0010, we noted this cell is linked to "Modification gains and losses, net". According to Annex V Reporting on Financial Information "*it shall include the amounts arising from adjusting the gross carrying amounts of financial assets to reflect the renegotiated or modified contractual cash flows*". In our view this concept does not refer to leased assets and in consequence it should not be considered in the mapping tool.

    Regarding F45.3_r0040_c0010/ c0020, these cells should be linked to F45.3_r0030_c0010/ c0020 "operating leases other than investment property"

instead of the cells F45.3_r0040_c0010/c0020 "Other", considering it is asked to include only from leased assets.

  - In rows related to interest bearing assets, the standard gives reference to gross carrying amounts in F18. As it is very well known, the gross carrying amounts include principal amounts that bear the interest and accrued interest which is the interest itself generated by the principal amount. Considering the idea of the regulation that in essence wants to cap the amount of net interest income with the 2.25% of the interest bearing assets in order to avoid unwarranted operational risk amounts derived from high-interest-margin countries, we believe that the entities when deriving the amounts from their F18 reports should isolate the amount of interest accruals included inside the gross carrying amounts in order to avoid double counting. This exact same concern applies to debt securities as well.

  - Additionally, interest bearing assets include all the balances with central banks without differentiating whether these balances kept at central banks generate any interest for the depositing institution or not. It should be noted that there are balances left at central banks both for regulatory reserve maintenance purposes and others for operational purposes to carry out payments of their clients. These balances in some cases depending on the decision of the central bank in question may or may not create interest for the institution subject to the decision of this central bank. In cases where these balances do not create any interest for the entity, there is no difference for this entity between the balance kept cash immediately available to the institution and these balances. Therefore, we propose that in cases where the balances kept at central banks as well as demand deposits kept at credit institutions do not generate any interest for the depositing institution, these should be kept out of scope of calculation of interest-bearing assets.

  - The row "expenses from other expenses", is linked to "other operating expenses" (F45.3). Conceptually the hyperinflation, which in our case means a significant contribution, is recorded under this heading according to the applicable regulations. On the other hand, the standard giving reference to these lines does not give any further clarification applying to institutions that apply hyperinflation accounting. Therefore, the questions arise on whether or not to consider the part of this item attributable to hyperinflation accounting adjustments in the calculation of BIC.

  - We kindly ask you to clarify the item "provisions or (-) reversals provisions" due to operational risk. Please clarify what type of items are expected to be included under this line.

- Asset component (Article 3 of the RTS on BI items) (p. 34)

  - The described "total assets" comprise gross carrying amount positions and carrying amount positions. However, total assets are defined as carrying amount. In order to deliver reliable data, all required positions which relate to template F18.00 should include column 0130 "accumulated impairment".

- The position asset component “a) Cash balances at central banks and other demand deposits” does not contain “cash on hands” (ref. F01.01. Cash, cash balances at central banks and other demand deposits).

Question 2: Do the respondents identify any discrepancies between these templates and instructions and the calculation of the requirements set out in the underlying regulation?

TEMPLATE 16.02

- Use of Fixing Exchange rate
    - The calculations of operational risk requirements are based on the average of the values of the last three financial years. Taking also into account that operational risk losses will materialise in the currency in which the company operates, we consider that the exchange rates to be applied in the case of subsidiaries with a currency other than the € for the purposes of calculating own funds requirements for operational risk should be the exchange rate at each reporting date. Otherwise, should FINREP exchange rates were used, capital requirements should be:
        - Outdated: Up to a 3-year gap since historic FX rates would be used.
        - Inconsistent with credit & market risk frameworks, which are calculated with up-to-date FX rates.
- Use of clean price approach and TB/BB reclassification.

  Regarding the determination of the ILDC component and the Financial Component, it appears that institutions using the so called “clean price” to produce the FINREP reporting might be penalized compared to institutions using the “dirty price” approach. As a reminder the clean and dirty price approaches are detailed in Instructions for FINREP reporting (Annex 5) as detailed bellow:

  “*Interest income and interest expense from financial instruments measured at fair value through profit or loss and from hedging derivatives classified in the category ‘hedge accounting’ shall be reported either separately from other gains and losses under items interest income’ and ‘interest expense’ (‘clean price’) or as part of gains or losses from these categories of instruments (‘dirty price’) (...)*

  ‘Interest income. Financial assets held for trading’ and ‘Interest expenses. Financial liabilities held for trading’ shall include, where the clean price is used, the amounts related to those derivatives classified in the category ‘held for trading’ which are hedging instruments from an economic but not accounting point of view to present correct interest income and expenses from the financial instruments that are hedged (...)

  Dividend income on equity instruments measured at fair value through profit or loss shall be reported either as ‘dividend income’ separately from other gains and losses from those classes of instruments where the clean price is used, or as part of gains or losses from those classes of instruments where the dirty price is used”.

  Institutions using the clean price approach reclassify interest income & expenses and dividend incomes from gains and losses from instruments held for trading or instruments designated at fair value through profit or loss to interest incomes & expenses and dividend income within F02.00. This does not constitute an accounting choice or method. These reclassifications are made for FINREP reporting purpose only.

However, in a situation where the P&L of the trading book of an institution would be negative, this reclassification would result to: i) deepen the loss of the P&L of the banking book and ii) increase the amounts of dividend incomes (as for example dividend revenues stemming from equity instruments measured at FV would be reclassified in dividend income).

That will mean that an institution using clean price approach for FINREP would be penalized compared to an institution using the dirty price approach as, considering the same P&L profile, in case of negative P&L of the trading book, one institution using clean price would see its FC (based on absolute value) increased by the amounts related to dividend revenues or net interest and its ILDC increased by the same amount, where another one using dirty price would not suffer from this effect.

We consider that institutions using clean price approach should not be penalized by the application of the clean or dirty price approach and ask EBA to allow institutions to neutralize the negative impact of the reclassification made for FINREP purposes (with the same reclassification mechanism that the one used for AA to PBA approach but allowing reclassification of dividend revenue and interest incomes/expenses from ILDC to FC).

- Use of the Prudential Boundary Approach (PBA).

  According to Article 314.4 of the CRR, the trading book component (TC) of the financial component (FC) should be "defined as appropriate either in accordance with accounting standards or, in accordance with Part three, Title I, Chapter 3" (i.e., the prudential boundary criteria). This requirement is also explicit in the mandate of Article 314.6 which requires that EBA develops the list of typical sub-items of the business indicator by "taking into account international regulatory standards and, where appropriate, the prudential boundary defined in Part three, Title I, Chapter 3".

  The draft RTS on the new framework for the business indicator for operational risk, also under consultation, does indeed provide the two required approaches to calculate the financial component in the proposed accounting approach (AA) and prudential boundary approach (PBA). There are, however, several issues with the requirements envisaged by EBA.

  First and foremost, the AA has been made the default approach while the PBA can only be used by way of derogation after meeting some conditions. This requirement goes beyond that of the CRR which does not favour one approach over another but, rather, requires that the PBA be available where and as appropriate. An institution should therefore be able to choose the PBA on a permanent basis if it considers such approach as appropriate. It should be noted that the CRR already imposes very strict requirements for the management of the trading book including for the inclusion of positions (Articles 102, 103 and 104), and equally strict rules to reclassify a trading book position (Article 104a) which contributes to the robustness of the PBA approach. However, to avoid continuous changes from one approach to another, it appears reasonable that when an institution has made the decision to apply the PBA, it would only be permitted to revert to the AA (and the other way round) if such change if triggered by material evolutions of its activity, environment or risk management (for example a change of business

model) and after approval from the competent authority. This would provide the consistency required for having a sound framework for the PBA and would ensure that no regulatory arbitrage is possible which, as previously mentioned, is already prevented by trading book framework of the CRR.

Second, in the approach proposed in the RTS on the new framework for the business indicator for operational risk the application of the PBA is conditional on several criteria including the presence of certain operations or accounting choices that result in an "unwarranted increase" of the FC when using the AA. Once again, this would limit the usage of PBA while CRR does not favour one approach over another nor intent to limit the usage of PBA. Furthermore, an unwarranted increase in the TC's P&L can be volatile by definition as it can be impacted by several market factors. An institution can therefore experience an unwarranted increase in a given reporting period and not experience any in a following reporting period while having similar operations and accounting choices. The application of the PBA should, therefore, not be based on an unwarranted P&L increase in the TC nor be subject to any limitation.

Finally, the notification process seems very cumbersome, especially as all the requirements (points (a) to (h) of Article 13.2) should be reviewed annually. All these requirements should only be required for the initial notification of the intention to use the PBA and the annual review should be limited to the independent review on the fulfilment of the conditions to use the PBA (point (h) of Article 13.2).

- TEMPLATE C16.03

  We have found discrepancies concerning the specific lines listed below:

  - row 0010. The row refers to "other expenses" in FINREP (F 45.3 r0040 c0020). However, it is unclear if the figures should be collected from FINREP as a whole (1:1) or if only the figures referring to the operational risk in FINREP should be collected?
  - row 0050. Please clarify where should the figures be collected from. It does not seem to be from FINREP.

Question 3: Do the respondents agree that the amended draft ITS fits the purpose of the underlying regulation?

No comment.

Question 4 - Cost of compliance with the reporting requirements: Is or are there any element(s) of this proposal for new and amended reporting requirements that you expect to trigger a particularly high, or in your view disproportionate, effort or cost of compliance? If yes, please:

▪ specify which element(s) of the proposal trigger(s) that particularly high cost of compliance,

▪ explain the nature/source of the cost (i.e. explain what makes it costly to comply with this particular element of the proposal) and specify whether the cost arises as part of the implementation, or as part of the on-going compliance with the reporting requirements,

▪ offer suggestions on alternative ways to achieve the same/a similar result with lower cost of compliance for you.

The fulfillment of the reporting and disclosure templates by March 31, 2025, is going to require institutions to make a very significant effort given the limited time they will have to prepare their IT systems and processes.

In addition, we would like to highlight the following elements as potentially problematic regarding the cost of compliance with the reporting requirements:

- Mergers & Acquisitions Adjustments in Supervisory Reporting

  The consultation draft regarding supervisory reporting on operational risks under Article 430(7) of CRR III, specifically addressing template C16.02, refers largely to FINREP. However, M&A activities necessitate retrospective adjustments to FINREP figures for periods before the integration of new entities. The RTS (EBA CP 2024/05) aims to revise CRR III and the ITS on supervisory reporting to clarify adjustment procedures, mandating the inclusion of newly acquired entities' data into FINREP reports based on their audited financials. This retrospective harmonization poses significant challenges, particularly when pre-existing business relations with acquired entities complicate the process. Despite these complexities, the influence of such adjustments on the business indicator is typically minimal, questioning the necessity of recalculating FINREP data for most M&A transactions. Against this background, we consider facilitations for M&A transactions with minor impact necessary.

  We advocate for exemptions on adjustments related to M&As transactions of minor significance. A reasonable measure of immateriality could be the M&A factor already introduced by the EBA. For example, up to an M&A factor of 1.1, M&A adjustments could be omitted.

  Another alternative, which would be a great relief for the institutions with only minor impact on the business indicator, would be the possibility to use the M&A factor method (according to Art. 1 (2) (b) of the RTS (draft) for adjustments to the business indicator (CP 2024/05)) up to an M&A factor of 1.1 in general (e.g., as first resp. standardized approach). Up to an M&A factor of 1.1, a notification according to Art. 1 para. 4 of the above - mentioned RTS should be omitted as well as the comparison of the three approaches acc. to Art. 1 par. 2 of the RTS.

- Simplifying Supervisory Reporting: Proposal to Streamline Template 16.02 and Eliminate Non-Essential Data Collection

  We suggest removing row 0310 from template 16.02 (OPR BIC), exclude the reference in the disclosure template and to exclude or make non-mandatory the template 16.03 (OPR BD) (consultation paper point 59 – we prefer option 1b: not to add a template with a breakdown of the total losses, expenses, provisions and other financial impacts).

  Our systems, specifically the General Ledger, cannot readily provide this granularity, and adapting to such requirements involves substantial financial and operational costs. These details, already encapsulated within "other operating expenses," are redundant for calculating the BIC and, hence, should be streamlined to avoid unnecessary data gathering.

- Exclusion Request for Specific Rows in Template 16.02 (OPR BIC)

  We recommend excluding rows 0420-0440 and 0470-0510 from template 16.02 (OPR BIC) since it is often not feasible to source this data directly from our General Ledger. Implementing the necessary system updates to capture this information entails significant expenditure without substantive benefits since this detailed information are

not relevant for calculating the BIC as they are part of the Trading and Banking book component. Streamlining these requirements would eliminate the need for exhaustive data collection without impacting the accuracy of the BIC.

- Information at subsidiary level in Template 16.04

  We question whether Template 16.04, information at subsidiary level, must be reported. It is common that subsidiaries do not report FINREP. If anything, the meaning of "subsidiaries" in this template should correspond to the sub-consolidated levels of Groups, namely, considering the 'geographical level' consolidation (by country). To have "single name" institutions in this map would lead to an extra workload with no clear advantages to the nature of this reporting item.

- Exclusion of Pillar III templates with data that cannot be recovered from COREP.

  We would suggest avoiding Pillar III templates with data that cannot be recovered from COREP. This requires creating an additional direct interface between OpRisk and Pillar III systems, whereas so far, the OpRisk systems fed just the COREP ones.

Question 5 - Do you agree that proposed instructions and templates reflected in this draft CP cover all the clarifications needed from existing Q&As on operational risk reporting and those Q&As should be archived (as explained in Section 3.3)? If not, please refer to the Q&A number when explaining.

Yes, apart from the points raised for question 1. We are not aware of Q&As on the new COREP.

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