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Santander's comments on Consultation paper on Draft Implementing Technical Standards on Disclosure for Own Funds

We welcome the EBA proposal on the definition of capital disclosure requirements, especially at a time when reducing uncertainty is crucial to recover market confidence. As a bank deeply committed with market transparency[1] we strongly support those initiatives that could contribute to ensure a similar level of transparency across institutions and comparability among them. This would reduce the cost of gathering and processing information for market participants, making easier the assessment of each institution's risk profile and thus allowing proper price discrimination among institutions. We are convinced that **market discipline is instrumental for ensuring the smooth and efficient functioning of the financial markets**.

However, for transparency to improve market discipline, **the definitions on which the information to be disclosed is built upon** should be previously harmonized. Disclosure of the capital ratios without previous consistency in these definitions or without a full disclosure of these differences could give a false sense of comparability that results misleading. Thus we encourage regulators to address pending issues such as consistency in the calculations of Risk Weighted Assets (RWA), accounting rules and other areas of national divergences and to promote equivalent disclosure regarding risk calculations and risk profile.

Thus, we welcome the on-going work, both at the BCBS and the EBA level, to ensure further consistency in the RWA calculations. However, until this consistency is achieved, we think that disclosure should cover the gap to guarantee meaningful comparisons. This could be done by promoting full disclosure of such differences in calculations or by requiring to also disclose the information under the basis of a "*common benchmark*".

In addition, the set of information to be disclosed **should be a subset of the information required by the supervisors** in order to reduce the burden and enhance comparability.

Moreover, the **definition of capital ratios at national level not fully aligned with Basel III**, should be avoided. It is a source of confusion among market participants and institutions that have to comply with different capital rules at the same time. For example, in Spain, we have now three different legal capital ratios we have to comply with: the "*capital principal*" defined in a Royal Decree at national level, the EBA "*core capital*" defined in the context of stress test and recapitalization exercises and the Basel II capital ratios, the two latter presenting large divergences in implementation across jurisdictions. We strongly support using a comparable capital ratio both internationally and across Europe.

[1] As an example of Santander's commitment with transparency in 2010 we enhance the disclosure of our real estate risk profile providing detailed breakdowns, and in 2011 we started to provide detailed information of our sovereign debt portfolio in our annual statements.

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Our major concern on the proposal is the **additional information to be reported during the transitional period**. We share the concerns of the BCBS regarding the challenges that the Basel III transitional arrangements and the different pace of implementation across jurisdictions pose from a proper disclosure point of view. However, the current proposal could imply a "*de facto*" anticipation of the Basel III final requirements, **making inoperative the transition arrangements**, with the consequent negative impact on the real economy. The BCBS estimates only a mild impact on real growth if implementation is progressive but anticipates much more dramatic effects otherwise, that's why transitional arrangements are introduced. Markets will automatically adjust capital ratios calculations by the full "*amounts subject to pre-Basel III treatment"* showed in the template, ignoring the effect of banks active management during the transition phase. The active management will result in a progressively lower impact of Basel III as banks adapt their policies and strategies in response to Basel III incentives (e.g. gradually reducing generation of deferred tax assets).

We firmly believe that an homogeneous implementation schedule across jurisdictions through the full application of the Basel III phase-in arrangements would ensure comparability while minimizing the unintended consequences in the real economy of Basel III implementation.

However, as this is likely not to be the case, we think that a better solution to ensure comparability would be to **show in an additional column not the amounts "*subject to pre-Basel III treatment"*, but the amounts that in each jurisdiction are subject to Basel III treatment above the minimum established at each time by the phase in arrangement**. That is, if a jurisdiction has decided to deduct the full amount of a specific balance sheet item since the first year instead of the 20% minimum, then in the additional column the banks in this jurisdiction should disclose the 80% subject to the stricter requirements (See Annex 1). In this way the benchmark for comparison would be not **CRR/Basel III 2018 capital requirements, but the minimum requirements according with the phase-in arrangements.** This approach would be more useful for comparability and more coherent with the spirit of the phase-in rationale.

This solution is more consistent both with the aim of comparability during the phase-in period and with the aim of reducing the unintended consequences of the implementation of Basel III.

With respect to the **reconciliation template** we think that especially for larger, complex banking groups the output of this particular exercise may more likely confuse users than enlighten them. This is because the resulting template would itself be complex, with a large number of 'many-to-many' linkages between the accounting and regulatory balance sheets, including a lack of one-to-one correlation in many instances. This complexity is mainly due by the algorithms established by the Basel text for some calculations. We can take as an example the reconciliation exercise for shares in the trading book and in the available for sale category of the same instrument issued by a financial institution on which the group has participation above 10%. The reconciliation between the amounts showed in the balance

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sheet with the amount to be deducted for prudential purposes entails a high degree of complexity, both from the point of view of its elaboration and from the viewpoint of its understanding by the final user. The effort expended in preparing this template would therefore be disproportionate to the value added. More helpful to users from the outset would be: a) to provide figures for the principal differences, both in terms of material amounts and significant topics that we know to be of interest to investors, and b) narrative to explain that data meaningfully to them.

In addition, in order to ensure similar quality standards we think that **disclosure requirements should be limited to audited financial statements**. As quarterly financial statements are not generally audited, we take the view that **yearly publication** represents the best trade-off between quality and timeliness, in line with the current "*Information of Prudential Relevance*" under the Basel Pillar III requirements.

Finally, the **timeline for implementation of the disclosure requirements is too short**. The implementation of the proposed disclosure requirements requires IT developments that constitute an investment in time and resources. Enough time should be given to the institutions to properly develop those systems and avoid inefficient short term solutions that go in the detriment of information quality.

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ANNEX 1

Example of :

- Goodwill deduction 100% according to Basel III in 2018.
- Phase-in arrangements establish a minimum of 20% each year from 2013 to 2018
- Country X regulation establishes a 20% in 2013 and a 40% in 2014 (minimum required by phase-in agreement).
- Country Y regulation establishes a 50% deduction in 2013 and a 100% in 2014 (that implies an acceleration with respect to the Basel III phase-in arrangements).

We have 2 institutions from different jurisdictions with €100M in Goodwill.

Treatment proposed by Basel III-EBA (Implicit benchmarking: Basel III 2018)

2013

INSTITUTION Country X	CRR treatment	Pre-CRR treatment
Goodwill	20	80

INSTITUTION Country Y	CRR treatment	Pre-CRR treatment
Goodwill	50	50

2014

INSTITUTION Country X	CRR treatment	Pre-CRR treatment
Goodwill	40	60

INSTITUTION Country Y	CRR treatment	Pre-CRR treatment
Goodwill	100	0

Comments: An additional column indicates the amounts of the regulatory adjustments that will be subject to the national transposition measures of Directive 2006/48/EC ('amounts subject to pre-CRR treatment or CRR prescribed residual amount' column).

Treatment proposed by Santander (Implicit benchmarking: minimum requirements according with the Basel III phase-in arrangements).

2013

INSTITUTION Country X	CRR treatment	Above min phase-in treatment
Goodwill	20	0

INSTITUTION Country Y	CRR treatment	Above min phase-in treatment
Goodwill	50	30

2014

INSTITUTION Country X	CRR treatment	Above min phase-in treatment
Goodwill	40	0

INSTITUTION Country Y	CRR treatment	Above min phase-in treatment
Goodwill	100	60

Comments: Additional column indicates the amounts that are subject to Basel III treatment above the minimum determined by the Basel III phase-in.

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