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EBA Consultation Paper "Guidelines on ICAAP and ILAAP information collected for SREP purposes"

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Prepared by Jg/To

Dear Mr Enria,

Thank you for the opportunity to comment on the Consultation Paper "Guidelines on ICAAP and ILAAP information collected for SREP purposes" published on 11 December 2015. Please find enclosed the comments of the German Banking Industry Committee.

Enclosure
Comments of the German Banking Industry Committee

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

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German Banking Industry Committee

Die Deutsche Kreditwirtschaft

Comments

EBA Consultation Paper "Guidelines on ICAAP and ILAAP information collected for SREP purposes"

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Berlin, 10 March 2016

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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General comments

We are grateful for the opportunity to respond to the present Consultation Paper and wish to begin by submitting some general comments on the EBA draft Guidelines.

In principle, we believe that the EBA's initiative to define a structured set of requirements for the information supporting the SREP makes sense. We also endorse the EBA's intention not to generate any additional requirements for institutions' ICAAP and ILAAP when specifying the necessary information. In the ILAAP's case, however, no account has been taken of this intention at numerous points, as we shall explain in more detail in the *Specific Comments* section below.

We expressly welcome the proportionality clauses contained in the draft Guidelines. In our view, their effectiveness will, however, depend on whether competent authorities are actually given the proposed discretion in the supervision of LSIs referred to in paragraph 14, among others. In this context, a notable positive is that the EBA has not drafted any proposals for reporting formats so as to allow national supervisors broad scope for implementing the principle of proportionality.

Seen individually, the requirements for the information to be provided by institutions are largely reasonable, particularly for the ICAAP. As a whole, however, they generate such a volume of paper that it is questionable whether supervisors will be able to inspect and evaluate all documents properly. For this reason, we believe it is essential to examine in detail whether, with materiality and cost-benefit considerations in mind, concentration on fewer information items and documents can be achieved. May we draw attention in this context to the EBA Banking Stakeholder Group's December 2015 report on "*Proportionality in Bank Regulation"*.

Due to the enormous amount of detailed information that is requested overall from Category 1 institutions, we were surprised to note that paragraph 13 contains wording ("*at least*") establishing a minimum requirement. We wish to suggest making quite clear at this point that the total package is a maximum requirement and that, from a risk perspective, it can be lowered for such institutions as well.

Given the sheer volume of documentation, we suggest including a note in the draft Guidelines expressly stating that the information does not have to be transmitted in paper form.

In addition, we would like to point out that the 30 June 2016 application date strikes us as a very ambitious deadline, especially in view of the fact that competent authorities may use the draft Guidelines to formulate information requests for 2016 cycle of SREP.

Specific comments on the EBA draft Guidelines (Section 4 of the Consultation Paper)

Section 4 – General considerations for collection of ICAAP and ILAAP related information

Section 4, paragraph 13
We assume that the “one” single set date mainly refers to quantitative data only, so that the last day of a quarter would be a reasonable choice. Moreover, it should be added that all additional documents should be the ones that are valid on this particular set date. Updating and approving all accompanying documents would impose an unduly heavy burden on institutions and jeopardise the quality of the approval process.

Section 4, paragraph 19
We doubt whether the proposal delivers any real benefit. On the contrary, in cases where a document is already available to a competent authority, it would be easier for an institution to submit the most up-to-date document (again, if in doubt) instead of regularly confirming which version the competent authority last received.

Section 4, paragraph 20
It is only the competent authority that benefits in this case as well, as it does not have to look at the documents. Institutions, on the other hand, are obligated to indicate which information they have not included. If in doubt, it is easier for institutions to simply forward the complete information. We therefore assume that institutions will be free to decide which approach to adopt. Clarification on this point would be appreciated.

Section 5 – Information that is common to ICAAP and ILAAP

Sub-section 5.2, paragraph 23d
This paragraph is very difficult to understand. It remains unclear what is expected from the industry.

Sub-section 5.3, paragraph 24
We assume that the risk appetite framework may consist of different documents and would welcome clarification on this point.

Sub-section 5.4, paragraph 25
Paragraph 25 sets out requirements for information on risk data, aggregation and IT systems. These requirements are extremely extensive. Their description suggests that financial institutions are required to deliver full and complete documentation on their data and IT architecture, starting with base data. We do not see how competent authorities intend to inspect and evaluate such documentation. A more appropriate approach would be to request summarised information from institutions and examine compliance with the principles by way of checks based on examples and random samples.

In addition, we consider it important to draw attention to the following:
Small financial institutions often outsource risk management structures to specialised external service providers. We believe it makes no sense, for practical reasons and due to the burden it would impose, to request from every single institution using such external service providers individual information on the

external provider's database, data aggregation and IT systems. A sensible solution for such cases could therefore be delivery of a standardised description by the external service provider that is supplemented, where necessary, by institution-specific descriptions. We should appreciate an explanation of what appropriate supervisory practice would look like in such cases.

Sub-section 5.5, paragraph 26
We fail to understand the requirements relating to the disclosure of information and are therefore strongly opposed to these.

re point a:
The relevant disclosure requirements are set out in the CRR (mainly Article 435 (1) and Article 438 (a)). We see no sense in having these explained again separately.

re point b:
This requirement would, if at all, only be of relevance to financial institutions with a capital market focus. Yet, in their case too, any impact on capital adequacy and funding emanates mainly from annual reports and possible ad hoc reporting, as well as from direct communication with investors. Disclosure under Pillar 3 only plays a subordinate role here in our experience. Furthermore, we wonder how the influence of Pillar 3 information is to be assessed separately from the other public relations activities. In order to conduct such an assessment, individual investors would have to be specifically interviewed to determine how helpful they found the disclosure report for their decisions. We believe this imposes an absolutely unreasonable burden and strongly oppose the requirement.

re point c:
Because of the principle of confidentiality and materiality inherent in Pillar 3, there are always deviations between internal information and disclosed information, particularly in the level of detail. Explaining these would impose an unnecessary additional burden on institutions.
We therefore suggest dropping paragraph 26 in its entirety. It should generally be sufficient to inspect institution's current disclosure report as part of the audit. These reports are publicly available, so that they do not need to be requested separately from institutions.

Section 6 – ICAAP specific information

Sub-section 6.5, paragraph 36
Reports on ICAAP/ILAAP stress tests (paragraph 36 a, paragraph 51 a) should be requested annually or less frequently. It remains unclear whether institutions are required to make available to the competent authorities on the date for delivery of information all reports for a year or only an end-of-year report in summarised form.
Given that competent authorities closely monitor Category 1 financial institutions also over the course of a year and promptly inspect numerous documents, we believe it is of little help to subsequently request an additional consolidated end-of-year report. This is superfluous.

Sub-section 6.6, paragraph 37
At numerous points, a requirement is set for financial institutions to not only deliver decisions and results but to also document discussions (see paragraph 37 and, similarly, paragraph 54 on ILAAP). This raises the question of how detailed such documentation should be. We regard the verbatim or action minutes of

meetings as generally too lengthy. We therefore suggest making clear that a brief account of the different positions taken in a discussion, indicating the outcome of the discussion, would be completely sufficient. This applies particularly to management board meetings.

Section 7 – ILAAP specific information

We do believe that the proposed order of contents of the ILAAP could be simplified and alternately structured in such a way as to allow firms to more clearly demonstrate their liquidity adequacy. As currently drafted, the order of sections begins with the liquidity risk management framework, moves on to funding strategy, then to liquidity buffers, funds transfer pricing, intraday risk, stress testing and contingency funding planning. This order is confusing and should be simplified in order to allow firms to better present their main liquidity and funding risks and how they manage these. We would welcome further clarity regarding the structure of the ILAAP contents.

As a practical alternative measure, the EBA should consider the proposed structure and content of ILAAP documents published by the PRA in their June 2015 paper "*PRA's approach to supervising liquidity and funding risks*". This suggested structure allows firms to clearly describe the conclusions of their overall liquidity adequacy review, clearly state their LCR positions, level of high-quality liquid assets, inflows and outflows, then describe their liquidity and funding risk assessments, before describing their risk management frameworks.

Sub-section 7.1.2, paragraph 39 a
The term "*intra-group liquidity risk*" is not defined satisfactorily under any supervisory rules. It can therefore be interpreted differently. Does it mean only the liquidity relationship within a group, excluding any external sources of liquidity of the individual group entities, or do external sources of liquidity have to be included? Clarification on this point would be appreciated.

Sub-section 7.2.2, paragraph 41 d
The wording "*after execution of the funding plan*" is misleading. Do competent authorities expect a hypothetical analysis (what-if scenario) or an ex-post analysis (back-testing)?

Section 7.3.1, paragraph 42 a
The wording "*required level of liquid assets*" suggests that competent authorities' expectations are influenced strongly by the LCR system. We should like to stress, however, that financial institutions may have their own, broader liquidity management methodology, such as the funding gap/liquidity surplus concept. We therefore suggest replacing the term "*liquid assets*" with "*level of required stress liquidity reserve portfolio to cover potential outflows*".

Sub-section 7.3.1, paragraph 42 b
The term "*collateral management*" can be interpreted very broadly. We therefore suggest making clear that financial institutions should be left to decide which collateral is concerned in this context.

Sub-section 7.3.1, paragraph 43 b
See our comments on paragraph 42 a. In this case, too, another liquidity term should be used instead of "*buffer of liquid assets*".

Sub-section 7.3.2, paragraph 43 d
We regard the request for "*projections of the development of the internal required minimum volume of liquid assets*" as a supervisory requirement going beyond the SREP Guidelines that is supposedly based on the need for information. The SREP Guidelines do not call for any such projections. In addition, we question the sense of this instrument, given that liquidity management is a highly dynamic process that needs to be adapted to changing environments. A "plan" or "projection" will very soon be outdated. Projections may be applied to secured funding via covered bonds or securitisation. Other encumbrance such as repos, lending or collateralisation is hardly projectable, but driven by operational liquidity management considerations. This paragraph should therefore be dropped.

Sub-section 7.5.1, paragraph 48 c
A new supervisory requirement is created at the point as well. There is no supervisory requirement to provide such a description. We doubt, moreover, whether such a description would produce any meaningful results, since interlinkage between intraday liquidity risk management and the Contingency Funding Plan will be very remote.

Sub-section 7.6.2, paragraph 51 c
We understand the requirement to be an obligation to produce a funding plan under stress assumptions in addition to the normal funding plan. We wish to point out that there is as yet no supervisory requirement to stress-test funding. The stress-testing requirements set by the EBA Guidelines sensibly cover liquidity aspects. We therefore suggest deleting this paragraph.

Sub-section 7.7, paragraph 53 b
We regard the expectations that competent authorities attach to the phrase "*concrete management action*" in this context as misguided. Information can, at best, be provided through a "*set of possible management actions*", since concrete management action can only be ordered in individual cases.

Sub-section 7.8, paragraph 54 d
This requirement is worded so generally that it must be concluded that every single new product/new market decision documentation that says anything about funds transfer pricing would have to be submitted. This again goes too far, in our view. The requirement should be limited to important decisions.

Sub-section 7.8, paragraph 54 f
This paragraph should be deleted. Management of intraday liquidity consists of a large number of daily decisions and actions. In this context, "*where relevant*" is a completely undifferentiated term, nor can it be defined more precisely. Competent authorities cannot and surely do not wish to stipulate that they receive a report annually covering actions over approximately 240 business days.

Section 8 – ICAAP and ILAAP conclusions and quality assurance

The Model Change Policy (MCP) has applied solely to Pillar 1 so far. Under Pillar 2, changes to the ICAAP concept are typically subject to subsequent examination (i.e. no approval by competent authorities in advance but examination-based decision). The requirements now call for information on changes (made or planned) to the ILAAP/ICAAP frameworks (paragraphs 55 c, 56). It should be made clear that no MCP and no conditional approval are being introduced at this point.

It could also be concluded that under paragraphs 55 a and b any and all changes to the business model, strategies, risk appetite, etc. have to be submitted to competent authorities before being implemented. This would, in our view, constitute interference in management's area of reponsibility.
For this reason, the descriptions of made or planned changes called for under paragaph 55 should be restricted to material changes made so as to keep the documentation burden within reasonable limits.

Paragraph 57
The phrase "*performed by independent validation function*" does not indicate which specific requirements there are in regard to independence. The independence of the validation function is not specified in the SREP Guidelines as a criterion for the supervisory review process. Contrary to the EBA's intention, a new supervisory requirement is thus introduced here, too. We do not consider a new requirement on this point in the present Guidelines to be appropriate and therefore request deletion of this phrase.

Section 5 of the Consultation Paper – Accompanying documents

Sub-section 5.1
The projected costs and benefits are vague and kept purely qualitative. It would be more convincing to quantify the additional burden for the individual categories of financial institution.
When assessing this, a distinction should be made between whether the documentation is already available to the required extent in financial institutions and whether it has still to be produced in part. Even for institutions which already have comprehensive documentation available, producing and regularly updating a "reader's manual" (including the change status of every single document since it was last delivered to the competent authority) is likely to impose a considerable additional burden. This will be compounded by the requirement to aggregate data and make it available annually in a single, consolidated package.