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Consultation response

Draft Implementing Technical Standards amending Commission Implementing Regulation (EU) 680/2014 on supervisory reporting of institutions

30 March 2016

Introductory comments

AFME welcomes the EBA consulting stakeholders on its proposal for "**Draft Implementing Technical Standards amending Commission Implementing Regulation (EU) 680/2014 on supervisory reporting of institutions**" ("the consultation"). We are however concerned with the tight deadline for considering the proposals. A thorough analysis of the different elements of the templates and instructions within less than 30 days is extremely challenging and, as a result, our comments below might not reflect all issues, errors or omissions which might otherwise have been identified and which could possibly give rise to unintended consequences on reporting institutions.

Moreover, given the lack of suitability of the EBA Q&A process when it comes to clarifying issues relating to reporting templates, it is essential that the templates be error free from the start of the final ITS adoption process.

While we are of course supportive of the EBA introducing new reporting requirements that are consistent with the provisions of the recently adopted Prudent Valuation RTS, we are of the view that certain aspects of the current proposals go beyond the provisions of the RTS and without providing information that will be meaningful for or useful to competent authorities. Moreover, the burden some of these new requirements will create for institutions should not be underestimated – our members expect that the reporting workload would in effect at least double – and we are concerned that the provision of what we view as being superfluous information risks detracting from the core information on the most important calculations. Lastly, firms will of course incur an IT cost in order to complete the new templates and will require a significant amount of time to implement such solutions. In the interim, completing these templates manually create an even more heavy workload.

All in all, we question therefore whether the right balance has been achieved with the current proposals, particularly given the short consultation period, and would encourage the EBA to revisit its templates in line with our recommendations provided below.

We are of course at the EBA's disposal to hold further, in depth discussions on these matters should that be helpful.

Please see below for our answers to the specific questions in the consultation.

Question 1: ***Do you agree with this statement? If not please explain your reasoning*.**

We are concerned that some of the proposals in the consultation documents go beyond what would be reasonably required for "*an understanding of where the accounting fair value sits within the notional range of plausible values at an aggregate level*". In particular, we are not in favour of the proposed calculation of upside uncertainty (column 120 of C 32.02) as this would in many cases at least double the workload undertaken by institutions for the purposes of estimating uncertainty. At the same time, upside uncertainty is not relevant to Prudent Valuation, which is precisely a "prudent", downside measure of uncertainty. Furthermore, in practical terms, estimating upside uncertainty requires a significant amount of inputs and methodologies which would not otherwise be used in the context of prudent valuation or any other reporting requirements. We therefore disagree with upside uncertainty being "essential context" for the downside of the plausible range, and the administrative costs associated with this option do not seem to be outweighed by possible benefits.

Question 2: ***Would the 'upside uncertainty' measure defined above and used in column 120 of template C 32.02 be suitable as a definition of the upside uncertainty? If not please provide reasons and any alternative suggestions for how such an upside measure could be defined.***

As mentioned above, in our response to Question 1 of the consultation, we do not believe that any inclusion of upside uncertainty would pass the cost-benefit analysis. We note that such a calculation is not required by the prudent valuation RTS. We would therefore propose, on the basis of the administrative costs that the requirement would create, the exclusion of the reference of upside uncertainty from the revised EBA reporting templates for prudent valuation. It should also be noted that resources utilised in calculating an upside uncertainty with the same rigour as downside would shift the focus of an institution's resources that are currently set towards AVA calculations.

In respect of our answer to Questions 1 and 2 above, we would also highlight the difficulty our members would have in providing the data required in a short timeframe. The uncertainty of the effect on banks' ability to produce the information mentioned in the consultation is also compounded by the brief consultation period on the proposals.

Question 3: ***Is the above approach to splitting out fair valued assets and liabilities and fair-value adjustments on the one hand between the different types of AVAs and on the other hand between asset classes and product categories practical to implement? If not please describe the practical obstacles. Please suggest any alternative approaches (particularly if an alternative approach has been found useful for internal reporting purposes).***

We support in principle the consultation's proposal to disclose fair value adjustments.

We are concerned however with the proposed breakdown, for example, of assets and liabilities by portfolios. We note that the reporting of most institutions is not built at this portfolio level and that therefore the approach suggested in the consultation document would add an additional layer of complexity which would go beyond what is required for the purposes of accounting valuation. This level of breakdown is also not implied by the Prudent Valuation RTS.

As an alternative, we suggest that the split be done at a business level, which would thus align the requirements with information that is used by firms for the purposes of their internal/management reporting.

We are also concerned with the list of required items including information on QTD Revenue for portfolios (in Column 150). We would not consider the revenue attributed to portfolios to which the fair value positions were assigned to be useful in meeting the objectives described in the explanatory note preceding question 3. The case has also not been made for why this would be relevant for valuation uncertainty, and we would therefore welcome the removal of this requirement from the template.

Question 4*: Is the above portfolio-based approach to splitting out AVAs and other attributes between 'Exotic' and 'Vanilla' practical to implement? If not please describe the practical obstacles. Please suggest any alternative approaches (particularly if an alternative approach has been found useful for internal reporting purposes).*

As explained above, there are practical difficulties to implementing the portfolio approach.

For example, AVAs are calculated at valuation exposure level. Typically, such exposures include contributions both from exotics and plain vanilla instruments on the same risk factor. For example, a typical calculation of AVA MPU for interest rate volatility considers the vega sensitivity generated by both interest rate exotics and their corresponding plain vanilla hedges. The resulting AVA MPU is a single figure, representing the entire valuation uncertainty corresponding to interest rate volatility uncertainty. There is no natural split between exotics and plain vanillas.

In our view, the split should instead follow the business organisation and the way activities are reported (this would allow the alignment of supervisory reporting rules to the business activities performed). We note that this way of proceeding also appears to be more aligned with the approach adopted in the forthcoming Fundamental Review of the Trading Book. The portfolio-based approach would otherwise be unduly onerous on market participants and would not mirror any of the existing reporting processes in use for either regulatory or internal purposes.

Similarly the requirement to report the Fair Value amounts for such portfolios is not currently possible at some institutions due to the different basis by which risk and financial data is collated by institutions. We would therefore welcome the EBA clarifying whether the intention of the wording on the requirements for Rows 040-160 (page 10 of Annex 2 to the consultation) referring to a "portfolio based allocation" is compatible with the way in which most businesses would currently report information on AVAs. If a portfolio approach is retained, at a minimum, we would welcome further clarification that firms have the ability to exercise judgment in allocating their internal reporting breakdowns to the proposed regulatory categories.

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Moreover, the split between the trading and non-trading books would also cause difficulties for most institutions and does not seem aligned with the initial RTS. The proposed definition for the non-trading books risks capturing products on trading desks which are seen from an IPV perspective to be a normal part of trading and would not need separating out for any other purposes.

The requirement to collate information separately for non-trading books would likely require significant additional work due to the extra calculations required to report the information. These calculations would be made difficult by i) the separation between trading and non-trading books not being built into existing systems and ii) the need to separately calculate any netting benefit on a group netted basis and on a portfolio basis. The final ITS should therefore clarify that banking book products that are part of a trading or capital market activity or offering do not need to be separated out into the non-trading book category.

Question 5: ***Do you think such mismatches between the portfolio-level AVAs and the institution-level AVAs would be significant? Please give examples.***

On the question of the mismatches between portfolio-level and institution-level AVAs, we note that the level of mismatch would depend on how much offsetting valuation exposures existed between the different portfolios.

Question 6: ***Where the difference is significant what additional practical difficulties would arise from calculating AVAs for each of the portfolio categories in rows 050-170?***

The effort required to perform the calculations increases significantly with additional splits of information required. Risks/valuation exposures should be able to be netted at the institution level for the AVA calculations. The significant extra effort required to perform these calculations for additional splits is the same regardless of whether the benefit is large or small since institutions would have to build and operate the additional calculation processes.

Question 7: ***What are stakeholders' views on the ability to usefully summarise in a few key words the models and products concerned, as well as on the associated reporting burden or IT issues?***

We note that column 050 requires a "Description of the main features of the valuation model that is used to derive the accounting fair value. This should include a description of any model-related Fair Value Adjustments where relevant".

While we welcome a standardised approach to the length of the description, and we agree that this could improve comparability across institutions, we note that only the basic features of the model could be explained in 60 characters.

We also wish to point out that, due to the absence of standardised model description across firms, there is a risk that that different descriptions of the same model by different institutions are collected, thereby reducing the comparability and usefulness of the data, potentially even in the case of simple models for plain vanilla instruments. For example the model associated to European interest rate caps/floors could be equally well described as "Black model", "Black model with SABR volatility", "SABR model", etc. We thus suggest enriching the model description with some standard fields with pre-determined answers. This high-level model inventory could be borrowed, for example, from the templates used in the Asset Quality Review.

Question 8: ***Do you find the proposed instructions on prudent valuation clear? Are there specific parts where definitions or instructions should be clarified?***

In relation to the clarity of the proposed prudent valuation instructions, we would like to reiterate some of the points we have raised earlier in our response. For example the way in which trading book portfolios are explained for rows 040-160 would seem to preclude using businesses/desks as the driver for categorisation (to give an example, Structured Ratesshould be reported in "Rates Exotics" and Flow Rates should be reported in "Rates Vanilla"). We also note that, due to the short consultation period it is likely that our members will have been unable to identify potential additional issues that may exist. We are concerned that this unnecessary (in our view) haste could create potential problems down the line when the reporting ITS is implemented in practice.

Question 9: ***Do respondents have any comments on the structure and content of the proposed templates on prudent valuation?***

In answer to Question 9 of the consultation, we would reiterate our introductory comments to this response letter, highlighting the difficulty our members had in analysing the proposed templates in detail given the short timeframe for the consultation. Our initial analysis did however raise a number of inconsistencies, some of which are mentioned below:

- The templates seem to be unduly onerous and not focused on the "essential context" required by the objective of capturing information which relates to reporting prudent valuation information.

- We would welcome the EBA clarifying whether the reference to "Model" in the proposed instructions to template C32.03 should actually refer to "methodology" – which is the term used by the Commission Delegated Act implementing the Prudent Valuation RTS in Article 19(3). If the two terms are meant to be equivalent, we are concerned the template proposed would not be produced as part of institutions' compliance with the RTS requirements.

- We agree that providing certain model related metrics alongside the model risk AVAs is useful with respect to Prudent Valuation. We do not, however, think that it is natural to allocate all of the proposed metrics to a given model and are concerned that this will lead to confusion and inconsistent interpretation. For example, a given trade can

reference a number of different models so the allocation of that MTM/notional between the models will not be objective. We also believe that disclosures around fair value adjustments and IPV should be limited specifically to those balances relating to model risk.

We are concerned with the requirements regarding the model risk and concentration AVA templates which may be onerous to implement even for banks with relatively little exposures to these AVAs. In particular we have concerns with some of the wording in paragraph 4.1 of Annex 2 to the consultation document (requiring "*report details of the top 50 individual model risk AVAs*"). As an alternative, we would suggest either applying a materiality filter to the requirement (e.g. 1% of total AVAs), or restricting the detailed information to the top AVAs needed to ensure sufficient coverage of the model risk in addition to the proposed limit of 50 line items.

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