

## Follow-up review of banks' transparency in their 2011 Pillar 3 reports



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## Executive summary

One of the EBA's regular tasks is to assess Pillar 3 reports of European banks / credit institutions<sup>1</sup> and monitor their compliance with the requirements of the Capital Requirements Directive (CRD). This analysis continues from Pillar 3 assessments that have been carried out annually since 2008. It focuses particularly on areas where the need for improvement was already identified in previous assessments. It also covers areas where new disclosure requirements entered into force in 2011. The current analysis was carried out in 2012 and covers the 2011 Pillar 3 reports of nineteen European banks<sup>2</sup>.

No significant changes in banks' practices were noted this year in the practical aspects of the publication of Pillar 3 information (e.g. timing, formats or verification of disclosures), although the EBA noted that banks have generally published their Pillar 3 information nearer to the reporting date of their annual accounts and publication of their annual reports. The EBA would prefer the Pillar 3 information to be published at the same time as these annual reports and accounts, and expects the situation to improve as a result of compliance with the new Capital Requirements Regulation (CRR). As far as remuneration disclosures are concerned, if these are not actually included in the Pillar 3 reports or annual reports, the EBA would also prefer them to be published at the same time and provide cross-references between the reports. This would then ensure that Pillar 3 report users (investors and other users) have timely access to the complete set of publicly available information that is essential for assessing credit institutions' risk profiles.

Disclosures on own funds were generally assessed as comprehensive, with credit institutions providing details of capital items and a meaningful breakdown of deductions. Cases of non-compliance were mostly related to disclosures on the grandfathering of instruments, qualitative details about the capital instruments or breakdowns of capital items. The EBA also believes that comparability of disclosures on own-funds will be significantly improved by the implementation of the CRR and of the related EBA's implementing technical standards on own funds disclosures, which will provide common definitions and templates for disclosures.

However, the analysis of information on credit risk – Internal Ratings Based (IRB) approach and securitisation risk – revealed certain weaknesses as well as the need for improvements and more explanation on the rationale for and the expected content of disclosure requirements.

In particular, credit institutions are expected to increase the “back-testing” disclosures. Half of the banks in the sample failed to comply with the relevant CRD requirement, and many of the banks provided confusing information about the assumptions underlying internally developed models. In this context, the EBA also notes that to allow meaningful and reliable conclusions to be drawn on the functioning of the model, disclosures of a comparison between expected losses against actual losses should be provided for a period of at least three years - a best practice that is not followed by the majority of the banks.

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<sup>1</sup> In this report, the words 'banks' and 'credit institutions' are used as synonyms

<sup>2</sup> Accordingly, when reference is made to last year's assessment, this covers analysis done in 2011 of banks' 2010 Pillar 3 reports

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As far as securitisation risk is concerned, the small number of disclosures assessed as adequate was mainly due to the introduction of new qualitative and quantitative disclosures requirements with the implementation of CRD III. Significant improvement is therefore needed for new disclosures on risk management and exposures in the trading book or related to special purpose entities (SPEs). However, there were also failures to comply with disclosure requirements which were related to pre-CRD III requirements.

Market risk was another area where many new disclosure requirements were introduced and here the analysis also identified certain areas where significant improvements were needed. These included disclosures on back-testing of internal models, stress testing, valuation models, adequate breakdown of market risk capital requirements, stressed VaR measure, the new incremental risk charge as well as the comprehensive risk measure.

On the other hand, significant improvements were noted in the area of remuneration disclosures with a total of 57% of the banks in the sample assessed as providing adequate disclosures or disclosures that captured the spirit of the CRD requirements.

In all these disclosure areas, the EBA identified some best practices which credit institutions are encouraged to follow to enhance the quality of Pillar 3 information.

In addition to the assessment results and detailed findings as set forth in this report, there are two other sections. The EBA decided to add further analysis that was not limited to a compliance exercise, but touched upon disclosure related issues, outside the Pillar 3 framework.

The EBA therefore carried out a thematic study reviewing and comparing Basel III implementation disclosures, focusing on information provided by banks about the resulting impact on own funds, and on disclosures for the EBA 2011 capital exercise. It was found that all credit institutions provided some disclosures, but the content and presentation of these greatly varied. Some institutions only disclosed qualitative elements while others supplemented these qualitative disclosures with some quantitative data. Data were however not comparable, due to differences in terms of granularity and of hypotheses used to estimate the impacts of regulatory changes on own-funds. Finally, Annex II of this report aims at clarifying CRD requirements in areas where quality of disclosures could be improved.

As last year, the EBA noticed that one of the main challenges of Pillar 3 information, regardless the requirements considered, was comparability of disclosures between credit institutions. The EBA still believes greater comparability or some standardisation would enhance the benefits of Pillar 3 information for users, including the ESAs and the ESRB.

The conclusions of the report are the result of productive discussions between the National Supervisory Authorities and the EBA, informed by inputs from preparers and users of Pillar 3 disclosures. These conclusions have highlighted topics where further discussions should be encouraged between those preparing and those using of Pillar 3 information and the NSAs/EBA to enhance of quality of disclosures in these areas. The EBA will use these conclusions as a basis for initiating discussions and also as essential input for defining and developing its strategy in enhancing the area of transparency.

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Indeed, as a result to the findings from this report, the EBA will in 2012 and 2013 :

- Keep on identifying best practices of public disclosures in the publications
- Keep on identifying the CRD requirements for which compliance has to be improved and those that should be improved, and work on these improvements, including in the area of comparability
- Consult and work with industry and users to improve transparency in areas where it is needed

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## 1. Introduction, objectives and methodology

This report presents the results of the EBA's annual assessment of banks' Pillar 3 disclosures. The same analysis has been carried out since 2008 and monitors how banks comply with the Pillar 3 disclosure requirements of Directive 2006/48/EC, specifically with regards to Title V, Chapter 5 of this Directive, 'Disclosure by credit institutions' and Annex XII 'Technical criteria on transparency and disclosures' which extended in specific areas (e.g. disclosures on securitisation, market risk), after the CRD III entered into force in 2011

The analysis carried out last year and presented in the report 'Follow-up review of banks' transparency in their 2010 Pillar 3 reports', confirmed that banks were making efforts to improve disclosures but reiterated problems of comparability and the need for further harmonisation. This need has also been stressed subsequently by other organisations involved in financial disclosure assessments.

Last year's report identified the following specific disclosure areas where banks needed to intensify their efforts:

- disclosures on remuneration policies and practices (first disclosure in the 2010 Pillar 3 reports);
- credit risk – IRB approach; quantitative back testing information;
- credit risk – Counterparty credit risk; wrong-way risk;
- interest rate risk; sensitivity analysis.

The EBA also conducted a thematic study last year and supplemented the findings from last year's assessment of 2010 Pillar 3 reports with some observations about how banks dealt with the interaction between IFRS and some Pillar 3 requirements (the same that were included in the EBA Pillar 3 analysis from the year before, e.g. scope of application, own funds, credit risk, interest rate risk etc.). This thematic study revealed the need for further work on the interrelationship between IFRS and Pillar 3 with a view to giving users of the information a better understanding of the overall profile of the credit institution as reflected by both the accounting and prudential information.

### 1.1 Sample for the 2012 assessment

The exercise was based on the Pillar 3 information disclosed by 19 European banks with cross-border activities (see Annex I)<sup>3</sup>.

### 1.2 Scope of the 2012 assessment

The 2012 assessment focused, as last year, on areas where improvements are still needed and on areas where new disclosure requirements came into force in 2011.

This report therefore concentrates on the following disclosure areas:

- scope of application;
- own funds;
- credit Risk;
- internal Rating Based approach;
- securitisation;

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<sup>3</sup> The sample of banks used for the 2012 assessment is the same as for 2011 one with one exception

- 
- market risk;
  - remuneration.

### 1.3 Questionnaire on investors/users needs regarding Pillar 3 information

To improve the outcome of the current analysis, the EBA decided to launch a targeted dialogue with investors and/or users of Pillar 3 information. The EBA issued a questionnaire, inviting interested parties to comment on those issues/areas within the scope of the 2012 assessment, that were most important to investors and/or users.

Responses – although in limited number – were received from rating agencies, credit institutions and analysts<sup>4</sup>. For rating agencies/analysts the main issues regarding Pillar 3 disclosures were the following: i) lack of a consistent and transparent format (which could be addressed by developing and adopting standardised formats and templates); ii) absence of consistent definitions, with similar concepts like EAD being labelled differently by the different credit institutions; iii) timing of the publication of Pillar 3 reports, especially the time-lag between the end of a credit institution's accounting period and the publication of its Pillar 3 report, and iv) lack of comprehensive information on the risk profile of entities, partly due to the lack of reconciliation between Pillar 3 and annual reports.

It is interesting to note that credit institutions are against a mandatory increase in the frequency of the full set of Pillar 3 disclosures and the adoption of standardised formats since that these are not seen to be beneficial, but rather are regarded as time consuming and costly.

### 1.4 Assessment methodology

The assessment methodology involves both an analysis at individual bank level carried out by national supervisors, and a horizontal assessment of each disclosure area for all credit institutions in the sample, carried out by dedicated small teams of two or three national supervisors.

National supervisors discuss the final assessments and scores with the institutions from their jurisdiction covered in the assessment. This provided direct and immediate feedback about the outcome of the analysis and also gives the supervisors an opportunity to understand any specific issues facing particular banks (e.g. applicability of specific disclosure requirements).

The purpose of this approach was to reduce potential bias implicit in any assessment and to promote greater consistency in the assessment of the banks sampled. As banks have had time to gain experience with preparing their Pillar 3 disclosures, the EBA has further tightened its assessment process with a view to enhancing consistency and reducing subjectivity (see below). However, it is essential to note that a degree of judgement is inherent to the nature of the assessment.

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<sup>4</sup> Both the questionnaire and the non-confidential responses are published on the EBA's website under the following link : <http://eba.europa.eu/News--Communications/Year/2012/Responses-to-the-questionnaire-on-the-identificati.aspx>



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## 1.5 Scoring scale and other issues considered

The same scoring scale used in last year's assessment also applies for this year's analysis, meaning that a disclosure area only received an 'adequate' score (a score of 3) when all items and sub-items deemed to be applicable to that area, were provided.

The scores were as follows:

- n/a = item is not applicable (it is then expected that no information would be provided for this item/sub-item);
- 0 = no information is provided (if information is regarded as immaterial, proprietary or confidential, and as such it is not disclosed, then the non-disclosure should not be penalised);
- 1 = insufficient information is provided (the disclosure is non-compliant with the CRD requirements);
- 2 = sufficient information is provided, but disclosures could be improved (the disclosures are largely compliant but some disclosure items or sub-items are missing);
- 3 = information provided is adequate (the disclosure is compliant with the CRD requirements);
- 3\* designates disclosures that are compliant with the letter and the spirit of the CRD (and often go beyond the CRD requirements or disclose information in a meaningful and useful way, thus being regarded as best practice disclosures)<sup>5</sup>.

Appropriate and extensive/detailed disclosures can therefore be awarded a score of 2, despite their quality, if one or some disclosure items or sub-items were not provided. Similarly, a disclosure area with a score of 2 does not exclude individual items or sub-items of this disclosure area being regarded as an example of best practice.

### 1.5.1 Immaterial, proprietary or confidential information – applicability of information

For the assessment of information as immaterial, proprietary or confidential and the applicability of information provided in each item, the following approach was adopted:

- The score will be lower than 3:
  - if information is not disclosed because it is immaterial, proprietary or confidential, but there is no specific reference to this;
  - if information is not provided, but the national supervisor has confirmed that it is applicable.
- The score will be 3 when information is not disclosed because it is immaterial, proprietary or confidential and there is specific reference to this.

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<sup>5</sup> The best practice examples are not intended to be exhaustive or exclusive. Rather, they are considered to be particularly useful and conducive to increasing comparability and in promoting disclosures that are deemed as compliant with the spirit of CRD.

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### 1.5.2 Disclosure of Pillar 3 information in English

Although nothing is specified in the CRD about this matter, the EBA considers that for internationally active banks, providing an English translation of Pillar 3 information would allow a wider range of stakeholders to access the information. Pillar 3 disclosures not provided in English were therefore given a score lower than 3.

## 1.6 Best practices and additional explanation of disclosure requirements

In previous assessments, the EBA had identified and promoted best practice disclosures. This year the EBA decided to supplement these best practices with an additional explanation section on the purpose of specific disclosure items and the information that is expected to be disclosed according to the EBA. Developing such explanations was considered useful since it supports those preparing Pillar 3 disclosures in addressing new disclosure requirements and in improving disclosures to fully comply with requirements in the future. This additional explanation section supplements best practices in the sense it aims at promoting better harmonization and comparability of banks' Pillar 3 disclosures on a voluntary basis. The EBA encourages banks to consider the explanations disclosed in Annex II of this report in their production of Pillar 3 reports. Annex II should however not be regarded as an official guidance or as a binding text, and following its provisions does not waive the requirement for banks to comply with any existing national guidance on Pillar 3 that is applicable to them.

## 1.7 Thematic study

This year's report also looks at Basel III implementation disclosures. Basel III lays down tougher capital standards and introduces liquidity standards, both of which may require some banks to change their business models. These reforms will also require banks to undertake significant process and system changes to upgrade stress testing and their capital management infrastructure. In light of preparation for the implementation of Basel III, banks provided information on the impact of the Basel rules, their capital optimisation strategy, analysis and selection, risk profile and capital, management process enhancements, stress testing and contingency plans.

The EBA decided to undertake a thematic study to assess and compare the information disclosed by credit institutions about how they would be affected by the implementation of the Basel III, focusing on disclosures related to own funds. As there are currently no specific disclosure requirements on implementation of Basel III, the study performed by the EBA was not a compliance exercise, but rather a qualitative review of all relevant credit institutions' disclosures (annual report, Pillar 3 report, press releases and investors presentations) released mainly at 2011 year-end and Q1 2012. The purpose was to identify differences or commonalities across the EU such as what information banks chose to disclose and see how the information could be meaningfully disclosed. At the same time, best practices/principles that banks could follow for disclosures on Basel III preparation / impact were put forward.

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## 2. General observations

The complementary character of Pillar 3 and the nature of market discipline lead many supervisors to adopt a non-prescriptive approach for practical aspects of the publication of Pillar 3 information, such as timing, presentation formats or verification of disclosures.

### 2.1 Timeframe and frequency

The current CRD does not give a specific deadline for publication of Pillar 3 disclosures, but expects financial institutions to publish them as soon as practicable. It nevertheless empowers national supervisors to set deadlines. This practice has been adopted in three countries<sup>6</sup> (from a total of nine countries in this year's assessment sample), resulting in Pillar 3 information being published on or close to the date of publication of the annual report.

The actual publication dates of Pillar 3 disclosures still varied significantly between the banks in the sample, ranging from early March 2012 to the beginning of June 2012. Overall however, most banks published their Pillar 3 reports earlier compared to last year and closer to the date of their annual reports.

The efforts made by banks in this respect are important in the context of the forthcoming Basel III framework. Article 420 of the new CRR/CRD (Part Eight 'Disclosure by Institutions') indeed explicitly states that 'Annual disclosures shall be published in conjunction with the date of publication of the financial statements.' Due to this stricter legal approach, the EBA expects that if there is not simultaneous publication, then there is a further reduction of the time lag between the publication dates of the annual report and the Pillar 3 information.

Regarding the frequency of disclosures, the conclusions in the EBA's 2011 review are still valid, meaning that some supervisors require their banks to publish certain quantitative disclosures and significant changes to qualitative information more frequently than the minimum frequency set by the CRD (publication of Pillar 3 information annually at least)<sup>7</sup>.

### 2.2 Presentation and location

A majority of banks (around 58%) in the sample produced a stand-alone Pillar 3 report. Some banks (around 21%) presented their Pillar 3 disclosures in their annual reports. The other banks opted for a hybrid approach by producing a separate Pillar 3 document with various cross-references to the annual report. Some banks in the sample chose to publish remuneration related disclosures in a separate remuneration report that was sometimes published later than the publication date of the other Pillar 3 information. Given that remuneration disclosures are part of the Pillar 3 disclosure framework, the EBA would prefer to see full publication of all Pillar 3 information at the same time.

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<sup>6</sup> These countries are Germany, Spain and Italy

<sup>7</sup> Detailed conclusions with regards to frequency of disclosures can be found in the 2011 report under the following link (page 6) :  
[http://eba.europa.eu/cebs/media/Publications/Other%20Publications/Others/2011/EBA-BS-2011-132-\(Follow-up-review-of-banks--transparency-in-their-2010-Pillar-3-reports\)---FINAL.pdf](http://eba.europa.eu/cebs/media/Publications/Other%20Publications/Others/2011/EBA-BS-2011-132-(Follow-up-review-of-banks--transparency-in-their-2010-Pillar-3-reports)---FINAL.pdf)

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The CRD only requires Pillar 3 information to be disclosed publicly. All the banks included in the sample published the Pillar 3 information on their website, which is currently the best way to make information easily accessible.

Irrespective of the format chosen, the EBA would like to stress again the importance of clear links between Pillar 3 information and the annual report so that readers can find the complete set of disclosures. This concern has also been addressed in the CRR/CRD IV proposal, Article 421: ‘To the degree feasible, all disclosures shall be provided in one medium or location. [...] If a similar piece of information is disclosed in two or more media, a reference to the synonymous information in the other media shall be included within each medium. [...] If disclosures are not included in the financial statements, institutions shall unambiguously indicate in the financial statements where they can be found.’

### 2.2.1 Other considerations

Regarding the provision of the Pillar 3 information in English, two banks in the sample did not provide translations into English. This may however be justified by the mostly national/regional character of these bank’s business activities. In addition, four other banks had not (yet) provided an English version of their disclosures on remuneration requirements at the time this report was written.

## 2.3 Verification of the disclosures

According to Article 149 (d) CRD, Member States shall empower the competent authorities to require credit institutions to use specific means of verification for the disclosures not covered by statutory audit.

In all countries but one<sup>8</sup>, Pillar 3 disclosures are not required to be audited by an external auditor. Three banks had their Pillar 3 disclosures audited by an external auditor on a voluntary basis (e.g. on the assumption that audit work performed gives reasonable assurance to users of Pillar 3 information), one of which adopted this practice for the first time this year.

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<sup>8</sup> In Germany, an external audit of the processes for the determination and disclosures of Pillar 3 information (not equivalent to a certification of the content) is formally required. In Austria, the external auditor is required to perform similar tests, but in the broader context of the review of the overall control environment of the bank, thus including procedures to comply with the Basel capital requirements. Nevertheless, the results of this audit work, both in the case of Germany and Austria, are not disclosed to the public, but only to the national supervisor.

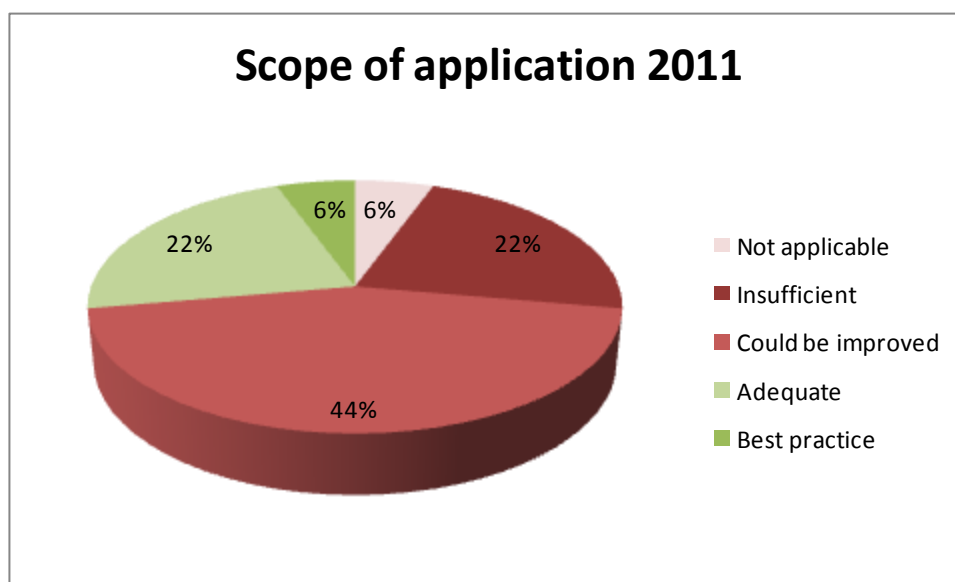
### 3. Findings on specific Pillar 3 disclosure areas

#### 3.1 Scope of application and own funds

##### 3.1.1 Scope of application

► Findings and observations

Table 1



Pillar 3 disclosures are required on a consolidated basis following the prudential rather than the accounting scope of consolidation. One of the banks in the sample presented its disclosures on an individual basis due to its structure. As a consequence, this year's analysis is limited to 18 out of the 19 banks in the sample.

In addition to disclosure under the prudential scope of consolidation, information that allows reconciliation with the accounting scope helps to convey the global risk profile of banking groups, especially with regard to risks posed by groups' non-banking financial activities (e.g. insurance) and equity participations in non-financial sectors.

The findings concerning the specific CRD requirements were as follow:

- As last year's assessment, all institutions provided clear identification of the reporting entity to which the Pillar 3 disclosures apply.
- A total of 78% of banks in the sample described both the accounting and the prudential scope of consolidation, providing an outline of the differences between the two scopes. This represents a considerable improvement compared to last's year assessment, where in some cases disclosures only provided a theoretical analysis of the differences in scope and failed to clarify whether such differences applied to the particular bank.
- Although 61% of the sample provided a detailed list of entities scoped out of the prudential perimeter or deducted from own funds, which is a significant improvement compared to last year's findings, it seems that there are still credit institutions that are reluctant to provide such information.

Moreover, no credit institution disclosed information on the implications (e.g. for capital or RWAs) of differences between the accounting and the regulatory consolidation scope

- A total of 78% of the sample disclosed information on impediments to the prompt transfer of own funds or repayment of liabilities by subsidiaries, this being a significant improvement compared with last year.
- Although not as significant as those noted above, improvement was also seen in disclosures on the shortfall in own funds compared to the required minimum for subsidiaries not included in the consolidation, with 61% of the banks in the sample providing such information.
- Still only half of the banks in the sample provided information on the exemptions from complying with capital requirements for some entities in the group.

▶ Best practice disclosures

The EBA identified the following best practice disclosures:

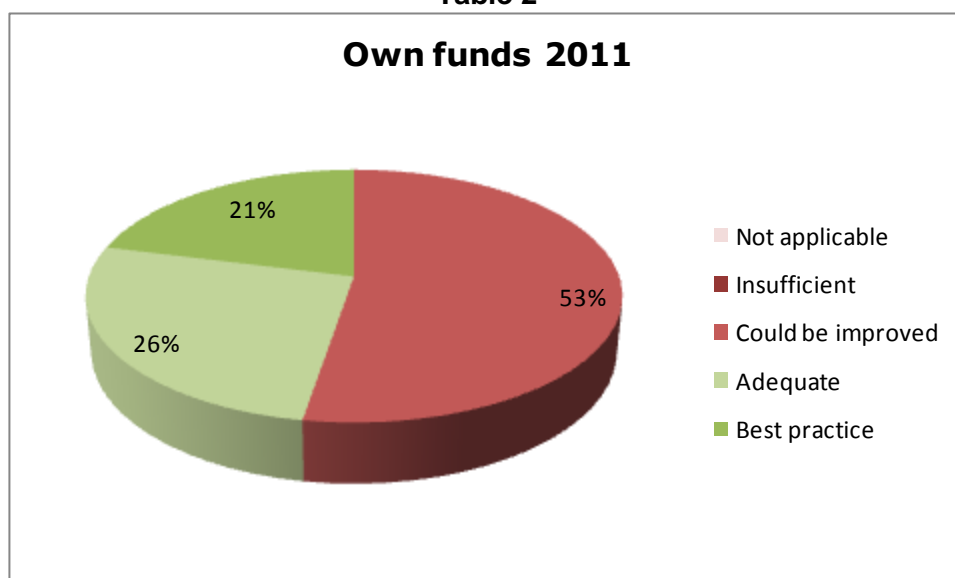
- Description of the evolution of the consolidation scope due to changes in the perimeter and corporate transactions (Santander, RZB).

### 3.1.2 Own funds

▶ Findings and observations

Almost half of the banks in the sample are broadly compliant with the main CRD requirements. However, the proportion of banks providing either adequate disclosures or best practice disclosures has decreased compared with last year's assessment (respectively 50% and 15% in the 2011 assessment of 2010 disclosures).

**Table 2**



This difference is due to some reports not being published in English (as mentioned above absence of information in English automatically leads to a lower score, regardless of the content) and due to a

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stricter application of the score approach, notably on the disclosure of information on the grandfathering of instruments.

Only 16% of the banks in the sample provided information on grandfathered instruments, but it is likely that this information is not relevant for some banks.

Despite the decrease noted in the percentage of the banks assessed as fully compliant, the disclosures provided in the area of own funds were assessed as sufficiently clear and extensive, with most banks providing details of the capital items and a meaningful breakdown of the deductions.

Nevertheless, where the banks were not fully compliant, there were no comprehensive qualitative details of the main features of the capital instruments (e.g. subordinated debts, innovative or grandfathered capital instruments), or the quantitative information on the breakdown of capital items contained insufficient details.

Sometimes the information on capital items was provided in cross-referred accounting sections in annual reports and the eligibility of these instruments in Tier 1 or Tier 2 was unclear.

Often the deductions were neither clearly explained nor sufficiently detailed; the amount was simply reported along with the effects on Tier 1 and/or Tier 2.

Some banks mentioned national regulation in quantitative templates, but they failed to explain the content of these regulations in the comments to the templates. Some further explanations would be welcome where waivers or specific rules are applied (e.g. the treatment of financial conglomerates according to the CRD or the treatment of insurance holdings).

Some banks use terms according to the current CRD framework, such as core Tier 1 or core capital, that were not always clear.

More than a third of the sample already provided a clear reconciliation between IFRS accounting equity and prudential own funds as recommended by the EBA and as it will be required in the next years under the new CRR.

The EBA has been working on Binding Technical Standards (BTS) for own-funds, including disclosures and reconciliation between prudential own-funds and accounting equity, to implement the related provisions of the CRR. These BTS will provide common definitions and templates. The implementation of these BTS will soon result in enhanced comparability in the own-funds disclosure area.

► Best practice disclosures

The EBA identified the following best practice disclosures:

- clear disclosures on the reconciliation between IFRS equity and prudential own funds (Barclays, HSBC, Royal Bank of Scotland, Deutsche Bank, Commerzbank, UBS, Intesa SanPaolo);

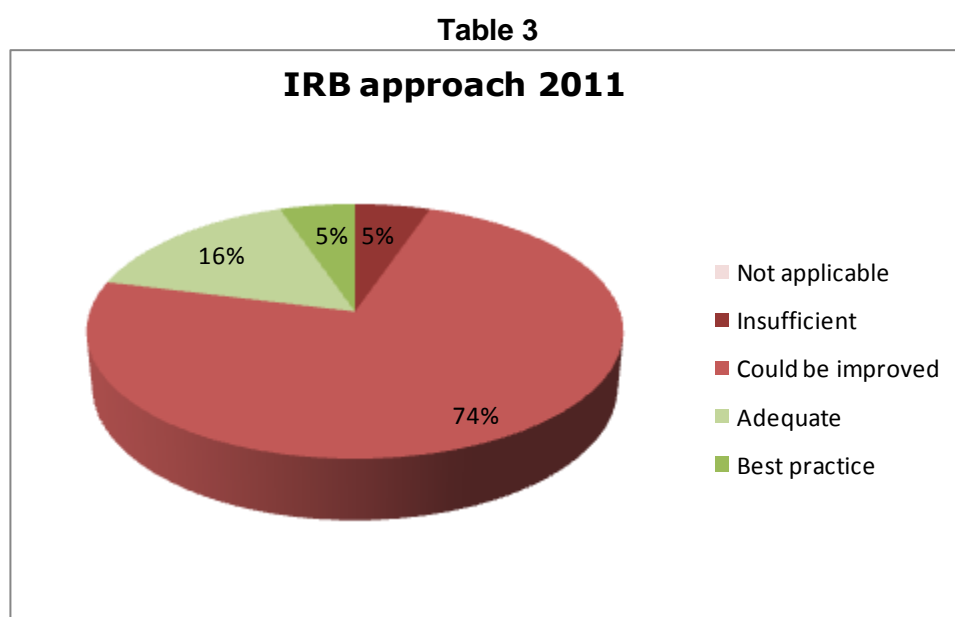
- informative disclosures on regulatory capital and its components (core Tier 1, Tier 1, Tier 2 and Tier 3, if any) (BBVA, Intesa SanPaolo, Commerzbank, Deutsche Bank);
- comments on changes compared to previous year (UBS, Crédit Agricole SA);
- details on the available for sale (AFS) revaluation reserves providing information on unrealised gains or losses that are recognised in the equity but not through the P&L account (Intesa SanPaolo, UniCredit Group);
- information on the results of the EBA recapitalisation exercise (ING).

## 3.2 Credit risk

### 3.2.1 Internal Ratings Based approach

#### ► Findings and observations

The analysis of the IRB Pillar 3 disclosures required by the CRD showed that disclosures provided by the majority of banks in the sample could be improved, similarly to last year.



The review showed that there was no significant improvement in the IRB disclosures in 2011 compared to 2010. As in last year's analysis (on the 2010 disclosures), half of the banks in the sample did not provide disclosures on back-testing, i.e. a comparison of estimate of losses against the actual losses over a period longer than one year. Some banks stated that such a comparison was not relevant, while 10% of banks in the sample disclose instead an EL/EAD (Expected Losses/Exposure At Default) ratio, following recommendation noted in the European Banking Federation report 'Driving alignment of Pillar 3 disclosures' from September 2008. A total of 79% of disclosures provided by sampled banks 'could be improved' or were 'insufficient'. This would fall to 42% if compliance with back-testing disclosure requirements were excluded.



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As for those banks which did provide back-testing information, only 20% of them presented comparisons between EL and actual losses, as well as between estimated PD (probability of default) and LGD (loss given default) versus actual values. In addition, only four institutions provided a comparison for a period longer than one year. Moreover, it was not always clear in the comparisons whether the actual losses were cumulative actual losses or actual losses incurred in the current year.

In general, the EBA considers that all disclosure items required by the CRD should be provided, regardless of how relevant credit institutions may consider them. The EBA also regards it as a best practice to disclose comparisons between actual losses against estimates of losses for a period of at least three years as best practice (see Annex II).

Room for improvements was also noted regarding the provision of actual losses, e.g. disclosure on impaired exposures. Almost half of the credit institutions in the sample did not disclose this piece of information, although almost all provided impairment disclosures for their credit exposures in total, without differentiating between those under the standardised or the IRB approach. In addition the disclosure of factors affecting the losses in the preceding period was often too generic and, in some cases, no information was provided. The EBA encourages credit institutions to report actual losses for the period under review accompanied by comparative data on the reported amounts for previous periods. As required by the CRD (see Annex II), every quantitative disclosures on losses should be supplemented by relevant qualitative information explaining any significant change between the current and previous periods amounts of losses (evolution of loss rates, but also other factors that may undermine comparability like changes of portfolios or modification of the IRB scope).

A total of 65% of the banks in the sample provided a rating scale to illustrate their internal rating procedure. Internal rating systems were usually described by exposure classes, with description of the rating process, methodologies and models applied and where relevant of the specific rating scale. One of the sampled banks also provided a description of the model used by its subsidiary.

While all banks disclosed information on the relationship between the internal ratings and the external ratings, there is a lack of meaningful disclosures providing a clear link between the internal model and the external ratings was not always given. The EBA considers it as a best practice to include a table, or a rating scale that clearly link the internal ratings/grades to the external ratings (see Annex II).

Most banks provided a clear description about the use of internal estimates other than for calculating risk-weighted exposure amounts including detailed information about where these estimates were used and about the control mechanisms for rating systems (approval of internal rating system; departments responsible for regularly reviewing the adequacy and integrity of the rating systems; development and implementation of new rating models).

With regards to the management and recognition of credit risk mitigation, 95% of the sample disclosed adequate explanations and reviews of the process for managing and recognising credit mitigation or the control mechanisms for rating systems, as well as quantitative information on personal guarantees, and collateral, and the use of credit derivatives, credit insurance and master netting agreements.

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The breakdown of exposure by obligor grades was satisfactory; nonetheless, the range of PD grades used by banks varied significantly from a minimum of only three grades to a maximum of twenty-seven grades. Similar variations are observed when EL ranges used for retail exposures. However, 70% of the sample uses between 6 to 15 PD and EL grades. The EBA considers that banks should use a meaningful number of PD or EL grades as required by the CRD (see Annex II).

Quantitative disclosures could also be enhanced, especially disclosures concerning conversion factors /undrawn commitments (respectively 55% and 30% non-compliance with these disclosure requirements), exposure-weighted average LGD (20% non-compliance), and average risk-weight (15% non-compliance). Moreover, it was not always clear whether credit institutions used their own estimates of LGD and / or CCF (credit conversion factor) since they did not mention it when disclosing this data. It tended also to be unclear whether exposures in default were included in the breakdown of exposures by obligor grade, especially when there were fewer grades displayed in the breakdown than in the rating scale.

Lastly, it was felt that in many cases, the basis for disclosures of figures (gross EAD, net EAD, IFRS values) could have been made clearer. The EBA considers bank should clearly state which disclosure basis they are using. Explanations are therefore provided on this issue in Annex II.

► Best practice disclosures

The EBA identified the following examples of best practice:

- clear disclosure of internal rating process (HSBC) and models with very clear link between internal ratings, default grades and external ratings outlined either through text or under a tabular format (Société Générale, Commerzbank, Santander, UBS, RZB, Royal Bank of Scotland, ING);
- identification of the scope of application of the IRB approach by subsidiary or portfolio (Société Générale, BBVA, Barclays, DZ Bank) and synthetic presentation of the types of models and / or parameters used (LGD, PD, CCF) by type of exposure (BCEE, UniCredit Group, Intesa SanPaolo, RZB, Erste Bank) ;
- educational approach with definition of the main concepts used under the IRB approach (Société Générale, Crédit Agricole SA, ING, HSBC) ;
- comparison between expected losses and actual losses over a longer period 2008 -2011 (Deutsche Bank);
- model performance that includes a comparison of expected and actual values for PD, LGD and EAD (HSBC);
- presentation of EL/EAD ratio following the recommendation of the EBF report 'Driving alignment of Pillar 3 disclosures' (Credit Agricole SA, Société Générale);
- EAD split by geographical area (Santander) accompanying a breakdown by industry sector (Royal Bank of Scotland);
- provision of both the accounting (balance sheet value or off-balance sheet pre-CCF value) and the EAD exposure value (BBVA, Santander, Unicredit, Société Générale, BNP Paribas, Credit Agricole SA);

- geographical breakdown of impaired exposures (BNP Paribas, Crédit Agricole SA) or impairment charges (HSBC);
- good disclosure of factors affecting impairment losses on assets (Santander);
- detailed information on the use of internal rating for purposes other than calculating risk-weighted exposure (DZ Bank).

### 3.2.2 Securitisation

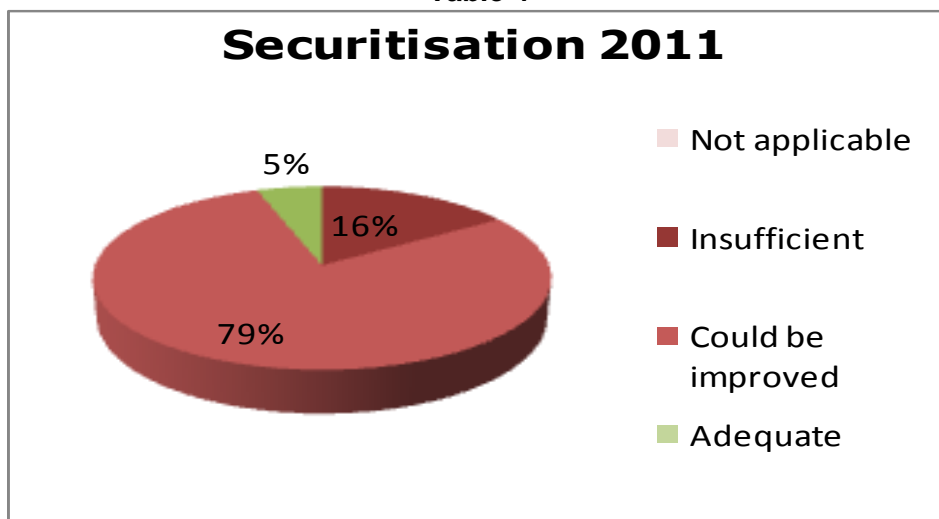
#### ► Findings and observations

In 2011, a significant number of new disclosure requirements regarding securitisation exposures were introduced, with the purpose of better reflecting the risks arising from securitisation and re-securitisation activities. These new requirements focused on exposures related to sponsoring activities and involvement in re-securitisation transactions, as well on the risks of securitisation exposures and on the ways they were managed.

Due to extensive modification of the requirements for disclosures on securitisation, any comparison here with the scores in the last year's assessment is not considered particularly relevant.

Overall, the EBA noted stability in the quality of credit institutions' disclosures related to disclosure requirements that were already in force the previous years. Nevertheless, there is room for improvement, especially in the disclosures related to the new requirements, with many of these remaining totally or partially unfulfilled, as reflected in the high number of 'could be improved' disclosures.

**Table 4**



All credit institutions provide adequate disclosures on the objectives and roles played in securitisation transactions, as well as on the methodologies for calculating own-fund capital requirements. Although the analysis found cases of non-disclosure of specific item/sub-items without relevant explanation, there were improvements noted compared to last year's assessment, such as clear statements that the absence of information stemmed from a lack of positions, especially for revolving exposures, assets awaiting securitization, and the absence of a hedging policy.

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Examples of non-compliance with qualitative disclosure requirements introduced by the CRD III were as follows:

- Disclosures on the risks inherent in securitised assets and attached to the seniority of re-securitisation positions were often missing or not fully detailed. There was also often non-compliance with the disclosures on the monitoring of market and credit risks and on hedging policies, or these disclosures were limited to short statements, providing little detail.
- A total of 90% of credit institutions assessed used the Internal Assessment Approach (IAA) where they acted as sponsor. However qualitative disclosures on IAA tended to have little detail, especially for control mechanisms and stress factors. This is in contrast with the qualitative disclosures regarding the application of IRB approach for other credit exposures, while the purpose of the new qualitative disclosures on IAA approach was to align qualitative information about securitisation exposures under internal approach with qualitative information about the other credit exposures under internal approach.
- There was no explanation provided for the different types of securitisation special purpose entities (SSPEs) listed by credit institutions when they had such exposures to or advised them. Moreover, the extent of this exposure was often undisclosed, and credit institutions tended not to distinguish between consolidated and non-consolidated SSPEs under a regulatory scope, especially if disclosures were cross-referred to annual report.

Examples of non-compliance with quantitative disclosure requirements introduced by the CRD III were as follows:

- Trading book exposures were omitted, without explanation, by almost a quarter of the sample.
- Although outstanding securitised amounts are provided by 85% of the sample, 60% of the banks – having both originator and sponsor activities – did not indicate whether they had exposures recorded under both originator and sponsor roles, and therefore it was unclear whether the sponsor activities disclosed were solely related to sponsor-only activities. In addition, 15% of credit institutions stating they acted both as sponsor and originator did not disclose figures for sponsor exposures separately without stating the reasons for not doing so (e.g. that there was no sponsoring activity during the specific reporting period).
- A total of 25% of disclosures on retained and purchased exposures did not always identify off-balance sheet exposures separately and no reason was given for this (e.g. not applicable, immateriality, other). Furthermore, half of the credit institutions did not disclose their retained exposures in the trading book.
- The number of exposure classes used for quantitative disclosures varies between five and seventeen, affecting comparability. A total of 65% of the sample used underlying exposure classes, and 35% of them made disclosures by security types (ABS asset-backed security, CDO collateralised debt obligation...) or provided the two sets of disclosures (underlying and security types).
- Capital requirements associated with the breakdown of exposures across risk-weight-bands were missing in 35% of the sample, which only provided a breakdown of exposures by risk-weight bands. Furthermore these disclosures sometimes lacked granularity, and the number of risk-weight bands varied from three to twelve across credit institutions, thus impairing comparability. In half of the sample no distinction was made between the different regulatory methods used for securitisation exposures and/or the different methods included in the IRB approach (RBA ratings-based approach, SFA supervisory formula approach, IAA).

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- Although re-securitisations often appeared in a separate exposure class, less than a third of the sample complied with the disclosure requirement regarding their hedging, or the breakdown per guarantor, while only 30% of the whole sample had no hedging policy, as either stated in the disclosure information or that could be inferred from it. The same goes for revolving exposures: most of credit institutions did not provide any disclosures, although only 60% of the sample had no exposure.

Moreover, there was still room for improvement regarding the following disclosure requirements already in force from the CRD II and that were also already assessed in last year's exercise:

- Disclosures on accounting policies too often referred to the main provisions of IAS 39 without any specific information on the credit institution's policy, and there was low compliance with the new requirements (assets awaiting securitisation, liabilities accounting).
- The content of disclosures on value adjustments was sometimes unclear (P&L charge or the stock of value adjustments).
- Disclosures on securitisation activities during the year were often made with no disclosure of related gains and losses.
- Reference was made to some provisions of national regulation without explaining them further.

In addition to these shortcomings related to specific requirements, there were also more structural issues to be noted, as below:

- Scope of disclosures: the scope of quantitative disclosures was not always clearly spelled out, and some credit institutions provided disclosures on an accounting rather than a prudential basis (e.g. including transactions without significant risk transfer and holdings of insurance companies).
- Exposure values: credit institutions did not always indicate the metrics of the exposure values they are using, especially for retained and purchased exposures, capital requirements, and impairment. Furthermore, for the same disclosure requirement, different institutions may have used different values, such as accounting values, EAD, RWAs (risk-weighted assets), par value of issued notes, or notional value exposure; this impaired comparability and may have led to data inconsistencies within a single report.
- Cross references: there was sometimes no cross-reference to disclosures included in the annual report even when these disclosure items are not included in the Pillar 3 report (especially for risk disclosures and disclosures on valuation of securitisation positions). Moreover, some of the cross-references provided were assessed as not adequate given that the information to which they referred was either irrelevant or could not be regarded as compliant with the regulatory framework, especially for disclosures on exposures to SSPEs.

For a few credit institutions (representing less than one quarter of the sample) in the sample, especially the non-internationally active ones, the reason for non-compliance with the new requirements may have been their limited securitisation activity regarding or the phasing out of their securitisation business.

More generally, the EBA believes that given the extent of non-compliance, at least part of it may come from lack of understanding of some items/sub-items due to their complexity, especially the ones introduced by the CRD III. Therefore some further explanations about the purpose of these requirements and on how they could be covered in the Pillar 3 reports would enhance compliance and

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result in greater consistency of securitisation disclosures across Europe. These explanations are provided in Annex II.

► Best practice disclosures

Despite these cases of insufficient compliance or cases where disclosures could be improved, the EBA identified some best practices:

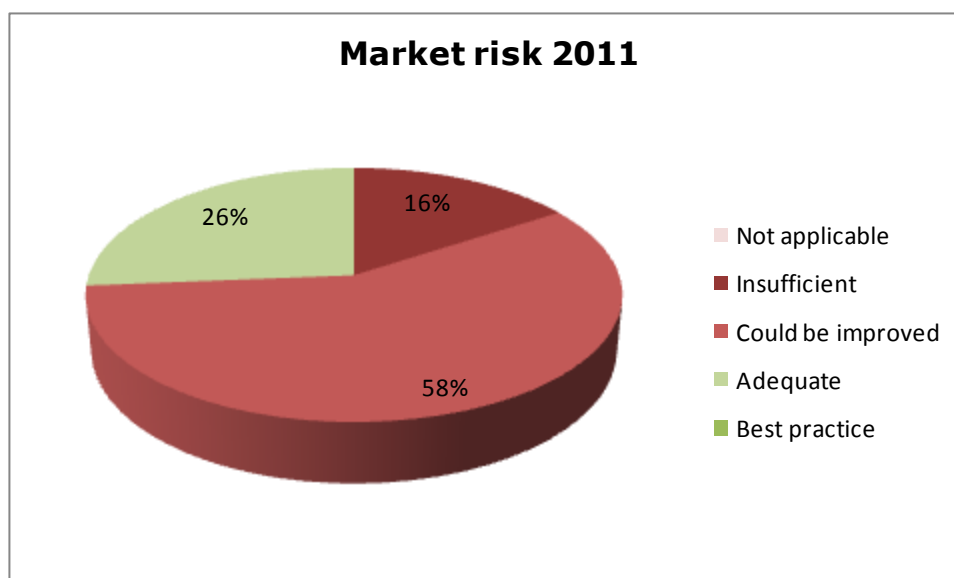
- information provided on prudential derecognition criteria (HSBC, Royal Bank of Scotland, ING) including for assets awaiting securitisation (BNP Paribas);
- separate disclosure of the retained part of the originated exposures (UBS, Santander) or of the retained exposures among the investor's retained and purchased exposures (HSBC, UniCredit Group, Intesa SanPaolo, Barclays);
- detailed disclosure on the extent of involvement in the transactions originated (Intesa SanPaolo, UniCredit Group, BBVA) and quantitative information on the extent of risk exposure to SSPEs (Intesa SanPaolo, UniCredit Group, DZ Bank, Royal Bank of Scotland, HSBC, ING, Commerzbank);
- geographical breakdown of securitised exposures (Intesa SanPaolo, UniCredit Group, Deutsche Bank, Société Générale, Santander);
- disclosure of RWAs associated with securitisation positions by underlying exposure classes (Société Générale);
- definition on the terms and concepts relating to securitisation transactions (Royal Bank of Scotland, Crédit Agricole SA, ING);
- breakdown of retained and purchased exposures by seniority tranche (Intesa SanPaolo, UniCredit Group, Santander, BNP Paribas, BBVA) and by credit rating (Intesa SanPaolo, Santander) with risk management disclosures not limited to credit and market risk (Royal Bank of Scotland, Rabobank).

### 3.3 Market risk

► Findings and observations

In 2011 there was a significant reshaping of market risk disclosures as new CRD Pillar 3 requirements were introduced, some of which replacing previous ones. The purpose of the new requirements was to identify the risks from trading book exposures in a better way. New requirements include disclosures on the new incremental risk charge, the comprehensive risk measure and stressed VaR, and disclosures on back-testing of internal models used to calculate market risk capital requirements.

Table 5



Approximately 26% (2009: 67%) of the banks in the sample complied with all market risk disclosure requirements. A total of 58% (2009: 25%) of the sample provided adequate information, but their disclosures could be improved. A total of 16% (2009: 0%) provided insufficient market risk disclosures. Areas where many banks' disclosures should be improved are summarised below.

Last year's assessment on 2010 Pillar 3 reports did not cover market risk disclosure requirements so the comparison is based on the EBA's scoring of market risk disclosures in the banks' 2009 Pillar 3 reports. The main reason for the fall in the number of banks complying with all market risk disclosure requirements in 2011 compared with 2009 is the introduction of a range of new or amended disclosure requirements, as many banks failed to cover, or adequately cover, all of these.

The main findings regarding the market risk disclosures in the Pillar 3 reports were:

- Breakdown of market risk capital requirements: some banks failed to provide breakdown of the capital requirement by risk type for portfolios under the standardised approach. Few banks provided an adequate breakdown of the capital requirement for portfolios under the internal models approach. Very few banks disclosed the capital requirements for specific interest rate risk of securitisation positions separately; moreover, none of the credit institutions that failed to comply with this requirement provided cross-references to the securitisation part of the Pillar 3 disclosures, even if they disclosed the relevant information in this part.
- Disclosures on the new incremental risk charge, the comprehensive risk measure and the stressed VaR measure: many banks using internal models to calculate the market risk capital requirement did not disclose adequate information relating to the incremental risk charge (capital charge for default and migration risk for debt securities) and comprehensive risk measure (capital charge for securitisation positions in correlation trading portfolios) in terms of the amount of the capital charge and the methodologies used. In addition, some banks provided insufficient or no information about stressed VaR.
- Back-testing of internal models used to calculate market risk capital requirements: some banks did not provide a comparison between the daily VaR measure and the daily gains and losses, or



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provided this comparison with insufficient detail. Other disclosure areas with ample scope for improvement included the need for a sufficiently detailed analysis of any significant overshooting. In addition, in many cases, banks that provided an overshooting analysis failed to disclose its impact of any overshooting on the models used, or details of any steps taken to adapt those models.

- Disclosures about stress testing: the EBA noted significant variations in the disclosures on stress testing. For example, some banks provided detailed descriptions of the stress scenarios used, while others were more general. Some banks disclosed quantitative information about their stress-testing outcomes, while other banks did not.
- Disclosures on valuation models and adjustments to achieve prudent valuation: some banks did not provide a disclosure on the extent of the use of valuation models and the different types of adjustments carried out to achieve prudent valuation, with the types of products to which they relate.
  - ▶ Best practice disclosures

The EBA identified the following best practice disclosures:

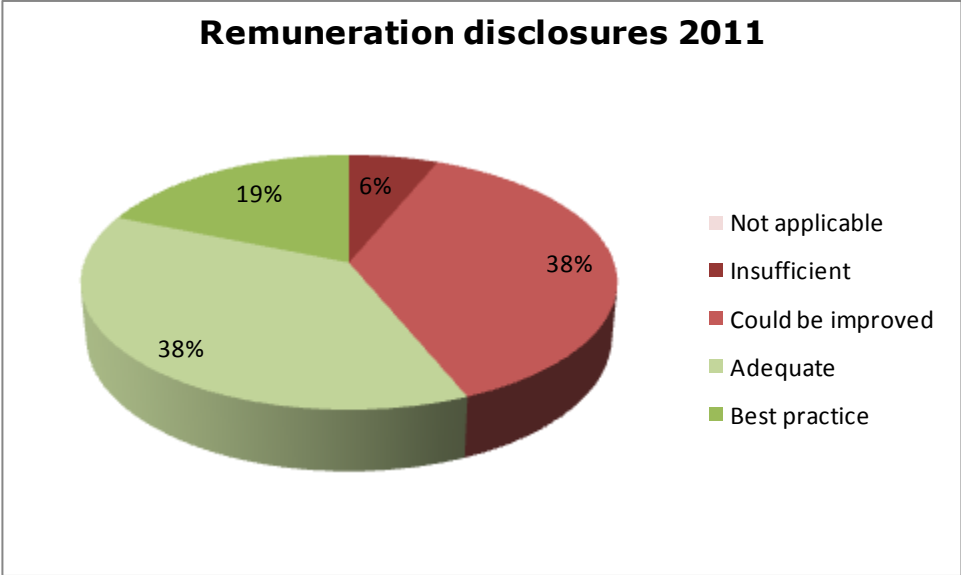
- disclosure of a disaggregated over-shooting analysis (Barclays); the EBA believes that it would be best practice for banks to provide a disaggregated over-shooting analysis beyond an analysis at group level, for example at business area or entity level;
- clear and detailed explanation of the internal model used or internal validation process (UniCredit Group);
- clear description of stress test and scenario analysis (UniCredit Group, Société Générale);
- detailed description of valuation and controls (Intesa SanPaolo);
- clear disclosures on VaR back-testing, analysis and clear explanation between P/L and VaR overshooting (UniCredit, Intesa SanPaolo);



### 3.4 Remuneration disclosures

► Findings and observations

Table 6



There were significant improvements in this area compared to last year’s assessment. No institution fully complied with the CRD requirements in that assessment, but this year 38% of the banks in the sample provided adequate disclosures, while 19% of the sample supplemented these adequate disclosures with best practices.

At the date this report was written, some banks had still not provided their disclosures<sup>9</sup>, which were thus very late compared to the publication dates of the annual and Pillar 3 reports. Some banks also provided related disclosures only in their national language. Nevertheless most of the remaining banks in the sample provided useful insight into the decision making process for setting the remuneration policy, and these banks described the main characteristics of the remuneration system, with notable enhancements such as the definition of staff whose actions have a material impact on the risk profile of the credit institution (‘material risk takers’).

In addition, more banks now described how measures adopted to take account of current and future risks in the remuneration process were linked to the overall risk management framework (e.g. the risk implications of the remuneration process, identified as best practice in last year’s assessment). However, remuneration disclosures were still often included in the annual report or a separate remuneration report rather than the Pillar 3 Report, and in some cases clear cross references were still missing.

<sup>9</sup> One bank (BCEE) is a state-owned company whose remuneration policies and practices are strictly governed by a law specific to the organisation and are subject to approval by the government. As such, this bank does not have to publish specific remuneration disclosures. In addition to this case, there are also two cases where the remuneration disclosures have not been published by the time EBA was finalised its assessment and as a result the current analysis doesn’t cover them.

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Although greater standardisation of disclosures in this complex and specialised area would be welcome (along with the simplification of some of the disclosures), there were significant improvements in the way banks provided remuneration information. The trend seems to be towards a less literal, checklist style approach to compliance, in favour of disclosures which try to capture the spirit of the requirements beyond their mere form.

Concerning quantitative disclosures, more institutions have provided information broken down by business area, as well as different components of remuneration for senior management and material risk takers.

► Best practice disclosures

The EBA identified two significant examples of best practice:

- comprehensive information on aspects of remuneration, such as compensation governance, compensation scheme and employees involved (Deutsche Bank);
- reconciliation of bonus pool to accounting costs recognized in the financial statements (UBS).

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## 4. Thematic study – Basel III implementation disclosures and disclosures on EBA 2011 capital exercise

### 4.1 Findings and observations

The thematic study of this year's analysis focuses on the one hand on Basel III implementation disclosures presenting the expected impact on credit institutions' own-funds, and on the other hand on credit institutions' disclosures on the EBA 2011 capital exercise, where applicable. A total of 64% of the banks in the sample provided information on the former issue and 53% on the latter.

#### 4.1.1 Presentation of disclosures

In most cases the relevant information was included in the capital disclosures sections in Q1 2012 publications (press releases, presentation slides, interim reports), while the 2011 publications were mostly focused on information presenting the impact of the CRD III implementation. Fewer than 25% of credit institutions provided disclosures in their Pillar 3 reports, and those which did often made cross-references to relevant sections of their annual reports. Regardless of how information was presented, disclosures on Basel III implementation and preparation plans for it were overall not highly developed and structured. The heterogeneity of information disclosed meant it was difficult to make comparisons between the credit institutions in the sample.

#### 4.1.2 Definitions of own funds elements

One of the most noticeable aspects of credit institutions' disclosures was the lack of definition of the concepts used. Credit institutions tended to use different concepts for Tier 1, Core Tier 1 and Common Equity Tier 1 (CET 1) when they provided information on the shifts in capital requirements imposed by the EBA 2011 capital exercise and the implementation of Basel III. However, hardly any of the credit institutions in the sample defined these concepts, and some even used them in a confusing way. For instance Common Equity Tier 1 (CET 1) ratios were presented under the Basel 2,5 / CRD 3 scope (although CET 1 is a concept introduced in the Basel III / CRD IV package), or disclosures were made on ways to retain an appropriate Core Tier 1 ratio under Basel III (whereas the Core Tier 1 ratio was a concept used within the framework of the EBA 2011 capital exercise)<sup>10</sup>.

#### 4.1.3 EBA 2011 capital exercise

Regarding the disclosures linked to the EBA 2011 capital exercise, around 50% of the banks in the sample provided a comparison between their estimate of the Core Tier 1 ratio versus the Core Tier 1 ratio calculated under the EBA methodology, or alternatively they disclosed their Core Tier 1 ratio under the EBA methodology as of the respective reporting date and compared it with the estimated ratio as of the deadline imposed by the EBA 2011 capital exercise. In doing so, 12% of the sample

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<sup>10</sup> Basel III Common Equity Tier 1 as per the definition provided in Article 24 of the CRR proposal. Core Equity Tier 1 as coined for the EBA capital exercise is defined as the CRD Tier 1 (ordinary shares or similar instruments) net of deductions of participations in financial institutions, less hybrid instruments including existing preference shares, plus hybrid instruments provided by governments as part of measures consistent with the European State aid rules and approved by the European Commission. Core Tier 1 instruments should be simple, issued directly by the institution itself and able, both immediately and without any doubt, to meet the criteria of permanence, flexibility of payments and loss absorption in going concern situations (EBA Capital buffers for addressing market concerns over sovereign exposures Methodological Note). For further details please refer to the EBA publication under the link <http://stress-test.eba.europa.eu/capitalexercise/Methodology%20FINAL.pdf>

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noted the differences between the ratios, and the impact due to the treatment of sovereign exposures, while 18% of the sample provided information on the capital gap that had to be covered to reach the EBA target. In addition, 27% of the credit sample accompanied the comparison with reconciliation, either between the Basel II ratio as of end 2010 and their EBA ratio as of end 2011 or the Basel 2,5 ratio and the EBA ratio for the same reporting dates. One institution only provided a statement that it met the EBA requirements with no disclosure on the resulting impact on its ratio.

#### 4.1.4 The implementation of Basel III

As for the implementation of the Basel III requirements, almost one third of the banks in the sample did not provide detailed information, but instead gave general statements about their ability to meet the future capital requirements. Nevertheless some credit institutions accompanied these statements with more detailed quantitative information about the impact of Basel III implementation, with the majority of the disclosures focusing on CET11, although with quite different disclosures which thus limited comparability. In some cases, disclosures on RWA were also provided.

For some institutions the disclosures were very granular, with information on the impact on the ratio in basis points and the increase in RWAs in nominal amounts for every new requirements introduced by the Basel III framework, for instance modifications of the Deferred Tax Assets (DTA), new minorities qualification regimes, introduction of the Credit Valuation Adjustment charge (CVA charge) or modification of the treatments of pension plans.

The main differences observed in Basel III implementation disclosures were as follows:

- lack of consistent use of ratios with no indication about the scope of the different ratios disclosed (Basel II, Basel 2,5, Basel III fully loaded or not, Basel III pro forma),
- varying degree of definition/details about the different adjustments applied in conformity with Basel III,
- differences in hypotheses retained in the calculations regarding adjustments (e.g. some assumed earnings generation whilst others did not, some included deduction of DTA and others did not) or in the hypotheses quantifying the impact on the ratio;
- the information disclosed did not always have the same reference day (e.g. some credit institutions provided their Basel III ratios as of year-end 2013, others as of the beginning of 2013)

#### 4.1.5 Observations relevant for both the EBA capital exercise and the implementation of Basel III

Almost all credit institutions in the sample, including those which did not provide any quantitative data, generally stated they had already met or would meet the EBA target and /or the Basel III capital requirements by or before the deadline. Some emphasized that they would achieve these targets without any governmental support. Around 20% of the sample limited their disclosures to such statements, but most provided details about measures taken to reach the various target ratios. Qualitative disclosures referred to the different capital measures taken by credit institutions (e.g. capital increase or issuance of other qualifying items, earnings retention, dividend payments, earnings generation, hybrid debts buy-backs, deleveraging, asset disposals, and also other structural changes like the change of models or modifying the IT infrastructure for supervisory reporting). Such

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<sup>11</sup> Only one credit institution discloses information on the impact of Basel III on its Tier 1 and total capital ratios.

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disclosures were sometimes quantified in basis points and/or in nominal amounts. Quantification was sometimes done on an aggregated basis (presenting the impact of all foreseen measures) or individually for each measure taken, and it was sometimes accompanied by the relevant calculation hypotheses.

Some of the measures taken to cover the new capital requirements were part of more global preparation, transformation or compliance plans to adapt the credit institution and its activities to the changing regulatory environment. All credit institutions, even those who did not provide the quantitative impact of the new capital requirements, disclosed information about such plans, but the granularity of disclosures varied significantly. Some only disclosed the fact that these plans were on-going and provided the global amount or the global percentage by which RWA had fallen since the last reporting date or listed some of the actions they had already taken. Others provided detailed disclosures about their deleveraging and transformation plans, with the amounts and types of assets sold by business line (e.g. legacy assets or even shares due to modification of consolidation scope), the resulting change in RWA and a comparison of how far they had fulfilled their initial objectives.

The impact of these plans on ratios may not be straightforward when it is not directly disclosed, or when the amount of RWA is not provided or not expressed under the Basel III scope.

Besides deleveraging and adaptation, for other transactions like reclassification of held-to-maturity (HtM) sovereign securities, buybacks of issued, debt or issue of new qualifying capital instruments, disclosures were often lacking about the resulting CET or RWAs gains.

► Best practice disclosures

The EBA identified the following examples of best practice:

- definition of Core Tier 1 (Société Générale, ING, Rabobank, Erste Bank, RZB, Commerzbank);
- description of the main Basel III provisions (HSBC, Royal Bank of Scotland, Barclays, ING, Rabobank, Société Générale, RZB);
- reconciliation between current ratios and Basel III ratios with disclosure of the assumptions underlying the assessment of the resulting impact (Société Générale, BNP Paribas, UniCredit Group, HSBC), while also providing granular information (Intesa SanPaolo) accompanied by two assessments (Barclays) or reconciliation between phased-in and full Basel III figures (Deutsche Bank);
- information on specific transactions like sales of legacy assets or HtM securities, disposal of a subsidiary, buy-backs of own-debts, issuance of new qualifying capital instruments (Erste Bank, RZB, Rabobank, Société Générale, Crédit Agricole SA, BNP Paribas, Commerzbank);
- quantitative information on deleveraging plans (BNP Paribas, UniCredit Group, Erste Bank, RZB, Rabobank, Barclays, Société Générale, Royal Bank of Scotland, Commerzbank) with figures like RWA expressed under a Basel III scope (Crédit Agricole SA, UBS).

Based on the above findings, the EBA believes credit institutions should consider the following recommendations in order to improve the quality of the Basel III implementation disclosures and increase comparability among credit institutions:

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- disclose qualitative and/or quantitative data with granular information on the expected impact of Basel III implementation (e.g. use of prudential filters, treatment of minority interest), possibly through extending of the scope of disclosures (e.g. not only impact on prospective CET 1 but also on prospective Basel III Tier 1 and Tier 2 ratios);
  - specify the differences between the ratios used and their scope of calculation, as required in section 91 of the December 2010 Basel Agreement;
  - disclose whether their Basel III figures are fully-loaded or phasing-in figures;
  - disclose the hypotheses underlying the calculation of anticipated effects.

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## Annex I – Sample for the 2012 assessment

a/a	Country	Credit institution
1.	AT	Erste Bank
2.	AT	RZB
3.	CH	UBS
4.	DE	Commerzbank
5.	DE	Deutsche Bank
6.	DE	DZ Bank
7.	ES	BBVA
8.	ES	Santander
9.	FR	BNP Paribas
10.	FR	Crédit Agricole SA
11.	FR	Société Générale
12.	IT	IntesaSanPaolo
13.	IT	UniCredit Group
14.	LU	BCEE
15.	NL	ING
16.	NL	Rabobank International
17.	UK	Barclays
18.	UK	HSBC
19.	UK	Royal Bank of Scotland

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## Annex II – EBA explanations on the purpose and expected content of specific Pillar 3 disclosure areas

Annex II aims at clarifying CRD requirements in areas where quality of disclosures could be improved. This additional explanation supplements the identification of best practices from credit institutions in the sense it aims at promoting better harmonization and comparability of banks' Pillar 3 disclosures on a voluntary basis.

The content of this section reflects the EBA's views about the purpose of different disclosure requirements and about the related expected disclosures. These views are expressed after consideration of existing material, such as the footnotes of the Basel Agreement or relevant private sector guidance, like the European Banking Federation reports 'Driving alignment of Pillar 3 disclosures' from September 2008, or 'Industry good practice guidelines on Pillar 3 disclosure requirements for securitisation' from December 2008 and January 2010. As a result, some content of this Annex may be very similar or identical to the above-mentioned material.

### Credit risk – Securitisation disclosures

#### Qualitative requirements (CRD requirement: Annex XII, Part 2, point 14)

- b) *The nature of other risks including liquidity risk inherent in securitised assets.*

Users of Pillar 3 reports should obtain a comprehensive view about the different kinds of risks attached to securitised assets, including but not limited to liquidity risk and credit risk. Risks should first be defined and then listed and clearly explained for each product/ asset class subject to securitisation (e.g. retail loans, mortgages, ABS). Explanations should include consideration of stress scenarios (possible scenarios where risks may occur in a particularly adverse way) and their impact on the securitised assets and ultimately on credit institutions depending on their role in the securitization transaction.

- c) *the types of risks in terms of seniority of underlying securitisation positions and in terms of assets underlying those latter securitisation positions assumed and retained with re-securitisation activity.*

Users of Pillar 3 reports should be provided with a comprehensive insight into the risks involved by re-securitisation exposures both in terms of transaction structure and underlying assets. Insight should also be provided on the compliance of the credit institution with its pre-investment analysis obligation laid down in Article 122a) CRD. For the main categories of re-securitisation products in which they have significant activities, credit institutions should describe the tranches of underlying securitisation exposures and their risks (nature and type of underlying assets, origination vintage, credit rating).



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- f) a description of the processes in place to monitor changes in the credit and market risk of securitisation exposures including, how the behaviour of the underlying assets impacts securitisation exposures and a description of how those processes differ for re-securitisation exposures.

Users of Pillar 3 reports should gain an insight into the rigor and soundness of the risk monitoring / managing processes implemented by credit institutions investing in securitisation products or holding securitisation positions. Credit institutions should describe the processes, tools and IT infrastructures they have in place (quantitative tools, valuation models and stress-tests of sufficient sophistication) to monitor risks and to ensure that information on securitisation transactions in their banking and trading books are updated in a timely manner. These descriptions should also provide information on concentrations and structural features and on how these processes and systems make it possible to track risks at different levels (deal, business lines...).

- g) A description of the credit institution's policy governing the use of hedging and unfunded protection to mitigate the risks of retained securitisation and re-securitisation exposures, including identification of material hedge counterparties by relevant type of risk exposure.

Users of Pillar 3 reports should be provided with an understanding of the hedging policy and be able to identify any potential resulting counterparty risk. Descriptions of hedging strategies should be entity-specific and be provided by different types of hedged exposures. Names of main guarantors/hedge counterparties should be provided and referenced to the main hedged exposures / risks that they hedge.

- i) the types of SSPE that the credit institution, as sponsor, uses to securitise third-party exposures including whether and in what form and to what extent the credit institution has exposures to those SSPEs, separately for on- and off-balance sheet exposures, as well as a list of the entities that the credit institution manages or advises and that invest in either the securitisation positions that the credit institution has securitised or in SSPEs that the credit institution sponsors;

The purpose of this requirement is to ensure there is adequate transparency regarding the sponsor and associated risks. Credit institutions should disclose separately, in a list or preferably in table form, the name, activities, types of assets and liabilities, consolidation status, and extent of their exposure to the SSPEs (securitisation special purpose entities) referred to in this requirement. This exposure can be provided qualitatively (types of exposures, scenarios under which the exposure is likely to increase or decrease, etc.), or quantitatively (amount of the different off and on balance sheet exposures, SSPE size...). Sponsored SSPEs should be identified individually. For funds credit institutions either manage or advised, money market mutual funds are to be listed individually while personal and private trusts should be listed collectively.

- j) a summary of the credit institution's accounting policies for securitisation activities [...]

Users of Pillar 3 reports should be provided with an explanation of where the accounting and regulatory treatments diverge on securitisation exposures. Regarding derecognition of securitised assets for example, detailed description should be provided for the criteria used to assess risk transfers under the regulatory framework and how they differ from the accounting criteria should be

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specifically disclosed. The same applies for the credit institution's rationales for both prudential and accounting consolidation/non-consolidation.

**Quantitative requirements** (CRD requirement: Annex XII Part 2, point 14)

Scope: for originator exposures, the scope of quantitative disclosures is only those transactions that qualify for regulatory de-recognition; as for sponsored transactions, they should be scoped-in regardless of whether they qualify for regulatory derecognition.

Exposure values: exposure values should be defined as:

- financial statement values gross of provisions, or
- regulatory exposure values calculated according to the CRD values after taking account of conversion factors but prior to the application of credit risk mitigations
- current amount of notes outstanding possibly drawn from investor reports or own valuations (when 1) or 2) is not available)

Credit institutions may apply the values listed in 1) or 2) for securitised exposures, revolving exposures and impairment disclosures, but credit institutions should apply 2) for their retained or purchased exposures.

Exposure types: securitisation exposures (securities, liquidity facilities, protection, credit enhancement, other commitments etc..) should be broken down by the underlying exposures (for instance mortgage, credit cards, securitisations) and by type of securities, such as RMBS (residential mortgage-backed securities), CMBS (commercial mortgage-backed securities), or CDO (collateralised debt obligations). Every asset class that makes up more than 10% of an aggregate exposure value should be individually identified. On and off-balance sheet exposures should be disclosed separately and re-securitisation positions should be clearly identified in every disclosure.

- n) separately for the trading and the non-trading book, the following information broken down by exposure type: i) the total amount of outstanding exposures securitised by the credit institution, separately for traditional and synthetic securitisations and securitisations for which the credit institution acts only as sponsor;

This disclosure requirement covers origination activities (of own assets or assets purchased from third parties) and involvement in securitisation transactions as sponsor. Where the credit institution acts both as originator and sponsor, assets should be disclosed under the originator activity if it is the sole asset provider to the securitisation scheme; if it is one of a number of asset providers in a scheme, the credit institution's assets should be disclosed under the originator activity and the whole transaction under the sponsor activity. In such cases, any double-counted assets should be clearly identified (separate line in the disclosure item or footnote).

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- n) separately for the trading and the non-trading book, the following information broken down by exposure type: ii) the aggregate amount of on-balance sheet securitisation positions retained or purchased and off-balance sheet securitisation exposures;

On and off-balance sheet exposures should be identified separately. Retained exposures in the trading book should also be disclosed separately under another disclosure requirement. Every holding amounting to 10% or more of total exposure should be disclosed separately.

- o) separately for the trading and the non-trading book, the following information: the aggregate amount of securitisation positions retained or purchased and the associated capital requirements, broken down between securitisation and re-securitisation exposures and further broken down into a meaningful number of risk-weight or capital requirement bands, for each capital requirements approach used;

Both exposure values and the associated capital requirements should be broken down by risk-weight bands (there should be a capital requirement by band). Disclosure of RWA can also be provided but they cannot be a substitute for disclosure of the capital requirements. Breakdown by risk-weight band should be done separately for on and off-balance sheets exposures. The breakdown should be carried out across a sufficient number of risk-weight bands, aligned on the number of risk-weight bands used for regulatory calculation, with separate disclosures of amounts under the 1250% weight. Disclosures should be provided in table form for each regulatory capital approach used, meaning for instance for each subset of the IRB approach used (IRBA, SFA, IAA, look-through, etc.).

- p) for the non-trading book and regarding exposures securitised by the credit institution, the amount of impaired/ past due assets securitised and the losses recognised by the credit institution during the current period, both broken down by exposure type.

The purpose of this disclosure item is to provide an insight into the credit quality of the underlying pools of securitisation transactions, and indicate the credit risk to which the originator remains exposed due to retained exposures. This disclosure item applies to all securitised assets in originated or sponsored transactions qualifying for regulatory derecognition that are past due or impaired according to accounting classifications. Losses (allowances, charge-offs or write-downs, recognition of liabilities for probable future financial support) should be recognised for an amount equal to the negative impacts on the P&L after considering the effect of offsetting and other qualifying credit protection under the prudential framework. Disclosures should be made separately by originator and sponsor, and for synthetic and traditional securitisations.

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## Credit risk - IRB approach

► CRD requirement: Annex XII, Part 3, point 1 (b):

The credit institutions calculating the risk-weighted exposure amounts in accordance with Articles 84 to 89 shall disclose an explanation and review of:

- (i) the structure of internal rating systems and relation between internal and external ratings;

A qualitative description of the structure of the internal rating system should be provided. There should be a right balance between the details and the clarity of the disclosures provided in relation to the structure of the rating system and of the various control mechanism in place. In addition, information that clearly explains the link between the internal rating system and external ratings should be provided. It would be preferable to include the information on how the internal ratings compare to the external ratings in a graph or a mapping table.

► CRD requirement: Annex XII, Part 3, point 1 (e)

The credit institutions calculating the risk-weighted exposure amounts in accordance with Articles 84 to 89 shall disclose for each of the exposure classes central governments and central banks, institutions, corporate and equity, and across a sufficient number of obligor grades (including default) to allow for a meaningful differentiation of credit risk, credit institutions shall disclose:

- (i) the total exposures (for the exposure classes central governments and central banks, institutions and corporate, the sum of outstanding loans and exposure values for undrawn commitments; for equities, the outstanding amount);

- (ii) for the credit institutions using own LGD estimates for the calculation of risk-weighted exposure amounts, the exposure-weighted average LGD in percentage;

- (iii) the exposure-weighted average risk weight; and

- (iv) for the credit institutions using own estimates of conversion factors for the calculation of risk-weighted exposure amounts, the amount of undrawn commitments and exposure-weighted average exposure values for each exposure class.

The purpose of this disclosure requirement is to show the aggregate credit volume broken down into the categories of claims and into adequate rating classes, including exposures that are in default.

The PD, LGD and EAD disclosures should reflect the effect of collateral, netting and guarantees/credit derivatives that meet the criteria for recognition under the CRD framework. The exposure value should be the EAD post credit conversion factor after regulatory on balance sheet netting and after credit risk mitigation. For credit institutions using their own estimates of conversion factors, to make the information comprehensible, it might be useful to disclose EAD estimates of the respective EAD categories, along with pre-CCF undrawn exposure to which the EAD relate.

In addition, the EBA would see as a best practice the provision of a reconciliation between the accounting on and off-balance sheet exposure values to the EAD, and where possible, disclose

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separately the effects of scope differences (for instance securitisation transactions that only qualify for prudential derecognition) and the effects of valuation differences (for instance offsetting of derivatives). It should also be specified whether the reconciliation is between net balance sheet exposure and gross EAD exposure, or between net balance sheet exposure and net EAD exposure.

The breakdown by a sufficient number of obligor grades (PD breakdown) is specific to each credit institution: the CRD does not provide for a masterscale with a minimum number of PD grades and their corresponding external rating grades. Credit institutions should apply a meaningful number of PD grades that is sufficient to provide a representative breakdown of the distribution of those grades used in the IRB approach. PD grades may be aggregated provided the breakdown remains representative of the distribution of grades used for the IRB approach. The number of PD grades applied should reflect the bank's risk management process and should be consistent with those used in their provisioning methodology. The EBA observed in its different Transparency reports that banks used from three to fourteen grades, with most using at least six grades.

► CRD requirement: Annex XII, Part 3, point 1 (g)

the actual value adjustments in the preceding period for each exposure class (for retail, for each of the categories as defined under point (c)(iv) and how they differ from past experience.

The purpose of this disclosure requirement is to show the change in value adjustments. In this context, value adjustments mean specific accounting impairment losses (i.e. impairment charges to the P&L as well as total write-offs. This quantitative disclosure for the period should be accompanied by comparative quantitative information at least from the previous year. Figures for impaired / past due exposures should be on an accounting basis. Disclosures should help users understand the risk profile of each of the credit institutions' portfolios.

► CRD requirement: Annex XII, Part 3, point 1 (h)

a description of the factors that impacted on the loss experience in the preceding period (for example, has the credit institution experienced higher than average default rates, or higher than average LGDs and conversion factors).

The purpose of this disclosure requirement is to indicate which significant factors had the most impact on the actual losses in the last period. Information disclosed has to provide users with the relevant context of valuation adjustment changes that occurred in each portfolio in the last period. It would be helpful to highlight any important differences between the assumptions and parameters used in the rating system and the factors that impacted the actual losses experience.

► CRD requirement: Annex XII, Part 3, point 1 (i):

The credit institutions calculating the risk-weighted exposure amounts in accordance with Articles 84 to 89 shall disclose the credit institution's estimates against actual outcomes over a longer period. At a minimum, this shall include information on estimates of losses against actual losses in each exposure class (for retail, for each of the categories as defined under point (c)(iv) over a period sufficient to allow for a meaningful assessment of the performance of the internal rating processes for each exposure class (for retail for each of the categories as defined under point (c)(iv). Where appropriate, the credit institutions shall further decompose this to provide

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analysis of PD and, for the credit institutions using own estimates of LGDs and/or conversion factors, LGD and conversion factor outcomes against estimates provided in the quantitative risk assessment disclosures above.

Credit institutions should disclose estimates of losses compared to the actual losses (i.e. losses incurred in P&L for impairment and upon exiting assets from balance sheet) for each exposure class. These should be accompanied by the explanation on the relationship between the estimated losses and actual losses, and any significant year-on-year movements. For the retail exposure classes, credit institutions should distinguish between the qualifying revolving retail exposures and other retail exposures, unless these portfolios are insignificant in size (relative to overall credit exposures) and the risk profile of each portfolio is sufficiently similar such that separate disclosure would not help users understand the risk profile of the credit institutions' retail business.

Credit institutions should provide the required information in line with their risk management practices — for example, if banks use 10-year data series for their risk management, they might choose to disclose the average default rates for each PD grade over that 10-year period. At a minimum the EBA expects credit institutions to disclose the actual losses versus the expected losses for the preceding three years.

## Market risk

- ▶ CRD requirement: Annex XII, Part 2, point 9

The credit institution calculating their capital requirements in accordance with Article 75(b) and (c) shall disclose those requirements separately for each risk referred to in those provisions. In addition, the capital requirement for specific interest rate risk of securitisation positions should be disclosed separately.

The purpose of this disclosure requirement is to give to users of Pillar 3 reports a breakdown of the risk drivers for market risk in the bank's trading book and the level of capital resources assigned to each one of these risk drivers.

- ▶ CRD requirement: Annex XII, Part 2, point 10

The following information shall be disclosed by each credit institution which calculates its capital requirements in accordance with Annex V to Directive 2006/49/EC:

a) for each sub-portfolio covered:

(i) the characteristics of the models used;

(ii) for the capital charges in accordance with points 5a and 5l of Annex V to Directive 2006/49/EC separately, the methodologies used and the risks measured through the use of an internal model including a description of the approach used by the credit institution to determine liquidity horizons, the methodologies used to achieve a capital assessment that is consistent with the required soundness standard and the approach used in the valuation of the model;

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(iii) a description of stress testing applied to the sub-portfolio;

(iv) a description of the approaches used for back-testing and validating the accuracy and consistency of the internal models and modelling processes.

Some credit institutions use internal models to determine the level of capital resources assigned to each underlying risk driver by portfolio. As models are built on assumptions that reflect how each bank deals with market risk, the purpose of this disclosure is to (i) identify clearly the characteristics of models used and stress testing carried out; and (ii) help users understand the facts behind the total level of capital resources.

The VaR models used are 99.9% 10-days models. Disclosures should provide a clear and comprehensive description of the risks assessed, and the assumptions and methodology used in internal model. For example, disclosures should give details about the use of historical data and the different assessment techniques used. It is also important to have a description of the limits of the model and mitigation strategies used by the bank to monitor model outputs.

Points 5(a) and 5(l) of Annex V to Directive 2006/49/EC refer to the use of internal models to calculate specific capital requirements (5a: incremental risk charge for incremental default and migration risks; 5l: capital charge for securitisation positions within correlation trading portfolios).

According to Point 2 and Point 4 of Annex V, credit institutions are required to perform daily back-testing to demonstrate the adequacy of their internal models and their capital requirements computed in this way. Data on the processes and the results of back-testing and stress tests should be disclosed or cross-referenced to other parts of the Pillar 3 report where they can be found, for example, under disclosure item (f) below.

c) a description of the extent and methodologies for compliance with the requirements in accordance with the requirements set out in Part B of Annex VII to Directive 2006/49/EC.

The purpose of this disclosure is to describe the methodologies used in the valuation process clearly and fully, including the different value adjustments used to achieve prudent valuation, thus allowing users to make informed decisions. So that users can be sure there is compliance with the requirement in part B of Annex VII to Directive 2006/49/EC, credit institutions should disclose at least the extent of the use of valuation models, the independent price verification processes including their frequency, and the different adjustments used (for example, to take into account model risk, illiquidity and size of positions), with the types of products to which they relate. A best practice would be disclosure of the quantitative effects of compliance with these requirements (e.g., the extent of price adjustments).

f) a comparison of the daily end-of-day value-at-risk measures to the one-day changes of the portfolio's value by the end of the subsequent business day together with an analysis of any important overshooting during the reporting period.

The purpose of this disclosure is to highlight any events that result in overshooting in the reporting period, thereby helping users understand and assess the limitations of the models. The analysis of any overshooting should provide the reasons for this in a clear and comprehensible way. Information

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should also be disclosed about on the steps taken in response to these occurrences, including what has been done to adjust the model where relevant. As a best practice, credit institutions could disclose the regulatory capital consequences of the overshooting events they experienced during the reporting period.



## Annex III Benchmark table

Credit institution:	Member performing the assessment:		Link to Pillar 3 report:	
CRD DISCLOSURE REQUIREMENTS	Score at time (Y)	EBA identified best practices from the 2011 report <sup>12</sup> and elements of attention	Summary description of disclosures and related observations / Assessment	Comparison to the previous assessment [with reference to the (Y-1) score]
<p><b><u>Scope of consolidation: Annex XII, Part 2, point 2 (a)-(e)</u></b>            The following information shall be disclosed regarding the scope of application of the requirements of this Directive:</p> <p>(a) the name of the credit institution to which the requirements of this Directive apply;</p> <p>(b) an outline of the differences in the basis of consolidation for accounting and prudential purposes, with a brief description of the entities that are:</p> <p>(i) fully consolidated;</p> <p>(ii) proportionally consolidated;</p> <p>(iii) deducted from own funds; or</p> <p>(iv) neither consolidated nor deducted;</p> <p>(c) any current or foreseen material practical or legal impediment to the prompt transfer of own funds or repayment of liabilities among the parent undertaking and its subsidiaries;</p> <p>(d) the aggregate amount by which the actual own funds are less than the required minimum in all subsidiaries not included in the consolidation, and the name or names of such subsidiaries; and</p> <p>(e) if applicable, the circumstance of making use of the provisions laid down in Articles</p>		<p>Some banks provided reconciliations between Pillar 3 and annual accounts</p> <p>Good practice proposed by S&amp;Ps: granular information on the implications (capital, RWA...) of the differences between the accounting and the regulatory consolidation scope, especially for financial conglomerates (issue of insurance subsidiaries)</p> <p>Good practice from the supervisory checklist: comment on the evolution of the consolidation scope</p>		

<sup>12</sup> These best practices are provided for illustration. They are also intended to facilitate the identification of other best practices.

Credit institution:	Member performing the assessment:		Link to Pillar 3 report:	
CRD DISCLOSURE REQUIREMENTS	Score at time (Y)	EBA identified best practices from the 2011 report <sup>12</sup> and elements of attention	Summary description of disclosures and related observations / Assessment	Comparison to the previous assessment [with reference to the (Y-1) score]
69 and 70.				
<p><b><u>Own funds: Annex XII, Part 2, point 3 (a)-(e)</u></b>  <i>The following information shall be disclosed by the credit institutions regarding their own funds:</i></p> <p>(a) <i>summary information on the terms and conditions of the main features of all own-funds items and components thereof; including instruments referred to in Article 57(ca), instruments the provisions of which provide an incentive for the credit institution to redeem them, and instruments subject to Article 154(8) and (9);</i></p> <p>(b) <i>the amount of the original own funds, with separate disclosure of all positive items and deductions; the overall amount of instruments referred to in Article 57(ca) and instruments the provisions of which provide an incentive for the credit institution to redeem them, shall also be disclosed separately; those disclosures shall each specify instruments subject to Article 154(8) and (9);</i></p> <p>(c) <i>the total amount of additional own funds, and own funds as defined in Chapter IV of Directive 2006/49/EC,</i></p> <p>(d) <i>deductions from original and additional own funds pursuant to Article 66(2), with separate disclosure of items referred to in Article 57(q);</i></p> <p>(e) <i>total eligible own funds, net of deductions and limits laid down in Article 66.</i></p>		<ul style="list-style-type: none"> <li>• a description of the changes related to the application of CRD II;</li> <li>• clear disclosures regarding the reconciliation between IFRS equity and prudential own funds;</li> <li>• informative disclosures on regulatory capital and its components (core Tier 1, Tier 1, Tier 2 and Tier 3, if any);</li> <li>• comments on changes compared with the previous year; and</li> <li>• a direct link between the capital structure and capital ratios</li> </ul>		

Credit institution:	Member performing the assessment:		Link to Pillar 3 report:	
CRD DISCLOSURE REQUIREMENTS	Score at time (Y)	EBA identified best practices from the 2011 report <sup>12</sup> and elements of attention	Summary description of disclosures and related observations / Assessment	Comparison to the previous assessment [with reference to the (Y-1) score]
<p><b><u>Securitisation: Annex XII, Part 2, point 14 (a) – (g)</u></b> <i>(new disclosure items added)</i></p> <p><i>The credit institutions calculating risk weighted exposure amounts in accordance with Articles 94 to 101 or capital requirements in accordance with point 16a of Annex I to Directive 2006/49/EC shall disclose the following information, where relevant, separately for their trading and non-trading book:</i></p> <p><i>(a) description of the credit institution's objectives in relation to securitisation activity;</i></p> <p><i>(b) The nature of other risks including liquidity risk inherent in securitised assets;</i></p> <p><i>(c) the types of risks in terms of seniority of underlying securitisation positions and in terms of assets underlying those latter securitisation positions assumed and retained with re-securitisation activity.</i></p> <p><i>(d) the different roles played by the credit institution in the securitisation process.</i></p> <p><i>(e) an indication of the extent of the credit institution's involvement in each of the roles referred to point (d).</i></p> <p><i>(f) a description of the processes in place to monitor changes in the credit and market risk of securitisation exposures including, how the behaviour of the underlying assets impacts securitisation exposures and a description of how those processes differ for re-securitisation exposures.</i></p>		<ul style="list-style-type: none"> <li>• information on the management of securitisation risks;</li> <li>• comprehensive breakdown by exposure type, geographical area and maturity, for securitisations carried out on behalf of clients;</li> <li>• definition of concepts;</li> <li>• comments on the evolution of the exposures and/or on impaired exposures;</li> <li>• amount of assets transferred but not derecognised; and</li> <li>• information on banks' securitisation exposures in the trading book and breakdown of retained exposures by accounting portfolio.</li> <li>• Provision of reconciliation tables and explanations for differences between Pillar 3 and annual reports (for instance consequences of the differences between the accounting and prudential derecognition rules</li> </ul>		

Credit institution:	Member performing the assessment:		Link to Pillar 3 report:	
CRD DISCLOSURE REQUIREMENTS	Score at time (Y)	EBA identified best practices from the 2011 report <sup>12</sup> and elements of attention	Summary description of disclosures and related observations / Assessment	Comparison to the previous assessment [with reference to the (Y-1) score]
<p>(g) <i>A description of the credit institution's policy governing the use of hedging and unfunded protection to mitigate the risks of retained securitisation and re-securitisation exposures, including identification of material hedge counterparties by relevant type of risk exposure.</i></p> <p>(h) <i>the approaches to calculating risk weighted exposure amounts that the credit institution follows for its securitisation activities including the types of securitisation exposures to which each approach applies.</i></p> <p>(i) <i>the types of SSPE that the credit institution, as sponsor, uses to securitise third-party exposures including whether and in what form and to what extent the credit institution has exposures to those SSPEs, separately for on- and off-balance sheet exposures, as well as a list of the entities that the credit institution manages or advises and that invest in either the securitisation positions that the credit institution has securitised or in SSPEs that the credit institution sponsors;</i></p> <p>(j) <i>a summary of the credit institution's accounting policies for securitisation activities, including:</i></p> <p style="padding-left: 20px;"><i>(i) whether the transactions are treated as sales or financings;</i></p> <p style="padding-left: 20px;"><i>(ii) the recognition of gains on sales;</i></p> <p style="padding-left: 20px;"><i>(iii) the methods, key assumptions, inputs and changes from the previous period for valuing securitisation</i></p>		<ul style="list-style-type: none"> <li>• Geographical breakdown of securitised exposures</li> <li>• separate identification in the relevant disclosure items of assets held in application of the 5% retention requirement.</li> <li>• quantification of the use of hedging for retained and purchased exposures and of guarantor concentration.</li> <li>• provision of information on the rating of securitisation exposures and their undelyings.</li> <li>• provision of the accounting classification or retained and purchased exposures.</li> <li>• Description of the accounting policies applied to securitisation activities to be bank-specific and not generic.</li> </ul>		

Credit institution:	Member performing the assessment:		Link to Pillar 3 report:	
CRD DISCLOSURE REQUIREMENTS	Score at time (Y)	EBA identified best practices from the 2011 report <sup>12</sup> and elements of attention	Summary description of disclosures and related observations / Assessment	Comparison to the previous assessment [with reference to the (Y-1) score]
<p><i>positions;</i></p> <p><i>(iv) the treatment of synthetic securitisations if this is not covered by other accounting policies.</i></p> <p><i>(v) how assets awaiting securitisation are valued and whether they are recorded in the credit institution's non-trading book or the trading book;</i></p> <p><i>(vi) policies for recognising liabilities on the balance sheet for arrangements that could require the credit institution to provide financial support for securitised assets;</i></p> <p><i>(k) the names of the ECAIs used for securitisations and the types of exposure for which each agency is used.</i></p> <p><i>(l) where applicable, a description of the Internal Assessment Approach as set out in Part 4 of Annex IX, including the structure of the internal assessment process and relation between internal assessment and external ratings, the use of internal assessment other than for IAA capital purposes, the control mechanisms for the internal assessment process including discussion of independence, accountability, and internal assessment process review, the exposure types to which the internal assessment process is applied and the stress factors used for determining credit enhancement levels, by exposure type;</i></p> <p><i>(m) an explanation of significant changes to any of the quantitative disclosures in points (n)</i></p>				

Credit institution:	Member performing the assessment:		Link to Pillar 3 report:	
CRD DISCLOSURE REQUIREMENTS	Score at time (Y)	EBA identified best practices from the 2011 report <sup>12</sup> and elements of attention	Summary description of disclosures and related observations / Assessment	Comparison to the previous assessment [with reference to the (Y-1) score]
<p><i>to (q) since the last reporting period;</i></p> <p><i>(n) separately for the trading and the non-trading book, the following information broken down by exposure type:</i></p> <p><i>(i) the total amount of outstanding exposures securitised by the credit institution, separately for traditional and synthetic securitisations and securitisations for which the credit institution acts only as sponsor;</i></p> <p><i>(ii) the aggregate amount of on-balance sheet securitisation positions retained or purchased and off-balance sheet securitisation exposures;</i></p> <p><i>(iii) the aggregate amount of assets awaiting securitisation;</i></p> <p><i>(iv) for securitised facilities subject to the early amortisation treatment, the aggregate drawn exposures attributed to the originator's and investors' interests respectively, the aggregate capital requirements incurred by the credit institution against the originator's interest and the aggregate capital requirements incurred by the credit institution against the investor's shares of drawn balances and undrawn lines;</i></p> <p><i>(v) the amount of securitisation positions that are deducted from own funds or risk-weighted at 1 250 %;</i></p> <p><i>(vi) a summary of the securitisation activity of the current period, including</i></p>				

Credit institution:	Member performing the assessment:		Link to Pillar 3 report:	
CRD DISCLOSURE REQUIREMENTS	Score at time (Y)	EBA identified best practices from the 2011 report <sup>12</sup> and elements of attention	Summary description of disclosures and related observations / Assessment	Comparison to the previous assessment [with reference to the (Y-1) score]
<p><i>the amount of exposures securitised and recognised gain or loss on sale.</i></p> <p>(o) <i>separately for the trading and the non-trading book, the following information:</i></p> <p style="padding-left: 20px;">(i) <i>the aggregate amount of securitisation positions retained or purchased and the associated capital requirements, broken down between securitisation and re-securitisation exposures and further broken down into a meaningful number of risk-weight or capital requirement bands, for each capital requirements approach used;</i></p> <p style="padding-left: 20px;">(ii) <i>the aggregate amount of re-securitisation exposures retained or purchased broken down according to the exposure before and after hedging/insurance and the exposure to financial guarantors, broken down according to guarantor credit worthiness categories or guarantor name;</i></p> <p>(p) <i>for the non-trading book and regarding exposures securitised by the credit institution, the amount of impaired/ past due assets securitised and the losses recognised by the credit institution during the current period, both broken down by exposure type.</i></p> <p>(q) <i>for the trading book, the total outstanding exposures securitised by the credit institution and subject to a capital requirement for market risk, broken down</i></p>				

Credit institution:	Member performing the assessment:		Link to Pillar 3 report:	
CRD DISCLOSURE REQUIREMENTS	Score at time (Y)	EBA identified best practices from the 2011 report <sup>12</sup> and elements of attention	Summary description of disclosures and related observations / Assessment	Comparison to the previous assessment [with reference to the (Y-1) score]
<i>into traditional/synthetic and by exposure type.</i> ;				



Credit institution:	Member performing the assessment:		Link to Pillar 3 report:	
CRD DISCLOSURE REQUIREMENTS	Score at time (Y)	EBA identified best practices from the 2011 report <sup>12</sup> and elements of attention	Summary description of disclosures and related observations / Assessment	Comparison to the previous assessment [with reference to the (Y-1) score]
<p><b>Remuneration: Annex XII, Part 2, point 15 (a) – (h)</b>  <i>The following information, including regular, at least annual, updates, shall be disclosed to the public regarding the remuneration policy and practices of the credit institution for those categories of staff whose professional activities have a material impact on its risk profile:</i></p> <p>(a) <i>information concerning the decision-making process used for determining the remuneration policy, including if applicable, information about the composition and the mandate of a remuneration committee, the external consultant whose services have been used for the determination of the remuneration policy and the role of the relevant stakeholders.</i></p> <p>(b) <i>information on link between pay and performance.</i></p> <p>(c) <i>the most important design characteristics of the remuneration system, including information on the criteria used for performance measurement and risk adjustment, deferral policy and vesting criteria.</i></p> <p>(d) <i>information on the performance criteria on which the entitlement to shares, options or variable components of remuneration is based.</i></p> <p>(e) <i>the main parameters and rationale for any variable component scheme and any other non-cash benefits.</i></p>		<ul style="list-style-type: none"> <li>• detailed description of the risk implications of the remuneration process; and</li> <li>• publication of remuneration disclosures in the Pillar 3 report (or separately but clearly cross-referenced to the report) so users can understand how remuneration is linked to an institution's risk strategy. Some banks disclose such prudential information elsewhere for different reasons, such as national requirements, and this is believed to impair that understanding.</li> <li>• information could be disclosed on the sensibility of the deferred component to: a) the degree of responsibility of the staff member; b) its impact on the credit institution's risk profile; and c) its absolute variable remuneration</li> </ul>		

Credit institution:	Member performing the assessment:		Link to Pillar 3 report:	
CRD DISCLOSURE REQUIREMENTS	Score at time (Y)	EBA identified best practices from the 2011 report <sup>12</sup> and elements of attention	Summary description of disclosures and related observations / Assessment	Comparison to the previous assessment [with reference to the (Y-1) score]
<p>(f) aggregate quantitative information on remuneration, broken down by business area.</p> <p>(g) aggregate quantitative information on remuneration, broken down by senior management and members of staff whose actions have a material impact on the risk profile of the credit institution, indicating the following:</p> <p>(i) the amounts of remuneration for the financial year, split into fixed and variable remuneration, and the number of beneficiaries;</p> <p>(ii) the amounts and forms of variable remuneration, split into cash, shares, share-linked instruments and other types;</p> <p>(iii) the amounts of outstanding deferred remuneration, split into vested and unvested portions;</p> <p>(iv) the amounts of deferred remuneration awarded during the financial year, paid out and reduced through performance adjustments;</p> <p>(v) new sign-on and severance payments made during the financial year, and the number of beneficiaries of such payments; and</p> <p>(vi) the amounts of severance payments awarded during the financial year, number of beneficiaries and highest such award to a single person.</p> <p>(h) Credit institutions shall comply with the</p>				

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<p><i>requirements set out in this point in a manner that is appropriate to their size, internal organisation and the nature, scope and complexity of their activities and without prejudice to Directive 95/46/EC.</i></p>				
<p><b>Market risk: Annex XII, Part 2, point 9</b></p> <p><i>The credit institutions calculating their capital requirements in accordance with Article 75(b) and (c) shall disclose those requirements separately for each risk referred to in those provisions. In addition, the capital requirement for specific interest rate risk of securitisation positions should be disclosed separately</i></p> <p><b>Market risk: Annex XII, Part 2, point 10 (a) – (f)</b></p> <p><i>The following information shall be disclosed by each credit institution which calculates its capital requirements in accordance with Annex V to Directive 2006/49/EC :</i></p> <p><i>(a) for each sub-portfolio covered:</i></p> <p><i>(i) the characteristics of the models used;</i></p> <p><i>(ii) for the capital charges in accordance with points 5a and 5l of Annex V to Directive 2006/49/EC separately, the methodologies used and the risks measured through the use of an internal model including a description of the approach used by the credit institution to determine liquidity horizons, the methodologies used</i></p>		<p><i>(from the 2010 report)</i></p> <ul style="list-style-type: none"> <li>• clear and comprehensive discussion of models used;</li> <li>• detailed description of valuation controls;</li> <li>• graphs of VaR over the period;</li> <li>• quantitative information on average, maximum and minimum VaR levels during the period (provided by several banks) as well as a comparison of the daily end-of-day VaR measures to the one-day changes of the portfolio's value; and</li> <li>• information provided on stressed scenarios considered as part of stress testing regime.</li> <li>• disclosure of any capital shortfall identified and reported to the supervisor when calculating capital</li> </ul>		

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<p><i>to achieve a capital assessment that is consistent with the required soundness standard and the approach used in the valuation of the model;</i></p> <p><i>(iii) a description of stress testing applied to the sub-portfolio;</i></p> <p><i>(iv) a description of the approaches used for back-testing and validating the accuracy and consistency of the internal models and modelling processes.</i></p> <p><i>(b) the scope of acceptance by the competent authority; and</i></p> <p><i>(c) a description of the extent and methodologies for compliance with the requirements set out in Part B of Annex VII to Directive 2006/49/EC.</i></p> <p><i>(d) the highest, the lowest and the mean of the following:</i></p> <p><i>(i) the daily value-at-risk measures over the reporting period and as per the period end;</i></p> <p><i>(ii) the stressed value-at-risk measures over the reporting period and as per the period end;</i></p> <p><i>(iii) the capital charges in accordance with points 5a and 5l of Annex V to Directive 2006/49/EC separately over the reporting period and as per the period-end;</i></p> <p><i>(e) the amount of capital in accordance with points 5a and 5l of Annex V to Directive 2006/49/EC separately, together with the weighted average liquidity horizon for each</i></p>		<p>requirements using VaR models and its consequences.</p> <ul style="list-style-type: none"> <li>quantitative disclosure of the valuation adjustments (difference between trading book accounting value and prudential value).</li> <li>disclosure of the regulatory capital consequences of the VaR overshooting experienced during the reporting period</li> </ul>		

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<p><i>sub-portfolio covered.</i></p> <p><i>(f) a comparison of the daily end-of-day value-at-risk measures to the one-day changes of the portfolio's value by the end of the subsequent business day together with an analysis of any important overshooting during the reporting period.</i></p>				

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<p><b>IRB approach: Annex XII, Part 3, point 1 (a) – (g)</b>  <i>The credit institutions calculating the risk-weighted exposure amounts in accordance with Articles 84 to 89 shall disclose the following information:</i></p> <p>(a) <i>the competent authority's acceptance of approach or approved transition.</i></p> <p>(b) <i>an explanation and review of:</i>  <i>(i) the structure of internal rating systems and relation between internal and external ratings;</i>  <i>(ii) the use of internal estimates other than for calculating risk-weighted exposure amounts in accordance with Articles 84 to 89;</i>  <i>(iii) the process for managing and recognising credit risk mitigation; and</i>  <i>(iv) the control mechanisms for rating systems including a description of independence, accountability, and rating systems review.</i></p> <p>(c) <i>a description of the internal ratings process, provided separately for the following exposure classes:</i>  <i>(i) central governments and central banks;</i>  <i>(ii) institutions;</i>  <i>(iii) corporate, including SMEs, specialised lending and purchased corporate receivables;</i>  <i>(iv) retail, for each of the categories of exposures to which the different correlations in Annex VII, Part 1, points 10 to 13 correspond; and</i></p>		<ul style="list-style-type: none"> <li>• clear presentation of the parameters by exposure classes including PD range (to allow for comparison), meaningful differentiation of credit risk, total amounts, comparative amounts (to highlight changes);</li> <li>• emphasis placed on key points (to explain the main changes and other important facts); and</li> <li>• user-friendly presentation of the rating process by exposure class.</li> <li>• Enhanced disclosures on concentration (debtor, geography).</li> <li>• Mapping of the internal rating scale on eight standard (or at least 4-5) buckets, comparable to the rating categories used by rating agencies and with a range for the probability of default (the lowest category would be for the defaulted assets)</li> <li>• Overview of exposures by the kind of approach followed.</li> </ul>		

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<p><i>(v) equities.</i>  <i>For the purposes of point (c), the description shall include the types of exposure included in the exposure class, the definitions, methods and data for estimation and validation of PD and, if applicable, LGD and conversion factors, including assumptions employed in the derivation of these variables, and the descriptions of material deviations from the definition of default as set out in Annex VII, Part 4, points 44 to 48, including the broad segments affected by such deviations.</i></p> <p><i>(d) the exposure values for each of the exposure classes specified in Article 86. Exposures to central governments and central banks, institutions and corporates where credit institutions use own estimates of LGDs or conversion factors for the calculation of risk-weighted exposure amounts shall be disclosed separately from exposures for which the credit institutions do not use such estimates.</i></p> <p><i>(e) for each of the exposure classes central governments and central banks, institutions, corporate and equity, and across a sufficient number of obligor grades (including default) to allow for a meaningful differentiation of credit risk, credit institutions shall disclose:</i>  <i>(i) the total exposures (for the exposure classes central governments and central banks, institutions and corporate, the sum of outstanding loans and exposure values for undrawn commitments; for equities, the</i></p>				

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<p><i>outstanding amount);</i></p> <p><i>(ii) for the credit institutions using own LGD estimates for the calculation of risk-weighted exposure amounts, the exposure-weighted average LGD in percentage;</i></p> <p><i>(iii) the exposure-weighted average risk weight; and</i></p> <p><i>(iv) for the credit institutions using own estimates of conversion factors for the calculation of risk-weighted exposure amounts, the amount of undrawn commitments and exposure-weighted average exposure values for each exposure class.</i></p> <p><i>(f) for the retail exposure class and for each of the categories as defined under point (c)(iv), either the disclosures outlined under (e) above (if applicable, on a pooled basis), or an analysis of exposures (outstanding loans and exposure values for undrawn commitments) against a sufficient number of EL grades to allow for a meaningful differentiation of credit risk (if applicable, on a pooled basis).</i></p> <p><i>(g) the actual value adjustments in the preceding period for each exposure class (for retail, for each of the categories as defined under point (c)(iv) and how they differ from past experience.</i></p> <p><i>(h) a description of the factors that impacted on the loss experience in the preceding period (for example, has the credit institution experienced higher than average default</i></p>				



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<p><i>rates, or higher than average LGDs and conversion factors).</i></p> <p><i>(i) the credit institution's estimates against actual outcomes over a longer period. At a minimum, this shall include information on estimates of losses against actual losses in each exposure class (for retail, for each of the categories as defined under point (c)(iv) over a period sufficient to allow for a meaningful assessment of the performance of the internal rating processes for each exposure class (for retail for each of the categories as defined under point (c)(iv). Where appropriate, the credit institutions shall further decompose this to provide analysis of PD and, for the credit institutions using own estimates of LGDs and/or conversion factors, LGD and conversion factor outcomes against estimates provided in the quantitative risk assessment disclosures above.</i></p> <p><b><u>Annex XII, Part 2, point 8</u></b></p> <p><i>The credit institutions calculating the risk-weighted exposure amounts in accordance with Annex VII, Part 1, points 6 or 19 to 21 shall disclose the exposures assigned to each category in Table 1 in point 6 of Annex VII, Part 1, or to each risk weight mentioned in points 19 to 21 of Annex VII, Part 1.</i></p>				