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Our response to the EBA consultation paper on draft implementing technical standards on supervisory reporting requirements for leverage ratio (EBA/CP/2012/06)

Introduction

The Building Societies Association (BSA) represents mutual lenders and deposit takers in the UK including all 47 UK building societies. Mutual lenders and deposit takers have total assets of over £375 billion and, together with their subsidiaries, hold residential mortgages of over £235 billion, 19% of the total outstanding in the UK. They hold more than £250 billion of retail deposits, accounting for 22% of all such deposits in the UK. Mutual deposit takers account for 34% of cash ISA balances. They employ approximately 50,000 full and part-time staff and operate through approximately 2,000 branches.

The BSA is a member of the European Mortgage Federation, and contributed to, and supports, the EMF's response to this consultation dated 22 August.

Summary

We support efforts to introduce global standards of **leverage** for deposit takers and appreciate the need of regulators for accurate, comparable, relevant and timely information to enable them to supervise and monitor risks.

Like our members, we are keen to engage with the European Banking Authority to ensure that the business of mutually-owned deposit takers, in particular their low risk business models and mutual ownership structures, are properly understood.

We understand the rationale behind the proposal to apply a backstop measure such as a leverage ratio – of total assets to capital - and therefore are open to the concept of such ratios, though it is open to the twin objections that it adds little further value if run in parallel with the existing risk-weighted asset methodology, and it is too crude to be an alternative (nor is that proposed). A single leverage ratio also creates perverse incentives for low-risk business models such as mortgage lending, as it may easily become the binding constraint rather than a backstop. The BSA therefore supports the position of the European Parliament in its compromise text which calls for a tiering of leverage ratios differentiated by riskiness of business model. But any reasonable measure that limits unsustainable growth, and helps avoid repeating the current contraction of liquidity and consequent financial crisis, deserves consideration.

We note the intention to incorporate the reporting of the leverage ratio into COREP but consider that all requirements including templates should be finalised, agreed and integrated before anything goes live. It is not helpful for institutions to have to build systems to deliver new reports in such a piecemeal fashion.

Mutuals such as building societies do not create derivatives, so while we agree that derivative activity needs to be captured, we do not offer a methodology for doing so, though we would point out that derivatives subject to effective netting arrangements should be included on a net, rather than a gross basis. We would also like to see a possible distinction in any leverage calculation between the treatments of derivatives as part of a trading book, and derivatives used (as UK mutuals such as building societies use them) only for hedging purposes to manage and reduce risk.

Q1: **Do institutions agree with the use of existing and prudential measures? Is there additional ways to alleviate the implementation burden?**

We understand that the EBA has tried to reduce the reporting burden on institutions and to draw on information that is already reported to avoid double reporting. To that end, it has proposed that the leverage ratio be reported as part of the COREP framework. This will mean the same fields will be used but with different reporting frequencies for some templates.

As the EBA has acknowledged itself, one problem with tying the framework with COREP is that COREP has not yet been finalised or agreed (though in the UK, the national authority, the FSA, has confirmed it will implement it from 1 July 2013).

Another potentially more significant problem is the fact that the leverage ratio reporting requirement is based on quarterly averages of monthly data, whereas COREP is based on quarterly reporting. This means that institutions will need to have the data available in the same format on a monthly basis unless the national authority grants a waiver. We do not see what added benefit this calculation brings to regulators. The leverage ratio was meant to be a simple backstop measure; it now appears to be more complicated. One remedy is to calculate the leverage ratio at the end of a quarter. So, in common with the EMF, we call for end of quarter reporting only.

We understand that the template for the ratio is similar to – but not the same as - the one used in the QIS using, where possible, the same fields. For those larger institutions that are taking part in the QIS, a mapping for to the COREP templates might be helpful (at the public meeting EBA said that the DPM will help here).

Our members tell us that many more items are required to be reported than are needed to calculate the ratio. For example, one member tells us that half the LR form is not required for the calculation and is reported elsewhere eg on LR 3, 4, 6 and 8. Indeed LR 8 is about encumbrance rather than leverage so we question its inclusion here. We support the proposal to collect information on encumbrance but consider that it should be part of another reporting framework. If the EBA does go ahead and expands the fields requested beyond those that are required to calculate the leverage ratio, we suggest that the costs of this decision are separately calculated and disclosed.

In addition, it would useful for institutions if the EBA could incorporate a general principle allowing firms not to populate fields that are clearly immaterial or allowing them to adopt a simplifying calculation where the difference would not be material. For example, the requirement to include mortgage interest receipts or operational expenses could result in significant additional costs for firms without providing any significant benefit for the regulator.

Q2: **Do institutions already have the data required under this proposal on a monthly basis? If so, is this data of the required standard as other data reported to supervisory authorities?**

Some of our members have told us that they do have the data – though it was suggested at the EBA public meeting, however, that some institutions produce this data at the end of a quarter only. The EMF response indicates that across the rest of the EU *most* credit institutions do *not* have the required data on a monthly basis.

Q3: **The same timelines are proposed for reporting on a consolidated level as well as on an individual level, is this seen as problematic? If so, would you propose a different timeline for reporting on a consolidated level?**

We understand that those institutions reporting on a consolidated level will require longer submission periods – basically to facilitate manual intervention - for the leverage ratio (as they will with the liquidity coverage ratio).

Q4: **What additional costs do you envisage from the proposed approach to reporting the leverage ratio in order to fulfil the requirements of the CRR outlined in this ITS?**

Our members are best placed to answer this. Their main costs will be in systems set-up, ongoing costs, maintenance and review of reported data.

EBA remarks that the costs are not envisaged to be “over and above those incurred if the leverage ratio reporting templates were constructed in an alternative manner. In fact, without the extensive re-use of information from COREP templates, presumably the operational costs would be significantly higher.” Rather than make such a bald statement, we consider it would be more helpful if the EBA carried out a thorough cost benefit analysis. This is especially pertinent given 8,000 institutions are expected to be affected. Requiring the reporting of the ratio, particularly while the CRD/CRR package and COREP templates are not finalised, is an expensive activity for institutions. They have to install systems that are flexible enough to cope with this uncertainty; some may have to install completely different systems if there are significant changes in the final CRD/ CRR.

Q5: **Is the calculation of the derivatives share threshold sufficiently clear?**
Q6: **Do you believe this method captures institutions derivatives exposure in a sensible way?**

We welcome the fact that the EBA has decided to address proportionality in some respect and consider whether all institutions should report everything. It has focused on derivatives given the large number of cells in the template that are dedicated to such data – and despite these positions representing only a fraction of the leverage ratio total exposure for the majority of institutions.

To effect this, the EBA has decided that institutions need provide detailed data on derivatives only if they exceed certain thresholds: dividing the leverage ratio exposure value for derivatives by the leverage ratio total exposure measure. It has proposed that a threshold range for derivatives reporting should, initially at least, be within the range of 0.5% to 2.0%.

The EBA notes that the proposal to use the COREP templates for reporting and monitoring leverage ratio data runs the risk of producing different datasets for exposures under the standardised and IRB approaches for credit risk (COREP uses different templates for the two approaches). To address this, the EBA proposes adding fields to the COREP templates. We question this: it seems at odds with the aim of reducing the reporting burden through proportionality, especially when more fields mean more costs. The EBA says this extra data are needed to provide granularity for analysis purposes – again we are concerned that the backstop nature of the ratio may be clouded should the data (and analysis) become unduly complex.

In the UK, mutuals such as building societies do not create derivatives, so while we agree that derivative activity needs to be captured, we do not offer a methodology for doing so, though we would point out that derivatives subject to effective netting arrangements should be included on a net, rather than a gross basis.

Q7**: Does the reduction of fields to be reported in a given period by institutions that do not exceed the threshold value in that period, lead to a significant reduction in administrative burden?**

To cover instances where, for example, an institution is under the threshold in one period and over it the next, there would be no significant reduction as the systems set-up costs would still be incurred. A way to get over this would be to include a buffer.

While the reduction of fields is, of course, welcome, we consider that further alleviation of the administrative burden could be made by aligning all aspects of the leverage ratio calculation and reporting with COREP. Again, a cost benefit analysis would inform the EBA on this point.

It would have been helpful to have the data point model which aims to explain how the leverage ratio reporting requirement interfaces with COREP. Without this either, it is hard to make a judgment on administrative burdens.

Q8: **Preliminary internal calculations by supervisors suggest that a threshold value should be in the range of 0.5% to 2%. Would you suggest a different threshold level, if yes, please justify this?**

We would like to see a possible distinction in any leverage calculation between the treatments of derivatives as part of a trading book, and derivatives used (as UK mutuals such as building societies use them) only for hedging purposes to manage and reduce risk. If this happened, then we believe the threshold value for derivatives used only for hedging could be raised to 5%.

Q9: **Is the calculation of the nominal amount threshold sufficiently clear?**

Our members have not informed us otherwise.

Q10: **Preliminary internal calculations by supervisors suggest that the nominal threshold value should be in the range of €200 to 500 million. Would you suggest a different threshold level, if yes, please justify this?**

We support this nominal threshold value but suggest it is reviewed periodically.

Q11: **Is the term "reference name" and the distinction from "reference obligation" sufficiently clear?**

Our members have not informed us otherwise.

Q12: **Is the treatment of credit derivatives referring to indices and baskets sufficiently clear?**

Our members have not informed us otherwise.

Q13: **Which additional contractual features should be taken into consideration when assessing offsetting of written and purchased credit derivatives? How would this add to complexity and reporting burden?**

Building societies in the UK are not permitted to write derivatives. For that reason, we do not comment.

Q14: **Is the classification used in template LR6 sufficiently clear?**

Our members have not informed us otherwise.

Q15: **Do you believe the current split, which is predominantly based on the exposure classes for institutions using the standard method are appropriate or would you suggest an alternative split?**

Many of the fields are not strictly required in order to calculate the leverage ratio and in some cases are already included in other regulatory reporting. Therefore we would suggest that this split is unnecessary.

Q16: **Is the classification used in template LR7 sufficiently clear?**

Our members have not informed us otherwise.

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