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Revised Pillar 3 Disclosure Requirements

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Summary

In January 2015, the Basel Committee on Banking Supervision (the “Committee” or “BCBS”) published its final framework on the revised Pillar 3 disclosure requirements for credit risk, counterparty credit risk (CCR), securitization, and market risk. This framework incorporates the feedback received on a June 2014 consultative paper, “Review of the Pillar 3 Disclosure Requirements.” It applies to internationally active banks and replaces the existing Pillar 3 disclosure requirements, which were introduced in 2004 as part of Basel II and were then revised in 2009 as part of Basel 2.5.

The key objective of this revision is to ensure comparability and consistency of disclosures across banks. It enables market participants to access key information about a bank’s overall regulatory capital, compare that information with the bank’s peers, and make more informed investment decisions. To achieve this objective, the Committee introduced harmonized templates with a number of standardized definitions. A hierarchy of disclosures was also introduced to balance the use of mandatory templates that promote consistency and comparability of reporting across banks, with senior management flexibility to provide views on a bank’s specific risk profile. The hierarchy includes fixed and flexible templates, and flexible tables. The fixed templates are to be completed with quantitative information that is considered essential for the analysis of a bank’s regulatory capital requirements. The flexible templates are to be completed with quantitative information that is considered meaningful to the market, yet is not central to the analysis of a bank’s regulatory capital. The flexible tables provide qualitative information primarily, which in a few cases may be supplemented with quantitative information. Banks are also expected to provide a qualitative commentary that explains significant changes between the reporting periods and a voluntary commentary from the senior management on the bank’s specific circumstances and risk profile.

The revised framework, which will take effect from year-end 2016, offers the following key improvements over the existing Pillar 3 disclosure requirements:

» Requires banks to publish Pillar 3 reports in a separate document that serves as a readily available source of prudential data for users.

» Ensures consistency and comparability of disclosures across banks through greater use of templates for key quantitative data and by standardizing a number of key definitions.

» Introduces consistency in the frequency and timing of publication of Pillar 3 reports.

» Links banks’ financial statement line items and regulatory exposure data in their Pillar 3 reports.

» Requires Pillar 3 information to be subject to, at least, the same level of internal review and control processes as the information provided by the banks in their financial reporting.

A detailed summary of changes from the existing framework is available in appendix A.

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1. Background

The Basel Committee published a consultative document on the "review of the Pillar 3 disclosure requirements" in June 2014, with the aim of enhancing market discipline through effective disclosures and promoting a sound and safe banking system. This document highlighted weaknesses of the existing disclosure framework and proposed ways to promote consistency and comparability of disclosures across banks. After incorporating the feedback received on this consultation, the Committee released its final framework on revised Pillar 3 disclosure requirements in January 2015. The revised framework will be enforced concurrently with banks' financial reports for the year-end 2016. The Committee encourages early adoption by individual jurisdictions.

2. Scope of the Framework

The revised Pillar 3 disclosure requirements framework has the following scope:

» It will apply to internationally active banks at the top consolidated level and will replace the existing Pillar 3 disclosure requirements for credit risk, CCR, securitization, and market risk. These requirements were introduced as part of Basel II in 2004 and were then enhanced in 2009 as part of Basel 2.5.

» It will complement the disclosure requirements, issued separately by the Committee, for liquidity coverage ratio[1], leverage ratio[2], remuneration[3], composition of capital[4] and global systemically important banks[5].

» Disclosure requirements for operational risk and interest rate risk in the banking book are not part of this framework and will be updated in phase 2 of the review by the Committee.

3. Need and Objectives

A revised disclosure framework was needed due to the following weaknesses in the existing disclosure regime:

» Lack of consistency and comparability of disclosures across banks regarding the form and granularity of the information disclosed, and in the interpretation of disclosure requirements.

» Failure to promote identification of a bank's material risks and provide sufficient, and sufficiently comparable, information to market participants.

» Variability in the medium and location of disclosures and lack of clear sign posting[6] between financial and Pillar 3 reporting. This variability often resulted in disclosures spread across financial reports and Pillar 3 reports and created difficulty for users in locating them.

» Lack of consistency in the frequency and timing of publication of Pillar 3 reports across banks and jurisdictions.

» Concerns about the opacity of internal model-based approaches to calculate minimum regulatory capital.

» Lack of clarity on the level of internal controls and processes needed to provide assurance on the quality of Pillar 3 data

1 Liquidity coverage ratio disclosure standards, January 2014, BCBS 272 (link)
2 Basel III leverage ratio framework and disclosure requirements, January 2014, BCBS 270 (link)
3 Pillar 3 disclosure requirements for remuneration, July 2011, BCBS 197 (link)
4 Composition of capital disclosure requirements, June 2012, BCBS 221 (link)
5 Global systemically important banks: updated assessment methodology and the higher loss absorbency requirement, July 2013, BCBS 255 (link)
6 Signpost means that banks can disclose their Pillar 3 information in a separate document by reference to that document in Pillar 3 report.

The revised Pillar 3 disclosure framework aims to address these weaknesses. It requires banks to present information in a way that facilitates comparability and consistency of disclosures across banks over time. The objective is to enable market participants to assess a bank's overall capital adequacy, compare it with the bank's peers and make more informed investment decisions. The five guiding principles for banks' Pillar 3 disclosures are (1) disclosures should be clear (2) disclosures should be comprehensive (3) disclosures should be meaningful to users (4) disclosures should be consistent over time, and (5) disclosures should be comparable across banks.

4. Reporting Location, Frequency, Timing and Assurance of Pillar 3 Disclosures

To ensure consistency in frequency and timing of disclosures across banks, ease of location by users, and assurance of the quality of Pillar 3 data, the revised framework requires the following:

» Reporting location: Banks are required to publish their Pillar 3 reports in a separate document that provides a readily accessible source of prudential data for users. This document must be easily identifiable to users and may be either appended to, or form a discrete section of, a bank's financial reporting. Banks or supervisors must make available an archive of Pillar 3 reports on their websites for a suitable time period, to be determined by the supervisors.

» Frequency of disclosures: Depending on the nature of the disclosure requirement, the reporting frequencies can be quarterly, semiannually or annually.

» Timing of disclosures: Banks are required to publish Pillar 3 reports concurrently with their financial reports for the corresponding period. However, for periods, when a bank does not publish any financial report and Pillar 3 report is required to be published, the Pillar 3 report must be published as soon as possible and the time lag must not exceed that allowed to the bank for its regular financial reporting at period-ends.

» Assurance of Pillar 3 data: The information in Pillar 3 must be subject, at least, to the same level of internal review and control processes as the information provided by the banks in their financial reporting. Banks must establish a formal Board-approved disclosure policy for Pillar 3 data, including the internal controls and procedures for disclosure of such information. The key elements of this policy should be described in the year-end Pillar 3 report or should be cross-referenced to a location where they are available. One or more senior officers of a bank must attest in writing that Pillar 3 disclosures have been prepared in accordance with the board-approved disclosure policy.

5. Presentation of the Disclosure Requirements

5.1 Format of Presentation

To ensure comparability and consistency of disclosures across banks, the revised framework has introduced harmonized templates with a number of standardized definitions. To achieve a balance between the use of mandatory templates and the need to permit flexibility to senior management to provide qualitative commentary on a bank's specific risk profile, a hierarchy of disclosures has been introduced. This hierarchy includes templates, which must be filled with quantitative data in accordance with the definitions provided, and tables, which address qualitative requirements[7]. The revised framework introduces the following types of templates and tables[8]:

7 Quantitative information is also required in tables in some instances such as in table CRB.

8 To help users navigate among templates, linkages across templates are provided in the explanations to the templates.

Fixed-format templates:

- These require quantitative information that is considered essential for the analysis of a bank's regulatory capital requirements.
- Information must be provided in accordance with the given definitions and instructions.
- Banks may delete a particular row/column from the template if they consider it to be irrelevant to their banking activities or of no meaning to users. However, the numbering of the subsequent rows and columns must not be altered[9].
- Banks may add extra rows and extra columns to the template if they want to provide more detailed disclosures, but the numbering of prescribed rows and columns in the template must not be altered.

Flexible-format templates:

- These require quantitative information that is considered meaningful to the market, yet is not central to the analysis of a bank's regulatory capital.
- Banks may present the required information either in the format provided by the Committee or in the format that better suits the bank. However, the information provided in the customized format must be comparable with the information required in the disclosure template.

Flexible tables:

- These require qualitative information. However, some quantitative information is also required in the table CRB "additional disclosure related to the credit quality of assets" as follows:
  - Breakdown of exposures by geographical areas, industry and residual maturity.
  - Amounts of impaired exposures and related allowances and write-offs, broken down by geographical areas and industry.
  - Aging analysis of accounting past-due exposures.
  - Breakdown of restructured exposures between impaired and not impaired exposures.
- Banks may choose the format for presenting the required qualitative information, as the Committee did not prescribe the format for the presentation in tables.

Banks are expected to supplement templates with a narrative explaining significant changes between the reporting periods, key drivers of such changes and any other issue that might be of interest to the market. Senior management may also disclose information on the bank's specific circumstances, business model and risk profile, if it was not adequately captured by the regulatory disclosure requirements. The bank has the discretion to decide the format of this additional narrative.

5.2 Conditions of Sign Posting

To avoid unnecessary duplication with other disclosures and address the issue of unclear sign posting in the existing regime, the revised framework allows for the sign posting of Pillar 3 disclosure requirements in only certain circumstances. Further, banks are required to signpost clearly, in their Pillar 3 reports, where the disclosure requirements have been published. The sign posting must include:

9 In cases where banks consider that the information required in a template or table would not be meaningful to users and choose not to disclose it, they are required to describe the portfolios excluded and their aggregate total RWAs with a qualitative commentary on why it considers such information not to be meaningful to users.

- The title and number of the disclosure requirement.
- Complete name of the separate document in which the disclosure requirement has been published.
- A web link, where relevant.
- Page and paragraph number of the separate document where the disclosure requirements can be located.

Sign posting of fixed-format disclosure requirements is permitted when the following criteria are met:

- The disclosure in the sign-posted document is mandatory.
- The information in the sign-posted document is equivalent in terms of presentation and content to the information required in the fixed-format template.
- The information in the sign-posted document is based on the same scope of consolidation as the one used in the disclosure requirement.
- The supervisory authority ensuring the implementation of Basel standards is legally constrained in its capacity to require the reporting of duplicative information.
- The level of assurance on the reliability of data contained in the sign-posted document is equivalent to, or greater than, the internal assurance level required for the Pillar 3 report.

6. Required Formats and Reporting Frequency of Disclosure Requirements[10]

The following table presents the required disclosures, presentation formats and frequencies.

Disclosure Requirement	Required Templates and Tables		Format Type	Frequency
Overview of risk management and RWA	OVA	Bank risk management approach	Flexible Table	Annual
	OV1	Overview of Risk-weighted Assets (RWA)	Fixed Template	Quarterly
Linkages between financial statements and regulatory exposures	LI1	Differences between accounting and regulatory scopes of consolidation and mapping of financial statements with regulatory risk categories	Flexible Template	Annual
	LI2	Main sources of differences between regulatory exposure amounts and carrying values in financial statements	Flexible Template	Annual
	LIA	Explanations of differences between accounting and regulatory exposure amounts	Flexible Table	Annual

10 For details on disclosure requirements and their format of presentation, refer to parts 2-7 of BCBS 309 (link).

Disclosure Requirement	Required Templates and Tables		Format Type	Frequency
Credit Risk	CRA	General information about credit risk	Flexible Table	Annual
	CR1	Credit quality of assets	Fixed Template	Semi-annual
	CR2	Changes in stock of defaulted loans and debt securities	Fixed Template	Semi-annual
	CRB	Additional disclosure related to the credit quality of assets	Flexible Table	Annual
	CRC	Qualitative disclosure requirements related to credit risk mitigation techniques	Flexible Table	Annual
	CR3	Credit risk mitigation (CRM) techniques – overview	Fixed Template	Semi-annual
	CRD	Qualitative disclosures on banks' use of external credit ratings under the standardized approach for credit risk	Flexible Table	Annual
	CR4	Standardized approach – credit risk exposure and CRM effects	Fixed Template	Semi-annual
	CR5	Standardized approach – exposures by asset classes and risk weights	Fixed Template	Semi-annual
	CRE	Qualitative disclosures related to Internal Ratings Based (IRB) models	Flexible Table	Annual
	CR6	IRB – Credit risk exposures by portfolio and probability of default (PD) range	Fixed Template	Semi-annual
	CR7	IRB – Effect on RWA of credit derivatives used as CRM techniques	Fixed Template	Semi-annual
	CR8	RWA flow statements of credit risk exposures under IRB	Fixed Template	Quarterly
	CR9	IRB – Back testing of PD per portfolio	Flexible Template	Annual
	CR10	IRB (specialized lending and equities under the simple risk weight method)	Flexible Template	Semi-annual
CCR	CCRA	Qualitative disclosure related to CCR	Flexible Table	Annual
	CCR1	Analysis of CCR exposure by approach	Fixed Template	Semi-annual
	CCR2	Credit valuation adjustment (CVA) capital charge	Fixed Template	Semi-annual
	CCR3	Standardized approach of CCR exposures by regulatory portfolio and risk weights	Fixed Template	Semi-annual
	CCR4	IRB – CCR exposures by portfolio and PD scale	Fixed Template	Semi-annual
	CCR5	Composition of collateral for CCR exposure	Flexible Template	Semi-annual
	CCR6	Credit derivatives exposures	Flexible Template	Semi-annual
	CCR7	RWA flow statements of CCR exposures under the Internal Model Method (IMM)	Fixed Template	Quarterly
	CCR8	Exposures to central counterparties	Fixed Template	Semi-annual
Securitization	SECA	Qualitative disclosure requirements related to securitization exposures	Flexible Table	Annual
	SEC1	Securitization exposures in the banking book	Flexible Template	Semi-annual
	SEC2	Securitization exposures in the trading book	Flexible Template	Semi-annual
	SEC3	Securitization exposures in the banking book and associated regulatory capital requirements – bank acting as originator or as sponsor	Fixed Template	Semi-annual
	SEC4	Securitization exposures in the banking book and associated capital requirements – bank acting as investor	Fixed Template	Semi-annual

Disclosure Requirement	Required Templates and Tables		Format Type	Frequency
Market risk	MRA	Qualitative disclosure requirements related to market risk	Flexible Table	Annual
	MRB	Qualitative disclosures for banks using the Internal Models Approach (IMA)	Flexible Table	Annual
	MR1	Market risk under standardized approach	Fixed Template	Semi-annual
	MR2	RWA flow statements of market risk exposures under an IMA	Fixed Template	Quarterly
	MR3	IMA values for trading portfolios	Fixed Template	Semi-annual
	MR4	Comparison of VaR estimates with gains/ losses	Flexible Template	Semi-annual

Note: The shaded rows are tables, mostly for qualitative information, and the unshaded rows are templates for quantitative information.

Appendix A: Summary of Primary Changes from the Existing to the Final Framework

	EXISTING FRAMEWORK	FINAL FRAMEWORK
Reporting location of disclosures	» Allows banks discretion to decide the appropriate medium and location of their risk and regulatory disclosures, which often results in disclosures spread across banks' financial reporting and Pillar 3 reports. » Often lacks clear sign posting between the two reporting regimes, thus making it difficult for users to locate disclosures.	» Requires banks to publish their Pillar 3 reports in a separate document that provides a readily accessible source of risk data for users. This document may be either appended to or form a separate section of a bank's financial reporting and must be easily identifiable to users. Banks are also required to make available an archive of Pillar 3 reports on their websites. » Allows for sign posting of disclosure requirements only in certain circumstances and clearly specifies what the sign posting must include, with the aim to avoid unnecessary duplication with other disclosures and address the issue of unclear sign posting in the existing regime.
Frequency and timing of disclosures	» Lacks consistency in the frequency and timing of publication of Pillar 3 data across banks and jurisdictions.	» Introduces consistency in the frequency and timing of publication of Pillar 3 disclosures across banks and jurisdictions, thus enabling market participants to compare disclosures. » Requires banks to publish their Pillar 3 reports simultaneously with their financial reports when the two reporting dates align. For periods, when a bank does not publish any financial report and Pillar 3 report is required to be published, the Pillar 3 report must be published as soon as possible and the time lag must not exceed that allowed to the bank for its regular financial reporting at period-ends.

	EXISTING FRAMEWORK	FINAL FRAMEWORK
Assurance of Pillar 3 data	» Does not specify the level of internal controls and processes to which Pillar 3 information should be subjected. Also, does not require Pillar 3 disclosure policy to be described in Pillar 3 report.	» Requires Pillar 3 information to be subject to, at least, the same level of internal review and control processes as the information provided by the banks in their financial reports. » Requires banks to establish a formal Board-approved disclosure policy for Pillar 3 information and to describe the key elements of this policy in the year-end Pillar 3 report or to cross-reference them to a location where they are available. One or more senior officers of a bank must attest in writing that Pillar 3 disclosures have been prepared in accordance with the board-approved disclosure policy.
Linkages with accounting information	» Difficult for the market participants to understand differences in banks' financial statements and the regulatory exposure data in the banks' Pillar 3 reports.	» Ensures linkages between banks' financial statements and the exposure data in their Pillar 3 reports by setting out a process to map the line items of banks' financial statements to exposure amounts in Pillar 3 reports. It also identifies and explains the main sources of differences between the two[11].
Consistency and Comparability	» Lacks in consistency and comparability of disclosures across banks due to differences in form, quality and granularity of data disclosed and interpretation of key definitions.	» Ensures consistency and comparability of disclosures across banks through greater use of templates for key quantitative data and by standardizing a number of key definitions.

References

1. Basel Committee on Banking Supervision, January 2015, "Revised Pillar 3 Disclosure Requirements" – Final Framework (link)
2. Basel Committee on Banking Supervision, June 2014, "Review of the Pillar 3 Disclosure Requirements" – Consultative Document (link)
3. Basel Committee on Banking Supervision, June 2006, "International Convergence of Capital Measurement and Capital Standards" (link)

11 For details, refer to part 3 of BCBS 309 (link).

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