



ESRB Secretariat staff response to the European Commission's consultation document “Fitness check on supervisory reporting”

The Secretariat of the European Systemic Risk Board (ESRB) welcomes the European Commission's consultation document “Fitness check on supervisory reporting”. This response details issues identified by the ESRB Secretariat with the aim of ensuring that supervisory reporting requirements contribute to financial stability. At the same time, it highlights areas for improvement and benefits that can be achieved by streamlining reporting processes via increased use of granular data and global standards.

While the issues discussed in this response have been commented on by the ESRB Advisory Technical Committee and General Board, it is not a formal ESRB response and remains the responsibility of the ESRB Secretariat.

The importance of having prompt access to detailed information about the various components of the financial system is one of the key lessons from the global financial crisis. The crisis revealed clear gaps in data availability that prevented authorities from monitoring the build-up of systemic risk. Moreover, the lack of timely, granular and accurate information hindered the ability of policymakers and market participants to develop effective responses as the crisis unfolded.¹ One of the first initiatives to address this problem was the Data Gaps Initiative launched by the Group of 20 (G20) Finance Ministers and Central Bank Governors in 2009.² The second phase of this initiative is currently under way.³

The global financial crisis also highlighted the need to strengthen European supervisory arrangements, in particular by establishing oversight of the financial system as a whole. The

¹ See [Report to the G20 Finance Ministers and Central Bank Governors](#).

² The G20 Finance Ministers and Central Bank Governors endorsed 20 recommendations put forward jointly by the Financial Stability Board and International Monetary Fund (see link above).

³ Under this initiative, specific recommendations were made to G20 members and other participating economies to enhance the sharing of granular data at both the national and international levels (e.g. through common identifiers, as well as by revisiting, as appropriate, confidentiality rules and legal frameworks). See the summary table in the [Second Progress Report](#) issued by staff of the Financial Stability Board and International Monetary Fund on the second phase of the initiative.



ESRB has a broad mandate⁴ to oversee risks to financial stability in the EU financial system. Timely access to data, encompassing the various components of the financial system, is a *sine qua non* for the ESRB to fulfil its mandate. To this end, the ESRB Secretariat has been assigned the task of developing data infrastructures and analytical methods to provide the ESRB with the necessary statistical and analytical support.⁵ Under the ESRB Regulation,⁶ the ESRB:

1. is given an explicit mandate to “**determine and/or collect and analyse all the relevant and necessary information**” and
2. is granted access to “**all the information necessary to perform its duties**”.

More specifically, the ESRB Regulation sets out **general rules for the collection and exchange of information**, based on close cooperation between the ESRB, the European Supervisory Authorities (ESAs), the European System of Central Banks, the national supervisory authorities and the national statistics authorities, while safeguarding confidentiality and proportionality.⁷ For instance, the ESRB analysis builds on datasets provided by the ESAs, access to which is crucial for the monitoring of financial stability risks originating from different parts of the financial system. While this response focuses on experience gained in house in the development of data infrastructure and analytical frameworks for data to which the ESRB has direct access, it is equally important for financial stability that the ESAs’ regular reporting frameworks (such as FINREP, COREP, Solvency II supervisory reporting) remain robust.

Moreover, in order to ensure that it is able to detect and address the build-up of risks in a timely manner, **the ESRB has been granted direct or indirect access to data on specific activities or sectors**, as follows:

1. the European Market Infrastructure Regulation (EMIR),⁸ a pillar of the financial reforms which relates to the derivatives markets, grants the ESRB access to the EU-wide dataset on derivatives transactions;
2. the Alternative Investment Fund Managers Directive (AIFMD)⁹ grants the ESRB access to data reported by alternative investment fund managers;

⁴ The ESRB was established as part of a wider reform aimed at better protecting the citizen and rebuilding trust in the financial system and is charged with overseeing risk in the financial system as a whole; its task is to monitor and assess systemic risk in normal times for the purpose of mitigating the exposure of the system to the risk of failure of systemic components and enhancing the financial system’s resilience to shocks. See Article 3 of the Regulation (EU) No 1092/2010 of the European Parliament and of the Council of 24 November 2010 on European Union macro-prudential oversight of the financial system and establishing a European Systemic Risk Board.

⁵ Under Article 4(4) of the ESRB Regulation.

⁶ Regulation (EU) No 1092/2010 of the European Parliament and of the Council of 24 November 2010 on European Union macro-prudential oversight of the financial system and establishing a European Systemic Risk Board.

⁷ See Article 15 of the ESRB Regulation.

⁸ Regulation (EU) No 648/2012 of the European Parliament and of the Council of 4 July 2012 on OTC derivatives, central counterparties and trade repositories.

⁹ Directive 2011/61/EU of 8 June 2011 on Alternative Investment Fund Managers and amending Directives 2003/41/EC and 2009/65/EC and Regulations (EC) No 1060/2009 and (EU) No 1095/2010.



3. the Securities Financing Transactions Regulation (SFTR)¹⁰ grants the ESRB access to the dataset of securities financing transactions;
4. the recently adopted Regulation on Simple Transparent and Standardised Securitisation¹¹ grants the ESRB access to data on securitisations.

The box below discusses these regulatory frameworks in more detail, highlighting which of the data gaps revealed by the global financial crisis they each aim to close.

The reporting frameworks listed above have been rolled out gradually; while data reported under EMIR and the AIFMD are already available, data on securities financing transactions and securitisations will not be available until later.

One of the pillars of the reforms proposed in the aftermath of the crisis by the G20 leaders in order to make derivatives markets safer is the collection of transaction-level data on over-the-counter (OTC) derivatives transactions. EMIR mandates the reporting to trade repositories of details of all derivatives transactions entered into by EU counterparties, to which the ESRB has been granted full access. The analysis of these data is already proving to be fundamental to our understanding of these markets from a systemic perspective. The ESRB and its member institutions have pioneered the analysis of such large datasets and will continue this work. The ESRB Chair stressed in his address to the European Parliament in November 2017 that “the ESRB is specifically focusing on developing data infrastructures and analytical methods to move towards a timelier and more detailed monitoring of these markets”.¹²

In this response, the ESRB Secretariat outlines the following key pillars for supervisory reporting, from the perspective of the macroprudential oversight of the financial system of the European Union:

1. **accessing granular, timely and high quality data,**
2. **supporting the process of data standardisation,**
3. **continuing the adoption of existing and new technologies to improve efficiency,**
4. **enhancing the ability to monitor developments across markets, instruments, and sectors.**

These pillars are interrelated and reinforce one another.

¹⁰ Regulation (EU) 2015/2365 of the European Parliament and of the Council of 25 November 2015 on transparency of securities financing transactions and of reuse and amending Regulation (EU) No 648/2012.

¹¹ Regulation (EU) 2017/2402 of the European Parliament and of the Council of 12 December 2017 laying down a general framework for securitisation and creating a specific framework for simple, transparent and standardised securitisation, and amending Directives 2009/65/EC, 2009/138/EC and 2011/61/EU and Regulations (EC) No 1060/2009 and (EU) No 648/2012.

¹² See [Hearing before the Committee on Economic and Monetary Affairs of the European Parliament](#).



Only data at a high level of granularity can capture and reflect the rapidly increasing complexity and interconnectedness of integrated financial systems. Moreover, a high level of granularity ensures greater flexibility for both reporting institutions and supervisors. Reporting institutions should already possess and use high quality granular data, not only for supervisory reporting purposes but primarily to properly assess and manage their risks. Developments and risks can then be efficiently monitored at various levels of aggregation directly from granular data, at any time, avoiding multiplication of reports.

Proper monitoring of an increasingly complex, interconnected and adaptive financial system is only possible with timely and high frequency information. Developing frameworks to rapidly detect potential threats to financial stability is key for the ESRB to fulfil its mandate.

High quality data are a common good which benefits both reporting entities and supervisors. To ensure data quality, constant monitoring and checks across various sources are required so that supervisors are able to detect issues in reporting. This should be seen as a comprehensive, collective effort, to which all must contribute. For instance, the ESRB favours the logic underpinning the “double-sided” reporting of derivatives transactions,¹³ which leads to improvements in the quality of the data through a reconciliation process, supports the design of data quality checks and allows reporting issues to be identified promptly.¹⁴

Further progress on the adoption of international standards is another key element which will lead to great benefits by providing common ground for improving communication and streamlining processes, both within firms and with supervisors. From an analytical perspective, standards enhance comparability across time and facilitate process automatization, thereby reducing costs related to data collection and analysis. To this end, the action of the European Commission to investigate options for a framework of interoperable standards is very welcome.¹⁵

The collection of data on derivatives transactions mandated under EMIR is a powerful example of how granularity and standardisation allow greater efficiency to be achieved in reporting. As data are collected at a high level of granularity, authorities are able to access very detailed data without the need for counterparties in derivatives transactions to submit multiple reports and respond to ad hoc requests. While this process naturally involves a series of initial methodological challenges and costs, it is already proving its worth and will allow even greater efficiency to be gained in the medium to long term.

Granularity and standardisation bring advantages deriving from economies of scale and scope. This, in turn, is reflected in lower costs and improved risk management. Granularity and standardisation benefit from network effects since the more widespread the adoption, the

¹³ See [Revision of the European Market Infrastructure Regulation](#).

¹⁴ See, for instance, the analysis contained in “[Shedding light on dark markets: First insights from the new EU-wide OTC derivatives dataset](#)”, ESRB Occasional Paper No 11, September 2016, which makes extensive use of consistency and quality checks associated with the double-sided reporting obligation.

¹⁵ See [Towards better financial data reporting](#). The Secretariat was also informed that some of the ESRB member institutions have participated in initiatives to increase the harmonisation and/or standardisation of statistical data, such as the [Banks Integrated Reporting Dictionary](#) and the [European Reporting Framework](#).



greater the benefits derived. Granularity could also allow integration of statistical and supervisory reporting requirements, insofar as this is permitted by law.

A successful example of a global financial standard is the creation of an identifier for legal entities engaged in financial transactions: the Legal Entity Identifier (LEI). This identifier was developed in response to a problem that emerged during the global financial crisis, namely the “inability to identify parties to transactions across markets, products, and regions”.¹⁶ The Financial Stability Board, together with the G20, advocated the creation of such a standard at the global level. This standard supports various financial stability objectives, from improving risk management and promoting market integrity to supporting data quality and accuracy.¹⁷ The LEI is defined in ISO standard 17442. Currently new LEIs are being issued on a daily basis. Once issued, the same LEI can be reused in a variety of supervisory reports. Information associated with each LEI is freely available on a daily basis on the Global LEI Foundation (GLEIF) website. The GLEIF is working to expand counterparty data to include not only “who is who” but also “who owns whom”, thereby enabling ownership structures to be identified across the globe.

The data on activities and sectors outlined above, to which the ESRB has access, capitalises on the LEI and other standards. In particular, when monitoring developments in the derivatives markets using data reported under EMIR, the ESRB Secretariat makes extensive use of the LEI standard by linking datasets containing granular information reported by entities identified by LEIs (e.g. the EMIR dataset) to LEI information (e.g. data maintained by the GLEIF). In this way, large datasets can be processed in a matter of seconds. This represents a dramatic improvement compared with having to match information on counterparties contained in different datasets, conducting additional quality checks and maintaining this information over time.

Standards for identifying simple concepts, such as currencies, country codes, sectors, dates and times, etc., have already proven invaluable and now standards for identifying more complex concepts are undergoing a process of harmonisation which promises to deliver great benefits. **For instance, the definition of a standard for a Unique Transaction Identifier (UTI) and Unique Product Identifier (UPI)¹⁸ will be key to understanding complex derivatives transactions;** improving consistency in aggregations and analysis; and increasing the comparability, including over time, of transactions reported to trade repositories.

As the global financial crisis showed, threats to financial stability typically arise from the interaction of the different parts of an integrated financial system. Entities in the financial sector are interconnected via complex company structures (encompassing different sectors and jurisdictions), contractual obligations, non-contractual exposures and other linkages. While increased interconnectedness is a key element of a developed financial system, it may engender

¹⁶ See [History of the Global LEI System](#).

¹⁷ See [The Financial Stability Board \(FSB\) and GLEIF](#).

¹⁸ After carrying out a [feasibility study on approaches to aggregate OTC derivatives data in 2014](#), the Financial Stability Board asked the Committee on Payments and Market Infrastructures and the International Organization of Securities Commissions to develop global guidance on the harmonisation of data elements reported to trade repositories and that are important for the aggregation of data by authorities, including UTIs ([guideline](#) published in February 2017) and UPIs ([guideline](#) published in September 2017).



vulnerabilities that need to be monitored and addressed at the level of the system as a whole. Therefore, given the growing importance of the non-bank sector and securities financing transactions, as well as the overall interconnectedness of the financial system (in particular between banks and non-banks¹⁹), it is crucial for the ESRB to have a comprehensive view of systemic risks. Looking ahead, it would be desirable to enhance the ESRB framework so that information on all components of the EU financial system can be accessed in a more streamlined way. Granularity and increased standardisation represent indispensable tools for continuously monitoring the rapidly changing nature of interconnectedness across markets, instruments and sectors.

The aforesaid objectives can be achieved by adopting new data technologies. Technological improvements will not only enhance the ability to understand the data in a timely and sound manner, but will also contribute to reducing costs in the long run. The adoption of “big data” technologies, coupled with high granularity and standardisation, will improve the coherence and reliability of the data. Furthermore, granular data allow accurate figures to be obtained directly, without the need for intermediate aggregations, thereby increasing timeliness, quality and analytical rigour. Additionally, granularity and standardisation, in combination with new data technologies, will allow for more scalable and secure processes for both firms and supervisors.

In the long run the combination of granularity, standardisation and technologies will contribute to streamlined reporting processes, reduce costs and enhance efficiency and security. This, in turn, will contribute to greater transparency and will foster new and more effective analytical approaches.

In order to ensure that it is able to detect and address the build-up of risks in a timely manner the European Systemic Risk Board (ESRB) has been granted by the EU legislator direct or indirect access to data on specific activities or sectors. This box provides a brief overview of the relevant reporting frameworks, highlighting which of the data gaps revealed in the financial crisis they are intended to address.

The complexity and opaqueness of financial markets, together with the lack of appropriate prudential standards, were one of the fault lines that contributed to the global financial crisis. In the run-up to the crisis the build-up of key vulnerabilities went unnoticed by both market participants and regulators. Specifically, this opacity engendered instability in the over-the-counter (OTC) derivatives markets, securities financing transactions markets and securitisation markets. During the crisis the lack of information prevented authorities and market participants from obtaining a comprehensive picture of developments, which, in turn, shattered market confidence and compounded systemic distress.

The opaqueness of the derivatives markets prevented authorities from being able to identify sufficiently early the extent to which risks were being concentrated in a handful of institutions and,

¹⁹ See the ESRB's [EU Shadow Banking Monitor](#) for a detailed discussion in this regard.



consequently, the effects that their distress would have on financial stability. It also prevented market participants from knowing exactly what exposures their counterparties had to defaulting entities (the events in the credit default swaps market after the failure of Lehman Brothers are a case in point), which resulted in loss of confidence and the drying-up of liquidity in the interbank money market.²⁰ Moreover, while risk transfer instruments were increasingly used, their opaqueness rendered it impossible to understand where risks were ultimately placed across institutions and markets.²¹

In 2009 the G20 leaders committed to greater transparency in derivatives markets.²² The European Market Infrastructure Regulation implements this initiative in Europe and requires EU entities engaging in derivatives transactions (whether or not cleared via central counterparties) to report details of these transactions to trade repositories registered with the European Securities Markets Authority (ESMA).²³ The ESRB has been granted access to the full EU-wide dataset.

The global financial crisis also showed that activity and behaviour in the securities financing markets were a key locus of systemic risk and a key channel for the transmission of systemic shocks during the crisis.²⁴ Securities financing transactions (SFTs)²⁵ can pose a risk to financial stability since they allow the build-up of procyclical leverage and interconnectedness in the financial markets. The opaqueness and complexity of SFTs impeded authorities from detecting the build-up of these vulnerabilities and understanding developments across the full spectrum of market participants.²⁶

In 2013 the Financial Stability Board (FSB) adopted a policy framework for addressing shadow banking risks in securities lending and repurchase agreements,²⁷ including a recommendation on enhanced transparency. This policy framework was endorsed by the G20 leaders in September 2013. It was followed by the Securities Financing Transactions Regulation (SFTR), which was adopted in the EU in 2015. Under the SFTR, EU counterparties²⁸ report details of SFTs to trade repositories registered with ESMA²⁹ and the ESRB was granted access to this information.

It is worth noting that the rules and standards regarding SFT reporting build on infrastructures, operational processes and formats that were introduced for reporting derivatives contracts to trade repositories.

²⁰ See **Ensuring efficient, safe and sound derivatives markets**.

²¹ See footnote 1.

²² See **“Shedding light on dark markets: First insights from the new EU-wide OTC derivatives dataset”**, ESRB Occasional Paper No 11, September 2016.

²³ Or with third country trade repositories recognised by ESMA.

²⁴ See **Strengthening Oversight and Regulation of Shadow Banking**.

²⁵ SFTs comprise a variety of financial contracts. Under the Securities Financing Transactions Regulation, they include repurchase agreements (repos), reverse repos, buy/sell-backs and sell/buy-backs, securities or commodities lending and borrowing arrangements, and margin lending or borrowing transactions.

²⁶ See footnote 24.

²⁷ Idem.

²⁸ Or a third country counterparty, if the SFT is concluded in the course of the operations of an EU-based branch of that counterparty.

²⁹ Or third country trade repositories recognised by ESMA.



The ESRB also has indirect access to the information reported under the Alternative Investment Fund Managers Directive (AIFMD). This reporting framework focuses on leverage employed by managers of alternative investment funds,³⁰ since it is procyclical and can therefore amplify systemic risk, including the risk that abrupt deleveraging could cause a spillover to the wider financial system.³¹ While the primary aim of AIFMD reporting is to allow national supervisory authorities, ESMA and the ESRB to detect, monitor and respond to risks arising from leverage, the information obtained under this framework is also an important tool for assessing systemic risk originating from alternative investment funds, including concentration, interconnectedness and liquidity risk.³² In its set of Recommendations aimed at addressing structural vulnerabilities stemming from asset management, the FSB confirmed the importance of data collection and monitoring of leverage in investment funds.³³

The EU legislator has recently decided to increase the transparency of securitisation markets (given the risks of increased interconnectedness and excessive leverage posed by securitisation) and has introduced a general obligation for the originator, sponsor or special-purpose entity to make information on securitisations³⁴ available via the securitisation repository authorised and supervised by ESMA. The Regulation on Simple Transparent and Standardised Securitisation tasks the ESRB with overseeing the securitisation markets and grants it direct access to data on securitisations.

³⁰ While investment funds regulated under the Undertakings for Collective Investments in Transferable Securities (UCITS) Directive are subject to direct restrictions on the use of on-balance-sheet and off-balance sheet leverage, the Alternative Investment Fund Managers Directive does not introduce such direct restrictions for alternative investment funds.

³¹ See footnote 19.

³² See [Response from the ESRB to the ESMA Consultation Paper on Guidelines on reporting obligations under Article 3 and Article 24 of the AIFMD](#).

³³ See [Policy Recommendations to Address Structural Vulnerabilities from Asset Management Activities](#).

³⁴ Private securitisations are exempt from the reporting obligation.



Imprint

© European Systemic Risk Board, 2018

Postal address 60640 Frankfurt am Main, Germany
Telephone +49 69 1344 0
Website www.esrb.europa.eu

All rights reserved. Reproduction for educational and non-commercial purposes is permitted provided that the source is acknowledged.

ISBN 978-92-9472-036-8 (pdf)
DOI 10.2849/462532 (pdf)
EU catalogue No DT-02-18-390-EN-N (pdf)