EMBARGO
This document is free for publication from 9 a.m. CET on Wednesday, 23 October 2013.
No data from the document may be released before the above embargo has expired.
Any publication that breaks the embargo will cease to receive texts in advance of the release time.

EUROPEAN CENTRAL BANK

NOTE
COMPREHENSIVE ASSESSMENT
OCTOBER 2013

1 INTRODUCTION

The ECB and the participating national competent authorities (NCAs) responsible for conducting banking supervision will carry out a comprehensive assessment, in line with the provisions of the Regulation on the single supervisory mechanism (SSM Regulation)[1]. The SSM Regulation will enter into force in early November 2013. The ECB will conclude this comprehensive assessment of the banking system in October 2014, prior to assuming its new supervisory tasks in November 2014.

This comprehensive assessment is an essential element of the preparations for the SSM, providing the necessary clarity on the banks that will be subject to the ECB's direct supervision. The SSM Regulation enables the ECB to obtain all the relevant information from the NCAs of the participating Member States that it needs to carry out a comprehensive assessment of the relevant credit institutions. The exercise will comprise a supervisory risk assessment, an asset quality review and a stress test. The integrated outcome of the comprehensive assessment may lead to a range of follow-up actions, possibly including requirements for changes in a bank's provisions and capital.

This note provides an initial overview of the key features of this comprehensive assessment.

2 UNDERLYING RATIONALE

Recent periods of economic downturn and financial market stress have impacted banks' balance sheets, with negative consequences for lending to the real economy. In Europe, supervisors and regulators have already taken many actions to address these adverse developments, and the banks themselves have made significant progress in strengthening

1 Council Regulation (EU), conferring specific tasks on the European Central Bank concerning policies relating to the prudential supervision of credit institutions, Official Journal of the European Union, soon to be published in the Official Journal of the European Union.

their balance sheets, not least by raising significant amounts of capital. Since the onset of the global financial crisis, euro area banks have raised around EUR 225 billion of fresh capital and a further EUR 275 billion has been injected by governments, equivalent in total to more than 5 per cent of euro area GDP. Today, the median Core Tier 1 capital ratio of the largest euro area banks stands close to 12%, and most of these banks comply already with the minimum regulatory capital requirements of the fully implemented Capital Requirements Directive IV/Capital Requirements Regulation (CRD IV/CRR) framework. In countries under international assistance programmes, problematic legacy assets have largely been removed from banks' balance sheets to ensure that they will no longer curb banks' lending to profitable businesses. In addition, banks are in the process of restructuring their business models in the aftermath of the financial crisis.

Nonetheless, weaknesses remain, compounded by the perception that banks' balance sheets are not transparent and concerns about their overall risk situation. Against this background, the ECB plans to conduct a thorough review of banks' balance sheets and risk profiles, in preparation for the operational start of the single supervisory mechanism in late 2014. More generally, this review will foster greater transparency in banks' balance sheets and advance the consistency of supervisory practices in Europe. The exercise has three main goals: *transparency*, that is, enhancing the quality of information available concerning the condition of banks; *repair*, by identifying and implementing necessary corrective actions, if and where needed; and *confidence building*, namely assuring all stakeholders that banks are fundamentally sound and trustworthy. If capital shortfalls are identified against a capital benchmark, banks will be required to adopt corrective measures. In its capacity as the new supervisory authority, the ECB will be able to monitor and enforce the implementation of those measures.

3 PROCESS OVERVIEW

The ECB will conduct the comprehensive assessment, cooperating with the NCAs, within the framework of the SSM. Given the unprecedented scale of the exercise that will involve some 130 credit institutions in 18 Member States, covering approximately 85% of euro area bank assets, a system-wide approach is necessary. The ECB will conduct the exercise, detailing its design and strategy, monitoring its execution in close cooperation with the NCAs, performing quality assurance on an ongoing basis, collecting and consolidating the results and finalising and disclosing the overall assessment. The NCAs will execute the exercise at the national level, on the basis of the centrally developed data

requirements and methodology, thereby effectively harnessing local knowledge and expertise. To ensure consistency of execution across both countries and banks, quality assurance measures will be fully integrated into all processes.

Oliver Wyman, an international management consultancy group, will support the ECB by providing independent advice on the methodology, while assisting in the design and implementation of the execution, including the implementation of quality assurance measures. Its services will also be available to NCAs, to support national project organisations and to advise them on implementation. When conducting the comprehensive assessment, all NCAs will call upon the services of private sector experts (consultants, auditors and/or others) to assist with tasks including on-site file reviews, appraisals and valuations.

4 ELEMENTS OF THE UNDERLYING STRATEGY

The comprehensive assessment will cover the banks in the attached list. As required by the SSM Regulation, the comprehensive assessment should be conducted among at least those credit institutions which are deemed to be "significant" under its provisions, and are hence supervised directly by the ECB. However, the full and final list of significant banks will only be compiled in 2014 when up-to-date statistics have become available.[2] With this in mind, the attached list covers all banks that could plausibly be regarded as significant at the time the list is finalised in 2014 (see the attached explanatory note). Euro area countries currently engaged in similar bank review processes may benefit from complementarities that arise in conducting the comprehensive assessment, but national exercises are not a substitute for full participation in the comprehensive assessment.

The comprehensive assessment comprises three complementary pillars:

1) A **supervisory risk assessment**, addressing key risks in the banks' balance sheets, including liquidity, leverage and funding. In particular, it will embody quantitative and qualitative analysis based on backward and forward-looking information aimed at assessing a bank's intrinsic risk profile, its position in relation to its peers and its vulnerability to a number of exogenous factors. The ECB and the NCAs are jointly developing a new risk assessment system that will be deployed as a key supervisory tool in the future SSM. This methodology will

2 Article 6(4) of the SSM Regulation prescribes the conditions that banks must fulfil to qualify as "significant".

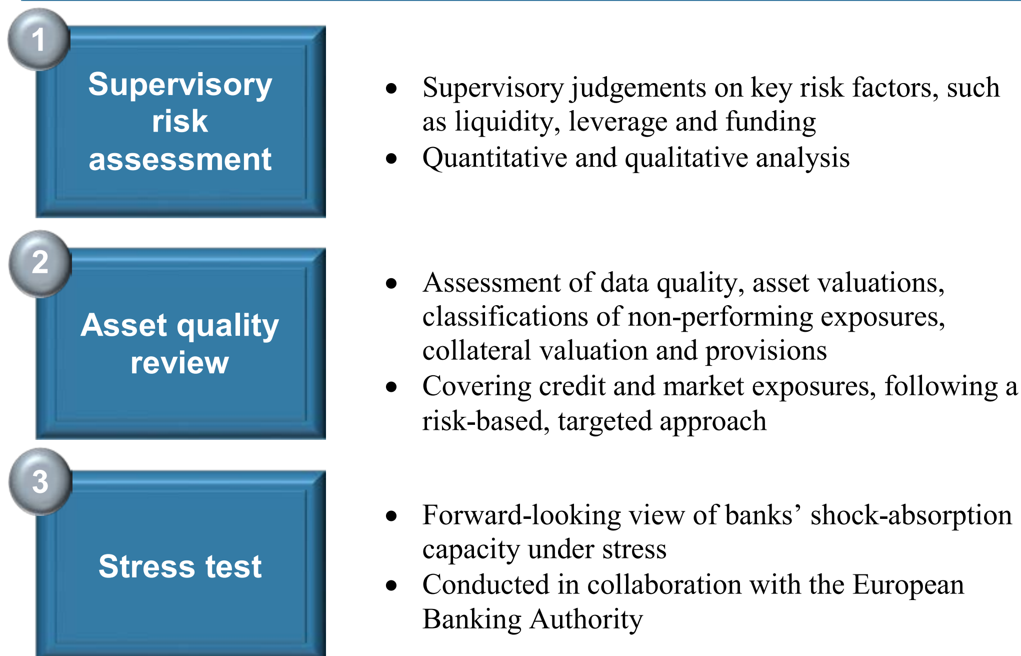
be partially used as of next year, initially in parallel with the national risk assessment systems, to allow comparability of results and to ensure a smooth transition.

2) An **asset quality review**, as elaborated below, examining the asset side of bank balance sheets as at 31 December 2013. This assessment will be broad and inclusive, comprising credit and market exposures (including a quantitative and qualitative review of hard-to-value assets, particularly those qualifying as level 3 assets[3]), on and off-balance sheet positions and domestic and non-domestic exposures. All asset classes, including non-performing loans, restructured loans and sovereign exposures, will be covered. The asset quality review will be conducted with reference to harmonised definitions, including those for non-performing exposures and forbearance; for example, the simplified definition in the recent proposal of the European Banking Authority (EBA) for non-performing exposures.[4] If the information needed to apply the EBA definition of non-performing exposures is not available, relevant data will be estimated.

3) A **stress test**, building on and complementing the asset quality review by providing a forward-looking view of banks' shock-absorption capacity under stress. The ECB and the EBA have agreed to perform the next EU-wide stress testing exercise in close cooperation. They will agree on, and communicate, further details on the stress test, the methodology and the scenarios to be used and the correspondent capital thresholds in due course.

3 The Basel Committee on Banking Supervision describes level 3 assets as those assets that, in the absence of a liquid market or close comparators, need to be valued using models (cf. IFRS 13).

4 Implementing Technical Standards (ITS) on supervisory reporting on forbearance and non-performing exposures (EBA/ITS/2013/03).



Together, these three pillars combine to provide a wide-ranging yet in-depth review of banks' balance sheets. The outcome of the comprehensive assessment will result from the findings of all three pillars – supervisory risk assessment, asset quality review and stress test – and any necessary follow-up actions will be based on this comprehensive outcome.

The ECB will conduct the comprehensive assessment in full independence but will liaise with other European authorities during the process to ensure consistency in action and communication. Specifically, the exercise will be consistent with the EBA Recommendation on the conduct of asset quality reviews.

5 THE ASSET QUALITY REVIEW

Asset reviews are currently conducted by supervisory authorities in participating Member States as a complement to stress tests and other supervisory processes. The asset quality review in preparation for the SSM, however, is a new initiative, unprecedented in its European scale. The asset quality review will be risk-based and will concentrate on those elements of individual banks' balance sheets that are believed to be most risky or non-transparent. However, to ensure that a significant portion of banks' balance sheets are

assessed, strict minimum coverage criteria, at both country and bank level, will be observed. The sampling of the portfolio selections used in the conduct of the assessment will also be subject to strict minimum requirements. A data integrity validation will be undertaken, ensuring that the quality and consistency of bank data are verified and remedied if necessary. While a full assessment of internal models used for the calculation of risk-weighted assets will not take place within the time frame of the exercise, the outcome of the exercise will lead to adjustments in the risk-weights, where justified.

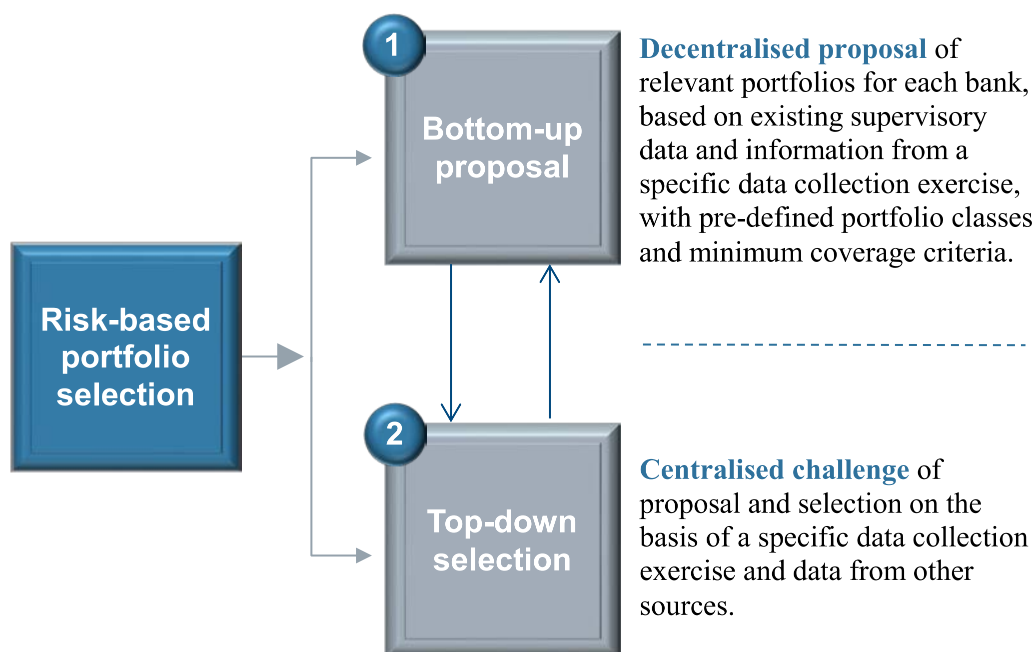
Specific objectives of the asset quality review

- **Assessment of adequate provisioning** for credit exposures
- Determination of the appropriate **valuation of collateral** for credit exposures
- Assessment of the **valuation of complex instruments and high-risk assets** on banks' balance sheets

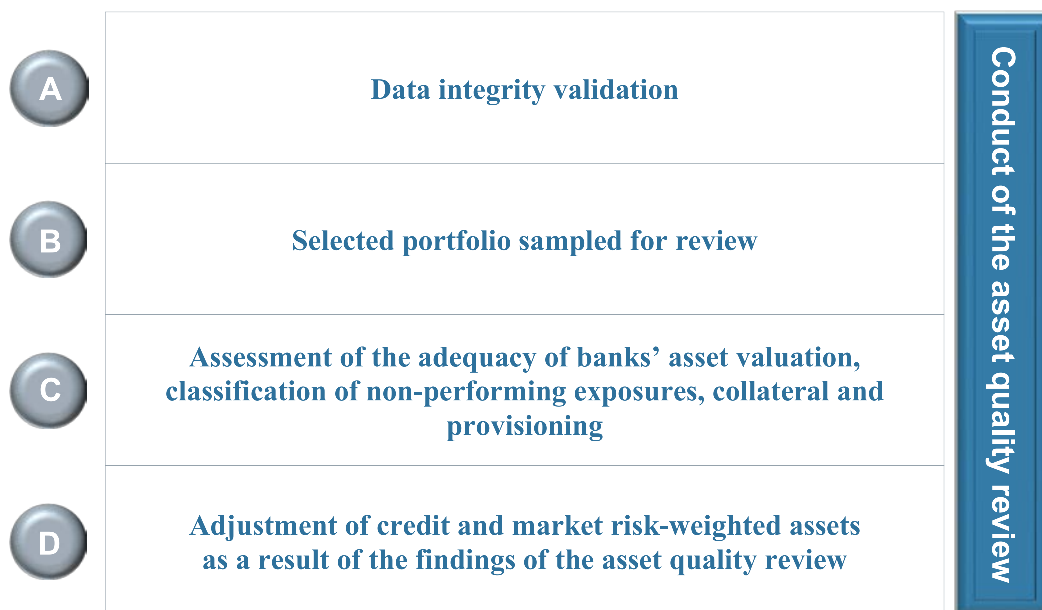
The exercise is broad in scope and will cover sovereigns and institutional (including interbank), corporate and retail exposures. Exposures to borrowers located in SSM and non-SSM Member States as well as non-EU countries will be reviewed. Both the banking book and the trading book will be reviewed, as will on-balance sheet and off-balance sheet exposures (loan commitments, guarantees and credit derivatives for certain national generally accepted accounting principles). Finally, all types of financial instruments will be subject to revision according to a conservative interpretation of current International Financial Reporting Standards (i.e., available for sale, fair value option, held to maturity, held for trading, and loans and receivables), where necessary taking national generally accepted accounting principles into account. Special consideration will be given to illiquid assets, valued through models (fair value level 3 assets).

The asset quality review will comprise three key phases, namely: i) portfolio selection, ii) execution, and iii) collation. The first phase, portfolio selection, will be essential in ensuring that exposures with the highest risk are subject to in-depth review. For this phase, the NCAs will propose – at bank level and on the basis of current risk assessments – the portfolios that should be included in the execution phase. These proposals will be

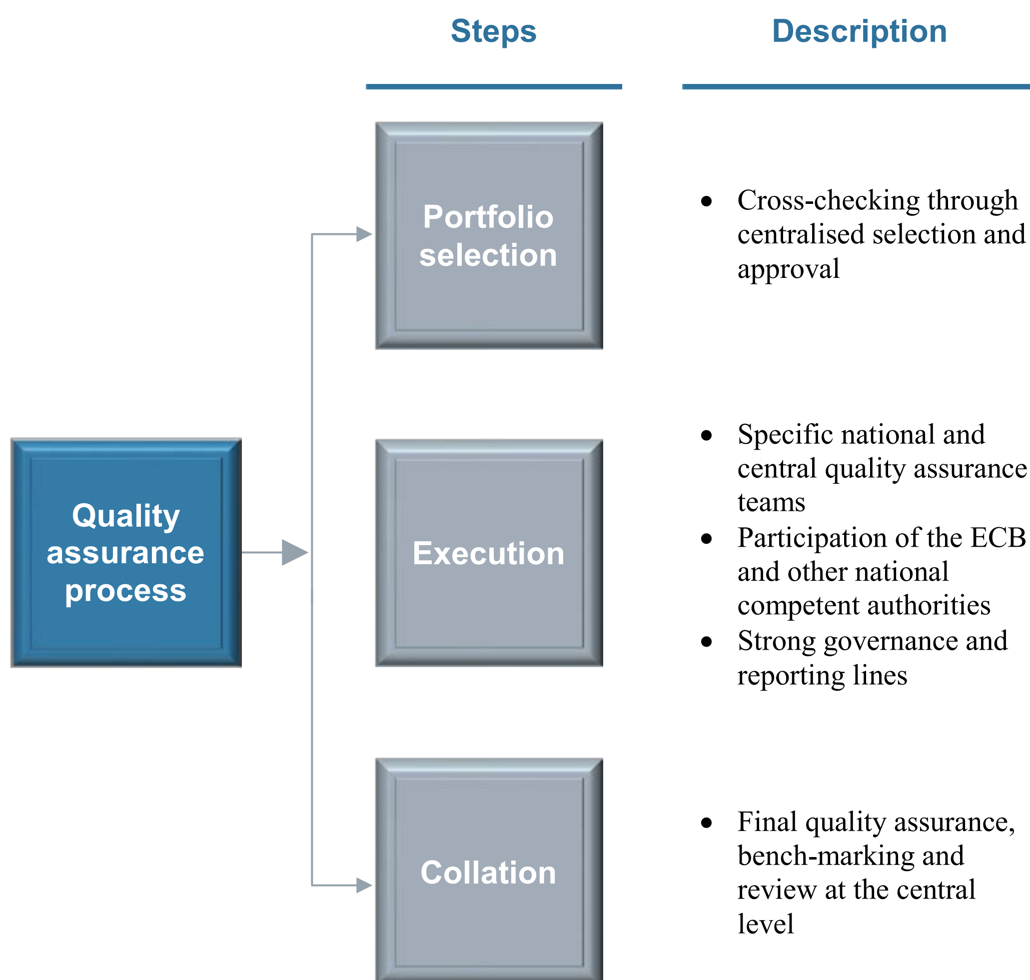
subject to the minimum coverage criteria at country and bank level. The ECB will review and challenge these proposals before making selections, not only on the basis of supervisory data and outputs from the risk assessment system, but also on the basis of macro-financial analysis and information from a specific data collection exercise.



The second phase, execution, will be the most complex, including data integrity validation, sampling, on-site reviews of files, collateral valuation and the recalculation of provisions and risk-weighted assets.



The third phase, collation, will include a final consistency exercise to ensure the comparability of results across all portfolios for all significant banks. There will be a strict process for ongoing quality assurance, with prescribed guidelines and harmonised definitions in order to achieve consistent results.



6 THE CAPITAL THRESHOLD

Capital thresholds will be set as a benchmark for the outcomes of the exercise. The capital benchmark will be set at 8% Common Equity Tier 1. The capital definition of 1 January 2014 will apply for the asset quality review, whereas the definition that is valid at the end of the horizon will be used for the stress test.

The threshold can be decomposed into a Common Equity Tier 1 ratio of 4.5%, and in addition, the 2.5% capital conservation buffer. An add-on of 1% will be requested to take into account the systemic relevance of the banks considered significant under the SSM Regulation.

This total Common Equity Tier 1 ratio of 8% will constitute the minimum capital requirement for all of the banks covered by the comprehensive assessment. It is calculated as a ratio to risk-weighted assets, derived from the asset quality review,

including any necessary adjustment to the risk weights. In this context, the leverage ratio will provide supplementary information for assessing the outcomes.

The relevant modalities and parameters for the stress scenarios will be defined and communicated at a later stage, following analyses conducted jointly by the ECB and the EBA.

7 THE PROJECT ORGANISATION

In order to foster transparency, consistency and sound communication throughout the exercise, the NCAs will periodically involve staff from the ECB and from other Member States' NCAs to assess and review the implementation of the comprehensive assessment at the national level. This will also facilitate ongoing quality assurance processes, at both the national and central level, to ensure the consistent application of the methodology. The asset quality review will have a strong central governance structure, responsible for establishing the methodologies and the project organisation, overseeing the execution phases and assuring the quality of the results.

8 FOLLOW-UP ACTIONS AND BACKSTOPS

The results of the comprehensive assessment, where necessary, will be followed by corrective measures (for example, recapitalisation, also through profit retention, equity issuance, re-orientation of funding sources, asset separation and sales). The timelines for implementing such measures will be part of the outcome of the assessment. The ECB will acknowledge and welcome corrective actions taken, also before the conclusion of the exercise, by banks and supervisory authorities, in the form of enhanced disclosure and provisioning, as well as recapitalisation, asset separation and sales, and other measures.

For the success of the exercise, the ex ante availability of backstops is critical. The special conditions that characterise the comprehensive assessment – the largest such exercise ever undertaken in terms of the number of banks, their overall size and geographical reach – need to be fully recognised at the outset. It is essential to ensure that any banks that have viable business models, but are required to build additional capital for prudential reasons, will be able to obtain such additional resources within an appropriate time frame. Capital shortfalls identified for viable banks should, first and foremost, be made up with private sources of capital. If private sources of capital are insufficient or not readily available, public backstops might need to be drawn upon, in compliance with

national practices and European rules, with the overriding goal of ensuring financial stability. As concluded by the European Council in June this year, "…Member States taking part in the SSM will make all appropriate arrangements, including the establishment of national backstops, ahead of the completion of this exercise."

9 STEPS AHEAD

The ECB will soon convene meetings in Frankfurt with the banks that will undergo the comprehensive assessment.

The process of portfolio selection for the assessment will start in November 2013, based on specific data collections. The ECB will provide further information to the participating credit institutions as needed, when these data collections are launched. To ensure a smooth implementation of the comprehensive assessment, active collaboration among the ECB, the NCAs and the credit institutions will be essential.

Before assuming its supervisory role in November 2014, the ECB will provide a single comprehensive disclosure of the results and any recommendations for supervisory measures to be undertaken by the banks.

Annex

Institutions included in the comprehensive assessment

Austria
BAWAG P.S.K. Bank für Arbeit und Wirtschaft und Österreichische Postsparkasse AG
Erste Group Bank AG
Raiffeisenlandesbank Oberösterreich AG
Raiffeisenlandesbank Niederösterreich-Wien AG
Raiffeisen Zentralbank Österreich AG
Österreichische Volksbanken-AG with credit institutions affiliated according to Article 10 of the CRR
Belgium
AXA Bank Europe SA
Belfius Banque SA
Dexia NV[5]
Investar (Holding of Argenta Bank- en Verzekeringsgroep)
KBC Group NV
The Bank of New York Mellon SA
Cyprus
Bank of Cyprus Public Company Ltd
Co-operative Central Bank Ltd
Hellenic Bank Public Company Ltd
Russian Commercial Bank (Cyprus) Ltd
Germany
Aareal Bank AG
Bayerische Landesbank
Commerzbank AG
DekaBank Deutsche Girozentrale
Deutsche Apotheker- und Ärztebank eG
Deutsche Bank AG
DZ Bank AG Deutsche Zentral-Genossenschaftsbank

5 The assessment methodology for this group will duly take into account its specific situation, and in particular the fact that an extensive assessment of its financial position and risk profile has already been carried out in the framework of the plan initiated in October 2011 and approved by the European Commission on 28 December 2012.

HASPA Finanzholding
HSH Nordbank AG
Hypo Real Estate Holding AG
IKB Deutsche Industriebank AG
KfW IPEX-Bank GmbH
Landesbank Baden-Württemberg
Landesbank Berlin Holding AG
Landesbank Hessen-Thüringen Girozentrale
Landeskreditbank Baden-Württemberg-Förderbank
Landwirtschaftliche Rentenbank
Münchener Hypothekenbank eG
Norddeutsche Landesbank-Girozentrale
NRW.Bank
SEB AG
Volkswagen Financial Services AG
WGZ Bank AG Westdeutsche Genossenschafts-Zentralbank
Wüstenrot & Württembergische AG (W&W AG) (Holding of Wüstenrot Bank AG Pfandbriefbank and Wüstenrot Bausparkasse AG)
Estonia
AS DNB Bank
AS SEB Pank
Swedbank AS
Spain
Banco Bilbao Vizcaya Argentaria, S.A.
Banco de Sabadell, S.A.
Banco Financiero y de Ahorros, S.A.
Banco Mare Nostrum, S.A.
Banco Popular Español, S.A.
Banco Santander, S.A.
Bankinter, S.A.
Caja de Ahorros y M.P. de Zaragoza, Aragón y Rioja
Caja de Ahorros y Pensiones de Barcelona
Caja España de Inversiones, Salamanca y Soria, CAMP

Cajas Rurales Unidas, Sociedad Cooperativa de Crédito
Catalunya Banc, S.A.
Kutxabank, S.A.
Liberbank, S.A.
MPCA Ronda, Cádiz, Almería, Málaga, Antequera y Jaén
NCG Banco, S.A.
Finland
Danske Bank Oyj
Nordea Bank Finland Abp
OP-Pohjola Group
France
Banque Centrale de Compensation (LCH Clearnet)
Banque PSA Finance
BNP Paribas
C.R.H. - Caisse de Refinancement de l'Habitat
Groupe BPCE
Groupe Crédit Agricole
Groupe Crédit Mutuel
HSBC France
La Banque Postale
BPI France (Banque Publique d'Investissement)
RCI Banque
Société de Financement Local
Société Générale
Greece
Alpha Bank, S.A.
Eurobank Ergasias, S.A.
National Bank of Greece, S.A.
Piraeus Bank, S.A.

Ireland
Allied Irish Banks plc
Merrill Lynch International Bank Limited
Permanent tsb plc.
The Governor and Company of the Bank of Ireland
Ulster Bank Ireland Limited
Italy
Banca Carige S.P.A. - Cassa di Risparmio di Genova e Imperia
Banca Monte dei Paschi di Siena S.p.A.
Banca Piccolo Credito Valtellinese, Società Cooperativa
Banca Popolare Dell'Emilia Romagna - Società Cooperativa
Banca Popolare Di Milano - Società Cooperativa A Responsabilità Limitata
Banca Popolare di Sondrio, Società Cooperativa per Azioni
Banca Popolare di Vicenza - Società Cooperativa per Azioni
Banco Popolare - Società Cooperativa
Credito Emiliano S.p.A.
Iccrea Holding S.p.A
Intesa Sanpaolo S.p.A.
Mediobanca - Banca di Credito Finanziario S.p.A.
UniCredit S.p.A.
Unione Di Banche Italiane Società Cooperativa Per Azioni
Veneto Banca S.C.P.A.
Luxembourg
Banque et Caisse d'Epargne de l'Etat, Luxembourg
Clearstream Banking S.A.
Precision Capital S.A. (Holding of Banque Internationale à Luxembourg and KBL European Private Bankers S.A.)
RBC Investor Services Bank S.A.
State Street Bank Luxembourg S.A.
UBS (Luxembourg) S.A.

Latvia
ABLV Bank, AS
AS SEB banka
Swedbank
Malta
Bank of Valletta plc
HSBC Bank Malta plc
Netherlands
ABN AMRO Bank N.V.
Bank Nederlandse Gemeenten N.V.
Coöperatieve Centrale Raiffeisen-Boerenleenbank B.A.
ING Bank N.V.
Nederlandse Waterschapsbank N.V.
The Royal Bank of Scotland N.V.
SNS Bank N.V.
Portugal
Banco BPI, SA
Banco Comercial Português, SA
Caixa Geral de Depósitos, SA
Espírito Santo Financial Group, SA
Slovenia
Nova Kreditna Banka Maribor d.d.
Nova Ljubljanska banka d. d., Ljubljana
SID - Slovenska izvozna in razvojna banka, d.d., Ljubljana

Cases in which one or several of the three most significant credit institutions in a participating Member State are subsidiaries of banking groups already included in the sample (list above):

Slovakia
Slovenská sporiteľňa, a.s.
Všeobecná úverová banka, a.s.
Tatra banka, a.s.
Malta
Deutsche Bank (Malta) Ltd

Methodology for identifying the institutions subject to the comprehensive assessment

According to Article 33(4) of the SSM regulation, the ECB shall "[…]carry out a comprehensive assessment, including a balance sheet assessment, of the credit institutions of the participating Member State[s]. The ECB shall carry out such an assessment at least in relation to the credit institutions not covered by Article 6(4)." This implies that the comprehensive assessment is to be conducted for at least those institutions which qualify as "significant" according to the criteria stated in Article 6(4). This is the case if:

i) the total value of their assets exceeds €30 billion;

ii) the ratio of total assets to GDP of the participating Member State of establishment exceeds 20 per cent, unless the total value of their assets is below EUR 5 billion;

iii) the institution is among the three largest credit institutions in a participating Member State.

Accordingly, the attached list of institutions includes all those whose total assets as of year-end 2012 meet these criteria at the highest level of consolidation. Since total assets figures can fluctuate between two reporting periods to a degree that may affect the significance of institutions close to the thresholds, a 10% margin of deviation has been applied to these thresholds, which leads to the inclusion of institutions with total assets between €27 billion and €30 billion or 18% and 20% of GDP as of year-end 2012.

Further criteria mentioned in Article 6(4) of the SSM regulation which involve supervisory judgement for classifying institutions as significant were generally not considered, since such judgement should be made at a later stage, once the operational arrangements of the SSM have been published pursuant to Article 33(2) of the SSM regulation.

The implications of considering the *highest level of consolidation in participating Member States* in the assessment of whether institutions meet the criteria cited above should be noted. Numerous banking groups included in the list have established subsidiaries in other participating Member States that would themselves meet the criteria on a sub-consolidated or solo basis. The latter are not listed separately unless they are among the three largest credit institutions in a participating Member State, since in principle, the comprehensive assessment is to be conducted at the consolidated level.