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Solvency 2 News, September 2023

Dear members and friends,

According to EIOPA's Insurance Risk Dashboard, macro risks top insurers' worry list.

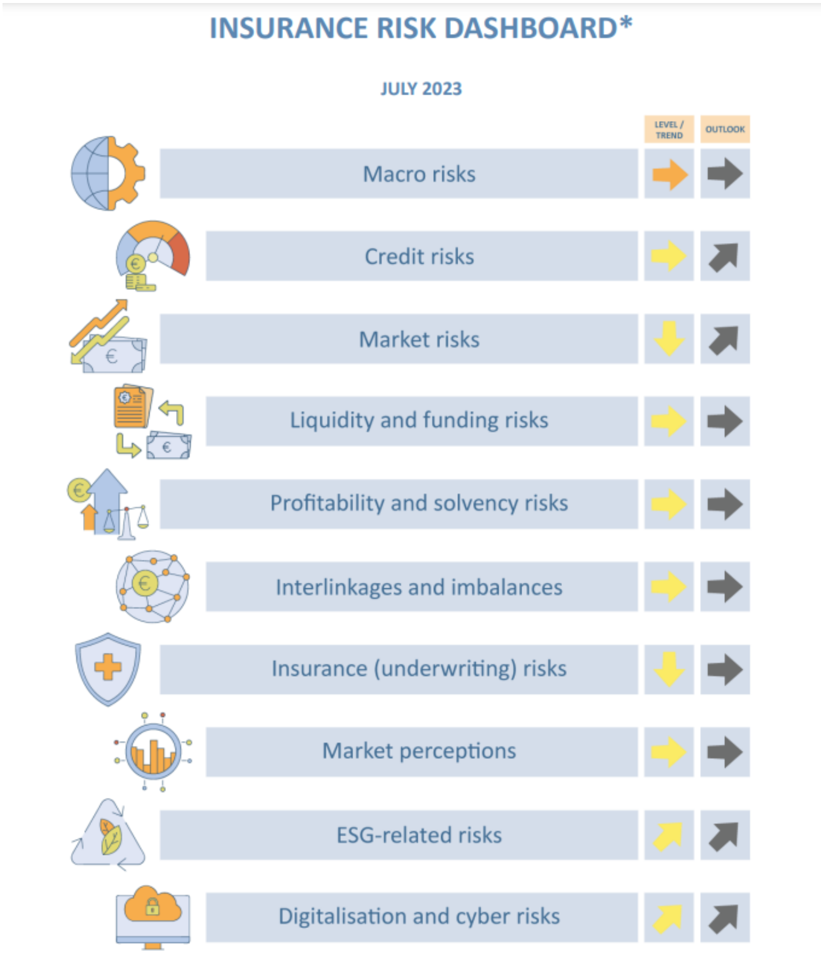
1. Risk levels for the European insurance sector remain broadly constant, with all risk categories pointing to medium risks with the exception of macro risk.

Macro-related risks remain among the most relevant for the insurance sector.

Forecasted GDP growth at global level further increased to 0.74%. CPI forecasts slightly decreased to 3.22%, yet remaining at high level.

Credit risks is at medium level. The CDS spreads increased for financial secured bonds in the second quarter of 2023, while CDS spreads for other fixed income market segments receded slightly.

Market risks decreased from high to medium level as volatility in equity market decreased and duration mismatch narrowed compared to the previous assessment.



2. Liquidity and funding risks show an increase in cash holdings and a drop in the liquid assets ratio in the first quarter of 2023.

Profitability and solvency risks show a drop in the investment return for life insurers in 2022 mainly due to the large increase of unrealized losses following the increase of interest rates.

The distribution of the SCR ratio for insurance groups decreased. Similarly, life insurers reported a slight decline in the median SCR ratio.

On the other hand, assets over liabilities increased due to the higher interest rates.

Interlinkages and imbalances risks remain at medium level while insurance risks decreased in Q1-2023, with the median year-on-year premium growth for non-life insurance decreasing to end 2021 levels.

3. Market perceptions show positive returns for insurance stocks, albeit an underperformance of life insurance stocks when compared to the market for the second quarter of 2023.

4. ESG related risks display an increasing trend with the median exposure towards climate relevant assets slightly increased to 3.3% of total assets. Moreover, the catastrophe loss ratio also deteriorated.

On the other hand, the share of insurers' investments in green bonds over total green bonds outstanding is stable compared to the previous quarter.

5. Digitalization and cyber risks also display an increasing trend with the materiality of these risks for insurance as assessed by supervisors increasing in the first half of 2023.

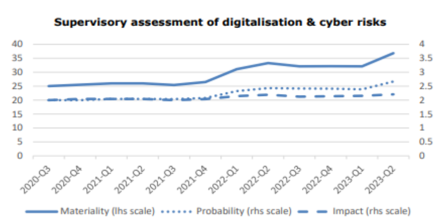
The frequency of cyber incidents impacting all sectors of activity, as measured by publicly available data, increased since the same quarter of last year. The indicator cyber negative sentiment indicates a decreasing concern in the second quarter of 2023.

DIGITALISATION & CYBER RISKS

Digitalization and cyber risks remain at medium level, but increasing. The materiality of these risks for insurance as assessed by supervisors increased for the first half 2023. The frequency of cyber incidents impacting all sectors of activity, as measured by publicly available data, increased since the same quarter of last year. Cyber negative sentiment indicates a decreasing concern in the second quarter of 2023.

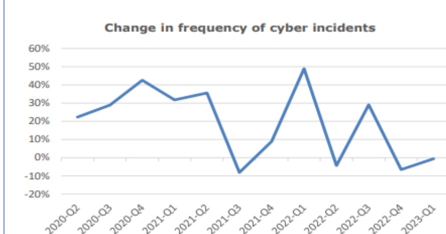
LEVEL: MEDIUM
TREND: INCREASE

The supervisory assessment of digitalisation and cyber risks increased in the first half of 2023. Cyber-attacks are on a growing trend and concerns of a hybrid geopolitical conflict remain.



Note: Scores compiled based on the assessment of probability and impact (rhs: scale from 1 to 4) of digitalisation & cyber risks from National Competent Authorities. The country averages for each answer is then normalised (lhs: scale 0-100). Source: EIOPA's Insurance Bottom-up Survey

The y-o-y change in frequency of cyber incidents has increased in the first quarter of 2023, with the number of cyber incidents affecting all sectors of activity in line with the long term average.



Note: Year-on-year change in frenquency of cyber incidents. Source: HACKMAGEDDON website

To read more: https://www.eiopa.europa.eu/system/files/2023-07/July%202023%20Risk%20Dashboard.pdf

FSB Global Regulatory Framework for Crypto-Asset Activities

FSB FINANCIAL STABILITY BOARD

The FSB is finalising its global regulatory framework for crypto-asset activities to promote the comprehensiveness and international consistency of regulatory and supervisory approaches.

It consists of two distinct sets of recommendations:

(i) High-level recommendations for the regulation, supervision and oversight of cryptoasset activities and markets (CA recommendations);

(ii) Revised high-level recommendations for the regulation, supervision, and oversight of "global stablecoin" arrangements (GSC recommendations).

The framework is based on the principle of "same activity, same risk, same regulation" and provides a strong basis for ensuring that crypto-asset activities and so-called stablecoins are subject to consistent and comprehensive regulation, commensurate to the risks they pose, while supporting responsible innovations potentially brought by the technological change.

The recommendations focus on addressing risks to financial stability, and they do not comprehensively cover all specific risk categories related to crypto-asset activities.

It takes account of lessons from recent events in crypto-asset markets. Central Bank Digital Currencies (CBDCs), envisaged as digitalised central bank liabilities, are not subject to these recommendations.

The events of the past year have highlighted the intrinsic volatility and structural vulnerabilities of crypto-assets and related players. They have also illustrated that the failure of a key service provider in the crypto-asset ecosystem can quickly transmit risks to other parts of that ecosystem.

As recent events have illustrated, if linkages to traditional finance were to grow further, spillovers from crypto-asset markets into the broader financial system could increase.

The G20 has asked the FSB to coordinate the delivery of an effective regulatory, supervisory and oversight framework for crypto-assets, including finalising the FSB's high-level recommendations for the supervision and regulation of crypto-asset activities, and of so-called global stablecoins (GSCs), by July 2023.

In addition, these recommendations, constituting a regulatory and supervisory framework for crypto-assets and stablecoins, will provide input to a joint paper with the International Monetary Fund (IMF) to be delivered to the G20 in September 2023, which will support a coordinated and comprehensive policy approach to crypto-assets by synthesising the policy findings from IMF work on macroeconomic and monetary issues and FSB work on supervisory and regulatory issues.

The FSB and the sectoral standard-setting bodies (SSBs) have developed a shared workplan for 2023 and beyond, through which they will continue to coordinate work under their respective mandates to promote the development of a comprehensive and coherent global regulatory framework commensurate to the risks crypto-asset markets activities may pose to jurisdictions worldwide, including through the provision of more granular guidance by SSBs, monitoring and public reporting.

To read more: https://www.fsb.org/wp-content/uploads/P170723-1.pdf

Data Governance Act: common logos to easily identify trusted EU data intermediaries and data altruism organisations to re-use data

The Commission has introduced common logos to easily identify trusted data intermediation service providers and data altruism organisations in the EU, which will connect data holders, both individuals and companies with data users.

Identifying trusted data intermediation services and data altruism organisations is part of the implementation of the Data Governance Act.

The data intermediation services and data altruism organisations that satisfy the conditions enshrined in the Data Governance Act and opt for the use of the logos, will have to display the logo clearly on every online and offline publication.

The use of these logos at EU level will differentiate the recognised trusted services from other services, contributing to transparency in the data market.

The logo for data altruism organisations recognised in the EU must be accompanied by a QR code with a link to the EU public register of recognised data altruism organisations, which will be available as of 24 September 2023.

The logos have been adopted through an Implementing Regulation and will be registered as trademarks, to protect them from improper use.

Data is a powerful resource that can fuel innovation across Europe's industrial ecosystems.

The Data Governance Act aims to make more data available by increasing trust in data-sharing and tackling technical barriers.

To learn more: https://digital-strategy.ec.europa.eu/en/news/data-governance-act-common-logos-easily-identify-trusted-eu-data-intermediaries-and-data-altruism

https://digital-strategy.ec.europa.eu/en/library/data-governance-act-implementing-regulation

The Importance of a Comprehensive Risk Assessment by Auditors and Management

Paul Munter, SEC, chief accountant

Introduction

Managements and auditors risk assessment processes are critical to the decisions regarding financial reporting and the effectiveness of internal control over financial reporting (ICFR).

Accordingly, we are troubled by instances in which management and auditors appear too narrowly focused on information and risks that directly impact financial reporting, while disregarding broader, entity-level issues that may also impact financial reporting and internal controls.

Such a narrow focus is detrimental to investors as it can result in material risks to the business going unaddressed and undisclosed, thereby diminishing the quality of financial information.

Issues that may also impact financial reporting and internal controls often present themselves as isolated incidents across an issuer—for example, a data breach in a system not part of ICFR, a repeat non-financial reporting-related regulatory finding classified as lower risk, a misstatement to the financial statements determined to be a revision restatement (i.e., “little r”), or a counterparty risk limit breach.

Some management and certain auditors may be inadvertently biased toward evaluating each such incident individually or rationalizing away potentially disconfirming evidence, and conclude that these matters do not individually, or in the aggregate, rise to the level of management disclosure or auditor communication requirements.

This statement discusses management’s obligation to

(1) take a holistic approach when assessing information about the business and avoid the potential bias toward evaluating problems as isolated incidents, in order to timely identify risks, including entity-level risks;
(2) design processes and controls that are responsive to identified risks; and

(3) effectively identify information that issuers are required to communicate to investors. We also discuss auditors' responsibilities as gatekeepers to hold management accountable in the public interest.

Risk Assessment

Management Considerations

Changing economic conditions may have a significant and sudden impact on an issuer's business, which could change risks or create new ones.

Therefore, to be effective, risk assessment processes must comprehensively and continually consider issuers' objectives, strategies, and related business risks; evaluate contradictory information; and deploy appropriate management resources to respond to those risks.

For example, management's risk assessment process may consider observations from regulators, analyst reports, and short-seller reports. Management is also required to provide auditors complete information related to certain communications from regulatory agencies.

Management needs to be alert to new or changing business risks to identify changes that could significantly impact its system of internal control, and design and implement responses that support issuers' ability to appropriately disclose information in its periodic filings.

Business risks, such as a company's loss of financing, customer concentrations, or declining conditions affecting the company's industry, could affect issuers' ability to settle their obligations when due, and affect the risks of material misstatements in financial statements not being identified on a timely basis.

Likewise, risks related to changes in technology could impact the effectiveness of controls around processing of transactions.

Auditor Considerations

Risk assessment forms the basis of the audit process.

A lack of professional skepticism, including objective consideration of contradictory information, in this critical process could result in an auditor not identifying or assessing risks appropriately, which could impact the effectiveness of the audit.

When identifying risks of material misstatement and designing appropriate audit responses, auditors should remain alert to potential changes in issuers' objectives, strategies, and business risks.

Auditors should consider the possible impact of an issuer's public statements regarding changes in their strategy, board composition, or other governance matters—and whether such statements contradict management's assessment of its control environment.

Auditors also should assess the consistency of information disclosed by issuers in periodic filings and the judgments made by management throughout the financial reporting process compared with the information obtained throughout the performance of the audit.

If material inconsistencies exist, auditors should determine whether those disclosures indicate a potential new or evolving business risk that could materially affect the financial statements or the effectiveness of ICFR.

Entity-Level Controls

Management should evaluate whether issuers have implemented processes and controls that can timely prevent or detect a material misstatement in financial statements.

While an issuer's financial reporting objective may be separate from its operational or compliance objectives, an issuer's internal control system should be dynamic and expand beyond a singular focus on ICFR.

When evaluating control deficiencies identified outside of an issuer's financial reporting objective, management and auditors should consider the root cause of the deficiency and whether it impacts the issuer's ICFR conclusions.

For example, the root causes behind a regulator's findings related to enterprise-wide governance and controls, while not directly related to financial reporting control activities, could have an impact on management's ICFR conclusions due to their impact on the risk assessment and monitoring components of ICFR.

Rather than a biased defaulting to an assessment of narrowly defined, process-level deficiencies, management and auditors' aggregation analysis should consider the root cause of individual control deficiencies, to determine whether such deficiencies indicate a broader, more pervasive deficiency at the entity-level.

We encourage auditors to avoid potential bias toward rationalizing away disconfirming evidence and instead to apply objective judgment when evaluating whether insufficient deficiency evaluations by management constitute evidence of ineffective monitoring activities.

Further, when assessing the severity of control deficiencies identified as a result of a misstatement, management and auditors should consider not only the actual misstatement, but also the magnitude of potential misstatement (i.e., the so-called “could factor”).

The “could factor” evaluation includes assessing the total population of transactions or amounts exposed to the deficiency in the impacted accounts or classes of transactions.

In particular, when the root cause is an inadequate entity-level risk assessment process, the “could factor” can extend to a wider population of potential misstatements beyond the identified misstatement.

Reporting Obligations

Clear and transparent communication for the benefit of investors is critical. Management’s financial reporting obligations include disclosures around its annual ICFR evaluations, descriptions of identified material weaknesses, and, on a quarterly basis, changes that have materially affected, or are reasonably likely to materially affect, an issuers’ ICFR.

Additionally, management is required to provide a discussion in its filings of material factors that make an investment in the registrant speculative or risky.

Management may identify these factors for disclosure as part of their risk assessment procedures, which includes an evaluation of all information available, including contradictory information.

In some instances, business risks may also impact financial statement disclosures when the risks and uncertainties could significantly affect the amounts reported in the financial statements in the near term.

Auditors protect investors and further the public interest through the preparation of informative, accurate, and independent audit reports. Therefore, the auditor’s report is a critical means of communication with investors, and auditors should consider the different mechanisms within the auditor’s report to communicate with investors.

In an integrated audit, an auditor’s reporting obligation includes expressing an adverse opinion on the issuer’s ICFR if there are deficiencies that, individually or in combination, result in one or more material weaknesses, including those resulting from entity-level control deficiencies.

If, through the auditor's risk assessment process, a business risk is determined to represent a risk of material misstatement to the financial statements that is discussed with the audit committee, these matters may meet the definition of a critical audit matter and require communication to investors within the auditor's report.

Although not required, we remind auditors that they may use an "emphasis paragraph" to highlight any matter relating to the financial statements and disclosures, which could include matters related to an issuer's objectives, strategies, and related business risks, as discussed above.

Conclusion

As Chair Gary Gensler has noted, "there's a basic bargain in our capital markets: investors get to decide what risks they wish to take" while "[c]ompanies that are raising money from the public have an obligation to share information with investors on a regular basis."

Timely and transparent reporting by management, and informative, accurate, and independent reports by auditors, are critical components of the system that help companies maintain their end of the bargain—their commitment to provide high quality financial information and information about the effectiveness of their ICFR to investors.

When business risks change, a robust, iterative risk assessment process and strong entity and process-level controls are essential to transparent and high-quality financial reporting.

Auditors in their public gatekeeper role serve as an independent check on management's performance of these critical functions and should transparently communicate with investors in accordance with PCAOB standards.

To read more: https://www.sec.gov/news/statement/munter-importance-risk-assessment-082523

Enabling innovation through a digital pound

Rachel Greener, from the Bank's Central Bank Digital Currency Division

Bank of England

The relevant authorities in the UK have indicated that a central bank digital currency, in wholesale or retail form – known as a digital pound – is likely to be needed.

One of the main motivations for a digital pound is that it should promote innovation in domestic payments. Against this backdrop, this article explores the academic literature on innovation for lessons on how to design a digital pound to encourage innovation in the payments ecosystem.

1: Introduction to CBDC

The Bank of England (the Bank) has published several policy papers on central bank digital currency (CBDC)footnote and on the specific CBDC under consideration in the United Kingdom, known as the digital pound.

These policy papers – most recently a Consultation Paper and Technology Working Paper – delve into such topics as the likely need for a digital pound, the features of its design, and how it might be used by consumers and businesses. We therefore do not intend to cover such well-trodden ground in this article.

Let us take it as read that a CBDC is 'an electronic form of central bank money that could be used by households and businesses to make payments and store value'. And as for the motivations for exploring CBDC (a rich topic in itself), we need only focus on the catalyst CBDC could offer to payments innovation.

The vast majority of central banks globally are at least researching the potential for CBDCs in their jurisdictions, with a handful having already launched.

In the United Kingdom, the Bank of England and HM Treasury recently stated that while it is too early to take the decision on whether to introduce the digital pound, it's likely that a digital pound will be needed in the future.

In an increasingly digital economy, the UK authorities see a role for the digital pound in (a) maintaining public access to retail central bank money and (b) promoting innovation, choice and efficiency in domestic payments. It is the latter motivation – and in particular the potential relationship between the digital pound and innovation – that is the focus of this article.

2: Why innovation matters for the digital pound

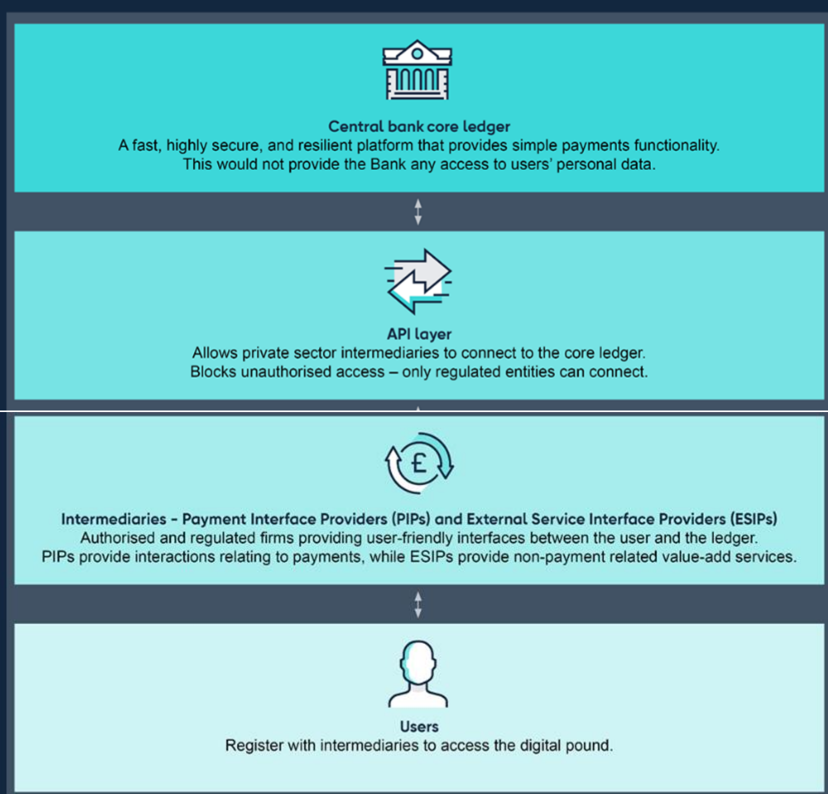
There has been significant innovation in the UK payments landscape in the past two decades, from the introduction of Faster Payments, to contactless card and smartphone transactions, to Open Banking to name a few.

Still, the Bank and HM Treasury judge that there is scope for innovation to generate further efficiencies in payments and to respond to evolving payments needs.

Core infrastructure in any industry is often both costly to maintain and disruptive to improve – hence the oft-debated challenges of 'legacy infrastructure' in banking.

CBDC, as both a new type of money and a new payment system, presents an opportunity to reshape the contours of the financial system. Done well, innovation would be both an input and an output of a UK CBDC.

Figure 1: The platform model of the digital pound



The digital pound would build on innovations in digital banking and payments, and create opportunities to serve new payments-use cases.

A common theme of recent payment innovations is the role of public authorities in kickstarting their introduction and/or their widespread adoption. The development and implementation of both Faster Payments and Open Banking were encouraged, if not mandated, by the UK government.

And Transport for London's early adoption of contactless payments for public transport fares is seen to have helped catalyse the widespread use of contactless payments among consumers.

But another common feature of these innovations was the role of the private sector in delivering them to end-users. And so, it is the Bank's vision that a digital pound would be provided by a public-private partnership, via an architecture called 'the platform model'.

To read more: https://www.bankofengland.co.uk/quarterly-bulletin/2023/2023/enabling-innovation-through-a-digital-pound

The EBA updates data used for the identification of global systemically important institutions (G-SIIs)

- This year's publication includes, for the first time, two additional institutions
- The publication covers 13 indicators used to measure systemic importance
- The data is accompanied by user-friendly tools and bank-specific PDFs

The European Banking Authority (EBA) updated today the 13 systemic importance indicators and underlying data for the 32 largest institutions in the EU whose leverage ratio exposure measure exceeds EUR 200 bn.

This disclosure includes updated data items specific to the recognition of the Banking Union and of institutions that are part of the Single Resolution Mechanism. Acting as a central data hub in the disclosure process, the EBA updates this data on a yearly basis and provides user-friendly tools to aggregate it across the EU.

This end-2022 data will assist competent authorities to identify a subset of banks as global systemically important institutions (G-SIIs), following the final decision by the Basel Committee on Banking Supervision (BCBS) and the Financial Stability Board (FSB).

A stable sample of 27 institutions shows that the aggregate amount for total exposures increased by 0.7% to EUR 21 135 billion at the end of 2022.

Over-the-counter derivatives and payments activity increased by 12% and 10.9% respectively, both achieving the highest value since 2013.

Intra-financial system liabilities and cross-jurisdictional liabilities increased by 5.9% and 5.2%, which for the latter indicator means reaching the highest value since 2013.

Level 3 assets, underwriting activity and assets under custody were the only indicators showing a decreasing trend from 2021 to end of 2022, by 34.2%, 20% and 12.6% respectively.

Background legal basis and next steps

The identification of a G-SII, which leads to higher capital buffer requirements, falls under the responsibility of national competent authorities and this process is updated by December 15 every year.

The identification is based on the disclosure of global denominators and G-SIB exercise results, which are expected to be published by the BCBS and the FSB in November each year.

Any higher capital buffer requirements will then apply after about one year from the publication by competent authorities of banks' scoring results, thus allowing institutions enough time to adjust to the new buffer requirement.

The EBA Guidelines on disclosure of G-SIIs, as amended by EBA/GL/2022/11, define uniform requirements for disclosing the values used during the identification and scoring process of G-SIIs, in line with the internationally agreed standards developed by the BCBS and the FSB.

Having in mind the G-SIB assessment methodology review announced by the Basel Committee on the 31st of May 2022, the EBA supports the disclosure by EU authorities of the cross-jurisdictional indicators and underlying data items needed to calculate the parallel set of scores specific to European Banking Union banks.

EBA EUROPEAN BANKING AUTHORITY

(thousand EUR, data as of end-2022)

	Categories												
	Size	Interconnectedness			Substitutability/Financial Institution Infrastructure				Complexity			Cross-Jurisdictional Activity	
	Indicators												
Bank name	Total exposures	Intra-financial system assets	Intra-financial system liabilities	Securities outstanding	Payments activity	Assets under custody	Underwriting activity	Trading volume	OTC derivatives	Trading and AFS securities	Level 3 assets	Cross-jurisdictional claims	Cross-jurisdictional liabilities
ABN Amro	414 885	94 074	32 632	75 155	4 162 967	179 545	11 695	20 485 200	1 834 616	2 953	915	80 212	57 952
Banco BPM	194 390	29 794	18 562	25 612	2 682 526	86 846	7 496	344 974	169 906	3 734	1 388	31 121	18 198
Banque Postale	270 996	59 522	46 456	40 249	211 192	13 384	0	29 786	188 043	9 729	786	23 120	10 780
Bayern LB	268 713	55 746	84 562	47 968	4 037 192	95 374	6 749	377 095	706 909	8 125	315	36 986	11 975
BBVA	742 023	63 974	89 143	96 587	6 990 278	416 753	23 436	324 003	5 074 720	13 781	3 582	396 869	319 583
BNP Paribas	2 388 876	336 835	298 893	317 231	58 091 405	5 854 163	178 373	4 310 445	26 324 698	73 926	16 348	1 359 358	1 255 194
BPCE	1 400 296	107 584	117 587	323 425	29 258 502	91 922	47 824	1 769 335	10 860 006	46 527	19 401	232 138	227 933
Caixabank	569 660	28 095	10 048	84 059	3 593 935	179 202	209	86 709	916 202	2 491	866	109 811	52 564
Commerzbank	549 987	54 342	59 993	53 798	39 819 203	364 174	40 398	727 780	4 899 449	16 921	5 147	310 659	253 721
Credit Agricole	2 038 885	396 422	233 453	236 809	53 994 067	3 048 198	71 970	1 746 310	19 070 717	34 330	17 305	573 606	440 175
Credit Mutuel	942 825	81 254	74 382	170 249	18 824 325	387 853	4 540	389 299	680 618	24 815	9 850	162 646	71 234
Danske Bank	441 853	52 618	42 796	143 151	1 832 492	194 983	31 113	2 153 365	6 431 874	28 319	794	194 659	222 531
Deutsche Bank	1 251 604	161 849	136 542	133 710	129 807 405	3 020 137	195 310	3 203 933	41 645 482	30 018	26 218	936 990	717 225
DNB	292 814	16 088	16 088	109 564	11 102 799	221 006	57 425	365 656	631 664	1 068	5 307	103 184	126 582
DZ Bank	441 447	243 137	268 583	111 098	8 977 749	237 756	31 308	1 829 705	1 644 336	13 311	2 629	122 320	71 411
Erste Group	333 946	27 801	27 079	48 857	15 630 252	217 129	12 930	647 065	295 208	4 091	1 950	185 647	139 307
Handelsbanken	300 306	8 894	12 689	154 949	12 405 469	55 238	7 668	110 998	422 753	1 214	64	121 585	77 024
Helaba	206 069	45 762	70 778	47 970	2 920 673	66 549	11 943	114 647	789 725	8 595	2 065	74 246	30 172
ING	1 067 532	145 822	126 626	168 735	33 650 731	243 508	36 792	888 735	4 614 247	24 045	7 526	940 712	797 068
Intesa Sanpaolo	865 691	236 504	77 622	133 566	11 046 567	582 593	20 283	282 289	3 359 166	5 129	10 784	226 708	157 833
JP Morgan SE	355 680	147 837	181 160	15 171	63 418 832	2 872 119	27 450	2 271 986	14 983 044	1 609	6 937	285 835	337 984
KBC	345 387	70 015	57 262	14 690	9 716 350	333 850	15	241 414	770 298	1 153	1 625	170 756	138 022
LBBW	354 644	122 533	107 870	56 954	6 775 226	366 160	32 466	364 962	4 536 319	16 505	1 674	112 632	13 277
Nordea	554 698	122 965	38 235	227 430	24 833 064	278 536	83 437	201 832	7 114 698	14 930	3 588	410 979	233 136
Nykredit	234 643	13 130	1 240	179 266	301 746	36 651	2 570	345 887	169 002	4 292	520	16 104	3 833
Rabobank	657 806	35 475	41 088	121 731	30 531 519	0	7 816	1 103 751	5 850 813	2 988	2 665	270 447	97 211
Sabadell	256 777	6 151	7 627	26 332	231 127	43 286	1 836	52 468	183 951	655	157	89 883	74 830
Santander	1 769 214	117 253	146 909	294 087	10 086 441	528 524	69 746	1 245 086	6 852 254	25 565	7 848	1 245 404	989 443
SEB	329 949	36 839	50 933	97 588	31 996 982	1 637 124	23 027	21 061	3 224 456	5 611	641	131 078	274 056
Societe Generale	1 352 781	263 272	285 446	230 590	40 315 620	2 521 232	107 037	4 939 393	13 521 745	102 927	14 688	545 976	509 492
Swedbank	247 872	13 527	18 174	96 538	3 262 569	227 047	0	858 603	2 745 710	1 387	90	63 256	63 275
Unicredit	950 743	201 408	168 659	119 738	13 889 372	460 917	67 331	975 930	6 812 909	14 593	7 358	518 230	444 184

To promote a level playing field in the EU and to increase transparency in the internal financial market, the current level of disclosure goes beyond the minimum standards required by the BCBS, both in terms of granularity of the disclosed information and applicable scope of institutions.

Consequently, some of the group-specific templates currently published belong to institutions that have not contributed directly to the BCBS's G-SIB exercise.

The Regulatory Technical Standards (RTS) on the specification of the methodology for the identification and definition of subcategories of G-SIIs, and Guidelines on disclosure of G-SIIs have been developed in accordance with Directive 2013/36/EU (Capital Requirements Directive - CRD IV) on the basis of internationally agreed standards, such as the framework established by the BCBS and the FSB.

To read more: https://www.eba.europa.eu/eba-updates-data-used-identification-global-systemically-important-institutions-g-siis-2

Lessons from Mount Everest: acting now to curb nature-related financial risks

Klaas Knot, President of the Netherlands Bank, at the Launch Event of the NGFS Conceptual Framework on nature-related financial risks, Paris.

Thank you, François, for stressing the importance of the Conceptual Framework and the need for urgent and collective action. This is indeed an important document and a fine piece of work. It provides a common language that enables us to work together.

The groundwork has been done. Now we can proceed with the actual job at hand, and that is assessing and reducing the risks the nature crisis poses to the economy and the financial system. The question we need to address today is: how?

The risks are real and they are urgent. The rapid degradation of nature is threatening ecosystems and the services they provide. Services such as clean water, healthy air, food and materials that are all essential to our economies and our very existence as humans.

As central banks and supervisors, we have every reason to be concerned, because it's an illusion to think we can preserve financial stability if this degradation continues. A degradation to which financial institutions under our supervision also contribute through the activities they finance.

A degradation that in turn creates risks they need to manage. Therefore it's squarely within our mandate to address these risks and to use our leverage to bend the curve. From nature degradation to nature restoration.

The Kunming-Montreal Global Biodiversity Framework sets clear targets to halt and reverse nature loss by 2030, putting us on a path to living in harmony with nature by 2050.

The Framework also foresees a role for the financial sector, with explicit targets for matters such as disclosure and the alignment of financial flows. We have only seven years left to deliver on that commitment to halt and reverse the current trend. Seven years that are critical for nature, but also for the climate. Because without nature, our actions to address climate change are bound to fall short.

So our task is as important as it is urgent. The question for us today is: how to proceed? There is no straightforward answer. The interaction between nature, climate and the economy is exceptionally complex. And let's face it, our working culture does not help us here.

We, as central bankers, are by nature risk-averse and methodical. We first want to have a good data set, then we want to reach consensus on what is the most robust analytical framework, then we assess the risks, etc etc. The sheer complexity of the subject, together with our usual approach to problem solving, may mean we will be too late.

One way to help us approach this problem may be to compare our quest to climbing a mountain. A mountain no-one has ever climbed before. When Tenzing Norgay and Edmund Hillary first reached the summit of Mount Everest in 1953, they were not alone. They were part of an expedition team of about 15 climbers, and a large number of porters.

First they created a number of advance camps, gradually reaching higher up the mountain. And then they sent a series of two climbers for an assault of the summit, one pair after another.

Despite all their preparation, each pair of climbers faced the same problem: they did not know exactly what they would find on their path.

Each pair encountered new obstacles, like technical problems with the oxygen sets.

But the expedition team learned from those obstacles, and the climbing pairs also made discoveries that helped the next pair do a better job.

Finally, on May 29th, on returning from the summit, Hillary's first words to his colleague George Lowe were "Well, George, we knocked the bastard off".

I think what this analogy teaches us is that, in order to make meaningful progress as NGFS members, three things are essential: starting now, working together, and keeping our eyes on the summit.

First, like the Mount Everest expedition team, we just have to get going, without the benefit of perfect knowledge. Because the problem is too complex to approach it the "old central bankers' way". This means we have to start now with improving how we measure nature degradation and its effects on our economy and the financial system.

We need to enhance and harmonize our data, metrics and scenarios, as François has rightly pointed out. At DNB we have embarked on such a first attempt to measure financial risks for a few transition scenarios, such as ending harmful subsidies.

We aim to share our findings later this year. I am confident that the technical recommendations by the NGFS team working on nature scenarios will help us to expand and refine such efforts together.

Starting now also means engaging with the financial sector today on ways to manage their nature-related risks. And it means finding ways to practice what we preach, for example by exploring how we can manage current nature-related financial risks to our own reserves.

This is also a way to better understand the challenges the market is facing. In that light, we have started a pilot to explore how the TNFD framework could apply to DNB's own reserves. And I am sure there are many other examples to be found here in this room today.

Second, like the Mount Everest team, we need to collaborate closely. This is all the more important since we may sometimes work in smaller teams to tailor the approach to our different circumstances.

Sometimes we may stumble into an obstacle that forces us to take a step back and look for a different route. And sometimes we may make an important discovery that helps us and others to take the next steps.

Close communication is key here. And with the Conceptual Framework, we can now communicate in a common language. Via the NGFS, we can help each other take those first steps on data, scenarios, supervision and reserve management.

Together, we can search for critical ecosystems whose degradation is a material source of risk to our economies and financial systems.

We can investigate the macroeconomic impacts of nature loss. And we can search for ways to contribute to the scaling up of finance for nature.

Always taking into account the restrictions and possibilities that our mandates provide, and the need for other actors, including governments, to do their part as well. These are all areas where the success of our individual efforts will be greatly enhanced by sharing our experiences as we proceed.

And finally, like the Mount Everest team, we need to keep our eyes on the summit. Just as climbers know they have to reach the summit by noon in order to make a safe return, we need to meet the Kunming-Montreal Global Biodiversity targets by 2030, to stay on track for living in harmony with nature by 2050. If we lose sight of our goal, we will start to drift and we will almost certainly arrive too late or not at all. This underscores the relevance of transition plans, also for us as central banks and supervisors.

The task is complex. The mountain that we have to climb is high and shrouded in mist. But it is our duty as central bankers to climb the mountain, and the urgency is high.

We now have a common language, the Conceptual Framework, that will help us meet the challenge together. This meeting is called a Launch Event. But it's not the Framework we have to launch, it's already there and it's great. It's ourselves we have to launch.

And if we start our ascent now, if we communicate constantly on our findings, and we if we keep our eyes on the summit, like the 1953 expedition team, we have a high chance of success. Then hopefully in 2050, we can say, as Ed Hillary did: "Well George, we knocked the bastard off".

To read more: https://www.dnb.nl/en/general-news/speech-2023/lessons-from-mount-everest-acting-now-to-curb-nature-related-financial-risks/#:~:text=related%20financial%20risks-,Lessons%20from%20Mount%20Everest%3A%20acting%20now,curb%20nature%2Drelated%20financial%20risks&text=At%20the%20Launch%20Event%20of,economy%20and%20the%20financial%20system.

Reflections on the 2023 banking turmoil

Pablo Hernández de Cos, Chair of the Basel Committee on Banking Supervision and Governor of the Bank of Spain, at the Eurofi Financial Forum 2023, Santiago de Compostela.

Good evening, and thank you for inviting me to speak at our dinner tonight.

I should start by wishing you all "una gran bienvenida" to Spain. And, in the event that some of you came to Santiago de Compostela by completing the Camino, let me say "felicidades" and "Ultreia et Suseia"!

A common expression in Spain is that "el Camino da más de lo que recibe" – the Camino gives more than it receives. While I cannot claim to offer you any more ecclesiastical insights this evening, I will be reflecting on the recent banking turmoil and the implications for the global banking system and the Basel Committee.

For some of you, the turmoil may seem like a distant memory. Since the frenzied months of March to May, many banks have been reporting bumper financial results on the wave of rising interest rates.

A cursory look at financial markets since that period would also suggest that the worst may be behind us. So why do I plan to look back at what may be regarded as some as a historical event?

Put simply, the banking turmoil that started in March is the most significant system-wide banking stress since the Great Financial Crisis (GFC) in terms of scale and scope.

Over the span of 11 days – from 8 to 19 March 2023 – four banks with total assets of about $900 billion were shut down, put into receivership or rescued. This was followed by the failure of a fifth bank with roughly $230 billion in assets on 1 May 2023.

To give you a sense of the order of magnitude, the total value of these banks' assets is roughly equivalent to Spain's annual GDP (leaving aside the stock versus flow nature of these numbers).

The distress of these individual banks, while having largely distinct causes, triggered an assessment of the resilience of the broader banking system.

In response, large-scale public support measures were deployed by some jurisdictions to mitigate the impact of the stress, including significant central bank liquidity provision to banks, the activation of FX swap lines, government backstops or guarantees, and, in certain cases, an extension of deposit guarantee schemes.

In many respects, today's stabilisation of the banking system is due to a combination of public support measures and the increased resilience provided by post-GFC regulatory reforms, most notably Basel III. We had hoped that we would not need to rely on the former so frequently.

Against that backdrop, the Basel Committee undertook a review of this period and conducted a stocktake of the regulatory and supervisory implications of these developments, with a view to learning lessons.

I am pleased to inform you that, as recently announced by the Group of Governors and Heads of Supervision, good progress has been made with this work.

I will focus my remarks tonight by offering my personal views on some of the main takeaways and identifying some issues that may warrant further reflection.

Risk management and governance

There is perhaps a near universal agreement that one of the main lessons from the turmoil is the importance of banks' risk management practices and governance arrangements as the first and most important source of financial and operational resilience.

The boards and management of banks should be the first port of call in managing and overseeing risks; these functions cannot be outsourced to supervisors.

Jumping straight to discussions about the regulatory and supervisory implications of recent events is akin to forgiving banks for not fulfilling their primary responsibilities and likewise shareholders for not exercising due diligence.

Yet the banking turmoil highlighted a series of weaknesses by some banks in this area, including:

- fundamental shortcomings in (basic) risk management of traditional banking risks (such as interest rate risk and liquidity risk, and various forms of concentration risk);
- a failure to appreciate how various risks that were building up were interrelated and could compound one another;
- inadequate and unsustainable business models, including an excessive focus on growth and short-term profitability (fuelled by remuneration policies), at the expense of appropriate risk management;
- a poor risk culture and ineffective senior management and board oversight; and
- a failure to adequately respond to supervisory feedback and recommendations.

Many of these elements may appear obvious and quite basic in nature. So it is of deep concern to see that, in 2023, some banks' boards and senior management failed in their most elementary responsibilities of overseeing and challenging a bank's strategy and risk tolerance. More is clearly needed to shore up such responsibilities.

Consider the following historical anecdote.4 In 1800, a French chemist by the name of Éleuthère Irénée du Pont set up a gunpowder factory in Delaware. He quickly realised that gunpowder factories have an undesirable property: they tend to explode frequently. In response, du Pont took two initiatives.

First, he required that the director (himself) live inside the factory with his family, putting his life on the line – what you could view as "skin in the game".

Second, he established a rule that every new piece of machinery had to be operated for the first time by the factory's senior management. If the machine blew up, the manager would suffer the consequences. Needless to say, the safety of the plant increased overnight.

I don't think I need to draw out explicitly the comparisons with today's banking system. But it is clear that the turmoil raises some fundamental questions about the current banking system.

Is it simply inevitable that there will always be "outlier" banks with serious governance and risk management shortcomings?

Is this a "feature" of a banking model that combines leverage and maturity transformation with a focus on short-term gains?

Have we optimised the alignment of incentives between banks' boards and senior management and broader financial stability objectives?

I don't have the answers to all of these questions, but I think they certainly merit further reflection.

To read more: https://www.bis.org/speeches/sp230914.htm

NIST CSWP 29 (Initial Public Draft)
The NIST Cybersecurity Framework 2.0

Date Published: August 8, 2023
Comments Due: November 5, 2023

This is the public draft of the NIST Cybersecurity Framework (CSF or Framework) 2.0.

The Framework has been used widely to reduce cybersecurity risks since its initial publication in 2014. Many organizations have told NIST that CSF 1.1 remains an effective framework for addressing cybersecurity risks.

There is also widespread agreement that changes are warranted to address current and future cybersecurity challenges and to make it easier for organizations to use the Framework.

NIST is working with the community to ensure that CSF 2.0 is effective for the future while fulfilling the CSF's original goals and objectives.

NIST seeks feedback on whether this draft revision addresses organizations' current and anticipated future cybersecurity challenges, is aligned with leading practices and guidance resources, and reflects comments received so far.

In addition, NIST requests ideas on the best way to present the modifications from CSF 1.1 to CSF 2.0 to support transition.

NIST encourages concrete suggestions for improvements to the draft, including revisions to the narrative and Core.

This draft includes an updated version of the CSF Core, reflecting feedback on the April discussion draft.

This publication does not contain Implementation Examples or Informative References of the CSF 2.0 Core, given the need to frequently update them. Draft, initial Implementation Examples have been released under separate cover for public comment.

NIST seeks feedback on what types of Examples would be most beneficial to Framework users, as well as what existing sources of implementation guidance might be readily adopted as sources of Examples (such as the NICE Framework Tasks, for example). NIST also seeks feedback on how often Implementation Examples should be updated and whether and how to accept Implementation Examples developed by the community.

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As the CSF 2.0 is finalized, the updated Implementation Examples and Informative References will be maintained online on the NIST Cybersecurity Framework website, leveraging the NIST Cybersecurity and Privacy Reference Tool (CPRT).

Resource owners and authors who are interested in mapping their resources to the final CSF 2.0 to create Informative References should reach out to NIST.

To read more: https://csrc.nist.gov/pubs/cswp/29/the-nist-cybersecurity-framework-20/ipd

https://nvlpubs.nist.gov/nistpubs/CSWP/NIST.CSWP.29.ipd.pdf

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