



Standing for trust and integrity

ECB Comprehensive Assessment of 124 European banks: possible consequences for the accountancy profession

The European Central Bank (ECB) has [announced](#)¹ a full assessment of the 124 major banks in the Eurozone, before assuming direct supervisory authority over these banks in November 2014.

Relevance of the ECB Comprehensive Assessment

This year-long review includes a risk assessment, stress test and asset quality review (AQR) which can significantly impact the accountancy profession. Particularly the AQR, as it directly concerns the statutory auditors of these 124 banks. The AQR is also extremely relevant for auditors who would be asked to assist their national competent authority, responsible for conducting banking supervision, with on-site file reviews, appraisals and valuation. The ECB has published a tentative list of the banks included in this exercise, which facilitates addressing the relevant auditors.

FEE supports the ECB's assessment in its aims to provide transparency on Eurozone bank operations, repair potentially undercapitalised banks and build confidence for all stakeholders of the banking community. The European Banking Authority (EBA) has also asked national supervisors in other countries in the European Economic Area to carry out AQRs that will feed into stress tests on other major banks outside the Eurozone.

Anticipating the asset quality review (AQR)

The AQR will focus on the credit worthiness of the banks' asset portfolios at 31 December 2013. Accounts and valuations closed at year-end 2013 will only be assessed by the ECB by mid-2014. It is essential, as always, for banks to scrutinize the value of their asset portfolios appropriately and robustly as of 31 December. This valuation includes the impairment of loans, the proper valuation of collateral and the correct rating/classification.

The AQR is of a regulatory nature, particularly related to regulatory capital adequacy. It does not intend to give a view on impairment losses calculated for financial reporting purposes. Nevertheless, proper presentation and valuation of the assets as of 31 December minimizes the risk that the ECB's findings in 2014 may lead to a perception that banks should have taken additional impairments, also under IFRS, in 2013. Even though those charged with governance of banks are primarily responsible for reporting and the valuation of assets, auditors are responsible for evaluating the judgments made by those charged with governance on those valuations.

Any significant discrepancies between the 2013 year-end valuations of the same assets in different banks and countries, as well as unjustifiable discrepancies between the 2013 year-end and later valuations, carry potential reputational risk for the profession. This is particularly relevant in the aftermath of the financial crisis.

¹ <http://www.ecb.europa.eu/press/pr/date/2013/html/pr131023.en.html>



Process

In performing the assessment, the ECB will collaborate with the relevant national competent authorities and will seek the support of independent third parties. The ECB has no institutional experience with banking supervision and has limited staff resources. It is therefore expected that the ECB will heavily rely on external expertise and manpower.

Loan loss provisioning is different in regulation and in financial reporting

There is potential for misperceptions about the different objectives of loan loss provisions for financial reporting and loan loss provisions for regulatory purposes (related to the appropriate risk weighting and the regulatory capital requirements). Loan loss provisioning for regulatory purposes is typically not based on the applicable incurred loss model required by IFRS, but established on a more conservative basis. Consequently, regulatory loss calculations are typically expected to be higher for regulatory purposes than for accounting purposes.

Transparent and public communication about those differences in objectives is essential. It is thus important for regulators, standard setters and the accountancy profession to work together in this regard. Clear communication may prevent unwarranted criticism of accounting standards or the profession, in case shortfalls in regulatory capital are identified.

In addition to this Alert, FEE has submitted a (public) [letter to the ECB](#)² on the Comprehensive Assessment. This letter recommends the ECB to address certain issues related to the Comprehensive Assessment that have been raised within the accountancy profession.

For additional information, please see the relevant [ECB Note](#)³.

NOTES FOR EDITORS

About FEE

FEE (Fédération des Experts-comptables Européens – Federation of European Accountants) is an international non-profit organisation based in Brussels that represents 48 institutes of professional accountants and auditors from 36 European countries, including all of the 28 EU member states.

FEE has a combined membership of more than 800.000 professional accountants, working in different capacities in public practice, small and large accountancy firms, businesses of all sizes, government and education – all of whom contribute to a more efficient, transparent and sustainable European economy.

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² http://www.fee.be/images/Angeloni_140130_ECB_Comprehensive_Assessment.pdf

³ <http://www.ecb.europa.eu/pub/pdf/other/notecomprehensiveassessment201310en.pdf>