

# ***Valuation of assets and liabilities***

**FSVC-FSI-MENA FRI seminar**

**Global financial turmoil and the changing face of  
financial sector supervision**

**6-7 April 2009**

European Commission  
Internal Market & Services DG



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Banking & Financial Conglomerates



# Objectives

## Inform about some valuation issues

- The objective of financial reporting
- Fair value
- Basel supervisory guidance on fair valuing
- Provisioning



# The objective of financial reporting

## Investors versus financial stability

***G20- WG 1 Recommendation 1: As a supplement to their core mandate, the mandates of all national financial regulators ... and standard setters (IASB....) should take account of financial system stability.***

***G20- WG 1 Recommendation 13 Accounting standards setters and prudential supervisors should work together to identify solutions that are consistent with the complementary objectives of promoting the stability of the financial sector and of providing transparency of economic results in financial reports.***

# The objective of financial reporting

- Investment decisions (economic value)
- Discharge of management
- Creation of “buffers”
- Level of management discretion

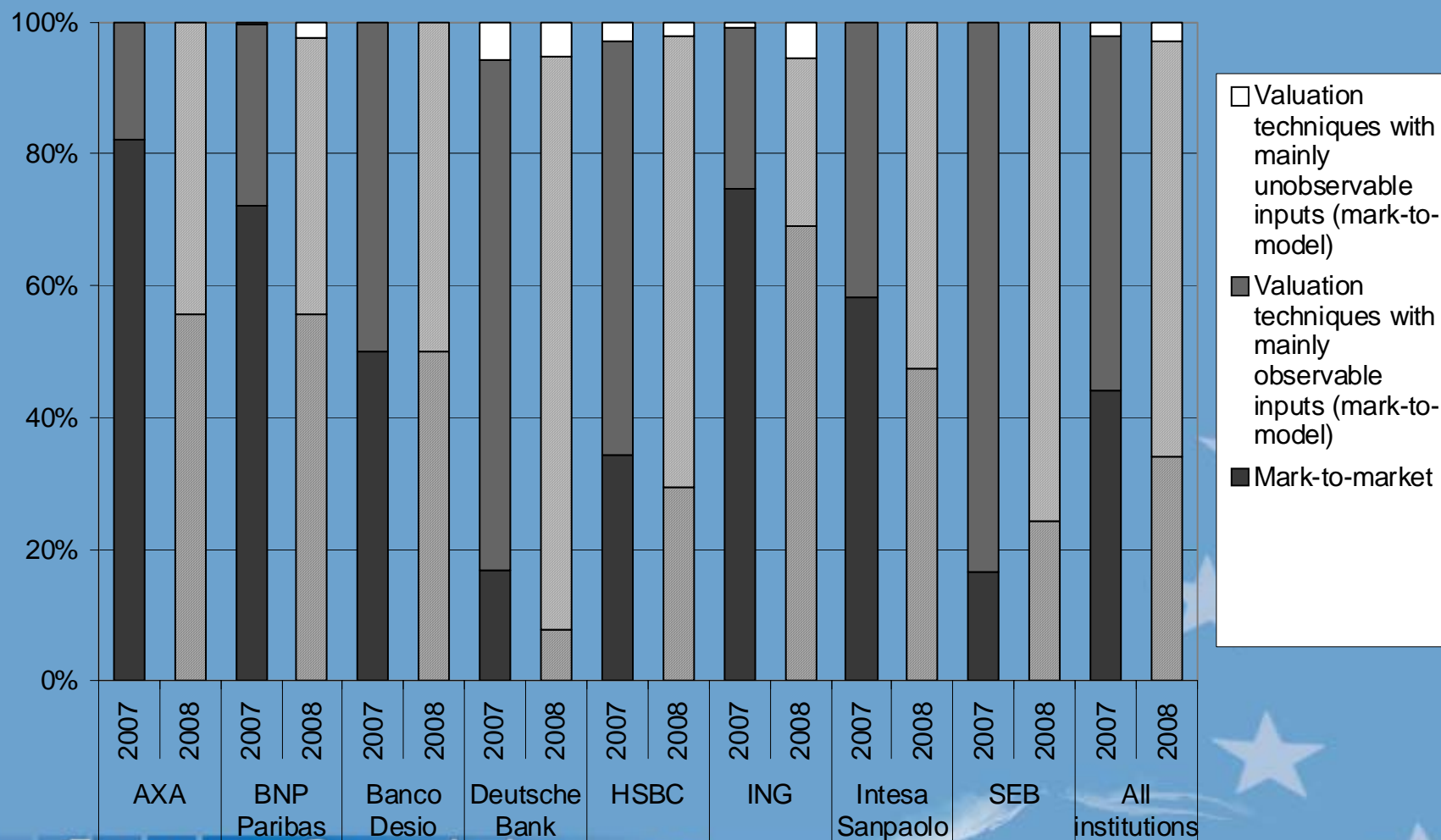
# Fair value

- Good concept but....
  - not for all assets and liabilities
  - Pre requisites (deep and liquid markets)
- Counterintuitive: own credit risk
- Measurement: reliability versus relevance
- Pro-cyclical?
- No filter on unrealised gains / losses

# Use of fair value by EU banks

- Significant use by European banks
  - on average 44% of assets and 26% of liabilities at fair value;
  - in total €18 trillion EU banking assets and €10.5 trillion liabilities at fair value;
  - FVO 5%, AFS 11%, trading 28%
- About 10% profits unrealised gains
- IAS 39 reclassification option over €200 billion
- In 2008 Greater use of valuation techniques (mark-to-model)

# Valuation techniques used by EU financial institutions



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# BCBS fair valuing guidance

10 principles clustered into 3 categories

1. Valuation governance and controls
2. Risk management and reporting for valuation
3. Supervisory assessment

Supervisors expect that, may require, should ....



# BCBS fair valuing guidance

- Senior management responsibility
- Independent regular and rigorous model valuation
- adequate resources
- Quality and reliability of model input
- Valuation uncertainty
- Valuation adjustments

# Provisioning

- IAS 39 impairment
- Basel II expected loss model
- Imarginal differences?
- No “general” provisions under IFRS
- Dynamic provisioning (or reserving)?

# Provisioning by EU banks

- All banks used historic loss data to estimate collective impairments
- Impairment data adjusted for economic circumstances
- Cumulative impairments between 0,3 and 3,3%
- annual impairment cost between 0,05 and 1,4%
- Significant disclosure differences on collective impairment
- A kind of expected loss approach under IAS 39



***Thank you.***

***[http://ec.europa.eu/internal\\_market/bank/regcapital/index\\_en.htm](http://ec.europa.eu/internal_market/bank/regcapital/index_en.htm)***

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