

EBA Final Guidelines on ICAAP and ILAAP  
information collected for SREP purposes

ECB supervisory expectations and Draft Guides  
to the ICAAP and ILAAP

European Banking Authority and European Central Bank

# List of abbreviations

| Abbreviations | Meaning                         |
|---------------|---------------------------------|
| CA            | Competent Authority             |
| CAS           | Capital Adequacy Statement      |
| CET1          | Common Equity Tier 1            |
| CRD IV        | Capital Requirements Directive  |
| CRR           | Capital Requirements Regulation |
| EBA           | European Banking Authority      |
| ECB           | European Central Bank           |

| Abbreviations | Meaning  |
|---------------|--|
| ICAAP         | Internal Capital Adequacy Assessment Process   |
| ILAAP         | Internal liquidity adequacy assessment process |
| GL            | Guidelines                                     |
| LAS           | Liquidity Adequacy Statement                   |
| SI            | Significant Institution                        |
| SREP          | Supervisory Review and Evaluation Process      |
| SSM           | Single Supervisory Mechanism                   |

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# Introduction

**The EBA published in November 2016 Final Guidelines on ICAAP and ILAAP information that supervisors should collect for SREP purposes. Further, the ECB published in March 2018 Draft Guides to the ICAAP and to the ILAAP for SIs according to the SSM framework**

## Introduction

- The CRD IV requires institutions to have in place an internal capital adequacy assessment process (**ICAAP**); and an internal liquidity adequacy assessment process (**ILAAP**). These processes are key risk management instruments for institutions, and competent authorities (CAs) review them as part of the Supervisory Review and Evaluation Process (**SREP**).
- In the European Union, the **European Central Bank** (ECB) assumed responsibility for the supervision of significant institutions (SIs) within the Single Supervisory Mechanism (SSM) from November 2014 onwards. Thus, the ECB is responsible for carrying out the SREP with respect to these institutions.



### EBA

- The EBA published in November 2016 **Final Guidelines (GL)** intended to ensure convergence of supervisory practices in the assessment of ICAAP and ILAAP as required by the SREP<sup>1</sup>.
- In particular, these GL specify what **information on ICAAP and ILAAP CAs should collect** from the institutions in order to perform their assessments.
- In addition to specifying information requirements, these GL also set **general criteria** for CAs to organise collection of ICAAP and ILAAP information from institutions and to use such information for the purposes of their assessments of other SREP elements.



### ECB



- In January 2016, the ECB published for the first time its **expectations on ICAAP and ILAAP**, together with a description of what ICAAP and ILAAP-related information institutions should submit.
- In order to foster those improvements, the ECB initiated in February 2017 a **multi-year project** to develop **comprehensive SSM Guides on ICAAP and ILAAP** for SIs.
- In this regard, the ECB launched in March 2018 a public consultation on its **Draft Guide to the ICAAP** and on its **Draft Guide to the ILAAP** with the aim of developing a more detailed set of supervisory expectations<sup>2</sup>.

This **Technical Note** summarises the content of the EBA GL, and also the ECB supervisory expectations and the Draft Guides on ICAAP and ILAAP.

(1) They should be read together with the EBA GL on common procedures and methodologies for SREP.

(2) Joint Supervisory Team at the ECB will start using these Guides as from 2019 when assessing ICAAPs and ILAAPs.

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# Executive summary

## GL on ICAAP and ILAAP information

**Information items to be collected by CAs are divided into four categories: information common to ICAAP and ILAAP, ICAAP-specific information, ILAAP-specific information, conclusions and quality assurance**

### Executive summary

| Scope of application   | Regulatory context  | Next steps  |
|--|---|---|
| <ul style="list-style-type: none"> <li>Institutions as defined in the CRR / CRD IV: <b>credit institutions</b> and <b>investment firms</b>.</li> </ul> | <ul style="list-style-type: none"> <li><b>CRD IV</b> (European Parliament and Council, June 2013).</li> <li>GL for common procedures and methodologies for the <b>SREP</b> (EBA, December 2014).</li> </ul> | <ul style="list-style-type: none"> <li>CAs must report whether they comply with the GL no later than two months after their translation.</li> <li>The GL apply from <b>1 January 2017</b>.</li> </ul> |

### Main content

#### General considerations

- The GL contain general considerations related to operational procedures (i.e. notification to institutions about reference dates, frequency, etc.), the proportionality principle, additional information and cross-border banking groups.
- A 'reader's manual' shall be included providing an overview of the documents submitted to the CAs and their status.

| Information common to ICAAP and ILAAP   | ICAAP-specific information  | ILAAP-specific information   | Conclusions and QA  |
|---|---|--|---|
| <ul style="list-style-type: none"> <li>Business model and strategy</li> <li>Risk governance and management framework</li> <li>Risk appetite framework</li> <li>Stress testing framework</li> <li>Risk data, aggregation and IT systems</li> </ul> | <ul style="list-style-type: none"> <li>Overall ICAAP framework</li> <li>Risk measurement, assessment and aggregation</li> <li>Capital planning</li> <li>Internal capital and capital allocation</li> <li>Stress testing in ICAAP</li> </ul> | <ul style="list-style-type: none"> <li>Liquidity and funding risk management</li> <li>Funding strategy</li> <li>Strategy on liquidity buffers</li> <li>Cost benefit allocation mechanism</li> <li>Intraday liquidity risk mgmt.</li> <li>Liquidity stress testing</li> <li>Liquidity contingency plan</li> </ul> | <ul style="list-style-type: none"> <li>Conclusions of the ICAAP and ILAAP and their impact on the risk and overall management</li> <li>Quality assurance</li> <li>Internal audit reports</li> </ul> |

# Executive summary

## ECB supervisory expectations and Draft Guides to the ICAAP-ILAAP

The ECB documents, both the supervisory expectations and the Draft Guides to the ICAAP and to the ILAAP, apply to significant institutions within the SSM

### Executive summary

#### Scope of application

- **Significant institutions** within the SSM, as defined in the Guide to banking supervision.

#### Regulatory context

- **CRD IV** (EP and Council, June 2013).
- **GL on ICAAP and ILAAP** (EBA, November 2016)
- GL for common procedures and methodologies for the **SREP** (EBA, December 2014).

#### Next steps

- The Final Guides will be considered in the assessment of institutions' ICAAPs and ILAAPs as a part of the SREP **as from 2019**, and will replace the ECB ICAAP-ILAAP expectations.

### Main content

#### ECB supervisory expectations

##### Harmonised collection of information

- Specifications on **dates and format** (deadline and reference date, etc.).
- Specifications on **content**
- **Conclusions and quality assurance.**

##### Supervisory expectations on ICAAP

- **Governance**, general **design** of the ICAAP, ICAAP **perspective, risks** considered, definition of **internal capital, assumptions** and key parameters, inter-risk **diversification** effects, and **stress testing.**

##### Supervisory expectations on ILAAP

- **General definition of the ILAAP** (clear and formal statement, sound economic perspective, etc.).
- **ILAAP reporting** (information items not covered, short term exercise, etc.).

#### Draft Guides to the ICAAP and to the ILAAP

**7 principles** on ICAAP and ILAAP.

1. Governance
2. Management framework
3. Continuity of the institution
4. Material risks
5. Internal capital / Internal liquidity buffer
6. Risk quantification methodologies
7. Stress testing

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# GL on ICAAP and ILAAP information

## General considerations



The EBA GL include general considerations concerning operational procedures, the proportionality principle, additional information that may be requested, cross-border banking groups and the 'reader's manual' on ICAAP and ILAAP

### General considerations

#### Operational procedures

- CAs should notify institutions about the **dates** by which the information should be provided, the **reference date** (specifying whether different references dates can be used for individual information items), the **frequency** and the **technical means and format** for the submission of information.

#### Proportionality

- The operational procedures should be proportionate to the category of an institution.
  - For **SREP Category 1 institutions**<sup>1</sup>, the information items should be provided on an annual basis by one single set date.
  - For **non-Category 1 institutions**, CAs may determine different frequency, reference dates, etc.

#### Additional information

- CAs may request institutions to provide **additional information** needed. Furthermore, CAs may request some specific information outside the regular ICAAP and ILAAP submission cycle.
- CAs should determine the appropriate **level of granularity and quantity of information** through an ongoing supervisory dialogue with a SREP institution, ensuring that they receive the **valid and applicable** information at the remittance date.

#### Cross-border banking groups

- CAs involved should coordinate the dates, means, format and detailed scope of each information item **consistently for all group entities**.

#### 'Reader's manual'

- CAs should ensure that the 'reader's manual' is prepared as an overarching document that facilitates the assessment of ICAAP and ILAAP documents by providing an **overview** of them and their **status**. This manual should also provide information regarding the material changes to the information items compared with the previous submission of information, and any exclusions from the submission.

# GL on ICAAP and ILAAP information

## Information common to ICAAP and ILAAP



**Common information to ICAAP and ILAAP refers to items related to the institution's business model and strategy, risk governance framework...**

### Common information to ICAAP and ILAAP

#### Business model and strategy

- Description of the **current business models**, including identification of core business lines, markets, geographies, subsidiaries and products the institution operates.
- Description of **main income and cost drivers**, allocated to core business lines, markets and subsidiaries.
- Description of the **changes planned** by the institution to the current business model and its underlying activities (e.g. operational changes or governance issues).
- **Projections of key financial metrics** for all core business lines, markets and subsidiaries.
- Description of how the **business strategy and ICAAP/ILAAP** are linked.

#### Risk governance and management framework

- Description of the **overall governance arrangements** (e.g. roles and responsibilities within the risk management and control organisation, including at the level of management body and senior management across the group), covering:
  - Risk taking, risk management and risk control.
  - ICAAP and ILAAP and their key components, including inter alia risk identification, risk measurement, stress testing, capital and liquidity planning, etc.
- Description of reporting lines and frequency of regular **reporting to the management body** covering the risk management and control of the risks.
- Description of **interaction between risk measurement and monitoring** and **actual risk taking** practice (e.g. limit setting, monitoring, dealing with breaches, etc.).
- Description of **processes** and arrangements that ensure that the institution has in place a robust and integrated framework for the **management of its material risks** and their evolution, including: i) the **interaction and integration** of capital and liquidity management (e.g. interaction between ICAAP and ILAAP); ii) the interaction between the institution-wide risk management and its various categories; and iii) integration of ICAAP and ILAAP into the risk management and the **overall management** of an institution.
- Where appropriate, description of **separation of tasks** within the banking group, **institutional protection scheme** or **cooperative network** concerning risk management.

# GL on ICAAP and ILAAP information

## Information common to ICAAP and ILAAP



...as well as to the institution's risk framework, stress testing framework and programme and risk data aggregation

### Information common to ICAAP and ILAAP

#### Risk appetite framework (RAF)

- Description of the correspondence of the **strategy and business model** of the institution with its **risk appetite framework**.
- Description of the **process and governance arrangements**, including the roles and responsibilities within senior management and management body, in respect of the design and implementation of the **risk appetite framework**.
- Information on the **identification of material risks** which the institution is or might be exposed to.
- Description of the **risk appetite/tolerance levels, thresholds and limits** set for the identified material risks, as well as time horizons, and the process applied to keeping such threshold and limits up-to-date.
- Description of the **limit allocation framework** covering core business lines, markets and subsidiaries.
- Description of the **integration and use** of the risk appetite framework in the **risk and overall management**.

#### Stress testing framework

- General description of the institution's **stress testing programme** including types, frequency, methodology, etc.
- Description of the **governance arrangements**, in particular the stress tests used for ICAAP and ILAAP purposes.
- Description of the **interaction (integration) between solvency and liquidity**, and the role of reverse stress tests.
- Description of the **uses of stress testing and its integration** into the risk management and control framework.

#### Risk data, aggregation and IT systems

- Description of the framework and process to **gather, store and aggregate risk data** across various levels.
- Description of **data flow and data structure** of risk data used for ICAAP and ILAAP.
- Description of **data checks** applied for risk data used for ICAAP and ILAAP purposes.
- Description of **IT systems** used to gather, store, aggregate and disseminate risk data used for ICAAP and ILAAP.

# GL on ICAAP and ILAAP information

## ICAAP-specific information



With regard to ICAAP-specific information, CAs should collect from institutions both methodology and operational documentation, covering the overall ICAAP framework, risk measurement, assessment and aggregation, and capital planning

### ICAAP-specific information (1/2)

|   | METHODOLOGY AND POLICY DOCUMENTATION   | OPERATIONAL DOCUMENTATION  |
|---|--|--|
| Overall ICAAP framework                     | <ul style="list-style-type: none"> <li>Description of the <b>scope of the ICAAP</b>.</li> <li>Description of the approach to the <b>identification of risks</b> and the inclusions of them within risk categories and sub-categories.</li> <li>Description of <b>key objectives</b> and <b>main assumptions</b> of ICAAP, including how these ensure the capital adequacy.</li> <li>Description of whether the ICAAP is focused on the risks' impact on <b>accounting figures</b> or on the <b>economic value</b>, or both.</li> <li>Description of <b>ICAAP time horizons</b>.</li> </ul> | <ul style="list-style-type: none"> <li><b>List of risk categories and sub-categories</b> (e.g. definitions and perimeter).</li> <li>Explanations of <b>differences</b> between risks covered by the ICAAP and the risk appetite framework.</li> <li>Description of any <b>deviations</b> in the ICAAP process and in the <b>key assumptions</b> within the group and the entities of the group.</li> </ul>                           |
| Risk measurement assessment and aggregation | <ul style="list-style-type: none"> <li>Description of key features of quantification <b>methodologies and models</b> (metrics, assumptions, and parameters).</li> <li>Specification of <b>actual data used</b>.</li> <li>Descriptions of the main <b>differences</b> between models used for ICAAP and those for minimum own funds requirements<sup>1</sup>.</li> <li>Description of the approach to <b>aggregation of internal capital estimates</b> for entities and risk categories covered, including the approach to inter-risk diversification benefits.</li> </ul>                  | <ul style="list-style-type: none"> <li><b>Internal capital estimates</b> to cover all risk categories and subcategories<sup>2</sup>.</li> <li>The <b>results of the calculation of internal capital estimates</b> on a risk-by-risk basis.</li> <li>The results of the <b>aggregation of internal capital estimates</b> for entities and risk categories, including the effects of diversification and/or concentrations.</li> </ul> |
| Capital planning                            | <ul style="list-style-type: none"> <li>Description of the <b>general set-up of capital planning</b>, including dimensions considered (e.g. internal, regulatory), time horizon, capital instruments, capital measures etc.</li> <li>Description of the <b>main assumptions</b> underlying the capital planning.</li> </ul>   | <ul style="list-style-type: none"> <li>Forward-looking view on the <b>development of risks and capital</b> in terms of both internal capital and regulatory own funds.</li> <li>Description of the <b>current conclusions</b> from capital planning (issuances, planned changes to the balance sheet, etc.).</li> </ul>  |

(1) In case an institution is using advance models approved by the CAs.

(2) Institutions should explain when certain risks are better covered by qualitative mitigating measures.

# GL on ICAAP and ILAAP information

## ICAAP-specific information



The GL also specify that CAs should collect ICAAP-specific information with regard to internal capital and capital allocation and stress testing in ICAAP

### ICAAP-specific information (2/2)

#### Internal capital and capital allocation

- METHODOLOGY AND POLICY DOCUMENTATION**
- **Definition of the internal capital** used to cover ICAAP capital estimates, including all capital elements/instruments considered.
  - Description of the main **differences** between internal capital elements/instruments and regulatory own funds instruments.
  - Description of the methodology and assumptions used for the **allocation of internal capital** to group entities, core business lines, and markets, where appropriate.
  - Description of the **monitoring process** (comparison of internal capital estimates vs. allocated capital).

#### Stress testing in ICAAP

- Description of **adverse scenarios** considered under ICAAP, including the description of how reverse stress tests have been used to calibrate the severity of scenarios used.
- Description of **key assumptions** used in the scenarios, including management actions, business assumptions regarding balance sheet, reference dates, etc.

#### OPERATIONAL DOCUMENTATION

- **Amount of internal capital available** to date.
  - **Actual amounts of internal capital allocated** to risks, group entities, core business lines and markets.
  - **Quantitative comparison** between the actual internal capital usage relative to the internal capital allocated based on ICAAP estimates.
- 
- **Quantitative outcome** of the scenarios and **impact on key metrics**, including P&L and capital, internal and regulatory own funds, prudential ratios, as well as, in integrated approaches, the impact on liquidity position.
  - Explanation of how **scenario outcomes** are relevant to the business model, strategy, material risks and group entities by the ICAAP.

# GL on ICAAP and ILAAP information

## ILAAP-specific information



The ILAAP-specific information includes, among others, items on liquidity and funding risk management, such as the scope of the ILAAP, the description of the set-up of the ILAAP, etc.; and items on the funding strategy, such as the description of the funding plan

### ILAAP-specific information (1/3)

#### Liquidity and funding risk management

#### METHODOLOGY AND POLICY DOCUMENTATION

- Description of the **scope of the ILAAP**.
- Description of the **set-up of the ILAAP** explaining the relation between all its components and providing reasoning how that set-up ensures the institution has access to sufficient liquidity.
- **Criteria** applied for the selection of **significant risk drivers** for liquidity and funding risk.
- **Criteria** applied for the selection of appropriate **tools and assumptions** for ILAAP, such as the method of measuring and projecting current and future cash flows over appropriate time horizons.

#### Funding strategy

- Description of the general **set-up of the funding plan**, including sources of funding, tenors, key markets, etc.
- Where appropriate, a policy document on **maintaining presence in markets** to ensure and periodically test market access and fund raising capacity of the institution.
- Where appropriate, a policy document on **funding concentration risk**.
- Where appropriate, a policy on **funding in foreign currencies**, including the most relevant assumptions with regard to availability and convertibility of these currencies.

#### OPERATIONAL DOCUMENTATION

- Assessment of **intragroup liquidity flows and funding positions** including legal impediments to the transfer of liquidity within the (sub-)group.
  - Reasoning for selection of the **significant risk drivers** and a **quantitative overview** of these risk drivers.
  - Quantitative overview of the **funding profile** and its perceived stability in all significant currencies.
  - Evidence of the monitoring of **compliance** with prudential requirements regarding liquidity and funding risk<sup>1</sup>.
- 
- The **current funding plan**.
  - Quantitative overview of the characteristics of **recent funds raised** and analysis of the **feasibility of execution of the funding plan**.
  - A forward-looking view on the (desired) **development of the funding position** over a forward-looking time horizon<sup>2</sup>.
  - An assessment of the **funding and risk positions** after execution of the funding plan.
  - **Information on back-testing** of the funding plan<sup>2</sup>.

(1) in accordance with Article 105 of Directive 2013/36/EU.  
(2) EBA GL on harmonised definitions and templates for funding plans.

# GL on ICAAP and ILAAP information

## ILAAP-specific information



**CAs should also collect information on the strategy on liquidity buffers, such as the methodology for determining the minimum level of liquid assets, the policy document on asset encumbrance, etc.; and information on the cost benefit allocation mechanism**

### ILAAP-specific information (2/3)

#### Strategy on liquidity buffers

#### METHODOLOGY AND POLICY DOCUMENTATION

- Methodology for determining the **internal minimum required size of the liquidity buffer**.
- Policy document on **collateral management**.
- Policy document on **asset encumbrance** (e.g. principles for measuring encumbered and unencumbered assets).
- Principles for **testing the assumptions** relating to the liquidity value of and time to sell/repo assets included in the buffer.
- Policy document on **liquidity concentration risk** in the liquidity buffer, including any potential loss of available liquidity due to it.

#### OPERATIONAL DOCUMENTATION

- Quantification of the **minimum volume of liquid assets** adequate to meet internal requirements and of the **current liquidity buffer**.
- Description of **differences** between the definitions of the elements of the 'counterbalancing capacity' and 'high quality liquid assets'.
- Projections of the **internally required minimum volume of liquid assets** and **available liquid assets** over appropriate time horizons under normal and stressed conditions.
- Quantitative overview and analysis of **current and projected levels of asset encumbrance**.
- Assessment of the **time it takes to convert liquid assets** into directly usable liquidity.
- Analysis of the **testing of assumptions** in relation to the liquidity value and time to sell/repo assets within the buffer.

#### Cost benefit allocation mechanism

- Description of the **mechanism** and **selection criteria** for the liquidity and funding elements and the adjustment frequency of prices.
- Description of the **interlinkages** between the mechanism and the risk management and overall management of the institution.
- The information referred to above should cover the **set-up and functioning of LTP<sup>1</sup>**.

- **Description of this mechanism** and a quantitative overview of its **current calibration<sup>1</sup>**.
- Description of the current integration of the mechanism into the **measurement of profitability** for new asset and liability generation, and into **performance management**.
- The information referred to above should cover the **functioning of LTP<sup>2</sup>**.

(1) e.g. interest rate curves, internal reference rates for main categories of assets and liabilities in use.

(2) For the institutions with liquidity transfer pricing (LTP) mechanisms in place.

# GL on ICAAP and ILAAP information

## ILAAP-specific information



The ILAAP-specific information also includes items related to intraday liquidity risk management, liquidity stress testing and the liquidity contingency plan

### ILAAP-specific information (3/3)

#### Intraday liquidity risk management

- Description of the **criteria and tools** for measuring and monitoring **intraday liquidity risk**.
- Description of the escalation procedures for intraday liquidity **shortfalls** which will ensure that settlement obligations are met on a timely basis under **normal and stressed conditions**.

#### Liquidity stress testing

- Description of the **adverse scenarios** applied and assumptions considered in **liquidity stress testing** (number of scenarios used, scope, reporting frequency, applied time horizons, etc.).
- Description of the **criteria** for calibrating scenarios, selecting appropriate time horizons, etc.

#### Liquidity contingency plan

- Description of the **lines of responsibilities** for designing, monitoring and executing the **liquidity contingency plan**.
- Description of the **strategies for addressing liquidity shortfalls** in emergency situations.
- Description of a **tool to monitor market conditions** that allow institutions to determine in a timely manner whether escalation and / or execution of measures is warranted.
- Description of **testing procedures**, where available<sup>1</sup>.

#### OPERATIONAL DOCUMENTATION

- Quantitative overview of **intraday liquidity risk** over the past year at an appropriate frequency.
- The total number of **missed payments** and an explained overview of material payments missed or material obligations not met in a timely manner.
- **Quantitative outcome**, including clear analysis and insight into the relevance of the outcome for the internal limits, liquidity buffers, etc.
- Analysis of the outcomes on the **funding profile**.
- The **current liquidity contingency plan**.
- Information on the **possible management actions**<sup>2</sup>.
- The **management view on the implications** of all liquidity-related public disclosures.
- Recent **analysis on testing**.
- Internal view on the **impact of executing the management actions** in the plan.

(1) e.g. examples of sales of new asset types, pledging collateral with central banks, etc.

(2) e.g. assessment of their feasibility under stress scenarios).



# GL on ICAAP and ILAAP information

## Supporting information on ICAAP and ILAAP



**In addition to the information items referred previously, CAs should ensure that they receive from institutions all relevant supporting information, including minutes of relevant committees and management body meetings evidencing the sound implementation of ICAAP and ILAAP**

### Supporting information

- CAs should ensure that they receive all relevant supporting information, including **minutes of relevant committees and management body meetings** evidencing the sound set-up and implementation of ICAAP and ILAAP. In particular, CAs should ensure they receive the information items below<sup>1</sup>.

#### ICAAP

- **Approval** of overall **set-up of ICAAP**.
- **Approval** of the **key ICAAP elements**, such as general objectives and main assumptions or stress scenarios.
- **Discussion** on **risk and capital situation, limit breaches**, etc., including decisions on management actions or the explicit decision not to take any action.
- Significant decisions on **new product approval committees** (or the respective decision making body).
- **Decisions on management actions** related to internal capital estimates, their aggregation and their comparison to the available internal capital.
- **Discussion on the outcome of stress testing** in ICAAP and decision on management action.
- Where available, **internal self-assessments** in which institutions can justify their level of compliance against publicly available criteria regarding risk management and control that affect ICAAP.

#### ILAAP

- **Approval** of overall **set-up of ILAAP**.
- **Approval of key ILAAP elements** (e.g. funding plan, liquidity contingency plan, etc.).
- **Discussion** on the **liquidity and funding risk profile**.
- Decisions in **new product approval committees**.
- **Discussion** of the **feasibility of the funding plan**.
- **Decisions on management actions** related to intraday liquidity risk, where relevant.
- **Discussion of the outcome of Liquidity Stress Tests** and decision on any management actions.
- Discussion on the **regular testing of the liquidity contingency plan**.
- Decision relating to the **size and composition of the liquid asset buffer**.
- Discussion regarding the **testing of the liquidity value** of and **time to sell/repo assets** included in the buffer.
- Where available, **internal self-assessments** in which institutions can justify their level of compliance against publicly available criteria regarding risk management and control that affect ILAAP.

(1) Discussion and decisions require evidence, in both ICAAP and ILAAP processes.

# GL on ICAAP and ILAAP information

## Information on conclusions and quality assurance



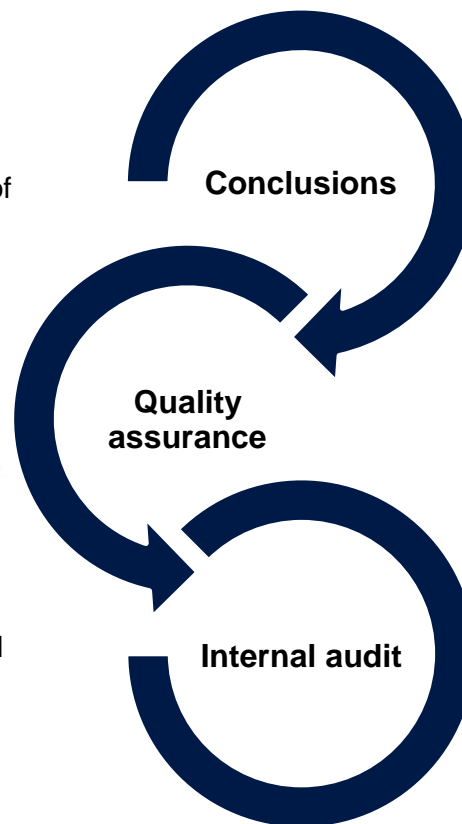
**CAs should collect from institutions the findings arising from the assessments; an adequate explanation of how they ensure that the ICAAP and ILAAP frameworks provide reliable results, including information on validation; and the internal audit reports covering ICAAP and ILAAP**

### Information on conclusions and quality assurance

- Conclusions of the **ICAAP and ILAAP**.
- Impact on the **risk and overall management** (including summary of main conclusions in order to form a concise view of the current capital and liquidity position of the institution; material changes to the risk management framework; to business models, strategies or risk appetite frameworks; and to ICAAP and ILAAP frameworks)<sup>1</sup>.



- **Internal audit reports** covering ICAAP and ILAAP.



- Adequate explanation of **how institutions ensure** that the ICAAP and ILAAP frameworks used provide **reliable results** (validation concepts, validation reports).
- Description of both the internal **validation approach** (process, frequency) and the **validation content**. This includes all available results of the internal validations/reviews of ICAAP/ILAAP methodologies and calculation outcomes performed by **independent validation function**.



(1) Competent authorities should ensure that this information has the approval by the pertinent body within the governance framework responsible for the ICAAP and ILAAP. Moreover, it should be accompanied by specific timelines associated with the planned changes.

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# ECB supervisory expectations and Draft Guides to the ICAAP-ILAAP

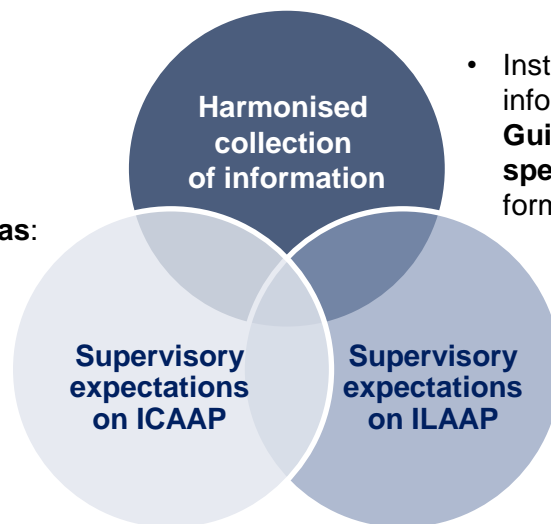
## Supervisory expectations – Overview

The ECB published in January 2016 a document specifying that significant institutions within the SSM shall follow these Guidelines, and setting out a set of supervisory expectations with regard to the ICAAP and the ILAAP

### Overview

- The experience of 2015 revealed that the **information submitted by significant institutions on their ICAAPs and ILAAPs was often not in line with Single Supervisory Mechanism (SSM) expectations**. This partly reflected a wide range of practices within SSM countries so far.
- In order to encourage institutions to develop and maintain high-quality ICAAPs and ILAAPs, and to clarify the type of information they should share with the SSM on these, the ECB document includes provisions with regard to the **harmonized collection of information**, and **supervisory expectations on the ICAAP and the ILAAP**.

- The document sets out baseline expectations with regard to **9 ICAAP areas**:
  - Governance.
  - General design of the ICAAP.
  - ICAAP perspective.
  - Risks considered.
  - Definition of internal capital.
  - Assumptions and key parameters.
  - Inter-risk diversification effects.
  - Severity level of stress tests.
  - Stress testing scenario definition.



- Institutions shall submit ICAAP and ILAAP information as spelled out in the **EBA Guidelines**, but taking into account the **specifications** concerning the delivery dates, formats and content.
- The document sets out expectations with regard to **2 ILAAP areas**:
  - General definition of the ILAAP.
  - ILAAP reporting.

# ECB supervisory expectations and Draft Guides to the ICAAP-ILAAP

## Supervisory expectations – Harmonised collection of information



**Significant institutions within the SSM shall submit the information items as spelled out in the EBA Guidelines, but taking into account some specifications regarding dates and format, contents, risk measurement assessment and aggregation for ICAAP...**

### Harmonised collection of information (1/2)

#### Dates and format

- ICAAP and ILAAP information shall be provided electronically to the relevant joint venture team (JST) by **30 April**, with the **preceding year-end** as the reference date<sup>1</sup>.
- Information should be provided according to **levels of application of ICAAP and ILAAP** set out in the CRD IV.
- However, for the **2016 SREP**, the assessment will mainly focus on the **consolidated level**<sup>2</sup>.
- Institutions are requested to provide a **reader's manual**, containing:
  - An overview of the documents and their status, highlighting, where relevant, material changes since the last submission.
  - An overview of where the information items specified in the EBA GL and in the specifications can be found in the documentation (or if information items are not included, an explanation why the item is not relevant).

#### Contents

- Institutions are expected to **provide all information items** mentioned in the EBA GL or explain why the items are not relevant for the, taking into account the size, complexity and business model of the institutions.
- Institutions may include **examples of such information** in their information package for areas where it may be seen as important evidence of their compliance with the regulatory requirements. Where they decided not to submit detailed documentation, institutions should be transparent about this.

#### Risk measurement assessment and aggregation ICAAP

- The descriptions of the main **differences** between models used for ICAAP and those used for minimum own funds requirements should be complemented by a **quantitative reconciliation**<sup>3</sup>.
- Institutions should use a **template**<sup>4</sup> to annually provide information on their **risk categories and sub-categories**.
- Accordingly, institutions are expected to fill in the template using the numbers they have produced for internal purposes and in line with internal risk taxonomy.

(1) There are some exceptions (e.g. institutions with a fiscal year differing from the calendar year).

(2) Exceptions will be communicated to institutions on a case-by-case basis.

(3) The ECB specifies that the description of the main differences should also be provided by banks not using advanced Pillar 1 approaches.

(4) Included within an Annex of the ECB document.

# ECB supervisory expectations and Draft Guides to the ICAAP-ILAAP

## Supervisory expectations – Harmonised collection of information



...internal capital and capital allocation, supporting documentation relating to the ILAAP, and conclusions and quality assurance items

### Harmonised collection of information (2/2)

#### Internal capital and capital allocation

- The description of the **main differences** between internal capital element/instruments and regulatory own funds instruments should be complemented by a **quantitative reconciliation**.

#### Supporting documentation ILAAP

- Of particular importance is the **self-assessment** to justify the institution's level of compliance against publicly available criteria regarding risk management and control that affect ILAAP. This self-assessment should be provided using a **template**<sup>1</sup>.

#### Conclusions and quality assurance

- Concerning the ICAAP, institutions should provide a **concise statement about their capital adequacy**, supported by an analysis of the ICAAP set-up and outcomes and signed by the management body. It should contain an explicit internal definition of capital adequacy and the relevant outcomes from the ICAAP, including the forward-looking view of the main factors affecting capital adequacy.
- Concerning the ILAAP, institutions should provide a **concise statement on the liquidity adequacy**, signed by the management body. This statement should be in line with current risk appetite and provide an overview of the current liquidity and funding position.
- The statement should be substantiated by relevant arguments and facts supporting the conclusion, covering both the **short-term** (liquidity) and **longer-term** (funding) view.

(1) Included within an Annex of the ECB document.

# ECB supervisory expectations and Draft Guides to the ICAAP-ILAAP

## Supervisory expectations – ICAAP



Although institutions remain responsible for the design of the ICAAP, the ECB document sets out supervisory baseline expectations. These expectations are related to nine areas of the ICAAP: governance, general design of the ICAAP, ICAAP perspective, risks considered...

### Supervisory expectations on ICAAP

#### Governance

- The **ICAAP key elements** (e.g. governance structure; risks and perimeter captured, time horizon, key risk measurement assumptions and parameters) should be approved by the **management body**.
- Institutions should produce, at least once per year, a **clear formal statement** on their capital adequacy supported by an analysis of ICAAP outcomes and approved by the management body. Institutions should additionally integrate ICAAP related outcomes into their **internal reporting**<sup>1</sup>.

#### General design of the ICAAP

- The shorter-term perspective of usually one year has to be complemented by a **longer-term forward-looking process**<sup>2</sup>, including capital planning and the use of adverse scenarios.
- All the quantitative parts have to be fully interlinked with institutions' strategies, business decision-making and risk management processes. The strategies and processes have to be consistent and coherent throughout the group / financial conglomerate.

#### ICAAP perspective

- Institutions are expected to implement a proportionate ICAAP approach aimed at the survival of the institution and the fulfilment of requirements. In addition, institutions should take into account a **sound economic perspective** as a basis for their ICAAP (i.e. also consider migration risk, hidden losses, etc.).

#### Risks considered

- Institutions are responsible for implementing a regular **process for identifying all material risks** they are or might be exposed to. Institutions should take into account **at least the following risks**<sup>3</sup>:
  - **Credit risk** (including FX lending risk, country risk, credit concentration risk, migration risk).
  - **Market risk** (including credit spread risk, structural FX risk).
  - **Operational risk** (including conduct risk, legal risk, model risk).
  - **Interest rate risk in the banking book** (also including optionalities such as prepayment options).
  - **Participation risk, sovereign risk, pension risk, funding cost risk, risk concentrations, business and strategic risk** and, in the case of financial conglomerates and for material participations, **other inherent risks** (e.g. insurance risk).

(1) The frequency of the internal reporting should be at least quarterly, although depending on the institution, its business model and risk types, it should be monthly.

(2) Usually a three-year horizon.

(3) Or where these are not applicable, explain why they are considered immaterial.

# ECB supervisory expectations and Draft Guides to the ICAAP-ILAAP

## Supervisory expectations – ICAAP



...definition of internal capital, assumptions and key parameters, inter-risk diversification effects, severity level of stress tests, and stress testing scenario definition

### Supervisory expectations on ICAAP

#### Definition of internal capital

- The definition of internal capital has to be consistent with the ICAAP perspective on capital needs. The SSM has the expectation that **internal capital will be of sound quality** (e.g. where the definition is linked to regulatory own funds, it is expected that a large part of internal capital components will be CET1).

#### Assumptions and key parameters

- Institutions are responsible for **setting key parameters and assumptions** (confidence levels, holding periods, etc.) that are **adequate** for their individual circumstances.
- The parameters and assumptions should be in line with their risk appetite, market expectations, business model, and risk profile (i.e. parameters should be consistent with the assumed scenarios at all levels).

#### Inter-risk diversification effects

- Institutions should be aware that the **supervisor will not take into account inter-risk diversification** in the SREP.
- When applying inter-risk diversification effects, institutions are expected to be **transparent** about them. Moreover, institutions should consider that most of the **diversification effects disappear** in times of stress or behave in non-linear ways.

#### Severity level of stress tests

- Scenarios have to be tailored towards the institution's **individual key vulnerabilities**.
- Institutions are expected to conduct **reverse stress testing** in a proportionate manner.

#### Stress testing scenario definition

- At least once a year, institutions shall perform an **in-depth review of their vulnerabilities**.
- On the basis of that review, they shall define a **set of stress testing scenarios** to inform the capital planning process in addition to using a baseline scenario in their ICAAPs.
- Institutions should continuously monitor new threats, vulnerabilities, etc. to assess whether their **stress testing scenarios remain appropriate**.
- It is expected that the scenarios will be **reconfirmed and used periodically** (e.g. quarterly) to monitor potential effects on the relevant capital adequacy indicators over the course of the year.



# ECB supervisory expectations and Draft Guides to the ICAAP-ILAAP

## Supervisory expectations – ILAAP



Finally, the ECB also lays down some supervisory expectations on the ILAAP, with regard to its general definition and reporting

### Supervisory expectations on ILAAP

#### General definition of the ILAAP

- Institutions should produce, at least once per year, a **clear and formal statement** on their liquidity adequacy, supported by an analysis of ILAAP outcomes and approved by the management body. Institutions should additionally integrate ILAAP outcomes into their **internal reporting**.
- Institutions are expected to implement a proportionate ILAAP approach aimed at the survival of the institution. In addition, institutions should take into account a **sound economic perspective** as a basis for their internal view (i.e. considering all material risks to liquidity and funding, taking into account both macro and idiosyncratic perspectives)<sup>1</sup>.

#### ILAAP reporting

- The institution is requested to state explicitly in the reader's manual and self-assessment which documentation and **information items** are **not covered** owing to the proportionality principle.
- The internal liquidity adequacy statement of the bank should be **aligned with the risk appetite** of the bank and must be signed by the **management body**.
- The additional information submitted as part of the **short-term exercise** (relating to the liquidity coverage ratio, the net stable funding ratio, etc.) play an important role in the quantitative assessment of the ILAAP in the SREP. Institutions are requested to ensure **reliable and complete reporting**.

(1) In this regard, institutions are encouraged to take into account the existing guidance on liquidity buffers and survival periods (i.e. EBA Guidelines on Liquidity Buffers & Survival Periods), as well as the risk drivers listed in the SREP Guidelines.

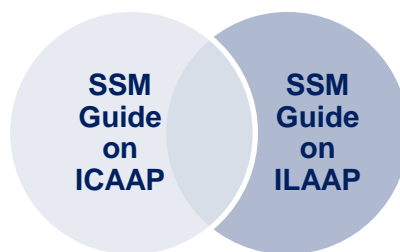
# ECB supervisory expectations and Draft Guides to the ICAAP-ILAAP

## Draft Guides – Overview

The ECB launched in March 2018 a public consultation on its Draft Guides to the ICAAP and ILAAP. The final version of these Guides and their principles will be considered in the assessment of each institution's ICAAP and ILAAP as a part of the SREP<sup>1</sup>

### Overview

- The experience of 2016 ICAAP and ILAAP exercises showed that there are still several areas in which improvements are necessary across banks. In order to foster these improvements, the ECB **initiated a multi-year project** in February 2017 to develop **comprehensive SSM Guides on ICAAP and ILAAP for Sis**.
- Further, in March 2018 the ECB published **Draft Guides to the ICAAP and to the ILAAP** with the aim of developing a more detailed set of supervisory expectations regarding these processes<sup>2</sup>. In particular, these Draft Guides cover the following aspects:
  - The document sets out **7 principles** for the SSM Guide on ICAAP:
    1. The management body is responsible for the sound **governance** of the ICAAP
    2. The ICAAP is an integral part of the overall **management framework**
    3. The ICAAP contributes fundamentally to the **continuity** of the institution by ensuring its capital adequacy from different perspectives
    4. All **material risks** are identified and taken into account in the ICAAP
    5. **Internal capital** is of high quality and clearly defined
    6. ICAAP **risk quantification methodologies** are adequate, consistent and independently validated
    7. Regular **stress testing** is aimed at ensuring capital adequacy in adverse circumstances
  - The document sets out **7 principles** for the SSM Guide on ILAAP:
    1. The management body is responsible for the sound **governance** of the ILAAP
    2. The ILAAP is an integral part of the overall **management framework**
    3. The ILAAP contributes fundamentally to the **continuity** of the institution by ensuring its liquidity adequacy from different perspectives
    4. All **material risks** are identified and taken into account in the ILAAP
    5. The **internal liquidity buffers** are of high quality and clearly defined; the **internal stable sources of funding** are clearly defined
    6. ILAAP **risk quantification methodologies** are adequate, consistent and independently validated
    7. Regular **stress testing** is aimed at ensuring liquidity adequacy in adverse circumstances



(1) These Guides are not relevant for SREP 2018.

(2) The final Guides will replace the 2016 ICAAP and ILAAP expectations with effect from 2019.

# ECB supervisory expectations and Draft Guides to the ICAAP-ILAAP

## Draft Guides – ICAAP



The ECB principles on the ICAAP are related to governance, management framework, continuity of the institution, material risks...

### Supervisory expectations on ICAAP (1/2)

#### Principle 1 – governance

- The **ICAAP key elements** (e.g. governance structure, documentation requirements, and the methodology used to assess capital adequacy) should be approved by the **management body**.
- The management body is expected to provide, on annual basis, a **Capital Adequacy Statement (CAS)** expressing its view on capital adequacy and main supporting arguments, including ICAAP outcomes.
- The management body has overall responsibility for the implementation of the ICAAP and shall **approve its governance framework**, which will be subject to regular internal review and validation.

#### Principle 2 – management framework

- Institutions are expected to have in place an **adequate quantitative** and **qualitative framework** for assessing capital adequacy, which should be consistent with each other and with the institution's business strategy and risk appetite. They are also expected to maintain a sound and effective overall ICAAP architecture and documentation of the interplay between the ICAAP elements.
- The ICAAP is expected to be integrated into the **business, decision-making** and **risk management processes** of the institution, as well as to be consistent and coherent throughout the group.

#### Principle 3 – continuity of the institution

- Institutions are expected to implement two complementary perspectives: i) the **normative perspective**, aimed at the fulfilment of capital-related regulatory and supervisory requirements; and ii) the **economic perspective**, considering all risks and losses that may cause economic losses and deplete internal capital (e.g. migration risk, hidden losses). The capital plan is expected to comprise baseline and adverse scenarios and to cover a forward-looking horizon of at least three years.

#### Principle 4 – material risks

- Institutions are responsible for implementing a regular **process for identifying all material risks** they are or might be exposed to. Institutions should identify at least annually risks that are material, based on:
  - The **risk identification process**, which should consider both normative and economic perspectives, and any risks and concentrations arising from pursuing their strategies.
  - A **risk inventory**, which is a list of underlying risks stemming from its financial and non-financial participations, subsidiaries, etc. (e.g. step-in and group risks, or reputational and operational risks).
- For all material risks, institutions are expected to **allocate capital** (or justify the reasons for not holding it).

# ECB supervisory expectations and Draft Guides to the ICAAP-ILAAP

## Draft Guides – ICAAP



### ...definition and quality of internal capital, risk quantification methodologies, and stress testing

#### Supervisory expectations on ICAAP (2/2)

##### Principle 5 – internal capital

- Institutions are expected to define, assess and maintain **internal capital under the economic perspective**. The definition of internal capital is expected to be consistent with the economic capital adequacy concept and internal risk quantifications of the institution.
- **Internal capital** is expected to be of **sound quality**, and determined in a **prudent and conservative manner**. The institution is expected to show clearly, assuming the continuity of its operations, how its internal capital is available to cover risks, thereby ensuring that continuity.

##### Principle 6 – risk quantification methodologies

- Institutions are responsible for implementing **risk quantification methodologies** adequate for their individual circumstances under the economic and normative perspectives. They are also expected to apply a very high level of **conservatism under both perspectives**.
- The **key parameters and assumptions** (e.g. confidence levels, and holding periods) are expected to be **consistent** throughout the group and between risk types.
- All risk quantification methodologies should be subject to **independent internal validation**.
- The institutions are expected to establish and implement an **effective data quality framework**.

##### Principle 7 – stress testing

- At least once a year, institutions shall perform a **review of their vulnerabilities**, capturing all material risks on an institution-wide basis that result from their business model and operating environment in the context of stressed macroeconomic and financial conditions.
- On the basis of this review, they are expected to define an **adequate stress testing programme** for both normative and economic perspectives. As part of the stress-testing programme, institutions are expected to determine adverse scenarios to be used under the normative perspective, taking into account other stress tests they conduct.
- In addition, institutions are expected to conduct **reverse stress testing** in a proportionate manner.
- Further, institutions should continuously **monitor and identify new threats, vulnerabilities and changes** to assess at least quarterly whether their stress testing scenarios remain appropriate and, if not, adapt them to the new circumstances.

# ECB supervisory expectations and Draft Guides to the ICAAP-ILAAP

## Draft Guides – ILAAP



Likewise, the ECB principles on the ILAAP are established in relation to governance, management framework, continuity of the institution, material risks considered...

### Supervisory expectations on ILAAP (1/2)

#### Principle 1 – governance

- The **ILAAP key elements** (e.g. governance structure, and documentation requirements) should be approved by the **management body**.
- The management body is expected to provide, on annual basis, a **Liquidity Adequacy Statement (LAS)** expressing its view on liquidity adequacy and main supporting arguments, including ILAAP outcomes.
- The management body shall **implement the ILAAP** and approve its governance framework (with a clear and transparent assignment of responsibilities), which will be subject to **regular review** and **validation**.

#### Principle 2 – management framework

- Institutions are expected to have in place an **adequate quantitative** and **qualitative framework** for assessing liquidity adequacy, which should be consistent with each other and with the institution's business strategy and risk appetite.
- The ILAAP is expected to be integrated into the **business, decision-making** and **risk management processes** of the institution, as well as to be consistent and coherent throughout the group.

#### Principle 3 – continuity of the institution

- Institutions are expected to implement a **proportionate ILAAP approach** that is prudent and conservative and integrates both complementary internal perspectives (normative and economic). The ILAAP is aimed at maintaining the continuity of the institution by ensuring an adequate liquidity and funding position.
- Institutions are expected to have a formal **Liquidity Contingency Plan (LCP)** that clearly sets out the measures for addressing liquidity difficulties under stressed circumstances.

#### Principle 4 – material risks

- Institutions are responsible for implementing a **regular process for identifying all material risks** they are or might be exposed to. Institutions should identify, at least annually, risks that are material, based on:
  - The **risk identification process**, which should consider both normative and economic perspectives, and any risks and concentrations arising from pursuing their strategies.
  - A **risk inventory**, which is a list of underlying risks stemming from its financial and non-financial participations, subsidiaries, etc. (e.g. step-in and group risks, or reputational and operational risks).
- For all risks identified, institutions should either cover the risks with **sufficient liquidity** or **document the justification for not holding the liquidity**.

# ECB supervisory expectations and Draft Guides to the ICAAP-ILAAP

## Draft Guides – ILAAP



### ...definition and quality of the internal liquidity buffers, risk quantification methodologies, and stress testing

#### Supervisory expectations on ILAAP (2/2)

##### Principle 5 – internal liquidity buffers

- Institutions are expected to define **internal liquidity buffers and stable sources of funding** under the economic perspective, consistently with the economic liquidity adequacy concept and internal risk quantifications of the institution.
- The internal liquidity buffers are expected to be of **sound quality**, and determined in a prudent and **conservative manner**, and the sources of funding are expected to be stable to ensure that business operations can also continue in the longer term.

##### Principle 6 – risk quantification methodologies

- Institutions are responsible for implementing **risk quantification methodologies** that are adequate for their individual circumstances under both the economic and normative perspectives. They are also expected to apply a very high level of **conservatism under both perspectives**.
- The **key parameters and assumptions** (e.g. confidence levels and holding periods) are expected to be **consistent** throughout the group and between risk types.
- All risk quantification methodologies should be subject to **independent internal validation**.
- The institutions are expected to establish and implement an **effective data quality framework**.

##### Principle 7 – stress testing

- Institutions shall perform a regular tailored and in-depth **review of their vulnerabilities**, capturing all material risks on an institution-wide basis that result from their business model and operating environment (in the context of stressed macroeconomic conditions), on a yearly basis and more frequently, if necessary.
- On the basis of this review, they are expected to define an **adequate stress testing programme** for both normative and economic perspectives. As part of the stress-testing programme, institutions are expected to determine adverse scenarios to be used under the normative perspective, taking into account other stress tests they conduct.
- In addition, institutions are expected to conduct **reverse stress testing** in a proportionate manner.
- Further, institutions should continuously **monitor and identify new threats, vulnerabilities and changes** to assess at least quarterly whether their stress testing scenarios remain appropriate and, if not, adapt them to the new circumstances.

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➡ Next steps

# Next steps

The final Guides to the ICAAP and to the ILAAP will be published in the second half of 2018 and will replace the 2016 ICAAP and ILAAP expectations with effect from 2019

## Timing

