



Template for comments

Public consultation on the draft addendum to the ECB guidance to banks on non-performing lo

Institution/Company

MAZARS GROUP

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Please tick here if you do not wish your personal data to be published.

General comments : Please refer to our cover letter

Template for comments

Public consultation on the draft addendum to the ECB guidance to banks on non-performing loans

Please enter all your feedback in this list.

When entering feedback, please make sure that:

- each comment deals with a single issue only;
- you indicate the relevant article/chapter/paragraph, where appropriate;
- you indicate whether your comment is a proposed amendment, clarification or deletion.

Deadline: 8 December 2017

| ID | Chapter | Paragraph | Page | Type of comment | Detailed comment | Concise statement as to why your comment should be taken on board | Name of commenter | Personal data |
|----|---------------------|-----------|------|-----------------|---|--|-------------------|---------------|
| 1 | 2 - General Concept | 2.1 | 3 | Amendment | "Finally, the backstops are applicable at a minimum to new NPEs classified as such from January 2018 onward." | it should be made clear that backstops are applicable only to new NPEs classified as such from January 2018 onward, "at a minimum" should be deleted | | Publish |
| 2 | 2 - General Concept | 2.1 | 3 | Amendment | "In line with the NPL Guidance, this addendum applies to all significant banks directly supervised by the ECB " | there is a risk of level playing if only applicable of SI, the SSM should clearly requires NCA to apply similar rules to LSI. Besides, the scope of application should be clarified notably for subsidiaries of SSM banks located outside the eurozone | | Publish |
| 3 | 2 - General Concept | 2.3 | 5 | Clarification | " If the applicable accounting treatment is not considered prudent from a supervisory perspective" | it would be worth that the SSM clarify to what extent it may consider that an accounting treatment is not prudent. In such cases could the SSM clarify that banks will be asked to apply own funds deduction in accordance with CRR article 3 ? | | Publish |
| 4 | 2 - General Concept | 2.3 | 5 | Clarification | "...and, crucially, the NPE vintage category." | the SSM should explicit the calibration of its backstops since it does not fit current legal proceedings of collateral realisation in some countries | | Publish |

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|----|--------------------------------------|-------|----|---------------|--|---|--|---------|
| 5 | 2 - General Concept | 2.3 | 6 | Clarification | "deviations from the backstops are possible[...] and on the basis on acceptable evidence[...]payments amounting to a significant portion...[...][...]the application of backstop is not reasonable in justified circumstances" | could the SSM clarify how it will assess: - that an evidence will be considered as acceptable or not ? - what a significant portion is (20% ? Others ?) - which kind of circumstances are envisaged ? | | Publish |
| 6 | 3 - Definitions | 3.1 | 7 | Clarification | "Thus, the vintage count for "unlikely to pay" and "past due" exposures is the same, and for exposures moving from "unlikely to pay" to "past due" the counting continues and is not reset" | NPE is related to status of default, which is by the way related to the default materiality threshold and not harmonised so far (common materiality threshold will only apply as of 2021). Until that date could the SSM provide guidance for a common threshold to be used for NPE designation ? | | Publish |
| 7 | 3 - Definitions | 3.2 | 7 | Clarification | "This is based on the principle that the prudential regime has to deviate from the accounting treatment if that treatment is not considered prudent..." | same statement as for ID 3 | | Publish |
| 8 | 3 - Definitions | 3.2a) | 7 | Amendment | "All types of immovable property collateral" | It should be made clear that guarantees that secured residential loans are considered collateral as well, an amendment is desirable to explicit it. | | Publish |
| 9 | 3 - Definitions | 3.2b) | 7 | Amendment | "other eligible collateral[...]that fulfil the criteria...of Chapter 4 of the CRR, irrespective of whether an institution uses the standardised approach or the internal ratings-based approach." | Article 108(2) of CRR states that institutions may use CRM in accordance with Chapter 3 for A-IRB exposures. Hence 3.2b should be amended as follows "...Chapter 3 and 4 of the CRR irrespective of whether..." | | Publish |
| 10 | 3 - Definitions | 3.3 | 9 | Clarification | "the collateral value should be regularly reviewed..." | could the SSM clarify what is an appropriate frequency of review from a supervisory perspective (excluding immovable property) ? | | Publish |
| 11 | 4 - Prudential provisioning backstop | 4.1 | 10 | Amendment | "This means that full prudential provisioning is required after seven years" | The SSM is not entrusted to adopt binding regulation for all banks. Accordingly it is not supposed to require full provisioning. An amendment is desirable : replacing required by would be expected. | | Publish |
| 12 | 4 - Prudential provisioning backstop | 4.1 | 10 | Deletion | "it is immaterial whether the delays in realising the security were due to reasons beyond the banks control" | This provision should be removed as it seriously marginalised the concept of risk mitigation | | Publish |
| 13 | 4 - Prudential provisioning backstop | 4.2 | 11 | Deletion | "banks should assume at least a linear path for the backstop" | There is no valid reason to require banks to apply any prudential backstop linearly for fully secured exposures | | Publish |

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|----|-----------------------------------|---|----|---------------|---|---|------------|---------|
| 14 | 5 - Related supervisory reporting | 5 | 12 | Clarification | "...with regard to the newly classified NPE after 1 january 2018" | This provision contradicts paragraph 2.1. See our statement ID 1 | ██████████ | Publish |
| 15 | 5 - Related supervisory reporting | 5 | 12 | Deletion | "a public disclosure of NPE coverage by vintage" | Prior to any disclosure requirement, the SSM should carefully assess the risk of potential side effects of undesired disclosure | ██████████ | Publish |
| 16 | 5 - Related supervisory reporting | 5 | 12 | Clarification | "The JSTs will provide banks with further details regarding this process, and the related templates, sufficiently in advance" | The SSM has to ensure that data will not be redondant with data already required otherwise. Moreoever any templates has to be provided to banks sufficiently in advance in order for them to be prepared. | ██████████ | Publish |

Cover letter – Mazars’ response to the European Central Bank (« ECB ») in respect of the public consultation on the draft addendum to the ECB Guidance to banks on non-performing loans (NPLs)

Paris, December 8th 2017

Mazars welcomes the opportunity to comment on the ECB draft addendum to the ECB Guidance on non-performing loans (NPLs) which has been published the 4th of October 2017, following the consultation initially made the 12th of September 2016.

As per our previous response to the ECB consultation on the draft Guidance on management of NPLs, we reiterate our support to the ECB’s initiative to clarify banking supervision expectations going forward, address the NPLs reduction issue and allow the banks to strengthen their balance sheet to refocus on their core businesses.

However, if the purpose of the ECB Guidance published as of March 2017 to encourage banks to have a strong governance and an appropriate NPLs management is relevant, we question the objective of this addendum of setting minimum level of prudential provisioning after many years of vintage, for all banks under the direct ECB’s remit. We understand it is not the ECB’s intention to issue a binding regulation, yet recent opinions issued by the European Parliament and the Council of the EU state that the ECB does not have the mandate for its bad loan measure. Indeed, as per EU rules, supervisors may only impose binding capital measures on specific banks but not on the entire banking system.

Solving the issue of the high level of NPLs is on the top of the agenda of several regulators, as shown by the issuance of the consultative document by the European Commission on the “statutory prudential backstops addressing insufficient provisioning for newly originated loans that turn non-performing”. We therefore encourage the ECB to limit or avoid any potential areas of redundancy in its draft guidance, against the background of pending decisions of an NPLs Pillar I framework at the EU level. Regulatory uncertainty and the overlap of different regulations ruling the same topic might be not well perceived by the markets and could impair the ability of the banks to properly plan their future actions.

Beyond these general comments regarding the status of this draft addendum to ECB’s Guidance on NPLs, we think it may raise other issues, which are listed below.

A same level playing field issue in relation to...

...the **scope of application** since the addendum would only apply to Significant Institutions (SI) which are under the direct supervision of the ECB. If National Competent Authorities (NCA) responsible for the Less Significant Institutions (LSI) decide not to apply the prudential provisioning backstop to them, there might be unintended consequences such that LSIs pile up bad loans and major lenders be deterred to finance economy.

Besides we would welcome further clarification in the draft addendum in relation to scope of application since it is not so clear whether subsidiaries - of significant banks - located outside the SSM area are subject to the addendum and therefore to the prudential provisioning backstop as well.

...the lack of harmonisation of legal insolvency and recovery procedures between EU Member States since each country has its own procedures in terms of insolvency and recovery. Thus, the prudential provisioning backstop may be more penalising for certain countries where legal procedures are structurally longer than for countries where legal framework allow faster procedures and recovery. Due to the lack of homogeneity between countries, would it be an option that:

- The ECB rather considers its backstop as a target and sets up transitional phase for dealing with exceptions;
- or the ECB should ensure that each bank have appropriate loan loss provisioning level resulting from a constructive dialogue with the bank and without imposing the same backstop which would be seen as a minimum requirement level, binding for all banks under ECB's direct supervision

In addition, local risk classifications have not yet been superseded by the harmonised definition of NPE, as this is an "umbrella term". For long lasting legal procedures for credit recovery, what matters in terms of timing of recovery is the point in time where the legal procedure starts, which may or may not be aligned with the timing of "unlikeliness to pay". As such, the starting point for any sort of calendar provisioning should be when the legal procedure starts instead of when the loan is classified as UTP.

A calling into question of current prudential regulations and accounting standards

The prudential provisioning backstop may conflict with the legislative provisions currently in force and could alter the existing regulatory framework. It questions the accounting recognition of provisions that reflects the economic reality and may give bad signals to markets or users that accounted provisions are insufficient or insincere, even if compliant with the accounting standards. It could therefore supersede accounting standards, and potentially the new IFRS 9 which will entry into force as of January 2018, and will force banks to be more predictive in terms of loan loss provisioning.

Besides if banks were to decide to sell NPLs portfolios to external investors, they might be in a position of accepting lower prices as time goes by, in connection with an ultimate 100% level of provisioning required after 7 years of vintage. This might also have consequences on collateral, which would not be considered anymore for cost of risk computation even if compliant with CRR current minimum requirement for risk mitigation techniques eligibility. This might divert banks to monitor closely and strengthen their procedures in terms risk mitigation procedures and recovery. Moreover, it would be necessary to clarify the treatment of guarantees, which seem to be missing in the draft addendum.

Finally the addendum should be more explicit that the ECB will only act within the context of the Pillar II

And more specifically that the ECB will only give guidance to banks on their appropriate level of prudential provisioning, i.e. P2G "Pillar II Guidance", since the P2R "Pillar 2 Requirement" can only be used for capital requirements in relation to risks non-covered by Pillar 1 minimum requirements.

Our targeted comments to specific paragraphs of the draft addendum are listed in the attached template.

We thank you in advance for the consideration you may give to our letter and remain at your disposal should you have any questions.

Yours sincerely,

Emmanuel Dooseman
Partner, Global Head of Banking

