Transcript of the public hearing on the addendum to the ECB Guidance on non-performing loans held on 30 November 2017 at the ECB's Main Building premises in Frankfurt am Main.

Panel participants

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Question: As you know, one of the questions that banks might have is about the operational complexity of the expectations. So, will the expectations be targeting the specific exposure in terms of reporting, or more at a portfolio level?

Nouy: The complexity is not that big because what the ECOFIN measures are recommending is a Pillar 1 measure that will take some time to be implemented. You could have mentioned IFRS 9 as well; that will be implemented in parallel. But it will take some time to be fully covering the portfolios. Obviously if the ECOFIN decides to go for a Pillar 1 measure, that's to say legislative measures, once it is applicable and once it is addressing all the portfolios, we will adapt our own measures. So regarding our measures, these relate to the new NPEs, which is indeed a difference with the ECOFIN, which is targeting new loans. But we think that now is the moment to address NPEs, in particular because we are enjoying good economic conditions in the euro area. If we wait until there is a Pillar 1 text first, and then it is covering only new loans, we have to keep in mind that the full rolling over of the existing loan book can take a decade.

So we have also to address, in my view, the future NPLs until we have measures that will be implemented and fully rolled over the whole portfolio. So there is a sequence and we are ready to adapt our own guidance once there is something else. But still, there will stay room for Pillar 2.

We have first of all the accounting provisions. And the powers of the supervisors start when the accounting provisions are not sufficient. With IFRS 9, the provisions are less likely to be insufficient because they will be covering also expected losses. If there is a Pillar 1 tool one day then we will have only a smaller remaining part to address, for sure.

Donnery: Maybe I'll just add briefly, that regardless of the addendum - even leaving aside the addendum and its application to new NPLs - I think in general we would expect banks of course to have policies, practices and procedures for dealing with their provisioning. We would look at that through both a portfolio lens and a case-by-case individual bank file lens: for example, if we're doing on-site inspections, where we would look at examples of files. Certainly I think in terms of our expectations we're saying that banks need to look at individual loans and see where they are against these expectations. But of course we accept that there has to be a kind of practical way to implement that. This will be part of what we would discuss with the bank. I think that's particularly important where we'd be discussing for example, if it wasn't going to apply, the reasons why particular loans or particular portfolios of loans, for example, didn't require this type of treatment.

Question: I'm wondering in practical terms, when the vintage actually kicks in - once you have a loan that is considered defaulted, it usually takes three months, six months, nine months, maybe 12 months until the whole process has been set up, so everything is being done to restructure a loan. Now, is that period of time already being considered the relevant period of time by when you would have to provision such a loan? Once it has been restructured, is there any sort of cure period you have to be aware of until you can put it back into the good bank or the good book, so to speak?

The second question, derived from the answer of the previous one, did I understand that correctly, that given the IFRS 9 implementation is happening in just in a couple of weeks [Jan 1 2018] , would you consider that to be a double whammy for the banks in terms of stage 2 loans being considered, in terms of LLPs [loan loss provisions] or provisioning, plus the intended provisioning under your addendum?

Nouy: Well, a lot of good questions in this one. I will start with certain elements and then I will hand over to Sharon. First of all, you are describing first a process which is very much related to the statutory auditors and accounting process; and there is a separation between the accounting and the prudential. We are not authorised, as supervisors, to interfere with the work of accountants, statutory auditors, and also with accounting rules – which can be quite different in Europe because some banks are using IFRS, and some banks as well are using their own national general accounting principles, meaning we can have 20 different accounting systems, each with its own vocabulary and its own operational steps. So keeping that as it is, we come after the accounting provisions. The supervisory perspective comes after. Indeed you are right, the supervisory perspective now will have to take into account that the accounting rules, at least for IFRS – the international accounting standards - have changed. We had IAS39, now we have IFRS9.

So it means that when it is implemented, and it will take some time because the phasing-in is pretty long , we will look at what we consider insufficient as provisions from the supervisory perspective – so totally different – it's likely after IFRS that it will be better covered by provisions, - the credit risk - and we will intervene later. So that's the sequence and for us, we use as prudential [supervisors] a single definition of NPEs. This is the definition that has been produced by EBA [European Banking Authority]. It was a significant step forward to have a single definition of NPEs for the entire European market. This is what allowed us to undertake a consistent comprehensive assessment in 2014 [across all banks]. There are different ways of categorising non-performing exposures, but the good approach is to follow the EBA definition.

Donnery: So I start there actually with the EBA definition because I think it has been a very important point of progress. Both the addendum, and our earlier qualitative guidance, all operate on the basis of the EBA definition both of NPE and also of cure. So it's consistent with those definitions. I think the issue that you raise in terms of timing is actually quite important and goes maybe to some of the other questions and commentary that there has been about the addendum. So the first thing, what is set out in the addendum in terms of timing, is that the proposal would apply to new NPEs from the 1st January 2018. So this is a distinction between what is non-performing now and what is going to be newly non-performing. So really the scope is newly non-performing from the 1st January. The question then is, well, how does that get implemented operationally? Exactly as you describe, the bank has to go through a process of looking at that loan; are they able to put a restructuring process in place?

What is their own provisioning requirement for dealing with that loan? When would they apply that provisioning? How would they report that in their accounts and so on? Then over time if that continues to persist that that remains an NPE and it doesn't cure, then what we're saying is our expectation is if that's unsecured, then in two years' time we would be wondering why is that not 100% provisioned. If it was secured in seven years' time from the time it returns non-performing, why is it not yet provisioned 100%? That would be what the dialogue is about. So when we talk about time, that's the timeline by which we're thinking about implementation. Now, of course there's another question about when after the public consultation and I think Madame Nouy has commented on this publically already, we have to take in all of the comments.

We have to consider all of the feedback and then we have to finalise the guidance. So when it's actually published is another question about timing. But in terms of how it would work, that's the way it would work. Then in relation to 'cures'; then provided the EBA definition of cure would be met – and we explain this in the guidance – then the vintage count or the count at the days of non-performing returns to zero. But it must be in the context of meeting the EBA definition of 'cure'.

Question: I had two questions. One was just regarding the toolkit that the supervisor already has and whether it was felt that this aspect was missing or whether you could already have these conversations on a case-by-case basis in a non-binding manner, with everything as it stands today. Or whether it was felt that this was required in order to have that.

The second part would just be in terms of the publicity or otherwise. Once you have identified an entity that's perhaps not living up to that standard, is it intended that there would be some sort of disclosure to the market of that? Or is it going to be kept on a private basis?

Nouy: Well, the supervisors are not overstepping their mandate. Indeed, we have the obligation to address vulnerabilities in the banking sector and to guarantee the consistent application of regulation and supervisory policies. That includes providing guidance that ensures fair and equal treatment of banks and in particular on an issue which is as important, as delicate as NPEs. The Commission in the recent report on the SSM has explicitly encouraged us to take care of the necessary adjustment in case accounting provisioning is not sufficient from a supervisory perspective. It's important because there were certain institutions or people or banks that considered that the language was not clear enough. So it has been very much clarified and we consider that it is very good, so now nobody can doubt that we have the possibility to take what is called Pillar 2 measures, specific bank-per-bank, case-by-case measures.

It is the supervisor's prerogative to impose requirements on a case-by-case basis depending on the risk profile of the bank and that is complementing requirements of lawmakers: so even after the adoption by the legislators for example of a Pillar 1 tool and it's very good that they take the step of having also a Pillar 1 tool. So the strong basis will be there when it is there. We can complement bank per bank for the prudential part that will obviously be less important because part of it has already been done by IFRS 9 and by the legislator via Pillar 1.

Donnery: On the idea of whether it was missing or not, I would just echo what I said in my opening remarks, for us this is about being transparent. We do this for lots of other things. The ECB and many other supervisors publish often their expectations of all sorts of things. The ECB has other expectations around cyber risk for example and other risks. In doing the addendum – and in fact our qualitative guidance earlier - we are trying to be transparent about what we expect to see. That makes for a more informed supervisory dialogue because banks know already what to expect. Of course the public and the markets know as well, so I think this is an important point.

Nouy: If you allow me, Sharon, I will say that we have already published 17 such documents which produce expectations from the supervisors. Some of them were not so quantitative. But some were quantitative such as the expectations regarding dividend policies. So it's not something new; it's just that because of the issue it attracted more attention.

Donnery: Then on the disclosure point: clearly, as supervisor, we have lots of confidential information and we would not be proposing that we would disclose this. But we had already in our qualitative guidance some expectation set out there about further disclosures that banks should make. One of the disclosures that is listed there is that banks should disclose vintages and provisions by vintages and so on. This is also referred to in the addendum, so the disclosure would happen in this way.

Question: We recognise the need to reduce NPLs in all Europe and we welcome the introduction of your guidelines on NPL management in March 2017. It is important for us, the creation of a quasi-liquid private market for NPL which we would like to maintain stable, as much as possible. I have four questions if I may. The first one regards the impact analysis. The better regulation principle foresees that an impact analysis should be at the base of any proposal for new rules and providing an estimated impact on the proposed regulation per se over the specific industry; and more generally over the economic cycle. To this extent we wonder how the two years' and the seven years' timing have been computed. We understand that it was based on an international benchmark. Also we wondered if you have any estimation of the consequences of such ruling on credit pricing, credit supply, GDP growth et cetera. In our view, if you have any estimates on the impact on LGD calculation, this would be precious for us.

The second question again relates to the coordination between IFRS and tax and your prudential regulation. This proposed prudential regulation does not match with IFRS. In Italy all banks use full IFRS and tax rules. Banks could easily find themself in a situation in which IFRS and NPL addendum rules produce different computations, thus creating problems for financial communication and a potential impact on price-sensitive information both for listed and non-listed banks. In particular we have in mind the prospectus directive, the MAR [Markets Abuse Regulation]. Again we wonder how this ruling could impact on minimum capital requirements, on minimum distributable dividends and on the new MREL [Minimum requirement for own funds and eligible liabilities] requirements. As far as the taxation is concerned, IFRS provisioning and prudential calendar provisioning do have different treatments, thus creating a tax distortion. Is there any chance to avoid this problem and just find the solution? We are trying to find the solution to this.

The third question is that, as Madame Nouy said, there are different experiences in terms of the time taken by civil courts in Europe. But it seems to us that the NPL addendum does not take into account different traditions of judicial systems and especially these different 'lengths of civil courts' and those imposing a one-size-fits-all approach. We are extremely in favour of a rapid

convergence path in civil courts and bankruptcy courts. Every day we ask for a European set of common codes. But until we reach such convergence we should prudently take into account that there still exist differences.

The fourth question is that we hope this new NPL addendum will apply to new loans originating from a date in the future. Also taking into account the value of the current guarantees connected to NPEs. It is our opinion that the European Commission proposal could be a starting point for discussion even to allow us to correctly price new loans.

Donnery: Hopefully I can pick up all the points. So maybe I go in reverse order first? In terms of the new loans – and I think you mentioned guarantees – we do have a way of considering guarantees. I think Madame Nouy has already commented about the Commission proposal and how both Pillar 1 and Pillar 2 measures may be needed and also the fact that if the Commission introduced its proposal, it would clearly take some time. This is obviously required, or potentially required, now.

In relation to your questions about the impact analysis and the court systems, I might take the two of those together because they interact a little bit. So when we were considering the calibration of the two and the seven, we looked at a number of different things. We looked at similar requirements like supervisory expectations in other jurisdictions, including outside of Europe. We did look at exactly the point you make about the length of time it takes in judicial systems for collateral to be executed. This part of our work was very much informed by our stocktake of legal and judicial practices, which again we have already published in the interests of transparency. It was published earlier this year. So I certainly think we would share some of the concerns you mention about these differences and how the length of time particularly to execute collateral can vary across the banking union. We have raised that publically before.

But we took that into consideration when we were calibrating the seven years, particularly that in some countries it can take quite a length of time to get collateral. I think that we felt that seven years was a reasonable balance, taking into account all the different factors of how long it might take to go through court. But also to say that if after seven years you haven't managed to restructure a loan, you haven't written it off under your existing policies and you haven't managed to execute the collateral, it's reasonable to ask the question, well, why is this not fully provisioned? So that was part of the analysis there.

In relation to the more macro effects, I'm sure Danièle would want to comment on that. But I think we see that growth has improved in the eurozone consistently over recent years. I think we've a strong view that NPLs can cause tremendous problems in terms of the ability of banks to lend and finance the economy. So we have to take the opportunity of these types of growth to deal with the issue and we can't allow it to persist. From a macroeconomic point of view, this informed our assessment of how it would work.

In relation to your comments around tax and disclosure and interaction with the prospectus [directive], I certainly think this is a useful thing to have been raised in the consultation. If you have specific suggestions about how those kinds of things can interact, we would certainly look at those to make sure that they're clarified in the addendum.

Nouy: Thank you very much, Sharon. I will try to pick up the remaining points and if I miss one, feel free to ask me afterwards. You mentioned complexity compared with IFRS 9. Well, first of all what has not changed is there is a block which is the work of the accountants - statutory auditors - about accounting rules; and also what is prudential. They have always been different, the two blocks. On top of that, there is a long and complex, I recognise, phasing in of IFRS 9. The ECB was in favour of having the initial shock phased in. But not only this is being phased in, the additional provisions can be phased in even where they're caused by business decisions that have been made when IFRS 9 was already applicable. So it will take a lot of time before the full effects of IFRS 9 on the solvency of the banks for example will be taken into account.

So the risk of complexity is almost non-existent, but in any case it is not materialising, even if a little, for quite some time. Regarding the credit delivered in Italy for example, because you mentioned you are from this country and mentioned the point, I checked this morning before coming to this discussion and the hearing. The results from ECB statistics regarding Italy’s third quarter of 2017 are quite clear. They show an increase of credit for both households and firms, in a parallel move, towards more accommodative lending standards by banks to households and firms. So no such risk right now and precisely to the point that this period is the right one to do this. Before the recovery and economic situation, I was told by the Italian banks that I should wait until growth was back. And growth has been back for some time now and it's good to use the benefit of this good period of time.

You mentioned differences in taxes. Well, yes, that's absolutely correct but it has always existed. This is not something that can stop supervisory work. We have no power, no say in taxes and that's the way it should be in my view; it should not be the case. We are looking at risk and what has to be done to cover risk. You mentioned also the fact that judicial systems are different and some are more efficient than others. That's a pity because in the Banking Union that should not be the case. In fact Sharon and her team have spent a lot of time to produce 19 stocktakes of the situation of the different countries, best practices, and judicial systems and so on and so forth, precisely to make sure that the situation would improve. And what national governments should do is to take measures to improve the efficiency of judicial systems. Many are doing this; and this is work in progress, also in Italy, to the best of my knowledge. They should increase access to collateral and they should create faster out-of-court solutions.

Regarding the creation of a liquid market for distressed debt, yes that should happen. The magnitude of the problem is such that we need all tools that we can get to be able to adopt all kinds of solutions for these NPEs and all initiatives are welcome. Improved data quality and access, that's very important because the prices of NPEs if they are sold in liquid markets or European platform or whatever depends very much on the quality of the data that can be provided and precisely the level of certainty of the recovery of the collateral. If there is uncertainty because of the judicial system, that is preventing the prices going up. Obviously they should remove tax and legal impediments to debt restructuring that exist in certain countries. But that we cannot do; NPEs are a problem that goes beyond supervision and we need the help of all stakeholders.

Question: I have three questions. I'll try and make them quick. I think two are perhaps a little bit more fundamental, philosophical, and one is a technical question. The first question is about the nature of the supervisory dialogue. I think that our members welcome the fact that you have given clarity on your expectations here. That's quite clear. You say it's nothing new but it is a quantitative clarification. That is helpful. It's also very helpful that you've clarified that there is no automatic consequence and that there will be a supervisory dialogue. Perhaps it would be useful to make sure that that is reflected in the final – in the wording of the final guidance.

So this is my question; I wonder if you can say anything perhaps as to the supervisory dialogue and its process. I think that there might be a way to address at least the perceived burden of industry here and ensure that there is no confusion between accounting and prudential approaches. So we understand that it's not you intention for there to be any, but to ensure that there really is the clear separation.

Is there a reason why you would not – instead of using your expectation as the starting point and then asking a bank to explain and justify why it might deviate - is there a reason why you would not look at the accounting provisions and ask for justifications when you think they are necessary because the situation does not meet your expectations? So it's kind of difficult for me to explain. But I'm talking about trying to change a little bit the onus and the burden of proof, if you

like. That's not the right word, but to put the onus on the supervisor, on the ECB, to challenge when the expectation is not met. So the expectation really is a kind of backstop rather than a starting point to avoid a kind of confusion. So that's one question, if you could talk us a little bit through the supervisory dialogue steps and why the reversal might be possible or not.

The second question is the elephant in the room. You mentioned in your introductory remarks that this was not the point of the discussion today. But definitely there is a lot of interest in understanding whether there will be similar measures in relation to the stock. As soon as information can be made available on the approach that would be adopted there, I think that would be very helpful. It would help communication and dialogue between supervisors, the industry and also all of the other stakeholders who are involved in addressing this issue.

Then my third question, which is the technical one; are you able to provide a little bit more clarity on the definition of exposure when it comes to, for example, off-balance-sheet exposures and how those might be dealt with?

Nouy: I will take the supervisory part and let Sharon take the more technical one and also the possibility to add to the supervisory part if I forget something because Sharon has a very strong background of supervision as well. So, to start with

our expectations. I will use a concept that Sharon has already put on the table: transparency. When undertaking the job of supervision, we supervise up to 125 banking groups, comprised of 1200 banks in 19 countries. We need to have a methodology to benchmark so many different banks. So we need to have expectations, we need to have a discussion between supervisors and for the decisions of the supervisory board on what are our expectations. So that's why it is the starting point.

I would like to give examples on a couple of other issues that you have addressed. You say why not start with the accounting provision and have the prudential on top? In fact this is the way it works and I will give you the example of the 2014 comprehensive assessment. We had an asset quality review which was a part that specifically uncovered miss-valuation of assets, a lack of provision sometimes of assets. Then there was a stress test conducted on the basis of the corrected valuation. In fact what happened after the exercise? We had meetings with the statutory auditors of all the banks that were in the comprehensive assessment. We said to the statutory auditors: as supervisor, this is what we consider missing provisions. What are you taking into account in the accounting provisions? If you take 50% of that, we will take 50% on the prudential side. If you take everything, we will take nothing on the prudential side.

So there might be differences depending on the accounting rules, which are quite diverse, as I already mentioned. So if the work is done by the accountants, under the accounting rules, it's okay. But when it's not done, then we have to address the missing provisions on the prudential side. And this is the way it works still now. We look at what has been done by the auditors and the accountants and we compare that with our expectations and then bank per bank, because this is what it is, prudential supervision. It’s Pillar 2, bank per bank, case by case.

Regarding the supervisory dialogue, I will give you an example of supervisory dialogue by addressing the stock, the legacy assets. We had the qualitative guideline that was defined by Sharon's group. We were working on the expectation for the steady state[of NPEs], but during this period of time, in parallel with the consultation on the qualitative guidance and in parallel with the work on the steady state, we had this kind of supervisory dialogue with the banks that are burdened by NPEs. It means that following the completion and publication of the qualitative guidance last March, we meet with the significant banks that were burdened by this issue, and ask them their own NPE plans. Over the period between March to June, the banks submitted their plans, their strategies to address NPEs and the joint supervisory teams, [JSTs], met bilaterally with each of these banks on the issue.

We are now in a process, after one meeting or two or three meetings between the JST and the banks. So you see it's really a case by case approach. We are in the process of sending letters; JSTs will send letters to these banks assessing their strategies - based on whether they are ambitious enough - related obviously to the quantity and the magnitude of the effort; how realistic they are on governance - so based on ambition again, it's easy; gross reduction - the volume the bank is targeting, and how realistic it is: well, it depends, is it feasible?; and it depends on the measures that will be used to reduce NPEs. What are the tools? Cures, cash recoveries, write-offs, sales; how diversified those measures are. If you want to sell [NPEs], do you have enough provisions not to take losses or do you have enough capital to take some losses of top of the provision? So, this is what is realistic.

Then we look at governance: if it is a big project for the bank, if it is ambitious, if it is an important issue for the bank, obviously we expect the banks to have performance incentives, for example possible bonuses for the staff, bonuses that are based on the reduction of NPLs. So are there really good incentives? Also the quality of the plan, a plan that is pretty general and vague and that will be realised in two or three years - and has no milestones or nothing measurable at each milestone - is not exactly a good plan. So you see the supervisory dialogue is pretty intense and this is what we have done on the stock. We will do the same on the basis of the expectations for the future NPLs. This is already providing quite good results, so that's why also we are working on something for the stock. I don't know at all what this something will be because this is work in progress and I have not seen anything.

But obviously the idea is to have – we have three categories of banks. There are banks that decide, okay, the supervisors are very serious about that. It's the moment to undertake a serious turnaround of the bank and to have a kind of one-off cleaning and capital issuances. We have another category of banks which take the issue seriously, are a bit slower, but which will produce fruit as well. Then there are still banks nevertheless that are in denial or send us vague plans, that take effect in two or three years, but without explaining how the plans will be delivered and that do not have the capacity of ambition because they do not take enough provisions and so on and so forth. So we certainly want to push forward with a solution for the stock, for the ones that are still in denial. We don't want to create problems for the ones that are doing the right thing at a good speed.

Donnery: You talked about language and the redrafting and so on. In being transparent about our expectations, it's very important that people understand what they are. If there have been misunderstandings then obviously we have to address that. So that is exactly why we've had the consultation process and that is exactly why we're having this hearing. To give you an example of that, we have been clear in the addendum, if you have it there with you, that this is non-binding. We also have a kind of diagram or figure table in the addendum which says that there will be no supervisory measures if the dialogue delivers that deviations [from the guidance] are acceptable. There will be measures if the dialogue delivers that the deviations are not acceptable. So for me, it's clear that it's not automatic. Having said that, I think words like ‘comply and explain’ and so on have been interpreted as being automatic. So I hope we've been clear today that that is not the case and we will certainly take that into account in the drafting.

A further point on the dialogue which I think Madame Nouy has explained really, really well including the examples she's given: I think it's sometimes thought that the dialogue begins one day and it ends another day and that's it. In fact it's constant; it is going on all the time. So you talk about the burden of proof. I talk about challenging back a bank. The bank says something, I question that and vice-versa. So it is genuinely an iterative process that continues a lot. I think the strategies for NPLs is a really, really good example of that. Clearly we started with the comprehensive assessment. We didn't, kind of, not do anything else on NPLs in the meantime, until we published the qualitative guidance. This was ongoing dialogue all the time and the work on the strategies was definitely very focused on that. The last thing I would say about the stock is, clearly there is work ongoing and again we have been transparent about that.

I think, though, we have always tried to take into account the current situation. So we have gone step by step through the comprehensive assessment, through the qualitative guidance, through this addendum and quantitative guidance. We take into account what's going on in the wider economic environment; we take into account the situations of the individual banks. We take into account the progress that's being made or the progress that's not being made. All of these different aspects will inform whatever that further proposal is that we will make in the springtime. On the off-balance sheet exposures, I think Anne was going to say a word or two.

Fröhling: Off-balance sheet exposures are generally included because we use the EBA definition of NPEs. If you look into that definition it does include off-balance sheet items. Now, 95 per cent of NPEs are actually on balance sheet if you look into our latest supervisory statistics. So the off-balance sheet items on average are not a big deal. However, the coverage is relatively low; in our statistics you see it's only 14 per cent, so it can indeed be a relevant item for a couple of banks. If you have ideas or certain things that you think we need to clarify in the addendum, please let us know, otherwise I would see it as part of the supervisory dialogue to address these very specific topics.

Question: I have one question concerning the scope of the addendum. To my understanding, you mentioned in your guideline published in March that this guideline, or several parts, are primarily addressed to high NPL banks, so we would suggest that the addendum is also addressed primarily to high NPL banks, because we think, with this addendum, low NPL banks, also have to implement the processes, et cetera, and these banks would maybe be 'punished', by implementing this addendum, so that would be our proposal, to make it clear.

Nouy: Well, maybe we were not clear enough, but obviously, our expectations are covering all banks that we supervise. We want to implement a level playing field and consistency. Obviously, it is of interest for the banks that are above a certain threshold, above the average, for example, of the ECB SSM banks. But, precisely, certain countries are not necessarily very well equipped in their legal framework, because NPLs have not been an issue for them recently, and are not now, but this is the moment to change the judicial system for when they might be burdened by NPLs. It may happen. No country can consider that it cannot happen to them.

We have also another concept that was defined in our work regarding NPEs - there are banks that are over-burdened by the overall percentage of NPEs compared to their other loans and assets. But we [also] use the concept of pockets of non-performing exposures. There can be banks that have a small ratio of non-performing exposures, but still have — can be shipping, can be real estate - can have one problem that they have to fix; it's less of a big problem, because it's a pocket of NPEs in portfolios of credit risk that are of good quality for the rest, but still it doesn't mean that they should not address it. So obviously, the supervisory dialogue is very intense with the banks that are currently burdened, but we want the other banks to be properly equipped. We don't want to have a long phasing-in for new banks that could become burdened by NPEs. Everybody has to be ready.

Question: Thanks for taking my two questions. Actually, one would be a follow-up question regarding the supervisory dialogue, being, can you elaborate a little bit on how you ensure consistency in the 'explain' process within the supervisory dialogue, i.e. if in one discussion it turns out a certain portfolio, or a certain approach will be accepted as 'explained', how is it ensured that in another firm the same assessment will be done?

The second question is also a technical one. In order to also encourage the sales of non-performing loans amongst other banks, how are purchased credit-impaired assets being treated under this rule? So those are defaulted according to the definitions - those have to be considered. Is that something which we then have to take up in the 'explain' process, or is that something which can be, per se, excluded? Are there any ideas which you already have?

Nouy: I will start with the supervisory dialogue. How we obtain the consistency, first of all, is precisely by having expectations known and they are known publicly for this. So transparency helps. Also, because the outcome of this supervisory dialogue is an input into what we call the SREP process, the supervisory review and evaluation process, that on an annual basis delivers the Pillar 2 capital and other measures, other requirements, and guidance, and also by the fact that those decisions, the final outcome of this supervisory dialogue comes for decisions before the supervisory board of the SSM. Our members are cautious and prudent, and attached to consistency precisely. It's not unusual when we have a new development, a new point which is addressed, or something that has been addressed but not so often for everybody to remember it that I am asked by my colleagues, 'Prove to me that you...' or 'I want, this minuted in the summary of this meeting…', 'Prove to me that you are ready to take the same measure when there is a bank that will be in the same situation'. Obviously, it has to be the same situation, because Pillar 2 on supervisory action is bank per bank.

So this is something which is taken very, very seriously by members, and also, of course, by us, because this is what we want to do, to be fair in banking supervision, and to be fair you have to treat banks with consistency and fairness, and it's important, because if you are not fair you cannot be tough, and we need to be tough, because there is no room for complacency. We are coming from a very serious crisis. We have been established after a very serious crisis, to make sure that we are better equipped when there will be another crisis. So consistency, and a level playing field, is taken very, very seriously.

On explanation: well, this takes place in the dialogue between the banks and their JSTs. This is the way it starts: the visits by the banks, voluntarily, to Frankfurt or maybe via a JST asking a bank to come with a certain periodicity and certain agendas. In general, it's both: voluntarily, plus the programme of supervisory action for the year. What I always say to the banks that I meet, in particular when I go visiting the 19 countries of the SSM, is that if you are not fully satisfied by the explanations you have received from your JST, escalate the questions to the DG [Director General]. Pay a visit to the DG in charge of these JSTs, and if you are still not comfortable with the response or fully convinced by the response, or have not fully understood the response, you can come and see me. I have never refused a meeting with a bank, and in general, I would say that banks understand what I have in mind and what I am expecting them to do. Sometimes they will not like it, but they will get a clear response.

Donnery: I would just add to that, that internally within the JSTs, and the support structures that we have to support the JSTs in doing their work, behind the published guidance and the expectations, there's a lot of material about benchmarking comparisons across portfolios, across banks, across countries. There are processes where JSTs can get support from each other, and other colleagues internally to compare and understand explanations and to make sure that this kind of consistency and fairness is put in place, and that goes on as part of normal supervision, again, complementing the supervisory dialogue.

In terms of sales, the intention is that there isn't some way for you to kind of arbitrage the system by selling a portfolio from one bank to another, and if a new bank buys a portfolio of assets, then, of course, the same expectations would apply. But in the same way, I think you even mentioned that this would also be part of the dialogue, but maybe, Anne, you want to add something?

Fröhling: Yes, generally, fully in line with your comment, and I guess, if you have the financial means and operational capabilities to buy NPL portfolios, you will have done a sound due diligence, and this is very sound evidence for the supervisory dialogue, and if you can prove that the cash flows you had expected in the due diligence process are coming through, I think you really have a strong case for an exception.

Question: I have two questions. The overall idea of the NPL guideline, I understood that you want to manage non-performing loans better, but if banks need to provision their exposures, NPEs by 100 per cent, in a very short period of time, two years, even though clients might still recover, don't you see a risk for the real economy, that banks might be more reluctant to lend in the first place to less profitable clients, to sub-investment grade clients?

Then, also, when loans turn non-performing, the question is, what will happen to those loans? We assume that there will be a higher rate of non-performing loans trading, so if a bank, for example, has as a commercial lending team, loans in their books, do they then need to sell those loans to their trading desk to prove that there is still a value in it, because then the market has proven that there is value in that loan, and then they don't need to provision, and then we only have all those loans with the trading entities, and with not the commercial banks anymore, who are supposed to support the economy, private households, and corporates?

Nouy: Well, I don't think it's needed to go that far. We have a wonderful situation, being the supervisor of 19 countries, to have good knowledge, good appreciation, and a good benchmark of the situation, as I'm sure my colleagues can demonstrate, because their databases are incredibly comprehensive and precise, so no need to go to the market to have a price that could be negotiated with another counterparty. As a matter of fact, it would not be enough to have such a limited number of transactions. We have better information.

Your question seems to suggest, as well, that to take care of NPEs is hitting financial stability, at the end of the day, because of less loans and less growth maybe. We cannot ignore risk. If risks are not addressed, they are not disappearing; they are just getting bigger, so we need to address risk. We need to address risk early enough, when the piling up of NPEs is taking place. That will demonstrate to the banks that maybe there is something wrong with their credit underwriting criteria, if they are starting to pile up necessary provisions for NPEs, and it's better that they know it sooner rather than later, to be able to correct the trajectory.

As the President [of the ECB] said, banks that are burdened, because precisely they do not address NPE stocks at the beginning are the ones that constantly and consistently lend less to the economy. So I guess there is no other solution than to have a good knowledge of the situation, thanks to the supervisory dialogue and the need to make the provisions when new NPEs are appearing, to take the needed measures to correct this trend and address the problem of the stock - when there is a stock - fast enough so that banks are able to do their job and really lend to the economy, not spending their human resources on solutions for NPEs, instead of on changing their business model when it is needed, or finalising, fine-tuning their business model, rather than putting all their energy to address a big stock.

You can mention what you have in your databases, to avoid the need to, practically, get a price, Sharon?

Finn: We have, obviously, regulatory reporting, but we also have implemented enhanced reporting for banks with higher levels of NPLs. We also engage quite regularly with banks on management data; we engage with accountants, also, and statutory auditors on the level of transactions. We would monitor this on a quarterly basis. So if we were to see movements that maybe warranted us to focus on higher levels of risk, warranting a higher level of attention, this would absolutely be in our remit. This would be something the JSTs would deal with on a quarterly basis, really assessing the data, the level of granularity, mis-matches, et cetera. So this is definitely within our focus, and something, again, that we will continue to monitor when the guidance is implemented, so that we can ensure no arbitrage, for example, or unintended consequences. So absolutely on our radar.

Question: I’m from Confindustria, which is the Italian association representing 150,000 manufacturing and service companies employing around 5.4 million people. So just a few comments on the business side. Businesses are concerned about the impact of the addendum on credit supply to enterprises, and particularly to SMEs, which still rely heavily on bank lending. In this context, we are still particularly worried about the impact of the addendum on unsecured loans, which, of course, are very important to us.

We acknowledge the importance to keep reducing the NPL ratio, and the stock of NPLs. This is particularly important for Italian enterprises. But we believe that this has to be done gradually. We share these concerns with Business Europe, which is the European association, representing the associations of industrial companies from all over Europe. Business Europe sent a letter to Madame Nouy earlier this week, answering the consultation.

Together with Business Europe, we fear that the release of the addendum at the beginning of the recovery phase, which is very important to us, could represent a restrictive measure penalising economic growth across Europe. We do not agree with the argument that the addendum would have an impact only on specific countries or specific banks. On the contrary, we believe that due to an avoidable contagion effect in the EU, measures like the addendum could penalise the European banking sector as well, and the European economy, increasing systemic risk and not reducing systemic risk.

This is why we believe that before finalising new rules, it is essential to carry out an impact assessment of these rules on enterprises, in order to ensure that they encourage growth, and prevent damage to businesses in the wider economy.

Nouy: Because you represent the corporates, I would like to make a remark for the corporates as well, and then I'll hand over to my colleagues.

In fact, when NPEs are addressed early enough, it's much more likely that they will be able - those exposures, those loans - to be cured, to be restructured and transformed into a performing loan. That's important for corporates, because if this is not happening, an NPL on the balance sheet of the bank is something that is also on the balance sheet of the corporate. Until this is fixed with the lender, one way or another, the good banks, the banks that are not burdened by NPEs and that are making more loans than other banks, will not give loans to a corporate, that has a long list of items in the balance sheet that are just disputes with other banks: loans that are not performing, borrowings by the corporate that are not performing.

So we should not think only about sales or write-offs; though write-offs would help the corporates. But when it's done early enough, really, the way of addressing it is much easier and much less painful. Cure, restructure the loan; make it performing by extending the maturity, maybe, by structuring it differently.

And it's not a benefit for a corporate to have NPLs and not address them. It's even a double punishment, in fact, for the growth on the economy of the country.

Donnery: I would only complement that. I think the point about addressing earlier being better is absolutely the case. Unfortunately, many countries, and many of our supervisors have had bad experiences over the last few years with non-performing loans, and the negative effect that they can have.

Our qualitative guidance for the stock, when we prepared that, a lot of the work there was looking at best practices in banks and in other supervisors prior to the introduction of Banking Union, and certainly one of the key issues there was that addressing problems earlier and putting in place proper restructures, so not what we used to call extend and pretend, but proper restructures that are actually effective, is better, and so I would just add that to what has already been said.

I think the other aspect is, of course, in introducing something for new loans, we have to think about how that will interact with credit, but I think it's our responsibility to make sure that NPLs do not emerge as another problem into the future, and that is the key motivation in this case: to protect banks, and economies, and households, and firms from a build-up in the future, because we can see now the scale of the problem that we have with the pile of NPLs that we still have from the previous crisis.

Question: I have three questions to put on the table. The first one: Don't you think that an extant and general obligation for provisioning set at 100 per cent, denies the risk-taking and the risk management co-nature of the banking business?

The second one: I would like to come back to the macro-economic effect. There is no doubt that a growing economy, as we have at the moment, is a good environment for balance sheet cleaning, and to reduce significantly the stock of NPLs. However, what will happen during a downturn cycle? How do you overcome the likely procyclicality effect in an economic recession? Did the ECB carry out an impact assessment, and what are the results?

The third question: What do you think about implicit incentives given to market participant for NPLs? In my opinion, those incentives are not the right ones, because when buyers of NPLs

know that banks are obliged to sell their NPL portfolios within a binding deadline, they know that they have the upper hand on price-setting.

Nouy: We I will start in particular with your last question: incentives. I don't know, but I think an important incentive for banks, is that doing too little too late can take result in them failing, or can result in the SSM having to take a decision of failing or likely to fail. This has happened recently to a few banks, and that's triggered by investors that lose trust in the banks, and stop funding them at a certain point, because they consider that too little has been done and too late. So it's a very serious issue, which banks have to take seriously. That's the first point.

Donnery: I'll also start with this question about incentives. First thing to say, there is no obligation arising from either the original guidance or from the addendum for banks to sell portfolios of NPLs. I think we have been consistently clear in relation to this in all the communications we have made about both the original guidance and this addendum.

Clearly, the sale of NPLs is a tool that banks can use as part of their suite of measures, but we have not imposed any requirements on banks to do that. As part of the strategies and the dialogue that continues with the banks, of course, some banks may decide to do that, but we haven't set any expectations in that regard. I think you said, 'I think it obliged', and it's important to clarify that, because we haven't put an obligation like that in place.

In terms of your broader questions, about the economy and the backdrop of a growing economy being a good opportunity to clean balance sheets, and a concern about procyclicality, I think, of course, we have to take all of these things into account. But I think our view is, if you don't deal with these issues in a time of growth, then what happens if there is a downturn in the future, and there is still a significant problem or a growing problem at that time? So, for us, it's a balance of what is the right and prudent measure to take, particularly in this case, where we're talking about new loans, to prevent a build-up of NPLs into the future.

Then, if I understood your first question well, about the 100 per cent, effectively, putting a kind of obligation on the bank that denies its ability to do what it's there to do, which is to take risk and make loans, I think, and I certainly hope, we've been very clear today, that this is not a kind of binding approach. We are setting it out in a clear way that this is what we expect. I think it's reasonable, as a supervisor, to say if this hasn't been dealt with after two years, or seven years, 'What is going on here? Why has this not been dealt with? Why has it not been provisioned?' and we are setting that out as a starting point in terms of our expectations for the dialogue to take place. It doesn't mean that there's a general obligation on a bank to do something, or means that it can't take on loans and do its work in terms of managing risk.

Nouy: I have two points that I wanted to add. Something that was mentioned several times and we have not addressed. Why not an impact assessment? Well, we are talking about new NPEs, so it's a bit complicated to have an assessment of something that does not exist. We can use different elements to try to guess what the situation will be. We can easily do an impact assessment for everything related to the stock, but it's pretty difficult, and we believe that, due to this new framework that ensures that credit risk is taken more seriously, credit underwriting criteria will be reviewed and improved in the bank. There should be less new NPEs after the guidance, and after all the work on the supervisory dialogue which is taking place right now for the banks that have to address their problems.

Regarding, also, the automatic element on that, there was directly or indirectly a reference to disregarding the value of the collateral, for example, for the secured loans. We don't question at all the value of the collateral, but we question the timely ‘executability’ of the collateral, the recoverability of the collateral. Because if it cannot be exercised in such a fashion that it is covering the NPE, what is the benefit of having such collateral? And after such a period of time, the probability that something will be recovered from the collateral is much, much lower.

Well, yes, collateral is a credit risk mitigant, but once a loan becomes non-performing, seven years to take care of the ‘executability’ of the collateral is something already quite, I would say, maybe not generous, but reasonable, at least.

Question: **Two quick observations, and then a question, if I may. It seems that in the debate on NPLs and how to deal with them, one aspect that, perhaps, requires further attention, research, consideration, is precisely the role that collateral does play. I think it's not always about its execution. It doesn't necessarily have to be executed or realised to help restructuring and successful outcomes, and I think that that also might be at the root of some of the industry's nervousness about some of these proposals.**

A second comment, as an association representing financial markets, I think what we would like to say in terms of the development of secondary markets for NPLs, of course, that this is very important as being one of the solutions, that has been mentioned. I think we would encourage the ECB, but also all of the other institutions that are involved in these discussions, to ensure that there are no distortions that are created as an unintended side-effect in the market. So making sure that there is an appropriate balance between the supply and the demand side is very important. I'm not quite sure, but I hope that Sharon Finn's team would be looking at possible unintended consequences, or possible distortions that could arise in that context.

My question relates, again, a little bit to secondary markets and NPL purchases and trading. I was a little bit concerned about the response to an earlier question on how to deal with the purchases of NPLs, and whether the calendar provisioning expectation would apply in that case.

It occurs to me that a purchase of NPLs should, perhaps, not be considered as falling under the new NPL or new NPE category. I think it might be interesting to explore that, because while you do explain that there could be a case here to deviate from the supervisory expectation, depending on the dialogue that you would have with your supervisor, it seems to me that that could be a relatively burdensome process for some banks to have to go through to achieve that explanation, and acceptance from their JST. Whereas, other market participants who are not subject to these provisioning rules would not have that burden, and I wonder if there might not be a little bit, again, perhaps, an unintended distortion in the secondary markets here.

Nouy: Well, this question was responded to by my colleagues here so I will defer to them but two remarks on your two first points, which are a kind of follow-up to what I said before. The role of collateral and what we expect from collateral, well, that could be improved, in fact, and will make the recoverability of collateral easier. When we look at what the banks sometimes call secured loans, they, in good faith, believe that they have secured loans, but sometimes they have in fact relied on collateral that was provided when the loan was allocated, was granted. But the maintenance of the legal documentation was not perfect, and, well, what is supposed to be secured all of a sudden is not secured, in fact, because the legal documentation is not properly maintained. On top of that, when it's possible, when the legal documentation is correct, indeed there are still too many uncertainties regarding the capacity of the judicial systems to permit this repossession.

Also, regarding the secondary markets for NPLs, you said something about the balance between supply and demand that has to be taken into account. Well, we have €800 billion of NPEs in SSM banks. It's not a market for the sellers; it will always be a market for the buyer, until we have much, much, much lower amounts. So in these circumstances, I would say it's better to be among the first to use the markets, because after a certain point, well, maybe there will be no buyers anymore. We don't know, but it cannot be a balance when you have so much to sell, really.

Donnery: On the burdensome process, we're here to hear the feedback, so thank you for that, and we will certainly take it into account. Just one observation: even if you leave aside the addendum, if you're a bank and you're buying a portfolio of NPLs, I think it's fair to say your supervisor is going to want to know a lot about that anyway, in terms of understanding why you're doing that, how you're going to manage that, what the recoveries are going to be like on that, and so on. So I think the point we were making was, as part of the due diligence process a bank would be doing anyway, to buy a portfolio of NPLs, there would be a discussion with the supervisor to understand; and then part of that now, with the addendum, would also be to take that into account. But I think you can expect that there would be some discussions and information to be provided, anyway. But nonetheless, we will take away your comments. I don't know if you want to add something, Sharon?

Finn: Yes, absolutely, because as part of the process to buy them, there is almost a right sizing of the value. So we'd have to take that into consideration: the value is coming down, coming off the balance sheet of the bank that's selling, and it's going onto the balance sheet of the bank that's buying, so as part of that transaction, as Sharon pointed out, the due diligence process, there is an in-depth loan-by-loan file assessment of the inherent value, the valuation of collateral. So there will be a right sizing; there will be a certain fixing of the problem, you could say, in terms of the estimated recoveries. So absolutely taken on board, and more and more JSTs are engaging with banks on these particular types of transactions. And as we move through the work on the strategies, we are receiving numerous different types of proposals similar to these, where we are looking at them in a horizontal fashion to make sure there is consistency and that the data supports the assumptions. So very much part of the process.

Question: Could you consider a general LGD [loss giving default] waiver on NPL sales for a specific period of time, in order to incentivise banks, to accelerate the sale of NPL?

Nouy: I'm not quite sure what you call an LGD waiver. You mean that we disregard the very low price in the LGD that will be used for the models? Well, we are obliged to implement the legislative text, what the legislators wanted - CRD4, [Capital Requirements Directive 4] - and as a matter of fact, being the former secretary general of the Basel committee, at the point when we drafted this regulation about models, I know what we had in mind, and in what I drafted in Basel, I am supported by my [ECB] colleague, Stefan Walter, also a former secretary general of the Basel committee, who knows what we had in mind.

In fact, you are correct, there is a small margin for specific situations that allows a little bit of flexibility for the consequences of very low prices, that could damage the LGD, but there are conditions for that. Normally, it has to be done for the sale of a comprehensive portfolio, the total portfolio, meaning that the portfolio that would have this damaging LGD is gone totally, and so no reason to have some kind of tainting of the other LGDs.

If it's not the case, where the portfolio is not totally gone, we have to have a supervisory dialogue here, as well, with the bank, to understand why what is remaining does not present the same characteristics as the portfolio that has been sold with low prices. And it can be the case. For example, we have situations where banks have different vintages and different origins of the sub-portfolios: for example at a bank that is the result of mergers that took place before. If the bank can demonstrate that, oh, this is coming from former bank A, and bank A was much worse than the two others with which it was merged, then you have a good case for the supervisor to take into account a difference.

So there is a possibility, the margin is narrow, pretty narrow, so we would not take the risk of not implementing properly the legislation for, I would say, a small operation. If a bank has good reasons on such an LGD issue, and on top of that is ready to do very serious one-off cleaning, then the bank gets the attention of the supervisor. This is what I can tell you on this.

Question: I'd like to come back to one of your previous comments. You were saying that risks have to be addressed early so that they disappear. However, by incentivising banks not to be the weakest ones - to sell their NPLs to less regulated, not to say unregulated, investors, mainly non-EU entities, and pushing NPL risks out of your supervisory scope only, - you therefore expose

SMEs and households to much more aggressive cultural recoveries. Banks build long-term relationship with their clients, when third parties will be, probably, more interested in short-term profits.

Nouy: Well, I will start by saying that this is about new NPLs, so not the situation that you describe. The situation that you describe is more related to the existing stock for which we can see sales. But, for the stock, we take the bank's own plans, and we challenge them to make them credible and ambitious enough; but we start with the bank's own plans. So we recommend nothing. The bank is deciding about the solution. Supervisors do not manage the bank or manage its problems; they just make sure that the banks address their problems.

In certain countries, where the levels of NPEs are pretty high, we can see what we called in our jargon ‘strategic defaulters’, meaning there are a number of customers that could pay but do not repay their loans because that's the average situation in the country. You don't repay until you are totally forced to do so, and hopefully it will not happen any time soon. So yes, they are probably the first customers to target, but that's the job of the banks to identify, and in general they know them very well, these strategic defaulters, that we would like to see addressed among the first.

Donnery: I don't think we have made any obligation on banks to sell portfolios. We recognise that this is one of the tools that they use, and while not within our competence, I know that in some countries, because we saw this in our stock-take of national practices, some countries have put in place frameworks to protect borrowers, particularly if they're personal borrowers, if their loans are sold on.

Question: Just to understand you, you gave an answer regarding massive disposals of NPLs. Imagine, we are in the process of having the proposal from the parliament for the new CRR [Capital Requirements Regulation] and we hope that article 181 of the CRR might be changed, allowing for the correct computation of LGDs in case of massive disposals. Would you be in favour of such an opportunity, of course, under the control of the SSM, or the national competent authorities? Because this would allow us to accelerate the disposal of NPLs, avoiding the second impact of the disposals.

The second question is: when we sell NPLs, we normally have in front of us two kinds of buyers. The first one is a non-bank, for example a fund, and the second one is a bank, subject to the CRR and all the rules, having a banking licence. The question is: would you apply the addendum to the bank, to the potential buyer again, even if this, for example, has a vintage of five? Because this is very important - to avoid, again, an unintended distortion of the number of potential buyers; we have been able, in Italy, to attract a vast number of buyers, and prices have soared from average 18 to average 32. It is of common interest to maintain the largest number possible. This could be two solutions.

Nouy: I will start with the LGD issue with my long past experience with models. No, I don't agree with what you are proposing, and you call it correct computation of LGDs when there is a massive sale. It's not correct computation of LGD. This is the real LGD. When you sell an NPL you are realising your real, true LGD. It's as simple as that. So no, I am not in favour of that. If we were to do that, we would kill the credibility of models of European banks, vis-à-vis our colleagues in other regions of the world; they have already expressed doubts about the risk-weighted asset variability of models in certain situations. We are using a lot of resources to revalidate the models of the SSM banks, to make sure they are well built, well maintained, and that they deliver adequate risk-weighted assets. So we will certainly not play games with LGDs; that's not at all a possibility.

We want the parameters of the models to be sound and safe; and we cannot ignore risk by having a reality which looks nicer than it is. It's also a matter of having a level playing field. A number of banks in the SSM countries are selling NPEs and taking the LGD consequences, and have been taking the LGD consequences for decades. So that would really be a very bad move, in my view, for the credibility of the models that we are creating through our TRIM [Targeted Review of Internal Models] project. This being said, as I mentioned earlier, in very specific circumstances, there is a little bit of margin, though this margin is thin, which is left to the consideration of the supervisors, and, frankly, with all the effort we have put into trying to address and fix this non-performing exposure issue, bankers that are willing to do the right thing, to take the right measures and that can give us good reasons as to why they want to use the possible flexibility on LGDs, well they will get our attention.

We will not start by being negative and saying ‘no, except if…’ we will say, 'okay, let's look at what you have to offer'. We saw that when we do that, we create a precedent, because another bank exactly in the same situation will need to have the same treatment. So we will be cautious, but open-minded. Provided we are still complying with the rules, and supervisors are there to implement the rules, indeed, there is a small margin, thin margin for flexibility. We want to see — you used the word ‘massive’, well yes, a ‘massive operation of cleaning’ would get our attention.

Donnery: I think your second question was complementary to the question or the discussion we were having earlier. So first, I would say in terms of definition, as we had said earlier, the definitions are consistent with the EBA definition, so to set the vintage account back to zero, or to say that a loan has been cured, obviously requires it to meet the criteria that have been set out in the definition, and all our guidance is consistent with that important work that has been done to standardise.

As we said earlier, if a bank is selling a portfolio to another bank, then, clearly, there's a process that's gone through, regardless of the addendum, in terms of supervisory dialogue, and also the due diligence process, which would be part of the discussion. But we will, I think, consider the feedback in terms of how, maybe, we can explain this a bit better in the addendum.

Question: I wanted to know if you could elaborate a little more on the linear path to this 100 per cent that you are mentioning, precisely because of the models, and to know your opinion on whether this linear path could jeopardise the credibility of the models. We've been working in models, reacting to the vintage of NPLs for a while, so I wanted to know your opinion on that.

Donnery: So first of all, about the linear path, the reason why we put it there was to try to mitigate against a kind of cliff-edge effect where nothing would happen, and then at the last moment there would be a large provision to be taken. So we were trying to set out that we expected banks to be able to do this gradually, and this would be a way that we would think about it.

It's important to emphasise, as well, though, that if the bank is taking more provisions than that itself, through its own policies and procedures, then, obviously, that's also the case as well, and we would be discussing that with the bank.

I think, then, in terms of LGD, it would be about the dialogue with the bank, and how those things actually work out, whether they have their own policies, whether they're taking a linear path, and whether they're doing something else. Maybe you want to add something?

Fröhling: I think the point is right that when we put in a suitable gradual path, we wanted to keep it quite open, which for the two years makes sense, I think, and it's good to keep it open and to give banks the time to consider what's adequate. But when it came to the seven years, we had a lot of discussion with our different supervisors in the 19 countries, and there were concerns that if we left it completely open and set a suitably gradual path, it could result in an unlevel playing field. So this is why, in the end, we decided to include some high level guidance.

Now, if there are ideas in this consultation phase where you say ‘we actually have a better idea of how to specify this, which we consider a bit better approach’, we'd be very happy to listen.

Question: I'm a journalist with Bloomberg News. I realise it's not a press conference, but since we're at the end of the hearing, I would like to ask one question, please. My question is about a potential delay to the implementation of the guidelines. Madame Nouy, you were very clear, very clear in Brussels at the ECON [European Parliament Committee on Economic and Monetary Affairs] hearing, that you will listen to all the feedback, you'll process it, and if that means you can't get something together for the 1st — or if it means you can't finalise your package for 1 January, you will take more time to finalise it.

So my question is: How much time do you think you have? Is this something which needs to be done in 2018? I mean, 2018 - it's a long period. Then, even if you can't tell us exactly the timeline on that, maybe you can tell us about the period of time that matters for this, because I sit on the outside, and I look at bank releases and quarterly reports, and they are quarterly, and I wonder how that figures into any potential delay and whether we should be expecting something which would be a month-by-month delay or a quarterly delay.

Nouy: Well, to be honest, I cannot be more precise than I have been in the European Parliament because we don't know yet how many comments we will receive and how complex the comments will be. As a matter of fact, it was just common sense, so we did it before this hearing: we asked our colleagues how many comments we have already received and what are the points that we should be ready to address in this hearing, because those are points of concern. And we could count on one hand the number of comments that we have already received. So I presume that we will receive a lot, because this is an issue that raises a lot of interest. But I don't know how many, I don't know how complex they will be. We have received already, not comments, but a number of legal consultations, the parliament's one in particular. We will certainly take into account all the good legal advice that we have received, to make sure that the addendum is drafted as cautiously as possible and translates the reality, and does not look like Pillar 1. For the rest, we don't know.

So what we will do is, after the deadline [for the consultation] which is 8 December, if I remember well, we will see where we are, and we know that it may take two or three more days to have all the comments because a few will come also, maybe, the day after. Then we will assess the quantity of work it takes to do what we always do through consultation. We take consultations very, very seriously. We publish the comments; we explain why we are taking comments, certain comments, and not others.

So it is based on the time it takes to do a good job in drafting the final addendum and this includes, going through the comments, taking the ones that we should take and explaining why we are not taking others. We will see what it means. Because, if we look at it from a different perspective, what is desirable is very obvious: to make sure that we address the future possible piling up of NPEs and the sooner the better. But it will take what it will take. It's a big issue. We started in 2014, so a couple of additional months would not be an issue. I was, indeed, clear in Brussels, because I explained to the MEPs that were in the hearings, that I was taking note of what they were telling me, and that the final decision, would be taken by the supervisory board of the SSM. But I also went as far as saying that I will recommend to my supervisory board members to postpone it a little bit, to make sure, if need be, that we can make full use of the comments, because, indeed, well, the timeline is very tight— probably too tight, even including a lot of time in the office between Christmas and New Year's Eve. So a few additional months are probably needed. But I cannot be more specific, because I don't know at all what we should expect.