Template for comments

Public consultation on the draft Guide on the supervisory approach to consolidation in the banking sector

Type of respondent

Banking Association

Institution/company

Spanish Banking Association (AEB)

Contact person

Mr/Ms

First name

Surname

Email address

Telephone number

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

General comments

The Spanish Banking Association (hereinafter, AEB) and its bank members would like to thank the European Central Bank (ECB) for the opportunity to comment on the consultation “Guide on the supervisory approach to consolidation in the banking sector”. We would like to highlight that the Spanish Banking Sector has been immersed in a deep consolidation process during the last ten years. The number of Spanish active banks has drop significantly after 2008. In this sense, we very much appreciate the visibility regarding to the supervisory expectations on consolidation that the ECB is providing to the banking sector.

First of all and as a general comment, we share the official view that supervisory or regulatory issues should not be one of the key drivers for a corporate transaction. However, it is true that supervisors should play a role facilitating or at least not complicating the transaction per se. As such we welcome this initiative that tries to simplify the potential supervisory/regulatory burden embedded in any corporate transaction.

In fact, in our view, there are some areas that allow supervisors to play a key role or at least trigger a potential transaction. To be more precise, art 27.1 of BRRD establishes the powers the SSM has under a financially deteriorated situation of a bank. One of these powers is the ability to require the Board of the bank to examine the situation and identify potential measures. This could be a trigger for a potential merger. The aim of this article is that the Board of a bank could take the required actions to find a solution to the situation and therefore overcoming the initial reticence by the management team to recognize and solve the situation.

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Please enter all your feedback filling in the table below as following :
- Fill in the 5 green columns only: "Paragraph", "Type of comment", "Detailed comment", "Concise statement as to why your comment should be taken on board", "Proposal for adjusted wording";
- Respect drop-down menus. Do not alter the drop-down menus.
- Other columns, blue columns, are filled in automatically; do not alter them;
- Each comment shall deal with a single issue only; you can enter two comments for the same paragraph if you see several issues in the same paragraph; you can enter the same comment several times if it applies to several paragraphs;
- Indicate whether your comment is a proposed amendment, clarification, deletion or addition to the guide;
- Propose an alternative wording when appropriate.

Please do not make any changes to the structure of the template. Any feedback provided in a modified template will not be processed.
To ease the feedback process, please ensure you provide your feedback in an xls format only (i.e. not pdf)

Deadline:	1 October 2020

Id	Paragraph	Page	Section	Type of comment	Detailed comment	Concise statement as to why your comment should be taken on board	Proposal for adjusted wording	Type of respondent	Institution/company	Name of commenter	Personal data
1	4	2	Introduction	Clarification	1.1. More clarity in consolidation principles for non-SSM entities. The Guide should provide more clarity for cases when the consolidation project involves a non-SSM entity. It would be helpful if the ECB could reiterate its support for consolidation and the benefits of cross-border consolidation in the guide by expressing its intention to facilitate the recognition of the Banking Union as a single jurisdiction where possible.	More clarity in consolidation principles for non-SSM entities.		Banking Association	Spanish Banking Association (AEB)		Don´t Publish
2	6	2	Objectives	Addition	Need for a Fit & Proper assessment fast-track. This fast-track assessment process for the Boards and Executive Committees of all bank entities of the Group acquired would be very appreciated by the industry. For instance, the ECB could grant an exemption from the Fit & Proper assessment when the appointed management body and Board members are already management body or board members from the participating entities and have already been vetted through a fit and proper assessment.	A specific fast-track process could be envisaged for FAP when target Board members have already been through that ECB process.		Banking Association	Spanish Banking Association (AEB)		Don´t Publish
3	7	2	Process	Addition	In the case of resolution case, sale authorizations fast-track. Until the formal authorisation is granted the sale is "on hold" and the buyer has to refrain for doing anything that cannot be reverted later on in case the authorisations weren´t obtained. This is a precious time, esp+A1ecially in resolution. It would be desirable that the guidelines include a manifestation from the ECB that confirms that the teams in charge of the review would have adequate resources, that standard documentation packages would be produced to facilitate the process, and that a calendar/timeline will be produced to ensure that the length of the process is monitored.	Need for recognition of a special regime for cases in which a bank in resolution is acquired		Banking Association	Spanish Banking Association (AEB)		Don´t Publish
4	7	2	Process	Addition	In a resolution case, an explicit exemption of the criminal responsibility of a legal person would be included to avoid the buyer entity facing the dead weight and uncertainty of such legacy.	Need for recognition of a special regime for cases in which a bank in resolution is acquired		Banking Association	Spanish Banking Association (AEB)		Don´t Publish
5	7	2	Process	Addition	In a resolution case, also, exemption from public responsibility derived from the previous mismanagement in procedures that do not intend to compensate clients/investors but to disincentive bad behaviours would also be contemplated.	Need for recognition of a special regime for cases in which a bank in resolution is acquired		Banking Association	Spanish Banking Association (AEB)		Don´t Publish
6	8	3	Early communication	Addition	In the case of a resolution operation, change of control clauses should not be activated in cases of mergers, spin-offs, or change of structure operations.	Need for recognition of a special regime for cases in which a bank in resolution is acquired		Banking Association	Spanish Banking Association (AEB)		Don´t Publish

7	14	5	Sustainability of the business model	Clarification	EBA Stress Test exercise. It should be considered the fact that performance of a recently acquired resolved bank cannot be taken as reference for future projections as the risk profile and management has changed dramatically with the integration on a sound bank.	Need to make an accurate analysis		Banking Association	Spanish Banking Association (AEB)		Don´t Publish
8	26	8	Pillar 2 capital requirements and Pillar 2 guidance	Clarification	Treatment of restructuring costs. In a consolidation transaction, one of the most relevant value levers nowadays is the potential value creation that could arise as a result of a more efficient combined entity. In practice, while this should be acting as an important catalyst for Bank consolidation, the reality is that it is having the opposite effect given the significant burden that entails recognizing the restructuring costs upfront particularly in a context of depressed valuations. The big challenge stands in the fact that restructuring costs in the context of a combination must be booked upfront while the potential benefits of such a transaction are accrued only at a later stage. This only happens in the context of a business combination because the same restructuring but happening in the ordinary course of business would have more synchronization between restructuring costs and value creation. It is possible to mitigate this negative effect of front-loading restructuring costs if it is allowed to have only (i.e. not pdf)cess, these analyses should be focused on the current circumstances avoiding the application of extra margins of conservatism. o On the other hand, in relation to the AIRB parameters that will be applied to the consolidated portfolio, although a joint parameter calibration could be an option, it is not suitable that the buyer's internal models could be impacted by the historical behaviour of the acquired portfolio. In this regard, a model adjustment to the buyer' internal models could be applied to the purchased portfolio assurin	The paragraph is not sufficiently clear for us		Banking Association	Spanish Banking Association (AEB)		Don´t Publish
9	26	8	Pillar 2 capital requirements and Pillar 2 guidance	Addition/Clarification	Reasons for adjusting the P2R/P2G starting point. In our opinion there are several factors that should be taken into account that could imply a reduction in the capital requirements (i.e.: business model of the new entity, risk management capabilities, etc). To be more specific: i) as a result of the merger, the combined entity normally adjusts its provisioning levels with a view to match coverage levels of the combined institution to the highest of the coverage levels of both independent institutions, thereby homogenizing coverage criteria; ii) As a result of the merger, the assets of the absorbed entity are valued at fair value and are normally adjusted by marking down the amortized cost fixed-income portfolios, therefore having a more conservative profile and iii) combined entity has a greater capacity to generate revenues and capital, to the extent that it has to book restructuring costs upfront.We are suggesting a freezing of the capital requirements (and guidance) during the integrating process and a recalibration once the transaction is executed.			Banking Association	Spanish Banking Association (AEB)		Don´t Publish
10	28	8	Pillar 2 capital requirements and Pillar 2 guidance	Addition	Additionally, the reference in paragraph 28 to "complex IT projects" is too general as most banks are likely to have complex IT infrastructure. Moreover, as written, the guide could be construed as implying any IT risk integration project would be deemed complex by the ECB with the consequences that this will always result in an upwards adjustment of the starting point. The guide should recognise factors which can be taking into account by assessment teams such as the relative size of the acquired entity of the acquisition and complexity of the IT integration project for the acquirer, its track record on IT systems integrations and actions set out in the integration plan to mitigate IT integration risk.			Banking Association	Spanish Banking Association (AEB)		Don´t Publish
11	32	9	Badwill	Clarification	Use of badwill. We more than welcome the confirmation of the principle that the ECB will recognise duly verified accounting badwill from a prudential perspective. However, the paragraph also indicates that the badwill distribution could not occur *"until the sustainability of the business model is firmly established"*. This phrase could in our opinion result in imposing distribution restrictions that do not exist in the legislative texts; we do not understand under which legal basis such restrictions could be imposed in an ECB guide. Even if there were legal basis for imposing those restrictions, we believe the notions of "badwill distribution" and of "the sustainability of the business model" are far too vague to be applied in a consistent manner. In addition to this, an entity's payout should not be limited to the extend that it continues to meet its obligations under P2R and P2G. Badwill is the compensation for, inter alia, transaction costs and other one-off costs and, the acquiring entity's payout may be reduced if forced to not make distributions out of the badwill.	This phrase could in our opinion result in imposing distribution restrictions that do not exist in the legislative texts		Banking Association	Spanish Banking Association (AEB)		Don´t Publish

12	New paragraph 37	10	Eligibility criteria	Addition	Restrictions on the full computability of AT1 and T2 of the acquired bank. Issuances of the acquired company should be fully included in the prudential computations from the resulting institutions. CRR treatment of minority interest implies a considerable detriment on the computability of capital instruments. SSM should analyze the possibility of overruling this effect through a conditional total capital requirement over the acquired entity with the aim of not showing any capital excess. In this regard the SSM could increase the capital requirement to the acquired bank to the reported capital level avoiding therefore any excess of capital and permitting the full computability of the capital instruments.	In order to minimise impediments to M&A activity, it would be helpful for the ECB to provide banks with some flexibility to manage the restructuring of their capital structure. The same considerations are also relevant for the MREL requirements, where the resolution strategy of the group could be adapted to facilitate an acquisition.		Banking Association	Spanish Banking Association (AEB)		Don´t Publish
13	36	10	Internal Models	Addition	More flexibility in the supervisory approach to the use of internal models. Need to extend the use of buyer's IRB models to all exposures of acquired bank as soon as these exposures are migrated to buyer's systems. This could imply: o Fast track authorization process to apply buyer´s internal model to the acquired portfolio (standardised and IRB).o In relation to the availability and quality of the historical data, the correction of the deficiencies in the data should not be a priority. The attention should be given to the current data and the regulator relaxing requirements if it is needed under certain circumstances. o The representativeness analyses regarding the default definition, scope of application, distribution of the relevant risk characteristics and lending standards and recovery policies are required by the regulation. In a banking consolidation scenario, satisfactory results of the representativeness analyses are not assured. Due to the changes of the management criteria and policies in the consolidation process, these analyses should be focused on the current circumstances avoiding the application of extra margins of conservatism. o On the other hand, in relation to the AIRB parameters that will be applied to the consolidated portfolio, although a joint parameter calibration could be an option, it is not suitable that the buyer's internal models could be impacted by the historical behaviour of the acquired portfolio. In this regard, a model adjustment to the buyer' internal models could be applied to the purchased portfolio assuring an appropriate performance in the current periods.	More flexibility in the supervisory approach to the use of internal models. Need to extend the use of buyer's IRB models to all exposures of acquired bank as soon as these exposures are migrated to buyer's systems.		Banking Association	Spanish Banking Association (AEB)		Don´t Publish
14	41	11	Foster the swift convergence of the newly combined entity with standard supervisory activities	Clarification	We miss a part related to the supervisory activity. A merge transaction absorbs a considerable amount of resources fully dedicated to ensure the success of the operation. As such, we would welcome that supervisors adapt the supervisory program to the new situation. In this regard, we would suggest to reduce, or eliminate, the "ordinary" activity and focus on how the bank is executing the integration. This means that the JST should avoid performing the Supervisory Examination Program (SEP) of the institutions under the operation and instead designing a new program adapted to the newly created bank. It is the same philosophy as during the Covid 19 crisis. The SSM has not cancelled the supervisory activity but on the contrary, they have increased the intensity of the supervisory pressure but focusing on how banks were managing the crisis and therefore postponing those supervisory activities meant to be performed under normal circumstances	A merge transaction absorbs a considerable amount of resources fully dedicated to ensure the success of the operation.		Banking Association	Spanish Banking Association (AEB)		Don´t Publish
15	41	11	Foster the swift convergence of the newly combined entity with standard supervisory activities	Addition	In a resolution case, Prudential authority's on-track inspections on the resolved institution should be "frozen" and remediation plans derived from previous inspections reviewed when there is a plan to integrate the management systems with those of the buyer.	Need for recognition of a special regime for cases in which a bank in resolution is acquired		Banking Association	Spanish Banking Association (AEB)		Don´t Publish

16	New paragraph 46	12	Regulatory issues (outside the SSM)	Addition	Larger institutions are penalised due to higher capital buffers for G-SIBs. Intra-Eurozone assets and liabilities contribute to the cross-border activity indicator of the international G-SIB buffer requirement, penalising cross-border institutions within the Eurozone in spite of progress made via the EU recovery & resolution framework and the reinforcement of group supervision under the SSM. We could ask for some discretion in the application of buffers in consolidation processes, as combined entity might move to higher size and a bucket in G-SIBs capital buffer. The new Basel operational risk framework, requires higher capital requirements to larger groups vs. smaller ones and an additional "extra buffer" to groups with subsidiary-based business models, by requiring the BIC to be calculated at consolidated level (instead of aggregating the BICs at a subsidiary level, like in the current framework). The lack of an EDIS (European Deposit Insurance Scheme) that impedes the free flow of funding and creates liquidity ring-fencing. The lack of harmonisation of legislation among Member States, such as insolvency rules, consumer protection or AML. The tax framework is particularly relevant for M&A transactions: in any cross-border transaction, deferred tax assets could be lost (depending on the transaction structure), even if there is no change in the parent company's head quarter. An additional tax inefficiency could be represented by taxes triggered by a change of control not only in case of takeover, but also in case of merger/combination. 2.5. Restrictions on distributions of excess capital: certain national laws/regulations do not allow the free movement of capital across Eurozone countries, even within the same group e.g. limits placed on the distribution of the excess capital from subsidiaries to the parent company. 2.6. Restrictions in the recognition of minority interests in group capital: The CRR restricts the inclusion of the minority interests (located in CET1, AT1 or T2) in the calculation of consolidated own funds, as the surplus capital pertaining to minorities is excluded from the calculation, whilst on the asset side partially-owned subsidiaries are fully consolidated at group level. As the level of capitalisation of subsidiaries is often higher than minimum requirements and because it not possible to recognise this excess at group level, the current regulation creates a significant disincentive to M&A transactions with minority interests.	The current regulatory framework in EU has to be modified in order to make consolidation processes more attractive		Banking Association	Spanish Banking Association (AEB)		Don´t Publish