

Template for comments

Consultation on the draft ECB Guidance for banks on non-performing loans

ID	Chapter	Section	Page	Type of Comment	Detailed comment	Name of comment	Personal data
1	7 - coll	7.1	85	Deletion	<p>The draft ECB guidance to banks on non-performing loans explicitly focusses on non performing loans (NPLs). Therefore we cannot understand why the scope of chapter 7 „Collateral Valuation for immovable property“ is extended to other banking processes („The main focus is on provisioning but the guidance can also be used where appropriate in the loan processing, monitoring and underwriting process“).</p> <p>To assure legal certainty of ECB-publications, the ECB guidance to banks on non-performing loans should be restricted to NPLs only. Escape clauses within the document that expand the rules also to other banking processes do not help to secure legal certainty within the European regulatory framework.</p> <p>Suggestion: We suggest deleting this escape clause and restricting the rules to NPLs .</p>		
2	7 - coll	7.1	85	Amendment	<p>It is clearly mentioned within this chapter that Art. 208 and 229 CRR apply for this guideline. Unfortunately all following drafted requirements dealing with valuation and monitoring/ review of property values are clearly stricter compared to the CRR requirements. They explicitly do not allow an application of Art. 208 and 229 CRR. Due to the escape clause in this chapter we have to assume, that the regulations on valuation and monitoring of property values might also be of relevance for further banking processes. Therefore we kindly ask for regulation in accordance with Art. 208 and 229 CRR. There might be reasons for stricter regulation as stated in Art. 208 and 229 CRR for the limited area on NPLs. However, such stricter rules should also be in line with already implemented processes in the banks to fulfil Art. 208 and 229 CRR and might add some elements.</p> <p>The following two examples shall show this problem clearly:</p> <ul style="list-style-type: none"> • Art. 208 (3) CRR allows a monitoring and review process for property values. The draft guidance to banks on non-performing loans ignores this process completely for NPLs of more than 300,000 EUR and demands regular updated individual property valuations. • Art. 229 CRR allows to value on the basis of market or mortgage lending value. The draft guidance to banks on non-performing loans only allows valuations on the basis of market value. <p>Suggestion: We propose to align valuation and monitoring/review requirements with Art. 208 and 229 CRR.</p>		

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3	7 - coll	7.2.2	87	Amendment	<p>According to Art. 208 (3) CRR institutions monitor the value of the property on a frequent basis and at a minimum once every year for commercial immovable property and once every three years for residential real estate. Institutions carry out more frequent monitoring where the market is subject to significant changes in conditions. Further on the property valuation has to be reviewed when information available to institutions indicates that the value of the property may have declined materially relative to general market prices and that review is carried out by a valuer who possesses the necessary qualifications, ability and experience to execute a valuation and who is independent from the credit decision process. For loans exceeding EUR 3 million or 5 % of the own funds of an institution, the property valuation shall be reviewed by such valuer at least every three years.</p> <p>Art. 208 (3) CRR already regulates monitoring and review of property values in clearly stated time frames as well as occasional reviews. Therefore we do not see the additional benefit of the several rules mentioned in chapter 7.2.2 to implement an internal quality assurance policy. Such instruments – common in the risk management of banks - do not necessarily have benefits in the process of collateral valuation. Further on we do not understand some of these rules, e.g.:</p> <p>(1)According to CRR valuations have to be undertaken by valuers “...who possesses the necessary qualifications, ability and experience to execute a valuation and who is independent from the credit decision process”. What other persons in the bank have a similar knowledge and experience to undertake such a test of the valuations of experienced and independent valuers? Who selects this sample and what kind of data shall be used that was not already used for the valuation anyway?</p> <p>(2) We also do not see an advantage of a rotation requirement (last para, p. 87) to improve the quality of valuations as long as (other) sufficient provisions and processes are in place that ensures accurate valuation results. The fulfillment of comprehensive requirements regarding independence and qualification of (internal and external) valuers, international and national valuation standards as well as internal plausibility checks of external valuations already secure a high quality of valuations.</p> <p>Suggestion: The rules stated in this chapter should be discussed with view to an alignment with Art. 208 and 229 CRR as well as workable processes within a bank .</p>	[REDACTED]	[REDACTED]

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4	7 - coll	7.2.3	88	Amendment/ Clarification	<p>With the requirements stated in this chapter the whole process of monitoring/ reviewing of properties as described in Art. 208 (3) CRR is obsolete for non-performing loans of more than 300,000 euro in gross value. We understand that there might be stricter requirements regarding review of values for NPLs. These monitoring processes should be oriented in accordance to different risk profiles of properties and might also vary according to the concrete business model of a bank. A European-wide basis of 300,000 EUR does not reflect the different price levels of regional property markets and therefore in our opinion is no suitable basis for assessment. We want to highlight that indexation is only one of many opportunities how to establish a monitoring process. Therefore within the guideline it should be handled as an option but not as headline for all monitoring processes based on statistical models.</p> <p>Suggestion: A European wide assessment basis should be avoided. Most suitable would be an assessment basis on individual banking level. Alternatively property types (here e.g. single family and semi-detached houses as well as apartments) could be the basis for easements. Statistical models used in the context of monitoring should be phrased more open, as already stated in Art. 208 (3) CRR.</p>		
5	7 - coll	7.3	90	Amendment	<p>The combination of chapter 7.2.3 and 7.3 would mean that for every NPL of a gross value of more than 300,000 EUR an individual valuation by an independent and qualified valuer is necessary, every year for commercial properties and every three years for residential properties. There might be reasons especially for NPLs that justify new valuation but as already mentioned in the remarks of chapter 7.2.3 this should focus on the concrete property portfolio of banks and consider different price levels in European national/ regional property markets. Further on we want to highlight that it is current practice within the appraising industry to link the fee for external valuers to the market value as it commonly reflects efforts and risks taken by the valuer. Therefore we would welcome a clarification as normal market practice fees as a percentage of the value per se do not impose a risk of incentivizing the external valuer, as the valuer is taking over liability for correctly calculating a fair market value in accordance with applicable regulations. Within the guidance a new term in the context of monitoring of property values is introduced: update of valuations. We want to stress that CRR already uses terms in this context – monitoring, review and revaluation - that are well established in the valuation industry. In our opinion the introduction of new terms should be avoided. If a new term is necessary, it should be clearly described.</p> <p>Suggestion: The rules stated in this chapter should be discussed with view to an alignment with Art. 208 and 229 CRR as well as workable processes within a bank and best practice within the valuation industry.</p>		
6	7 - coll	7.4.1	91	Amendment	<p>It is clearly stated that collateral should be valued on the basis of market value. As already mentioned above, Art. 229 CRR allows valuations on the basis of market or mortgage lending value.</p> <p>Suggestion: We kindly ask to open the accepted valuation basis for mortgage lending value.</p>		

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7	7 - coll	7.4.1	91	Amendment	<p>Valuations based only on the discounted replacement cost are not allowed. We cannot understand this general refusal of the replacement cost approach. German valuation standards for market as well as mortgage lending value consider the replacement cost approach for the valuation of single family houses and semi-detached houses. This approach has a long tradition in Germany and is well established within the valuation industry. From a theoretical point of view of course it is possible to use other valuation approaches – in the case of single family and semi-detached houses probably the comparison approach. But it has to be taken into consideration an important practical aspect: the data availability on regional market level. Banking regulation might counteract with national valuation standards as well as data availability on regional market level. A SSM guideline should respect national and regional characteristics of property markets in a way that the most suitable approach for the respective market can be applied, i.e. this approach that reflects best the regional market conditions.</p> <p>Suggestion: Requirements should focus on the usage of the most suitable valuation approach for the respective property type and regional market characteristics. The decision should be taken by the qualified valuer. The replacement cost approach should be allowed within this context as well</p>		
8	7 - coll	7.4.3	92	Deletion	<p>Within this chapter a back-testing approach is implemented (page 94). We want to stress that property valuation traditionally bases on property specific analysis. Statistical methods are an excellent instrument for the monitoring of property markets and portfolios but only with the objective of identification of properties that might need (individual) revaluation. Model based approaches as mentioned in the guidance are not common in the field of property valuation as they do not reflect the typical characteristics of a concrete property. Further on we do not understand the connection between the enormous requirements regarding the monitoring of property values (chapter 7.2 und 7.3) and this additional back-testing. It has to be highlighted that property valuation is consciously a process independent from lending, esp. credit decision. This is reflected in the enormous requirements on the independence of valuers. The determination of discounts on property values based on LGDs does not respect this principle of independence of the property valuation process. As already stressed in connection with the planned internal quality assurance policy (chapter 7.2.2) also back-testing is a common risk management tool that is not necessarily adaptable to collateral valuation.</p> <p>Suggestion: We suggest deleting these back-testing requirements within this guidance.</p>		