To: **Mr Giuseppe Siani**
Deputy Director General
Directorate General Micro-Prudential Supervision IV
European Central Bank
Email: Giuseppe.Siani@ecb.europa.eu

Brussels, 31 January 2017

Re: ECB draft guidance to banks on non-performing loans (NPLs)

Dear Mr Siani,

The European Banking Industry Committee (EBIC) takes note of the ECB's objective to reduce NPLs in banks' balance sheets. We understand the background of this initiative and support the development of clear standards in this field. In this context, we welcome the release of the ECB's draft guidance and stocktake of national practices, which we believe are a very useful work basis.

The application scope of the proposed guidance document is broad and its operational implications are important, as it will not only apply to significant institutions active across multiple jurisdictions, but also to small and medium-sized firms with various structural and organisational characteristics. To enable adaptation of banks' processes and technologies, we would appreciate a transitional implementation period allowing banks to prepare for the compliance with the guidance.

As highlighted by the ECB at its 7 November 2016 hearing, it is crucial to ensure sufficient flexibility in the implementation of these standards. For those institutions that do not carry high NPL stocks, we believe it should be sufficient for them to demonstrate that their governance and management of NPL's are sufficiently aligned with the ECB principal standards and have shown to be effective. Clarification needs to be included in the guidance establishing a clearer and more understandable connection to the proportionality principle and a separation of high and low NPL banks. We suggest to explicitly design the requirements of the guidance in a way that adequately reflects the proportionality principle. The requirements should be geared to classification as high or low NPL banks, with implementation of certain requirements being explicitly waived for low NPL banks.

For example, the requirements regarding organisational structure and operational set up are too detailed and prescriptive, and should be replaced by a set of principles. We understand the objective to separate the units responsible for loan origination from those in charge of NPL management to avoid conflict of interest. However, as also recognized by the ECB, appropriate internal controls should suffice to prevent potential conflicts of interest. Flexibility should be preserved where the establishment of a fully separate organisational unit is impossible or disproportionately costly (e.g. in the field of human resources). We believe that it should be left to individual banks to decide how to apply the principle of separation of these units. Similarly, the nature of Annex 6 in our view contradicts the flexibility the ECB is keen to provide in the field of NPL management and should be reviewed.

It is also important to ensure that the NPL strategy and methodology adopted are consistent with firms' business models, local market conditions and other external factors. The establishment of an "EU average NPL" as a benchmark is inappropriate as credit institutions' business models differ substantially. For example, there are banks that purchase NPL portfolios as part of their core business or chose segments with inherent high expected losses. Purchased NPL portfolio are often acquired at a price way below nominal amount. A high-NPL level can be a natural result of the management objectives and strategy in regards of purchasing NPL portfolios as part of a business model. In addition, institutions pursue different workout strategies based on the regulatory and legal environment in which they operate. For some of them NPL sell-off options are limited, while others can benefit from a regular sell-off process. Hence, setting one non-performing exposure target (NPE) for all, regardless of their business and operating models, and legal and regulatory environment does not create a level playing field. We are also concerned with potential complexity and uncertainty given that the average levels of NPLs are subject to frequent moves.

The ECB's expectations on the applicability of the guidance, impact of macroeconomic conditions on NPLs, disclosure obligations, supervisory measures for non-compliance, as well as the timeline for implementation should be further discussed and clarified. We would also welcome further clarification on the application of the guidance to banking groups. An identical implementation would not leave room for the proportionality principle. While it will be the responsibility of each bank to ensure compliance with the guidance, it should be clarified whether there will be any formal communication channel between supervisory teams and the bank to "trigger" compliance with particular requirements of the guidance.

It is also important that the guidance is applied in a balanced way that avoids sudden undue pressure on asset values.

The guidance should be aligned with European legislation and should not override or interpret accounting standards. For example**:**

- The identification of the financial difficulties should be aligned with the EBA ITS;
- Cure periods under the draft guidance should be aligned with EBA ITS;
- Collateral valuation requirements should be aligned with the Articles 208 and 229 of CRR;
- The requirement to establish a minimum provisioning level depending on the type of collateral as a supervisory best practice for exposures covered by collateral contradicts IFRS 9.

We understand that the ECB wishes to impose additional disclosure and reporting requirements on SSM banks. However, we believe that the supervisory reporting and public disclosure requirements should be set by European Regulation. The ongoing CRR review foresees substantial amendments to the regulatory reporting framework as well as disclosure requirements. In this context, the introduction of new regulatory reporting or disclosure requirements does not seem proportionate. We think that new reporting and disclosure requirements should only be considered as part of the wider legislative review of these requirements.

One final aspect that we wish to point out refers to forbearance measures. Local legal frameworks will often impose a very strict forbearance pathway and solutions. This is particularly relevant in a B2C environment. We are concerned that the ECB's list of forbearance measures could create some public expectations whereas, in practice, many credit institutions will have limited flexibility as to what type of solutions can be put in place, when and under what conditions. Apart from that the requirement that banks should use a net present value (NPV) approach to determine the most suitable and sustainable workout option for borrowers' varied circumstances seems, at least in the retail business, unnecessarily burdensome. A risk-based approach that takes the significance of the exposure into consideration would be more suitable.

We hope these points can be taken into account by the ECB and remain at the disposal of the Authority to discuss any further issues.

Yours sincerely,

Hervé Guider
EBIC Chairman