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EBA - Draft ITS on supervisory reporting on forbearance and non-performing exposures under article 95 of the draft CRR - CP-2013-06

The Division Bank and Insurance of the Austrian Federal Economic Chamber, as representative of the entire Austrian banking industry, appreciates the possibility to comment on the EBA Consultation Paper relating to Draft ITS on supervisory reporting on forbearance and non-performing exposures under article 95 of the draft CRR (CP-2013-06) and would like to submit the following position:

Question 1

Do you agree that building definitions of forbearance and non-performing by taking into consideration existing credit risk related concepts enables to mitigate the implementation costs? If not, please state why.

No, as the adjustments would trigger substantial implementation costs without generating substantial new regulatory necessary information.

Concerning the definition of "non-performing" assets:
We strongly doubt that the approach of EBA – to add a new definition and by this ignoring existing data, ignoring potential synergies and opening redundancies and adding complexity by the introduction of an additional definition not being aligned with the existing definitions and before the background that even the existing definitions are not aligned – is of an additional regulatory use. We specifically question the use in light of potentially huge implementation costs depending on the final definition. Confronting the credit industry with additional regulatory burdens in this respect is simply unacceptable, specifically due to the fact that the credit industry is already overloaded with regulatory requirements.
The authors assume that today the default and impairment definition is the same across the European Union. We want to underline that this is not the case today in case of the default-definition, due to national discretions (many of them being removed by CRD IV/CRR, but not all, e.g. debtor/transaction view choice), due to existing differences between IRB and standardized approach (which will also be aligned by CRD IV/CRR) but also by different levels of thresholds

(which will not be aligned by CRD IV/CRR). This means that even after the implementation of CRD IV/CRR we will face differences in the default definition country by country. For cross-border banking groups this is even without a new definition of non-performing assets a challenge. The existing differences are related to different geographical and economic situations (e.g. thresholds), to different histories, to different systems and to different goals (default vs. impairment vs. NPL). We doubt that a "single view", capturing all dimensions, as set out on page 24 of the paper, can be achieved and is even useful to achieve.
The proposed new definition is – compared to the current definitions – also somewhat complex. As examples in regard to the complexity/lack of clarity following issues could be mentioned:

- Page 8, third paragraph: Need to assess if consideration of the trading book really is necessary/ reasonable

We would therefore strongly recommend for the time being to use existing data from COREP and FINREP in terms of defaulted and impaired assets. Changes in definitions or additional reporting requirements are from our perspective currently not necessary.

Concerning the definition of "forbearance":
The complex definition presented by EBA, specifically with a view that every single transaction would have to be checked against this definition, is also simply unacceptable
As examples in regard to the complexity/lack of clarity following issues could be mentioned:

- Page 11 first bullet point (" a modified contract includes more favorable terms than those that the debtor could have obtained in the market"):

A comparison with other market terms appears challenging (e.g. how would the customer be rated by another institution, which conditions could he obtain); It is not realistic to expect lenders to check this: the loan conditions offered by competitors are not openly available in any market.
How are cases supposed to be handled where the change in contract is triggered by different issues (e.g. sales initiatives, different product strategy)?

- Page 11, third bullet point ("…or partially past-due more than 30 days")

What concerns the proposed 30-day period we strongly doubt that this period is appropriate due to the fact that this would simply mean that any action taken after the due date of one installment would have to be treated as a case of forbearance. The 30 DPD -period is too early an indicator and not necessarily indicative of longer term risk performance. The proposed criteria to identify payment difficulty for retail clients is 1x 60DPD in the past 3 months. This helps differentiate risky clients (60DPD) vs. sloppy payers (30DPD) and covers recent difficulty (last 3months). We are of the opinion that only cases where at least two installments are due should be taken into account, which means one time 60 days overdue during the past 90 days.

- Certain terminology is too vague, for instance on page 11 – last bullet point- "more than an insignificant amount"; page 12 first bullet point – how is a "probation period" defined? The significance of these terms appears questionable.

- As far as we understood, the proposed criteria would apply on a single transaction basis. Due to the fact that this would trigger enormous implementation/training, we would suggest setting up a simple framework, especially by formulating a definition that would allow implementing an automated process. Please also see below.

The forbearance definition should leave room and is not too close to the default/impairment-definition, otherwise forbearance could trigger default already. Credit institutions on the other hand need room to maneuver to handle cases of forbearance without automatically triggering a default.
On the other hand the quantity of forbearance cases is very limited. In terms of a comparison of the regulatory use vs. implementation costs this means that the definition has to be formed in a way that allows automation with a view to the generation of reporting data. It would at least be necessary to take out complexity radically in order to allow an automated analysis of existing data.
This could be done e.g. by focusing on:

- Large customers only, e.g. by using the large exposures definition
- Introduce a simple overdue definition, e.g. 60 days (see also below)
- Combination with the fact of a change in contracts
- No other criteria

We have to bear in mind that on the one hand the forbearance definition has to leave room vis-à-vis the default-definition and on the other hand the definition has to be distinct from any other cases of a change of contracts in the normal course of business and should not be included in the forbearance-definition. We believe that this issue could be handled by an appropriate overdue-criterion of 60 days.

Question 2

Do you agree with the proposed definitions? Especially, do you agree with the inclusion of trading book exposures under the scope of the non-performing and forbearance definitions? If you believe alternative definitions could lead to similar results in terms of identification and assessment of asset quality issues, please explain them.

Concerning the proposed definitions pls refer to the answer of question 1.

In our opinion, trading book exposures should neither be covered by the forbearance-definitions nor by the non-performing definition.

With regards to the inclusion of trading book exposures in the context of the forbearance-definition we expect a limited validity. An institution does not have a direct business relationship with the issuer of a traded debt instrument and no influence on forbearance practices or non-performing status. Debt instruments of issuers facing financial difficulties can be traded more quickly than the reporting can be processed. Therefore we believe that the questionable actuality of the reported data as well as the diverse nature of the business relationship with debtors of trading and banking book positions could lead to insufficient results.
With regards to the non-performing definition for trading-book assets we see little room for deviation from the impairment-definition. We do not see any added value in a deviation from the existing impairment-definition and an additional reporting in this respect.
Furthermore we refer to the sentence: “Debtor encompasses all the natural and legal entities in a group within the accounting scope of consolidation”. A group of connected customers in retail lending is not viable. We therefore strongly recommend to stick to the large-exposure-definition only.

Question 3
How long will it take you to implement, and collect data on, the definitions of forbearance and non-performing?

Beside our huge concerns as set out in the answers to questions 1 and 2: For a proper implementation we would currently consider a period of 2 years as necessary in any case, due to huge changes in data gathering/training, system changes, validation loops and data checks.

Question 5
Do you agree with the types of forbearance measures covered by the forbearance definition? If not, what other measure(s) would you like to be considered as forbearance?

The differentiation between forbearance and default should be clarified, especially in regard of „distressed restructuring".
We refer to the answers to questions 1 and 2.

Question 6
Do you agree with the following elements of the forbearance definition:

a) the criteria used to distinguish between forbearance and commercial renegotiation?
b) the criteria used to qualify refinancing as forbearance measures?
c) a 30 days past-due threshold met at least once in the three months prior to modification or refinancing, as a safety net criterion to always consider modification or refinancing as forbearance measures?
d) the proposed treatment for exposures with embedded forbearance clauses?

In case you disagree with the EBA proposal on the above-mentioned issues, please explain and provide an alternative to them.

We believe that the verification of the market comparison and the assessment of the feasibility in practice will be limited. A comparison with other market terms appears challenging (e.g. how would the customer be rated by another institution, which conditions could he obtain); It is not realistic to expect lenders to check this; the loan conditions offered by competitors are not openly available in any market. How are cases supposed to be handled where the change in contract is triggered by different issues (e.g. sales initiatives, different product strategy)?
The 30 days past-due threshold is the only quantitative criteria used to define forbearance whereas the other elements are more likely to be seen as principles. What concerns the proposed 30-day period we strongly doubt that this period is appropriate due to the fact that this would simply mean that any action taken after the due date of one installment would have to be treated as a case of forbearance. The 30 DPD -period is too early an indicator and not necessarily indicative of longer term risk performance. The proposed criteria to identify payment difficulty for retail clients is 1x 60DPD in the past 3 months. This helps differentiate risky clients (60DPD) vs. sloppy payers (30DPD) and covers recent difficulty (last 3months). We are of the opinion that only cases where at least two installments are due should be taken into account, which means one time 60 days overdue during the past 90 days.

Question 7

Do you agree with the proposed scope of on- and off-balance sheet exposures to be covered by the definition of forbearance?
N/A

Question 8

Do you agree not all forbearance transactions should be considered as defaulted or impaired?
Generally we would agree that not all forbearance transactions should be considered as defaulted or impaired as proposed in the paper. But this is related to the more general question in relation between the default – impairment – non-performing-definition, see also answer to question 1, where one proposal for a change would be an alignment between the definitions, which would – in turn – then mean also an alignment in the legal consequences.

Question 9

What types of forbearance transactions are likely, according to you, not to lead to the recognition of default or impairment?

Additionally to the examples set out in the context of the answers to question 1:

- In case the exposure is fully collateralized;
- Forbearance with no- or insignificant negative Net Present Value impact;
- Under the thresholds of 60d-period (see answer 1 & 6);
- Under the definition of large exposures (see answer 1).

Question 10

Do you agree with the proposed definitions of debtors and lenders and the scope of application of the forbearance definition (i.e. accounting scope of consolidation)?

What concerns the scope of consolidation we urge EBA to stick to the COREP scope of consolidation. The FINREP-scpoe should – this is a proposal by EBA – in the future be aligned with the COREP-scope. What is simply unacceptable is to link the definitions to the accounting scope of consolidation, i.e. including entities which are neither captured by COREP nor by FINREP. If it is the case that general data of these entities are not needed for regulatory purposes why should specific data be needed? It would drive implementation costs enormously with – again – limited to no additional value added data.

Question 11

Do you agree with the proposed mixed approach (debtor and transaction approaches) for forbearance classification?

The dimensions should in any case be aligned with the default/impairment-definition, in order to avoid implementation costs only to capture another dimension, e.g. debtor-view for NPL, transaction-view for default.

Question 12

Do you agree with the exit criteria for the forbearance classification? In particular:

a) ***what would be your policy to assess whether the debtor has repaid more than an insignificant amount of principal or interests?***

b) ***do you support having a probation period mechanism?***

See also our comments above regarding „insignificant“ and „probation“ (answers to questions 1, 6, 9).

Apart from the fact that a contract can only cease to be forborne and exit forbearance classification when the forbearance contract (with modified payment terms) ends. As long as a forbearance i.e. more favourable payment terms apply the contract should not be considered as a regular performing contract even if the customer performs all its obligations (given that this performance might only be due to lower payment requirements).
Ad lit a:‘No payment’ structures – where debt restructuring results in a payment schedule with no payment required from the customer in any period of time is not allowed. In addition in case of debt restructuring the new monthly installment cannot be less than 25% of the original installment. This requirement does not apply to customers who are already in default.
Ad lit b:The probation period mechanism adds value only if it provides an opportunity for the account to exit from default. Concerning defaulted/forborne exposures we would propose an alternative approach: When a debt restructured customer paid the required installment without delay (meaning never 30+ DPD) for at least 6 months the account can be removed from the default (if default event has been triggered) and considered as performing.
A probation period mechanism goes against the timeline of the forbearance contract concluded with the client: If the bank signs a 3-year forbearance contract with a retail client then even if the client fully performs according to the forbearance contract the contract should be classified as forborne.

Question 13

Do you agree with the proposed approach regarding the inclusion of forborne exposures within the non-performing category? In particular:

a) ***do you agree the generic non-performing criteria allow for proper identification for neither defaulted nor impaired non-performing forborne exposures? Would you prefer to have the stricter approach (all forborne exposures identified as non-performing) implemented instead?***
b) ***do you agree with the proposed consequences of forbearance measures extended to an already non-performing exposure? Especially, are the proposed exit criteria strict enough to prevent any misuse of forbearance measures or would stricter criteria be needed?***

Ad lit a: We do not agree with the implementation of the stricter approach.
Ad lit b: N/A.

Question 14

Do you agree with the following elements of the non-performing exposures definition:

a) ***the use of 90 days past-due threshold to identify exposures as non-performing?***
b) ***the proposed guidance for past-due amounts?***
c) ***the proposed treatment of collateral and especially the proposed valuation methodology for its reporting?***

In case you disagree with the EBA proposals on the above-mentioned issues, please explain and provide an alternative to them.

Pls refer to the answers above, specifically to answer 1.

Question 16
Do you agree with the proposed treatment for derivatives exposures? If not, what criteria would you suggest to enable identification of non-performing derivatives?

N/A

Question 17
Do you agree with the proposed criteria to identify off-balance sheet exposures as non-performing?

N/A

Question 18
Do you agree not to consider exposures subject to incurred but not reported losses as non-performing?

We agree with the proposal not to consider such exposures.

Question 19
Do you agree with the proposed approach regarding the materiality threshold?

We agree with the proposal not to define a specific threshold for the non-performing definition for now and to apply the default-threshold in the meanwhile.

Question 20
Do you agree with the proposed definitions of debtors and lenders and the application of the non-performing exposures definition on an accounting scope of consolidation?

We strongly oppose this approach, pls also refer to answer 10.

Question 21
Do you agree with the proposed approaches (debtor approach for non-retail exposures, and possibility of a transaction approach for retail exposures)? In particular, do you agree with the idea of a threshold for mandatory application of the debtor approach? If so, which ratio methodology would you favor and why?

We would strongly suggest sticking to the default-definition in the CRR which allows implementing a debtor or a transaction in the standardised approach at the moment, and a debtor-only-view in the case of IRB. What should be avoided in any case is an obligation for credit institutions to apply a different view on the basis of these new reporting requirements.

Question 22
Do you agree with the exit criteria from the non-performing category?

We refer to answer 12.

Question 23
Do you agree with the separate monitoring in a specific category of exposures ceasing to be non-performing? Do you think this specific category should be integrated within the performing or the non-performing category?

Performing exposures should be treated as performing exposures no matter their history was. We strongly plead not to oblige banks to additionally report data on performing exposures.

Question 24
Would you favor specific exit or specific separate monitoring criteria for non-performing exposures to which forbearance measures are extended?

See answer 12.

Kindly give our remarks due consideration.

Yours sincerely,

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