|  |  |
| --- | --- |
| To the  European Banking Authority (EBA) | **Division Bank and Insurance**  Austrian Federal Economic Chamber  Wiedner Hauptstraße 63 | P.O. Box 320  1045 Vienna  T +43 (0)5 90 900-DW | F +43 (0)5 90 900-272  E bsbv@wko.at  W http://wko.at/bsbv |

Your ref., Your message of Our ref., person in charge Extension Date

BSBV 115/Dr. Egger 3137 27 September 2019

Dear Sir or Madam,

**EBA Consultation Paper - EBA Guidelines on loan origination and monitoring**

The Division Bank and Insurance of the Austrian Federal Economic Chamber, as legal representative of the entire Austrian banking and insurance industry, appreciates the possibility to comment on the EBA Guidelines on loan origination and monitoring and would like to submit the following position.

**General remarks**

The common aim of both banking industry as well as banking supervisors is to achieve high standards in loan origination and monitoring in order to prevent new NPE. The consultation paper contains numerous details. It has to be noted that

1. most of them shall only be indicative instead of compulsory for giving room to individual internal procedures, and
2. by using the principle of **proportionality** to clearly indicate which requirements shall apply for larger and complex institutions only. General remarks as e.g. such as rec. 14 on page 15 remain too vague, leaving uncertainty.

Also with these guidelines supervisory aspects are mingled with **consumer protection** ones. While it is clear that the legislator should refrain from isolating supervisory requirements from other legal matters, and that interfaces need to be implemented, it is also clear that supervisory authorities are no consumer protection authorities. Should this tendency continue, many authorities need to declare only „partially compliant“ when adopting the guidelines under the „comply-or-explain“ - rule. We also want to point out that the competencies of the authorities of many countries are narrowed to supervisory issues only.

The **scope** of the guidelines should be limited to future exposures only, refraining from taking in existing exposures, as is the case e.g. on page 11 „*where terms are renegotiated*“. Information and structure of existing exposures could strongly deviate from the new standards, making it very cumbersome for institutions to get details afterwards. At least factors such as residual maturities or smaller amounts should be taken into account as thresholds.

**Question 1: What are the respondent’s views on the scope of application of the draft guidelines?**

We welcome the fact that the Guidelines contain an explicit commitment to the principle of proportionality at the beginning (para 12–16 “proportionality and implementation”). According to the Guidelines the principle of proportionality comprises to aspects: the size and complexity of the institution and the size and complexity of the credit facility:

The proportionality principle for lending standards (sections 5, 6, 7 and 8) is proposed to depend on size, nature and complexity of the credit facility. In practice, there are further relevant factors, which influence and are meaningful to differentiate the lending standards, i.e. industries; local accounting standards (in many local markets in the EU different local GAAP standards exist); local enforcement laws and market standards (vary in i.e. developed vs. emerging markets) and not solely the credit facility level. We think that harmonized lending standards can form a common baseline, but must allow for adaptation by individual banks to reflect the underlying accounting standards and legal framework, depending on the industry and customer segments. Therefore, we deem it of utmost importance to clarify the use of the proportionality principle in these guidelines in respect to the national legal and regulatory frameworks, national market characteristics or the risk level. It should be ensured that the proportionality principle allows for such adaptation by individual banks, depending on markets they are active in, in order to reflect the underlying accounting standards and legal framework, depending on the industry and customer segments. In our view, the requirements of the Guidelines do not reflect the principle of proportionality sufficiently.

The aspect of proportionality in relation to the size and complexity of the credit facility should be reflected throughout the Guidelines, with simplified requirements for small and simple credit facilities in the areas of governance, loan origination, valuation, pricing and monitoring procedures.

Furthermore, the various requirements must consider the size of the institutions. Small regional banks do not have the personal or monetary resources to comply with the detailed requirements of the Guidelines. Therefore, the principle of proportionality should be better reflected throughout the Guidelines by implementing lighter requirements and exemptions for small and less-complex credit facilities as well as for small and non-complex institutions.

Paragraph 15 of the Draft Guidelines (page 11) proposes that consumer protection aspects should not be subject to proportionality. In this vein, in particular Section 5, the Guidelines do not exclude small, unsecured loans. We strongly believe that the Guidelines should not apply to consumer loans, which are not covered by Directive 2008/48/EC of the European Parliament and of the Council of 23 April 2008 on credit agreements (CCD). According to Article 2 (2) (c) of the CCD, credit agreements involving a total amount of credit of less than EUR 200 are not covered by the Directive. Therefore, applying the Guidelines to small loans is disproportionate and should be avoided.

With regards to requirements for assessment of borrower´s creditworthiness, we would like to clarify that Austria has regulated the creditworthiness assessment in two different legal acts: § 7 VKrG – *Verbraucherkreditgesetz* (transposing the CCD) and § 9 HIKrG – *Hypothekar- und Immobilienkreditgesetz* (transposing the MCD).

While in § 9 HIKrG (applicable on mortgage loans) bank lending is clearly forbidden if the customer does not fulfil certain criteria, § 7 VKrG (applicable on consumer credits) does not include such a "ban of lending" under certain circumstances yet.

We therefore advocate for refraining from standardisation of assessment of creditworthiness or any ban of lending which goes beyond the CCD: We rely on a system of self-declaration by our customers when it comes to consumer credits. We think that the customer is best suited to provide information on him and that the customer is also the best suited person to assess whether he can handle the credit rates for his consumer credit. A ban of lending for certain cases of consumer credits is clearly something we do not support.

In general, it must be possible to deviate from the proposed requirements of the Guidelines where the loan amount is small and therefore should be excluded from the scope of application of the Guidelines due to the comparable low risk.

Regarding Austria, the FMA (national competent authority) has stipulated the possibility to deviate from credit risk provisions in its minimum standards , e.g.:

• According to paragraph 54 (Risk classification procedures) of the standards, if the low risk level of certain credit transactions or types of transaction does not seem to justify the risk classification procedure, such transactions can be disregarded for that procedure.

• Accordingly, paragraph 79 (Early-warning procedure) stipulates that managers can decide that certain business and credit transactions below certain amounts, which shall both be defined according to their risk level in the internal guidelines, shall be exempted from the procedure for early detection of risks.

In this vein, we advocate for including a deviation possibility in the Guidelines to avoid unproportionate burden for both borrower and lender.

Furthermore, with regards to the proportionality principle it is not mentioned, which level is applicable with regards to Annexes. We understand that these should be applied similarly to section 5, 6, 7 and 8. It is confusing that Annex 1 is explicitly mentioned in section 4 and the guideline stipulates that section 4 (see Pg 21; Rec 35 b) must be set in line with the proportionality principle based on the type, size, nature and complexity of the bank, as described in Title I of EBA Guidelines on internal governance, which we deem as not appropriate for the purpose of application for Annexes in scope of this guideline.

We would welcome if the proposed proportionality principle can be extended as follows “Institutions should apply sections 5, 6, 7 and 8 of these guidelines in a manner that is comprehensive and proportionate to the size, nature, complexity of credit facilities and where relevant, to the risk profile of customer segments" . In addition, for the sake of completeness and transparency in application, we propose to add in Rec. 14 the following: “(…) Institutions should apply sections 5, 6, 7 and 8, including Annex 1 and 2, of these guidelines in a manner that (…)."

For the determination of the scope for exclusion from application, it is not clear if the scope is defined by groups of connected clients or single clients. There might be constellations where the group of connected clients (GCC) is defined as "financial institutions" or "sovereign", whereby its single group members are professionals (i.e. state owned companies). In practice, credit decision on i.e. financial institutions, sovereigns, etc, are taken at the GCC level and based on a different set of criteria and information, as required in this guideline. In order to ensure efficiency and effectiveness of credit decision-making processes, we would deem it as meaningful to include a clarification on the scope for exclusion from application of this guideline.

We would welcome a clarification that the scope of exclusion is to be applied on the level of Group of Connected Clients (i.e. when the first principle is applied in the credit decision process in the sovereign segment). To avoid confusions and future discussions during the regulatory reviews, we propose to include a clarification in the document that if a Group of connected clients is segmented as "financial institutions" or "sovereigns" whereby single group members belong to professionals (i.e. state owned companies), the whole Group of connected clients is to be excluded from the scope of the application of these guidelines.

In addition, there are some banks that serve other purposes than solely a financial success (social banking). Social banking clients cannot be assessed based on full scope of application of this guideline and, because of its importance, social banking should have a special treatment under these guidelines. Otherwise some particularly vulnerable client segments (i.e. people at risk of poverty, socially excluded / marginalized groups, minorities, pensioners or disabled people) as well as social organizations (non-profit sector, NGOs, social enterprises) will be threatened by being further excluded from financial services. Moreover, disproportional regulatory requirements could result in higher loan costs for these vulnerable clients or financial exclusion of these segments.

Furthermore, we would like to include the following remarks:

Page 16 Paragraph 17 – Definitions

* The CRE loan definition is not in line with market standards and our understanding what a commercial real estate is and is viewed to be misleading and partially in contradiction to other requirements set in this guideline (i.e. in 5.2.5 point 125 "institutions should put emphasis on the borrower’s realistic and sustainable future income and future cash flow and not on available collateral"). The phrase "real estate used by the owners of the property for conducting their business" would mean that the financing of production sites for a corporate client will lead to a classification as CRE loan. In addition, the phrase “and secured by a CRE property” eventually might lead to undesired practices, contradictory to strengthening of risk management standards in banking, e.g. to not collateralize a loan to avoid certain undesired regulatory obligations. Moreover, the proposed definition includes social housing, whereas the market practice include social housing in the residential real estate segment (purpose driven) as they might be not income producing.
* The treatment of social housing must also be aligned with the CRR.

We propose to adapt the CRE and CRE loan definitions as follows:

* CRE (…) that is not classified as residential real estate (RRE); and includes social housing.
* A CRE loan means a loan extended (...) or a real estate used by the owners of the property for conducting their business, purpose or activity (or set of such properties), either existing or under construction, and secured by a CRE property (or set of CRE properties).
* Furthermore, currently there is no definition of a project and infrastructure finance included in the guidelines. Due to the fact that there is a dedicated section of guidance to project and infrastructure finance in chapter 5.2.8, we propose to include a dedicated definition to point 17 to avoid potential misinterpretations.
* Residential real estate loan definition is only connected to "a natural person", which indicates that every residential real estate loan taken by professionals is to be included in CRE. We propose to amend the definition of the residential real estate loan included in #17 as follows: "means a loan to a natural person secured by extended for acquiring a residential real estate property"
* A definition on social banking should be added: “Social banking: Providing financial services (incl. Lending) to financially excluded and vulnerable client segments (people at risk of poverty or social exclusion) and social organizations (non-profit sector, non-governmental organizations and social enterprises).”

Finally, the guidelines should only apply to newly originated loans and credit facilities granted after the application date, and not to loans existing before that date, as we explained in our general remarks above. The regular credit review of a deal should not trigger any of the new requirements. Complying with the requirements regarding the collection of information is operationally unachievable for the stock of operations. Hence the sentence “Section 5 also applies to loan agreements where terms are renegotiated or which require specific actions triggered by the regular credit review of the borrower after the application date, even if they have been originated before the application date. ” on page 14 paragraph 10 should be deleted.

**Question 2: Do you see any significant obstacles to the implementation of the guidelines by the application date and if so, what are they?**

We would like to express concerns about the short timeframe proposed for the implementation of the guidelines. According to the draft the Guidelines apply from 30 June 2020 (para 18). This application date is too early. Firstly, the final Guidelines will be published earliest at the beginning of 2020. Therefore, there would not be enough time left for banks to assess their gaps, change their processes and adapt their IT-systems to comply with the guidelines. Secondly, the time pressure is aggravated by the fact that some of the requirements (e.g. consideration of ESG risks, green lending-policy, requirement to perform sensitivity analyses in the field of consumer loans, prohibition of advanced statistical models in the valuation process) are entirely new. Thirdly, recent findings of the credit underwriting exercise show that there is no unionwide harmonized understanding of some of the customer data and financial key figures that must be collected according to the Guidelines. Such a harmonized unionwide understanding is a precondition for the unionwide application of the Guidelines.

Concerning the determination of a sufficient implementation it has to be borne in mind that the institutions - as an example - are granted an 18 months implementation period regarding the new requirements of CRD V while they are transposed into national law. The proposed requirements of the present EBA draft are much more comprehensive and complex with regard to their implementation in the internal processes of the institutions in comparison to the new CRD V requirements. Hence, the implementation period for the banks should be longer than 18 months.

Therefore, we suggest implementing a flexible date of application, according to which the Guidelines would be applicable at least 18 months after their final publication. If the extension is not granted, certain elements of the guidelines would need to be deleted in order to permit timely implementation.

**Questio 3: What are the respondents’ views on whether the requirements set in the draft guidelines are future proof, in particular in relation to technology enabled innovation (Section 4.3.2) and environmental factors and green lending (Section 4.3.3)?**

We would like to reflect on specific requirements in this chapter:

* **Credit risk policies and procedures (Credit Granting criteria)**

**Paragraph 35 – Credit risk policies and procedures**

This requirement would mean that any exception, even the one that does not result in an elevated risk, has to undergo a special process with a different approval authority. This requirement can be applied in the consumer business (mass business), where the borrowers form a homogeneous portfolio. The top segment of professionals is looking for tailor-made lending solutions that meet their individual requirements and therefore cannot be treated by strict rules but must be rather supported with a set of guidelines applied in a modular system.

Therefore the requirement as set in para 35 is not deemed meaningful for professionals, as not every exception to general (group-wide) risk policies immediately results in an elevated risk (especially if policies with lending standards cover diverse portfolios, which require an application of the “one size fits all” rule in order to achieve some degree of harmonization). Strict application of this requirement would result in some form of disproportionality, impairing the efficiency of the underwriting process that is viewed as not necessary for the achievement of the risk and regulatory objectives and may therefore compromise the competitive advantage of the banks. In addition, it could also result in a practice of setting limits and rules by banks that can rarely be breached or overridden, which we view as a contradictory trend to making sure that the bank’s portfolio become less risky and safer, perceived to be the overall aim of all regulatory initiatives.

We propose to amend this requirement to clarify that only exceptions or breaches resulting in an elevated risk need to be approved in a special process with different approval authorities. It is well understood that each bank must explicitly set criteria which may lead to an elevated risk and define an approval process for those. A bank can decide also to not allow for exceptions and breaches of its policies.

According to para 35 (b) of the Guidelines institutions are required to consider at least the items listed in Annex 1, when setting up their credit risk policies/procedures and specifying the credit granting criteria. This implies that institutions must then consider at least all those criteria in the credit granting process. Defining the minimum scope of criteria that must be considered in the credit granting process is not proportional. For smaller and simpler credit facilities the requirement to consider all the items is not appropriate at all. In our opinion the credit granting criteria listed in Annex 1 should provide an exemplary guidance to institutions, which criteria to consider in the credit granting process. Institutions should not be obliged to consider all the in Annex 1 mentioned criteria in each individual case.

This should be explicitly clarified in para 35 (b) of the Guidelines as follows:

“credit granting criteria; while specifying these criteria, institutions should at least consider items referred to in Annex 1 as an exemplary guidance;”.

● **Paragraph 40-42 (Anti-money laundering and counter-terrorist financing policies and procedures)**

We refer to other already existing legal requirements, making this chapter redundant.

* **Paragraph 47 (Credit risk policies and procedures - Technology enabled innovation)**

It is not exactly specified what is considered under "technology-enabled innovation for credit granting purposes", which may lead to different interpretations as the credit granting covers broad spectrum of activities. To avoid misunderstanding and be able to clearly define the scope of application of the regulatory expectations we propose a more detailed description what is considered as "technology-enabled innovation" in the view of this guideline.

Having automated and up-to-date processes is in the interest of any institution. More requirements for this could rather hinder technological developments. Robust and clear processes are a stipulation already set in the due-diligence requirements, and not only limited down to technological processes. This chapter should therefore be removed. Moreover, the chapter is redundant, since technological aspects should be covered with the ICT-guidelines of EBA.

Furthermore:

• **Paragraph 47 c**

There are different tools in place that can be applied when developing a technology enabled innovation in the credit granting. One of those include machine learning, which is often used by the Fintech companies competing for the same clients as banks with quite good results. One aspect of the machine learning is its ability to modify itself while being used, i.e. machine learning is dynamic and does not require human intervention to make certain changes. Therefore, when applying artificial intelligence for the purpose of credit granting, it will not be possible to fully understand and explain the entire underlying model, meaning each component of the model compared to other methodologies already in use for this purpose. However we agree that when applying artificial intelligence technology, banks need to ensure that the models are reproducible and auditable. We also agree that the banks must understand the structure of the artificial intelligence based models and be able to explain it, but due to the nature of the underlying technology, explanation of each component of the model may not be possible to the same degree as this requirement could be interpreted. Therefore, this requirement would hinder banks at applying the artificial intelligence for the innovation and therefore hinder them at keeping pace in terms of technology advancement with the growing competition of e.g. Fintechs.

The nature and specifics of machine learning should be reflected when setting the requirements for application of the technology based innovation in a way that it does not limit its use in the credit granting process. Therefore, we propose to add “to the extent that is proportionate given the purpose, size, complexity, term and potential risk associated with the loan.”

• **Paragraph 47 d**

The requirement to compare the performance & outputs with traditional tools will lead to an inefficient and costly parallel world of two approaches. Since the parallel maintenance and execution of traditional and technology-enabled methods/tools eliminates the benefits of the latter, this requirement should be removed from the Guidelines. The main reason of using technology enabled innovation processes is their better performance compared to traditional methods and tools. Hence, institutions should not be obligated to maintain traditional methods and tools. Furthermore, the requirement would lead to an additional burden for credit institutions which hinder them to keep pace in terms of technology advancement with the growing competition of e.g. Fintechs.

We understand the rational of back testing and comparing the outputs and performance of "technology enabled innovation" but these should be limited to the implementation and transition phase and not be a constant requirement during regular operations.

* **Paragraph 48 to 53 (Credit risk policies and procedures - Green lending)**

Several developments that are taking place could potentially change the current context and therefore complicate the implementation of the guidelines, particularly concerning environmental factors and green lending. The new texts could change the playing field in the upcoming years and result in a misalignment with the guidelines. Hence the implementation of the environmental factors and green lending requirements should be postponed until the final version of the EU Taxonomy is available.

According to the Guidelines (para 49) institutions that originate green credit facilities should develop specific green lending policies and procedures covering the granting and monitoring of such credit facilities. According to our understanding, this means that institutions must implement specific green lending policies and procedures in addition to their general policies and procedures. The requirement to implement completely new lending policies and procedures in relation to green loans is not appropriate, since most aspects of green loans are already covered by general lending policies and procedures. A subchapter within the general lending policies and procedures, applicable to green loans and covering their specificities, should be sufficient from our point of view.

In this regard institutions should be allowed to regulate the granting and monitoring of green credit facilities within their general credit policy by for example dedicating a subchapter of the general policy to green lending – and thereby fulfilling the requirements of para 49.

According to Para 48 of the Guidelines institutions should integrate ESG-risks in their risk management policies, credit policies and procedures. This requirement is not in line with Art 1 Para 29 d CRD V, which mandates EBA to develop a uniform definition of ESG risks, including physical risks and transition risks. This mandate implies that there is no uniform understanding of ESG risks. Since there is no uniform understanding of ESG risks, the requirement to consider those risks in management policies, credit policies and procedures is not appropriate. In addition, EBA has to do a report according to art. 98 para 8 CRD V until 28th of June, 2021 about the possible incorporation of ESG-risks. This report shall comprise a common definition of ESG risks (including physical and transition risks) as well as regulations, procedures, mechanisms and strategies used by institutions for evaluation and coping of ESG-risks, including appropriate methods and instruments for the analysis in regard to financing activities of the institutions. In our view, EBA is anticipating the result of this examination with chapter 4.3.4 of these guidelines.

Therefore, para 49 to 53 should be removed.

* **Paragraph 63 (Credit decision making - independence in credit decision making)**

According to para 63 of the Guidelines institutions should ensure that the principle of independence and minimization of conflict of interest is implemented in the framework for credit decision making. Para 63 (b) contains a list of specific situations, such as the presence of a personal or professional relationship with the borrower, in which an individual should not take part in credit decisions. Since small regional banks provide their services in rural areas, where people are usually familiar with each other, those specific sets of situations, in which an individual cannot take part in a credit decision, especially restricts their business activities.

Therefore, we suggest rather to generally describe the principle of independence in the guidelines, than listing specific situations, in which an individual is biased.

* **Paragraph 65 and 66 (Credit decision making - escalation procedures)**

Para 65 and 66 of the Guidelines contain requirements for exceptions and escalation procedures. According to para 66 institutions should ensure that staff members involved in credit granting and management escalate and report the full nature of exceptions to policies and breaches of limits internally to the appropriate governance body in accordance with the escalation procedure. We are of the view that not each single exception to policies and breach of limits should trigger an escalation procedure, since the execution of an escalation procedure affords personal and organizational resources, which is problematic especially for smaller banks.

For that reason, we suggest to implement a relevance limit for escalation procedures in the case of exceptions to policies and breaches of limits, below which no escalation procedure should be triggered.

* **Paragraph 76g (Credit risk management and internal control frameworks - Second/independent opinion)**

According to para 76 (g) of the Guidelines, institutions should ensure within their credit risk management and control framework that a second/independent opinion is provided in relation to the creditworthiness assessment and credit risk analysis. This requirement is neither proportionate in relation to simple and small credit facilities nor is it proportionate in relation to small regional banks, who cannot afford to provide a second/independent opinion in relation to the creditworthiness assessment and credit risk analysis in every single case.

Therefore, we suggest to include exemptions from the requirement to provide a second/independent opinion in relation to the creditworthiness assessment and credit risk analysis for simple and small credit facilities as well as for small institutions.

Para 76 (g) should be amended as follows:

***“providing independent/second opinion to the creditworthiness assessment and credit risk analysis, where it is appropriate***;”.

* **Paragraph 76g**

According to para 76 (k) of the Guidelines, institutions should ensure within their credit risk management and control framework that stress tests are performed on an aggregate credit portfolio as well as on relevant subportfolios and geographical segments. Especially, for small regional banks it is not feasible to perform regular stress tests, especially in the area of small consumers loans. Small regional banks would neither have the personal nor monetary resources to comply with the requirement to perform regular stress test for all sorts of loans.

Hence, para 76 (k) should be amended as follows:

“performing stress tests on the aggregate credit portfolio as well as on relevant sub-portfolios and geographical segments, where it is appropriate in relation to the size of the credit portfolio;”.

Furthermore, we would like to include the following remarks:

* **Page 67 – 69 – Annex 1**

Regarding the requirements proposed for Commercial real estate lending, at the beginning of the Annex 1 we propose to add “Where appropriate and possible to the extent necessary to reasonably assess the inherent risk”. Additionally, some comments regarding specific criteria in this section:

* 2. the requirements should be separated: a. minimum levels of equity and b. market value
* 7. This point should be removed or supplemented with “where appropriate”.
* 8. Not relevant for social housing as pre-selling requirements do not apply as for other types of CRE; the social housing is sold through the state supported price; tenders for a forward finance loan usually take place 2-3 years before the occupation of the property.

**Question 4: What are the respondents’ views on the requirements for credit risk policies and procedures (Section 4.3)?**

Paragraph 56 requires to use data also from NPE, which is going too far for processes dealing with new loans. This recital should therefore be removed.

**Questions 5 and 6: What are the respondents’ views on the requirements for governance for credit granting and monitoring (Section 4)?**

**What are the respondent’s views on how the guidelines capture the role of the risk management function in credit granting process?**

We would like to reflect on specific requirements in this chapter:

* **Paragraph 59**

For handling corporate clients, setting limits on the number of the credit decisions made under the delegated approval authority is not deemed as a meaningful instrument for controlling and managing risks. Credit approvals have a direct relation to the business volume processed within the institution, where credit turnaround times play a key role in providing a meaningful and timely service to customers. Thus setting limits on the number of credit approvals decided by the delegated authority would significantly impair the capability of the institution to timely process the requests from clients and does not reflect the quality / qualification of the staff that has been given the delegated approval authority and rather supports the decision making strongly relying on the organizational hierarchy. It also interferes with the goals of implementing a risk culture where all employees are expected to take the right decisions for the bank to mitigate risks, and is deemed to contradict the meaningful regulatory expectation that the staff involved in the credit decision processes should be adequately skilled, resourced and experienced (see section 4.1.1, point 21 f).

We would propose to amend this requirement set in # 59 by excluding the quantitative limits of decisions made in delegated approval authorities and to keep only the limitation of the time period for delegated powers, which means in practice that the delegation should be periodically reviewed, i.e. on annual basis, and confirmed.

“(…) on the time period for the delegated ~~powers and the number of delegated approvals~~."

* **Paragraph 60 and 61 (Credit decision making)**

When delegating tasks the number of approvals should not be limited as the number is no risk-related feature, whereas the credit limits and maximum exposures are already sufficient in curtailing the risk. Rec. 60 could be understood to involve risk functions also in daily business, as this is also the case with rec. 61 („when the credit risk management function and head of risk management function are represented in credit committees…“). Such functions shall oversee correct processes and manuals, and shall not be involved in day-to-day transactions.

* **Paragraph 63 (Credit decision making - independence in credit decision making)**

Potential conflicts of interest are determined too far in para 63. To find the correct way in order to prevent or mitigate such conflicts must still be at discretion of the institutions. The principles for conflicts of interest are deemed to be sufficient within the EBA-guidelines on internal governance (EBA/GL/2017/11).

Furthermore, according to para 63 of the Guidelines institutions should ensure that the principle of independence and minimization of conflict of interest is implemented in the framework for credit decision making. Para 63 (b) contains a list of specific situations, such as the presence of a personal or professional relationship with the borrower, in which an individual should not take part in credit decisions. Since small regional banks provide their services in rural areas, where people are usually familiar with each other, those specific sets of situations, in which an individual cannot take part in a credit decision, especially restricts their business activities.

Therefore, we suggest rather to generally describe the principle of independence in the guidelines, than listing specific situations, in which an individual is biased.

* **Paragraph 65 and 66 (Credit decision making - escalation procedures)**

Para 65 and 66 of the Guidelines contain requirements for exceptions and escalation procedures. According to para 66 institutions should ensure that staff members involved in credit granting and management escalate and report the full nature of exceptions to policies and breaches of limits internally to the appropriate governance body in accordance with the escalation procedure. We are of the view that not each single exception to policies and breach of limits should trigger an escalation procedure, since the execution of an escalation procedure affords personal and organizational resources, which is problematic especially for smaller banks.

For that reason, we suggest to implement a relevance limit for escalation procedures in the case of exceptions to policies and breaches of limits, below which no escalation procedure should be triggered.

* **Paragraph 68**

The materiality principle based on the size, nature and complexity of the credit facility (see para 14) is not applicable to section 4, in which the standards for lending to the affiliated parties are included in 4.4.3. Therefore this requirements reads that any lending to affiliated parties, including intra-group, even if the amount is rather minor (starting from €1) should be approved by the entire management body or its empowered committee, even if the amount is minor. Such interpretation of the rule is not practicable. Such lending should be subject to setting up appropriate approval authorities, which including de minimis rules and delegation, where appropriate. We propose the following amendment of para 68 to allow for de minimis rules and delegation:

“Lending affiliated parties, or any material changes of the terms of the existing credit facilities to affiliated parties should be subject to approval of the management body or a committee of the management body empowered to deal with affiliated party lending, where appropriate.”

Moreover, terhe is no definition for „affiliated party“, yet it is important to determine this to e.g. the rules of accounting.

* **Paragraph 70 to 76**

It is important to keep the level of detailled requirements down to the most necessary extent, and that only selected and very important requirements shall become mandatory for best practice, while others shall serve as examples only. Rec. 76 (k) is such an example, demanding stress tests for aggregated and relevant sub-portfolios. The rules for stress tests are already existing in other EBA-guidelines, with no need for duplication. Which data the institution shall take for robust stress testing (e.g. for new products, main product lines, certain subgroups etc.) shall be at the discretion of the institutions and the purpose it is aiming at. Rec. 76 should therefore be understood only as orientation, not as mandatory („*at least*“).

* **Paragraph 76 g (Credit risk management and internal control frameworks - Second/independent opinion)**

According to para 76 (g) of the Guidelines, institutions should ensure within their credit risk management and control framework that a second/independent opinion is provided in relation to the creditworthiness assessment and credit risk analysis. This requirement is neither proportionate in relation to simple and small credit facilities nor is it proportionate in relation to small regional banks, who cannot afford to provide a second/independent opinion in relation to the creditworthiness assessment and credit risk analysis in every single case.

Therefore, we suggest to include exemptions from the requirement to provide a second/independent opinion in relation to the creditworthiness assessment and credit risk analysis for simple and small credit facilities as well as for small institutions.

Para 76 (g) should be amended as follows:

“providing independent/second opinion to the creditworthiness assessment and credit risk analysis, ***where it is appropriate*;**”

According to para 76 (k) of the Guidelines, institutions should ensure within their credit risk management and control framework that stress tests are performed on an aggregate credit portfolio as well as on relevant subportfolios and geographical segments. Especially, for small regional banks it is not feasible to perform regular stress tests, especially in the area of small consumers loans. Small regional banks would neither have the personal nor monetary resources to comply with the requirement to perform regular stress test for all sorts of loans.

**Hence, para 76 (k) should be amended as follows:**

“performing stress tests on the aggregate credit portfolio as well as on relevant sub-portfolios and geographical segments, ***where it is appropriate in relation to the size of the credit portfolio*;**”.

Furthermore, we would like to include the following remarks:

* **Paragraph 82 (Institutions’ remuneration policies and practices)**

Regulation only valid for (retail) staff with decision making competence and receiving a relevant bonus payment:

The draft guidelines of EBA currently define the scope as *'all staff engaged in the credit granting, administration & monitoring process'*. However, credit institutions are actually developing and close to launch a fully digital (automated and pre-approved), end to end process for customers in the Retail loan granting process. Checks and decisions are generally fully automated or centrally decided and the role of the account manager in the front office is in this context, in general, limited to collect informations and documents from the customer. Therefore we request that the scope should be limited to the (retail) **staff with decision making competence** **and receiving a relevant bonus payment.**

* Long term quality only influenceable in the first 12 months:

The long-term quality of a credit beyond 12 months is rather driven by macroeconomic factors and is not really influenceable account managers. Therefore we need a clarification on how "long-term quality of credit" has to be seen in the variable remuneration of the sales staff, considering that whatever risk prevention role the account manager in the front office can perform relates mainly to fraudulent behavior measured by early warning types of KPIs, while the long-term quality of credit is mainly influenced by economic and social developments in the country.

**Question 7: What are the respondents’ views on the requirements for collection of information and documentation for the purposes of creditworthiness assessment (Section 5.1)?**

By far the most challenging requirements are to be found in this chapter and annex 2. The stipulation „should collect and verify…at least“ can only be done for certain products to this extent. Thus, they represent rather the maximum than the minimum of collectable information. There is only a differentiation between consumers and „professionals“, leaving open to guess what this term means. Moreover, a clearer distinction between at least SME and large corporates is missing. Standardised products need less information in general for evaluation than tailor-made ones. The criteria are too rigid for such differentiations. Features such as maturity, amount, new or existing customer could justify different levels of information, also. In total, much more room must be given for institutions which developed specific creditworthiness assessment tools. Those tools and systems will be continuously enhanced, using special algorithms, thus continuosly learning. By forcing those systems to take up certain mandatory features those algorithms could be disturbed. This could be a significant setback for such systems. Instead of demanding these features to be taken up „at least“, it is better to refer to „where relevant and applicable“. Para101 and following recitals are demanding for sensitivity analysis for consumers under various requirements. We want to refer in that respect to our former statement regarding stresstesting. Any other additional requirements can be extremely burdensome, such as those in para 144 to 146.

Moreover, the requirement to make enquiries to third parties could be difficult to handle in practice from an operational and data protection point of view. The obligation to respect Regulation 2018/1725 in efforts to verify information is duly noted and goes without saying. However, the GDPR also requires the consumer to give consent to the bank in order for these enquiries to be made. If this consent is not given and the information provided cannot be verified, banks will not be able to comply with the guidelines. We therefore understand “reasonable” in paragraph 88 to mean that in such a case verification is not required.

* **Paragraph 88 and 89 (Collection of information - Verification and reasonable enquiries)**

Para 88 and 89 of the Guidelines oblige institutions to assess the plausibility of any information and to make reasonable enquiries to the borrower or third parties (employer, public authorities). The requirement to assess the plausibility of any information is not appropriate. From our point of view information of the borrower should only then be verified, if the information is evidently false or there are serious doubts, whether the information is true or not. The borrower is primarily responsible for the verity of the provided information. A part of that, institutions should only then be required to make reasonable enquiries, if those enquiries are necessary to obtain further information. In cases, where institutions and creditors already have enough information (for example in the case of a long-term customer relationship), they should not be required to make reasonable enquiries.

Therefore, para 88 should be amended as follows as it would be in line with the wording in Article 20(1) Directive 2014/17/EU and Article 8(1) Directive 2008/48/EC.

“Institutions and creditors should assess the plausibility of any information and data provided by the borrower and should make any necessary checks to verify the authenticity of information, ***where the information is evidently false or there are serious doubts, whether the information is true****.* When verifying a borrower’s prospect to meet its obligations under the loan agreement, institutions and creditors should make reasonable enquiries to the borrower or third parties (e.g. employer, public authorities, credit register bureau) and take reasonable steps to verify the information and data collected, ***if necessary, to obtain further relevant information (…).”.***

* **Paragraph 92 (Collection of information – Information and data according to Annex 2)**

According to para 92 (para 94 regarding lending to professionals) institutions and creditors should at least consider collecting the information and data as set out in Annex 2. In our view it is inappropriate to collect all the information listed in Annex 2, such as detailed evidence of employment (type, sector, status, duration) and income (annual bonus, commission, overtime), in each single case (even in the case of minor overdrafts or small one-time credit facilities). As already mentioned above concerning Annex 1, Annex 2 should also rather provide an exemplary guidance to institutions.

**This has to be explicitly clarified in the Guidelines.**

Therefore, we suggest the EBA to change the wording of para 92 (para 94) in the following way:

“For the purposes of the collection and verification of information, institutions and creditors should ~~at least~~ consider collecting the information and data as set out in Annex 2 ***as an exemplary guidance*.”**

Furthermore, we would like to include the following remarks:

**Page 70 – 73 – Annex 2**

Diverse specific requirements (commercial real estate lending to professionals, real estate development lending, project and infrastructure lending should be supplemented by “where relevant” as some of the requested information depend on the type of a real estate; i.e. location specific review of supply and demand not relevant for social housing; Information on major tenants per property type, property age and location not relevant rented apartment construction.

* Lending to professional:

3. In case of ring-fenced RE structures the submission of financing statements on a consolidated level is difficult / not possible from the contractual point of view

* Commercial Real Estate Lending to professionals

1. submission of all contracts for particular property is currently not possible, also from the contractual point of view

6. The requirement is partially unclear and creates confusion. We would welcome guidance on what the regulatory expectation is meant with the information on the rationale for the property. Additionally this rules should recognize that the bank internal, independent from the market evaluators/surveyors are considered as acceptable.

* Real Estate development lending

5. submission of all contracts for particular development is currently not possible, also from the contractual point of view

6. The requirement is partially unclear and creates confusion. We would welcome guidance on what the regulatory expectation is meant with the information on the rationale for the property. Additionally this rules should recognize that the bank internal, independent from the market evaluators/surveyors are considered as acceptable.

7. In the real estate development lending states independent qualified and reputable quantity surveyor, whereas point 8 in the project and infrastructure finance states qualified and reputable surveyor.

In general, we propose to add “Where appropriate and possible to the extent necessary to reasonably assess the inherent risk” at the beginning of Annex 2.

In addition, we propose to align requirements to ensure consistency. The rules should recognize that bank internal, independent from the market, evaluators /surveyor should be considered as acceptable.

**Question 8:**

**What are the respondents’ views on the requirements for assessment of borrower’s creditworthiness (Section 5.2)?**

We would like to reflect on specific requirements in this chapter:

* **Paragraph 99 (assessment of borrower’s creditworthiness (p. 36f et seq):**

Ratios:Para 99 contains ratios for the assessment of the creditworthiness. Together with para 100 those ratios imply to reduce the assessment of creditworthiness to such ratios only. In practice those ratios are only one of many steps for the assessment. Para 99 could be introduced by „*Amongst others, institutions should*…“. Second, the ratios shown in the guidelines are of limited value in certain cases (e.g. debt service to income ratio), see for instance professions with irregular income such as free-lancers or seasonal workers. Alternative ratios reflecting such circumstances must be possible as well. The same is true for para 135 for „professional borrowers“. The „capitalisation rate“ (net operating income/market value) is easy to get for listed companies, while the reverse is true for any non-listed company. Moreover, „projection of **all** cost“ as demanded in para 122 and 166 is very difficult and burdensome to receive or to estimate, same with para140. Those items shall not be compulsory.

* **Paragraphs 101, 114 and 121 (Assessment of borrower’s creditworthiness - sensitivity analysis for consumer loans)**

According to para 101 (para 114 regarding other secured lending to consumers, para 121 unsecured lending to consumers) banks should carry out sensitivity analyses reflecting potential negative scenarios in the future when assessing the borrower’s ability to meet obligations under the loan agreement. Generally, it is unusual to perform sensitivity analysis in the field of consumer lending. Performing sensitivity analyses should not be required for small/simple credit facilities and credit facilities of limited duration. The EBA should set up a threshold regarding the loan amount in relation to the balance sheet and duration of credit facilities, below which no sensitivity analysis must be performed. This would better reflect the second aspect of the principle of proportionality in this requirement. A part of that, the Consumer Credit Directive (Directive 2008/48/EC) does not require institutions to perform sensitivity analyses in relation to consumer loans.

Against this background we suggest exemptions from the requirement to perform sensitivity analyses for smaller/less complex credit facilities and credit facilities of limited duration in relation to consumer loans (para 101, 114 and 121). The EBA could set up a threshold for credit facilities in relation to the balance sheet, below which no sensitivity analyses must be performed.

* **Paragraphs 104 / 117**

In respect to the requirement to make reasonable enquiries and take reasonable steps to verify the borrower’s ability to meet obligations (in particular related to self-employed or having seasonal or other irregular income) it is explicitly stated that such verification should include documentation of income, third party verification and tax declaration. In line with our comments on the proportionality principle to explicitly include next to considerations of the credit facilities also some client segments like i.e. social banking, the creditworthiness assessment of the vulnerable clients is based on the ability to prove “regular savings” as “income surrogate” in most cases.

In order to adapt these guideline also for other client segments like social banking, we would propose to explicitly allow the proof of “regular savings” as an adequate “income surrogate” within the creditworthiness assessment. Such proof over a pre-defined period (i.e. one year) can represent a very good surrogate for vulnerable client segments with irregular income.

* **Paragraph 107 (Assessment of borrower’s creditworthiness – retirement age)**

According to para 107 (Lending to consumers relating to residential immovable property) and para 119 (unsecured lending to consumers) if the loan term extends past the borrower’s expected retirement age, the institutions and creditors should take appropriate account of the adequacy of the borrower’s likely income and ability to continue to meet obligations under the loan agreement in retirement. It should be clarified in this regard that institutions should only then be required to take appropriate account of the adequacy of the borrower’s likely income in retirement, if the loan agreement significantly exceeds the retirement age. If – for example - a loan has a duration of twenty years and exceeds the retirement age only by one year, it would be inappropriate to require institutions to consider the borrower’s income in retirement.

A part of that, it must be ensured that the requirement to take appropriate account of the adequacy of the borrower’s likely income in retirement does not restrict lending to elderly people - who are near the retirement age - in a discriminatory way. Even today lending to elderly people and especially lending to pensioners is only allowed under restrictive conditions and therefore shouldn’t be further restricted.

**Hence, para 107 and 119 should be amended as follows:**

“If the loan term extends ***significantly*** past the borrower’s expected retirement age, the institutions and creditors should take appropriate account of the adequacy of the borrower’s likely income and ability to continue to meet obligations under the loan agreement in retirement.”

* **Paragraph 108 (Assessment of borrower’s creditworthiness – increase in income)**

According to para 108 (lending to consumers relating to residential immovable property) and para 120 (unsecured lending to consumers) institutions and creditors should ensure that the borrower’s ability to meet obligations under the loan agreement is not based on the expected significant increase in the borrower’s income unless the documentation provides sufficient evidence. The documentation requirement is insofar problematic, as it prohibits considering borrower’s likely raise of income in the near future, when it cannot be documented. Especially young borrowers, whose raise in income in the future is likely (but not documented), are restricted in taking up a credit. In this regard the Guidelines should allow institutions and creditors to consider the specific circumstances of the individual case.

**Therefore, para 108 and 120 should be amended as follows:**

“…is not based on the expected significant increase in the borrower’s income unless the documentation provides sufficient evidence, ***or the specific circumstances of the individual case indicate a significant increase in the borrower’s income***.”

* **Paragraph 126**

In principle we agree with the list of the requirements that need to be considered when carrying out the creditworthiness assessment. However some aspects listed as part of the considerations of the transaction structure in point g., i.e. leverage level, dividend distribution, capital expenditure, should be taken into account when performing the analysis of the financial position of the borrower as stipulated in a. and as defined in # 132 of these guideline. We propose the following amendment in #126 g:

“g. assess the structure of the transaction including the risk of structural subordination and related terms such as covenants, ~~leverage level, dividend distribution, capital expenditure~~ and, if applicable, third-party guarantees and collateral structure; and”

* **Paragraph 129**

In those cases where all of these risk are explicitly taken over by external credit assessment's (ECA), the additional extensive assessment of these risks by a bank is rather of a limited value added.

We would propose to amend the requirement to be only applicable in full if no ECA coverage is available.

* **Paragraphs 131 et seqq**:

According to para 131 of the Guidelines regarding the analysis of the borrower’s financial position in the field of lending to professionals’ institutions should ensure that the analysis is based on tangible facts and not on an expected significant increase in the borrower’s income unless there is sufficient evidence. According to this requirement it would be impossible to grant a credit to an entrepreneur, who has a convincing new business model, but cannot grant sufficient evidence for his future increase in income.

Against this background we suggest to amend para 131 as follows in order to allow the financing of new business models:

“Institutions should ensure that the analysis of the borrower’s financial position is based on tangible facts and not on an expected significant increase in the borrower’s income unless there is sufficient evidence***, or the specific circumstances of the individual case indicate a significant increase in the borrower’s income.”***

In general, we understand the rationale of the requirements for lending standards setting. Nevertheless banks define KRIs based on their risk appetite, business plans and risk strategy. Defining a list of mandatory KRIs would ignore the risk appetite, risk strategy and management expertise of the bank. Furthermore, the creditworthiness assessment should be based on a sound internal framework, which is comprehensive and creates a clear structure for individual easements based on their characteristics (market, products, industries). Therefore, as an example, the analysis of financial projections cannot be conducted in a "one-size-fits all" approach for all professional clients. A fully harmonized approach would not cover the full spectrum of the heterogeneity of transactions in the market and other relevant legal requirements. Furthermore, in some cases financial projections of the client are not available to the extent required. In particular, stock listed companies are reluctant in principle to explicitly provide financial projections and budgets due to a risk that in case this information is publicly shared, any deviation triggers an ad-hoc announcement to the market. If such information is not provided by the client, we do not view it as meaningful and valuable if the bank itself tries to predict the forward-looking figures for the client. The reliability of such projections is questionable. Therefore in our view, other tools like sensitivity analyses (see para 142-146) of the guideline) or stress scenarios, where relevant, are sufficient to understand the client’s key risks.

We propose to add to the requirement defined in para 132 "where appropriate and/or available". This would consider portfolio- and/or market-specific practices based on the local legal and accounting framework in line with principle of proportionality. As a consequence the ability to apply internal expertise and ensure that certain dynamics are monitored and analyzed regularly, identifying potential adverse developments early on and developing mitigating actions will be retained.

* **Paragraphs 133 / 135**

Complementary to the comments raised for # 131, the requirements defined in #135 read as a mandatory list of a minimum ratios to be considered in the creditworthiness assessment for all professional clients. However some of these ratios do not represent a meaningful metric for a creditworthiness assessment. For example:

* + EBITDA strongly depends on the industry in which the customer operates and is not deemed as an appropriate indicator to compare risk profiles of clients across different industries and within the same client segments (i.e. large corporate);
  + Return on equity and capitalization rate are indicators used by investors who seek for different levels of returns on investment depending on their appetite; in practice the benchmark is missing to assess i.e. which level of the return on equity is appropriate to ensure a long-term sustainability and viability of the company; especially now, when more and more companies abandon a singular focus on the interests of shareholders and instead pledged to “deliver value” to all stakeholders and are expected to manage multiple goals, like i.e. innovation, impact on climate change, and look beyond the single-minded focus of the financial bottom line. Moreover these ratios do not provide a meaningful information of the repayment capacity of the borrower as required in i.a. # 127 and #160, which is a key component for a bank deciding if to provide a financing to the client.

In addition, the following ratios only apply to a certain type of facility:

* + DSCR: only for project finance
  + LTV / LTC: only RE financing

Furthermore, there are some other ratios that allow for better comparability of the client’s risk profile across client segments and therefore have a wider scope of application:

* + Equity ratio as an indicator of a balance sheet (capital) structure

Therefore the listed ratios cannot be understood as a minimum that must be applied when assessing the creditworthiness of any client.

We would like to propose two alternatives:

1) New formulation of this requirement that in our view covers the spirit of the intended regulatory expectation, yet allowing the banks to define their own specific lending standards

“Institutions should use in their assessments of borrower’s creditworthiness financial metrics that cover:

i) Profitability;

ii) Indebtedness or leverage;

iii) Balance sheet (capital) structure;

iv) Cash flow;

v) Working capital;

vi) Repayment capacity;

vii) LTV and LTC for secured lending.”

2) Or the following amendment of # 131 to better aligned with the underlying basis for the proportionality principle defined in # 14:

“Institutions, where relevant, use at least the following financial metrics for the purpose of the creditworthiness assessment (…):

a. debt service coverage ratio;

~~b. EBITDA (earnings before interest, taxes, depreciation, amortisation);~~

c. interest coverage ratio;

d. loan to value ratio (for secured lending);

e. debt to equity ratio or leverage ratio;

f. loan to cost ratio;

g. ~~return on equity;~~ equity ratio

~~h. capitalisation rate (net operating income/market value)~~.

* **Paragraph 142-146**:

Complementary to the comments raised for # 131 et seqq, we consider the requirements defined in this section meaningful only if the client provides the financial projections to the lender. Financial projections are not always provided by every client. As commented above, stock listed companies are reluctant in principle to explicitly provide financial projections and budgets due to a risk that in case this information is publicly shared, any deviation triggers an ad-hoc announcement to the market.

Therefore we deem the requirements set in # 142 ((..) where utilized (…) as meaningful. However the requirements defined in 144, despite the proportionality principle explicitly mentioned in this point, seem to contradict # 142. In addition, the specification set in # 146 seems to be redundant when considering the requirements set in # 142 and 143. Moreover, the events mentioned under #145 are a direct consequence of the events mentioned #146 (e.g. a macroeconomic downturn [#146 a.] triggers a severe decline in borrower’s revenues [which is already covered in #145 a.], etc.)

We propose the following amendment in# 144:

~~Such sensitivity analysis should account for all general and asset class and product type - specific aspects that may have an impact on the creditworthiness of the borrower~~. Sensitivity analysis should be proportionate given the purposes, size, complexity, term and potential risk associated with the loan.

We propose the deletion of para 146

* **Paragraph 163**

This remark applies only if the definition of the CRE remains as currently included in the guideline – also see our comments to Pg 16; #17.

For e.g. social housing „lease length in relation to loan term“ is not a meaningful parameter in our view as although tenants could quit the contract by law, nevertheless due to the market demand, the vacancy rates are negligible. We propose to add "where appropriate" to the point 163.

* **Paragraphs 166b / 177b**

An assessment of all contactors, builders and architects that participate in the construction is currently not possible, also from the contractual point of view therefore we recommend to add; “where relevant and possible” to these requirements. We propose to add “where appropriate and possible to the extent necessary to reasonably assess the inherent risk”.

* **Paragraph 112 (Assessment of borrower’s creditworthiness – other secured lending to consumers)**

According to para 112 in relation to loan agreements secured by immovable property, where the property is in a development phase, institutions are required to assess the borrowers project plan, information on builders, architects etc., projection of all costs, permits and certificates for the development. We are of the view that it is the sole responsibility of the customer to assess the building project and not the responsibility of the bank. It would be exuberant to oblige institutions to assess, which legal norms are applicable in relation to a certain building project in order to assess all necessary permits and certificates.

Therefore, we suggest EBA to change para 112 of the Guidelines. Rather than specifying all the items that must assessed according to lit a – d, it could be required in a more general way that institutions have to assess the feasibility of the project.

* **Paragraph 126 (Assessment of borrower’s creditworthiness – analyses and assessments for loans to professionals)**

According to para 126 banks should at least perform several specific analyses and assessments when carrying out the creditworthiness assessment. The requirement to perform at least the enumerated analyses and assessments is not in line with the principle of proportionality. For example, the requirement in para 126b to analyze the integrity and reputation of the borrower, is not appropriate in relation to small credit facilities. Proportionality should also be reflected in para 132, according to which institutions should at least consider a set of specified aspects when analyzing the financial position of the borrower. For example, the requirement to consider the capacity to meet contractual obligations under possible adverse events should only be applicable, where the loan amount exceeds a certain threshold in relation to the balance sheet.

We suggest implementing exemptions in para 126 and par 132 from the requirements of analyses and assessments that must be conducted in the field of lending to professionals to allow lighter requirements for smaller and less complex credit facilities.

* **Paragraphs 145 and 146 (Assessment of borrower’s creditworthiness - sensitivity analysis for loans to professionals)**

Para 145 and 146 require institutions to consider a specific set of negative events (idiosyncratic events and market events) when performing the sensitivity analysis. The obligation to consider all those negative events would certainly lead to an overestimation of risk and severely restrict credit granting. It should be clarified that institutions are not obligated to consider all those events in each single case. Rather those sets of negative events should provide a guidance to institutions. When performing a sensitivity analysis, instead of being obliged to consider all the events listed in Para 145 lit a – g and 146 lit a – d in each single case, institutions should consider those events as an exemplary guidance. This would be in line with the EBA’s clarification in Para 144, according to which sensitivity analysis should be proportionate given the purpose, size, complexity, term and potential risk associated with the loan.

**Therefore, para 145 and 146 should be amended as follows:**

“Institutions should **~~take into account~~ *consider*** the following idiosyncratic/market events ***as an exemplary guidance:*”**

**Question 9: What are the respondents’ views on the scope of the asset classes and products covered in loan origination procedures (Section 5)?**

We would like to point out that it is in the EBA´s mandate to take into account **ESG factors** and therefore we believe that social lending/social banking should receive special treatment under these Guidelines (like it is the case for e.g. project and infrastructure finance or shipping finance). Social banking has specific characteristics that should be reflected in these Guidelines. We would therefore suggest to introduce an own chapter for Social Banking in Section 5.2.

The section on **social banking** should take the following aspects into account:

There are some banks that serve other purpose than solely a financial success, i.e. improving financial stability and inclusion for people on low income or fostering development and enlarging the impact of social organization. The social banking is an important contributor to the local societies and their financial stability in a long-term. Social banking clients cannot be assessed based on full scope of application of these guidelines. Therefore we would deem it as meaningful either to exclude them from the scope of application or explicitly allow for application of the proportionality principle accordingly. Otherwise some particularly vulnerable client segments (i.e. people at risk of poverty, socially excluded / marginalized groups, minorities, pensioners or disabled people) as well as social organizations (non-profit sector, NGOs, social enterprises) will be threatened by being further excluded from financial services. Moreover, disproportional regulatory requirements could result in higher loan costs for these vulnerable clients or financial exclusion of these segments.

* **Paragraph 133**

In respect to the requirement to assess the borrower’s capacity of profitably in the future (for borrowers who are unable to generate positive profits over time) it shall be pointed out that particular client groups, i.e. social banking clients will not have any profitability by the very nature of their business and applicable law (i.e. non-for-profit organizations, NGOs). This aspect shall be considered when setting the requirements for lending standards in order to ensure that these organizations with high social impact are not excluded from the financial services. Therefore for these client segments with the primary objective of producing positive and measurable effects for society rather than generating profit for its owners, members and shareholders (e.g. non-for-profit organizations, NGOs or Social Enterprises), the borrower’s repayment capacity is not be made in terms of the retained earnings and equity but the ability of such clients to reallocate their spendings. We propose to amend # 133 as follows:

“In cases where the borrower is unable to generate positive profits over time, institutions should also assess the borrower’s capacity of profitability in the future to measure the impact of retained earnings ~~and hence the impact on equity~~, where relevant.

* **Page 43 paragraph 142-146**

In addition, the requirements on a complex sensitivity analysis reflecting potential negative scenarios (combining idiosyncratic and market events) are not deemed meaningful for social banking clients and could result in stricter rejection criteria and exclusion of such clients from the financial services market.

This requirement should be subject to the proportionality principle for social banking clients as proposed above (see Pg 15; #14).

Below please find a drafting suggestion for the separate chapter on social banking, which should be included in the Section *5.2. Assessment of borrower´s creditworthiness*:

***5.2.x Social banking lending***

1. *The creditworthiness assessment for social organizations should consider the aspect of non-profit organization and assess the repayment capacity by the ability to decrease costs, create savings or generate additional income.*
2. *The creditworthiness assessment for other borrower in the segment Social banking should verify the ability and prospect to meet the obligations under the loan agreement. Regular savings (i.e. one year) and future income projections (i.e. related to training, education and qualification programs) can be considered as income surrogate for financially excluded and vulnerable clients.*
3. *Intuitions are encouraged to consider pro-active support for over-indebted clients. Combined debt advisory services and sustainable restructuring of loans should be considered for over indebted clients, in particular in case the non-performing is due to social causes (i.e. family member death, severe sickness / injury leading to inability to work or natural disaster) as alternative approach to enhanced loan selling activities.*
4. *Pricing should consider all costs as listed in 187 in chapter 6., but may neglect profitability targets for this customer segment.*

**Question 10: What are the respondents’ views on the requirements for loan pricing (Section 6)?**

General factors such as risk appetite, viability and sustainability are sufficient for the framework of pricing, as it is a basic economical principle for any enterprise. Details should serve as examples only.

In general, we support EBA´s understanding of a comprehensive framework for the pricing of loans. Giving guideline already in the process of pricing enables an accurate measuring and reporting of financial performance of a loan taking into consideration risk appetite and business strategy.

Furthermore, we share EBAs consideration regarding

a) Cost of capital – based on a given rule cost of capital should be allocated to all products to measure their capital consumption.

b) Cost of funding considering the contractual terms and behavioural assumption

c) Costs to be allocated when pricing a new loan. Entities have to make a decision if loans should bear full costs or only product costs. This view has to be fixed in our general rule book. Depending on the costs applied the ROE target in the pricing tool has to be set.

d) Credit risk costs – the application of Standard risk costs fulfil the request of homogenous risk groups / historical experience and application of respective risk models

e) Direct assignment of costs – it is reasonable to link directly assigned cost component to a deal. Regarding recognition of taxes within a pricing tool it has to be decided if the NPAT view on product level is part of the general steering concept on product level or not.

Measuring profitability of new loans with eg Economic Value Added (EVA) supports entities to monitor the contribution of each single loan to the overall profitability.

Ultimately, each single head of a business line is responsible for earning full costs of his/her business unit in order to achieve his/her EVA/ RoRAC targets. Therefore pricing single deals based on a fair cost allocation is a prerequisite to achieve this overall goal and hence we go hand in hand with EBA´s perception of cost allocation on individual loan level.

A regular – at least quarterly- review of post calculation on single deal level has to be done together with Business. Deals/portfolios which did not perform accordingly have to be reviewed and conclusions have to be incorporated in the pricing tool.

**Question 11: What are the respondents’ views on the requirements for valuation of immovable and movable property collateral (Section 7)?**

We would like to reflect on specific requirements in this chapter:

* **Paragraph 193 (Valuation at origination)**

According to the Guidelines (para 193) institutions should ensure that the property collateral is valued in accordance with applicable international, European and national standards. These standards often follow specific purposes. One standard’s purpose might be to determine the value, because the property is being sold. Another standard’s purpose might be to determine the property value for a probate proceeding. Hence, some of those standards might not be suited to determine the value for credit purposes. Therefore, we are of the view that those standards should not be applicable in the sense of a binding framework, rather they should be applicable as a general non-binding basis.

We suggest amending para 193 in the following way:

“Institutions should ensure that the property collateral is valued in accordance with applicable international, European and national standards, such as European Group of Valuers’ Associations (TEGoVA) European Valuation Standards and the Royal Institute of Chartered Surveyors (RICS) standards.***Those standards should not be binding, rather should they provide a general basis for valuation purposes.****”*

* **Paragraphs 195 and 196 (Valuation at origination)**

According to the Guidelines (para 195) institutions should set up policies and procedures specifying the valuation approaches for immovable property used by the valuer. The Guidelines specify in this regard that the usage of desktop and drive-by valuation approaches is only allowed in the cases of valuing and revaluing immovable property collateral that is of similar design, specifications and characteristics to the ones already valued or re-valued. Since the valuer holds the technical expertise, he should decide on a case by case basis, which valuation approach to use. If according to his expertise a desktop or drive-by valuation approach is the most appropriate one, he should not be restricted by the Guidelines to use such an approach.

The Guidelines must ensure that the valuer is granted enough flexibility to decide on a case by case basis according to his expertise, which valuation approach to use.

According to the Guidelines (para 196) institutions should carry out an assessment in terms of the liquidity and enforceability of the collateral including time to recovery, when the repayment capacity of the borrower significantly deteriorates. Since assessments regarding liquidity and (especially) enforceability require efforts and costs, it would be more efficient to carry out these assessments only when the borrower is already in default. This would correspond with the higher probability that the collateral is being realized when the borrower is in default.

For that grounds para 196 should be amended as follows:

“In the case **~~significant deterioration in the repayment capacity of the borrower~~ *of a default of payment*,** institutions should carry out an assessment in terms of the liquidity and enforceability of the collateral including time to recovery.”

**• Paragraph 197**

Demanding for a pool of external experts for valuation in case the bank wants to use external experts. There are many small and regionally active banks which are unable to provide such pools. The quality of those experts is more important than the sheer number of experts.

* **Paragraphs 201 – 206**

The requirements for **movable property collateral** seem to be extensive for banks with small portion of such collateral; esp. the establishment of panels of external valuators and the implementation of advanced statistic models for each and every type of movables seems disproportional to the economic benefit of such a requirement.

A more conservative valuation of such collateral (by applying bigger haircuts, limitation of valuation to defined types and age of the assets, etc.) may compensate such rules.

We would welcome if the rule is amended to allow for an introduction of materiality thresholds above which an expert valuation is to be mandatory.

* **Paragraph 214**

The requirements for **immovable property collateral** are meaningful however the rotation obligation for internal valuators shall be reconsidered as is not always practicable, especially in small banks that often have only one internal valuator and does not bring additional risk mitigation (the internal valuators have one superior who is responsible for the quality of their performance); rotation of external valuators is deemed meaningful. We propose to delete the rotation of internal valuators from the requirement.

* **Paragraphs 208 and 209 (Monitoring and revaluation)**

The Guidelines require institutions to set up policies and procedures to specify the approach and frequency of monitoring of the value of immovable property collateral (para 208, 209). In our view the current provisions of the CRR (Art 208 para 3 CRR) are specifying the monitoring of immovable property collateral sufficiently. Regarding the frequency of monitoring Art 208 para 3 lit a CRR stipulates that institutions should 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. Where the market is subject to significant changes in conditions, Art 208 requires institutions to carry out more frequent monitoring. Art 208 para 3 lit b CRR specifies the cases, where the review of the property valuation should be performed by a valuer. Hence, no further specification in institution’s policies and procedures is needed.

Requiring institutions to set up policies and procedures in this regard would cause additional administrative costs for institutions, without providing an equivalent benefit, since the CRR already contains provisions regarding the approach and frequency of monitoring of the value of immovable property collateral. Therefore, the requirements of the Guidelines to specify the approach and frequency of monitoring of immovable property collateral in policies and procedures should be removed.

Since the CRR already contains provisions that are specifying the monitoring of immovable property collateral sufficiently, there is no need for institutions to further set up policies and procedures.

Additionally, we would like to point out that the frequency of the obligations of the borrower to provide the institution with information should be aligned with the frequency of monitoring the value of the collateral in order to facilitate the monitoring process with up-to-date information and to make a monitoring consistent with CRR requirements feasible.

The Guidelines refer to LTV as credit granting criterion. As no calculation methodology is being introduced by the Draft Guidelines, we understand every institution can use its own justified and established calculation methodology.

Moreover, we believe that credit amortisation and development of immovable property should be consider for LTV purposes and the monitoring of the value. As a result, institutions should be able to adopt a lower LTV when the credit was substantially amortised (outstanding loan amount is reduced) and/or a building has been partially constructed (the value of the collateral is increased).

In this vein, Basel III: Finalising post-crisis reforms mentions both situations in its paragraph 62, according to which “modifications made to the property that unequivocally increase its value could also be considered in the LTV” and “When calculation the LTV ratio, the loan amount will be reduced as the loan amortises”.

* **Paragraph 214**

We advocate for deleting paragraph 214 as there is no indication that rotating valuers improves the quality of the valuation of collateral. Moreover, it should be noted that some institutions employ and rely on one valuer to operate economically. Mandatory rotation would therefore result in disproportionately high costs for institutions without significant benefits regarding the valuation of the immovable collateral.

In eventu, if the rotation of valuers is maintained against advice the rules should at least be less stringent than the ones for auditors, but could be considered as source for a similar softened provision regarding the rotation of the valuer. Instead of creating new and differing rules, the rotation requirement in Article 17 (1) and (7) of Regulation (EU) No 537/2014 of the European Parliament and of the Council of 16 April 2014 on specific requirements regarding statutory audit of public-interest entities and repealing Commission Decision 2005/909/EC should be considered although the valuation of collateral should be less strictly regulated than statutory audit.

*“1. A public-interest entity shall appoint a statutory auditor or an audit firm for an initial engagement of at least one year. The engagement may be renewed.*

*Neither the initial engagement of a particular statutory auditor or audit firm, nor this in combination with any renewed engagements therewith shall exceed a maximum duration of* ***10 years****.*

*7. The key audit partners responsible for carrying out a statutory audit shall cease their participation in the statutory audit of the audited entity not later than* ***seven years*** *from the date of their appointment. They shall not participate again in the statutory audit of the audited entity before* ***three years*** *have elapsed following that cessation.”*

We therefore suggest requirements applicable to valuers should not be more stringent than respective requirements for auditors as statutory audit is a key aspect for the validation of proper management and creditor protection.

Additionally, maintaining the rotation of valuers must be supplemented by a Cooling-Off-period for excluded valuers which should not exceed two years to make their reappointment possible.

Given the current wording Paragraph 224 seems disproportionate and could be adjusted as follows:

“*Institutions should assess the performance of the* ***external*** *valuers on an ongoing basis, in particular accuracy of valuations provided. As part of such assessments, institutions should also look at the concentration of valuations performed and* ***variable*** *fees paid to specific valuers*.”

* **Paragraph 222**

According to para 222 of the Guidelines any valuer carrying out the valuation task should be professionally competent and should have at least the minimum educational level that meets any national requirements and accepted professional standards for carrying out such valuations. Since internal valuers have a high expertise, but not always have the same educational level that is requested in the accepted professional standards, this requirement would severely restrict the use of internal valuers. We suggest amending para 222 (a) to allow the use of internal valuers in cases, where though they do not have the required educational level, they have a long-term working experience in the field of valuation.

Hence, para 222 (a) should be amended as follows:

“is professionally competent and has at least the minimum educational level that meets any national requirements and accepted professional standards for carrying out such valuations ***or has sufficient working experience in the field of valuation;”***.

* **Monitoring and revaluation (Advanced statistical models)**

On page 81 of the Guidelines the EBA generally prohibits the use of advanced statistical models for the initial valuation of immovable property collateral. In practice, advanced statistical models in the form of “reference-value procedures” have just recently been implemented by institutions on the basis of Art 208 CRR to support the valuer, when carrying out a valuation of immovable property. The use of advanced statistical models is in line with the current state-of-the-art and allows a transparent, high quality and cost-efficient valuation. The EBA itself recognizes that “a strict restriction on the use of those models can hamper the development in this market and the overall progress of the valuation market.” Nevertheless, EBA decides to generally prohibit the use of advanced statistical models, since they may create shortcomings in the risk management. In contrast to the EBA’s argument, the practical use of statistical models shows a qualitative increase regarding valuations.

Therefore, the use of advanced statistical models for the initial valuation of immovable property collateral should not generally be prohibited. Rather should their legitimacy be dependent on the type of advanced statistical model being used by an institution. The EBA could allow the use of advanced methods under additional conditions, such as additional controls of property data, or require evidence on the accuracy of such models. In case this evidence is provided by an institution, EBA could grant the use of advanced statistical models. However, a general prohibition to use advanced statistical models for the initial valuation of immovable property collateral is not differentiated enough, since it does not take into account the accuracy and quality of the different advanced statistical models in use.

**Question 12: What are the respondents’ views on the proposed requirements on monitoring framework (Section 8)?**

We would like to reflect on specific requirements in this chapter:

* **Paragraph 263**

In general we understand and agree with the listed early warning indicators as potentially relevant aspects that should be considered when implementing the EWS framework. However the current wording of this requirement may be understood that all these indicators must be a minimum binding consideration when setting the early warning frameworks. Our comments should be understood under consideration of comments made above for # 14, 131, 132, 135, 142-146 and 163. In our view, the defined requirements do not allow for consideration of the principle of proportionality as needed in this context. In line with the current definition of the principle of proportionality in para 14, the relevant considerations should be based on the size, nature and complexity of the credit facilities. However several of the proposed indicators are not relevant at the credit facility level but need to be considered at the portfolio and/or client level. In addition, several of these indicators strongly depend on the local accounting, market standards and laws, and the extent of the possible data collection (see our comments to the points mentioned above), and therefore their relevancy, strength and correlation to the default may differ across portfolios, industries and clients. For some of the indicators, the data collection my not be possible due to the GDPR and/or information availability constraints. Therefore in our view, similarly to the requirements formulated in other parts of the guideline, relevant proportionality considerations must be properly reflected in relation to the proposed list of the EWS indicators. Moreover the current requirement strongly suggests that the EWS systems should be set up based on several single indicators but in practice there are early warning systems in use that are based on the statistical models and yet fulfill the requirements in regard of the early warning framework. This may strongly influence the efficiency of the early warning (watchlist) process as some manual (human) inputs may be necessary in order to fulfill this expectation, which is not deemed as meaningful and necessary for this purpose.

As a result, we think that the current definition of the regulatory expectations for the early warning framework is unclear and has to be revised in order to avoid confusions.

We propose to add the following proportionality considerations to this requirement defined in this point:

As part of their ongoing monitoring of credit risk institutions should consider the following indicators “to the extent that is proportionate given the relevancy and predictive power of the indicators as well as the potential risk associated with the loan”.

* **Paragraph 255 (Stress testing in monitoring framework)**

According to para 255 of the Guidelines institutions are required to perform stress tests. Those stress tests should be performed at least annually and at least on the aggregate portfolio level. The requirement to perform stress tests on sub-portfolios is dependent on the relevance of the sub-portfolio. When assessing the relevance of a sub-portfolio institutions should take into account materiality and risk level. A part of that, it is our view that the type of counterparty (consumer or professional) should be taken into account as well, since performing stress tests in the consumer loan segment is exuberant.

**Against this background para 255 should be amended as follows:**

“Institutions should conduct stress tests at least on the aggregate credit portfolio and on relevant sub-portfolios, taking into account materiality, ***~~and~~*** risk level ***and the counterparty (whether it is a consumer or a professional).*”**

In addition, we want to point out further issues:

* **SME-Customers**

In many member states, SME is a very important loan segment. The guidelines impose too many details which are either not available for this segment, or not relevant. Many member states encourage SME with various methods, e.g. giving more time for setting up their financial statements. Hence, it has to be clarified that „timely information“ must always be linked to national requirements setting more extensive time horizons.

* **Refering to other guidelines**

The draft often touches topics already regulated in other guidelines, such as stress testing, ICT, internal governance, connected clients, AML and the like. We are of the opinion that this is creating redundancy. It is therefore sufficient only to refer to specific chapters of other guidelines since they should deal with these topics in accomplished way.

* **Single customer view**

It is industry standard also to allow for portfolio-analysis based granting of provisional lines of credit (so called „pre-approved limits“) – in this respect rec. 122ff. would narrow the lending process without taking into account certain industry standards.

* **Details of creditworthiness assessment**

As no difference is done between certain types of products or customer, or in our point of view not sufficiently, items such as „product type-specific metrics“ as in rec. 126 should become mandatory. We have to clearly point out that these metrics are only in use for „specialised lending“ such as project or object finance, but not for plain vanilla products. See also Rec. 135 and 140 in that respect. This example alone shows that the itemisation of the guidelines are going much too far, and are inappropriate for certain loan types. Again, this is not industry standard. The same goes with certain requirements such as multi-year plannning and forecast mentioned in rec. 131 and 142. For SME-customers, it will become very difficult to do this, and the effort will be in no relation to the relatively smaller loans of SME-customers.

In recital 17 of the consultation paper, EBA aims to provide a definition for “Green Lending”.

We advocate for aligning this definition, especially regarding the “environmental criteria” with the legislative work currently under way, in particular the Regulation of the European Parliament and of the Council on disclosures relating to sustainable investments and sustainability risks and amending Directive (EU) 2016/2341 and the Regulation of the European Parliament and of the Council on the establishment of a framework to facilitate sustainable investment and accordingly the work done by the TEG to define technical screening criteria.

A clear reference to the Taxonomy will ensure legal certainty as a definition not in line with the future level 1 definitions would jeopardize the process of developing clear and uniform criteria for what can be defined as “green” in the European Union.

We ask you to give our remarks due consideration.

Yours sincerely,

Dr. Franz Rudorfer

Managing Director

Division Bank and Insurance