By email

EBA Consultation Paper on close correspondence between the value of an institution's covered bonds and the value of the institution's assets relating to the institution's own credit risk

30 August 2013

Dear Sir or Madam,

The Association of Danish Mortgage Banks, the Danish Bankers Association and the Danish Mortgage Banks' Federation appreciate the draft RTS on the close correspondence between the value of an institution's covered bonds and the value of the institution's assets relating to the institution's own credit risk under Article 33 of the CRR (CP/2013/31). The draft RTS fits the Danish case well as it ensures that Article 33 does not unintentionally imply adverse consequences for the specific business model due to the match funding feature of the system.

Specific comments on the RTS

Article 2, paragraph 1, litra a of the draft regulation states that the fair value of the assets underlying the covered bond issued by the institution is at all times equal to the fair value of the covered bonds. We suggest that it is reformulated as "Any changes in the fair value of the covered bonds issued by the institution will at all times result in equal changes in the fair value of the assets underlying the covered bonds".

The fair value of the assets (mortgage loans) underlying the covered bonds is not at all times equal to the fair value of the covered bonds. The mortgage loans' fair value is determined as the fair value of the covered bonds reduced by reserves to cover changes in expected credit losses on the mortgage loans (the fair value of the credit risk on the borrowers). Hence, the institution's own funds will not be affected by changes in own credit risk, as any changes in fair value of the covered bonds will be equally reflected in fair value of the mortgage loans. This notwithstanding, own funds is reduced by the reserves to cover the expected credit losses on the mortgage loans.

Article 2, paragraph 1, litra b of the draft regulation states that a close correspondence requires that “the mortgage loan underlying the covered bond issued by the institutions to finance the loan may be at any time redeemed by the borrower by buying back the covered bond at market or nominal value (exercise of the delivery option).”

For technical reasons we suggest that the term “by the borrower” be omitted from the text.

The borrower always has the option to redeem the mortgage loan. In some cases, however, mortgage loans are distributed through an intermediary bank. When redeeming the mortgage loan, the covered bonds will be bought by the borrower *or* the intermediary bank and delivered to the issuer. Thus, it is not always technically the borrower that buys back the covered bonds in the market when redeeming the loan.

We thank you for taking our comments into account.

Yours sincerely

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