POLISH BANK ASSOCIATION

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Warsaw, 29 December 2014

European Banking Authority

Subject: Polish Bank Association response to EBA consultation on Draft Guidelines on payment commitments under Directive 2014/49/EU on deposit guarantee schemes (EBA/CP/2014/27)

Dear Sirs,

Polish Bank Association welcomes the opportunity to comment the EBA consultation paper related to Draft Guidelines on payment commitments under Directive 2014/49/EU on deposit guarantee schemes. In our opinion this document can have big impact on ability of deposit guarantee schemes in short time to meet their requirements and on the use of payment commitments as the tool of fund raising. The possibility indicated in text of Directive 2014/49/EU should be correctly applied for bigger capacity of deposit guarantee schemes. In Poland we are in such confortable situation that we can consider use of this tool only as additional source for the DGS financing because our DGS has already the available financial means higher than the minimum target level indicated in Article 10 of Directive. We are convinced it would be reasonable to construct system of payment commitments which will encourage and mobilize all stakeholders to raise the amount of financial means available for deposit guarantee schemes.

General Comments

Objective of Payment Commitments

The banking sector in Poland expresses its view that it was not the intention of policy makers in Europe to treat payment commitments for DGS purpose in the same way as cash funded payments in DGS.

We strongly ask the EBA to reconsider its position on the neutrality of choice pointed in paragraph 30 and to pass from current approach to a pragmatic prudential treatment of capital and leverage requirements for payment commitments, which will allow banks to continue to support the EU economy while also moving to a more robust deposit guarantee framework.

The inclusion of payment commitments in the Directive 2014/49/EU was intended to facilitate the achievement of the future target level of funding, particularly for those Member States which until now have not operated on a pre-funded basis. Recital 34 of the Directive states that "It should be possible for the available financial means of DGSs to include cash, deposits, payment commitments and low-risk assets, which can be liquidated within a short period of time." The inclusion of collateralised commitments allows Deposit Guarantee Schemes to have immediate access to funding when needed, without the need for banks to cash fund entirely upfront. Therefore we believe strongly that there should be regulatory advantages for payment commitments in order to mobilize this form of money collection for DGS purpose.

Prudential and Accounting Treatment of Payment Commitments

The prudential requirements for payment commitments, as all capital requirements, start with the accounting. The requirement that the commitment must be paid "upon simple and unconditional request of the DGS" will result in the recognition of a liability and an expense to P&L under IFRS. As a result there will be an immediate negative impact of payment commitments on level of CET1. This approach is consistent with the treatment of cash funded payments and therefore meets the principle of neutrality expressed in proposed paragraph 30 of Guidelines. However, it will not serve the purpose of strengthening the financial capacity of DGS.

In our opinion the treatment of all payment commitments, in all jurisdictions and whatever it is used for (Resolution fund or Deposit Guarantee Scheme fund), should be consistent, but different in comparison to that of cash payments. We recommend to provide a specific treatment for payment commitments in order to remove the burden which can be obstacle to development of this funding. The payment commitments should be treated as off balance sheet, with an appropriate capital and leverage treatment. In area of capital treatment risk weight under the standardised approach should be 20%, because DGS can be treated in the same way as entities belonging to public finance.

Treatment of Collateral

Overall we find the proposed collateral requirements (e.g. limits on concentration, currency, changes of collateral etc.) too restrictive as they would increase complexity for collateral management. We recommend to align collateral requirements under the DGS with common generally accepted marketable securities or with other collateral requirements, e.g. included in HQLA definitions for LCR purpose. A common framework will be more practical for consistent implementation of different regulation by banks without any risk for safety of DGS stability and credibility.

Part 4 Delivery of collateral by the collateral provider to the DGS

On paragraph 14, it is difficult for us to agree with the concept that the Financial Collateral Directive should be applied for payment commitments' purpose. We have to have in mind that all banks, also small local banks, have to participate in DGS funding and also all these banks will be obliged to create payment commitments is such decision will be made. These small local banks do not deliver sophisticated services to their clients and are not the active participants of transaction on own account on capital market. This is the reason why they have no experience in area of financial collaterals and do not have participate in Security Financial Collateral Arrangement. To have the access to this Arrangement only for payment commitments' purpose is to complicate task. In Poland the majority of the small banks can not provide services on capital market, they do not have its current account in the central bank (they have indirect access only via associating bank) and part of them do not have until now the securities which can be used as collaterals in transaction with the central bank. We are in favor to create a system as simple as possible. In our opinion we should not generate additional cost of managing the system of payment commitments in banks and raise cost of supervision of the system by the national DGSs.

Part 6 Criteria for eligibility and management of collateral

On paragraph 19 we would like to express our view that the criteria for eligibility of collateral should be same as designated by relevant central bank to accept securities as collateral for REPO transaction. It this the best solution and therefore no other criteria have to be defined. The access to the central bank operation will be the guarantee that the securities being payment commitments can be quickly transformed in cash and money be delivered to DGS.

On paragraph 20 in connection with our response to paragraph 19 we are not in favour to give the power to DGS to add new criteria concerning collateral quality such as exposure limits, diversification etc. We have to remember that only limited category of assets can be used in operations with the central banks and they are treated as the low-risk assets.

Expressing our position concerning paragraph 20 we can not treat the proposed paragraph 21 as necessary.

Part 7 Haircut

On paragraph 23 we agree that haircuts should be applied to collateral for payment commitments. The haircut are also used in bank operations with the central bank and the same approach should be applied for purpose of payment commitments.

On paragraph 24 we disagree to define haircut details in the Guidelines. As we expressed above, the principles of haircut should be those defined by the respective central bank for REPO transactions, respectively collateralized lending from the central bank to banks.

On paragraph 25 we disagree with this definition based on expected losses and expected time lapse to sale of the assets. Furthermore expected losses on collateral are not an expertise of DGSs. The expected time lapse of sale of assets is not relevant, as it is not a given that for the financing of a DGS payout the assets will be sold, as this will potentially have negative impact on asset markets. Rather financing will be done through REPO through the market or through the respective central bank.

On paragraph 27 we disagree with the idea of haircut-adjusted market value of the low-risk assets. We are convinced that the market value is important factor when payment commitments have to be delivered to DGS. But we have to remember that the haircuts for payment commitments are applied and not every change in market value should be not the reason to change the level of collaterals delivered by bank. These method will cause the high costs of collateral management for the DGS purpose.

The requirement to deliver additional collaterals goes very far. It should be very rare situation when the DGS demands the banks to supply the additional assets. We have to remember that the collaterals are low-risk assets and the DGS should not use the possibility to replace the payment commitments' collateral with other type of assets or with cash.

Answer to specific questions

1. Apart from the admissibility requirements suggested in the present guidelines, which objective criteria do you think could be applied, notably in order to determine the overall amount of payments to be accepted in a given year, or to be applied to individual banks applying for the option?

We first wish to point out that the present guidelines are at odds with the wording of the Directive. Article 10 (3) of the Directive states that payment commitments should not exceed 30% of the total amount of available financial means. This means that the 30% limit refers to the entire banking sector and not to an individual credit institution. We prefer the approach adopted in this respect by the Directive, because the changes in balance sheets of individual banks in each year can change drastically their level of payment commitments in following years.

When it comes to spreading payment commitments over time, we are in favour of a flexible approach on this point as well. It is clear that in 2024 payment commitments should not make up more than 30% of the available financial means. During the target level build-up phase, DGSs will, however, be allowed to both overshoot and undercut the limit. This is because, for one thing, the starting position differs in many countries. Member States which have in the past already paid a large proportion of contributions in the form of payment commitments may need a transitional period to reduce this proportion in an economically acceptable manner. Furthermore, payment commitments can be used to support anticyclical assessment of contributions. Assuming that reporting of payment commitments would be possible without any impact on the P&L statement, these could namely be used more heavily in economically trickier phases of bank business development, reducing on the same time level of cash funding. In this way, the size of contributions could be kept stable but the strain on balance sheets reduced.

Summing up, we therefore believe that it would be advisable to give DGSs discretion in distributing payment commitments with regard to their level and when they are used. At the same time, DGSs should be obligated to define at the start of the target level build-up phase clear-cut criteria for the use and distribution of payment commitments.

2. Do you agree with these provisions to be included in Payment Commitment Arrangements? Do you think other provisions should be provided?

We believe that the requirements for the elements of payment commitment arrangements are, in principle, appropriate. However, we have fundamental reservations about the unconditional right for a DGS to claim payments on demand. Such power to call up funds on an ad hoc basis is unnecessary and has a highly adverse effect on the accounting treatment for DGS members. An unconditional right to claim payments upon simple and unconditional demand would unquestionably lead to accounting affecting the P&L statement. In our opinion it is reasonable to clarify that a payment by a credit institution can only be required following a pre-defined default event introducing contingency upon a future determinable event for which the likelihood of its occurrence can be assessed. As each payment commitment is secured by securities the proposed amendment would not result in an increase of funding risk for the DGS and will still be in line with the Directive's objectives.

We have also to remember that payment commitments are collateralized, so cash coming from them can be generally delivered for DGS purpose within 2 working days from the call day. This should be included in analyzes concerning the right to claim payment.

3. Do you agree that a credit institution should pay in cash the Payment Commitment Amount, when its obligation becomes due, within 2 working days at the latest?

Looking only at the availability period, a period of up to 2 days for honouring payment commitments appears reasonable.

4. Do you agree with the option left to the DGS to enter into a Security Financial Collateral Arrangement (full ownership remains with the credit institution) or a Title Transfer Financial Collateral Arrangement (full transfer of ownership)?

The provisions of Part 3 of the EBA guidelines should be revised to clarify that the existence of a payment commitments is linked to the risk a credit institution contributes to the respective DGS. In other words, in the situation when the bank does not continue its deposit activity or joins the other DGS the payment commitment should terminate without settlement.

This example shows that the termination of a payment commitment appears to be justifiable. Where a credit institutions switches to other DGS, this leads to a reduced exposure for the earlier DGS and an increased exposure for the new one. Hence, the new DGS has to increase funding to cover the higher exposure either by means of increased general contributions or a specific contribution on the new member. However, having to settle the payment commitment with the old DGS as well leads to a double payment for the same exposure in this situation.

In this context, the requirement to annually amend or supplement payment commitments should be clarified so that it also allows for adjustment to reflect the actual current exposure contribution of a

credit institution. In other words, the payment commitments can be reduced or even terminated given that this is in line with the contribution of the credit institution to the overall exposure of the DGS.

5. Do you think other requirements about the choice of the custodians should be provided under these guidelines?

We agree that the default or insolvency of a custodian should not lead to losses to the credit institution or to the DGS. We agree that there should be full segregation in the books of the custodian.

6. Do you agree on the requirements suggested for the eligibility of collateral? Would you suggest other limits on concentration in exposures?

We do not agree with stated criteria on the eligibility of collateral. Criteria should be those defined by the central bank for REPO transactions. We have expressed broader our position in this area in general comments.

7. Do you consider appropriate not to consider the currency of issuance when determining whether debt instruments are correlated to an event of DGS pay-out, be it inside or outside the euro area?

We believe that is not appropriate to consider the currency of issuance when determining whether debt instruments are correlated to an event of DGS pay-out. As we expressed above we are convinced that the Guidelines should refer to the haircuts adopted by the respective central bank for purpose of transaction with banks.

8. Do you consider that the proposed wording correctly applies the concept of proportionality, or whether some limits to concentration should be envisaged also for smaller, locally operating banks?

Above we expressed our serious confusion concerning the application of the proposed system in small local banks as in bigger ones.

9. Do you agree with the criteria on the eligibility of the collateral provided in this Part 6? Do you think other requirements should be provided in these guidelines on this issue?

Please refer to our general comments in this area.

10. Do you agree with the criteria on the haircut provided in this Part 7? Do you think there are other requirements which should be provided under these guidelines about this issue?

Please refer to the general comments section. We can repeat that we are not convinced to give the DGS power to establish the haircuts. We can use in this area the central bank standards.

11. Do you agree with the prudential approach suggested? Would you suggest further details on the methodology to be applied, and if so which ones?

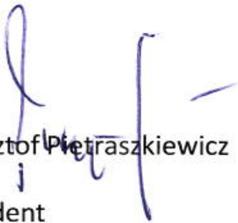
We expressed in the general comments our problem concerning the neutrality of cash payments and payments commitments. We understand however the general idea that the regulator does not want to create any advantage for payment commitments in comparison to cash payments.

We agree with the provision of paragraph concerning the different treatment of payment commitments for accounting purpose.

We agree also with the suggested approach but not on the last part of the last sentence of paragraph 33. We agree that the competent authorities should assess within the supervisory review and evaluation process, the risks to which the capital and liquidity positions of the credit institution would be exposed should the DGS called upon it to pay the commitment. The prudential treatment should reflect this assessment. The treatment should reflect the probability that the DGS is called upon and the potential losses stemming from a DGS intervention.

As a measure of simplification, we propose the payment commitments to be risk-weighted as an unrated institution under the standardized approach (i.e. 100%) with a credit conversion factor of 20%.

Yours faithfully,



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