POSITION PAPER

ESBG response to the EBA consultation on draft Guidelines on payment commitments under Directive 2014/49/EU on deposit guarantee schemes

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Dear Sir/Madam,

Thank you for the opportunity to comment on the EBA consultation on draft *Guidelines on payment commitments under Directive 2014/49/EU on deposit guarantee schemes*.

General comment:

The requirement that the commitments must be paid 'upon simple and unconditional request of the DGS' in page 12 of EBA´s consultation paper will result in the recognition of a liability and an expense to P&L under IFRS, especially under IFRIC 21. In addition, while the DGS wording seems to result in the requirement to account for the whole amount up front, it is understood that some national transposition will allow recognition of the annual contributions on day 1 each year. It would be of great assistance to all stakeholders if the EBA clarifies in its guidelines that payment commitments on eligible deposits are due on a specified date each year. This would avoid having to book the entire provision upfront, a situation which it is our understanding was not intended anyway.

In practical terms this would mean that for each contribution period, the annual contribution due by each institution that carries out its activity on 1 January would be determined for the contribution period on the basis of the annual target level of the DGS. The potential accounting and prudential impacts of an up-front recognition of this liability would be extremely harmful for our members and we therefore ask EBA to publicly support the progressive recognition of the liability.

In addition, coherence should be guaranteed between different legislative acts. We refer specifically to the accounting treatment of the payments commitments to the DGS which should be in line with the payment commitments to the Single resolution fund.

***Question 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?**

ESBG believes that the complexity, the risk management and sophistication of the different banks and banking groups should be taken into consideration. In this connection, the EBA could consider reducing the DGS contributions of banks that apply traditional bank business models with conservative loan to deposit ratios as their likelihood of default is smaller compared to others. Market share and concentration should be taken into consideration too.

<u>Question 3:</u> Do you agree that a credit institution should pay in cash the Payment Commitment Amount, when its obligations becomes due, within 2 working days at the latest?

ESBG would like to underline that a structured approach to Payment Commitments is needed, through the exchange of data and ideas between the financial institution and the national DGS Management. It would be commendable to establish a payment schedule between the concerned parties in order to ensure that the liquidity position of the financial institutions is not negatively impacted. The financial institution would thus be able to plan for its financial commitments whilst the DGS would know what funds are due and plan for their investment. ESBG are therefore in favour of a structured dialogue between financial institutions and the DGS Management.

<u>Question 4:</u> 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)?

ESBG recommends going for the first option, technically known as a Security Financial Collateral Arrangement, where the full ownership remains with the credit institution. Any interest earned on the pledged security should also remain with the credit institution.

<u>Question 5:</u> Do you think other requirements about the choice of the custodians should be provided under these guidelines?

ESBG asks the EBA to come up with clearer guidelines that will apply universally within the European Union, thereby removing the possibility of different interpretations emerging. The concept of the Single Rule Book should also apply in this area.

<u>Question 6:</u> Do you agree on the requirements suggested for the eligibility of collateral? Would you suggest other limits on concentration in exposures?

The eligibility of collateral and the concentration of exposures need to be carefully managed. In this regard, ESBG believes that a detailed impact assessment needs to take place where different scenarios must be analysed. The diversification of risk by having prime rated collateral pledged with the DGSs is certainly very positive, but one needs to look at the current market situation and the realities on the ground. The European banking industry is seeing an influx of new costly regulations and directives that are going to further strengthen the sector. Due to this influx of regulations, one needs to be very careful that the flow of funds to the economy remains in place without slowing down the access to finance. The recast DGSs and the contributions to the Single Resolution Fund are going to cost millions of euros in terms of cash contributions and payment commitments.

Any changes in the investment policies and collateral management policies need to be carefully phased in over a number of years. The European banking industry cannot afford more costly regulatory changes introduced overnight. The banking sector's human and financial resources are currently strained and cannot afford further large changes. Pausing the regulatory process to allow the industry to adopt the current influx of regulatory requirements could be considered.

It is a known fact that some Member States have a high concentration of Government securities as collateral. Any change of policies need to be carefully managed. The investment opportunities in some Member States are limited. The question of the rating of sovereign securities and papers needs to be very carefully handled as the impacts would be significant across the board. In short, ESBG emphasises that the European decision-makers should not send the wrong messages in respect of the rating and value of sovereign securities.

***Question 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?**

In ESBG's opinion, currency and foreign exchange issues need to be carefully factored into the equation as the impacts can be significant. Any changes need to be phased in over a period of time. It would be recommendable that a detailed impact assessment takes placed in coordination with the ECB and the Member States' competent authorities or national central banks. A percentage change can result in a larger or smaller drain on the DGSs.

***Question 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?**

The Directive on DGSs is certainly one of the most expensive EU directives that run into millions of euros. Therefore, a clear impact assessment, by looking at different scenarios, needs to take place before certain answers can be given and before certain decisions are made. It would be wise not to rush into the conclusion of just changing a couple of words or changing concentration risk criteria. More information on the ground needs to be collected.

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

The recommendations in part 6 concerning the criteria for eligibility and management of collateral are good from a theoretical point of view, but are in practice capable of causing problems for some Member States' banks that have a high market share and limited investment opportunities. Financial institutions that have a significant market share in some Member States are the main financiers of their national Government securities and contributors to their national DGS. It is a fact that the DGSs in some Member States mostly invest in their national Government securities and they (that is the financial institutions) offer their national Government securities as promissory commitments. In this context, ESBG believes that any changes in portfolio management need to be faced over time, not to lead to any panic sale of Government securities and causing a sudden fall in the value of their national Government securities. Every step needs to be carefully analysed as the situations change from one EU Member State to another.

<u>Question 11</u>: Do you agree with the prudential approach suggested? Would you suggest further details on the methodology to be applied, and if so which ones?

The cash contributions and collateral payment commitments vary from one EU Member State to another. For instance, in a particular EU Member State the cash contribution is currently 20 per cent whilst the collateral payment commitment is 80 per cent. Within this scenario and other similar scenarios, ESBG recommends that a progressive phased approach is taken with regards to increasing the cash contribution and reducing the collateral commitments over the period from 2016 to 2024. This phased approach would certainly be in line with the recast DGS Directive and would not undermine the financial stability of these Member States.

Indeed, a gradual approach is very important to ESBG's mind since cash contributions are immediately debited to the Profit and Loss Account whilst pledged amounts are treated differently. Regarding the collateral commitments, it would be a good idea if banks place a note in their financial statements disclosing the value of the assets which have been pledged in favour of the DGSs. Moreover, for regulatory purposes, the value of the pledged assets is deducted from own funds, and the note in the financial statements detailing the composition of the banks' capital-adequacy ratio should clearly illustrate this too.

About WSBI-ESBG (European Savings and Retail Banking Group)

ESBG brings together savings and retail banks of the European Union and European Economic Area that believe in a common identity for European policies. ESBG members support the development of a single market for Europe that adheres to the principle of subsidiarity, whereby the European Union only acts when individual Member States cannot sufficiently do so. They believe that pluralism and diversity in the European banking sector safeguard the market against shocks that arise from time to time, whether caused by internal or external forces. Members seek to defend the European social and economic model that combines economic growth with high living standards and good working conditions. To these ends, ESBG members come together to agree on and promote common positions on relevant matters of a regulatory or supervisory nature.

ESBG members represent one of the largest European retail banking networks, comprising of approximately one-third of the retail banking market in Europe, with total assets of over €7,300 billion, non-bank deposits of €3,480 billion and non-bank loans of €3,950 billion (31 December 2012).

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