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EFBS position paper concerning the consultation of EBA on draft guidelines on methods for calculating contributions to Deposit Guarantee Schemes (CP 2014/35)

The European Federation of Building Societies (EFBS) welcomes the opportunity to participate in the consultation of the European Banking Authority (EBA) on draft guidelines on methods for calculating contributions to Deposit Guarantee Schemes.

The EFBS is an association of credit institutions and organizations that assist in and support the financing of home ownership. Its purpose is to encourage the idea of acquiring home ownership in a Europe that is converging, both politically and economically. The members of the EFBS are specialized credit institutions, which operate in eight EU Member States (D, AT, RO, SLO, HR, CZ, LUX, and H). These provide for specific Bausparkassen Acts which regulate the so called Bauspar business. In compliance with the strict legal provisions the Bausparkassen offer contractual saving schemes to their clients and grant them loans which need to be secured by mortgages. They are not allowed to practice other kinds of banking businesses. They may invest their excess liquidity in gilt-edged products, such as state bonds of EU member states. Bausparkassen are specifically supervised by national banking supervisors. Interests on savings and credits in the context of Bausparen are fixed in advance and are usually lower than the market interest rate. In most Members States, Bausparkassen need to get a specific approval by the banking supervisor before offering new tariffs and products on the relevant market. Within this product testing Bausparkassen need to prove the sustainability of their products and tariffs. Furthermore, the low risk business model of Bausparkassen is determined by the strict legal provisions for the Bauspar business and for the reduced possibilities of financial investment. This is why, during the financial crisis, Bausparkassen have proved to be particularly resistant.

In this context we suggest to EBA to take low risk business models more appropriately into account in the EBA-guidelines.

Concerning the questions 4 and 5 we therefore would like to reply in the following way:

Q4: Considering the need for sufficient risk differentiation and consistency across the EU, do you agree on the minimum risk interval (75%-150%) proposed in these Guidelines?

EFBS welcomes the intention of EBA to adopt the initial idea of the European Commission to introduce in its draft guidelines a risk interval for the contributions to deposit guarantee schemes. The draft guidelines of EBA provide in paragraph 42 that credit institutions shall not pay less than 75% or more than 150% of the amount which a credit institution with an average risk would have to contribute. At the same time EBA explains that the lower limit should range between 50 % and 75 % whereas it should be possible to extend the higher limit to 200 %.

However, the EFBS would prefer that the guidelines of EBA indicate more clearly that a risk-weighted approach applies to the minimum risk interval which reflects the common political approach of the

EU institutions during the legislative procedure for the directive 2014/49/EU of 16 April 2014 on deposit guarantee schemes as a legal basis for the activity of EBA.

In the legislative procedure the European Commission suggested in article 11 (1) of the proposal for a directive on Deposit Guarantee Schemes that credit institutions should not pay less than 75% or more than 200% of the amount that a bank with an average risk would have to contribute to the deposit guarantee scheme. Within the first reading the Council opted for a risk interval of 50% – 200% and the European Parliament decided for a risk interval of 75% – 250%.

Such a wide risk interval would accommodate in a better way the variety of the banking sector with its different risks. It would allow specifically low-risk business models such as the Bausparkassen to pay a contribution to the deposit guarantee scheme which corresponds to their risk. To this effect, Article 13 (1) of the directive 2014/49/EU on deposit guarantee schemes provides that lower contribution rates apply to those credit institutions which, even by law, are obliged to operate under a particularly low-risk business model.

The business activities of Bausparkassen are strictly regulated. They accept savings deposits of their clients which are then used exclusively for the granting of housing loans secured with a mortgage in accordance with principles established in law. By law, Bausparkassen are not allowed to practice other business activities. The debt incurred under a loan takes the form of a mortgage which is secured against a property. This form of credit business offers a very high level of security: it involves thorough creditworthiness and valuation standards, encumbrance on property which is registered in the land register, and a high track record of repayment by customers. These factors guarantee that for many decades, the default ratio for loans guaranteed by Bausparkassen has been much lower even than those of universal banks with comparatively low-risk business models. The laws governing Bausparkassen thus contain very extensive and specific safeguards to protect deposits and loans for building purposes in this closed system of saving and financing. In Germany this safeguard is called the technical security reserve fund (“Fonds zur baupartechnischen Absicherung”).

Low-risk businesses are regularly calculated with tight margins. Bausparkassen do not have the opportunity to generate additional revenue in more risky business sectors with higher return on assets such as investment banking; this is because they are special credit institutions which are only authorized to operate in the housing finance sector. By law, customer deposits which cannot be used for the granting of Bauspar loans must be invested in particularly low-risk areas (i.e. not shares). This inevitably reduces the returns on these investments.

Unlike other sectors of lending, Bausparkassen cannot pass on all or part of the additional financial burdens associated with deposit guarantee schemes to their customers through revised interest rates conditions. This is because their financial products, i.e. savings contracts for building purposes, must be approved by the relevant supervisory authority prior to their market launch. This includes the terms and conditions of savings deposits and loans for building purposes, which are contractually established on a long-term basis.

Many Member States already take account of these specific characteristics of Bausparkassen in the calculation of contributions to the existing deposit guarantee schemes. For this reason this best practice should also serve for future calculation of contributions.

Against this background a minimum risk interval between 50 % and 250 % would be more appropriate than 75 % – 150 % as proposed by EBA.

Therefore, EFBS advocates a **clarification** that the minimum risk interval should always be **50 % to 250 %**. A wider interval could be established, as suggested by EBA, upon justification.

Q5: Do you agree with the core risk indicators proposed in these Guidelines? If not, please specify your reasons and suggest alternative indicators that can be applied to institutions in all Member States. Do you foresee any unintended consequences that could stem from the suggested indicators?

The core indicators which shall be used for the calculation seem to have been mainly designed for universal banks. They do not take sufficiently account of the particularities of low-risk business structures of deposit-based specialized credit institutions such as Bausparkassen, for example.

a. Leverage Ratio

EFBS rejects as a core indicator for the calculation of the contributions to Deposit Guarantee Schemes the leverage ratio. EFBS is of the opinion that the leverage ratio would not properly reflect the risk profile of Bausparkassen with their low-risk but high-volume business model. The leverage ratio is totally unsuitable because it is by nature lower for banks with low-risk businesses and therefore causes the default risk of the bank to appear higher.

b. Return on assets

EFBS does also not support the return on asset ratio (RoA) as a core indicator.

According to our opinion, the use of the return on asset ratio as one of the core indicators will disadvantage Bausparkassen or groups of institutions with a similar low risk profile compared to credit institutions with high risk profiles.

The return on asset ratio (RoA) reflects the profitability of the capital investments of credit institutions during a distinct period. However, this ratio does not show the risks which the credit institutions have taken in order to produce the annual profit. Therefore, the return on asset ratio is totally unsuitable to demonstrate the risk profile of a credit institution. This ratio will disadvantage Bausparkassen or institutional groups with a similar low risk profile vis-à-vis institutions fraught with risk.