

## **Eurofinas & Leaseurope response to the European Banking Authority's Draft Guidelines on loan origination and monitoring**

### **Introductory observations**

Eurofinas, the voice of consumer credit providers at European level and Leaseurope, the European Federation representing the leasing and automotive rental industries in Europe welcome the opportunity to respond to the Consultation Paper on Draft Guidelines on loan origination and monitoring.

Eurofinas and Leaseurope support the work of the European Banking Authority (EBA) in addressing the issue of non-performing loans, where measures taken are effective in achieving a coherent approach and common application of consumer protection across the relevant EU markets.

As a Federation, Eurofinas represents consumer credit providers across the EU as well as, depending on market characteristics and structure of Member Associations, first and second charge mortgage lenders.

Leaseurope represents leasing solutions providers offering a wide range of services ranging from financial leases to full service operational leases.

Eurofinas and Leaseurope share the EBA's view on the importance of the correct application of creditworthiness assessments. The Consumer Credit Directive (CCD) is the gold standard for regulation of consumer credit in the European Union. Its provisions set out the obligation to assess the creditworthiness of consumers who wish to borrow on the basis of sufficient information. Eurofinas and Leaseurope fully support this obligation and view it as a prerequisite for successful and responsible lending.

However, as further outlined in our response, we believe the Guidelines do not provide for the relevant flexibility required, but setting out actions that lenders "should" undertake "as a minimum", without providing sufficient consideration and safeguards to enable an proportionate approach by lenders and supervisors.

Such flexibility is especially relevant in light of the proposed scope of the Guidelines, which encompasses a wide range of products of varying risk and complexity. Therefore, whilst we welcome the initiative, we believe that further steps should be considered by the EBA to ensure the proportionate and effective application of the Guidelines, and to respect the relevant level 1 measures. We believe the general lack of proportionality would ultimately lead to a less diverse and competitive lending landscape, since many smaller players who provide lending would be disproportionately burdened if required to comply with the provisions set out in the Guidelines.

The specific selection and use of data points should remain within the remit of lenders. Based on their core expertise and local market knowledge, they can ensure the suitability of processes and data taking into account the specificities of the product and transaction value alongside the context of local market and regulatory characteristics. It should also be ensured that the sources used to provide this information are relevant and proportionate for the situation in question.

The full and coherent application of the proportionality principle should also apply in relation to consumer lending-related activities and the creditworthiness assessment, while at the same time fully respecting consumer protection obligations as set out by the relevant legislation.

Moreover, we believe that further steps could be considered by the EBA to take due account of the current developments in relation to the CCD as well as the Mortgage Credit Directive (MCD) which are both under current evaluation by the European Commission. To ensure a coherent and effective approach, we believe that the CCD and the MCD should be finalised well in advance of the full application of the Guidelines.

#### **Q1. What are the respondents' views on the scope of application of the draft guidelines?**

Whilst the material scope of the proposed Guidelines is clear, it raises a number of questions in relation to the general, practical applicability between different product categories as well as the suitability to cover both small value and high-value transactions, which have a varying degree of risk and complexity. In relation to relatively low-value transactions such as consumer credit characterised by short maturities, and especially those which have originated at the point-of-sell or online, the guidance appears to be overly prescriptive and non-practical in relation to the relevant risk, and far-reaching in light of the requirements set out in the relevant product legislation. Such products/business models already rely heavily upon automated and technology-driven tools for which the accurate control of the relevant risks have been demonstrated.

To apply the draft Guidelines in full to the described activities will inevitably lead to a fewer lenders offering their products in key consumer and SME segments, resulting in reduced competition, diminished access for consumers and ultimately greater financial exclusion. As such, it would undermine the European Commission's economic strategic goals without achieving additional consumer benefit.

In addition, we would like to raise the potential concern for the full compliance between the proposed Guidelines and the General Data Protection Regulation's (GDPR) demand that the processed data is adequate, relevant and limited to what is necessary in relation to the purposes for which they are processed in line with the data minimisation principle.

While the Guidelines set out best practices for specific lending activities, to ensure the relevant flexibility and general use, we believe that the proportionality principle should be applied to all aspects of the proposed guidance/activities, respecting the relevant level 1 legislation and the consumer protection rights and obligations enlistered therein. We would welcome further clarification of the application of proportionality based on size, type, nature, complexity and risk profile in relation to creditworthiness assessment of consumers in relation to unsecured lending.

In this context we would also like to highlight the distinction made between the creditworthiness assessment as set out in the CCD and the MCD. We believe that the final Guidelines should clearly take this into consideration, taking due account of the difference between the activities and their connected risk. Extending the additional obligations under the MCD to CCD related activities would not be in line with the legislators' clearly expressed intent. The separation was clearly outlined in the MCD, in light of the considerably higher amounts, timeframes and risks involved in relation to a mortgage loan vis-à-vis a consumer credit loan.

With regards to leasing, the guidelines explicitly state that certain requirements extend to leasing solutions. Within the wider European regulatory framework, leasing is already regarded as a "low risk" form of lending resulting from its link to the asset. As such, different types of leases are already subject to adjusted proportionate requirements. Furthermore, it should be recognised that, depending on the type of lease, many Member States do not classify leases as a financial service product at all, and as such many leases would fall outside of the scope of these guidelines.

Finally, the proposed scope also overlaps with existing regulations, including some which are currently under formal evaluations by the European Commission, not least the CCD and the MCD, and initiatives

that are currently subject to on-going work. This risks effectively pre-empting the legislative process, leading to inconsistent approaches and definitions, as well as ineffective implementation.

**Q2. Do you see any significant obstacles to the implementation of the guidelines by the application date and if so, what are they?**

The extensive nature of the draft Guidelines would require significant adjustments to business operations and IT systems, as well as to relevant staff training activities. Notably it would require the adaptation of systems for granting of contracts, and in order to meet documentation requirements

In addition, with the European Commission's formal evaluations of the CCD and MCD underway, this may provide for revisions of relevant legislation under the co-decision process. This should be taken into account in the finalisation of the draft Guidelines to allow for the effective and coherent implementation, and to avoid asymmetry between the various initiatives.

In view of these considerations, the proposed deadline of application, i.e. 30 June 2020, will not provide the industry with enough time to adapt its internal systems and processes in a comprehensive and coherent manner.

We therefore propose that the deadline of application is pushed back 18-24 months following the finalisation of the Guidelines. We also propose that aspects subject to potential review are removed from the guidance in the situation of an earlier date of application.

The Guidelines should not apply before 31 December 2021 at the earliest.

**Q3. 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 appreciate the EBA's outlook and continuous work on the enabling and application of new financial technology. However, in parts, the proposed Guidelines provide for a high degree of prescription and we fear that this may create issues in the practical application of the Guidelines and the promoted uptake of new innovative technologies as well as the effective utilisation of digital distribution channels. They also challenge already existing technology-enabled procedures, e.g. in relation to consumer credit in the online environment or the application of scoring models. Indeed, consumer credit and leasing activities have already been largely automated by providers which has proved to be effective.

There is a real risk that the strict application of the Guidelines would result in the benefits and improvements in efficiency brought about by the use of technology in risk management being undermined, and in their practical applicability being threatened. This is particularly problematic for lower value loans and small-ticket leasing, which often relies on automated processes and the use of technology, which aids accessibility and consumer affordability and for smaller SMEs and professionals. Moreover, the resources that would be required to facilitate this strict interpretation would be wholly disproportionate when weighed against the negligible potential benefit that would be brought about by such change.

Another important consideration is the importance of coherence with other relevant initiatives at both EU and international level (e.g. the European Commission's High-Level Expert group on AI and its policy recommendations). A lack of coherence will likely lead to issues, for example, in the application of advanced and more automated decision-making processes, in the utilisation of artificial intelligence, as well as in relation to various emerging Open Banking initiatives.

In order to take due account of the new digital reality and consumers' expectations for how services and products are provided, we believe it is important to ensure that any foreseen requirements are adapted to the digital world. This is particularly important in the context of the collection of information. Consumers today expect their providers to simplify such procedures and provide a smooth user experience. As a consequence, the use of standardised approximations of relevant living costs may be preferable to the collection of vast amounts of -potentially irrelevant- information. The key focus should always be to enable consumers to make the best informed choice possible using data metrics that are tailored to the situation under review.

On green lending, whilst we welcome the EBA's focus on the importance of green lending and sustainability, we want to stress the importance of avoiding confusion and interpretation between the Taxonomy on Sustainable Finance and other initiatives.

The requirements included in paragraph 49 of the Guidelines provide for a relevant responsibility for lenders in relation to high-value lending. However, in relation to consumer credit loans or leasing solutions, e.g. connected to electric vehicles or energy saving solutions for domestic use, we believe that the requirements do not provide for a proportionate approach.

**Q4. What are the respondents' views on the requirements for credit risk policies and procedures (Section 4.3)?**

While suitable for certain lending activities, we generally believe that the requirements as set out do not provide for due consideration of the type of loan in question, i.e. amount, duration, counterparty, distribution channel, risk and/or complexity, etc. Indeed, the criteria listed in Annex 1 may not be applicable in certain situations.

In the leasing sector for example, a "business to business" approach is often adopted where the leasing company (which may be a bank or a supervised financial intermediary) signs commercial agreements directly with the dealer. This always occurs after a proper evaluation of the financial and economic situation of the lessee.

In relation to the implementation of technology-driven credit granting solutions, we believe it would be relevant to further specify the nature and steps of analysis to compare outputs based on more traditional methods. Paragraph 47.d., providing for comparable verification and regular monitoring of credit decisions, appears to be a "step backwards" for innovation in the consumer credit space.

**Q6. What are the respondent's views on how the guidelines capture the role of the risk management function in credit granting process?**

A "one-size-fits-all" approach to the role of risk management, as set out in the draft Guidelines, is not appropriate. The level of risk undertaken when granting credit varies widely between organisations, depending on the size of the organisation and the nature of the financial activity being undertaken within it. In light of this, the requirements set out in paragraph 82 could be regarded as overly burdensome and prescriptive, since they require precise criteria for variable remuneration policies of the staff in charge of credit granting.

A second level check on the credit risk assessment would already be undertaken according to the principle established by the Guidelines and is also currently undertaken in the context of small ticket leasing with vendor programmes. In these programmes a "four eyes" principle is applied to grant an independent judgment of credit risk. The risk management function evaluates the risk assessment and the commercial function takes the final decision on the basis on both client creditworthiness and business evaluations.

**Q7. What are the respondents' views on the requirements for collection of information and documentation for the purposes of creditworthiness assessment (Section 5.1)?**

As stated above, in order to ensure the relevant flexibility and enable the effective application of the Guidelines to the many product groups and activities covered, we want to stress the importance of the full application of the proportionality principle in relation to consumer-related creditworthiness assessments, i.e. allowing for due consideration of the type, the value, the risk profile and the complexity of the individual transaction in the process.

The CCD, supported by the European Court of Justice's case-law (e.g. Case C-449/13), provides lending institutions with a degree of flexibility to take due consideration of the specific credit application at hand and the operational reality in the various markets, e.g. relating to the availability of data, etc. The Court recognised that the CCD "affords the creditor a margin of discretion for the purposes of determining whether or not the information at its disposal is sufficient to demonstrate the consumer's creditworthiness and whether it is necessary to check that information against other evidence".

There is a real danger that this flexibility would be undermined by the Guidelines in their current form. The application of the proportionality principle needs to be clearly emphasised, particularly for consumer-related activities, and further enabled by amending the wording of Guidelines in relation to the data to be assessed, removing overly commanding words such as “at least” and replace them with more appropriate terminology such as “if relevant”, which is more adequate within the context of non-binding guidance.

Whilst the information listed under Annex 2 of the Guidelines may be relevant for the assessment of an applicant borrower’s creditworthiness, this may not hold true for all lending activities and situations. In line with the relevant provisions of the CCD and supporting case law, discretion should remain with the lender based on their expertise. The collection of the full set of data, as prescribed in the Guidelines, would create major practical and technical challenges for large-scale consumer credit operations. Moreover, it would also raise concerns as to the necessity of the data and, thus, the institution’s adherence to relevant data protection obligations. It should be further clarified that the annexes set out possible indicators, and not strict requirements.

A very diverse landscape exists across Europe for credit bureaus as well as other public registers, with regards to their existence, organisation and the type of data held. Indeed, in some Member States it is legally not possible to establish a credit register with both positive and negative credit data. Some obligations provide for substantial operational challenges beyond the control of lending operators. For example, point 11 of Annex 2 calls for the use of “data from credit registers or credit information bureaus, covering at least the information on financial liabilities and arrears in payment”. Indeed, while the use of external sources can be encouraged, one cannot rule out that in certain circumstances this is simply not relevant or necessary. Additionally, it may not necessarily be compatible with the available resources for lenders.

We would also like to stress the principle of responsible borrowing, echoed in existing legislation, and that the customer should remain responsible for information that he/she is best placed to provide, e.g. on their tax status or whether the borrower has loans with other providers. We should reiterate that not all credit registers in Europe, whether held by public or commercial entities, provide this information.

The concept of a single customer view is generally favoured in the draft Guidelines. However, we want to stress that, although information may be collected by the institutions during the loan origination process, or existing within a company group, this data might not be necessarily be available on a “main” system. In practice, there may be a series of different single customer views within different entities of a group; but not centrally available without significant adjustments to relevant IT systems.

In this context, we also want to raise practical issues with verification of information with third parties. From both a legal and practical view point, it raises a number of potential issues, partially due to the general reluctance for processing of personal data for fear of potential non-compliance with the GDPR, irrespective of whether this fear is well-founded. In practical terms, this processing may prove difficult to carry out. In our view, the EBA’s reference to “reasonable” in paragraph 88 should be interpreted to acknowledge this potential situation and, thus, not forcing such a demand when not possible, e.g. when the data subject does not provide his / her consent for such processing.

We also want to suggest that the final guidance, in relation to consumer credit origination, provide for an opportunity to base the assessment by the means of statistic tools, e.g. rating and scorecard, to evaluate the ability of a borrower to meet its obligations, and, thus, limit the obligation to collect and verify information to situations over a defined threshold, etc. As outlined above, this would be in line with consumers’ expectations in the digital world as well as well-established and proven models in place.

Paragraph 90 of the Guidelines sets out a requirement for the documentation of relevant processes. We seek further clarification as to the precise obligations. A duty for the lender to systematically and fully collect and archive documents testifying the borrower’s declared information for low-value lending activities, e.g. consumer credit at the point of sale or online, would not be compatible with a proportionate approach and also surpass the CCD’s requirements.

We welcome the clarification in paragraph 91 that information on the purpose on the loan should be collected and verified “where relevant for the type of product”. For the majority of consumer credit products, e.g. revolving credit, personal loans, overdraft, etc., the gathering and processing of such data is not necessary where the granted amounts are not significantly above the average. Moreover, it is also unclear how such information would be clearly processed, valued and acted upon by a lender.

**Q8. What are the respondents’ views on the requirements for assessment of borrower’s creditworthiness (Section 5.2)?**

As outlined above, the information and documentation mandated to be assessed in the creditworthiness assessment go further than the requirements set out by both the CCD and MCD, as well as established case-law. The current framework already provides for a strong focus on responsible lending.

We want to stress the need for the necessary flexibility to ensure a general applicability of the Guidelines to all product categories, not least commonly distributed consumer credit products. The ability to adjust processes and steps with the characteristics of the individual situation and with the varying local operational realities, is necessary for a proportionate approach and is reflected in the relevant product legislation.

As previously outlined, the legislator provided for a degree of flexibility in the CCD in light of the varying market conditions and operational challenges differing across the Member States, further confirmed by Court of Justice, and for the differentiation of the creditworthiness assessments to be carried under the CCD and the MCD, respectively.

The current EBA guidance on the assessment to be carried out in relation to a mortgage loan (GL/2015/11) also calls for reasonable steps and enquiries to be fulfilled in order to assess an applicant borrower’s income or ability to meet the financial obligations arising from a loan agreement.

The proposed Guidelines do however provide for a considerably more static approach, with prescriptive and detailed steps to be taken, beyond the requirements set out in both the CCD and the MCD. Given that lending practices vary depending on the type of product as well as local market characteristics, we believe that the Guidelines need to appropriately reflect this and be phrased in a sufficiently broad and flexible manner.

A strict and formalised application of the listed metrics and parameters would require an overhaul of lenders’ existing scoring models, despite the fact that their efficiency and relevance have been proven. The Guidelines would ultimately entail a strict and rigid framework that would be disproportionate in relation to the risk reduction that could be expected, increasing costs and diminishing access to appropriate credit products.

The proposed focus of sensitivity analyses risks to lead to onerous, uncertain and intrusive measures. Such projections are difficult to carry out with any great certainty and may require far-reaching and intrusive processing to assess matter beyond than fairly uniform, i.e. likely retirement age/effect, etc. This raise concerns as to the practical application, but also for the interplay with the GDPR. For low value loans of short durations, such measures are generally considered unnecessary and would raise compliance issues. We believe that the requirement should be eliminated or be further clarified as to extent, and as a “best effort” measure, which, in line with the proportionality principle, may not be relevant for all credit activities.

It is our view, the assessment of an applicant borrower’s creditworthiness should provide for the relevant flexibility taking due account of the type, value, risk and complexity. With the proposed wide scope of the Guidelines, this is of even greater importance, to ensure the practical application across the various product categories covered, and to avoid unnecessarily burdensome requirements exceeding the complexity and risk of the relevant loan products.

**Q9. What are the respondents’ views on the scope of the asset classes and products covered in loan origination procedures (Section 5)?**

As set out above, we believe that the requirements set out in Section 5 of the Guidelines should be subject to the application of the proportionality principle, taking account of the characteristics of the

specific activities. Such a uniform approach for the processes relating to loan origination is not practical nor proportionate. Consumer credit, and potentially leasing covered, activities are generally characterised by the large-scale distribution of small value/tickets of typically short durations, and cannot be compared to other, more complex lending activities.

**Q10. What are the respondents' views on the requirements for loan pricing (Section 6)?**

The parameters listed in paragraphs 186-190 of the Guidelines carry relevance both in relation to prudential and consumer protection measures. However, serving very different purposes, they are not suitable to form part of a "one-size-fits-all" approach. A strict requirement to consider the parameters on individual loan basis, would lead to pricing standardisation and commoditisation, thereby reducing the incentive to innovate. It effectively risks raising the cost of lending and increasing financial exclusion. Ultimately it would be very close to the parameters of what can be done in prudential supervision, and risks encroaching on the commercial judgement of operators. To achieve a more proportionate wording, we suggest to replace "inter alia" in paragraph 187 by "for example"

**Q11. What are the respondents' views on the requirements for valuation of immovable and movable property collateral (Section 7)?**

The requirements for the valuation of immovable and moveable property collateral, as set out in the Guidelines, are not compatible with the business model of many leasing firms. Leasing firms' employees are typically responsible for ascertaining the value of assets they fund, and this is particularly prominent in certain types of leasing. For example, this is very common practice in vendor financing, where finance is provided by equipment manufacturers, who are best placed to assess the value based on their market expertise. The requirements set out in section 7, requiring the party responsible for valuing the asset to be independent from the party financing the asset, would not allow for this practice to continue. In addition, performing immovable property full appraisals for revaluation purposes as set out in paragraph 213 instead of the customary drive-by appraisal paired with desk research, would significantly increase the appraisals' annual cost, and likely delay delivery time.

**Q12. What are the respondent's views on the requirements on monitoring framework (Section 8)?**

The processes set out by the Guidelines are elaborate and advanced, and of particular relevance in relation to complex and high-value lending activities. However, in relation to typical consumer credit activities they appear disproportionate and unjustified. Clarifications on a proportionate application of the requirements would be necessary.

Additionally, as previously outlined, a comprehensive financial view of a borrower is not always possible, e.g. due to internal IT limitations and/or varying access to, and content of, relevant credit databases.

**Eurofinas and Leaseurope are entered into the European Transparency Register of Interest Representatives with IDs n° 83211441580-56 and n° 430010622057-05**