

**European Central Bank**

Brussels, 15 November 2016

*Re: Eurofinas/Leaseurope response to the ECB consultation on non-performing loans*

Dear Sir/Madam,

Eurofinas and Leaseurope, the voices of consumer credit and leasing at European level, welcome the opportunity to respond to the European Central Bank's (ECB) consultation on the draft guidance to banks on non-performing loans (NPLs).

The membership of our two Federations covers institutions specialised in one or more of the following activities:

- Lending to consumers, for instance via personal loans, credit cards or lease/hire purchase agreements
- Leasing to businesses of all asset types, including machinery and industrial equipment, ICT and others assets
- Motor finance, granted to individuals or businesses, either in the form of loans or leases

The consumer credit, asset finance and leasing markets have developed to respond to business investment and consumption needs as well as to accompany the development of local industrial production and distribution. The types of institutions represented by the Federations include specialised banks, bank-owned subsidiaries, the financing arms of manufacturers as well as other, independently-owned institutions.

In 2015, the leasing firms represented through **Leaseurope's membership helped European businesses invest in assets worth more than 315 billion EUR**, reaching 755 billion EUR of outstandings at the end of the year<sup>1</sup>. Leasing is used by more European SMEs than any individual category of traditional bank lending taken altogether (around 40% of all European SMEs make use of leasing which is more than any other individual form of lending)<sup>2</sup> and is also extremely popular amongst larger corporates<sup>3</sup>. It is also extremely useful to support the public sector (e.g. leasing to schools, hospitals, etc.).

In 2015, consumer credit providers that are members of **Eurofinas helped support European consumption by making more than 423 billion EUR goods, services, home improvements and private vehicles available to individuals**, reaching 981 billion EUR of outstandings at the end of the year<sup>4</sup>. Consumer lending is procyclical and is highly positively correlated with households' disposable income<sup>5</sup>. By providing access to finance to individuals and households, consumer credit supports the social and economic well-being of millions of consumers across Europe.

### **1. Preliminary observations**

We take note of the ECB's objective to reduce NPLs in banks' balance sheets. We understand the background of this initiative and support the development of clear standards in this field. In this context, we welcome the release of the ECB's draft guidance and stocktake of national practices which we believe are a very useful work basis.

The application scope of the proposed guidance document is large and its operational implications are important as it will not only apply to significant institutions active across multiple jurisdictions but also to firms with various structural / organisational characteristics. As highlighted by the ECB at the 7 November 2016 hearing, it is crucial to ensure sufficient flexibility in the implementation of these standards.

It is important to ensure that the strategy and methodology adopted are indeed consistent with firms' technical abilities and resources. It should obviously take into account the various processes in place and build on firms' experiences. This is particularly relevant for smaller-sized subsidiary firms which may be subject to specific scrutiny. In that spirit, we believe that supervisory teams should ensure a clear allocation of tasks and responsibilities within groups for NPLs treatment. Work at entity level should be restricted to what is strictly necessary.

---

<sup>1</sup> Leaseurope 2015 Annual Statistical Enquiry

<sup>2</sup> Oxford Economics, *The Use of Leasing Amongst European SMEs*, 2015; Eurostat, *Access to Finance Statistics*, 2011; International Finance Corporation *Leasing in Development: Guidelines for Emerging Economies*, 2009; European Investment Fund *The importance of leasing for SME finance*, 2012; and UEAPME, *UEAPME Newsflash*, 2012

<sup>3</sup> European Central Bank, *Survey on the Access to Finance of Small and Medium-Sized Enterprises in the Euro Area*, April 2013

<sup>4</sup> Eurofinas 2015 Annual Statistical Enquiry

<sup>5</sup> Eurofinas, *Consumer Credit, Helping European Households Finance their Tomorrow*, 2015

We also believe the guidance document should be fully consistent with the European Banking Authority's work on default.

## **2. NPL strategy**

### *Information flow*

The NPL strategy of a high NPL bank should be supported by an operational plan approved by the management body. We understand that the operational plan (including specific targets and processes) will be adopted at group level. Implementation will necessarily require a high-volume of information including macro-economic data, statistics on time to recovery and back-testing of estimated cash flows.

Subsidiary entities should have access to the necessary background information for implementing the operational plan. Data and benchmarks on time to recovery and valuation of specific assets provided by external databases or local associations should also be accessible.

- **We believe it should be clarified that, where appropriate, mother companies need to assist their subsidiary entities in the implementation of the operational plan including by providing sufficient background context and relevant data. Access to external data providers should also be permitted..**

### *Leasing*

The NPL strategy should be designed to fit a firm's various business segments and portfolios. For NPL management purposes, leasing contracts cannot always be treated similarly as standard loans. This is because the lessor is the legal owner of the leased asset. Liquidation or write-off of a leasing position therefore requires a preliminary sale/liquidation of the leased asset. This specificity is particularly important in the case of portfolio reductions through sales. A reference to leasing would therefore be helpful.

- **We believe institutions should be allowed to distinguish NPL strategies according to established priorities including products' legal characteristics should this be considered appropriate.**

## **3. NPL governance and operations**

### *NPL operating model*

We understand that international experience indicates that a suitable NPL operating model is based on dedicated NPL workout units. We appreciate the recognition that for some business lines and exposures, the implementation of a fully separate organisational unit may not be possible. As mentioned by the ECB, appropriate internal controls should suffice to prevent potential conflicts of interest.

- **Flexibility should be preserved where the establishment of a fully separate organisational unit is impossible or disproportionately costly. Recommendations on mitigation measures for conflict of interest (in the absence of dedicated workout units) would be helpful.**

#### *Technical resources*

We welcome the ECB's recognition of the value of adequate data, automatic monitoring systems and industrialised NPL management.

- **We would support further explanations on the interaction of IT systems with the NPL risk mitigation technics.**

#### *NPL segmentation criteria in retail*

We see the proposed sample of NPL segmentation criteria in retail as a useful work basis. We believe at least two important information are currently missing. The segmentation should include a reference to motor finance agreements which constitute a substantial business segment in Europe as well as a reference to moveable underlying collateral. In line with our previous comment on leasing, we would also like to suggest adjusting the segmentation to better capture the specifics of this product.

We would recommend adding the following criteria:

- Paragraph 7 – Purpose of credit facility (by product)
  - **Motor finance (loan and lease)**
- Paragraph 13 – Type of underlying collateral
  - **Moveable collateral**
  - Immovable collateral
    - Land
    - Building
- Paragraph 13 – Type of underlying collateral
  - **Leased assets**
    - **Equipment**
    - **Automotive**
    - **Real Estate**
    - **Other**

#### *Early Warning Indicators*

We take note of the proposed requirement to establish early warning mechanisms / watch lists to monitor performing loans and prevent the deterioration of credit quality and provide the management body and relevant committees/managers with periodic reports. We welcome the provision of samples

of early warning indicators in Annex 4. As the ECB will know, similar indicators are being implemented by credit institutions for accounting purposes in line with IFRS 9 standards.

- **We would welcome further synchronisation of these indicators to facilitate a unique approach for NPL management and accounting.**

#### **4. Forbearance**

##### *Diversity of measures*

We welcome the listing of most common forbearance measures. We think this an interesting and valuable recap of possible solutions. As recognised by the ECB at the 7 November 2016 hearing, local legal frameworks will often impose a very strict forbearance pathway and solutions. This is particularly relevant in a B2C environment. We think this will necessarily have an impact in terms of consistency between forbearance measures as well as the nature of the solutions which will be implemented by institutions. It is likely that an institution will have as many approaches to forbearance as the number of markets it is active in. This is an aspect which supervisory teams will need to be fully briefed on.

- **We believe the publication of a compendium of forbearance processes required by law (within the EU/EEA area) would bring true added value to both supervisory teams and institutions.**

##### *Affordability assessment*

We take note of the proposed requirement to conduct an affordability assessment of the borrower (both retail and corporate). We believe this is standard practice across most business segments. However, we are concerned by the very prescriptive nature of Annex 6 which, in our view, contradicts the flexibility the ECB is keen to provide in the field of NPL management.

We think there should be consistency with the criteria as well as tools already used for the assessment of applicant borrowers' creditworthiness before contracting.

- **It should be clarified that Annex 6 is purely indicative.**

#### **5. Collateral valuation for immovable property**

##### *Indexed valuations*

We see the threshold of 300,000 EUR in gross value for the use of indexation or automated processes for immovable property collaterals as disproportionately low.

- **We think the threshold should be reassessed.**

##### *Foreclosed assets*

The valuation and management of foreclosed assets are not always possible in the short proposed one year timeframe.

- **It would be helpful to recognise that pluri-annual sales programme of repossessed sales assets are compliant with the proposed guidance.**

I remain at your disposal, should you be interested in discussing any specific issue. Alternatively feel free to contact my colleagues Alexandre Giraud ([a.giraud@eurofinas.org](mailto:a.giraud@eurofinas.org) - tel: + 32 2 778 05 64) and Rafael Alarcón Abeti ([r.alarconabeti@leaseurope.org](mailto:r.alarconabeti@leaseurope.org) – tel +32 2 778 05 69)

Yours sincerely,



Leon Dhaene  
Director General

***Eurofinas and Leaseurope are entered into the European Transparency Register of Interest Representatives with ID n° 83211441580-56 and 16013361508-12***