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EACB comments on

EBA consultation paper on Guidelines on loan origination and monitoring

Contact:

The EACB trusts that its comments will be taken into account.

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General comments

The EACB welcomes the opportunity to comment on the EBA consultation on its draft Guidelines on loan origination and monitoring. We understand how a set of minimum supervisory expectations in this regard could help in avoiding the build up in the future of new NPLs.

We see, however, a number of critical aspects in the approach outlined in the EBA draft Guidelines, both in general terms (e.g. role of the Guidelines, which are supposed to be only an instrument aiming to clarify, assist with interpretation existing level 1 legislation and promote harmonisation of supervisory practices, overall consistency with other relevant elements of the regulatory framework, extremely short implementation date, etc.) and in terms of granular requirements proposed. We would emphasize that, according to Art. 16 of the EBA Regulation, guidelines are an instrument aiming "to establishing consistent, efficient and effective supervisory practices within the ESFS, and to ensuring the common, uniform and consistent application of Union law".

➢ *EBA should stick to current Level 1 regulation and should not pre-empt upcoming legislation*

To begin with, we are concerned that the proposed Guidelines go beyond what is required by the relevant level 1 legislation and that the EBA oversteps its mandate in doing so. This is for example the case for the Consumer Credit Directive (CCD) and the Mortgage Credit Directive (MCD).

While the EBA received a mandate from the Council to outline the supervisory guidance on loan origination and monitoring, this should be done in a way that is consistent with the level 1 legislation and that does not define an entirely new framework outside the legislative process. Many proposals go beyond the current legislation. This is, for example, the case for:

- Section 4.4 where the EBA refers to the notion of independence without specifying whether independence means formal independence or independence of mind. However, the CRD mentions only the notion of independence of mind and, therefore, the EBA should explicitly refer to it.
- ESG risks and considerations became an important regulatory development for regulators, supervisors and banks. These are also very complex concepts with multiple dimensions. At EU level, the legislative framework has been under preparation for over a year and some pieces will enter into force in the coming months while other will require some more time to be finalised. Given the importance and complexity of the matter, it is essential that EBA refrains from defining concepts, extending scopes and pre-empting the level 1 legislation. The EBA proposes definitions of concepts, which have not been defined at level 1 (transition risk; physical risk. EBA even includes legal risks under the transition risk definition). If these definitions were to remain in the Guidelines, we run the risk of them ending-up non-aligned with future level 1 definitions (legal uncertainty and instability); we would like to underline that the "NGFS report Macroeconomic and financial stability" from July 2019 comes to the conclusion that much more research is required in order to come to a convergent assessment of the impact of climate risk on financial stability aspects. What is needed certainly goes beyond the possibilities of a single institution.
- The EBA's proposals are even more surprising as the Commission's consultations on the CCD, the Distance Marketing of Consumer Financial Services Directive (DMFSD) and soon the MCD have been or might soon be launched. We are particularly concerned that standardised rules for creditworthiness assessment would exclude some categories of consumers. Co-operative banks wish to be able to keep on supporting atypical consumers that they trust. Moreover, applying similar mortgage credit assessment rules to consumer credits is not justified as the size, type, risk and complexity of the credit are not the same. Finally, the level 1 legislation thresholds and scope (e.g. the CCD) should be respected.

- *A more proportionate and principle-based approach is required*

We would also stress that proportionality should be further and more prominently spelt out in the draft Guidelines. We appreciate that the principle of proportionality is clearly mentioned and is not limited to size of the institutions but encompasses the wider business model, risk profile, and complexity of activities.

However, we believe that the level of detail and complexity of the Guidelines does not fit with the spirit of Pillar 2 requirements, which should be proportionate and principle based. The requirements set forth in the draft do not reflect features such as the volumes of transactions, the types of business, the complexity of the banks. It seems hardly possible that all requirements can be applied to all banks and all transactions.

We consider that the general framing of proportionality as expressed in para. 12 is not sufficient for an adequate implementation of the Guidelines. This is possibly a choice of EBA with a view to a more rules based approach rather than a more principle based one. It is evident that the aim is to give all supervisors very clear cut orientations, to which they can stick. In such a case, however, it is not sufficient to put some general references to proportionality in the beginning. Rather, indications should be built in to allow all requirements to be declined by all institutions in light of their business and applying proportionality and materiality. In fact, the challenge for supervisors will consist in a way to ensure that these prescriptive expectations are applied in a way that is appropriate to a specific loan or category of loans. In order to be successful regarding the harmonisation effort sought by the Guidelines, it seems important to give also some indications on how to handle proportionality aspects. In particular, one should keep in mind that a too conservative application of the Guidelines (when supervisors feel uncertain on how proportionality aspects could be reflected) could hamper the level playing field. Moreover, we believe that, too many elements of the Guidelines are indicated as minimum requirements, leaving little room for a proportionate and sensible implementation. We believe that the wording “at least” should be removed in a considerable number of areas (further explored below) and the elements suggested as minimums to be left as examples.

In particular for Sections 5-8 proportionality should always be applied taking into account the volume, nature and complexity of the credit facility. The EBA should write explicitly that each institution will have the discretion to set up their own internal policy in terms of threshold and nature/complexity for using the proportionality criterion at the credit facility level.

In this vein, we advocate for having adequate wording in the Guidelines to exclude an automatic tick the box approach to all facilities and avoid a disproportionate burden for both borrower and lender.

It would be necessary to ensure that the language of the Guidelines allows for more differentiation, especially regarding materiality aspects in order to allow banks to decline requirements appropriately and setting materiality levels or proportionality levels internally on the basis, for instance, of the complexity and riskiness of the credit business. The wording of para. 93 for example, creates the impression that standards that are suitable for loans to complex customers are to be applied also to the smallest companies (SMEs, one person enterprise etc). In fact, the collection of information for the business model and the corporate structure of the bakery store around the corner may not require very much. The Guidelines should therefore clarify much better that the information to be collected under para. 93 should be appropriate to the specific case. The same should apply in other parts of the Guidelines. Eventually, an approach allowing the banks to set up internal thresholds could help in avoiding disproportionate implementation costs particularly for customer segments with lower margins, and in geographies where the business environment is mainly characterized by SMEs. The key question is clearly the right level of granularity in the implementation.

We acknowledge that the EBA during the bilateral meeting and the hearing clarified that the requirements listed in Annexes are not to be considered as prescriptive. However, we suggest clearly specifying in the text of the Guidelines that Annexes are not intended to be a mandatory

checklist but rather that the information and data set out in the Annexes are to be considered as examples. This can be clearly stated in the "Executive Summary" or in the "Background and Rationale" Section or at the beginning of each Annex.

If the elements listed in the Annexes were to be maintained as mandatory requirements, we see that important difficulties would arise for both consumers and corporates' credit due to a very bureaucratic interview process for instance. It would also lead to longer waiting times and more costly efforts for analysing and processing, costs which would inevitably also fall on customers. For instance, the requirements for commercial credit are applied to both corporate customers and SMEs (usually for smaller amounts), evidently with different consequences. There is a clear lack of mechanisms that allow, for instance, smaller transactions to be performed efficiently.

Particularly para. 101 (and 114, 121, 140-146, 163, 248 and 257) and the sensitivity analysis requirements are too far reaching. Especially for unsecured consumer loans the individual sensitivity analysis are disproportionate and inefficient, also in consideration of the amounts of the transactions concerned. Moreover, para. 145-146 present events for which very few SMEs loans would not be endangered. This would only lead to reject most loan applications. Eventually this would result in a credit crunch and a shift of transactions to the unregulated market and shadow banking.

- *Setting an adequate implementation date*

The implementation date should be postponed to allow an adequate adjustment of processes and take into account the related IT challenges and necessary updates. This would also allow for appropriate consideration of any links (or 'knock-on effects') with the IRB modelling for which the final deadline is set at 31 December 2022.

We would suggest that at least a two to four year implementation is considered, in line with the timeline applied to the implementation of the updated definition of default, also with a view to a modular introduction of the elements demanded by the Guidelines. E.g. the implementation could start at 30th June 2022 for more qualitative elements and be finalised by December 2023 particularly for IT related adjustments.

Institutions need also have sufficient time to do their gap analysis. Such an analysis can only start after the Guidelines have been finalized (i.e. during 2020). Writing policies and procedures, and start the process to adapt IT-systems cannot start before such an analyses is completed. A thorough analysis and the consequent adjustments cannot reasonably be completed in 6 months as suggested by the EBA.

We would highlight that while certain data could even be available, they are not stored in platform/databases linked to credit risk. From a data point of view it is operationally challenging to establish the appropriate links and sourcing of the data points in a short time frame.

Even if industry feedback is reflected in the final Guidelines, there will be far-reaching consequences for the lending business and lending processes. The detailed requirements trigger a wide range of considerable adjustment. The requirements and gap analysis in order to develop a good IT solution, functional and technical concepts, IT implementation and testing, adjustments to the internal guidelines and policies, any necessary application and integration tests as well as the training of the employees involved in the credit process are not possible with such a short application period. A correct functional implementation, which also helps to avoid IT risks and ensures an integrated IT solution, is ensured by sufficient testing of the IT solution.

Also requirements like sensitivity analysis at loan level are tremendously disproportionate and cannot be achieved over a short horizon. In general, we believe that existing requirements should be considered when envisaging an adequate timeline. For example, the stages classification of IFRS 9 already addresses a number of concerns in order to avoid situations of untimely recognition of impaired exposures or too little too late provisioning. This is even enhanced by existing

requirements for macroeconomic assumptions and the use of stress testing (also at portfolio level) and back testing of models.

Additionally, the CCD and MCD are currently in the process of being evaluated or reviewed. It cannot be ruled out in this context that there will be changes to the creditworthiness assessment for consumer loans. Implementing these requirements will involve considerable effort and cost for institutions. The effective date of the Guidelines should therefore be harmonised with the evaluation of the EU directives in terms of both content and timing.

- *Facilities in the scope of the Guidelines*

In general, we believe that the Guidelines should only be applied to newly originated facilities. In this respect, the EBA should take appropriate account of the fact that monitoring the credit risk in the portfolio on newly introduced elements is not always possible for existing facilities. Also (legal) enforcement of newly proposed items is not always possible within various jurisdictions. We also see that the references in the Guideline (such as paras 8, 10 and 11) compared to the description of option 1b in the cost-benefit analysis is rather confusing. We see that the full new scope of loan origination requirements would apply to renegotiated facilities only when there is a significant impact on borrower's affordability assessment from the changes in the contract. At the very least the EBA should clarify which sections are applicable only to new or to renegotiated facilities.

- *Ensuring that the definitions are aligned with other pieces of the regulatory framework*

We recommend EBA to ensure that the proposed definitions are in line with all relevant elements of the regulatory framework, both from a prudential perspective (CRR, NPE management regulatory products, supervisory initiatives such as the credit underwriting data collection etc.) and from the standpoint of consumer legislation (CCD, MCD).

Answers to specific questions

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

- It should be ensured that the proposed Guidelines are consistent with the current regulations and initiatives as set by the European Commission, the European Council and the European Parliament. For example, 1) the Regulation amending CRR as regards minimum loss coverage for non-performing exposures (so-called NPL backstop), and with the other measures adopted within the European Council Action Plan on tackling the high level of NPLs and the supervisory expectations laid out in this respect (ECB Guidance March 2017 and EBA GL/2018/06), and 2) with other European initiatives regarding ESG factors and green lending. Clarification by the EBA is needed to enable institutions to ensure that any adjustment needed in the loan origination and monitoring is in line with the processes set out for the management of NPLs.
- In parallel with this consultation on loan origination, the European Commission is running a process to evaluate the CCD. The two initiatives overlap on the topic of consumer credit worthiness and in particular in Sections 5.2.1 and 5.2.4. Apart from the comments it may have on the content of the draft Guidelines, the EACB is concerned that – if the two initiatives follow their respective course each in their own timeline – the two initiatives will lead to two sets of changes having to be introduced in banks processes and IT systems in a relatively short timeframe. This should be avoided at all cost. The EACB thus calls for the EBA not to pursue the idea of Guidelines for unsecure lending until it is clear what will be the outcome and timeline of the Commission's work on level 1. A similar comment can be made regarding the review of the MCD which has also started.
- As mentioned during the bilateral meeting with the EBA officials on 17 September, we would like the EBA to clarify weather the Guidelines also apply to Third Party Providers (TPPs) under PSD2, especially to Account Information Service Providers (AISPs). PSD2 allows the following AISP business activity as an example:
    - A PSU wants to transmit data about itself to get a competing offer for a mortgage from the AISP. The AISP uses the transmitted data to evaluate the PSU's creditworthiness.
    - PSU A is on the AISP application. It supplies data about itself to the AISP ("KYC").
    - PSU A is then asked to use the AISP software to transmit data from its existing accounts with ASPSP A.
    - Now, PSU B rather than PSU A logs into ASPSP B and transmits the data from PSU B's accounts.

  By reading Article 4(1) of Regulation (EU) No 575/2013 (ESAs founding text), it seems that these AISPs would not be in scope as they are not payment institutions. At the same time, the CCD and MCD would not bring them into scope either as whether a given institution is in scope depends on the credit provided, not on their role in the credit process. If our analysis above is correct, the described AISP activity would not be subject to the Guidelines whereas the actual activity they undertake constitutes a creditworthiness assessment.
- If the Guidelines do not apply to unregulated non-banking financial institutions, they could serve their clients faster and under less requirements than regular banks. Consequently, clients would choose unregulated non-banking financial institutions over regular banks. Therefore, we encourage the EBA to ensure a level playing field by applying the requirements of the Guidelines to non-banking financial institutions in the same way.
  Apart from that, further tightening regular bank's lending abilities causes rejected applicants to apply for loans at the unregulated non-banking market, which would be detrimental to consumer protection.
- We would also welcome clarification by the EBA on which sections are applicable only to new or renegotiated facilities, and which ones are applicable to both new and existing facilities. In this respect, the EBA should take appropriate account of the fact that monitoring the credit risk in the portfolio on the basis of newly introduced elements is not

always possible for existing exposures. Also the (legal) enforcement of the newly proposed requirements would not always be possible across various jurisdictions. We understand that for the renegotiated loan agreements the full new scope of loan origination requirements would apply only when there is a change in the contract and when there is a significant impact on borrower's affordability assessment arising from the changes in the contract. We also note that the references in the Guidelines (e.g. paras 8, 10, 11) when compared to the description of option 1b in the cost-benefit analysis are very confusing.
- In general, the Guidelines should be applied considering the overall risk profile of loans; in some Member States (e.g. in Austria) the NCA has even stipulated[1] the possibility to deviate from credit risk provisions, for instance in the Risk classification procedures, if the low risk level of certain credit transactions or types of transaction does not seem to justify the risk classification procedure, such transactions can be disregarded for that procedure. At the same time, para. 79 (Early-warning procedure) stipulates that managers can decide that certain business and credit transactions below certain amounts, which shall both be defined according to their risk level in the internal guidelines, shall be exempted from the procedure for early detection of risks.
- We underline that the EBA should clarify and ensure alignment with various related regulatory products, both in terms of scope and content:
    - The EBA Guidelines on NPE and the management of forborne exposures (for instance, the word "renegotiated" might imply a conceptual connection with the definition of forborne exposure, especially in consideration of the fact that para. 6 makes reference to "throughout the life cycle" and to "monitoring of performing exposures).
    - The ECB credit underwriting data collection being performed.
    - The ECB guidance on leveraged transactions.
- Leasing and micro-financing also appear to be in scope. We note that the requirements as described in these guidelines are too burdensome for small tickets, given their specific nature, type, average size and complexity of the credit facilities granted (average contract size is € 25k). The Guidelines focus heavily on individual assessment of the creditworthiness of the borrower, with an extensive analysis of a large number of (financial) metrics and parameters. However, it should be noted that, among others, lease providers rely heavily on score-cards and automated decision making for the credit approval process. The draft Guidelines do not seem to cater for this kind of (automated) credit scoring and decision taking, unless the limited guidance under Section 4.3.3 "Technology-enabled innovation for credit granting" can be construed as such.
- With respect to para. 85, we note that it is not clear whether this "single customer view" should be available on the basis of credit commitments towards the institution, or whether commitments of other banks need to be included as well. If it refers to the former, then due to national requirements on data protection (amongst others), it might be extremely difficult to comply with this requirement.

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

The date of application of 30 June 2020 is too ambitious, in particular when considering:

- **Scope of application** – indeed institutions should apply the Guidelines on an individual, sub-consolidated and consolidated basis; to do so, also in consideration of the overall timeline for finalisation of the Guidelines, it is hardly possible to adjust over six months.

[1] FMA, Mindeststandards für das Kreditgeschäft und andere Geschäfte mit Adressenausfallsrisiken (02/2005), 13.04.2005

- **ESG factors** – insofar definitions concerning environmental factors and green lending are still under discussion, particularly within the negotiations on the proposal for a regulation on the establishment of a framework to facilitate sustainable investment. The final version of the taxonomy is expected to be issued by the end of the year and, to give sufficient time to market actors to perform the requested IT developments, it is expected to become applicable from 1 January 2022. Moreover, the assessment of risks associated to ESG factors requires professional skills that are not typical of staff employed in banks, particularly in the credit granting function, therefore, an adequate timeframe is needed to fill this knowledge gap. ESG factors are also part of supervisory reflections for their integration in the SREP, it should be avoided that different approaches are put in place in the banks at various point in time.
- **Consumer credit issues** – indeed it is problematic that the EBA issues such Guidelines while the assessment of the CCD launched by the European Commission is still ongoing and before the publication of the outcomes of such assessment. We consider that the on-going democratic process must be respected. In other words, it seems difficult to have Guidelines on points that are still discussed and may be reviewed in this context. Moreover, a consultation on the MCD might also be launched in the coming months by the European Commission.
- **Complexity of organisational processes** – the new requirements imply significant changes to the organisational processes related to credit granting and monitoring. In many cases this means that the IT system needs to be adapted and staff deeply trained. Those changes require a long period of time. This time pressure is aggravated by the fact that some of the requirements – for example, as mentioned above, in the area of environmental factors and green lending – are completely new.
- **Harmonised Understanding of Customer Data and Financial Key Figures** – recent findings of the credit underwriting exercise show that there is no EU-wide harmonised understanding of some of the customer data and financial key figures that must be collected according to the Guidelines. Such a harmonised EU-wide understanding is a precondition for the application of the Guidelines.
- **CRD V implementation period** – concerning the determination of a sufficient implementation it has to be borne in mind that the institutions – as an example – are granted an 18 months implementation period regarding the new requirements of CRD V while they are transposed into national law. The proposed requirements of the present EBA draft are much more comprehensive and complex with regard to their implementation in the internal processes of the institutions in comparison to the new CRD V requirements. Hence, the implementation period for the banks should in any case be longer than 18 months.
- **Data infrastructure** (Section 4.3.5 of the draft EBA Guidelines) – the requirements across the entire credit lifecycle (loan application, credit assessment, credit decision, credit granting, credit risk monitoring, repatriation, prolongations or early risk detection, forbearance and / or restructurings, reorganization, settlement or seizure of collateral etc.) seem very far-reaching, also in consideration of the expected granularity (loan by loan), to be implemented with reasonable effort by the proposed deadline of 30th June 2020, as for instance data collection and management need an IT structure that would be in some cases newly designed and in other cases adjusted to the new requirements introduced by the Guidelines. Consequently, if the final Guidelines are published by end of the year, it will be extremely challenging to prepare for implementation in time, due to budgeting

requests for 2020 already completed in the banks, and the need for definition of IT specifications. The IT teams are already under extreme pressure given by the changes of the current regulatory environment (and further changes are expected once the new Basel framework is implemented), by digital transformation, by new challengers that come with FinTechs etc.
Finally, the requirements are already ambitious for IRBA banks which have a certain degree of maturity in terms of data infrastructure and credit granting process, thus becoming even more demanding for SA banks that would need even more time and resource to cover, pedagogic aspects, and a strong change of practices.

Based on that, we would propose to postpone the date of application of the Guidelines to 31st December 2022 at the earliest, with a phased implementation of IT-related elements up to 4 years. An implementation date in December 2022 is also logical when looking at the IRB roadmap, as the EBA considers that the final deadline for implementation of the changes to the rating systems should be the end of 2022 (application date from 1 January 2023). This is also in line with other crucial elements like the EBA Guidelines on definition of default. The implementation of such pieces and their interconnectedness and the impact on credit granting processes and IT systems is extremely impactful (See further comments below on paras 27, 28, 29, Question 4).

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 4.3.3) and environmental factors and green lending (Section 4.3.4)?

Regarding Section 4.3.3, para. 47(d) states that "when using technology-enabled innovation for credit granting purposes, institutions should (…) verify and regularly monitor the outputs and compare their performance with the outputs of traditional methods/tools*".* However, the parallel maintenance and execution of traditional and technology-enabled methods and tools eliminates the benefits of the latter and constitutes an unnecessary impediment. Therefore, this requirement should be removed from the Guidelines. Should the para. be maintained, it should at least be reworded as follows: "(…), institutions should (…) verify and regularly monitor the outputs and compare their performance with the related outputs and compare their performance with those of traditional methods/tools, except when an AI model is already natively explicable (for which a comparison with traditional methods is less/not relevant). Regarding black-box models, the comparison should be carried out at the development stage ("build") only or when the monitoring of the performances shows a decrease, and that a rebuilt is needed."

Moreover, it does not seem necessary to ensure that the management body understands how the underlying technology enabled innovation is used and affects institutions' credit granting procedures as specified in para. 47(f). Indeed, an adequate information flow from technical staff to the management board should be sufficient.

Regarding Section 4.3.4, we would highlight that the Guidelines are likely to steer green lending from a personal loan logic to one of "allocated" credit or linked credit, which is contrary to the current understanding of how risk and return are chosen. This is also likely to discourage the development of this type of financing given the constraints in terms of formal elements to consider.

We would also point out the following:

- Regarding para. 26, the credit limit framework, defined in consistency with the credit risk appetite, should remain aside from the RAF, while the current wording may suggest mixing the two. Moreover, we believe that a detailed specification of the desired composition of the credit portfolio is disproportionate (particularly for banks operating in a very geographically delimited area) and the RAF should be sufficient.
- It would be helpful if terms like auditability, traceability, robustness and resilience would be clarified in respect to technology-enabled innovation. Especially, because technology-enabled machine output is by its nature less auditable and traceable. This risk is mitigated by several "interpretation" algorithms.
- For para. 47 more guidance regarding technology-enabled credit granting would be welcome, as this innovated technology-based way of credit-assessment differs substantially from the traditional way of assessment as described in Section 5. It seems that the Guidelines do not fully embrace new methods of creditworthiness assessments such as data based predictive (payment) behaviour.
- The Guidelines should take into consideration the growing importance of ESG factors and green lending but should refrain from defining concepts, pre-empting level 1 legislation and being too prescriptive. In this context:
    - We advocate for aligning this definition, especially regarding the "environmental criteria" with the legislative work currently under way, in particular the Regulation of the European Parliament and of the Council on disclosures relating to sustainable investments and sustainability risks and amending Directive (EU) 2016/2341 and the Regulation of the European Parliament and of the Council on the establishment of a framework to facilitate sustainable investment and accordingly the work done by the TEG to define technical screening criteria.
    - A clear reference to the Taxonomy will ensure legal certainty as a definition not in line with the future level 1 definitions would jeopardize the process of developing clear and uniform criteria for what can be defined as "green" in the European Union.
- According to para. 48, institutions should integrate ESG-risks in their risk management policies, credit policies and procedures. This requirement is not in line with Art. 1 para. 29(d) CRD V, which mandates EBA to develop a uniform definition of ESG risks, including physical risks and transition risks. This mandate implies that there is no uniform understanding of ESG risks. Since there is no uniform understanding of ESG risks, the requirement to consider those risks in management policies, credit policies and procedures is not appropriate.
- Para. 49 sets very burdensome requirements implying an excessive responsibility for institutions on the use and destination of loans. If those requirements remain unchanged, the risk is that lending to enterprises may be significantly reduced. In particular, para. 49 states that "institutions that originate green credit facilities should develop specific green lending policies and procedures covering the granting and monitoring of such credit facilities". This could be understood as if institutions were to implement specific green lending policies and procedures in addition to their general policies and procedures. However, a subsection within the general lending policies and procedures, applicable to green loans and covering their specificities, should be sufficient since most aspects of green loans are already covered by general lending policies and procedures.
- Para. 51 stipulates that "institutions should in particular take into account risks associated with environmental factors and climate change in their credit risk policies and procedures. The risks of climate change for the financial performance of borrowers can be classified as

physical risks or transition risks". However, one category of physical risks are acute physical risks that, per definition, are not predictable. Therefore, it is unclear, how such risks could be integrated in risk policies.

- The EBA should at least also clarify how "borrowers" should be interpreted in this context. Should it be read as all the borrowers of the institution or the ones with a green lending project?
- It will take time to gain insight in both transition and physical risk on a qualitative and quantitative basis. Institutions and borrowers will need a time path of years (as has also been recommended by the TCFD) to get the right information and insight on these subjects.
- EBA proposes specifications for the banks' assessment process of their green loans proceeds (limited to professional clients; it would be useful to understand whether this relates to professional clients as defined under MiFID): those specifications are too prescriptive for guidelines and create a problem of data access for banks (let alone the implementation of the adequate IT systems). Moreover, as the EU taxonomy that is currently under legislative scrutiny has not been designed for credit activity, EBA cannot refer to it and therefore proposes when it comes to green activities reference that banks "provide a list of the green projects and criteria that the institutions consider as eligible as part of their green lending policy or relate to one or more generally accepted standard on what type of lending is considered to be green" (para. 49(a)) Yet, the European Commission's ambition is that the EU taxonomy become the main reference for European finance (included in due course, for credit). By preempting future EU legislative developments, EBA does not take into account future evolutions of the EU taxonomy.

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

Regarding Section 4.3, para. 35(b) states that institutions are required to consider at least the items listed in Annex 1, when setting up their credit risk policies/procedures and specifying the credit granting criteria. Defining the minimum scope of criteria that must be considered in the credit granting process is not proportionate, especially for smaller and simpler credit facilities.
In our opinion, as far as credit granting criteria in general are defined in Annex 1, the principle of proportionality should be enshrined. According to the Guidelines, institutions are required to consider at least the items listed in Annex 1, when setting up their credit risk policies. This implies that institutions must then consider at least all those criteria in the credit granting process. Defining the minimum scope of criteria that must be considered in the credit granting process is not strengthening the principle of proportionality: while for some loans considering all the items listed in Annex 1 might be appropriate, for simply structured loans the requirement to consider all the items is exuberant.
The credit granting criteria listed in Annex 1 should only provide an exemplary guidance to institutions on which criteria can be considered in the credit granting process. Institutions should not be obliged to consider all the criteria mentioned in Annex 1 in each individual case.
On that basis, we suggest para. 35(b) should be reworded as follows: "credit granting criteria; while specifying these criteria, institutions should at least consider items referred to in Annex 1 as an exemplary guidance;".

Furthermore we would highlight the following:

- Para. 27: The top-down is generally well established. However, banks need more time than 6 months to implement the bottom-up.
- Para. 28: This is certainly an area for which a longer timeline would be needed. Para. 29 in particular asks for metrics and limits in a wider extent than today's practice.
- Para. 29: The Credit Risk Appetite is a global assessment document, while in this instance a more detailed approach is required. For such, a phase-in period for implementation is needed.
- Para. 35:
  - We suggest replacing "b. credit granting criteria; while specifying these criteria, institutions should at least consider items referred to in Annex 1;" by "should define the list of internal items to apply, as for examples, the items in Annex 1."
  - The introduction of the sensitivity analysis as referred to in Section 5.2 is a complete change of methodology. The Section 5.2 considers scenarios at the loan level, whereas today it is performed at the portfolio level. This is a further element that would justify a phased in implementation.
  - With regard to letter (i): The requirements relating to what is to be documented and recorded as part of the credit granting process including for sampling and audit purposes generate a huge work and IT cost for setting-up a full process of registration. At the moment, IRBA banks might be closer to achieve this requirement, but SA banks are far from having IT capacity to implement it. A phased in transition (define an adequate infrastructure, budget assessment, time to implement) is necessary.
- Para. 48: The word "holistic" is extremely strong. If we want to avoid a stillborn market, we should be really cautious about the requirement. Otherwise, no initiative will rise. Indeed, it should be consider as any new product, from idea to implementation. Otherwise, the scope and meaning of "holistic approach" should be defined with details.
- Paras 52-53: Only IRBA banks with an Utility Credit Analytics Department would be able to manage this requirement on time. The level of requirements is so high than SA banks may not have the dedicated team to deal with such credit loans.

Regarding Section 4.3.1 "Anti-money laundering and counter-terrorist financing policies and procedures", it should be noted that:

- Contrary to what is practice under AML legislation, the principles set forth by the draft Guidelines are not risk based and they apply throughout the entire life cycle of the credit.
- The measures required are extensive, covering the origin of flows (repayment by the borrower) and the source of funds.
- The measures required make no distinction between a lender that holds the account (a bank which grants a credit) and a financial institution (a specialised provider of consumer credit such as Cofidis).
- The control over the use of funds cannot apply in case of a non-purpose loan or disbursement is made into an account and followed by a cash withdrawal.
- Moreover, we would highlight that the required third party identification for all contracts (para. 40 (b)) seems not only in contrast with the AML Directive, but also rather imprecise as it is unclear which parties would actually need identification. Also, with regard to guarantees, it seems questionable the need to identify a guarantor for the purpose of AML

as the nature of the guarantee does not involve a monetary transaction in itself; moreover this would particularly complicate processes for syndicated loans.

Our proposals are the following:

- The controls should only cover the search of potential third party and never cover the source of funds, save in exceptional cases (politically exposed persons in case of high risk defined in a risks classification).
- A risks classification should be defined with the aim to have a thorough knowledge of the borrower in case of high risk (creditworthiness, analysis of the investment's profitability, the use of funds if possible…) and a detection of unusual transactions (particularly complex transactions, unusually large transactions or transactions which have no apparent economic or visible lawful purpose).
- The vigilance measures should not apply, if during the relationship which cannot be limited to the credit, there isn't any payment incident, any new application for credit, any change of IBAN or any material change.
- The specificity of non-purpose loans and of specialised providers of consumer credit which are not account holders should be taken into account.
- A risk based approach and the implementation of risk-proportionate measures are necessary.

Finally, according to para. 56, data requirements for NPL are extended to PL that, in our opinion, seems excessive.

Q5: What are the respondents' views on the requirements for governance for credit granting and monitoring (Section 4)?

Overall, the requirements on credit decision-making and monitoring should not lead to decrease the efficiency of banks' lending activity.

As far as the notion of independence in credit decision-making is concerned (paras 63 and 64), we appreciate that the Guidelines make a clear reference to the EBA Guidelines on internal governance. However, it should be clearly stated that the notion of independence only refers to the independence of mind and not to the notion of formal independence. Indeed, CRD does not mention formal independence, rather it refers to independence of mind and conflict of interest.

Moreover, criteria laid down in para. 63 on conflict of interest go beyond what is provided for in CRD, CRR, in the EBA Guidelines on Internal Governance, and in the EBA-ESMA Guidelines on the assessment of the suitability of members of the management body and key function holder and may create legal uncertainty.

Moreover, para. 63(b) seems difficult to match with the case of:

- Loans granted to the employees of the bank, where there is always a professional relationship between the borrower and individual involved in the credit decision-making (para. 63(b)(i)).
- Small regional banks providing their services in rural areas, where people are usually familiar with each other: those specific sets of situations, in which an individual cannot take part in a credit decision, especially restrict their business activities (para. 63(b)(ii)).

Banks have already internal process for sensitive demands: confidentiality, verified documentations, assessment performs on financial figures, and so on. We ask for terms which

would be reasonably applicable. We mean that it is possible to stress the responsibility of the banks on these specific cases, but anyway, we ask for "no blocking" terms for implementation.

On that basis, we would propose deleting para. 63b.

Regarding the management body responsibilities, the Guidelines – while they shall not refer to a specific governance structure – should nevertheless clearly state whether the term "management body" refers to its supervisory function or its executive function. Besides, "management body" should be redefined as "management body and relevant delegated decision making bodies".

We also point out that the requirements in para. 57 on credit committees should be better clarified. It should be sufficient in fact that only loans of particularly high ticket and/or that deviate from the overall credit strategy or risk appetite of the institution would need to be approved at board level or at a directors' committee level.

Regarding the remuneration schemes mentioned in para. 63©, it is worth mentioning that they are not linked only to volume but also to other parameters such as the quality of lending. Therefore separating commercial staff from any functions dealing with loan administration would be detrimental in terms of a more complex and less efficient lending process. In this context, it should be underlined that "those who are subject to remuneration schemes associated with the growth of new business" (as stated in para. 63(c)) is potentially very wide.

Regarding Section 4.4.2 "Exception and escalation procedures", para. 66 provides that "institutions should ensure that staff members involved in credit granting and management escalate and report the full nature of exceptions to policies and breaches of limits internally to the appropriate governance body in accordance with the escalation procedure". It is worth highlighting that the execution of an escalation procedure affords personal and organizational resources. Therefore, we are of the view that not each single exception to policies and breach of limits should trigger an escalation procedure; rather the Guidelines should allow institutions to implement a relevance limit for escalation procedures in the case of exceptions to policies and breaches of limits, below which no escalation procedure should be triggered.

In addition, regarding Section 4.4.3 "Lending to affiliated parties", it is worth noting that transactions with related parties are already covered by para. 113(d) of the EBA Guidelines on Internal governance, therefore, we suggest paras 67, 68 and 69 should be deleted. If those paragraphs are not deleted, the Guidelines should at least clearly specify that the notion of "affiliated party" is in line with the notion of "related party" as defined in CRD V.

Finally, with regard to para. 76(g), we wish to point out that an independent second opinion is not necessary for each and every creditworthiness assessment. For example, in different European countries loans that are not risk-relevant are decided in a "single vote procedure". The decision on the applicable risk relevance limit is a matter for the institutions and thus enables appropriate, lean lending processes in the small-scale lending business.

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

The draft Guidelines indicate that the Credit risk management and internal controls framework should provide an "independent risk opinion to the credit decision takers" (para. 76©) and an "independent/second opinion to the creditworthiness assessment" (para. 76(g)), which would seem to imply a preliminary involvement of the risk management function in the credit process.

Such an active role for the risk management function seems hard to realise firstly due to the fact that the prior involvement of the risk control function would not be fully coherent with the separation of responsibilities between the ex-ante first line of defence (lending functions) and the ex-post second line of controls (risk management) and more generally with the principle of segregation of duty. The separation of duty and responsibilities is for instance also remarked in the framework of NPLs' management (ECB Guidance March 2017 and EBA GL/2018/06) which marks a distinction between workout units and units responsible for loan origination.

For para. 76(l) the requirement to perform regular individual credit reviews (rather than a portfolio monitoring approach) should also be risk-based, such as for consumers and other retail.

Secondly, the need for a preliminary opinion of the risk management on the creditworthiness assessment bears to risk of leading to process inefficiencies, duplication of activities and skills in charge of different functions, additional staffing costs, etc. This is particularly the case for small ticket loans. The role of the risk management and internal control functions is not developing new credit products, we would rather see that the risk management function and the compliance function should be involved in approving new products or significant changes to existing products or be involved in complex credit demand. In the latter case they often are in charge for delivering a "non-objection".

In addition, as far as remuneration policies are concerned, we fully agree with the principles underlying para. 81 (i.e. consistency with the overall credit risk appetite, prevention of conflicts of interest; protection of consumers' rights and interests). Those core principles are already in line with CRD, EBA Guidelines on remuneration policies and MiFID regulation.

National provisions have been adjusted accordingly in the past, not least because of the MCD.

However:

- Subjecting all staff involved in credit granting to additional remuneration requirements – as set down in para. 82 – seems superfluous and impractical. Indeed, the general requirement implying remuneration policies and practices should be consistent with and promote sound and effective risk management is already incorporated in the CRD IV (Articles 74 and 92). This requirement is already applicable to all staff in credit granting so that there is no need for a separate provision with regard to "credit exposures" (para. 82(a)) or "credit risk appetite" (para. 82(b)). The same holds true for the requirements on the rights and interests of consumers and misselling prevention practices (para. 82(c)) which are already stipulated in CRD IV, EBA/GL/2015/22 on sound remuneration policies and EBA/GL/2016/06 on remuneration policies and practices related to the sale and provision of retail banking products and services. The plurality of new and even more detailed requirements for different groups of staff results in a more complex remuneration system. This, in turn, overburdens small and middle-sized institutions. We also recall that the new CRD V introduced specific rules for small-non complex institutions to alleviate the complexities of variable remuneration rules, the Guidelines should not constitute a way to introduce regulation via the backdoor. Linking variable remuneration of all staff to the long-term quality of credit exposures (para. 82(a)) is not appropriate. Indeed, the goal should be achieved at bank level, not at portfolio level and, in any case, never through indicators/metrics applied at individual level. Integrating metrics on the intrinsic quality of credits could lead to a problem of access to credit for a large number of clients: indeed, encouraging employees to the long-term quality of credit exposures means that banks would end up financing only top-rated counterparties – as their credit risk

managers would be motivated in accepting top-quality request only – and therefore stop financing the real economy.

- Using any credit quality metric to compute variable remuneration of all staff involved in credit granting (i.e. not only front office staff but also credit risk staff) would not be fair: indeed, the portfolio's credit quality is volatile by nature; therefore, even if credit risk staff have perfectly done their job (i.e. well defined the limits, well monitored them, well analysed the risk profile, etc.), this staff's remuneration would be penalised due to external factors that are impossible to be anticipated years in advance and are linked to the global environment among other things.
- Para. 82(c) is useless since the rights and interest of consumers are deeply embedded in any process as part of institutions' code of conducts.

We therefore suggest paras 81 and 82 should be deleted.

Should para. 82 be kept, we consider that the element to be taken into consideration for computing variable remuneration should not be the quality of credit itself, but rather the respect of the institution's credit risk policy, as well as internal guidelines and procedures regarding the credit granting process and its monitoring. On that basis, we suggest the following rewording of para. 82:

82. Institutions' remuneration policies and practices should in particular ensure that:

a. variable remuneration of the staff involved in credit granting should be linked, among others, to the ~~long-term~~ **respect of the credit risk policy, guidelines and procedures of the institution as regards** ~~of long-term~~ **the credit granting process and its monitoring;**

b. variable remuneration of the staff involved in credit granting that is linked to performance objectives/targets should include **criteria on the** ~~credit quality metrics~~ **respect of the credit risk policy, guidelines and procedures of the institution related to the credit granting process and its monitoring in their activities** and be in line with credit risk appetite**.**~~; and~~

~~c. remuneration policies and practices related to the staff's activities should take into account the rights and interests of consumers and should not incentivise any misselling practices.~~

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

General observations

- Although the principle of proportionality is mentioned on para. 13 in the "Background and Rationale" Section of the Guidelines, we would much appreciate a specific reference to this principle of proportionality at the beginning of Section 5. A proportionate approach is necessary with regard to data collection, taking into due account the credit volumes, size and riskiness of the loans etc. It is also necessary to better reflect in an adequately differentiated manner the differences between loans for consumers, real estate and so on.

- We strongly believe that the scope provided for under both the CCD and the MCD should be strictly applied. The EBA Guidelines should only apply to those credits which fall under the scope of the current level 1 Directives. The requirements provided for in the proposed EBA Guidelines, and in particular those in Annex 2, go beyond the applicable Directives and are too prescriptive. We strongly believe that they should be drafted in a way that allows

consideration of the type of credit amount and the necessary flexibility for the various distribution channels used. We acknowledge that the EBA during the bilateral meeting and the hearing clarified that the requirements listed in Annex 2 are not to be considered as prescriptive. However, we suggest clearly specifying in the text of the Guidelines that Annex 2 is not intended to be a mandatory checklist but rather that the information and data set out in the Annex are to be considered as examples. This can be clearly stated in the "Executive Summary" or in the "Background and Rationale" Section or at the beginning of Annex 2.

Comments to the "General requirements"

- Para. 85: We suggest clarifying that the requirements for the creditworthiness assessment should reflect the type, the size and the complexity of the loan concerned.
  - It is not clear what is meant in para. 85. with "comprehensive" view of a financial position. Does it mean for example a view over the connected client group of the customer? Specifically, for micro and SME customers in the retail segment or SME customers in the corporate segment such a comprehensive view cannot be at the same level as for large companies. Moreover, we presume that in particular for very small loans such as overdrafts or credit card limits, information provided by borrowers about their income will be sufficient. Only in special cases (e.g. suspected fraud) should this have to be documented by additional evidence/documents. However, such a clarification would also be desirable for loans below a limit to be defined by the institution based on risk aspects, because the risks are manageable. We therefore suggest deleting both occurrences of the word "comprehensive" in this paragraph.
  - With regard to the wording "single customer view", we suggest deleting "single" as the wording borrower can be a single customer, but also a household, a couple or life partnership, etc.
- Paragraphs 88-89: The proportionality principle could be explicitly reflected, and the requirements should consider given asset class, product, purpose, size, complexity and potential risk.
- Para. 88: The obligation to respect Regulation 2016/679 (GDPR) in efforts to verify information is duly noted and goes without saying (although we would appreciate the EBA to mention the correct Regulation in the Guidelines). We would also like to point out that the GDPR outlines six legal bases for the lawfulness of processing. According to the wording used in para. 88, "consent" is the only legal basis that creditors and institutions must rely on. We suggest rephrasing the sentence as follows: "Where, for the purposes of these guidelines, institutions and creditors make enquiries regarding a borrower's personal data, institutions and creditors need to ensure that the requirements, in particular to inform and seek permission from the borrower, of Regulation (EU) No 2016/679 are met, before making such enquiries to third parties".

  In addition, in cases where consent is the legal basis used by institutions, applying the current version of the Guidelines would mean that if the customer does not give consent for information to be obtained, the verification of the information he/she has provided cannot be done. We understand the word "reasonable" in para. 88 thus to mean that verification in such case is not required.

  Finally, para. 88 obliges institutions to assess the plausibility of any information and to make reasonable enquiries to the borrower or third parties. While the MCD in its Recital 58 and Art. 20(1) obliges creditors to appropriately verify information on the financial and economic

situation, including the borrower's income and expenses, this is not the case for the information under the CCD and we therefore find that the EBA's requirement to assess the plausibility of any information is not appropriate. We suggest rephrasing the paragraph as follows: "Institutions and creditors should **consider** assess**ing** the plausibility of ~~any~~ information and data provided by the borrower, and should **consider** make**ing** ~~any~~ necessary checks to verify the authenticity of information".

- Para. 90 states that institutions and creditors should document the information and data that lead to credit approval, including the actions and assessments, in particular steps taken to verify income, carried out by the institutions and creditors, and maintain this documentation in an accessible form (readily available for competent authorities) for at least the duration of the loan agreement.
  It should be explained what "maintaining this documentation" means. Do the credit policies count as documentation for cases based on which a very light customer verification is done? How is this documentation interpreted in relation to the digital environment that all banks are heading towards?

Consumer loans

General comment

- Although para. 86 states that the information and data to be collected should be proportionate given the purpose, size, complexity and potential risk associated with the loan, the subsequent obligations under paras 91 to "creditors should collect… at least" and 92 to "at least consider" can lead to collect and verify all the information under Annex 2 for consumer loans, seemingly with no room to take proportionality into account. We assume this is because under para. 15 (page 11), the EBA states that consumer protection cannot be subject to proportionality, but this does not frame creditworthiness assessments.
  From the outreach exchanges organised by the EBA, it appeared that this would be the case for consumer protection strictly speaking (e.g. case of abuses, mis-selling etc.), not for considerations from a risk perspective. Thus, the intention would be to see the requirements in Annex 2 as a set of examples, this should be more clearly explicated. Consequently, also para. 15 should be adjusted or adapted to mirror pars 91 and 92, which in turn have to be adjusted to allow for differences in information and data collection/verification based on, for example, whether the loan is a general consumer loan or relates to real estate as well as the amount and duration of the loan. Our reasoning is the following:
  - Consumer loans are typically for smaller amounts and shorter duration and should be distinguished from other types of loans such as mortgage credit/home loans.
  - Loans under Euro 200 or loans granted free of interest and without any other charges and loans under the terms of which the credit has to be repaid within three months and only insignificant charges are payable are outside the scope of the CCD which governs the provision of unsecured consumer loans in Europe; for these loans, the application of the requirements set in the proposed EBA Guidelines would be disproportionate. The cumbersome process requiring the systematic collection of supporting documents will deter institutions from offering this type of loans, which are widespread and represent recognised sources of growth and consumption and which meet the needs of consumers and retailers.

- Depending on the institution, the market and the Member State, co-operative banks may rely, for the collection of certain information, such as the type, sector, status and duration of employment, also on self declaration by the customer as it could be difficult or too costly in proportion to the loan to obtain this information itself/to verify this information (see also our comment on para. 88).
- The systematic collection of documentation is challenging for some distribution channels, such as credit at a distance or linked credits in shops.
- The EACB believes that the principle of responsible borrowing should also apply and that the customer should remain responsible for some of the information relative to his person on which he/she is best placed to provide it. Examples are a person's tax status or whether the borrower has loans with other providers. In the context of this latter information, it should be remembered that not all credit registers in Europe, whether held by public or commercial entities, provide for this information.

Considering the above, we suggest the following amendments:

- Para. 91 "Where appropriate, institutions and creditors should collect and verify information in relation to ~~at least~~ the following".
- Para. 92 "For the purposes of the collection and verification of information, institutions and creditors should ~~at least~~ consider collecting**, where appropriate,** the information and data as set out in Annex 2".

Loans to professionals/SMEs

General comment

The wording of para. 93 creates the impression that standards that are suitable for loans to complex entities are to be applied to the smallest companies. In fact, the collection of information of the business model and the corporate structure of the bakery store around the corner may not require very much. The Guidelines should therefore clarify much better that the information to be collected under para. 93 should be appropriate to the specific case. It has to be clarified that banks can decline the collection and verification of the information required along materiality and proportionality aspects. Furthermore, it has to be made clear that only the "usually available information" can be requested. For example, not all professionals are required to establish balance sheets. Art. 93, together with Annex 2 rather creates the impression that balance sheets have to be considered in all the cases.
In this context The EACB would like to stress that for the majority of loans granted to SMEs – which represent a significant proportion of the loan portfolio for many banks – some of the required information (listed in Annex 2) determine high and disproportionate collecting costs, compared to the economic value of the financing transaction or to the added value in the creditworthiness analysis. It has to be clarified much better that the Annex 2 elements are not mandatory requirements.
The EACB therefore considers that the Guidelines should further clarify how proportionality could be applied to professional clients for example by further segmenting the different kinds of professional clients into individual firms, small corporates, mid-sized companies, large firms.

Comments on specific paragraphs:

- Para. 93: In EACB's opinion, the listed requirements should not be considered minimum requirements. First, within the proportionality principle business plans (e) and financial projections (f) are not available for micro and SME enterprises in the retail segment. Financial projections are also not typical to be provided by stock-exchange listed companies. Questionable is also how a financial projection should be verified. It could lead to very subjective lending practices across the institutions on how this requirement would be met. Accordingly, we suggest rephrasing the sentence as follows: "For the purpose of the creditworthiness assessment of professionals, institutions should **take reasonable efforts** to collect and verify relevant information**, where available,** in relation to ~~at least~~ the following".
- Para. 94: The minimum requirements for collection and verification to professional clients in Annex 2 are too granular for small businesses included in the retail segment. Reference should be included that the requirements are proportional to the segment/sizes and complexity of facilities. Consequently, we suggest rephrasing the sentence as follows: "For the purposes of the collection and verification of information, institutions should ~~at least~~ consider collecting**, where appropriate,** the information and data as set out in Annex 2". See also comments to para. 93 about business plans and financial projections.

Although during the bilateral meeting and the hearing with the EBA officials, the EBA said that the list of information and data set out in Annex 2 are not intended to be mandatory, we would welcome an explicit clarification in the text of the Guidelines (see also our comments at the beginning of Question 7). This being said, we would like to make some comments on some specific points of Annex 2:

- Point 11 under "Lending to consumers" – "Data from credit registers or credit information bureaux should cover at least the information on financial liabilities and arrears in payment". However, in some countries, information is only available on credit repayment incidents (negative information) and it is arguably not within the scope of the EBA Guidelines to regulate the nature (positive or negative) of the credit registers in Member States.
- Point 3 under "Lending to professional" – "Financial statements covering a reasonable period…": In the case of specialised lending where a new asset is being financed, there would be no existing financial statements covering the previous years.
- Point 16 under "Lending to consumers" – The requirements regarding information on the enforceability of collaterals are disproportionate if applicable to any type of loan origination. Depending on the nature of the collateral (mortgage, privilege of the money lender – PPD, guarantee given by an insurance company or a financial institution) the terms for calling the collateral into play within a Member State should be sufficient, complemented by information on the collateral itself as required by point 12.

  Regarding "Lending to professionals", in the case of specialised lending, substantial control of the collateral is achieved through different security packages. The power of this security package is notably that it enables lenders to put strong pressure on sponsors (who brought the equity), which makes restructuring easier. The recovery generally best obtained through a restructuring is based on cash flows to be generated by the collateral on which the lenders have a substantial claim through different structures and security packages. The rating and loss given defaults (LGDs), based notably on the efficiency of such security package in terms

of future cash flow benefit, is assessed by the internal legal teams and front officers and validated by the risk department. Therefore, regarding point 16, we suggest adding "**in the case of specialised lending, description of the structure and security package of the transaction**".
- References to "evidence of" – As long as this information is in the credit applications or in the annual review memos, this should be considered as sufficient evidence. It should not be necessary to record this information in IT systems. Having the financial accounts of the borrower in PDF format, for example, should be considered as sufficient.

Q8: What are the respondents' views on the requirements for assessment of borrower's creditworthiness (Section 5.2)?

While recognising the need for thorough creditworthiness assessments, the EACB repeats some of the messages formulated under Question 7. Consumer loans are typically of short duration and relatively low value, and must be distinguished from other types of loans such as mortgage credit. In accordance with the principle of proportionality, the creditworthiness assessment should reflect the type, the size and the complexity of the loan concerned. As they stand, the requirements for the assessment are too detailed and would need to allow for more proportionality.

Too much details risk leading banks to a situation of a more standardised creditworthiness assessment process, which would block the market without taking into consideration the peculiarities of each Member State, which may have an influence on the creditworthiness assessment process (e.g. social security system, amounts, economic growth, growth prospects job markets, saving habits, national rates of divorces, cost of education for children, etc.) and would translate into an impoverishment of the offer, preventing any kind of customisation.

Moreover, the standardised requirements imposed by the EBA would be such as to eliminate the credit at the point of sale, with the resulting macroeconomic consequences throughout the intermediation chain for car dealership partners or large distribution. In fact, when a consumer goes to a store to make a purchase that she/he wishes to finance by means of a credit, she/he does not have at her/his disposal her/his tax assessment, her/his employment contract or her/his payroll. The inability to request credit may in many cases lead consumers to abandon a purchase.

Detailed comments

Consumer lending

- Para. 96: It is difficult to understand how to draw consequences from matching the risk appetite of the credit institution with the borrower's profile in the credit assessment. The former is formulated as an aggregate across all lending activities, while the latter depends exclusively on his individual circumstances. We suggest deleting this paragraph.
- Para. 100 should also foresee the possibility to include persons closely related to borrower and to look at the total picture such as for example in the case of household income.
- Paras 98, 101, 114, 121: The principle of proportionality should be introduced. Credit institutions should be allowed freedom in what elements to take into consideration in the context of a credit worthiness assessment. Indeed this is the expression of the credit institutions own expertise and risk appetite. The information outlined in para. 98 should therefore be seen as a suggestion rather than as a minimum.
  Consequently, we suggest rephrasing the sentence as follows: "The creditworthiness assessment should cover, **for example** ~~at a minimum~~, an assessment of the borrower's

income, disposable income, financial situation and source of repayment capacity to meet contractual obligations".
A sensitivity analysis should not be mandatory for small ticket and/or short term loans. It is not necessary from the risk point of view due to the low credit amount and would unnecessarily increase the effort and make the lending process more expensive and slower. What is the overall aim of a loan level sensitivity analysis on revenues, or where should the bar be set? For instance, for bullet loans with a 1 year maturity, it is hard to justify performing a loan level sensitivity analysis on the basis of a link with the Probability Default.
Banks are used to dealing with information at the time of the origination. By setting a sensitivity analysis for granting a loan, the full credit assessment methodology is changed. This implies a comprehensive review of the methodology, the training of the risk analyst, the IT process and storage, and so on. This is not sustainable without a phase-in transition period. Until now, sensitivity analyses take part of the Stress test/Back test analysis which may lead to increase provisions. We would maintain such an approach.
Moreover and with regard to para. 121 (unsecured lending to consumers), for most consumers, income comes from wages. The adverse impact is an unemployment situation where the loan is not granted anymore in most cases. Indeed, unemployment compensation covers basic consumption needs and leaves no room of manoeuver for granting a loan. Thus, this paragraph appears inapplicable for consumers. It is not relevant to assess a credit loan on unemployment compensation to be sure that the borrower will able to pay in adverse circumstances. It looks inapplicable to define the same approach for consumers as for an enterprise or any professional activities.
For the above reasons, we suggest rephrasing the sentence as follows: "When assessing the borrower's ability to meet obligations under the loan agreement, the institutions and creditors should **consider** carr~~y~~**ing** out sensitivity analyses reflecting potential negative scenarios in the future, including, for example, a reduction of income; an increase in interest rates in the case of variable rate loan agreements; negative amortisation; balloon payments, or deferred payments of principal or interest." With regard to the phase-in transition period, please refer to our comments on the timeline of the Guidelines.

- Para. 103: It is important to remember that, unless the consumer is able to provide information on what "variability" could occur, a lender cannot reasonably be expected to know how a particular consumer's situation evolves over time.
- Paras 105 and 118 introduce a presumption of responsibility of the lender's part in the event of borrower's default, by suggesting that the lender took part in the borrower's hardship or over-indebtedness. It implies that in the event of payment difficulties or over-indebtedness of the borrower it would be concluded that the creditworthiness assessment had not been appropriately carried out by the creditor.
  In addition, it is very difficult for lenders to assess whether undue hardship (which seems a vague principle to apply in practice) and over-indebtedness will occur, because in the vast majority of cases the causes are beyond the lender's control, resulting from macro-economic factors and accidents of life.
  We suggest rephrasing the second part of the paragraphs as follows: "**Institutions** ~~The factors~~ **should take reasonable effort to consider** ~~include~~" the various factor indicated in the paragraphs.
- According to para. 107 (Section 5.2.2 "Lending to consumers relating to residential immovable property") and para. 119 (Section 5.2.4 "Unsecured lending to consumers"), if the loan term extends past the borrower's expected retirement age, the institutions and creditors should take appropriate account of the adequacy of the borrower's likely income and ability to continue to meet obligations under the loan agreement in retirement. It should be clarified in this regard that institutions should only then be required to take due account

of the adequacy of the borrower's likely income in retirement if the loan agreement significantly exceeds the retirement age. If, for example, a loan has a duration of twenty years and exceeds the retirement age only by one year, it would be inappropriate to require institutions to consider the borrower's income in retirement. It must be ensured that the requirement to take account of the adequacy of the borrower's likely income in retirement does not discriminate against people who are near the retirement age. Even today, lending to elderly people and especially lending to pensioners is only allowed under restrictive conditions and therefore shouldn't be further restricted. Hence, paras 107 and 119 should be amended as follows: "If the loan term extends **significantly** past the borrower's expected retirement age, the institutions and creditors should take appropriate account of the adequacy of the borrower's likely income and ability to continue to meet obligations under the loan/credit agreement in retirement."

- According to para. 108 (Section 5.2.2 "Lending to consumers relating to residential immovable property") and para. 120 (Section 5.2.4 "Unsecured lending to consumers") institutions and creditors should ensure that the borrower's ability to meet obligations under the loan agreement is not based on the expected significant increase in the borrower's income unless the documentation provides sufficient evidence. The documentation requirement is problematic insofar as it prohibits considering an increase in a borrower's income in the near future, when it cannot be documented. Especially young borrowers, whose income in the future is likely to increase (but not documented), are restricted in taking up credit. In this regard the Guidelines should allow institutions and creditors to consider the specific circumstances of the individual case.
  We suggest rephrasing the paragraphs as follows: "The institutions and creditors should ensure that the borrower's ability to meet obligations under the loan agreement is not based on the expected significant increase in the borrower's income unless the documentation provides sufficient evidence~~.~~**, or the specific circumstances of the individual case indicate a future increase in the borrower's income**".
- In order to prevent age discrimination, the aspects mentioned in paras 107 and 109 should apply only to long-term (housing) loans.
- Para. 112: We understand the rationale of the proposed rules for under-construction property loans in Sections 5.2.3 and 5.2.6. Nevertheless, the requirements included in para. 112(b) and (c), which are similar to the requirements included in paras 166, 173 and 177, are burdensome and difficult to fulfil. Lenders have no data and cannot be responsible for assessing the quality of architects or engineers who take part in property development. Furthermore, certifying the costs associated with the development is not easy to obtain and could be very expensive for the borrower. We are of the view that it is the sole responsibility of the customer to assess the building project and not the responsibility of the bank. It would be excessive to oblige institutions to assess what laws are applicable in relation to a certain building project in order to assess all necessary permits and certificates. We would appreciate a clear statement in the final Guidelines that the proportionality principle is applicable to these paragraphs. We suggest rephrasing the paragraphs as follows: "Institutions and creditors should **take reasonable effort to consider"**.

Lending to professionals

- Para. 122: It is difficult to understand how to draw consequences from matching the risk appetite of the credit institution with the borrower's profile in the credit assessment as the former is formulated as an aggregate across all lending activities and the latter depends exclusively on his individual circumstances. We suggest deleting this paragraph.

- Para. 125 seems to imply a ban on loans with no repayment of principal until sale of the collateral. This would go beyond what these Guidelines are meant to do; this paragraph could be relevant for credit granted to people waiting for the end of the construction for starting to pay the new loan and for selling the previous property for instance. So called Crédit Relais in French. We appreciate that trade finance and bridge financing are excluded from the scope of this paragraph.
- Para. 126: While the need for a through creditworthiness assessment is clear, the principle of proportionality should be introduced. Credit institutions should be allowed freedom in what elements to take into consideration in the context of a credit worthiness assessment. Indeed this is the expression of the credit institutions own expertise and risk appetite. The information outlined in para. 126 should therefore be seen as a suggestion rather than as a minimum. We suggest rephrasing the sentence as follows: "When carrying out the creditworthiness assessment institutions should **consider** perform**ing** ~~at least~~ the following […]".
- Paras 127 and 132: As mentioned under Question 7 under para. 93, we believe the requirements to collect "financial projections" should be restricted to cases where this is relevant and possible; we would also highlight indeed that many of the requirements seem more geared for IRBA banks where some of these information are already or more easily available. For Standardised Approach banks, even considering the improvement of methodologies, the level to reach in this Guidelines is not proportionate to the activity considered and the staff. We suggest rephrasing the sentence as follows: "For the purposes of the analysis of the financial position within the creditworthiness assessment as specified above, institutions should consider ~~at least~~ the following: a. current and projected financial position, including income, cash flow and source of repayment capacity to meet contractual obligations, including**, where possible,** under possible adverse events […]". Concerning para. 132, the sentence would be as follows: "For the purposes of the analysis of the financial position within the creditworthiness assessment as specified above, institutions should consider ~~at least~~ the following: a. both current and projected financial position, especially**, where possible,** the capacity to meet contractual obligations under possible adverse events […]".
- The applicability of para. 130 (ESG) will depend on a reference framework defining what these risks are and how they impact credit risk, which is yet to be fully developed. Banks are dependent on the outcome of other work streams in this area, and it should be avoided that they are expected to develop too strict methodologies or approaches that may need to be revised shortly after, as the regulatory and supervisory framework in this area are in the making.
- According to para. 131 institutions should ensure that the analysis is based on tangible facts and not on an expected significant increase in the borrower's income unless there is sufficient evidence. According to this requirement, it would be impossible to grant a credit to an entrepreneur who has a convincing new business model but cannot grant sufficient evidence for his future increase in income. Against this background we suggest amending para. 131 as follows in order to allow the financing of new business models: "Institutions should ensure**, as far as relevant and proportionate,** that the analysis of the borrower's financial position is based on tangible facts and not on an expected significant increase in the borrower's income unless there is sufficient evidence~~.~~**, or the specific circumstances of the individual case indicate a future increase in the borrower's income."**

- Para. 134: the details' analyses require Senior Credit Analysts and a full review of the credit model. For IRBA, this framework exists, but for SA banks, the analysis models have to be built, the teams have to be trained, the IT framework to be created. For instance, the cash conversion cycle analysis goes beyond the net revenue analysis and financial capacity to pay the loan currently practices for SME loans.
- Para. 135: It should be clarified that the list of ratios is only indicative, not exhaustive, and that not all the ratios need to be used. This is particularly relevant especially with respect to the characteristics and amount of the transaction. Not to mention that difficulties may arise, for instance, from the calculation of DSCR (Debt Service Coverage Ratio) when estimating the cash flow available for debt service (e.g. business plans for a SME may not be available) and the amortization profile of third parties debt. We suggest rephrasing the sentence as follows: "Institutions**, where relevant and proportionate,** use ~~at least~~ the following financial metrics for the purposes of the creditworthiness assessment, and, where relevant **and possible**, assess them against the metrics and limits as set out in their credit risk appetite, credit risk policies, and limits in accordance with Sections 4.2 and 4.3".
  Moreover, no mention is made with regard to the documentation of the use of these metrics for credit decision purposes and their relation with existing rating systems of institutions.
  It has to be noted that internal models (both the authorised IRB ones for the calculation of capital requirements, those used only for rating purposes, and also the ones recently developed for the purpose of ECL estimation under IFRS 9) may not recur to the same metrics set out by EBA as in terms of predictive/explanatory value for the profile of the borrower other have been deemed more significant. It should be avoided that institutions find themselves having to implement new metrics in their models and/or having to fulfil contradicting requirements.
- Para. 143: Trying to anticipate potential adverse market events is a challenge due to the many variables that could enter into play during the duration of the loan agreement. We suggest rephrasing the sentence as follows: "Institutions should **consider** assess**ing, as far as relevant and proportionate,** the sustainability and feasibility of the borrower's financial position and repayment capacity under potential adverse market and idiosyncratic events that may occur in the duration of the loan agreement."
  Moreover and as further consideration with regard to paras 143 and 144, shall institutions consider that the ECL calculations leading to a provision already fulfil "potential adverse market condition"? In such circumstances, why to exacerbate the loan origination process? Conversely, since the sensitivity analysis "should be proportionate given the purposes, size, complexity, term and potential risk associated with the loan", we believe this would mean that institutions may result in having a part of the portfolio that will never require a sensitivity analysis. This would be sensible and should be made explicit.
  Similarly, the interest rate increase by 200 basis points takes part of the Stress Test analysis (para. 146). Why should we consider this scenario at the origination process whereas it is already performed at the portfolio level?
- Paras 145 and 146: It is not clear whether only some or all of the events should be considered. Using all the events would result in overestimation of risk and thus in severe limitation on the credit granting process. In particular, it will be difficult to obtain information about occurrence of severe management problems, the failures of significant trading partners, customers or suppliers and a significant reputational damage. We would like EBA to explicitly confirm that the proportionality principle as mentioned in para. 144 also applies to paras 145 and 146. We suggest rephrasing the paragraphs as follows:

  - Para. 145: "Institutions**, as examples and where possible,** should **consider** ~~take into account~~ the following idiosyncratic events".
  - Para. 146: "Institutions**, as examples and where possible,** should **consider** ~~take into account~~ the following market events".
- Para. 153: For banks using A-IRB models, correlation can exist between the borrower and the collateral. This should not prohibit them for taking into account such collateral as long as internal models enable to take into account the possible correlation.
- Para. 156: A due diligence of an agent in case of syndicated lending is against market standard and practice. The agent is never the sole issuer of guarantees or letters of credit in this kind of transaction. We suggest removing this requirement.
- Guidelines that are not proportionate to the size, complexity and type of loans/customers should be rephrased to include an "as far as possible"/"where relevant and proportionate" wording, such as paras: 123, 125, 126 (b, c, g, h), 128, 129, 130, 131, 132, 133, 134, 135, 143, 144, 148, 149, 150, 151, 157, 158, 159, 160, 161, 163, 168 and 179. In addition, the requirements for SME customers in 138-141 (for simplified accounting) are unproportional to micro businesses and SMEs in retail segment and would not allow for automatic decision making.
- With regard to para. 163(c) "capital expenditure risk and obsolescence risk", the sensitivity analysis on CRE may go beyond a bank expertise: on one hand, the mortgage should have an insurance against damage; on the other hand, the bank has to re-evaluate the mortgage to take into account the market value. Thus, the introduction of obsolescence risk on CRE could be removed.
- Paras 170 and 179: An audit of equity providers should only be required where there is an obligation to make additional contribution.
- Para. 176: The definition of specialised lending presented compared to the one in the CRR is too prescriptive. We consider that project finance security packages should be assessed as a whole to ensure that specialised lending conditions are met.

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

Our answer to Question 7, especially with regard to the applicability of the proportionality principle, should also be recalled to reply to this question. Any work should take into account the specific nature and characteristics of the products concerned. Consumer loans are typically of short duration and relatively low value, and must be distinguished from other types of loans such as mortgage credit. In accordance with the principle of proportionality, the assessment should reflect the size of the loan; any principles should also be sufficiently flexible to adapt to the specificities and frameworks of the local markets.

Moreover, we would like to restate that it is premature to impose such an extensive list of requirements when the European Commission is undergoing the evaluation of the CCD and has just started reviewing the MCD.

Furthermore, the Guidelines should regulate the notions of "consumer" and "business" in line with relevant EU directives. These terms are defined under civil law. Since the subject of credit assessment is already regulated under civil law and the Guidelines will in this respect have effects on civil law, known definitions should be used.

We propose closer coordination between definitions given in these Guidelines and those in the Art. 4 of CRR and other relevant CRR Articles relating to the calculation of RWAs for credit risk. Even more so in consideration of the fact that certain elements may change due to the upcoming process of implementation of the final elements of the Basel III framework (Basel December 2017 agreement).

The definition of "Commercial real estate" (CRE) seems aligned with the ESRB/2019/3 recommendation. However, we have doubts that property for conducting own business as well as social housing is to be seen as commercial real estate. Particularly the case of social housing is recognised also in the Basel 2017 framework, para. 68 (pages 22-23). Also, the ESRB definitions are primarily aimed at macro financial stability - monitoring purposes and not specific for credit granting purposes. ESRB also acknowledges that the different types of CRE vary and have different risk profiles and the new definition therefore requires separate reporting break downs.
The link with the EBA Guidelines on NPE and forborne exposures management should be carefully assessed (e.g. as the word "renegotiated" might imply a conceptual connection with the definition of forborne exposures and since para. 6 mentions both 'throughout the life cycle' and 'monitoring performing exposures'), and the same goes for the connection with ECB credit underwriting data collection.
We would also highlight that the EBA could reflect to a larger extent the lessons learned following the ECB credit underwriting data collection exercise, for which a number of definitions have been established by referring to FINREP/COREP and statistical reporting. If definitions are not clear and consistent, once the Guidelines are finalised the implementation may lead to situations where the SSM, when performing benchmarking analysis and evaluating the overall adherence to the Guidelines, may have supervisory expectations that could lead to further changes.

With regard to our request for a closer coordination between definitions, this should also apply to the definition of "consumer" used in the Guidelines and that in Art. 3(a) of the CCD and Art. 4(1) of the MCD.

"Professional means non-consumer": We note a divergence of the vocabulary across the existing definition, depending on the different perspective (Consumer protection vs. Risk management). Examples are: Household instead of Consumer and Enterprise instead of Professional. There is already a lot of to do for maintaining clean data. If we mix the various approaches, operational mistakes will arise. Therefore, we would require a longer phase-in to ensure that the different date sources are aligned and we would recommend the EBA to align the definitions to the current relevant legal text (e.g. CCD, MCD, CRR, etc…).
As an example, the EBA could consider that the Commission Recommendation of 6 May 2003 concerning the definition of micro, small and medium-sized enterprises (2003/361/EC) is a good reference, as it defines enterprise "any entity engaged in an economic activity, irrespective of its legal form. This includes, in particular, self-employed persons and family businesses engaged in craft or other activities, and partnerships or associations regularly engaged in an economic activity."

A definition of lender should be included to ensure that also the subprime segment and day loans is included.

With regard to para. 180, it is unclear how the way loan documentation is designed plays a role in the creditworthiness assessment and could prevent the borrower from providing the lender

with incomplete information. Moreover, the requirement seems to impose on lenders a responsibility for the possible misrepresentation of the information provided by the borrower. However, the bank cannot be responsible when the consumer knowingly withheld or falsified the information.

Finally, with respect to para. 183, we note that it will be burdensome to document every decision in detail. If the key issues are weighed correctly in the presentation, then repetition is redundant. We suggest rewording the paragraph as follows: "Credit decision should be clear and well documented".

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

We see that overall Section 6 would represent a considerable interference with the conduct of business. While we understand that EBA must remain vigilant as to a pricing that integrates the risk borne, we believe that the proposed Guidelines go well beyond. We could only understand this Section if seen as a set of best-practices. Pricing (methodology and profitability calculation) should continue to be flexible and based on individual methods / approaches.

More generally speaking, in the context of low interest rates, even zero or negative, the overall requirements look far away from the market reality. Banks have less and less room for manoeuver for developing sophisticated pricing methodologies.

It should also be underlined that the objective of creditworthiness assessments is indeed to determine whether the customer has the capacity, in terms of his personal and professional situation, to repay the proposed loan. It is at the very heart of the credit institution's expertise to ensure, as accurately as possible, that the client will be able to repay the loan. On the other hand, the pricing policy of an institution should not be confused with the credit risk management or treated as such by the EBA.

Here again, any move towards a standardization of rates based on risk profiles will inevitably lead to a reduction in access to credit, to the detriment of the most atypical customer profiles. This standardization will also prevent for instance the offsetting of the cost of risk across different categories of customers reducing the flexibility of the bank in responding to the market.

We fear that the orientation is to only focus on risk in order to reduce it regardless of the return. But risk cannot be decoupled by the idea of appropriate return. In practice, pricing must also take into account competition, and it is also necessary to evaluate the profitability by customer and not by service or deal (e.g. the margins on real estate loans are currently extremely tight, but fees contribute to the profitability). The expertise of each institution should not be overlooked, as well as the global customer relationship, and the risk of exclusion, we should avoid that a single distribution model is promoted by supervisory expectations. Moreover, the EBA requirements would be very difficult to implement when dealing with practices, for instance, such as promotional rates in consumer credit, as these do not necessarily cover the various components listed by the EBA, including the cost of refinancing. Finally, with regard to consumer credit, the introduction of customer segment pricing and their risk profile while easier to apply on a short chain (BtoC), it is much more complex on a long distribution chain (BtoBtoC = intermediated credit distribution via retail partner, small sales partners and car dealership partners). In fact, for intermediated distribution, pricing is also the subject of negotiation with the intermediary credit partner.

We see that the consideration of credit risk costs and cost of capital in the loan pricing is indeed a crucial element. This can only stress, in a different context, the fact that the upcoming implementation of the 2017 Basel reforms of the credit risk framework will have consequences on the credit provision to the real economy and the competitiveness of EU banks vis à vis other international players.

It should also be considered that, with regard to para. 187, those institutions applying national GAAPs do not methodically apply expected loss models. Thus, this would mean that the necessary parameter estimates (including product or segment-specific migration profiles) would first need to be established with great cost and effort. Furthermore, it is important that the parameters listed in para. 187 do not turn into an obligation to define minimum pricing thresholds for every single transaction depending on the level of risk.

In addition, with regard to paras 188, 189 and 190, should be mindful of the practices of each institution. We appreciate that EBA recognises the fact that business units (and types of loans) can cross subsidize others, however banks may account for cost allocation in a different manner.

The guidelines should reflect the fact that though capital and funding costs would impact the profitability of a given loan for an institution and hence influence its initial willingness to lend, the actual pricing of the loan would be subject to wider considerations like for instance market competition.

It should also be noted that, for consumer loans which are very widely distributed through a network of sales intermediaries (car dealerships, large retailers), the pricing applied to the final consumer are often not those established by the lending institutions as publicized. Indeed, the business partners are likely to take on a part of the customer pricing in order to offer preferential rates to their customers. The EBA guidelines do not take this element into account.

It should not be forgotten that in many respects already the risk appetite framework and the overall profitability profile of the institution take such elements into account. In general, such requirements need an adequate timeframe to adjust to which is not compatible with the aim of compliance by 30 June 2020.

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

As stated in other sections, the EBA Guidelines are overly prescriptive and go beyond the current requirements set by level 1 legislation.

On the valuation of immovable property collateral as defined in paras 191 to 200, the requirements are not compliant with the MCD. In particular, the following paragraphs require special attention:

- Para. 191: It should be clarified exactly what is meant by "origination" in this paragraph i.e. whether "origination" means the accurate date and time of the evaluation of the collateral, and not the moment of disbursement.
- Para. 194: This paragraph goes beyond the MCD, which does not require a valuation for the granting of credit, but rather seeks to ensure that where a valuation is conducted it is done so in accordance with specific standards. As such, this paragraph should be aligned with the MCD.

In general, as no calculation methodology is formally specified for the LTV, we understand every institution can use its own justified and established calculation methodology.

We appreciate the reference to the requirements for monitoring of the value of collateral to Art. 208 CRR. This is particularly relevant as it would play a role also in the implementation of the revised Basel III framework in the EU. Particularly, this would point in the direction of Option 2 of the policy recommendation of EBA (27 of the credit risk SA) from its response to the Commission call for advice (i.e. allow upwards adjustments of collateral).

Indeed, we believe that credit amortisation and development of immovable property should be considered for LTV purposes and the monitoring of the value. As a result, institutions should be able to adopt a lower LTV when the credit is substantially amortised (outstanding loan amount is reduced) and/or a building has been partially constructed (the value of the collateral is increased).

In this vein, *Basel III: Finalising post-crisis reforms* mentions both situations in para. 62, according to which "modifications made to the property that unequivocally increase its value could also be considered in the LTV" and "When calculation the LTV ratio, the loan amount will be reduced as the loan amortises". Furthermore, we see the risk that the combination of Basel IV requirements and the requirements set in Section 7 of the Guidelines could push lenders to enter into lending activities with less collateral because of the administrative burden, or also in order to remain competitive with other parties to whom these Guidelines do not apply. It should also be noted that there might be a shifting of volumes towards other credit granting parties to whom these guidelines do not apply.

In addition, we also have to note that the overall requirements need considerable adjustment to avoid translating in an excessive administrative burden that may also not be justified for certain categories of loans or credit decisions. In the Guidelines there appears to be no distinction between cash flow based lending and asset based lending. It seems disproportionate to apply all requirements to cash flow based lending. In our view, the strict requirements for valuation are also not needed to the same extent when the collateral is not taken into account in LGD models.

Another issue is the valuation with respect to leasing. A lease company is an asset based company, and provides financing for the purchase amount of the asset. So in principal, a valuation is not deemed necessary, as the financing amount equals the purchase amount (which equals the market value, whereby checks are performed on the market conformity of the purchase price).

Furthermore, for immovable collateral valuation must be independent, whether internal or external. The external valuations used are often indices (e.g. including statistics of notaries) or independent valuers, in some countries for outstanding amounts exceeding € 3 million, which does not seem compatible with the proposals of the draft Guidelines. For both movable and immovable collateral the requirement of the rotation of valuers is problematic. This change in market practices is particularly difficult to implement and would come at a huge additional cost for the activities affected. It is essential, in ensuring high quality, that the valuers obtain a deep knowledge of specific local real estate markets – hence the same immovable property could be monitored/revalued by the same valuer over a significant time period in order to maintain and enhance knowledge of the market.

Also, requirements for monitoring and revaluation of immovable property allow for the use of statistical models. However, the CP does not allow for the use of advanced statistical models for valuation purposes at origination, even though these models produce reliable results. Disallowing their use would in our view not contribute to making banks' lending standards more robust.

Instead, it would result in additional costs, without direct benefits to the client and the bank. For asset classes where advanced statistical models have proven to be reliable, we advise EBA to allow a continuation of use. A strict restriction on the use of those models can hamper the development in such markets and the overall progress of the valuation market. In addition, it should be noted that for residential mortgages national legislation[2] allows to determine the value at origination of the credit based on a statistical model and purchase price of the property (for which the LTV is capped at to 90%). The EBA Guidelines cannot conflict with national regimes.

With regard to para. 194, the EBA should clarify that the wording refers only to "asset reliant" CRE financing. The EBA should recognise the fact that institutions would not find it necessary or expedient to obtain independent property valuations for properties that are not pledged against the loans extended to real estate borrowers. The guidelines should clarify that such valuations need not be considered necessary for property that is not pledged (hence, there is a need for clarification or removal of the word "irrespective" in para. 194). Also, it is not clear whether the EBA requires an individual valuation of all collateral irrespective of whether it is used in the LGD models for capital relief. In our view, the strict requirements for valuation in this section should not be of the same extent in case the collateral is not taken into account in LGD models.

With regard to para. 196, we understand that this paragraph is applicable to lending for professionals. When mortgage lenders enjoy a strong protection in relation to borrowers (strong legal right of recourse and in the practice of enforcement), an assessment on the liquidity (except from an updated LTV) and enforceability of the collateral seems unnecessary.

The implementation of a panel of accepted external appraisers (para. 197) should be seen as a recommendable option for immovable property to ensure the quality of the valuation and the valuers but not as mandatory precondition for eligibility. Also, an indemnity insurance (para. 198) is not market practice in every country and it is not needed to ensure valuation quality. It is questionable whether banks should ensure that external valuers have adequate insurance in place.

Para. 199 should be adjusted to accommodate the situations where the legal framework allows the borrower to deliver an independent valuation report and where the lender relies on audited financial statements (accounting values). In both paragraphs, the required quality could be ensured in different alternative ways.

The requirements of para. 199 seem to disregard the reality of loans such as syndicated financing or receivables from other banks in which another bank is or was the actor of the property valuation. We believe that credit institution should not have to carry out or commission the valuation itself in such situations. A formal and material review of the submitted report should be sufficient.

We believe that para. 200 should be clarified indicating that the requirements are applicable for risk relevant lending decisions. In case of non risk-relevant lending decisions, the requirements of para. 200 letter (b) and (f) should not be mandatory. Furthermore a brief description of the collateral, its location and local market position is adequate. The legal attributes of the collateral can be assessed with a simple checklist.

The Guidelines mention that the use of models at the stage of loan origination may create shortcomings in the risk management. However, the concern of insufficient level of transparency

[2] e.g. Dutch legislation: Article 115 Besluit Gedragstoezicht Financiële Ondernemingen WFT

and inadequate governance in relation to these methodologies employed can be relieved by requiring adequate mitigating measures regarding model performance and quality assurance. We consider therefore that there is no need to forbid the use of these models when they have proven to produce reliable results. We see that in the future, it is expected that the progress in information technology and development of large property and transaction databases will increase the precision of advanced statistical models. A strict restriction on the use of those models can hamper the development of this market and the overall progress of the valuation market.

Regarding moveable property collateral, in our view, the book value of collateral items can serve as the primary source of information. Financial data is – by nature – highly reliable, as the processes that generate them are bound by numerous assurance measures, including independent external audits. Moreover, the appropriateness of these valuations can be evidenced (via back-testing) and it cannot be concluded that any other method (i.e. valuer or advanced statistical model) will result in more accurate valuations. Our understanding is that also EBA would see that book value can be used for movable assets (other than vessel and aircrafts), but we would ask EBA to explicitly describe this in the final guidelines.

To further underline this, we would like EBA to clarify the scope of Section 7.1.2. Where the requirements are relevant for the explicitly mentioned examples of moveably collateral (e.g. vessels, aircrafts, etc.), they are less relevant for others types of moveable collateral (in particular less standardized / comparable types as other means of transportation or inventories with low individual values) and commodities.

We see that in para. 201 should be specified that for insignificant credit risks and standardized loan agreements, institutions shall define de minimis thresholds for the individual valuation and use of simplified procedures.

Similarly, in para. 214 for less significant credit risk decisions, a rotation of valuers should not be mandatory. Moreover, it should be noted that some institutions employ and rely on one valuer to operate economically. Mandatory rotation would therefore result in disproportionately high costs for institutions without significant benefits regarding the valuation of the immovable collateral. Institutions should be allowed to define de minimis limits and use of simplified procedures. Moreover, we believe if the rotation of valuers is introduced the rules should at least be less stringent than the ones for auditors. One should consider the well-established provisions applicable to auditors as a valuable source for a similar provision regarding the rotation of the valuer. Additionally, a cooling-off-period for excluded valuers, which should not exceed two years, to make their reappointment possible should be included. For example, instead of creating new and differing rules, the rotation requirement in Article 17 (1) and (7) of Regulation (EU) No 537/2014 of the European Parliament and of the Council of 16 April 2014 on specific requirements regarding statutory audit of public-interest entities and repealing Commission Decision 2005/909/EC should be considered[3].

We therefore suggest requirements applicable to valuers should not be more stringent than respective requirements for auditors as statutory audit is a key aspect for the validation of proper

[3] "*1. A public-interest entity shall appoint a statutory auditor or an audit firm for an initial engagement of at least one year. The engagement may be renewed.*
Neither the initial engagement of a particular statutory auditor or audit firm, nor this in combination with any renewed engagements therewith shall exceed a maximum duration of 10 years. […]
7. The key audit partners responsible for carrying out a statutory audit shall cease their participation in the statutory audit of the audited entity not later than seven years from the date of their appointment. They shall not participate again in the statutory audit of the audited entity before three years have elapsed following that cessation."

management and creditor protection. In fact, the valuation of collateral, if anything, could be addressed less stringently than statutory audit.

The requirement to form panels of accepted external valuers (para. 203) is disproportionate and impracticable, if possible at all, for many types of collateral due to the lack of qualified valuers and the heterogeneous nature of collateral. We also note that while such requirement is included in the ECB NPL guidance the draft EBA Guidelines address loan origination which have a wider scope. Indeed, in certain market sectors such as the automotive sector, major independent and recognised players carry out the valuation of vehicles taken as collateral for credit, without having to resort to several of them alternately. We would also welcome a clarification indicating that appraisers of affiliated valuation companies are to be regarded as external, qualified and independent.

With regard to paras 207-213, the approach to valuation would completely modify the current perimeter of identification applied to collateral subject to revaluation and the frequency of the update. Due to the significant gap between the current and new proposed approach, further potential changes would require high IT budget allocation and banks would not expect to meet the EBA proposed deadlines for the new guidelines.

In addition, we believe that in para. 208 it should be clarified that "appropriate frequencies for monitoring the value of the collateral" is aligned with the requirements on monitoring of property values at a minimum once every year for commercial immovable property and once every three years for residential property according to Article 208(3)(a) CRR.

Additionally, we would like to point out that the frequency of the obligations of the borrower to provide the institution with information should be aligned with the frequency of monitoring the value of the collateral in order to facilitate the monitoring process with up-to-date information and to make a monitoring consistent with CRR requirements feasible.

Para. 211 seem to suggest the impossibility to use statistical valuation alone but only in conjunction with expert valuation say, which seems redundant and unnecessary. Where statistical methods have proved to be reliable their use should be allowed.

With regard to paras 209 and 215, we believe it should be clarified that the required evaluations can be conducted on pooled/aggregated data. This would be relevant for banks with common risk methodology and pooling data arrangements (e.g. members of an IPS). We would also stress that banks should not establish separate policies and procedures but be allowed to take a more comprehensive approach if appropriate to the nature and complexity of their business.

Para. 224 requires the continuous assessments of the performance of valuers. The added value of this requirement is unclear to us. Also it is unclear how banks could apply this requirement in practice. Institutions should be allowed to rely on other mitigating measures to ensure quality and independence of the appraisal such as (external) validation institutes or codes of conducts of national association of external valuers.

The wording should at the very least be adjusted as follows: "Institutions should assess the performance of the **external** valuers on a periodical basis, in particular accuracy of valuations provided. As part of such assessments, institutions should also look at the concentration of valuations performed and **variable** fees paid to specific valuers."

The requirement of no relation between the appraiser and the buyer or seller of the property in para. 225 could be made part of the contracts between Bank and appraisers but not realistically ensured.

Q12: What are the respondents' views on the proposed requirements on monitoring framework (Section 8)?

The ongoing monitoring requirements proposed by the EBA draft Guidelines are excessively complex and elaborate, this is not justified when put in relation to the average size of loan portfolios.

In line with CRR and EBA/GL/2017/16, we consider that the EBA should make a distinction in the requirements set in Section 8.2 when the borrower is a consumer and when it is a professional. In addition, we would like the EBA to clarify for Section 8 which paragraphs refer to a requirement on exposure or borrower level (i.e. we need to consider this at origination and for individual monitoring) and which paragraphs are referring to a portfolio and reporting perspective.

The requirements are overall very wide and granular and particularly difficult to comply with for all institutions taking in due account the proportionality principle, not only for small and medium-sized institutions, not to mention that all banks would have to face costs that are not proportionate with the loss risk of the transactions. The materiality of the risk of credit loss should be taken into account to a greater extent.

Regarding Article 229(e), without the roll-out of a unique and unambiguous data model and data dictionary, institutions cannot be held accountable that their credit risk monitoring framework allows for the use of peer group analysis. In addition, not all data as indicated in this Section can be used for comparison across other institutions: one example is the number of exceptions to credit policies, as credit policies of different institutions might be more or less strict.

Concerning para. 231, we understand that the terms "should at least cover" would allow banks to define themselves their framework based, for examples, on the items indicated, as this would provide room for implementing adequate internal policy, the EBA could clarify this better.

Also, the outlined approach to early warning indicators and watch lists does not seem suitable for adequately taking into account the different characteristics of institutions and customer groups. The requirements appear in many parts only practical for corporate customers.

In general, we would also stress that the ongoing monitoring should not lead to additional reporting requests from the supervisors which would add to the administrative and reporting burden.

Also, it should be better specify whether and in which situation the Warning on Monitoring should be performed at portfolio level or at loan level. We would also welcome a clarification on how the supervisory expectations related to the watch list (para. 266) translate, i.e. would it require a first part on monitoring and reporting (therefore mainly at portfolio level), and a second part seem for operational actions/assessment?

With respect to the key risk indicators in para. 263, we believe that the list should not be seen as exhaustive nor as a ticking box to be performed point by point. In some instances the indicators do not allow for a timely detection of increased credit risk in the aggregate portfolio. For example, a significant drop in turnover would have a temporary lag that would not ensure promptness.

We see that the monitoring of covenants is explicitly mentioned and that a violation of the covenants or a late submission of the declaration of compliance with the covenants is a trigger in the early warning system pursuant (para. 253), and also non-financial collateral agreements are monitored (para. 254). We understand the aim to include an explicit requirements for the monitoring of covenants, this, however, requires the technical mapping of these instruments. Credit institutions often face the challenge of missing data budgets for covenants due to the use of manual workarounds.

The comprehensive requirements for stress testing (para. 255 and seq.) and the expected granularity cannot be met at reasonable cost for banks in the timeframe envisaged by the draft Guidelines and taking into due account the proportionality principle. Special employee qualifications, IT systems and data structures are needed that can only gradually be built up. The institutions' internal stress testing are part of the wider SREP framework and their adequateness and frequency should be seen in the context of the wider supervisory dialogue.

We understand the more concrete requirements with regard to the early warning systems and the associated indicators. However, banks are faced with the challenge of revising the early warning system, taking into account the regulatory requirements for NPL management (EBA Guidelines and ECB guidance), and the EBA definition of default. This requires to take a wide angle perspective on the needed changes stemming from the regulatory framework, again the timeline for this should be long enough to allow for consistent and sound results.