

EBA BSG 2017 012

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Banking Stakeholder Group

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Location: London

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EBA-Unrestricted

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## Banking Stakeholder Group – Minutes

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### Item 1.: Welcome and adoption of the agenda

1. EBA chairperson and BSG chair welcomed BSG members. The agenda and the minutes of the last BSG meeting were approved.

### Item 2.: BSG update on the latest developments

#### A) BSG Chairperson update on recent developments

2. BSG Chairperson informed that he was approached by the Chair of the ESMA Stakeholder Group with a view to sending a common letter on the Joint Consultation Paper on suitability of management body in addition to the response provided by both Stakeholder groups independently to this consultation.
3. He suggested to allocate the various ongoing consultation papers as follows:
  - Consultation on Guidelines on supervision of significant branches (EBA-CP-2016-24) under the WG on Capital, Liquidity and risks;
  - Consultation on RTS on CCP to strengthen fight against financial crime (JC-2017-08) under the WG on Supervision, Governance, Reporting and Disclosure;
  - Consultation on Guidelines on procedures for complaints of alleged infringements of the PSD2 under the WG on Payments, Digital and Fintech;
  - Ad-Hoc Working Group on regulatory sandbox has been set up.

#### B) Update of BSG Technical Working Groups' Activities

4. The leader of the Working Group on Consumer Protection explained the position expressed by the BSG on the consultation paper on Technical Standards on standardised terminology
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and disclosure documents under the PAD. The leader of the Working Group on Capital, Liquidity and Risks described the BSG response to the consultation paper on PD estimation, LGD estimation and treatment of defaulted assets. The leader of the Working Group on Payments, Digital and Fintech informed of the development of the work on big data and regulatory sandboxes. The leader of the Working Group on Supervision, Governance, Reporting and Disclosure recalled the main points of the response to the consultation paper on internal governance and suitability of management body.

### Item 3.: EBA update on general developments

#### A) The EBA Chairperson's update on general developments

5. The EBA Chairperson informed that a general discussion on the future of the European Supervisory Authorities (ESAs) should take place soon as the European Commission considered issuing a consultation paper with different options regarding the tasks or the architecture of the ESAs. The BSG was invited to submit its views in due time.
6. In light of the discussion on the new CRR/CRD/BRRD proposal, the EBA Chairperson described the approach followed to express the views of the EBA in this process. It was noted that the EBA did not intend to comment on topics for which EBA stances were already public but should focus on specific issues through letters or opinions addressed to the European institutions.
7. It was mentioned that the RTS on Strong Customer Authentication was approved by the EBA's Board of Supervisors. Changes were introduced to the previous version, including extension of exemptions.
8. With regard to Panama papers, it was noted that there were different interpretations amongst the supervisors about their role when dealing with tax evasion, tax crime or supervisory cooperation across the EU. Some concerns were raised regarding the difficulty to access information on subsidiaries because of the severity of rules governing data protection in some countries.
9. The EBA chairperson mentioned the dissent between the European Commission and the EBA regarding the proposed amendments to the final RTS on the separation of payment cards schemes and processing entities under the Interchange Fee regulation (IFR).
10. The BSG chair mentioned the possibility to submit a common paper with ESMA on the European Commission's consultation regarding the future of ESAs. Some BSG members raised their concerns about the exemptions embedded in the RTS on Strong Customer Authentication and the difficult balance between usability and security. On IFRS 9, one BSG member showed his sympathy for a dynamic approach rather than the static approach chosen by the EBA.

## B) Update on risks and vulnerabilities in the EU

11. EBA staff introduced the presentation by flagging two key challenges for the EU banking sector, namely low profitability and access to funding. It was mentioned that the CET 1 ratio continued to increase driven by continuous growth of capital and decrease of RWAs. However, it was also highlighted that profitability of EU banks was still subdued, in particular in a context of low interest rates, increasing IT costs and a sharp competition. Regarding the stock of non-performing loans (NPLs), the trend was reported to be downwards albeit slowly. It was noted that huge differences were perceptible across jurisdictions, bank models and asset classes. The total of NPLs reaches more than 1 trillion in the EU, which is a problem for the EU economy and actions on three fronts are needed. These are 1) supervisory action to push banks to address their stock of NPLs, 2) structural issues, 3) addressing market failures in secondary markets for NPLs.
12. Possible actions for tackling the NPL problems were then discussed. One BSG member raised the issue of a non-transparent framework of selling portfolios of NPLs by banks. It was mentioned that banks are selling NPLs with huge discounts (95% or even more), without offering consumers the opportunity to pay their debts with a discount too. A focus was on the public sector actions ranging from the improvement of data quality available on NPLs to the setting up of a single EU Asset Management Company (AMC). Regarding the latter, some clarification was provided on how such an entity could manage NPLs.
13. BSG members in general welcomed the proposal of an EU AMC, with some voices also raising concerns. They asked questions about:
  - Consumers' perspectives in the whole exercise,
  - Technical questions like differences between real economic value and market price of NPLs, the impact of NPL sales on LGDs, about the idea of a 3Y deadline for an EU AMC,
  - Feasibility of an EU Single AMC as certain EU countries have a low ratio of NPLs and do not have any appetite for the establishment of this type of entity, and others have already set up their own AMC.
  - Possible tools to increase transparency of assets quality.
14. Some concerns were raised about the context of banks' low profitability and at the same time the increase of high earners amongst the bankers. The EBA Chairperson explained that the data on high earners reflect a significant impact of EUR/GBP exchange rates, since most high earners are based in the UK.
15. Regarding the establishment of an EU Single AMC, EBA staff clarified that mutualisation of losses among EU member states was not part of the proposals. However, it was indicated that the current level of NPLs was worrying and constituted a significant problem for the EU real economy. Benefits of a single AMC were put forward as it would address market failures

in the secondary market by addressing asymmetry of information, providing clarity and consistency of the State Aids regime, credibility of the process of solving the NPLs issue and attracting cheaper funding. The concept of real economic value versus market value was also discussed.

16. On the NPLs issue, the EBA chairperson considered that the EU should ensure a right balance between the application of the newly-issued measures and the recourse to State Aids to avoid the experience of a Japanese scenario.

#### Item 4.: Consumer protection, financial innovation and payments

17. EBA staff presented several ongoing consultation papers. Regarding the Consultation Paper on the EBA Guidelines on Procedures for Complaints of Alleged Infringements of PSD2 recently published, EBA staff clarified the scope of the Guidelines. It was noted that the Guidelines were addressed to Competent Authorities (CAs) and should govern the process of the complaints submitted to CAs by payment service users and other interested parties about the alleged infringements by Payment Service Providers (PSPs) of Payment Service Directive 2 (PSD2). EBA staff informed that the consultation period was open until mid-May 2017 and that a response by the BSG, and the consumer representatives in particular, would be greatly appreciated.
18. Regarding the Consultation Paper on the EBA Guidelines on Incident Reporting under PSD2 applicable to CAs, it was indicated that the purpose was to deal with the information about incidents that CAs should share with the ECB and EBA. It was mentioned that, within the Guidelines, a separate set of requirements was applicable to PSPs on the classification of major incidents and on the content, the format, including standard notification templates, and the procedures for notifying such incidents. BSG members were requested to provide their comments by 7 March 2017.
19. One BSG member observed that static criteria for the classification of major incidents were not relevant for the biggest organisations.
20. Regarding the publication of the 2017 Consumer Trends Report, EBA staff recalled the considerations behind dropping the publication of the report in 2017.
21. Given the importance certain consumer associations have recently attached to the report, the EBA has reconsidered its position. Consequently, EBA staff informed that a “light” version of the report would be published in June 2017 and presented the modified methodology and content. It was noted that separate questionnaires would be sent out soon to national consumer associations and national competent authorities to be completed by early April 2017.
22. BSG members raised some concerns regarding the lack of statistical information in this “light” version of the report. Indeed, those BSG members viewed that statistics were a key source of information for regulators and politicians to better design regulation and the collection of data

was a key task of the EBA. They asked questions as to how the EBA envisaged collecting national consumer associations' views on the emerging risks in terms of consumer protection. The EBA chairperson clarified that BSG consumer representatives might help the EBA in the process of selecting the relevant national consumer associations. Some members supported the effort made by the EBA to focus on the enforcement of regulatory products in the area of consumer protection, but expressed their concerns about the reprioritisation of collection of statistics.

23. On the Consumer Protection Day scheduled on 23 June 2017 in Prague, BSG members welcomed the choice of place to organise the event in a CEE country. One BSG member called on the EBA to involve consumers even more than the envisaged plan of one consumer representative per panel while another cautioned that this would squeeze out the industry from the panels. EBA staff responded that the current plan achieves the desired balance of views that the ESAs envisage and that no changes will therefore be made. Some of them suggested discussing some topics such as cooperation between CAs and consumer associations, cross-border financial services, PRIIPs, mis-selling of financial products or improvement of the financial literacy of consumers with a view to disseminating best practices.

24. On big data, EBA staff informed that the three ESAs had published a Discussion Paper on 19 December 2016, with a submission deadline of 17 March 2017. It was noted that the ESAs would use the feedback received in order to decide which, if any, action was required to mitigate the risks while at the same time allowing participants to harness the potential benefits. The responses received to the EBA Discussion Paper on "Innovative uses of consumer data" might be combined with 'big data'.

25. On Dynamic Currency Conversion, the BSG Vice-Chair described the phenomenon as a service offered by payment service providers when a consumer withdrew cash in an ATM or when a consumer is paying at an E-POS and it is subject to high additional fees applied on currency exchange rate, when the cardholder is using its card denominated in other currency. He provided some concrete examples to illustrate this issue and suggested drafting a paper by end of March.

## Item5.: Discussion on general topics

### A) Implementation of the bail-in tool

26. A BSG presentation explained the interplay between EU State Aid and BRRD rules in recapitalisations. First it analysed the requirements of both the 2013 Banking Communication of the European Commission and the BRRD in terms of bail-in and public support. Then, it outlined the European Commission's proposals to amend the BRRD, focusing on key aspects such as relationship between Total Loss Absorbing Capacity (TLAC) and Minimum Requirements on Own Funds and Eligible Liabilities (MREL), level of MREL, or the effects of MREL shortfall. Lastly, he highlighted the possible implications of the BRRD framework for

investors since resolution of an institution may cause the bail-in of financial instruments that they hold. It also focused on self-placement practices and considered that investors should be better informed to clearly understand the underlying risks of such financial instruments.

27. Some BSG members commented on the loopholes of the 2013 Banking Communication illustrated by the recent ruling from the EU Court of Justice. They expressed their concerns about the self-placements and the possible need for regulating or banning those practices. Some members questioned about the perception of banks' risks by the market. One member insisted that precautionary recapitalisations illustrated the bail-in limits. Another member expressed the concerns of retail investors who needed further guidance to buy those instruments.

28. The BSG presenter responded to questions by flagging that there were difficulties during the transitional period to assess correctly the perception of risks. Once fully operational, the presence of a minimum requirement for eligible liabilities (MREL), placed to informed investors, may facilitate the assessment of risk. On the possible measures used to minimise the cost of remedying a capital shortfall, it was noted that the terminology was generic enough to cover a broad range of measures and referred to the conversion into equity of subordinated bonds for example. He considered as excessive the proposal to ban self-placements, even though he agreed on the need for regulation.

29. The EBA chairperson informed BSG that the EBA was working with the ESMA on the topic of bonds being held by retail customers. He informed that one of the policy options being under review was to consider subordinated bonds being held by retail customers as an impediment to resolvability. He also expressed the fact that banks had not bought back those bonds that are held by retail customers victims of mis-selling practices. The BSG presenter replied that one of the reasons the banks did not do so was due to the probably lower cost of self-placed bonds with respect to comparable market-placed bonds.

## B) Discussion on floor-rate clauses in mortgage loans with variable interest rates

30. One BSG member presented the issue triggered by floor-rate clauses in mortgage loans with variable interest rates. The floor-rate clause (or ground clause) was defined as a minimum interest rate below which the interest rate paid by the consumer could not go, even if the market rate dropped below that figure. It was noted that a minimum percentage was charged by the lender, even though the interest rate emerging from the sum of the reference rate plus the margin was lower. As a consequence it was noted that the floor-rate clause prevented borrowers from taking advantage of the market variation. In some cases, it was reported that the credit agreement contained only a floor-rate clause and no ceiling clause. In that case, there was an imbalance between the contracting parties handicapping the borrower. The BSG member called for more information in order to draw attention of the borrower to that before signing the contract. Some concrete examples from various jurisdictions were used to illustrate the issue.

31. Some BSG members shared their views and raised two key issues, transparency and fairness of terms and conditions of those loans. One member observed that recent court rulings in some countries against floors have introduced legal uncertainty that may jeopardise the functioning of mortgage markets that were so far quite efficient. Other members made a link with the banks' funding costs and this kind of practices.

## C) Discussion on Brexit

32. One BSG member presented his views on the role of the UK in the EU financial services to demonstrate its significance in the EU financial services network. He also explained benefits of the London cluster by mentioning London's unique ecosystem which would be very difficult to replicate elsewhere in Europe due to its access to substantial global capital pools, its historic financial infrastructures, its clustering effects, and its depth of the international talent pool with technical and multicultural background.

33. He considered that breaking up the current set-up would lead to higher capital requirements and operational costs, lower ability for international banks to provide increased lending, reduced access to markets for debt and equity placement.

34. He also presented the impacts on international financial services, national government (in terms of financial stability and fiscal balance for example) and regulators due to possible increased supervision complexity/uncertainty, and fragmentation in regulatory oversight and supervision. Amongst the key priorities, he mentioned market stability and confidence through the implementation of an orderly and transparent negotiation and exit, broad cross border market access, continued regulatory cooperation between the UK's domestic regulators and the EU's regulatory regime, secure and timely arrangements for continued access to third country markets. Some specific issues were also raised such as passporting and possible transitional arrangements.

35. Some BSG members commented on:

- costs of the Brexit for the other Member States,
- risks in terms of consumer protection as UK consumers would no longer be protected by EU law,
- costs for small and medium-size companies and innovative start-ups in particular in this competitive period,
- future of the EBA.

36. The EBA chairperson indicated that some issues might emerge in the context of Brexit such as a risk of regulatory arbitrage between the EU jurisdictions to attract business and a threat on continuity of cross-border business. He mentioned that the role of the EBA would be to ensure the smooth functioning of the supervisory and regulatory framework in place. Regarding the



future location of the EBA, the Executive Director clarified that a change to the EBA Founding Regulation was needed before the moving of the Authority and that the EU co-legislators would have to agree upon an European Commission's proposal. He indicated that a speedy decision with a long transition period was the preferred option from the EBA's perspective to ensure a smooth business transition.

## Item 6.:EBA update on other regulatory deliverables

### A) Internal Governance and Remuneration

- 37.EBA staff presented the results of the consultation paper on the Guidelines on the assessment of the suitability of members of the management body and KFH, informing that the Guidelines were expected to be finalised by mid-2017 and applicable by the end of 2017.
- 38.It was noted that the revised Guidelines were taken into account the findings of the peer review exercise, in particular on the extension of the scope of assessments to some specific Key Function Holders (KFH), the application of an ex-ante assessment process before the appointment of members of the management body and KFH with some exceptions duly justified, the implementation of interviews by CAs for significant firms and a stricter definition of independent directors.
- 39.It was indicated that the Guidelines should also provide guidance on some CRDIV requirements such as time commitment, collective knowledge of the management body, resources for induction and training and policy on diversity. EBA staff also flagged the main comments received during the period of public consultation. Common areas which the EBA has received comments on are the ex-ante assessment, the independence requirements and the composition of board committees.
- 40.EBA staff reported the main findings of the EBA's report on high earners completed with 2015 data. EBA staff observed that the number of high earners receiving remuneration of more than EUR 1 million increased significantly (33.04%) mainly driven by changes in the exchange rate between EUR and GBP. It was also noted that the largest population of high earners in the EU, was located in the United Kingdom (80.4% of the total number of high earners). Regarding the percentage of high earners who were considered to be identified staff, EBA staff noted that it remained relatively stable, representing 86% of all high earners. However, the average ratio of variable to fixed remuneration for all high earners was reported on a significant upward trend.
- 41.One BSG member stated that the requirements imposed on cooperative banks were irrelevant and very burdensome. Another member questioned about the possibility to disclose more granular information on remuneration such as level of remuneration, policies implemented by institutions in terms of remuneration, compensation and performance. Another member drew the attention on the attractiveness of board of directors that the Guidelines should not hamper.



## B) Overview of the EBA's completed and ongoing work on internal models

42. EBA staff presented the current status of the review of the IRB Approach. The whole process of the regulatory review of the IRB Approach was described from the starting point of minimising RWA variability. The work on supervisory practices was concluded with the finalisation of the assessment methodology, the introduction of a common definition of default and now moving to the finalisation of the estimation of risk parameters – the BSG was in this regard given preliminary feedback on the BSG opinion. Finally, the EBA was starting a review of the Credit Risk Mitigation (CRM) framework in order to further harmonise it.

43. EBA staff also presented the main findings of the 2016 Supervisory Benchmarking on Internal Models. It was reported that two reports on credit and market risks would be published during the next days and would present detailed results. It was noted that the sample of institutions was increased for this exercise, covering for the first time the entire population of banks in the EU that use internal models for capital requirements purposes. For credit risk, most of the RWs variability, and similar to previous exercises, were explained through few drivers, including the share of defaulted exposures, the share of non-EU exposures, and the portfolio-mix. EBA staff also flagged the result of the comparison of observed and estimated values, i.e. the outturn (backtesting) approach, indicating that on average the estimated values for PDs and LGDs were higher than the observed, i.e. conservative values for the estimation of risk parameters, however more studies need to be conducted. The annual EU benchmarking exercise is a supervisory tool that is helping in the assessment of the quality of the internal models and supervisory actions are expected, according to the Competent Authorities' assessment of the exercise and its main findings.

### Conclusion

44. BSG Chairperson recalled the dates of the two next meetings, namely the BSG meeting on 2<sup>nd</sup> May and the joint BSG/BoS meeting on 3<sup>rd</sup> May. Some topics for the joint meeting were suggested by BSG members, such as the role of home/host supervisors in the EU and the disruption triggered by Fintech in the banking industry.

### Participants:

**Chair** – Santiago Fernández de Lis, BSG Chairperson

Mike            Dailly            Govan Law Centre

Mark            Roach            ver.di

Fryni            Michael            Cyprus Consumers Association

Sergio	Iugaresi	italian banking association
Nikolaos	Daskalakis	GSEVEE
Sabine	Masuch	Association of Private Bausparkassen
Martin	Schmalzried	COFACE
Arnold	Kuijpers	Rabobank
Peter	Mülbert	University of Mainz
Alin	Iacob	Association of Romanian Financial Services Users (AURSF)
Michel	Bilger	Crédit Agricole
Gerda	Holzinger- Burstaller	Erste Group Bank
Giovanni	Petrella	Catholic University, Milano
Christophe	Nijdam	Independent
Giedrius	Steponkus	Lithuanian Investors association
Monika	Marcinkowska	University of Lodz
Jesper Bo	Nielsen	FSU-DK
Santiago	Fernández de Lis	BBVA
Søren	Holm	Nykredit
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Dominic	Lindley	
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Cédric Coraillon-Parquet  
Anna Gardella  
Christopher Mills  
Bernd Rummel  
Larisa Tugui