



EBA/CP/2014/27

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# Consultation Paper

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Draft Guidelines

on payment commitments under Directive 2014/49/EU on deposit  
guarantee schemes

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# 1. Responding to this Consultation

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The EBA invites comments on all proposals put forward in this paper and in particular on the specific questions summarised in 5.2.

Comments are most helpful if they:

- respond to the question stated;
- indicate the specific point to which a comment relates;
- contain a clear rationale;
- provide evidence to support the views expressed/ rationale proposed; and
- describe any alternative regulatory choices the EBA should consider.

## Submission of responses

To submit your comments, click on the 'send your comments' button on the consultation page by 02.01.2015. Please note that comments submitted after this deadline, or submitted via other means may not be processed.

## Publication of responses

Please clearly indicate in the consultation form if you wish your comments to be disclosed or to be treated as confidential. A confidential response may be requested from us in accordance with the EBA's rules on public access to documents. We may consult you if we receive such a request. Any decision we make not to disclose the response is reviewable by the EBA's Board of Appeal and the European Ombudsman.

## Data protection

The protection of individuals with regard to the processing of personal data by the EBA is based on Regulation (EC) N° 45/2001 of the European Parliament and of the Council of 18 December 2000 as implemented by the EBA in its implementing rules adopted by its Management Board. Further information on data protection can be found under the Legal notice section of the EBA website.

## 2. Executive Summary

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Directive 2014/49/EU of the European Parliament and of the Council of 16 April 2014 on deposit guarantee schemes (henceforth 'DGSD'), establishes that the available financial means to be taken into account, in order to reach the target level required under Article 10 of DGSD, may include payment commitments as defined in point (13) of Article 2(1).

Under Article 10(3) of DGSD, EBA is required to issue guidelines on payment commitments, in order to ensure consistent application of the Directive.

These guidelines have to be issued in accordance with Article 16 of Regulation (EU) N.º 1093/2010 of the European Parliament and of the Council, of 24 November 2010 (the "EBA regulation").

The main aspects covered by these draft guidelines are set out below:

- Main terms to be included in contractual or statutory arrangements for the provision of payment commitments by credit institutions to a DGS;
- The powers of the DGS, at the occurrence of an enforcement event, to realise or appropriate the low-risk assets provided as collateral;
- The terms of the delivery of the low-risk assets provided as collateral by the credit institution to the DGS, which should be fulfilled by means of a deposit of the collateral (i) with custodians, identified by the designated authority or by the DGSs and (ii) on a securities account held by the DGS specifically destined to the registration of low-risk assets provided by credit institution in fulfilment of the payment commitments;
- The criteria enabling the DGSs to assess the inexistence of third party rights on the low-risk assets provided by credit institutions as collateral of the payment commitment;
- The criteria for eligibility and management of the collateral, since, pursuant to the DGSD, DGSs can only accept low-risk assets as collateral to secure the payment commitment. As a result, these draft guidelines include provisions requiring DGSs and designated authorities to determine appropriate criteria on the eligibility of the collateral, taking into account, for example, credit and market risks of the issuers of the low-risk assets and also the liquidity of those assets;
- These draft guidelines also provide, in Part 7, that DGSs and designated authorities should always apply a haircut to the value of the low-risk assets provided as collateral. This implies that the value of the underlying asset is calculated as the market value of the asset less a certain percentage (haircut). For this purpose, and without prejudice to other schedules or procedures, the haircut schedules for assets eligible for use as collateral by central banks is offered as a possible reference;

- Finally these draft guidelines require competent authorities to mitigate any potential advantage that could stem from the prudential treatment of payment commitments as compared to contributions paid in cash.

These Guidelines will be finalized following the outcome of a 3 month consultation period, by [•] at the latest.

### 3. Background and rationale

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Directive 2014/49/EU of the European Parliament and of the Council on deposit guarantee schemes ('DGSD'), was published in the Official Journal of the European Union on 12 June 2014.

DGSD aims at "harmonising the methods of financing DGSs"<sup>1</sup>, via a mix of ex ante and ex post contributions. As provided in recital 34, in order to guarantee that the available financial means of DGSs reach the target level, *"It should be possible for the available financial means of DGSs to include cash, deposits, payment commitments and low-risk assets, which can be liquidated within a short period of time"*.

Pursuant to Article 10(3) of the DGSD, the available financial means to be taken into account in order to reach the target level of the DGS may include payment commitment not exceeding 30% of the total amount of available financial means raised in accordance with that Article.

The Commission services have interpreted this provision as laying down an obligation for Member States to provide DGSs with the ability, through a power to accept payment commitments up to 30% of the available financial means. In any event, national authorities are bound to implement EU law in an objective and non-discriminatory criteria and therefore those principles should also underpin the application to banks of criteria for the admissibility of payment commitments. This does not mean that no difference can be applied between banks but such differences should be linked to objective differences.

Under point (13) of Article 2(1) of DGSD, payment commitments are defined as *"payment commitments of a credit institution towards a DGS which are fully collateralised providing that the collateral: (a) consists of low risk assets; and (b) is unencumbered by any third-party rights and is at the disposal of the DGS"*. In order to ensure consistent application of the previous mentioned provisions, Article 10(3) mandates the EBA to issue guidelines on payment commitments.

Payment commitments are a novelty in the EU regulatory framework on deposit guarantee schemes as well as in most Member States.

It is important to ensure, on the one hand, that DGSs and designated authorities follow the compulsory requirements that are foreseen under DGSD when including payment commitments within the available financial means of DGSs, and on the other that consistency in the criteria and procedures is achieved in order to establish a level playing field, prevent regulatory arbitrage and promote legal clarity.

Accordingly, these guidelines endeavour to provide guidance on the legal instruments which should be entered into by DGSs and credit institutions, providing for the terms and conditions for the inclusion of payment commitments within the available financial means of the DGS, so that it is guaranteed, for instance, that the DGS has an irrevocable right to claim those payments on demand, and that the collateral is unencumbered by any third-party rights and at disposal of the

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<sup>1</sup> Recital 27.

DGS. These guidelines also aim to provide criteria on the eligibility and management of the collateral regarding, for example, the valuation haircuts which should be applied in the valuation of underlying assets.

## 4. Draft EBA Guidelines on Payment Commitments

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### Status of these Guidelines

This document contains guidelines issued pursuant to Article 16 of Regulation (EU) No 1093/2010 of the European Parliament and of the Council of 24 November 2010 establishing a European Supervisory Authority (European Banking Authority), amending Decision No 716/2009/EC and repealing Commission Decision 2009/78/EC (the EBA Regulation). In accordance with Article 16(3) of the EBA Regulation, competent authorities and financial institutions must make every effort to comply with the guidelines.

Guidelines set out the EBA's view of appropriate supervisory practices within the European System of Financial Supervision or of how Union law should be applied in a particular area. The EBA therefore expects all designated authorities and deposit guarantee schemes (DGSs) to whom these guidelines are addressed to comply with them. Designated authorities and DGSs to whom these guidelines apply should comply by incorporating them into their practices as appropriate (e.g. by amending their legal framework or their processes).

### Reporting Requirements

According to Article 16(3) of the EBA Regulation, competent authorities must notify the EBA as to whether they comply or intend to comply with these guidelines, or otherwise with reasons for non-compliance, by [•]. In the absence of any notification by this deadline, competent authorities will be considered by the EBA to be non-compliant. Notifications should be sent by submitting the form provided at Section [•] to [compliance@eba.europa.eu](mailto:compliance@eba.europa.eu) with the reference [•]. Notifications should be submitted by persons with appropriate authority to report compliance on behalf of their competent authorities.

Notifications will be published on the EBA website, in line with Article 16(3).

## Title I - Subject matter, scope and definitions

1. Article 10(3), subparagraph 2, of Directive 2014/49/EU of the European Parliament and of the Council of 16 April 2014 on deposit guarantee schemes (hereafter 'DGSD') mandates the EBA with the task to issue guidelines on payment commitments. For this purpose, these Guidelines provide terms to be included in the contractual or statutory arrangements for the provision by credit institutions of payment commitments to the benefit of a DGS, as well as the criteria for eligibility and management of the collateral.
  2. These Guidelines are addressed to DGSs and designated authorities, as defined in point (1) and (18) respectively of Article 2(1) of the DGSD, and to resolution authorities as defined in Article 4(2), (iv) of Regulation (EU) No 1093/2010 of the European Parliament and of the Council establishing the European Supervisory Authority (European Banking Authority) as subsequently amended ('EBA Regulation'). They are also addressed to competent authorities within the meaning of Article 4(2)(i) of Regulation 1093/2010 insofar as the prudential treatment of payment commitments is concerned. These Guidelines apply in accordance with the national legal framework on the inclusion of payment commitments within the available financial means to be taken into account in order to reach the target level.
  3. If the operation of the DGS is administered by a private entity, designated authorities should verify that, according to the law governing such arrangement, the DGS enjoys the creditor's protection afforded by Directive 2002/47/EC of the European Parliament and of the Council of 6 June 2002 on financial collateral arrangements, amended by Directive 2009/44/EC of the European Parliament and of the Council of 6 May 2009 (hereafter the 'Financial Collateral Directive').
  4. Resolution authorities should inform designated authorities that when exercising their powers in accordance with Articles 69, 70 and 71, of Directive 2014/59/EU establishing a framework for the recovery and resolution of credit institutions and investment firms, they shall give due consideration to ensuring effective creditor protection to the DGS.
  5. For the purpose of these Guidelines the following definitions apply:
    - i. "Payment Commitments" has the same meaning as set out in point (13) of Article 2(1), of the DGSD, i.e. payment commitments of a credit institution towards a DGS which are fully collateralised providing that the collateral: (i) consists of Low-Risk Assets; (ii) is unencumbered by any third-party rights and is at the disposal of the DGS;
    - ii. "Low-Risk Assets", has the same meaning as set out in point (14) of Article 2(1) of the DGSD, i.e. items falling into the first or second category referred to in Table 1 of Article 336 of Regulation (EU) No 575/2013 or any assets which are considered to be similarly safe and liquid by the competent or designated authority, including cash, financial instruments and credit claims fulfilling the abovementioned requirements;
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- iii. “Payment Commitment Arrangement” means the arrangement to be entered into between the DGS and the credit institution, providing for the terms and conditions for the inclusion of payment commitments of a credit institution within the available financial means of a DGS, and in particular (i) the indication by the DGS of the Payment Commitment Amount and (ii) the credit institution’s irrevocable and collateralised obligation towards the DGS to immediately and unconditionally pay the Payment Commitment Amount at the DGS’s request;
- iv. “Payment Commitment Amount” means the share and the monetary amount of the contribution to the DGS as indicated by the DGS, which the credit institution undertakes to provide by means of the Payment Commitment under the terms and conditions of the Payment Commitment Arrangement;
- v. “Security Financial Collateral Arrangement”, consistently with the definition set forth in Article 2(1), (c), of the Financial Collateral Directive, means an arrangement, governed by the law transposing the Financial Collateral Directive, under which the credit institution secures the obligations undertaken in the Payment Commitment Arrangement by provision of Low-Risk Assets collateral by way of security to the DGS, where the full ownership of the Low-Risk Assets collateral remains with the credit institution when the security right is established;
- vi. “Title Transfer Financial Collateral Arrangement”, consistently with the definition set forth in Article 2(1), (b), of the Financial Collateral Directive, means an arrangement, governed by the law transposing the Financial Collateral Directive, under which the credit institution secures the obligations undertaken in the Payment Commitment Arrangement by transferring the full ownership of the Low Risk Assets to the DGS. The collateral may consist of securities or cash;
- vii. “Financial Collateral Arrangement” means a title transfer financial collateral arrangement or a security financial collateral arrangement
- viii. "Enforcement Event", means at least (i) the failure by the credit institution to pay the Payment Commitment Amount within the period provided under the Payment Commitment Arrangement when required to do so by the DGS; or (ii) the occurrence of any event referred to in Part 3, paragraph 13, letter (d) of these Guidelines, entailing the acceleration of the obligation to pay the Payment Commitment Amount so as to become immediately due. Under the terms of the Financial Collateral Arrangements and consistently with Article 2(1), letter (l) of the Financial Collateral Directive or by operation of law, the occurrence of an Enforcement Event entitles the DGS to realise the Low-Risk Assets collateral provided by the credit institution by way of sale or of appropriation without the need of prior jurisdictional notice or authorisation.

## Title II - Guidance on Payment Commitments

### Part 1 – General considerations

6. The DGSD aims at harmonising the methods of financing DGSs<sup>2</sup>, via a mix of ex ante and ex post contributions.
7. Pursuant to with Article 10(3) of the DGSD, the available financial means to be taken into account in order to reach the target level of the DGS may include payment commitments, provided the total share of payment commitments does not exceed 30% of the total amount of available financial means raised in accordance with that Article.
8. This provision implies an obligation for Member States to provide DGSs with the power to accept payment commitments up to 30% of the available financial means. Article 10(3) of the DGSD, should not be read as an automatic right for credit institutions, opposable to the DGS, to provide their contributions in the form of payment commitments. The DGS should implement this mechanism on the basis of non-discriminatory criteria. In particular DGSs should not accept more than 30% of a given member's ex ante contributions to be made in the form of payment commitments.
9. Designated authorities should verify that Payment Commitment Arrangements and Financial Collateral Arrangements entered into by the DGS and the credit institution are consistent with these Guidelines.

#### Questions

1. Apart from the admissibility requirements suggested in the present guidelines, which objective criteria do you think could be applied, notably in order to determine the overall amount of payments to be accepted in a given year, or to be applied to individual banks applying for the option?

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<sup>2</sup> Recital 27 of the DGSD

## Part 2 – The Payment Commitment Arrangement

10. The admissibility of Payment Commitments should be conditional upon the conclusion of individual written Payment Commitment Arrangements between the DGSs and their member institutions. The Payment Commitment Arrangement may be concluded each year, or included into a master arrangement that is amended or supplemented each year to take into account new calls for ex ante contributions.
11. The Payment Commitment Arrangement should at least include the following elements:
  - a) The Payment Commitment Amount;
  - b) The irrevocable obligation for the credit institution to make the promised cash payment of the Payment Commitment Amount at any time, upon simple and unconditional request of the DGS, without undue delay and at any rate no later than 2 working days from the receipt of the notice pursuant to letter (c) below. Such payment period is reduced to 1 working day in case early intervention or crisis management measures are applied on the credit institution by the competent or resolution authority. The arrangement should preclude any reduction in the Payment Commitment Amount, or any termination of the Payment Commitment Arrangement, without the consent of the DGS.
  - c) The provision of a notice by the DGS to the credit institution by any effective means of communication ensuring receipt, whenever the DGS claims the cash payment of the Payment Commitment Amount;
  - d) The obligation for the credit institution to immediately communicate to the DGS any event affecting the institution's ability to honour its obligations, or the DGS's ability to enforce its rights, under the Payment Commitment Arrangement or the Financial Collateral Arrangement, including the institution's downgrades by external credit rating agencies and any material prudential or business changes or any deterioration in the value of the Low-Risk Assets provided as collateral;
  - e) The conclusion of a Security Financial Collateral Arrangement or a Title Transfer Financial Collateral Arrangement between the DGS and the credit institution securing the obligations undertaken by the credit institution in the Payment Commitment Arrangement, by way of provision by the credit institution to the DGS of Low-Risk Assets collateral, that are unencumbered by any third-party rights and are put at the disposal of the DGS.

### Questions

2. Do you agree with these provisions to be included in Payment Commitment Arrangements? Do you think other provisions should be provided?
3. Do you agree that a credit institution should pay in cash the Payment Commitment Amount, when its obligation becomes due, within 2 working days at the latest?

### Part 3 – The Financial Collateral Arrangement

12. In order to safeguard the DGS's creditor position, a Financial Collateral Arrangement should explicitly include the following contractual terms:
  - a) The credit institution undertakes to substitute the Low-Risk Assets provided as collateral when they fall due, when they no longer comply with the requirements laid down in Part 6 and 7 of these Guidelines or in other specific cases agreed upon with the DGS, so that the Payment Commitment is permanently secured by appropriate collateral;
  - b) In case of Security Financial Collateral Arrangement, the credit institution is not allowed to dispose of the collateral (e.g. sale, encumbrance);
  - c) The credit institution is required to top up the Low-Risk Assets provided as collateral upon request of the DGS, in the event the value of the underlying collateral asset, after the haircut provided for in Part 7 of these Guidelines, or in consideration of the applicable exchange rate in case of cash collateral, falls below Payment Commitment Amount;
  - d) The provision of Enforcement Events as defined in Title I, para. 5, point (viii) of these Guidelines. Pursuant to point (ii) of such definition, the obligation of the credit institution to pay the Payment Commitment Amount is accelerated so as to be immediately due, at least when:
    - (i) The credit institution fails to replace the Low-Risk Assets provided as collateral when they fall due, when they no longer comply with the requirements laid down in Part 6 or Part 7 of these Guidelines, or in the other specific cases agreed upon with the DGS;
    - (ii) The credit institution fails to top up its collateral when required to do so by the DGS, in the event of a breach of the coverage level, as laid down in Part 7 of these Guidelines;
    - (iii) The authorisation of the credit institution is withdrawn;

- (iv) The credit institution is no longer a member of DGS;
- (v) The credit institution is subject to reorganisation measures other than early intervention or crisis management measures, or is being wound up.
- e) At the occurrence of an Enforcement Event, the DGS should realise or appropriate the Low-Risk Assets provided as collateral in accordance with the terms of the Financial Collateral Arrangement;
- f) The DGS should release and return the Low-Risk Asset collateral upon cash payment by the credit institution of the Payment Commitment Amount.

#### Questions

4. Do you agree with the option left to the DGS to enter into a Security Financial Collateral Arrangement (full ownership remains with the credit institution) or a Title Transfer Financial Collateral Arrangement (full transfer of ownership)?

#### Part 4 - Delivery of the collateral by the collateral provider to the DGS

13. Under the Financial Collateral Arrangement, the DGS should ensure that the credit institution delivers the Low-Risk Assets to the DGS in accordance with one of the modalities provided in the Financial Collateral Directive as applicable, so that the Low Risk Assets are in the possession or under the control of the DGS.
14. Such delivery by the credit institution to the DGS should be fulfilled by means of crediting the collateral as follows:
  - a. In the case of a Security Financial Collateral Arrangement, the Low Risk Assets provided as collateral should be credited on a securities account (i) maintained with custodians or intermediaries, identified by the designated authority or by the DGS, that are able to provide complete, accurate and up to date information regarding both the credit institution and the Low-Risk Assets and (ii) held by the DGS specifically and destined to the registration of Low-Risk Assets provided by credit institutions in fulfilment of the Payment Commitments. The designated authority or DGS should ensure that custodians are not allowed to dispose of the Low-Risk Assets provided as collateral and that they have contractually waived any retention right or right of pledge they may otherwise have over the Low-Risk Assets.

- b. In the case of a title transfer financial collateral arrangement, a transfer to the DGS on a securities or cash account held by the DGS specifically destined to the registration of Low-Risk Assets provided by credit institution in fulfilment of the Payment Commitments. If a DGS is entitled to receive cash deposits from members, the cash collateral may be provided directly to the DGS by the credit institution. The designated authority or DGS should ensure that custodians are not allowed to dispose of the Low-Risk Assets provided as collateral and that they have contractually waived any retention right or right of pledge they may otherwise have over the Low-Risk Assets
15. For the purpose of a Security Financial Collateral Arrangement, DGSs or designated authorities should only accept custodians or intermediaries that ensure full segregation and protection of the Low-Risk Assets provided as collateral and enable the DGSs' prompt access to the financial instruments upon request. This in order to prevent any losses to the credit institution or to the DGS due to the default or insolvency of the custodian.

#### Questions

5. Do you think other requirements about the choice of the custodians should be provided under these guidelines?

#### Part 5 – Criteria to assess the inexistence of third party rights to the collateral

16. Point (13) of Article 2(1) of the DGSD provides that the collateral must be unencumbered by any third party right. Accordingly the DGSs and the designated authorities should not accept any Low-Risk Assets which are already encumbered or collateralised by means of pledge or other security arrangements.
17. The assets provided under a Financial Collateral Arrangement must be legally realisable without prior claim over the assets concerned. It should not be possible for third parties to intervene and successfully claim the assets pledged or any rights attached to them.
18. For that purpose the DGS should require under the Financial Collateral Arrangement that credit institutions warrant that no Low-Risk Asset provided as collateral is being simultaneously encumbered or used as collateral to the benefit of any third party or to secure another already existing obligation towards the DGS, and undertake that no asset used under the Security Financial Collateral Arrangement is given as collateral to any third party.

## Part 6 – Criteria for eligibility and management of collateral

19. Pursuant to the DGSD, DGSs should only accept Low-Risk Assets as collateral to secure the Payment Commitment Amount. DGSs and designated authorities should determine appropriate criteria on the eligibility of the collateral, taking into account the credit and market risks of the issuers of the Low-Risk Assets and the liquidity of those assets, so as to avoid illiquid assets such as asset backed securities. They should also take into account the concentration and currency risks.
20. DGSs or designated authorities should also provide exposure limits, ensuring for each credit institution a high diversification of the assets having regard, at least, to their issuer and maturity. For small institutions which are not able to deliver Low-Risk Assets compliant with the requirements regarding diversification and exposure limits, the level of diversification of the Low-Risk Assets delivered as collateral can be lower provided that a high overall level of diversification of Low-Risk Assets within the DGSs' portfolio is still met.
21. Notably, DGSs should limit their exposure to debt, whether public or private, issued in the country where the DGS operates, insofar as its value is highly correlated to events where the DGS would have to repay depositors or contribute to resolution and therefore might have to call in the payment commitment. However the currency of denomination of debt should not be considered for this purpose as it would place excessive constraints on the ability to provide collateral. For small institutions which are not able to deliver assets as collateral compliant with this requirement, in line with the principle of proportionality, the level of correlation could be higher, provided that the overall level of correlation within the DGS's portfolio remains low.

### Questions

6. Do you agree on the abovementioned requirements? Would you suggest other limits on concentration in exposures?
7. Is it in your view appropriate not to consider the currency of issuance when determining whether a debt instrument's value is correlated to an event of DGS pay-out, be it inside or outside the euro area?
8. Do you consider that the proposed wording correctly applies the concept of proportionality, or whether some limits to concentration should be envisaged also for smaller, locally operating banks?

22. In addition, DGSs and designated authorities should address in an adequate manner the differences, where they exist, between the currency of denomination of the collateral and the currency of denomination of the deposits covered by the DGS.

#### Questions

9. Do you agree with the criteria on the eligibility of the collateral provided in this Part 6? Do you think other requirements should be provided in these guidelines on this issue?

### Part 7 – Haircut

23. DGS or designated authorities should always apply a haircut on the value of the Low-Risk Assets provided as collateral, unless collateral is provided in cash in the same currency as the Payment Commitment. Thus the value of the underlying asset should be calculated as the market value of the asset less a certain percentage (haircut).
24. DGS should ensure that the haircut is related to the credit, market and liquidity risk arising from the exposure value of each asset. For that purpose, different haircuts should be determined having regard to the type of issuer and its credit quality, as well as to the maturity of the assets and to the currency of denomination.
25. The application of haircuts should also be based on a quantification of expected losses and the expected time lapse to the sale of the assets.
26. While a variety of haircutting schedules and methodology can be envisaged, the haircut schedule for assets eligible for use as collateral by central banks offers a sound solution.
27. DGSs or designated authorities should ensure that the value of the Low Risk Assets is marked-to-market on a regular basis, and possibly on a daily basis.
28. Furthermore, the haircut-adjusted market value of the Low Risk Assets provided as collateral should be maintained over time. This implies that if the value of the underlying assets marked to market on a regular basis falls below a certain threshold and no longer complies with the coverage ratio resulting from the application of the haircut, the credit institution should be required to supply additional Low-Risk Assets or replace the relevant part of the Payment Commitment with cash.
29. In any event DGSs or designated authorities are not precluded from imposing on member institutions additional reporting and notification requirements.

#### Questions

10. Do you agree with the criteria on the haircut provided in this Part 7? Do you think there are other requirements which should be provided under these guidelines about this issue?

### Part 8 – Prudential Treatment

30. The prudential treatment should ensure that the choice of institutions between cash payments and payment commitments is neutral from the prudential standpoint. To achieve this result the prudential treatment should be different depending on the way payment commitments are classified under applicable accounting rules.
31. While payments in cash will mechanically impact the profit and loss statement of credit institutions, payment commitments may receive different treatments under applicable accounting rules.
32. If, according to the accounting treatment, the payment commitment is fully reflected on the balance sheet (as a liability), or the collateral arrangement is fully reflected on the profit and loss statement, there should not be any need to apply an ad hoc prudential treatment to ensure equivalence with cash payments.
33. If, in contrast, according to the accounting treatment the payment commitment and the collateral arrangement remain off balance sheet, competent authorities should assess, within the supervisory review and evaluation process, the risks to which the capital and liquidity positions of the credit institution would be exposed should the DGS called upon it to pay the commitment, and exercise the appropriate powers to ensure that the payment commitment is treated in a way equivalent to the cash payment from the prudential standpoint.

### Questions

11. Do you agree with the prudential approach suggested? Would you suggest further details on the methodology to be applied, and if so which ones?

## Title III – Final Provisions and implementation

### Date of application

34. DGSs and designated authorities should implement these Guidelines by incorporating them in their practices within [•] after adoption. Thereafter, DGSs and designated authorities should ensure that these guidelines are applied effectively. The same implementation timeframe applies to resolution authorities and to competent authorities to the extent they are addressees of these Guidelines.

## 5. Accompanying documents

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### 5.1 Impact Assessment

#### Introduction

Article 10(3) of the DGS Directive requires the EBA to develop guidelines on payment commitments.

As per Article 16(2) of the EBA Regulation (Regulation (EU) No 1093/2010 of the European Parliament and of the Council), any guidelines developed by the EBA shall be accompanied by an annex setting out an Impact Assessment (IA) which analyses ‘the potential related costs and benefits’. Such annex shall provide the reader with an overview of the findings as regards the problem identification, the options identified to remove the problem and their potential impacts.

This annex presents the IA with cost-benefit analysis of the provisions included in the guidelines described in this Consultation Paper. Given the nature of the guidelines, the IA is high-level and qualitative in nature.

#### Problem definition and the baseline scenario

Under Article 10(3) of the DGSD, the available financial means raised by Deposit Guarantee Scheme (DGS) may include payment commitments. Under Article 2 (1), point 13, of the DGSD, the payment commitments of an institution towards a DGS must be fully collateralised and the collateral must consist of unencumbered low risk assets. The total share of the payment commitments should not exceed 30% of the total amount of available financial means of the DGS.

Currently the financing of DGSs is not harmonised. As a result many DGSs are only financed ex post. Where DGSs already rely on ex ante financing, their available financial may include cash, deposits, and low risk assets, which can be liquidated within a short period of time, but a minority of member states [DK, FR and PT] have instruments similar to payment commitments.

The DGSD requires Member States to provide DGSs or their designated authorities with the power to accept payment commitments as part of the financing modalities of the DGSs. If the provisions of DGSD on payment commitments were not to be transposed and implemented in a similar and consistent manner across Member States, the variations may lead to differences and uneven level playing field for institutions and DGS, and hence damage fair competition in the EU banking sector. For example, if the timeframe in which institutions have to make the cash payment for their commitments varies across jurisdictions then the institutions operating under a system which allows longer timeframe would have an advantage over their competitors subject to shorter timeframe. Similarly, if the similar underlying (low-risk) assets for collaterals are treated differently across jurisdictions, for example in terms of the application of haircuts, then the

differences may create uneven playing field. The same is true when the provisions regarding the enforcement events and the rights for the creditor rising there from are not harmonised across Member States. Inconsistent application of enforcement provisions when institutions are in breach of contract or of the provisions related to payment commitments may deteriorate market discipline.

Consistent and harmonised implementation of the elements in relation to payment commitments is a necessary condition in the EU banking sector with great cross-border dimension.

## Objectives

In line with Article 16 of the EBA Regulation, these guidelines aim at establishing consistent, efficient and effective practices, to ensuring the common, uniform and consistent application of the provisions of the DGSD Directive related to payment commitments.

Payment commitments are a component, although optional, of the policy mix foreseen by the DGSD for the financing of deposit guarantee. Therefore these Guidelines should be consistent and support the objectives underpinning the financing provisions of the DGSD as illustrated in recital

- Harmonising financing methods of DGSs
- Ensuring that the costs of financing are in principle born by credit institutions themselves and that the financing capacity of the DGS is proportionate to its liability
- Ensuring a similarly high level of protection for depositors in all Member States.

Within the framework of the objectives stated above, a crucial element is the common standards in the implementation of the DGS framework across Member States. Hence, the guidelines aim to introduce a set of common fundamental rules that the DGS and designated authorities across Member States can benchmark when they design payment commitment arrangements. Precisely, the guidelines aim to provide a common framework for the payment commitment and financial collateral arrangements, which should be entered into by and between the DGS and a credit institution, as well as the criteria for eligibility and management of the collateral. A common framework is also expected to enhance cross-border transaction and competitiveness in the EU banking sector.

## Technical options

In line with the problem definition, the following alternative approaches in the development of the guidelines were considered:

- a. **Collateral agreement**
  - Option 1a: Introducing the Security Financial Collateral Arrangement;
  - Option 1b: Not specifying any collateral arrangement;

- Option 1c: Introducing the Title Transfer Financial Collateral Arrangement.
- b. **Haircut schedule for the value of collaterals**
- Option 2a: Defining a specific haircut schedule;
  - Option 2b: Providing an option to DGS and designated authorities to adopt the haircut schedule for assets eligible for use as collateral adopted by central banks.
- c. **Treatment of sovereign bonds of collateral**
- Option 3a: Provision specific to sovereign bonds as collateral;
  - Option 3b: No specification on sovereign bonds as collateral.

### Assessment of the technical options

a. **Collateral agreement**

Introducing a specific contractual arrangement within the scope of payment commitments is more effective to achieve the harmonisation objectives. A specific contractual arrangement is also expected to contribute to the consistency in the implementation of provisions related to payment commitments. Not specifying any collateral arrangements leaves the choice at member states' discretion and fails to address the identified problems.

In this context, the Security Financial Collateral Arrangement has three main advantages. First, the contractual arrangement was introduced by the European Directive (2002/47/EC) and the transposition of the Directive is already completed. Therefore, Member States are expected to have high net benefit from the implementation of the Security Financial Collateral Arrangement in the framework of payment commitments.

Secondly, under the Security Financial Collateral Arrangement the DGS as creditor and collateral-taker improves its position since there are special rules concerning close-out netting provisions and winding-up proceedings and reorganisation measures against the collateral provider. Precisely, the Directive 2002/47/EC on financial collateral arrangements provides that a financial collateral arrangement, including pledges and the right arising there shall be valid from the start and during the winding-up proceedings and reorganisation measures against collateral provider.

In addition, under the Security Financial Collateral Arrangement, DGS and credit institutions may agree on some important elements of the contract such as the right to use, the right of sale or appropriation of the financial collateral on the occurrence of an enforcement event. Such contractual provisions may not be valid under a normal pledge arrangement designed under some national laws. For example, in some Member States [PT], the creditor does not have the right to realise the pledged assets on the occurrence of an enforcement event.

An alternative to the Security Financial Collateral Arrangement is the Title Transfer Financial Collateral Arrangement, whereby full ownership of financial collateral would be transferred to the DGS. In the framework of the payment commitments, such title transfer offers more direct access to the collateral for the DGS. On the other hand the securities will feature on the balance sheet of the DGS which will have to sustain possible fluctuations in value (until offset by further posting of collateral or cash compensation by the institution). In addition it is very demanding for the credit institution which loses the property of the collateral and the rights of gathering its proceeds. Therefore the advantage of a payment commitment collateralised through Title Transfer might be seen as very reduced compared to cash payments.

Considering these arguments, at the stage the guidelines offer an option between both a Security Financial Collateral Arrangement or a Title transfer financial collateral arrangement.

#### **b. Haircut schedule for the value of collaterals**

The Guidelines provide that the DGS should always apply haircuts to the value of the collateralised low-risk assets and the criteria on the haircut should be related, at least, on the credit, market and liquidity risk that these assets are exposed to. This suggests that different haircut levels should be set and applied according to the type of issuer, its credit quality, the maturity of the assets and the currency of the denomination.

The current IA considered as technical options designing provisions on haircut schedule specific to current guidelines (Option 2a), on one hand, and providing an option to DGS and designated authorities to adopt the haircut scheme of the current guidelines with the schedules used by central banks (Option 2b)<sup>3</sup>, on the other hand.

The cost of introducing a haircut scheme specific these guidelines is expected to be high and the marginal benefit of this approach is expected to be negligible, if positive at all. This is mainly due to the existence of well-established central banks haircut schemes in the EU.

The application of central banks haircut schedules would represent a useful practical reference as to how the haircut that should be applied. Credit institutions of Member States in the Eurozone and at least some DGSs (via Central Banks) are familiar with the ECB haircut schedule.

Given these arguments the preferred option is to offer the haircut schedule with the schedule adopted by central banks as an indicative compliant method (Option 2b).

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<sup>3</sup> Haircut schedule that is used in monetary policy.

Table 1 presents an overview of the advantages and disadvantages of the technical options considered in the IA.

**Table 1 Overview of the main advantages and disadvantages of the technical options**

| Policy area                                      | Technical options  | Advantages  | Disadvantages   |
|--|--|---|---|
| c. Collateral arrangement                        | Option 1a: Introducing the Security Financial Collateral Arrangement                             | <ul style="list-style-type: none"> <li>- Familiarity with the current practice in the EU</li> <li>- Harmonised framework</li> <li>- Low transition cost</li> <li>- Standardised contract increases transparency</li> <li>- Simple practice to handle cases</li> </ul>   | <ul style="list-style-type: none"> <li>- Less flexibility</li> </ul>  |
|  | Option 1b: option to use Security Financial Collateral or Title Transfer Collateral arrangements | <ul style="list-style-type: none"> <li>- No compliance cost</li> <li>- Flexibility</li> </ul>   | <ul style="list-style-type: none"> <li>- Lack of harmonised framework</li> </ul>  |
|  | Option 1c: Introducing the Title Transfer Financial Collateral Arrangement.                      | <ul style="list-style-type: none"> <li>- More direct access to the collateral for the DGS</li> <li>- Familiarity with the current practice in the EU</li> <li>- Harmonised framework</li> <li>- Low transition cost</li> <li>- Standardised contract increases transparency</li> <li>- Simple practice to handle cases</li> </ul> | <ul style="list-style-type: none"> <li>- DGS bears the risk of fluctuations in the value of the collateral on its balance sheet (until offset by further posting of collateral or cash compensation by the institution)</li> <li>- Less flexibility</li> <li>- Potential disadvantages for credit institutions related to transfer of full ownership of the financial collateral</li> </ul> |
| d. Haircut schedule for the value of collaterals | Option 2a: Defining a specific haircut schedule  | <ul style="list-style-type: none"> <li>- Full harmonisation</li> <li>- haircut scheme that is fit for purpose</li> </ul>  | <ul style="list-style-type: none"> <li>- Cost to design new scheme</li> <li>- Regulatory burden for the institutions and for the DGS/designated authorities</li> </ul>  |

|  |   |  |  |
|--|---|--|--|
|  | <p>Option 2b: Expressly provide the option to adopt the haircut schedule used by central banks.</p> | <ul style="list-style-type: none"> <li>- Aligning with other practices in the EU framework</li> <li>- Familiarity with the current practice in the EU</li> <li>- Harmonised framework</li> <li>- Low transition cost</li> <li>- Less volatile with respect to other schemes</li> </ul> | <ul style="list-style-type: none"> <li>- some DGSs and NCA outside the Eurosystem not familiar with the method</li> <li>- Cost of implementation for non-euro banks</li> </ul> |
|--|---|--|--|

## 5.2 Summary of the questions for consultation

1. Apart from the admissibility requirements suggested in the present guidelines, which objective criteria do you think could be applied, notably in order to determine the overall amount of payments to be accepted in a given year, or to be applied to individual banks applying for the option?
2. Do you agree with these provisions to be included in Payment Commitment Arrangements? Do you think other provisions should be provided?
3. Do you agree that a credit institution should pay in cash the Payment Commitment Amount, when its obligation becomes due, within 2 working days at the latest?
4. Do you agree with the option left to the DGS to enter into a Security Financial Collateral Arrangement (full ownership remains with the credit institution) or a Title Transfer Financial Collateral Arrangement (full transfer of ownership)?
5. Do you think other requirements about the choice of the custodians should be provided under these guidelines?
6. Do you agree on the requirements suggested for the eligibility of collateral? Would you suggest other limits on concentration in exposures?
7. Do you consider appropriate not to consider the currency of issuance when determining whether debt instruments are correlated to an event of DGS pay-out, be it inside or outside the euro area?
8. Do you consider that the proposed wording correctly applies the concept of proportionality, or whether some limits to concentration should be envisaged also for smaller, locally operating banks?
9. Do you agree with the criteria on the eligibility of the collateral provided in this Part 6? Do you think other requirements should be provided in these guidelines on this issue?
10. Do you agree with the criteria on the haircut provided in this Part 7? Do you think there are other requirements which should be provided under these guidelines about this issue?
11. Do you agree with the prudential approach suggested? Would you suggest further details on the methodology to be applied, and if so which ones?