EBA EUROPEAN BANKING AUTHORITY

EBA BSG 2017 001
Banking Stakeholder Group
8 December 2016/ 9:30 - 16:30
Location: London
EBA-Restricted

Banking Stakeholder Group –Minutes

Item 1: welcome and adoption of the agenda

1. The BSG Chairperson welcomed BSG members. The agenda and the minutes of the 24 October meeting were approved.

Item 2: BSG update on the latest developments

A) BSG Chairperson to update on recent developments and to allocate the work on the EBA's Consultation Papers

2. BSG Chairperson informed that no comments were received on the suggested changes to the current procedures for replying consultation papers circulated by email. It was decided that the BSG would apply those rules for the future.

3. The Chairperson sought BSG opinion on the ongoing EBA's Consultation Papers to be allocated. BSG decided not to respond to two Consultation Papers, one on additional monitoring metrics for liquidity (EBA-CP-2016-22), and the other on operational risk and sovereign exposures in supervisory reporting (EBA-CP-2016-20), whereas the Consultation Papers on a new prudential regime for investment firms (EBA-DP-2016-02), on authorisation and registration under PSD2 (EBA-CP-2016-18) were allocated for drafting responses.

4. BSG Chairperson also updated BSG members on the possible joint response with ESMA's stakeholder group with regard to the Joint Paper on suitability of management body. It was agreed exploring the possibility of a joint reply.

5. It was agreed to setup two technical working groups, one on regulatory sandboxes and the other on Dynamic Currency Conversion (see next point).

B) Update of BSG Technical Working Groups' activities

6. On the EBA's consultation on standardised terminology and disclosure documents under the PAD, it was noted that the draft opinion was circulated ahead of the meeting and should be finalised shortly. On Dynamic Currency Conversion, BSG members decided to set up a group mandated to draft a short paper describing the BSG position including concrete examples. BSG Vice-Chair committed himself to coordinate this informal group and would share the paper with the Working Group on Payments in a view to table it at one of the next BSG meetings.

7. On Capital, Liquidity and Risks, it was reported that the working group was working on the current consultations on the Guidelines for PD, LGD and defaulted assets.

8. On Reporting, Disclosure and Governance, it was mentioned that two consultations were subject to a BSG opinion, including the joint consultation on suitability of management body on which the BSG was exploring a joint reply with ESMA stakeholders.

9. On Fintech and Payment, it was agreed that it was of interest for the group to set up an Ad-Hoc Working Group on regulatory sandboxes. The EBA Chairperson explained that the EBA was developing a strategy on FinTech and intended to publish a white paper. Under those conditions, it was a perfect timeline to issue a BSG Opinion.

C) Presentation on the bail-in in Slovenian banks

10. One BSG member presented the case of bail-in in Slovenian banks. He underlined that the implementation of the bail-in tool across EU countries shows material divergences in the treatment of banks' shareholders and debtholders and that this implementation had been the most severe for Slovenian banks, where all shareholders and subordinated bondholders have been wiped out without compensation. He also questioned the effectiveness of the investors' protection under Bank Recovery and Resolution Directive (BRRD) in a context where there would be a large asymmetry of information since banks and competent authorities refused to disclose relevant information.

11. BSG members provided their comments on this particular case and the implementation of the resolution framework in general. Several members argued that the implementation of the bail-in tool creates retroactive effects. Some of them argued that the bail-in tool is the cornerstone of the BRRD and it is important to understand that it is used to avoid losses for taxpayers. The need to ensure adequate transparency, in particular as regards the "no creditor worse off than in liquidation" principle, was also mentioned. Other members considered that the BRRD needed to be improved to better take into consideration the possible involvement of taxpayers, to possibly implement public backstops. The need for progress towards further harmonisation of subordination was mentioned in this context.

12. The EBA's chairperson explained that as long as the rules on valuation are properly applied, there should not be any retroactive effects coming from the BRRD. He explained that the different cases under comparison reflected different types of crises, under different stages of

application of the BRRD. However, he agreed that there had been a lack of consistency in the application of bail-in across the EU. With regard to the treatment of investors, he noted that there was room for improvement, in particular in the way to communicate information to investors. He observed that the European Commission was open to work within the State Aid framework to allow the compensation of investors where appropriate.

13. BSG Chairperson concluded that this important topic of bail-in should be discussed at the next meeting focusing on cross-border comparison and in retail clients.

Item 3: EBA to update on general developments

A) The EBA Chairperson's update on general developments

14. The EBA Chairperson informed BSG members of the letter received from the consumers and users of banking services with regard to the possible cancellation of publication of the Consumer Trend Report for 2017 due to resource constraints. He noted that BoS members were reluctant to provide further assistance with resources to the EBA in the task of working on this report.

15. On Pillar II guidance, he mentioned the BoS discussion on capital guidance in SREP suggesting the SREP Guidelines should be updated. He indicated that further consistency in the application of Pillar 2 capital guidance (P2G) should be applied until SREP Guidelines were revised and in force.

16. He updated BSG members on the Basel discussion held in the last Basel Committee on Banking Supervision (BCBS) meeting in Santiago and noted that the main remaining issue is the one of the output floor where it is important that Europeans' representatives at the BCBS align their positions.

17. He mentioned the Discussion Paper that the EBA intended to publish on proportionality in early 2017 and welcomed BSG members to put forward their views in the wake of the BSG Proportionality Report published last year.

18. Following the BoS discussions on FinTech, the EBA Chairperson presented the proposed way forward dividing the work into four broad sections: authorisation regimes, prudential risks to credit institutions, consumer and retail conduct of business risks and impact on credit institutions business models. He also noted the importance of coordinating the work externally with other bodies working on the same topic, such as the ECB, the EC or the FSB. He observed that the proposed work should not be excessively focused on banks, and include other players, such as payment and e-money institutions.

19. He presented the results of the peer review conducted by the EBA on the ITS on supervisory reporting. One of the major finding was uncertainty caused by late endorsement by the European Commission of the reporting standards which need to be adjusted continuously.

The EBA's intention was to seek more delegation from the European Commission to issue technical templates without formal Commission endorsement.

20. He finally exposed the EBA's major project of data infrastructure in order to expand to the full banking population the submission of ITS supervisory data from CAs to the EBA. He explained the strategic role of the project for the EBA and recognised the importance of the full sample for the EBA's effective analysis of existing rules and to promote transparency in order to capture the differing business models across the single market. As the data are already collected by national Competent Authorities and the ECB, he clarified that it would not imply additional burden for institutions and Competent Authorities.

21. Some BSG members raised another controversial issue within the Basel discussion regarding specialised lending, for which a more balanced approached towards risk sensitivity should also be sought by European representatives. With regard to the ITS on reporting and the EBA project on data infrastructure, a BSG member observed that the frequent changes to the Reporting framework were costly and time-consuming for banks. He advised to make the whole reporting process easier for institutions and avoid regular changes.

22. The EBA Chairperson admitted that the endorsement of the reporting framework was cumbersome for banks and considered that the EBA should take the opportunity of the Discussion Paper on proportionality to introduce proportionate measures with respect to the size, the complexity of business models of institutions.

B) Update on Risks and Vulnerabilities in the EU

23. EBA staff presented an overview of risks and vulnerabilities in the European banking system and focused on non-performing loans (NPL), banks' profitability, and the recent developments in capital structures. It was noted that while asset quality challenges persist, the amount of NPL was slightly declining. Progress is nevertheless slow and very much dependent to the banks' jurisdictions. EBA staff regards NPL to be an issue for the single market as a whole, which requires continuous supervisory pressure and efforts for banks to increase their provisions and reduce their level of NPLs. In terms of profitability, it was observed that return on equity (RoE) was lower than cost of equity (CoE), and RoE continuously decreasing since 2015. EBA staff also observed CoE's growth since the beginning of 2016 partly due to further increase of equity risk premiums. Equally, it was mentioned that banks struggled to generate sufficient returns to meet their CoE. On capital structure, it was reported that CET1 ratios continued to grow due to the increase in capital. In parallel, a rather subdued build-up of the AT1 capital component was confirmed by EBA staff.

24. BSG members commented on NPLs issues, suggesting that the main problem might be an issue of pricing of distressed assets. Indeed, IRB banks were experiencing a low recovery preventing them from cleaning up their balance sheet. It was also mentioned that NPL were

accrued in a different economic environment. Consequently BSG members questioned about the incentives to apply prudential requirements to those NPLs.

25. On profitability, some BSG members viewed that the low profitability was linked to regulation which affected the banks in terms of capital requirements. This argument was contested by other BSG members who considered that subdued profitability was the result of low growth. BSG members commented on the EBA analysis on the latest development of CoE. They broadly considered that CoE was difficult to assess and to interpret due to its volatility mostly driven by uncertainty of supervision, regulation and business models. One BSG member deemed that more attention to national specifications should be paid in the EBA's Risk Assessment Report as most of the results were not totally applicable to certain segments of the German financial market.

26. On AT1, one BSG member called for further clarification on relationship between AT1 and CoE. He viewed that AT1 instruments were expensive because of their connection with CET 1. He viewed that banks did not issue AT1 because of Leverage Ratio and Large Exposures requirements.

27. EBA staff agreed in general with the views expressed by BSG members and reminded that the survey on which the risk analysis was conducted was based on the responses provided by banks included in the EBA sample, and was necessarily partial. EBA staff indicated that the EBA would like to expand the sample of banks to get a broader view of the EU banking sector. It was explained that the impact of regulation on banks' profitability should be further analysed and compared with the performances of banks in other jurisdictions, e.g. the US.

C) Discussion on the lessons learnt on the 2016 EU-wide Stress Test

28. EBA staff presented the results of the 2016 EU-wide stress test and discussed the possible options to replace this stress test exercise, including a top-down exercise or a transparency exercise. The stress test exercise was deemed to be the best option from the EBA's perspectives.

29. With regard to the lessons learnt from the past exercise, it was considered that methodology was improved but increased the level of complexity. For the future, it was noted that the EBA should make the methodology simpler and adapted to take into account IFRS 9 standards. Templates were considered as improved too but they triggered an increased complexity. The scenarios defined for this exercise were more challenging. In this regard, an area for improvement would be to add a definition of risk specific scenarios and benchmarks. In terms of timeline, methodology should be finalised earlier to give sufficient time for industry feedback.

30. In light of the past exercise, EBA staff observed that institutions were generally positive on how caps and floors helped ensure consistency and simplify the quality assurance process. It

was also mentioned that the application of the static balance sheet assumption might help ensure comparability.

31. BSG members asked questions about the scenarios or the inclusion of conduct risks. They also discussed the benefits of the implementation of a dynamic balance sheet assumption generally perceived as more useful than a static approach in terms of supervision. One BSG member observed that the stress tests were preliminary an exercise of transparency and became a tool for supervisors. In this regard, stress tests were not considered as a comprehensive tool to understand the risks. Another BSG member insisted that the role of the stress test was to restore trust. He also mentioned that the design of the current stress test exercise was not too focused on solvency and liquidity.

32. EBA staff replied to questions. In particular, it was indicated that liquidity stress tests were conducted outside the scope of the EBA's stress test. EBA staff agreed that much work should be done to better take into account conduct risks.

Item 4: EBA Update on Consumer Protection, Financial Innovation and Payments

33. EBA staff gave an overview of the EBA mandates under Payment Accounts Directive (PAD) related to the standardised terminology for the most common services linked to a payment account and subject to a fee, and standardised presentation format of the fee information document (FID) and the statement of fees (SoF) as well as their common symbols. BSG members were also updated on the main concerns raised during the public hearing held in November on these topics. The EBA staff concluded this item by mentioning that the consultation period for the Consultation Paper on the presented topics finishes on 22 December 2016 and that BSG Members are invited to respond to the Consultation Paper.

34. An overview of the EBA mandates under PSD 2 was also provided to BSG members. Regarding the RTS on Strong Customer Authentication, it was noted that the EBA was in the process of assessing the large amount of responses received to the Consultation Paper. Comments would be summarised in a feedback table and published alongside the final draft RTS. EBA staff mentioned two significant issues related to this consultation, namely third party access to customer information and accounts, and exemptions to strong customer authentication, including industry demand for a risk-based exemption. EBA staff informed that the EBA intended to publish the final draft RTS early 2017.

35. One of the BSG members touched on the lobbying around the RTS and referred to contentious debates at the European Parliament, expressing concerns with regards to consumer protection and commenting that the principle of Strong Customer Authentication existed to protect consumers and that the EBA should not lose sight of it. The member also mentioned that National Competent Authorities completed an anti-fraud exercise and queried whether it would be beneficial to set a permanent observatory on fraud in order to make the RTS more efficient. EBA staff noted that the ultimate aim of PSD 2 was to limit

fraud and the PSD2 also requested national authorities to collect fraud data and share them with the EBA. EBA staff also offered reassurance on the importance of consumer protection. One BSG member raised his concerns over the absence of a risk-based exemption in the draft RTS and another touched on the debate of access, relaying the position of the issuing banks with regards to allowing existing practices like screen-scraping to remain. EBA staff thanked members and confirmed that these views had been expressed in the responses received and were being assessed. EBA staff explained the difficult trade-off the RTS was trying to make between different, and at times conflicting, objectives.

36. Regarding the Guidelines on Professional Indemnity Insurance (PII) for account information services (AIS)/payment initiation services (PIS) providers, it was indicated that the public consultation period was over. Further analysis would be provided to stakeholders once the review of comments would be completed.

37. One BSG member deemed that it would be difficult to assess the availability of insurers to offer an insurance policy. Further work should be done on this issue before publication of the Guidelines.

38. With regard to authorisation of Payment Institutions (PIs), EBA staff explained that the EBA was mandated to specify the information to be provided to the Competent Authorities in the application for the authorisation of payment institutions. The Guidelines would also apply to AIS Providers, when applying for registration and to Electronic Money Institutions, when applying for authorisation. A consultation paper was published on November 3rd for a 3 month consultation period. The final Guidelines should be published in the second quarter of 2017. One BSG member deemed that the level of details requested in the draft RTS was too high with regard to authorisation. EBA staff explained that the level of details aimed to address one of the key issues that the industry was currently facing under PSD1 of not knowing the level of detail expected from them when submitting the application form. This led to undesirable continuous additional requests of information and to very long and inefficient authorisation procedures. In addition, setting this level of detail was in line with the maximum harmonizing nature of the guidelines, which implies that CAs will not be able to require any other information than what is specified in the GLs.

39. Regarding the Consumer Trends Report for 2017, BSG members representing consumers and users of banking services informed BSG of the letter they sent to the EBA Chairperson about their concerns. Some BSG members queried how the EBA would be able to define its Consumer Protection Work Programme without evidence provided by stakeholders. They also asked how the BSG could help. The EBA Chairperson explained that publishing such a report was a long process and that the EBA was experiencing a lack of resources. With a limited number of staff and a large number of mandates (including under PSD2) to deliver, the EBA had to re-prioritise its work. EBA staff also explained that EBA had developed half a dozen initiatives in 2016 that were aimed at following up on consumer trends identified in previous years and were starting supervisory work following consumer representatives' request. BSG Vice-Chair suggested leading an ad-hoc Working Group including BSG

volunteers and EBA staff members involved in Consumer Protection issues with a view to presenting concrete proposals for the next year EBA's Consumer Trends Report and for the Joint Consumer Day.

Item 5: EBA update on other regulatory deliverables

A) Presentation of the report on covered bonds

40. EBA staff presented the EBA mandate and the background of this report. The report presents a regulatory and market analysis as well as EBA recommendations on how to harmonise covered bond frameworks in the EU. It has been developed in line with the ESRB recommendation and as a follow up to the previous EBA report on covered bonds published in July 2014. Regulatory analysis highlighted diversity of the national covered bond frameworks and the level of alignment with the EBA best practices. It concluded that covered bond instruments with different quality characteristics across the EU are subject to the same European regulatory rules and benefit from a favorable regulatory recognition. Market analysis confirmed inter alia geographical expansion of the covered bonds outside the EU, changes to the composition of the investor base and increasing use of innovative covered bond structures (such as soft bullets and conditional pass through). They also explained EBA's aim in terms of harmonisation and the principles behind the EBA recommendations in this regard. They finally defined the three-step approach to harmonisation of covered bond frameworks in the EU, building on the results of the analysis.

41. BSG members asked questions about the metrics regarding loan to income limit, the differences in the characteristics and legal framework with respect to different covered bond structures (hard bullet, soft bullet and conditional pass-through), treatment in the report of different covered bond issuance models and the next steps envisaged by the EBA. They sought information about the planned review of the covered bond framework by the European Commission.

B) Report on results from the EBA Impact Assessment of IFRS 9

42. EBA staff presented the EBA's work plan related to IFRS 9 and the objectives of this impact assessment exercise. They informed BSG members of the key findings of the report. Amongst the main consequences of IFRS 9 on own funds, it was noted that the major drivers were very much dependent to the type of exposure, the counterparty, the current level of provisions, the choice between standardised approach or IRB model, and the current capitalisation level. They showed that most of the banks were in a design phase of IFRS 9 implementation and that smaller banks of the sample were less advanced than larger banks. They also assessed the impact on volatility of own funds. They pointed out that time was a significant challenge for banks in the implementation of IFRS 9 and focused their attention to the ownership of

project by senior managers and allocation of resources for timely and high-quality IFRS 9 implementation.

43. EBA staff observed that banks were expected to work on further addressing challenges identified in classification, measurement and impairment. Regarding the next steps, the EBA's current work was to assess the interactions between IFRS 9 and prudential rules to determine adequate policy options. It was noted that a second impact assessment was launched in November 2016 and preliminary output should be available by first quarter 2017.

44. BSG members asked clarification about the shortage of capital that IFRS 9 might trigger for IRB banks and on the average impact on CET 1. EBA staff provided an oral update of the quantitative estimates and explained that banks which were in a shortfall situation at the moment of the exercise will have already part of the impact from IFRS 9 impairment reflected in own funds.

45. They also questioned that an accounting change should result in an impact on provisions along the cycle, and asked about procyclicality of the accounting rules. EBA staff made clear that there was no identified trend to confirm possible procyclicality so far. One BSG member relayed the industry's request on the postponement of the deadline of the second round. EBA staff reported being aware of the problems caused by such a tight deadline. Another BSG member raised his concerns as to whether an early application of IFRS 9 compared to the new standards of CRR. Some questions also focused on the implications for the pricing of loans or the differences between banks with respect to the hedge accounting. Regarding the pricing of loans, EBA staff reported that the observed trends regarding pricing should not be detrimental for most banks.

C) Presentation of the final EBA's report on Minimum Requirements on Eligible Liabilities and Own Funds (MREL)

46. EBA staff presented the timeline and the objectives of the final MREL report which included feedback received during the consultation period. They reported that the issues of restrictions on distributions in case of MREL breach and the possible extension of subordination requirement to O-SIIs were among issues discussed at length by resolution authorities and competent authorities.

47. Regarding MREL eligibility criteria, EBA staff explained that subordination requirements were useful to improve resolvability and facilitate resolution planning. They presented the case of G-SIBs for which TLAC subordination should be a minimum. They also discussed the opportunity to extend subordination requirement beyond G-SIBs, in particular to O-SIIs as they were viewed of systemic importance.

48. With regard to determination of MREL, EBA staff stated that the calibration of MREL should, in all cases, be closely linked to and justified by the institution's resolution strategy. They

considered that MREL should be set as the higher of the requirement resulting from the current MREL assessment framework and any ‘floor’ requirement (e.g. TLAC for G-SIBs), should one be introduced.

49. Regarding the enforcement of MREL, EBA staff described the toolbox and clarified the respective roles of supervisor and resolution authority. It was reminded that MREL should be met at all times. Should MREL requirements be subject to a breach, two options were described. The first option was called “stacking order approach”, characterised by no MREL breach but a buffer breach which may trigger a MDA suspension either on an automatic basis or on a case-by-case basis. The second option, called “parallel stack approach”, should not imply a buffer breach but MREL breach which may be dealt with by MREL toolbox.

50. Reporting and disclosure requirements were also discussed.

51. BSG members commented on the interaction of MREL with the maximum distributable amount and asked questions on stack approach. Some BSG members also discussed calibration requirements.

Item 6: AoB

52. BSG Chairperson reminded that the next BSG meeting would be on 22 February 2017.

Participants:

Chair – Santiago Fernández de Lis, BSG Chairperson

Mike	Dailly	Govan Law Centre
Mark	Roach	ver.di
Fryni	Michael	Cyprus Consumers Association
Sergio	lugaresi	italian banking association
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Peter	Mülbert	University of Mainz
Alin	Iacob	Association of Romanian Financial Services Users (AURSF)
Michel	Bilger	Crédit Agricole
Giovanni	Petrella	Catholic University, Milano
Christophe	Nijdam	Finance Watch
Giedrius	Steponkus	Lithuanian Investors association
Dermott	Jewell	Consumers' Association of Ireland
Monika	Marcinkowska	University of Lodz
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Dominic	Lindley	
Anne	Fily	BEUC
Thaer	Sabri	European Money Association
Ernst	Eichenseher	Unicredit
Sara Paulina	Monteiro	Portuguese SME
Guillaume	Prache	Better Finance

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