



EBA BSG 2015 043

Banking Stakeholder Group

27th April 2015

Location: London

Banking Stakeholder Group – Minutes

Item 1.: Welcome and Approval of the Agenda and the Minutes

1. The BSG Chairperson welcomed the BSG members. The draft agenda for the meeting was approved.
2. The BSG approved the minutes of the last BSG meeting held on 3rd March 2015.
3. The BSG Chairperson noted that the Ad-Hoc Working Group on the conduct of stress test has yet to be established as envisaged at the last BSG meeting.

Item 2.: New BSG Member

4. The BSG Chairperson welcomed the new BSG member, Arnold Kuijpers.
5. The BSG Chairperson also updated on the latest developments of the BSG membership. He noted that two BSG members have recently resigned and a third BSG Member will be asked to step down due to his lack of attendance at the last three consecutive BSG meetings.
6. The EBA Chairperson informed on the dearth of suitable candidates in the consumers' category on the reserve list based on the applications received for the second term of the BSG. The BSG Chairperson proposed that the EBA staff selects a candidate in the users of financial services category to replace the consumer vacancy.

Item 3.: BSG Chairperson to update on developments

7. The BSG Chairperson reported on the BSG activities since the last meeting, highlighting the various BSG contributions to the EBA's Consultation Papers. He also referred to the letter that he, together with the BSG Vice-Chairperson, intended to address to the European Commission and the European Parliament expressing BSG concerns about the impact on the EBA's work stemming from the reduction in the EBA's budget which would also have implications for BSG.
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The BSG Chairperson made clear that they will seek the EBA senior management's review of the facts before sending the letter.

8. The BSG Chairperson also distinguished the problem of resource levels due to the budget cuts with the financing mechanism of the EBA. He suggested that the budget cuts might be a prelude to a change in the way of financing the EBA, such as possible direct funding by the banking industry. The EBA Executive Director noted that this option was clearly embedded in the mission letter of the EU Commissioner for Financial Stability, Financial Services and Capital Markets Union¹. He also indicated that due to the fluctuation in the exchange rate between the Euro and the British Pound, the EBA was considering seeking a budget adjustment to reflect the exchange rate issue. On financing the EBA budget, one BSG member referred to the European Financial Reporting Advisory Group (EFRAG) which has a mixed funding structure, partly financed by the banks and partly by EU funds. Another BSG member noted that a dual system of funding based on tax funding and banking industry funding might be relevant, as EU citizens as well as the banks benefit from good regulation.
9. The BSG Chairperson also updated on the BSG submission to the Basel Committee on Banking Supervision (BCBS) on Capital Floors and the New Standardised Approach.
10. The BSG Vice-Chairperson suggested that the BSG could incorporate its comments to the BCBS into the BSG response to the EBA Discussion Paper on IRB Models (EBA/DP/2015/01).
11. The BSG Chairperson noted that several BSG submissions had not yet been placed on the EBA website and requested greater consistency in the timely publication of BSG submitted opinions. Another BSG member requested the EBA to provide a landing page for the BSG activities on the EBA's website. The EBA Executive Director agreed to assess the feasibility of these requests.
12. Further, the BSG Chairperson updated the BSG members on the Consultation Papers yet to be allocated:
 - DP/2015/01:
 - CP/2015/03
 - CP/2015/04
 - CP/2015/05
 - CP/2015/06

¹ http://ec.europa.eu/commission/sites/cwt/files/commissioner_mission_letters/hill_en.pdf

13. One BSG member updated on the status of the draft BSG contribution to the EBA on the methodology and the conduct of the EBA's stress tests, which should be ready in early May. The Ad-Hoc Working Group on the conduct of the stress tests would then be asked to provide its thinking on the paper in due course.
14. The BSG Chairperson informed that the BSG was preparing a response to the EBA Consultation Paper on sound remuneration policies (EBA/CP/2015/03), with respect to the BSG's concerns with regard to proportionality. One BSG member pointed out that the issue of proportionality might significantly impact the smallest banks, making clear that the problem of identified staff is not relevant for the small credit institutions.

A) Workstream of BSG technical Working groups' Activities and Allocation of BSG Work

15. The BSG coordinator of the Working Group on Capital and Risk Analysis updated the BSG members on the outstanding consultations, namely i) the future of the IRB Approach (EBA/DP/2015/01), and ii) limits on exposures to shadow banking entities (EBA/CP/2015/06). The BSG Chairperson also noted the positive aspects of the shadow banking system insofar as it may provide liquidity to the banks in difficult conditions and be an alternative source of funding. The BSG Chairperson highlighted that the Draft EBA Guidelines should be balanced so as to not impair the shadow banking sector too much.
16. The BSG coordinator of the Working Group on Recovery and Resolution presented the work undertaken by the Working Group. He flagged the important issue raised by the Consultation Paper on Business Reorganisation Plans (EBA/CP/2015/05).
17. One BSG member noted that credit institutions would have difficulties to implement the proposals contained in the EBA Consultation Paper on contractual recognition of bail-in (EBA/CP/2014/33) due to the disproportionate efforts in order to make the instruments bail-inable. The BSG member asked the EBA to consider issuing some guidance so as to assist the credit institutions with the practical aspects. Other BSG members supported his intervention.
18. One BSG member raised the issue of consistency with the global plans for banks' total loss absorbency (TLAC). The EBA Chairperson observed that the MREL was designed to enable the National Competent Authorities (NCAs) to comply with the requirements imposed by TLAC for EU SIFIs. Several other BSG members had concerns on the German subsidiary proposal regarding TLAC/MREL. As each Member State has different subordination framework which could create cross-border groups, the EBA Chairperson deemed it was an interesting issue on which the EBA would welcome the BSG views.

B) Discussion on Proportionality Project

19. The BSG coordinator of the Ad-Hoc Working Group on Proportionality informed on the developments of the report. He noted that the draft report had been shortened and circulated

on 23 April 2015 to BSG members. He aimed to present a final paper to the BSG at its 22 June meeting.

20. The BSG Chairperson suggested providing a set of clear and precise recommendations based on the report's analysis. He suggested an additional Ad-Hoc Working Group meeting to finalise the report.
21. The coordinator of the Ad-Hoc Working Group on Proportionality asked for comments on his latest draft by the end of May and proposed to convene a meeting on 4 June 2015 in Brussels with a view to finalising the report.
22. One BSG member viewed that the EBA should assess the proportionality dimension in its impact assessment considerations of regulatory products, and suggested that the BSG could propose to the EBA how this dimension could be better performed. The BSG Chairperson reflected on his own experience on performing cost/benefit analysis, where he viewed that they should be done as early as possible in the process, so as to inform the policy deliberations. Another BSG member underlined that the need to use relative measures rather than absolute measures to perform the impact assessment. Another BSG member suggested that the EBA should define more clearly the sought objective(s) and scope for every new Regulation, and then assess the proposals for the different categorisations of credit institutions.
23. The EBA staff informed the BSG members of the second EBA workshop on Proportionality which is planned to be held on 3 July 2015.

Item 4. Update on Regulatory and Oversight Developments

A) EBA Chairperson to update on general developments

24. The EBA Chairperson referred to the EBA's Proportionality Workshop, ESAs Joint Consumer Day, EBA's Call for Papers for its fourth Annual Research workshop and that the EBA is considering hosting a Conference to mark fifth Anniversary in early 2016. He informed that the EBA had recently published its revised 2015 Work Programme to reflect the EBA's updated priorities in light of reduced resources and additional mandates. He updated on the EBA's report on Supervisory Convergence, which denotes the clear shift from rules making to supervisory implementation.
25. The BSG Chairperson suggested that the BSG might make a contribution to support the EBA's fifth anniversary.
26. Further, the EBA Chairperson informed on the EBA's request to the European Commission for a corrigendum for the RTS on non-delta risks, following a change introduced by the Commission to the EBA proposal, as part of the EC's adoption process which makes resulting RTS non-compliant with BCBS standards.

27. The EBA Chairperson updated on some topics emerging from the recent Eurofi conference, including the concern of American banks that they are being driven out of market making and its impact on their banking activities. The BSG Chairperson viewed that the need for market liquidity is important and could be compromised by regulation.
28. Regarding the Capital Market Union (CMU), the EBA Chairperson informed that the EBA was in the process of finalising its advice to the European Commission on securitisation due by July 2015.
29. The EBA Chairperson informed that the EBA was finalising a paper with the EIOPA on Conduct Risk.
30. One BSG member asked about the EBA's involvement in the ECB's work on national discretions under CRD/CRR. The EBA Chairperson responded that, whilst the CRD contains national discretions to which Competent Authorities may exercise, the EBA had published how Competent Authorities exercise their discretion as part of its supervisory disclosure work. Further, the EBA had noted that many discretions are contained in the transitional provisions.
31. The BSG Vice-Chairperson raised his concerns about the Technical Papers on sovereign risks issued by the ESRB proposing solutions and the implementation of new rules impacting risk weights, floors, lists of concentration.
32. EBA staff updated the BSG members on the envisaged EBA Consultation Papers to be launched in the coming weeks, in line with the EBA's (revised) published work programme.
33. One BSG member asked about the EBA's proposals for supervising IT risks, underlining that it was a technical issue to legislate on, due to the multiple existing approaches in the EU. He viewed that in this regard the EU could benefit from the US practice.

B) Consumer Protection, Financial Innovation and Payment Services

i. Update on Mortgages: EBA Guidelines and other outputs

34. The EBA Staff updated on mortgage-related outputs, including the two Guidelines that are due to be published in the coming weeks, namely Guidelines on arrears and foreclosure (EBA/GL/2014/43) and Guidelines on creditworthiness assessment (EBA/GL/2014/42) and the Opinion on good practices for mortgage creditworthiness assessments and arrears and foreclosure. Further, the comments received during the public consultation on the requirements passport notifications for credit intermediaries under the Mortgage Credit Directive (MCD) were presented. The EBA staff highlighted the mandate for EBA under the Mortgage Credit Directive to set a benchmark rate.

35. One BSG member raised concerns as to whether an EBA benchmark rate would take into account the differences in base rates used across the EU and in particular the different funding costs that banks incur. Another BSG member linked the topic to the discussion on benchmark regulation in the European Parliament.

ii. Discussion on EBA's work on innovative types of payments

36. The EBA staff presented the EBA's work on innovative types of payments. The current work is focused on the identification of the risks and benefits arising from innovative types of payments, the prioritisation of them, and the measures to mitigate the risks. The EBA staff requested the BSG members to kindly share their views on innovative types of payments, including their perceived priority of associated benefits, risks and risk drivers by 1 July 2015.

37. The BSG Chairperson suggested coordinating the BSG responses to the survey and sending a collective response, noting that the dispersion of views would have to be reflected in that response. One BSG member pointed out that the consumers would take advantage from the innovative types of payments that may be potential drivers for efficiency. To this end, the EBA's analysis should be well balanced. Another BSG member underlined that non-banking entities may provide innovative types of payments, and suggested that the EBA's analysis should consider this aspect.

38. The EBA staff confirmed that a balanced approach to innovative types of payments is being taken, taking into consideration their potential benefits as well as risks. The EBA staff acknowledged that non-banks may play an important role in providing innovative types of payments but informed the BSG that, at the current state of the analysis, only entities that fall within the EBA's remit for consumer protection and financial innovation are being considered (i.e. credit institutions, payment institutions and e-money institutions).

iii. Consumer Trends Report 2015

39. The EBA staff updated on the Consumer Trends Report 2015 for which the BSG members were consulted. The report is due to be published mid-2015. The BSG's contribution was also presented. The BSG members identified most commonly the topics of indebtedness, banking fees and costs, innovative payments, deposits and structured deposits. The EBA staff mentioned that these coincided with the references received by the national authorities at EBA's Working Group and therefore would be included in the Report.

40. One BSG member referred to crowdfunding as a loophole in the field of the consumer protection. The EBA referred to its Opinion provided on crowdfunding which had noted this issue.

41. Another BSG member highlighted that the same issues are captured in the Consumer Trends Report year after year. Another BSG member raised the threat of the consequences of

negative interest rates from a consumers' perspective. The EBA staff informed that the EBA's Report duly notes that some recurrent issues are identified and also interest rate risks.

C) Risks in the banking sector

42. The EBA staff highlighted the main risks and vulnerabilities in the EU banking sector, focusing on decreasing credit risks and stabilisation in terms of access to funding and maturity distribution. Capital ratios appear to be increasing and a noted turnaround from deleveraging toward stabilisation and growth. The asset quality was now showing a trend towards stabilisation. The EBA staff remains concerned with the volatility of banks' profitability with nearly 60% of the banks acknowledging that their current earnings were not covering the cost of equity. It was noted that market funding conditions were stabilising, reflecting a more benign market sentiment with some vulnerabilities including a widely expected decrease in trading market liquidity. The EBA envisaged publishing its next report on risks and vulnerabilities in end June/early July 2015.
43. On methodological issues, the BSG Chairperson raised his concerns on the cost of capital, to which the banks needed to address, else exit from some business lines. He suggested that a CAPM model could be used to estimate the cost of capital for each bank in the sample. He also suggested the report assess how banks make provision for bad loans and foreclosures. Another BSG member asked on the measures of the cost of equity (CoE) and the possibility of measuring the weighted average CoE compared to the return on equity (RoE). The EBA staff responded that ideally they should test empirically, but to do so they would need more data.
44. Another BSG member expressed concern of some banks' weak IT infrastructures and the associated cost to replace.
45. Another BSG member questioned to what extent the banks were deluding themselves on the issue of conduct risk and their ability to comply with international regulations.

D) Discussion of the Guidelines on the management of Interest Rate Risk arising from non-trading activities (IRRBB)

46. The Chair of the EBA's working group on interest rate risk arising from non-trading activities (IRRBB) updated the BSG on the proposed revision to the Guidelines on the management of IRRBB, following consideration of comments received during the public consultation, noting the BSG did not formally provide its opinion. These include an additional IRRBB Principle to cover governance aspects, further clarification and specification of methodology used to calculate the 'supervisory standard shock' in order to promote consistency, and further additional technical guidance on aspects of IRRBB. The additional guidance proposed now includes guidance on the setting and use of scenarios for stress testing purposes, on measurement assumptions, on methods to measure interest rate risk, on governance of interest rate risk, and on the identification, calculation and allocation of capital to IRRBB.

47. The BSG Vice-Chairperson remarked that the use of economic measures would be better than the measures based on current earnings that were presented as less relevant and encouraging short-term perspectives. The EBA staff put forward that the “standard shock” described in the Guidelines is intended to have a standard benchmark for supervisory comparability purposes that helps to assess the relative sensitivity of IRRBB to a given institution. It should not be used for internal risk management purposes.
48. One BSG Member expressed his concerns on two constraints that the Guidelines would introduce : 1) on capital and 2) on customer deposits. The Member expressed a view that the treatment of capital with a duration of one day would be inconsistent with the concept of unexpected loss used in the Basel framework. The Member also viewed that the behavioural assumptions of setting of a 5-year maximum average limit on the duration ascribed to customer accounts without specific re-pricing characteristics for the purpose of assessing the standard supervisory shock could have severe shortcomings for banks in France.
49. In the opinion of the BSG Member, the EBA’s proposal would impede banks’ ability to offer fixed rate mortgages in France - a system that works well to the satisfaction of customers, public authorities and banks - as the two liabilities items were natural ALM hedges for these mortgages
50. The EBA took note of the comments. It mentioned that the average five-year restriction is not intended to apply to internal measures used by institutions to quantify their own interest rate risk.
51. Another BSG Member noted that the Basel Committee on Banking Supervision (BCBS) is also assessing this topic; and suggested that the EBA should wait for the BCBS to complete its discussions before finalising its proposal.

E) Draft RTS on Mortgage Lending Value

52. With a view to providing a long-term, sustainable value as a stable basis for judging the suitability of a property as a security for a mortgage which will continue through potential market fluctuation, the EBA staff presented its considerations on the rigorous criteria for the assessment of the mortgage lending value (MLV). The EBA staff illustrated the main difference between the MLV and the market value (MV), making clear that the MLV is intended to be an estimate of the value of the property for a long period of time, whereas the MV is an assessment only at the valuation date.
53. The EBA is mandated to set out rigorous criteria for the assessment of the MLV in statutory or regulatory provisions and is developing a methodology based on the existing approaches used in national member states: the Income Approach, Comparison Approach, Residual Approach and Cost Approach and intends to use these four approaches as its main building blocks.
54. One BSG member asked about the implications of these RTS in Member States that do not use MLV. He noted that the United Kingdom has not used MLV so far. The EBA staff responded

that the EBA's proposal seeks to address its mandate on MLV (provided in the CRR) to promote more consistency amongst the Member States and institutions that do apply the MLV. Moreover, it is not within the scope of the EBA's mandate to harmonise across valuation concepts (MV and MLV).

55. Another BSG member suggested that these draft RTS would have to be compatible with the different system of mortgages in the EU. He also queried whether covered bonds would be covered by the RTS, to which the EBA staff noted that the draft RTS will follow the scope of the CRR.

56. Another BSG member raised concerns about the relevance of the cost approach defined as a second valuation approach, to which EBA staff responded that the cost approach is a secondary valuation approach, implying that it should serve as a back-stop. He also questioned the ramifications of the distinction proposed for rental properties, such as between residential and commercial properties. EBA staff responded that the classification of properties is intended to be most closely aligned with the use and purpose of the property, in order to ensure a consistent assessment of MLV.

57. One BSG member cross referred the proposal against the Irish experience of the crisis, where the market value has significantly decreased, inducing economic damage in spite of the fact that the country applied the technical standards. The EBA staff responded that MLV is not used in Ireland; instead the concept of market value is applied.

Item 5.: Preparation for the following day's BSG/BoS Joint meeting

58. The BSG Chairperson and Vice-Chairperson presented the key issues to be tabled. Those BSG Members presenting either their views or acting as a discussion outlined their respective presentations.

Item 6.: A.O.B

59. The BSG Chairperson requested the BSG members to suggest their respective suggestions for agenda items for the next BSG meeting which is due to be held on 23 June 2015.

Participants at the meeting of the Banking Stakeholder Group (BSG)

London, 27 April 2015

<u>BSG Member</u>	Representing
David T. Llewellyn (Chairperson)	Top-ranking academics
Andrea Resti (Vice-Chairperson)	Top-ranking academics
Alf Alviniussen	Users of banking services
Michel Bilger	Credit and investment institutions
Javier Contreras	Consumers
Mike Dailly	Consumers
Nikos Daskalakis	SMEs
Santiago Fernández De Lis	Credit and investment institutions
Chris De Noose	Credit and investment institutions
Ernst Eichenseher	Credit and investment institutions
Jose Antonio Gonzalo-Angulo	Top-ranking academics
Sandra Hafner	Credit and investment institutions
Troels Hauer Holmberg	Consumers
John Hollows	Credit and investment institutions
Zdenek Hustak	Top-ranking academics
Robin Jarvis	Users of banking services
Bostjan Krisper	Consumers
Arnold Kuijpers	Credit and investment institutions
Nina Dietz Legind	Top-ranking academics
Louise Lindgren	Credit and investment institutions
Dominic Lindley	Users of banking services
Sabine Masuch	Credit and investment institutions
Ute Meyenberg	Employees
Jesper Bo Nielsen	Employees
Robert Priester	Credit and investment institutions
Holger Schwannecke	Credit and investment institutions

From the EBA

Andrea Enria – EBA Chairperson

Adam Farkas - Executive Director

Rita Bairros

Valerie de Bruyckere

Cédric Coraillon-Parquet

Denise Delaney

Corinne Kaufman

Christoph Kuhn

Nick Lock, Chair of the EBA's working group on interest rate risk arising from non-trading activities (IRRBB)

Elisabeth Noble

Vinay Pranjivan

Mario Quagliariello