German Banking Industry Committee

Die Deutsche
Kreditwirtschaft

Comments

On the European Commission's proposal for a Regulation of the European Parliament and the Council on amending Regulation (EU) No 575/2013 as regards minimum loss coverage for non-performing exposures

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The **German Banking Industry Committee** is the joint committee operated by the central associations of the German banking industry. These associations are the Bundesverband der Deutschen Volksbanken und Raiffeisenbanken (BVR), for the cooperative banks, the Bundesverband deutscher Banken (BdB), for the private commercial banks, the Bundesverband Öffentlicher Banken Deutschlands (VÖB), for the public-sector banks, the Deutscher Sparkassen- und Giroverband (DSGV), for the savings banks finance group, and the Verband deutscher Pfandbriefbanken (vdp), for the Pfandbrief banks. Collectively, they represent more than 1,700 banks.

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The European Commission (COM) published a proposal for a Regulation of the European Parliament and of the Council on amending Regulation (EU) No 575/2013 as regards minimum loss coverage for non-performing exposures on 14 March 2018. We appreciate the opportunity to submit our comments.

As frequently stressed in the context of the completion of the Banking Union, the German Banking Industry Committee (GBIC) generally supports the intention in the Action Plan to reduce NPLs. However, we oppose the proposed backstop requirement to prevent inadequate provisioning for future NPLs as being not expedient, because we believe that this approach will result in unintended triggers for management errors. In order to achieve the goal of sufficient coverage by banks for existing and future NPLs intended by the Council and the Commission, we are of the opinion that it is both necessary and sufficient if the following three conditions are met:

- **Clear, harmonised risk management rules for identifying and treating non-performing loans** (Pillar 2, in line with the German MaRisk): An adequate risk management requirement at European level is likely to be the goal of the draft EBA guidelines currently consulted, on which we will comment separately. There is a particular need to harmonise implementation periods and deadlines.

- **Compliance with the existing accounting rules for recognising value adjustments** (incl. strict financial statement audit): There are evidently concerns about compliance with the accounting rules for recognising adequate valuation allowances in certain Member States. However, this shortcoming should be addressed more directly and any deficiencies should be remedied. There is nothing that can replace this – not even a prudential provisioning backstop. This would not make it any better, but merely more complicated, and in many cases ultimately inappropriate. This can already be seen, for example, in the planned treatment of collateral. In this case, the Commission is proposing that, as a general rule, only collateral that is recognised in Pillar 1 could be taken into account (for example no transfer of title for security purposes or similar, although this certainly plays a role in the actual amount of the acute risk). However, we are not focusing on criticising such "details", but on the shortcomings of the Pillar 1 approach itself. In the context of German Accounting Standards, we are particularly concerned that the backstop rule should not fuel any fundamental doubts about German accounting practice or German GAAP.

- **Monitoring of compliance with the existing rules by the supervisors in the context of the SREP**: The assessment of the adequate recognition of risk provisions is quite properly part of the SREP because of the complex, bank-specific interdependencies. The ECB has also introduced a quantitative benchmark for SIs via the Addendum to the NPL Guidance in the form of prudential expectations regarding adequate provisioning, which are very similar methodologically to the prudential backstop. However, the ECB stresses in its approach that the prudential expectations regarding provisioning are by no means binding, but merely a basis for discussions with the banks concerned; banks should be able to demonstrate in particular that their existing provisioning is adequate or that the level of the equally quite sweeping basis of the "prudential expectations" is not appropriate (comply or explain). In this respect, the ECB acknowledges the problems surrounding its one-size-fits-all approach and allows departures from it. By contrast, the proposed backstop rule represents a mandatory requirement for which no general justification for the calibration has been advanced, and which also only permits an extremely rough individual quantification in specific cases that is thus not, as a rule, appropriate. The risk of overstating in individual cases and hence of inappropriate capital deductions, together with the necessary implementation effort for a complex new deduction rule, thus impacts every bank. Moreover, individual business models may be affected excessively and much more heavily without any justification, in particular because of the undifferentiated and incomplete eligibility of collateral. Ultimately, the necessary individual treatment can only be ensured as part of a more strongly principle-based Pillar 2 rule.

Finally, the introduction of a regime that imposes one-size-fits-all prudential minimum risk provisions for non-performing exposures in the CRR is not in line with the requirement for proportionality under Article 5 of the Treaty of Lisbon, as adequate provisioning can also be achieved by other, more proportionate means. For example, Article 104(1)(a) of CRD IV already sets out that the competent authorities may impose higher own funds requirements in order to ensure that risks are adequately backed by capital. Under Article 104(1)(d) of CRD IV, the competent authorities can even require institutions to apply a specific provisioning policy or a specific treatment of the institution's assets in order to ensure adequate provisioning. For significant institutions that are supervised by the ECB, Article 16(2) points (a) and (d) of Regulation (EU) No. 1024/2013 (SSM Regulation) additionally provides for direct supervisory powers for the ECB. The introduction of a prudential backstop provisioning regime as part of the CRR is hence disproportionate and must therefore be rejected.

We have the following detailed comments with regard to the consultative document:

1. We have substantial concerns about the methodological implementation described for the proposed backstop. This relates to the effort that will arise in the case of simultaneously occurring unintended, and in particular procyclical, effects that are detrimental to SMEs and consumers. It should also be considered that there are already adequate process-related and accounting requirements both in the national German regulatory regime (in particular the "Minimum Requirements for Risk Management" (MaRisk) in Germany) and in the accounting rules, which also include IFRS 9, and that these function well in the GBIC's view and should be allowed to take effect. Moreover, because there is a lack of statistical and audit-related conspicuous anomalies with regard to NPEs, there is no evidence that would justify such comprehensive and far-reaching changes or potential additional burdens in the future for German banks. This relates in the first instance to the implementation effort that will arise, and culminates in the mid-term in potential capital deductions for new NPEs that are difficult to calculate and difficult to understand.

2. Even though the current basis means that no or only a minor impact is expected in Germany in the form of necessary capital deductions due to the conservative accounting principles, we have identified a methodological inconsistency in the backstop procedure that can lead to unintended consequences that are very difficult to predict. The need for any capital deduction should be rooted in a substantiated, quantitative basis and, especially in this case, it should only be necessary if verified, substantiated information is available about inadequate provisioning. In the final analysis, a consistent, appropriately aligned backstop calculation would generally have to satisfy the requirement of acting as a realistic indicator of accounting risk provisioning as part of the supervisory assessment. Only if this condition is met would a substantiated backstop for the purposes of "prudential provisioning" be suitable as a corrective and, for the purposes of the supervisory assessment, as a unifying measure. A one-size-fits-all calibrated backstop cannot meet this expectation, either methodologically or substantively. With the increase to 100%, the rule is actually clearly designed in such a way that the required provisioning must necessarily be exceeded after the (equally not understandable) defined period has expired, with the result that the approach already disqualifies itself in terms

of appropriateness. Ultimately, this deliberately designed exaggeration of the expected risk provision leads to the concerns about procyclical effects mentioned previously. Especially at banks that suffer from increased occurrences of NPEs in a crisis, the backstop can lead to additional charges that will additionally weigh on the capital situation of the institutions concerned. The actual goal of creating an "incentive" for adequate provisioning is therefore exaggerated because of the backstop, because the CET1 capital deduction under Pillar 1 is ultimately the strongest measure available to the supervisors. On the contrary: the deduction creates an incentive for potentially hasty, short-term countermeasures to avert the capital deduction, which can also lead to additional adverse effects on the credit market. Ultimately, the backstop should be and can only be an indicator that triggers a more in-depth review of the appropriateness of the risk provisioning. It is not suitable as the basis of a quantitative Pillar 1 rule that has a direct effect. In particular, there is no quantitative basis for this drastic rule or any substantiation for the prescribed values, so it lacks the necessary consistency and demonstrated appropriateness.

3. We also believe there is a risk that banks, which are potential buyers of non-performing loans, would have little interest in purchasing them if they had to apply the backstop rules to the purchased loans. Moreover, our experience shows that this would have a negative impact on purchase prices, which in turn could discourage the selling banks from pursuing a strategy of reducing their holdings of NPLs by selling loans.

4. With regard to the overall classification of the rule, we can also state that it represents an escalation of the deduction rules over and above the Basel standard, which in the final analysis impacts the level playing field with other jurisdictions.

5. In particular for non-IFRS preparers, which above all include most small and less complex banks, the implementation effort would probably be higher and would most likely differ from what was presented in the impact assessment. In addition, it is common practice at smaller banks to dispense with applying credit risk mitigation (CRM) techniques because of the administrative effort needed to satisfy the application criteria, and to accept higher own funds requirements from unsecured exposures. The backstop rule could force these banks to introduce CRM-related processes because these are decisive for classification as "secured" in order to avoid unjustified capital deductions. At these banks, the rule therefore leads to further indirect costs.

6. Measures with such short-term and possibly drastic incentive effects should be concentrated on those banks that have correspondingly high levels of NPE holdings of originated loans that are material for the system and are treated there under Pillar 2 (e.g. using the ECB's NPL Guidance), as only there is it possible to make the necessary individual assessment. If a solution based on the proposed backstop procedure will be introduced despite our concerns, at the most a threshold that can trigger the application of the backstop rule would be conceivable, so that institutions with small portfolios of NPEs or of low systemic importance are not burdened by this undifferentiated rule. Through purchases of NPEs at market prices, this would also enable institutions with small NPE portfolios to help credit institutions reduce their holdings of NPEs by selling loans. As already proposed by the EBA in the consultative paper on its guidelines on management of non-performing and forborne exposures, a threshold could be defined to select relevant banks, e.g. based on an adequately defined NPE ratio. To further narrow down systemic importance, the current definitions of and discussions on absolute

dimensions (or as a ratio to GDP) could be used. The advantage of such a procedure is that only banks with large NPE portfolios would be affected, while banks with a low NPE ratio would not be overly burdened (not least because of the associated procedural tasks). Moreover, this would not only take account of the actual risks, but would also reflect economic trends across the EU (including general NPE trends) and would thus also take into account the differing conditions in the individual Member States. However, with regard to the calculation of an NPE ratio as a potential benchmark for applying extended measures for managing NPEs, we wish to draw attention to what we believe is an existing weakness in the standard gross analysis used in the calculation. From our perspective, the existing risk provision should be kept out of the equation in the sense of a net analysis. If not, banks would still find themselves caught by the backstop rule despite their conservative provisioning policy in the same way as "problem banks". We will document corresponding remarks in our comments on the EBA guidelines, which already proposed an NPE ratio as a defining factor for more far-reaching requirements.

7. We are also critical of the fact that binding requirements are to be consistently imposed for all credit institutions regardless of their business model and the associated concrete risk and collateral structure, without allowing any option to take account of specific scenarios (e.g. by explicitly excluding certain recoverable collateral or at least by applying a comply or explain principle).

8. The one-size-fits-all, purely period-based backstop proposed by the Commission conflicts with banks' need to work out problem loans with the greatest possible recovery of collateral. As appropriate as the Commission's goal of forcing the rapid elimination in future of problem loans from banks' balance sheets may be, this proposed approach still contradicts the compatibility of prudential treatment with the bank's strategy for managing the existing risks. Accounting provisioning is based on an individual assessment that is determined on the basis of the information in individual cases relating to a) credit quality and collateral, and b) the bank's expectations regarding the future development of those factors, in particular in light of c) the chosen strategy for managing the exposure. The Commission's one-size-fits-all approach results here in both a departure from the previously used, statistically backed derivation of expected losses on the basis of portfolio-driven models, and in differences compared with the accounting treatment under international and national rules. In addition, such a one-size-fits-all approach renders other NEP requirements of the ECB and the EBA obsolete. As a result, for example, the institutional requirements for an NPE strategy would come to nothing.

9. We continue to take a critical stance of the Commission's plans to restrict loan collateral to recognised collateral within the framework of the CRR credit risk mitigation techniques. This means, for example, that physical collateral will be largely excluded except in the case of real estate collateral, whereas the EBA accepts all collateral in its proposal for managing non-performing loans. What is also particularly unsatisfactory in this context for SA institutions is that the EBA has not complied with its mandate under Article 199(8) of the CRR or otherwise sees itself unable to publish a list of physical collateral. The institutions could presuppose in this case that the conditions of Article 199(6) points (a) and (b) of the CRR with regard to liquid markets and well-established, publicly available market prices are satisfied. Especially for SA institutions, it is therefore still unclear – or it remains in future at the discretion of the competent authority – which physical collateral can generally be considered for eligibility as CRR collateral provided that the other relevant conditions in the CRR for credit risk mitigation are met. For example, there are liquid, well-functioning used vehicle markets

for motor vehicles with publicly available used vehicle prices (e.g. via Deutsche Automobile Treuhand or internet portals). To avoid legal uncertainty, especially for SA institutions, and to ensure a level playing field in Europe, Article 199(8) of the CRR should be amended by adding the physical collateral (e.g. motor vehicles) that institutions can accept in all cases so that the conditions referred to in Article 199(6) points (a) and (b) of the CRR are met. This is important so that institutions, and especially SA institutions, can include this collateral as CRR collateral free from any doubts, provided that the institution meets the other requirements in the CRR that can be influenced by the institution for recognising other physical collateral.

10. The general approach – or the underlying hypothesis – that collateral must necessary be deemed unrecoverable after no later than eight years and can therefore no longer be recovered, or not recovered in full, does not correspond to reality in the case of various types of collateral. One example here is ECA cover products and other state guarantees issued by the Federal Republic of Germany, which play a major role, for example in development cooperation, as well as domestic development programs. For ECA cover products, for instance, a lengthy recovery process is provided for and agreed in the contract, although this does not affect the recoverability of these guarantees in any way. The proposed one-size-fits-all approach therefore results in an unjustifiably high prudential risk provision even before the eight-year period has expired. A more flexible approach to the strict requirements, including for this sort of collateral, would therefore make sense. An adequate level of flexibility would also be desirable, for example to take appropriate account of the prospects of success for restructuring efforts, long durations and the complexity of exposures.

11. We are also critical of the very short period of two years within which unsecured exposures must be fully covered by risk provisions. It is not always necessarily evident after two years whether recovery measures will be successful. Compulsory 100% coverage by risk provisions could thus ultimately have a procyclical effect because the two-year period does not permit an adequate analysis of the prospects for recovery, and banks could be forced prematurely into resolution of the exposure (e.g. by a quick sale). We therefore believe that it makes sense to extend this two-year period by at least one year. The prospects of success for recovery can normally be determined after three years with a relatively high level of certainty. This is also reinforced by the exclusively prudentially driven definition of "unsecured" NPEs by reference to prudentially recognised credit risk mitigation techniques. Exposures secured by unrecognised collateral are exposed to an increased risk of reaching the two-year limit because of the time needed to recover the collateral. As a result, these loans and certain business models are subject to special pressure to ensure resolution.

12. In addition to the already complex calculation of deductions in accordance with Article 47c(1) of CRR 2 based on individual exposures and depending on the vintage period, collateral and past due status, additional implementation effort arises because of the application of Article 111(1) of CRR 2 and the existing Article 113(1) or Article 151(1) of the CRR. No risk weights must therefore be recognised to avoid double backing with own funds for amounts already deducted. In contrast to the backstop rule, in which our understanding is that net totals of all NPE portfolios are applied, the rule in Article 111(1) of CRR 2, Article 113(1) and Article 151(1) of the CRR is based on the level of individual exposures, i.e. it requires the amount already deducted from own funds to be calculated for each individual exposure and deducted from the exposure value. The proposed addition in Article 127(1) of CRR 2, which also unnecessarily complicates the process of calculating risk weights for secured NPE

exposures at the level of individual exposures, should also be mentioned. In this case, the backstop rule and the capital deduction in accordance with Article 36(1)(m) of CRR 2 can also result in the own funds requirement for the NPE exposure additionally increasing because a higher risk weight is assigned. This additional charge does not appear to be justified. Overall, the necessary individual exposure-based adjustments to exposures in the rules referred to above due to the proposed deduction rule under Article 36(1)(m) of CRR 2 lead to a high level of implementation effort that was evidently not taken into account in the evaluation in the course of the impact assessment.

13. Pursuant to Article 47a paragraph 2 sentence 2 in conjunction with paragraph 1 letter b) the term exposure shall include the full undrawn amount of a commitment irrespective whether the commitment i.e. credit facility may be cancelled unconditionally at any time and without notice. This is not proportionate, overly conservative, would impede the availability of credit facilities for borrowers being in a restructuring phase and could thus promote the failure of such borrowers. Against this backdrop, the ECB has decided in its addendum to supervisory expectations for prudential provisioning of non-performing exposures that undrawn credit facilities which may be cancelled unconditionally at any time and without notice may be disregarded (see 3.3 on page 9 of the ECB guidance). This should apply for this regulation as well. Thus, Article 47a paragraph 2 sentence 2 letter b) should be supplemented by the following sentence: "This does not apply for undrawn credit facilities which may be cancelled unconditionally at any time and without notice."

14. The announced more detailed specification and harmonisation of valuation rules and requirements governing recoverability and enforceability of collateral, which the EBA should consider, are generally sensible in our view (see page 14, Recital 11 of the Draft Regulation in conjunction with Article 47c(5) of the CRR). With regard to the planned common methodology, however, it needs to be pointed out that this can only be principle-based. The functioning of national real estate markets in Europe, the availability of data and the valuation methods vary considerably in some areas, so it must be possible to reflect these in a Europe-wide methodology.

15. Another critical aspect of the backstop rule is the potential impact on client relationships with borrowers. One-size-fits-all rules may lead to one-size-fits-all behaviour towards clients. Such a rule could have damaging effects for small and medium-sized businesses and consumers because the motivation when dealing with problem loans would no longer be primarily focused on reaching arrangements with the borrowers that are as amicable as possible (even if they may turn out to be protracted), but rather to sell problem loans as quickly as possible to specialised liquidators. The goal of this would be to avoid the need to provide 100% coverage for the loan (risk provision). This may well be a practicable solution in some cases, but it could sustainably impair the existing client relationship in connection with the development of secondary markets.

16. The rigid quantitative stipulations for the capital deduction in conjunction with the potentially greater orientation on the capital markets thus pose a risk to the concept of mutually agreed restructuring, as is the case in Germany and elsewhere. Such requirements also represent an intrusion into banks' proven business policies because they can force the possible sale of NPEs/collateral if the institution really has to comply with the minimum coverage level requirements, although it would not otherwise have done so for economic reasons. Borrowers would be affected because the consequences could

be fewer financing options due to the more restrictive lending practice, which would particularly impact private clients and companies with a higher risk profile. Moreover, the possible sale of NPEs (for example, in order to avoid a further capital charge) will not free up a significant amount of capital and hence open up greater opportunities for lending in all cases because the capital was already used up for the sale or the prior provisioning. In this respect, the rule tends to have a procyclical effect in emergency situations and stressed credit markets and, in our view, will tend to reduce rather than increase the banks' willingness to lend, because default and a consequent 100% risk provision could be expected for higher-risk clients in particular. Banks would probably also factor this expected provisioning into the pricing of higher-risk loans, which in turn would not be expedient for the borrowers.

17. The proposed model adversely affects, for example, a) sensible recoveries of collateral by the bank because the collateral is recoverable even though the loan is in default, b) workout exposures for which public indemnity bonds have been provided and c) clients with a higher risk profile, who must expect that it will be more difficult to obtain a loan, as well as higher prices. In the case of a), it may make sense from the purpose of the financing bank to also agree a potentially long-term restructuring through which, for example, the borrower will be in a position after the restructuring to repay the loan in full or to a significant extent. Restructuring measures that must also be approved by the courts in some jurisdictions are also subsumed under a) (for example under the terms of Articles 67 and 182 of the Italian Bankruptcy Law); these represent a solution that is acceptable to all parties involved, if necessary through one or more parties accepting a loss, and thus support the principle, mentioned above, of arriving at an amicable solution. If the bank consents to these measures following its analysis, this solution represents the most economically sensible solution for handling with a problem loan; expected losses from it must already be recognised in full in the accounting. Where the planned measures are supported by the bank, which could actually be an advantage from a macroeconomic perspective, such solutions would be penalised by the supervisors on the basis of the Commission's proposals. In the case of public guarantees under b), their terms may state that the financing bank must first be satisfied in the event of insolvency in order to collect the corresponding guarantee amounts. Any guarantee provided by a counterparty with an immaculate credit rating that can confidently be realised if the conditions are met might be regarded as entirely worthless because the Commission's proposal would require an insolvency procedure to be completed first. In both cases, this approach runs counter to the concept of valuing expected losses and will tend to have economically disadvantageous reactions for these institutions because of the threat of capital charges. In our opinion, case c) is in the interests of neither borrowers nor banks and, as we understand it, cannot also be the goal of this regulatory requirement.

18. Overall, the planned approach does not appear to use historical data and future expectations as the basis for estimating losses, but rather appears to develop a separate concept for regulatory purposes that is not substantiated any further and is unconnected to the expected loss. In addition, the intention of forcing the banks to resolve non-performing exposures quickly or, possibly, to sell them quickly, will generally strengthen the position of unregulated market participants that will then "collect" the loans they have purchased. This may result generally in both a risk agglomeration in the market not directly monitored by banking supervisors and in market behaviour that runs counter to consumer protection. It therefore triggers potentially undesirable incentives for short-term

measures. Ultimately, a longer period often results from extended, complex court and recovery processes, which in turn can also not be reduced by the rule. In particular, in many cases it does not involve the “wait and see” or “extend and pretend” strategies that are the focus of the restrictions, and that can only be assessed on the basis of an individual analysis. An individual analysis allows especially those measures to be identified that justify a longer period. In particular in light of the global grouping of NPEs by secured or unsecured, an appropriate approach would have to take into account corresponding measures of the bank that could lead to suspension and hence extension of the deadline, or that could reset the calculation of the period.

19. In addition, loans that are measured at fair value in accordance with IFRS 9 and for which no risk provisions have therefore been recognised are not treated appropriately by the proposed rule. For loans measured at fair value, Article 34 of the CRR applies “additional value adjustments” that could lead to an additional capital deduction. These loans should therefore be excluded from the rule because no risk provisions can be systematically recognised here and the valuation of these loans is already sufficiently conservative through the application of Article 34 of the CRR. Alternatively, fair value adjustments should be appropriately taken into account, e.g. as specific credit risk adjustments.

20. Irrespective of whether or not the Commission’s proposal is generally reasonable, it would lead to the underestimation of the actual risk provisioning in the case of non-performing loans to be treated using the IRBA; these loans are treated as non-performing in accordance with the definition in Article 47a of CRR 2, but they are not regarded as defaulted under Article 178 of the CRR. This is because such loans (in contrast to defaulted loans) must be backed by capital (positive RWAs). For this reason, the CET1 own funds requirements to be applied to these loans in accordance with Article 92 of the CRR would have to be added to the actual provisioning in Article 47c(1)(b) of CRR 2. Partial write-offs should be eligible as “other own funds reductions” pursuant to letter b) iii) if these partial write-offs are added to the exposure for the purpose of this regulation. This is necessary to avoid adverse effects of write offs on the capital ratios. According to this regulation credit institutions are incentivized to avoid partial write offs although both the ECB “Guidance to banks on non-performing loans” and the EBA “Draft guidelines on management of non-performing and forborne exposures” emphasize that when the bank has no reasonable expectations of recovering contractual cash flows of the exposure it should lead to a partial or full write-off of the exposure. For instance, in case of a secured exposure with a 5-year default vintage of 100 and an impairment of 50, the proposed prudential backstop would have no effect (factor of 0.4). If the bank however executes a partial write-off of 50, the remaining exposure would have a zero-impairment cover and suddenly the backstop would impact CET1. This creates a situation where any partial write-off would by definition be detrimental to the capital ratios of the bank. However, the only difference between a partial write off and a specific provision is that the partial write off reduces the accounting value of the exposure and thus the exposure value to be used for this regulation as well. If, however, the partial write off is added again to the exposure value for the purpose of this regulation then there is no difference between a partial write off and a specific provision with the result that partial write offs should be treated analogously. In order to avoid non-intended adverse effects the following sentence should be added after sentence 1: “A partial write off may be recognised as other own funds reduction pursuant to sentence 1 letter b) iii) if it is added to letter a) again for the purpose of this regulation.”

21. The COM, EBA and ECB proposals also differ in the detail. In the case of COM and ECB, the differences with regard to the coverage ratios must be scrutinised critically (number of years for secured loans, starting date for the measures). These differences also result in divergences in the case of existing definitions in COREP and FINREP and thus in disproportionate additional effort at the institutions. Harmonisation appears to make sense as a matter of principle. However, the requirements in the ECB Guidance relating to years and coverage ratios should not serve as a model for the COM proposals, because the former were consciously introduced in combination with a comply-or-explain mechanism in order to reflect the complexity of the issue through the analysis of individual instances.

22. In our view, there is no need to include an "NPE definition" in accordance with Article 47a in the CRR in addition to the definition of non-performing loans and to apply the provisioning backstop on this basis. At present, the institutions are in any case revising the definition of default in Article 178 of the CRR (EBA/GL/2016/07) published by the EBA in 2016 and required to be implemented by 1 January 2021. This clarification as good as eliminates the differences in the definition of default in Article 178 of the CRR and of NPEs in Regulation (EU) No 680/2014 Annex V (FINREP) starting in 2021 (e.g. default because of a further forbearance measure in the good behaviour period; strict rules governing recovery). Amending the CRR makes it more difficult for the institutions – especially IRBA institutions because of the diverging implementation periods and the model change that must be approved in the case of an amendment – to harmonise the CRR definition of default and the NPE definition. The same applies to the definition of forbearance measures in Article 47b of CRR 2. In this case, too, reference should be made to the existing FINREP classification in order to avoid inconsistencies and unnecessary implementation effort. In general, it must be stated that existing data from the reporting system should be used as far as possible in light of the implementation costs.

23. An editorial error appears to have crept into Article 47c(2) points (c) and (d) of CRR 2. We think that in both of these cases, it should read "as of the first day **after** the second year" rather than "as of the first day of the second year". The same applies to Article 47c(3) points (o) and (p) of CRR 2. The explanation on page 11 indicates that this means "after the defined time period", which is why it is followed in parentheses by "(i.e. after two years for unsecured NPEs and after eight years for secured ones)". For unsecured loans, this would also correspond to the requirements of the Addendum to the ECB Guidance on non-performing loans, which expects 100% coverage of unsecured loans through value adjustments after two years and not already on the first day of the second year.

24. The reference date of 14 March 2018 for new NPEs stipulated in Article 469a of CRR 2 should be reset to 1 January 2019 at the earliest or to a date after the rule has come into force, because defining a base date for initial classification as an NPE represents a new requirement. In addition, there is a need for an additional transition period for IT implementation, because this will be anything but trivial. The Commission's draft does not provide for any implementation period. Because the concrete requirements will still be the subject of discussions in the legislative procedure and amendments can therefore be expected, initial application should be set to at least 18 months after the regulation amending the CRR comes into force, and the initial application date should not be before 1 January 2021. This would also harmonise the timing with the Addendum to the ECB Guidance, which does not provide for initial inclusion in the SREP until 2021.