Minimum loss coverage for non performing exposures

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The Committee on Economic and Monetary Affairs adopted the report by Esther DE LANGE (EPP, NL) and Roberto GUALTIERI (S&D, IT) on the 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.

This proposal for the amendment of Regulation (EU) No 575/2013 on capital requirements (CRR) provides for a statutory prudential backstop against any excessive future build-up of non-performing exposures (NPEs) without sufficient loss coverage on banks' balance sheets.

The establishment of a comprehensive strategy to address the issue of NPEs is an important goal for the Union in its attempt to make the financial system more resilient.

The committee recommended that the European Parliament's position adopted at first reading under the ordinary legislative procedure should amend the Commission's proposal.

Non-performing exposures: the amended text stressed that '**exposure**' shall include any of the following items, provided they are not included in the trading book of the institution:

- a debt instrument, including a debt security, a loan, an advance and a demand deposit;
- a loan commitment given, a financial guarantee given or any other commitment given, irrespective whether revocable or irrevocable, except undrawn credit facilities which may be cancelled unconditionally at any time and without notice, or that effectively provide for automatic cancellation owing to deterioration in the borrower's creditworthiness.

The exposure value of a debt instrument that was purchased at a price lower than the amount owed by the debtor shall include the difference between the purchase price and the amount owed by the debtor.

It is stressed that **consumers should not be deemed exclusively responsible** for the cause of the severe build-up of NPEs during the years of the financial crisis. In some Member States, **housing bubbles** were caused by an over-reliance on the growth of house prices.

Parts of the banking sector contributed to this through **imprudent lending practices**.

Prudential back-stops: the prudential backstop shall not prevent competent authorities from exercising their supervisory powers. It should be possible for the competent authorities to go, on a **case-by-case basis**, beyond the requirements under this Regulation for the purpose of ensuring sufficient coverage for NPEs.

Forbearance measures: forbearance measures shall aim to **return the borrower to a sustainable performing repayment status** and shall comply with EU consumer protection requirements, but may have different justifications and consequences. It is therefore appropriate to provide that a forbearance measure granted to a non-performing exposure shall not discontinue the classification of that exposure as non-performing unless certain strict discontinuation criteria are fulfilled.

Calendar: the longer an exposure has been non-performing, the lower the probability for the recovery of its value. Therefore, the portion of the exposure that shall be covered by provisions, other adjustments or deductions shall increase with time, following a pre-defined calendar. NPEs purchased by an institution shall thus be subject to a calendar that starts to run from the date on which the NPE has originally been classified as non-performing, and not from the date of its purchase.

A uniform calendar shall be applied irrespective of whether the exposure is non-performing because the obligor is past due more than 90 days or if it is non-performing for other triggers. The prudential backstop shall be applied on an exposure-by-exposure level.

Secured and unsecured NPEs: secured NPEs are generally expected to result in less of a loss than unsecured NPEs, as the credit protection securing the NPE gives the institution a specific claim on an asset or against a third party in addition to the institution's general claim against the defaulted borrower. In the case of an unsecured NPE, only the general claim against the defaulted borrower would be available. Given the higher loss expected on unsecured NPEs, a **stricter calendar** shall be applied, i.e. a calendar of **three years**.

In order to allow institutions and Member States to improve the efficiency of restructuring or enforcement proceedings, as well as recognise that NPEs secured with immovable collateral and residential loans guaranteed by an eligible protection provider as defined in Regulation (EU) No 575/2013 will have a remaining value for a longer period of time after the loan turned non-performing it is appropriate to provide for a calendar of **nine years**. For other secured NPEs a calendar of **seven years** shall apply until full coverage has to be built up.