



Opening Statement by Gráinne McEvoy, Director of Consumer Protection, at the Oireachtas Committee on Finance, Public Expenditure and Reform, and Taoiseach

Good afternoon. Thank you for your invitation to appear at the Committee today to discuss the proposed measures published by the European Commission in March 2018 aimed at addressing the resolution of non-performing loans. I am joined by my colleague Adrian Varley, Head of the Banking Supervision Analysis Division.

I will provide an overview of the recently published European Commission package on Non-Performing Exposures (NPEs), which was released in March 2018. The proposals are a key aspect of the Commission's commitment to delivering on the Council of the EU's Action Plan on Non-Performing Loans (NPLs) of July 2017. The package consists of two legislative proposals:

- A proposal for a Regulation amending the Capital Requirements Regulation (CRR), which introduces minimum coverage requirements for incurred and expected losses on future NPEs¹ arising from newly originated loans; and
- A proposal for a Directive on credit servicers, credit purchasers and the recovery of collateral.

Discussion on the proposals in the context of the European policy making process are at a very early stage. The Central Bank is evaluating the potential impact these proposals will have on the Irish market. The Central Bank is also providing technical advice to the Department of Finance as part of these political negotiations and will continue to engage as discussions progress.

The level of NPLs increased significantly after the onset of the economic and financial crisis in 2007. High levels of NPLs pose a significant threat to economic stability and to the orderly functioning of the banking system across the European Union. High levels of NPLs also result in loss of confidence in banks, making it harder for them to raise capital, to borrow, to reduce interest rates and to make new loans to businesses and households. Loan sales can play an important role in transferring risks from banks to other types of investors, which reduces vulnerability in the banking system.

¹ NPEs include NPLs, non-performing debt securities and non-performing off-balance-sheet items. NPLs represent the largest share of NPEs and therefore these terms are commonly used interchangeably.



The Central Bank engages both at the European level (with the European Banking Authority, in its standard setting capacity, and European Central Bank Single Supervisory Mechanism, in its supervisory capacity) and domestic level (via direct supervisory engagement with the banks) to assist in the policy response to NPEs. The specific proposals at hand will be subject to significant scrutiny as part of the European legislative process and are likely to be amended considerably in advance of their implementation into law.

The proposals aim to prevent the build-up of high levels of NPEs on banks' balance sheets, through the incentives produced by increased provisioning requirements, and further to develop secondary markets for NPEs, with the aim of removing undue obstacles to loan servicing by third parties and to the transfer of loans to third parties. The package also aims to enhance the speed of recovery of collateral for business loans, through the introduction of an Accelerated Extrajudicial Enforcement Procedure (AECE).

The Commission's proposal for a Regulation establishes a minimum coverage requirement whereby banks must put aside certain amounts of money to cover incurred and expected losses caused by loans that turn non-performing. Where the bank does not meet the applicable minimum level, it will have to make a deduction from own funds. The minimum coverage requirement increases gradually depending on how long the exposure has been classified as non-performing.

The proposal sets out different coverage requirements for secured and unsecured exposures. When an NPE is secured, the required coverage levels for the secured part of the exposure can be phased in over a period of eight years, while unsecured exposures will be phased in over two years. The Commission's reasoning for this differentiation is that recovery rates are on average significantly higher for secured NPEs than for unsecured ones. It is also proposed that there would be different levels of coverage required depending on the criteria under which an exposure is classified as non-performing (i.e. whether it is past due or considered that the borrower is unlikely to pay).

Concerning the minimum coverage requirement, the Central Bank of Ireland is broadly supportive of the policy direction of the Commission's proposal. Without supervisory challenge, banks have been inclined to employ a 'wait and see' approach with respect to provisioning which means that new NPLs can build up to cause bank specific or system-wide problems. The



Commission's proposal, which would apply only to new loans originated after 14 March 2018 which become non-performing, would ensure banks have suitable levels of provisions, and if not, must hold appropriate capital for this risk.

The second aspect of the package is a proposal from the Commission for a Directive on credit servicers, credit purchasers and the recovery of collateral.

The proposal standardises the regulatory regime by seeking to harmonise the definition, authorisation, supervision and conduct rules applicable to credit servicers and credit purchasers. This legislative initiative aims to further develop secondary markets for NPLs, with the aim of removing undue barriers to loan servicing by third parties and to the transfer of loans to third parties.

The standardisation of a regulatory regime for credit servicers and credit purchasers is broadly supported as the proposal states that the assignment of creditors' rights under a credit agreement should not affect the level of protection to consumers in any way. To this end, the proposal provides that consumer protection rules will continue to apply in order to ensure the same level of protection, irrespective of who owns or services the credit and irrespective of the legal regime in force in the Member State of the credit purchaser or the credit servicer. This high level principle mirrors the objectives of the Credit Servicing Act 2015, which sets out a regulatory regime in respect of credit servicing firms, and brings such firms into the Central Bank of Ireland's regulatory remit.

Furthermore, the proposal does not require that credit purchasers must be directly authorised or regulated, but that they must appoint credit servicers or credit institutions who are regulated. This is in line with the current legislative regime, which requires an unregulated loan owner to appoint a credit servicing firm who is authorised and regulated by the Central Bank. Credit servicing firms are subject to all the Central Bank's statutory Codes and Regulations.

The second part of the proposal also aims to enhance the protection of secured creditors by introducing a more efficient method of realisation of security called the Accelerated Extrajudicial Collateral Enforcement (AECE) procedure. The aim of the AECE procedure is to increase the efficiency of debt recovery through the availability of an accelerated mechanism for the recovery of collateral for creditors of business borrowers only. This procedure would



only be accessible when agreed upon in advance by both the lender and borrower. It is not available for consumer loans and for real estate serving as the borrower's primary residence. It may only be effected where it has been explicitly stipulated in the original loan contract. While banks can enforce collateral under national insolvency and debt recovery frameworks, the process can be slow and unpredictable. The proposed mechanism is intended to introduce a more efficient mechanism, while at the same time balancing interests of creditors and borrowers.

Thank you for your attention and we look forward to addressing your questions.