German Banking Industry Committee

Die Deutsche Kreditwirtschaft

Comments

Draft Guidelines on loan origination and monitoring

Register of Interest Representatives
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Contact:

Torsten Jäger	Julia Thomas
Division Manager	Division Manager
Telephone: +49 30 1663-2160	Telephone: +49 30 1663-3110
E-Mail: torsten.jaeger@bdb.de	julia.thomas@bdb.de

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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 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 approximately 1,700 banks.

Coordinator:
Bundesverband deutscher Banken e. V.
Burgstrasse 28 | 10178 Berlin
Telephone: +49 30 1663-0
Fax: +49 30 1663-1399
www.die-deutsche-kreditwirtschaft.de

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General comments (re Question 1)

The intention behind the Draft Guidelines is understandable in principle. In their own interests and those of their clients, German institutions pursue a responsible lending policy based on existing regulatory requirements. Among other things, this is also evident from the low NPL ratios.

Nevertheless, we wish to point out that – in light of the legally prescribed requirements governing creditworthiness assessments – the banking business is and must also necessarily be inherently risky in order to perform to the economically desirable functions of the financial sector. For that reason, NPLs cannot be entirely avoided.

However, the design of the Draft Guidelines is not expedient. Pillar 2 requirements should be **proportionate and principle-based**; these principles are clearly not being observed here. Many requirements are **too sweeping** and do not sufficiently consider the nature, size, risk and complexity of the transactions, as well as the different sizes and orientations of the credit institutions. In our view, it is not appropriate to apply all the requirements to all the institutions on a one-size-fits-all basis.

Application of the **principle of proportionality** is expressly described in paragraph 12ff. in the "Background and rationale" section, but we believe that this is not sufficient for ensuring any practicable implementation of the Guidelines. Ultimately, every requirement would have to be assessed by individual institutions in light of the principle of proportionality. There is a risk that supervisory authorities and auditors who adopt a conservative stance will not permit the use of necessary exemptions, resulting in competitive disadvantages for certain institutions in the EU. Many requirements are also declared to be minimum ("at least") requirements, which contradicts a proportionate application of the requirements. For this reason, **the wording "at least" should be deleted throughout the entire document** and replaced by a designation as examples or other formulations that underscore the principle-based applicability of the Guidelines.

There is therefore a crucial need to redraft the Guidelines in a considerably more principle-based manner and to **integrate specific opening clauses and materiality aspects into the text of the Guidelines**. One solution, for example, could be to give the institutions discretion to define the specific arrangements for the individual requirements – depending on the risk and complexity of the lending transactions. This would be an adequate way to manage both small-scale lending business and large-volume corporate banking rationally in the institution's processes.

Annexes 1 to 3 in the Draft Guidelines should not be understood as minimum requirements, but as a supervisory recommendation in the sense of examples. The wording in the relevant paragraphs should be amended accordingly.

The German Banking Industry Committee is recommending that the Guidelines should be **substantially streamlined overall by removing overly detailed requirements and the Annexes**. **If specific lists** of data, ratios, etc. are to be retained, as a minimum they should be **designated as examples** and qualified by “where relevant/appropriate” or similar phrases. The specific comments contain suggestions for how the Guidelines could generally be realigned to a greater extent with the principle of proportionality.

Something we would find extremely useful would be the proven practice in Germany of **distinguishing between lending business that is and is not relevant for risk purposes** when meeting the requirements. In that context, no specific value limits are specified by supervisors. Rather, the distinction must be made independently by each institution from a risk perspective. It is generally accepted that the retail business is normally classified as lending business that is not relevant for risk purposes.

We also think it is advisable not to repeat existing regulatory requirements (e.g. of the EBA Internal Governance Guidelines) in the present Guidelines, or merely to adapt them to the specific case of credit risk. This makes the requirements less clear overall and harbours the risk of contradictions.

If they remain unchanged, the requirements in the Draft Guidelines would lead to **significant obstacles in taking out a loan, both for consumers and for professionals**. Besides extensive information requirements, bureaucratic counselling interviews and longer processing periods, they could also make loans more expensive because the institutions would ultimately have to pass on the considerably higher analysis and processing costs to their clients due to the current low interest rate environment. For example, the requirements in the commercial lending business focus on financing transactions for large clients. In quantitative terms, however, the bulk of the loans – including in the SME sector – are in smaller segments with lower Value of Risk. There are also no exemptions here that would allow uncomplicated lending to continue to be possible in the small-scale lending business without excessive process costs.

Examples include the required **sensitivity analyses** (paragraphs 101, 114, 121, 143, 144, 145 and 146), which we regard as too extensive and that should only be applicable where appropriate in specific cases (see also the specific comments under 2.). For unsecured consumer loans, for example, individual sensitivity analyses are not necessary from a risk perspective due to the low credit amounts. For SMEs, this would moreover pose an overall threat to loan financing in particular for SMEs. There are probably only a few companies, for example, where one or more of the potential events listed in paragraphs 145 and 146 would not compromise their ability to repay a loan. Are the institutions being expected to engage in a massive analysis effort in order, ultimately, to reject many loan applications because of very unlikely imponderables? If requirements are worded too strict and formally, implementing the Guidelines could, in the end, trigger a credit squeeze and shifts to unregulated lending markets and actors. This would result in eroding the business model of most European institutions, especially smaller ones that operate regionally. That is also not likely to be in the interests of the banking supervisors. Furthermore, this runs counter to the political objective of preserving diversity in the banking industry, a factor that – wherever it was present – contributed significantly to financial stability in the past as well as to the diversification of loan financing options, especially for SMEs.

Paragraph 15

Under paragraph 15 of the "Background and rationale" section, **consumer protection rules** should not be subject to the principle of proportionality and should be applied regardless of the size of the institution and the size/complexity of the loan. The current wording could be misunderstood to mean that e.g. all subsections of section 5 regarding consumers fall under this exclusion. If this is not meant - as explained in the Public Hearing on 20 September 2019 - at least a clarification should be made as to which particular requirements the statement refers to. Otherwise, this approach would be opposed to almost all national and European legislative measures. Because consumer protection is so important, binding application of the rules for all institutions is certainly important and reasonable. However, there needs to be a proportionate assessment, for instance in line with the total loan amount and the purpose of the loan. For example, it should be noted that small loan amounts (EUR 200 – EUR 75,000) quite rightly are already not subject to the full consumer protection requirements of the Consumer Credit or Mortgage Credit Directives. Applying the consumer protection rules to all loans would be far too sweeping and not consistent with client wishes for a simple, quick and uncomplicated lending process, especially in the area of small consumer loans. It is also not necessary from a risk perspective to apply the far-reaching rules to micro-loans, which would constitute considerable effort for the institutions and necessarily make the loans more expensive for clients. That is why individual requirements should also be supplemented by materiality aspects, opening clauses, etc., in the case of consumer loans.

At a general level, it should be noted that the existing Consumer Credit Directive (CCD) and Mortgage Credit Directive (MCD) have a protective effect for third parties with regard to their requirements governing creditworthiness assessments, in the sense that consumers can assert individual claims from breaches of these requirements. This sort of understanding corresponds to the high level of consumer protection that is practised in creditworthiness assessments in the consumer lending sector. In terms of the business sector, the Guidelines would also establish a very high level of protection for companies. **However, it should be clarified that this protection is of a merely supervisory nature and does not have any consequences under civil law.**

Even if industry feedback is reflected in the final Guidelines, there will be far-reaching consequences for the lending business and lending processes. Inter alia, IT-support has to be adapted and staff has to be further qualified. For this reason, the institutions need **an implementation period of at least two years** (once the translated versions are available). As all the requirements are ultimately interrelated, the time line for the entire Guidelines should be shifted. Additionally, the Consumer Credit Directive and Mortgage Credit Directive are currently in the process of being evaluated or reviewed. It cannot be ruled out in this context that there will be changes to the creditworthiness assessment for consumer loans.

Implementing the requirements will involve considerable effort and expense for the institutions. The effective date of the Guidelines should therefore be harmonised with the evaluation of the EU directives in terms of both content and timing. In light of this, the Guidelines should not apply before **30 June 2022 at the earliest**.

Specific comments

Scope of application, definitions (re Question 1)

Paragraph 9
We presume that the term **"public sector entities"** refers to public institutions, foundations, regional or local authorities and corporations. We therefore believe it would be appropriate to include companies established under private law that are wholly in public ownership (municipal companies) in this category and to exclude them from the scope of application. We would ask the EBA to clarify this.

Paragraph 10
Although it is emphasised at several points that the requirements are supposed to apply in part only to "newly originated loans" or to "significant increases" (e.g. paragraph 83), there are statements at several points that "amendments to existing loan agreements or the loan amount" are also affected (paragraph 97). In any event, the MCD and CCD only cover the conclusion of the loan agreement and any significant increase in the total amount of credit (Article 8(1) and (2) of the CCD; Article 18(1) and (6) of the MCD). Any extension beyond the existing scope of application is therefore not proportionate and runs counter to the legal provisions. Only the conclusion of a new agreement due to significant changes should lead to the application of Section 5.
In addition, it is questionable whether, based on the existing legal position, institutions actually have the power to enforce obligations resulting from the Guidelines on borrowers in the case of "legacy agreements". The EBA should therefore rule out the inclusion of legacy agreements if the changes do not result in any significant increase in the loan amount.
We presume that loans that are merely renewed internally do not fall within the scope of this paragraph. At least in the case of small-scale loans, loan monitoring is largely automated over the credit period. Human intervention is limited to situations where risk signals arise. This approach is risk-sensitive and efficient.

In addition, the entire Section 6 should also apply only to new or renegotiated loans.

Paragraph 14
The proportionality criteria correctly given here cannot be applied in practice if, at the same time, the **qualification "at least"** is used at many points, which runs counter to this key principle for implementing and assessing the requirements set out in these Guidelines. In loan processing, this would result in significantly increased requirements that would often be impossible to implement in individual cases, or could only be implemented with a significant increase in effort and costs that would not be proportionate to the credit volume, return and value added of the assessment. By contrast, the qualification "at least" indicates minimum requirements and in our view should be deleted in all cases. Instead, illustrative lists or the wording "where relevant" would be appropriate, as these would underscore the principle-based nature of Pillar 2 Guidelines. A principle-based approach is necessary not least because the

structure of the lending and loan monitoring processes associated with the different transaction types is institution-specific. Excessively rigid requirements do not give the institutions the flexibility and efficiency they need for the lending business.

Even though the Guidelines contain guidance on the principle of proportionality, we take the view that they are not, in principle, applicable to the **promotional banking** practised in many European countries. As an example, we wish to point out that pricing in the promotional banking is largely determined externally by national law. Calculating individual transactions would therefore not be expedient, including in light of the fact that promotional banks do not seek to maximise profits. Moreover, in some cases promotional loans can only be approved if the borrower’s income does not exceed a specific limit – for example with loans to students –, whereas by contrast, income that falls below particular limits is relevant in the competitive lending business. We therefore wish to propose the following addition:
“*<u>The specific characteristics of certain transaction types, such as the promotion-related business, may mean that parts of these Guidelines are not applicable in these areas.</u>*”

Paragraph 15
Lenders as defined in the directives listed in paragraph 12 should be added here, in order to ensure a consistent application of the requirements.

Paragraphs 16/17
The general validity of the definitions contained in a range of directives is stipulated in paragraph 16. Though, the definition of a “residential real estate loan” contained in paragraph 17 restricts the broader definition in Directive 2014/17/EU to a loan secured by residential real estate property. This means that loans to buy a property that are not secured by real estate would not be covered by the Guidelines (in contrast to the MCD). The EBA should clarify whether loans to buy a property that are not secured by real estate are excluded from the scope of application, and why.

Paragraph 17
The distinction between commercial real estate (CRE) and residential real estate (RRE) should be tightened. Mixing the designated use of the property together with the nature of the owner (natural person or legal entity) appears to us to be complicated and unnecessary. In addition, it results in discrepancies compared with the CRR. Point (75) of Article 4 of the CRR defines residential property as a residence that is occupied by the owner or lessee of the residence. The nature of the owner is irrelevant. As a result, a leased residence owned by a corporation would be classified as CRE under the present EBA Guidelines, but as RRE under the CRR. It would also be inadequate to apply the strict CRE requirements to owner-occupied commercial real estate, as the ability to repay the loan in the case of commercial real estate depends largely on the economic strength or cash flow of the client.

The separate mention of social housing in the definition of CRE should be deleted. It is still unclear whether this means that social housing cannot be RRE. The CRR does not make any distinction here.

Additionally, in the same way as the definition of a CRE loan, the definition of an RRE loan should be unconditionally linked to the purpose of the loan as a property loan for the construction, acquisition or renovation of RRE. Otherwise unequivocal classification is not possible. The broad collateral purpose agreements (so-called "*Sicherungszweckerklärungen"*) that are common in Germany and offer banks a high level of security would no longer be compatible with this definition.

As far as we can see, where loans to consumers are concerned there is no explicit requirement for the EBA Guidelines to apply "only" to consumer credits within the meaning of Directives 2008/48/EC and 2014/17/EU. The following definition should therefore be added to paragraph 17: "<u>Consumer credit means a loan within the scope of Directive 2008/48/EC and Directive 2014/17/EU.</u>"

In light of the principles of materiality and proportionality, it should be clarified that small craft enterprises and traders, members of the independent professions, self-employed persons, part-time entrepreneurs and casual freelancers who do not require commercially organised business operation do not fall within the definition of "professionals". In practice, loans to these groups of clients are often implemented using retail-style credit standards and processes. The Guidelines should clarify that the **credit standards for retail clients or the retail business can be applied to these groups of clients, with the necessary modifications**.

The definition of "shipping finance" does not make a sufficiently clear distinction between finance that is linked solely to the cash flow from operating the ship and general corporate finance using shipping as collateral. We therefore suggest adding "primarily" or "solely" before "…dependent on the cash flow…" in line four of this definition in paragraph 17.

To ensure completeness and Europe-wide implementation, terms such as "**sustainable finance**" (see paragraph 50) should also be defined in addition to the term "green lending", as long as no consistent specifications exist for the terms at Level 1 regulation.

Date of application (re Question 2)

Paragraph 18

Application from 30 June 2020 appears to us to be simply unrealistic. The detailed requirements will cause a wide-ranging and substantial need for modifications. The requirements and gap analysis, specialist and technical designs, IT implementation, modifications to internal policies, any application and integration testing that may be required, and training for staff involved in the credit processes cannot be implemented within a such a short time frame, among other reasons also because of the extensive requirement to evaluate software modifications and their correct technical implementation, including test procedures. The institutions require an implementation period of **at least two years** following publication of the final translated versions. The effective date of the Guidelines should be harmonised with the evaluation of the EU directives (CCD and MCD) in terms of content and timing. In light of this, the Guidelines should not apply before 30 June 2022 at the earliest.

Governance (Section 4) (re Questions 5 and 6)

Paragraph 21
In point c., “defining” should be replaced by “approving” in each case. There is no need for the management body to prepare policies itself.

Paragraphs 22 – 25
The EBA Guidelines on internal governance already contain very comprehensive requirements for implementing an appropriate corporate and risk culture. It is not clear to us why the EBA is now duplicating these requirements and incorporating them into these Guidelines specifically for loan origination. If the intention is to emphasise the importance of an appropriate risk culture again for this area, a reference to the EBA Guidelines on internal governance in paragraph 22 would be perfectly sufficient. **Paragraphs 23 – 25 should be deleted without replacement.**

Paragraph 26
Smaller credit institutions in particular would be overwhelmed by a detailed specification of the desired composition of the credit portfolio, including the composition of collateral. Such a high level of advance specifications would ultimately be an obstacle to business and hamper alignments especially at regional institutions, for example tracking structural changes in their regions.
We propose streamlining the requirement and rewording it in a more principle-based manner:
”The credit risk appetite, credit risk strategy and overall credit risk policy should be aligned with the institution’s overall RAF. <u>The institution’s credit risk appetite should specify the scope and focus of the total credit risk of the institution.</u>”

Paragraph 27
As a rule, the budgeting process contains additional cost and/or capital components in addition to the regulatory or economic capital intended to be used to mitigate risk. The second sentence should therefore be deleted. In addition, the requirement should be worded as non-binding:
“When defining the credit risk appetite, institutions ~~should~~ ~~ensure that~~ <u>may consider</u> both top-down (e.g. setting high-level targets) and bottom-up perspectives (e.g. operationalisation of these high-level targets). ~~These perspectives should be also supported by an adequate budgeting process.~~”

Paragraph 76
In point e., “commercial” should be replaced by “financial” (in line with the SREP guidelines).

Regarding point g., we wish to point out that an independent second opinion is not necessary for each and every creditworthiness assessment. In Germany, loans that are not risk-relevant are decided in a “single vote procedure”. The decision on the applicable risk relevance limit is a matter for the institutions and thus enables appropriate, lean lending processes in the small-scale lending business. Additionally, it is not clear how the requirement should be understood

with regard to the credit risk analysis. At any rate, there can be no requirement to duplicate work within the risk management function.
To avoid misinterpretations, point g. of para. 76 should be clarified as follows:
"*providing information, in which cases an independent/second opinion to the creditworthiness assessment is required.*"

Anti-money laundering and combating terrorist financing (re also Question 4)

Section 4.3.1, paragraphs 40ff.
The German Banking Industry Committee supports the challenge to society as a whole of combating money laundering and terrorist financing. In our opinion, however, the statements made in the Guidelines at this point and with this content do not serve the goal of effectively combating money laundering and terrorist financing. This applies both legally and structurally and in terms of substance.

The European Supervisory Authorities have published Guidelines on risk factors for preventing money laundering and terrorist financing. These address the due diligence needed to prevent money laundering and terrorist financing. They require each institution to identify the relevant product-or country-specific risks and to align the corresponding due diligence measures with those risks. From a legal and structural perspective, the present Guidelines issued for consultation should therefore merely include a reference to the aforementioned Guidelines on risk factors. If the EBA considers it to be necessary to define additional requirements for preventing money laundering and terrorist financing specifically for the lending business, they should be documented in the aforementioned Guidelines on risk factors. Preventing further fragmentation in the legal system in the area of the regulatory regime for preventing money laundering and terrorist financing is a vital requirement for creating legal certainty for obliged entities under money laundering legislation and for increasing the effectiveness of combating money laundering and preventing terrorist financing. Spreading requirements for efficiently combating money laundering and preventing terrorist financing across various guidelines, as proposed here, would be detrimental to those goals – increasing legal certainty and effective combating of money laundering and terrorist financing.

In terms of substance, the statements made in Section 4.3.1 are also, in part, not appropriate:

- For example, paragraph 40 b. requires *"**any third party** that might be associated with the credit facility"* to be identified. This represents a departure from the principle underlying the Money Laundering Directive that only precisely defined persons have to be identified (for example the contracting party), and leaves obliged entities and parties associated with a credit facility totally in the dark about who should be identified under the best practice proposed in the Guidelines. Additionally, this proposal to globally identify any and all persons who might possibly be associated runs counter to the risk-based approach in the Money Laundering Directive. There is no objective reason for the introduction of an identification obligation for all types of collateral providers tucked away in this requirement, since merely receiving loan collateral is not associated with any money laundering risk. No money flows at this point. In addition, physical collateral is commonly provided. By contrast, extending the identification obligation would have material adverse effects in practice and would considerably impair/complicate the lending business in many areas (e.g. in the area of syndicated loans). It is not uncommon in these cases to have a high double-digit number of collateral providers (mostly referred to as "guarantors"), who also frequently change during the life of a credit relationship. It is almost impossible in practice to identify such guarantors promptly and completely. Moreover, a large number of additional questions are linked to such a requirement, which the EBA does not answer in the short Section 4.3.1. In light of this, there is an urgent need to define the term "third party" in greater detail and to clarify in this context that it does **not** include loan collateral providers. As a minimum, there is a need for clarification that it is sufficient in relation to loan collateral providers to perform a very limited check on them if there is a cash flow or transfer of assets at some point.

- The requirement to verify the source of any funds that the client uses to service the loan appears to apply to any and all credit relationships. Admittedly, the Guidelines talk of "risk-sensitive measures" in this context. However, the impression is given in the overall context that the source of the funds must be verified in each and every credit relationship. If this understanding is correct, the source of the funds used to repay the originated loan must be verified regardless of the risk classification of the client as a low, medium or high risk, and/or regardless of the type of loan (e.g. a simple consumer loan in the retail business or a complicated loan transactions, such as in (cross-border) syndicated loans). In light of the requirements of the Money Laundering Directive, this appears to be too sweeping. The Money Laundering Directive only requires the source of assets that are used in the course of the business relationship with the credit institution or the transaction to be clarified in the case of certain client groups that are subject to enhanced due diligence. The undifferentiated extension of this requirement to each and every credit relationship, regardless of the client group, would also run counter to the risk-based approach enshrined in the Money Laundering Directive.

Technology (re Question 3)

Paragraph 47

In the opinion of GBIC, it is extremely questionable whether the stated requirements (especially in point c. of paragraph 47) also allow artificial intelligence to be deployed (meaning programmes that continue evolving through machine learning, and whose outcome cannot be completely understood or predicted). This would thwart genuine innovations. We recommend consulting DG-FISMA's ROFIEG (Regulatory obstacles to financial innovation) on this issue.

The comparisons required by point d. can only be implemented to a limited extent, not least because it is not clear what is meant by "traditional methods". Moreover, this requirement is superfluous because the overarching requirements governing the suitability of methodologies and processes must be observed (see Governance guidelines, paragraph 141). We are therefore advocating deletion.

ESG risks (re Question 3)

Paragraph 48
Under **paragraph 14** of the "Background and rationale" section, the requirements of Section 4 should be implemented by the institutions taking into account the principle of proportionality. It is not clear how the specific policies to do this should look in the context of ESG.
In accordance with **paragraph 48**, institutions should include ESG factors as well as risks and opportunities related to ESG in their risk management policies, credit risk policies and procedures. Institutions are expected to adopt a holistic approach to doing this.

As a general principle, we understand the challenges involved in combating climate change and are ready to participate in the policymaking process as part of a sustainable finance strategy. We welcome the launch of further concrete steps towards shaping a financial sector based on sustainability aspects. However, based on the issues raised by the EBA, we wish to note that the individual strands of work at EU level on the issue of sustainable finance are only partly taken into consideration.
In particular, there is no reference whatsoever to the taxonomy currently under development and to the associated technical evaluation criteria. The taxonomy in particular is expected to serve in the future as the basis for a common understanding of ESG criteria. In addition, already existing voluntary initiatives in the area of green lending, such as the green loan principles, are not mentioned at all. It would also be helpful if the reference framework were to be pointed out. For example, some of the requirements make reference to the recommendations and policies of the Task Force on Climate-related Financial Disclosures, without making this clear, so a more transparent approach would make sense here.

Article 98(8) of CRD V requires the EBA to assess the inclusion of ESG in the SREP and in internal risk management. Among other things, the report to be prepared by 28 June 2021, on the basis of which the Guidelines may be amended or prepared, should highlight a uniform definition of ESG risks and the development of qualitative and quantitative criteria for the assessment of the impact of such risks.

In light of the EBA's new mandate under Article 98(8) of CRD V, we believe that the inclusion of ESG factors in the risk management policies and credit risk processes proposed in the Guidelines is premature. Despite the necessary need for action to combat climate change, hasty legislative reactions that will burden the institutions must be avoided. It would make little sense for each institution to develop individual policies in the short term.

Paragraphs 49 and 50
As part of their credit policies and procedures, **paragraph 49** requires institutions that originate or plan to originate "green credit facilities" to develop specific policies and procedures governing granting and monitoring these credit facilities. Under **paragraph 50**, these should

be positioned within the context of the overarching objectives, strategies and policies related to the institution’s sustainable finance:

- It is not clear to us why institutions should develop objectives, strategies and policies for sustainable finance in the first place, which should then be specified in greater detail for “green credit facilities”.
- We are critical of the fact that no consistent interpretations of the terms are developed within the Guidelines. The definitions in Section 2 attempt to define the term “green lending”. By contrast, other terms such as “ESG” or “sustainable finance” are not explained.
- In light of the fact that there is not yet any common understanding of these terms due to the lack of any industry-wide definitions, and there are no generally accepted standards, each individual institution would itself be required to make an appropriate distinction. As stated in the cost-benefit analysis, we therefore do not see how only including ESG factors in the Guidelines can help counteract the fragmentation of ESG credits and create greater comparability between the institutions. This objective can only be achieved through a common understanding of sustainability, but this is only expected to happen when the taxonomy is available.

Paragraphs 51– 53

The interaction between the “holistic ESG approach” described in paragraph 48 and the pressing need to consider risks associated with climate change required by paragraph 51 is not clear.

Because no industry standard has yet emerged from a methodological perspective, the only possible analysis of ESG risks is a qualitative one. Further developments at European level should be awaited in this context. We assume in this respect that the requirement to consider physical or transition risks in the credit risk policies and procedures does not extend at the present time to the measurable inclusion of those risks.

Paragraphs 52 and 53

We also assume that physical and transition risks can be considered at the level of portfolios or client groups (geographical location, industry, etc.) in the context of credit processes. The individual assessment of these risks at the level of individual borrowers is neither sensible nor possible with regard to most of the characteristics given. We would ask you to clarify this.

Credit risk policies and procedures (re Question 4)

Paragraph 35

The information listed in Annexes 1 to 3 to which point b. of paragraph 35 and paragraphs 41, 92 and 94 and point d. of paragraph 132 in other sections refer is too extensive to be a minimum standard and should therefore not be declared to be binding in full. A minimum standard should refer to the mandatory relevant criteria from a risk perspective and leave scope for a risk-based extension, depending on the complexity and particular features of the transaction in question. The reference to Annex 1 in its entirety would mean, for example, that it would be almost impossible to implement simplified, uncomplicated sales financing for low-value consumer goods at the point of sale. In addition, the wording "at least" contradicts the principle of proportionality that is expressly mentioned in paragraph 14 and in paragraph 14 of the "Background and rationale" section, and which we believe must be taken into consideration as a core principle for implementing and reviewing the requirements documented in these Guidelines.

Point h. of paragraph 35: In principle, we can understand the requirement to document credit decisions that do not conform to the strategy or exceptions from the credit risk strategy or the internal policies. However, the materiality principle should be reflected in the requirement: "*requirements and associated procedures for the handling and approval of exceptions and <u>material</u> breaches […]"*

Paragraphs 43ff.
If an institution ascertains that no leveraged transactions are generated or acquired, we presume that more far-reaching internal rules are unnecessary. We would ask the EBA to clarify this.

Paragraph 44
In our view, the requirement to use fixed (quantitative) definitions of "acceptable" leverage levels as a risk-reducing general requirement can set inappropriate management triggers, especially in the structured business and in the specialised lending business. The same applies to traditional corporate finance. This is the case in particular because, as a rule, leverage is only one of several credit quality indicators and their overall assessment, including the economic environment, will always determine borrower creditworthiness. In addition, the transaction risks must always be seen in the context of the collateral/guarantee structure. We therefore advocate not requiring the credit institution to define acceptable leverage levels. Acceptable levels should be based on the rating note and the associated probability of default and level of collateralisation, and not on a single metric for the leverage level. However, if the EBA intends to stick to this requirement, it should stipulate that – as in the ECB Guidance on leveraged transactions – it is limited to syndicated loans.[1]

Paragraph 54
The requirements for consistent data retention over the entire credit life cycle appear to be very sweeping and not compatible with the requirements of the GDPR. We consider a requirement based on the principle of proportionality to be vital.

Paragraph 56
The requirements for data collection and management state that institutions should consider using the approximately 450 fields of the EBA's NPL transaction templates. When this template was published in December 2017, the EBA still emphasised that application was not obligatory

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[1] See Guidance on leveraged transactions, Section 5 Syndication activities, page 7, 3rd bullet point.

(see EBA NPL Templates, page 4; 14 December 2017). If application of the template is now required, it would trigger considerable investments that would not be proportionate to the associated benefits. The data fields recommended for NPL transactions are far too extensive for the normal lending business. In addition, according to EBA 2017 paragraph 12, the transaction templates are aimed "…at enabling potential bidders to perform a detailed analysis of the assets, commonly performed during the FDD and valuation phase, with regard to the NPL portfolio which forms the subject matter of the transaction". In other words, this means that the templates are only relevant in the event of a possible sale of an NPL portfolio. It is questionable in this context why the data fields already shall be filled before a loan becomes non-performing. We therefore propose deleting the reference to the NPL transaction templates.

Credit decision-making (re Question 5)

Paragraph 57
The establishment of a credit committee is not required by the Governance guidelines. Lending decisions by the executive board, the credit committee or a body delegated by one of them, are only necessary for large-volume or high risk loans, or specific cases where a loan departs from a strategic determination. In other cases, loans can be decided by individual staff in the delegated decision-making framework (see paragraph 62) or also by automated processes. The qualification "where applicable" should be added to this paragraph.

Paragraph 59
A requirement for fixed limits (time period and number) would generate bureaucratic effort without any additional benefits. Because there is a general requirement for the periodic review of the risk management framework (see Governance guidelines, paragraph 139), this requirement is dispensable.

In practice, the allocation of decision-making powers is determined by quantitative risk indicators that are derived from the characteristics of the relevant transactions and primarily consider the borrower's creditworthiness and aggregate exposure. In this respect, we consider that the requirement to account for all of the categories referred to in paragraph 59 (asset class, product type, type and quality of the borrower, geographic location of the borrower, economic sector and industry, and credit limits/maximum exposures") in the credit decision-making framework is not appropriate. The second sentence should therefore be deleted, or the categories should be labelled as examples.

Paragraph 60
Where needed, the risk control function can be consulted in an advisory role in individual lending decisions, but it should in principle be independent of the first line of defence (see paragraph 75). The wording of paragraph 60 could be ambiguous and should therefore be reviewed.

Paragraph 62
Seniority is not in itself a decisive qualification factor, so the words "and seniority" should be deleted.

Paragraph 63
Under point b., persons involved in lending decisions should not have any economic, political or other interest associated with the borrower at the time of the lending decision. In practice, potential interests are almost impossible to rule out because they require knowledge of future developments. A theoretical interest can be construed for almost any lending decision. Nor can these requirements be implemented in this form. The institution could only ensure that any and all direct or indirect conflicts of interest can be entirely ruled out if it obtains knowledge of all the relationships and interests of the workforce and the applicants. This would be neither expedient nor allowed.
In this context, we would like to point out that, in our view, the respective requirements of the governance guidelines are also too far reaching, especially paragraphs 107 to 109. These requirements have been inserted in the final governance guidelines without giving the banking industry the opportunity to provide feedback during the consultation.

The exclusion under point b. could also be an obstacle to the requirement under paragraph 68. In addition, it would run counter to the statutory decision-making obligations in Germany of the executive board for large exposures under section 13 of the German Banking Act (*Kreditwesengesetz* – KWG) and of the executive and supervisory boards for loans to connected persons and undertakings under section 15 of the KWG. For loans to a parent undertaking, for example, section 15 of the KWG requires the approval of the supervisory board, of which employees or managers of the parent undertaking are normally members.

With regard to point c., we wish to point out additionally that the administration and disbursement of approved loans is partly or completely automated, in particular in the small-scale lending business.

We suggest deleting this requirement.

In accordance with point c. of paragraph 63, individuals involved in lending decisions who have a personal or professional relationship with the borrower and are subject to a remuneration scheme associated with the growth of new business should be separated from functions dealing with loan administration, including disbursement, and from credit risk management. Ultimately, this also affects the level of the management body and would hence be impossible to implement. Please delete this, or at least clarify what is to be understood by this "separation". In our opinion, a separation of functions cannot be meant because this would call the institution's organisational rules into question for individual lending decisions. In addition, the specific influence of the remuneration system in such cases compared with other lending decisions is not evident to us.

Paragraph 66
In our view, these requirements should only apply to risk-relevant transactions in application of the principle of proportionality in order to prevent escalation of the effort for less risk-relevant transactions. Paragraph 66 should therefore be amended as follows:
"Institutions should ensure that staff members involved in credit granting and management escalate and report the full nature of exceptions to policies and breaches of limits <u>of risk-relevant transactions</u> internally to […]. <u>This requirement should be implemented proportionately to reflect the nature, size and complexity of the risk associated with the lending decision."</u>

Paragraphs 67 to 69
The term "affiliated parties" is not defined. If this is meant to be the "related parties" as defined in Article 88(1) of CRD V, please use this term and add a corresponding reference.

Paragraph 71
Sales control is not a task in which the risk control function should be involved. We recommend deleting the word "sales".

Paragraph 72
To avoid confusing the first and second line of control, we suggest amending paragraph 72 as follows:
"These functions should be fully integrated into the institutions' overall risk management ~~and risk~~ ~~control functions~~."

Paragraph 74
Paragraph 74 could be interpreted that an institution has to be organised in all areas ("any organisational structures") using the three lines of defence model. At many institutions, the principle of separation of functions has proven itself without any explicit application of the three lines of defence model. This approach should be retained in order to preserve a reasonable degree of flexibility and avoid unnecessary modification effort. Similar to the consultations on the EBA Guidelines on internal governance, during which the original explicit requirement of the three lines of defence model was deleted in the final version, we are also requesting its deletion here as well.

Resources

Paragraph 79
The word "frequently" should be replaced by "on specific occasions". There is no need for any fixed cycle for staff training.

Remuneration

Paragraph 82

The specific requirements in paragraph 82 addressing the remuneration policy arrangements are too sweeping in particular for small and medium-sized banks. The requirements are neither necessary nor practicable. The requirements set out in the Capital Requirements Directive (CRD) and the existing EBA guidelines on remuneration policies are sufficient and should not be expanded in any further detail here. GBIC is requesting the deletion of paragraph 82.

Loan origination process (Section 5)

5.1 Collection of information and documentation (re Question 7)

There is a need for a proportionate approach to all requirements addressed in this section. A graduated approach should be allowed in line with the nature, size and risk of the transaction in question. For example, the requirements of Directive 2014/65/EC (Mortgage Credit Directive) quite rightly stipulate far-reaching creditworthiness assessments, but these should not be applied to all consumer loans. In the consumer area, there should therefore be at least a differentiation between general consumer loans and consumer mortgage loans proportionate to the importance (amount and term) of the loan.

In particular for the lending to professionals, we wish to point out that the required data and information from small businesses, traders, self-employed persons etc. often do not exist. It should be clarified that the information given in Annex 2 is purely illustrative.

Please clarify that an overall assessment of all borrowers has to be made for a creditworthiness assessment of multiple borrowers. This would be essential in light of the common practice throughout Europe of basing the creditworthiness assessment on the borrowers collectively, for example in the case of spouses who take out a consumer loan together as borrowers.

Paragraph 83

We suggest clarifying that the EBA acknowledges a proportionality principle here (“sufficient level”) that also allows the creditworthiness of the borrower to be verified up to certain limits without individual information – other than income – but based on sustainably calculated standard data. A simplified process e.g. for overdraft and credit card limits up to a certain amount should be considered, in which clients are asked about their income, but this does not have to be verified.

Please provide a more detailed definition of “significantly”.

It is also not clear what the consequences are if a potential borrower is unable or prepared to provide certain information. At present, the bank usually reflects such a lack of information in the rating and thus in the pricing. If that approach falls within the envisaged outcomes, the EBA Guidelines should be clear on this matter.

Please clarify that the requirements for repricing do not apply to the specific German loan agreements known as “*unechte Abschnittsfinanzierungen*”. With these loan agreements, the consumer is already granted a long-term right to use the principal amount when the agreement is entered into. However, the interest rate agreement is not made for the entire period, but initially only for a certain fixed-rate period. A second creditworthiness assessment at the date of the subsequent interest agreement is not necessary because the lender must already verify the borrower’s creditworthiness when the agreement is entered into until the loan is repaid in full, and merely this subsequent interest agreement for the loan does not mean that a new loan agreement is entered into.

Paragraph 85
We presume that the review requirement in paragraph 85 does not mean that the lender must obtain credit information from other credit institutions. In any case, the loan agreements say nothing about the current level of disbursements, because the loans may already be partially repaid. An annual account statement or similar document should be sufficient evidence.

We suggest clarifying in paragraph 85, generally for the entire section, that the requirements for the creditworthiness assessment can be structured by the nature, size and risk of the relevant transaction (at the discretion of the institutions). In this context, we presume that in particular for very small loans such as overdrafts or credit card limits, information provided by borrowers about their income will be sufficient. Only in special cases (e.g. suspected fraud) should this have to be documented by additional evidence/documents. However, such a clarification would also be desirable for loans below a limit to be defined by the institution based on risk aspects, because the risks are manageable. We therefore suggest deleting both occurrences of the word “comprehensive” in this paragraph.

In order to clarify the understanding of the term "single customer view", we would like to suggest adding the following wording to paragraph 85: *“Borrowers within the meaning of Section 5 may also be several borrowers (consumers and/or professionals). In this case, the creditworthiness assessment must be carried out for all borrowers together (overall customer view).”*

Paragraph 86
With regard to the aspect of proportionality, we suggest clarifying that the timeliness of the data should refer above all to the lending date; anything else would require permanent monitoring. That applies in particular to granting instalment loans in the retail business. In addition, it should also be possible to satisfy the requirement for “accuracy of information” using validated standard values, as it is simply impossible to monitor expenditures with any precision. We suggest adding “sufficiently” (accurate...) in order to emphasise the aspect of proportionality.

Paragraph 87
According to paragraph 87, third-party guarantees are eligible for consideration for supervisory purposes, which we welcome. For the creditworthiness assessment under civil law, guarantees or collateral provided by third parties play no role in the context of the statutory requirements (MCD and CCD). This is appropriate in our view.

Paragraph 88
In our view, the requirement for “any necessary checks” goes beyond the corresponding requirements in the EU directives. For example, Article 20(1) sentence 3 of Directive 2014/17/EU requires the information to be “appropriately” verified, if necessary by inspecting independently verifiable documentation. Article 8 of Directive 2008/48/EC also does not stipulate such a far-reaching verification requirement for general consumer loans. As a

consequence, the German lawmakers also only expect “appropriate” verification of the information for consumer mortgage loans.
Especially in the case of consumer loans with small amounts, verifying information using third parties is not necessary or reasonable from risk and cost aspects. In particular, it will not be in the interests of borrowers for their employer to find out every time they apply for a loan. Standard checks with credit reporting agencies and checking the plausibility of the information provided by the borrower by comparisons with standard values should normally be sufficient. Inquiries of third parties can be one option for checking plausibility, but they should not be made mandatory. This paragraph should therefore be streamlined as follows:
“Institutions and creditors should assess the plausibility of ~~any~~ relevant information and data provided by the borrower, as far as these pieces of information are materially relevant for the assessment of creditworthiness.”

It should be clarified overall that the borrower has a duty to cooperate in the creditworthiness assessment. The borrower is obliged to provide complete, accurate information. This also results from Article 20(3) of the MCD, which allows the lender to terminate a loan agreement if it can be demonstrated that the consumer knowingly withheld or falsified information. Plausibility checks carried out by the institution are therefore only necessary if there are reasonable doubts about the accuracy of the information or if there is a concrete suspicion of fraud.

Paragraph 89
We wish to refer to our comments on paragraph 128. We also suggest clarifying that this requirement only applies in the context of consumer finance to cases where connected parties enter into concrete commitments in the context of the financing transactions (borrowers and collateral providers), and that it should only address information that is already known to the lender. Examining the group of connected parties for connections outside this concrete requirement can be very complex and it is not evident which specific insights could be gained from verifying such a group of connected parties.
If the intention here is to examine equity investments of the borrower for corresponding risks resulting from those investments, this would no doubt lead in many cases to denial of the loan for reasons of prudence, especially if no figures for the connected companies are available and the borrower is unable to produce them.
We believe that verifying the borrower’s income situation at this point is sufficient. It may also be possible here to define corresponding requirements above a particular lending limit.

Paragraph 90
The general requirement to store all information and data for the entire life cycle of the loan is not practicable. Paragraph 90 should therefore be deleted in its entirety. In the case of consumer loans, the burden of proof that a proper creditworthiness assessment was conducted lies with the institution. Storing the information and data for at least the duration of the loan agreement therefore already happens in the institution’s own interests. In the case of loans to business clients, the storage periods stipulated by commercial law must be observed (in Germany, 6 or 10 years under section 257 of the Commercial Code (*Handelsgesetzbuch* – HGB)).

Overall, the national differences in credit periods should also be considered here. In the case of long-term real estate loans of up to 30 years often encountered in Germany, these requirements would lead to totally inappropriate and unnecessary effort and expense. We also fear conflicts with the requirements of the GDPR.

Paragraphs 91 – 95
We wish to draw attention to our "general comments" on the principle-based approach and materiality aspects. Obtaining all of the information given in Annex 2, regardless of the importance of the loan, is not expedient. As a matter of urgency, the list of documents required in paragraphs 91 to 94 and in the Annexes for verifying creditworthiness should therefore be made contingent on the nature, size, complexity and risk of the lending transaction in question. This is the only way that the institutions will be able to meet and manage the requirements for the different types of loans. In general, the requirements appear to be based specifically on cash flow financing transactions for single companies (asset cash flow). They are too complex and unsuitable for other types of financing, for example for corporate finance transactions.

Not all the required information will be available in particular for small companies, traders, self-employed persons and members of the independent professions, as these borrowers are not generally required to prepare financial statements, with the result that they do not have detailed financial plans. For these groups of clients (small-scale diversified lending business), the required information is not therefore available in any level of detail. In Germany, for example, a materiality threshold of EUR 750 thousand is stipulated. We believe that such a threshold is realistic and proportionate.

For example, overdrafts and current account loans are also not tied to a specific purpose, with the result that no data is available regarding the purpose of the loan. For paragraphs 92 and 94, the insertion "where relevant …" is therefore missing, although it appears in point a. of paragraph 91 or point a. of paragraph 93. Overall, GBIC is therefore recommending that the **checklist-style formulations** in the Draft Guidelines should be reformulated in all cases expressly as examples. In each case, the wording should be modified as follows:
replace "at least" with "where applicable".

Paragraph 91
We suggest clarifying here that all that is meant is to ask "whether" there is employment in order to verify the sustainability of the income. In other respects, please refer to our comments on point 5 of Annex 2.
In our view, the requirement for consumer loans in point a. of paragraph 91 to determine the purpose of the loan is too sweeping. The purpose of the loan plays no role in small-scale lending, and becomes important only in the case of consumer mortgage loans. The sole decisive factor here is the outcome of the creditworthiness assessment. We therefore suggest clarifying that solely "the purpose to acquire or retain property rights in land or in an existing or projected building" (see Article 3(1)(b) of the MCD) should be recorded.

Paragraph 93
We refer to our comments on paragraphs 91 to 95. The minimum requirements set out in paragraphs 93ff. for lending to "professionals" are not necessary for smaller companies and, in part, not capable of being met. The EBA should clarify that it would be compatible with the principle or proportionality highlighted in paragraph 12 to affirm the creditworthiness of the "professional" even if individual information elements are not available. Without such a clarification, we see the hazard that auditors will require a compilation of certain documents solely for loan application purposes.

In addition, the emphasis on cash flow in point b. is not practicable, especially for small and medium-sized enterprises. Under the German Accounting Standards, direct method cash flow statements are only mandatory for certain size classes and/or publicly traded companies. Indirect method cash flow statements derived from the income statement and the statement of changes in net assets do not have the same informative value and are subject in part to misinterpretation. The information is thus not available in full in a high-quality form.
We take a critical view of **points d. and i.** of paragraph 93 and are therefore recommending their deletion. Staff members in the institutions are not responsible for verifying or checking the plausibility of the relevant business model of the borrower, as this concerns operating issues of the borrower. We therefore oppose any accompanying legal and business assessment. The staff members in the institutions do not have the necessary comprehensive specialised knowledge and legal expertise, and the business model and legal documents do not play the same role for the company's creditworthiness in all finance types and creditworthiness analysis systems.

Paragraph 94
We wish to refer to our comments on paragraph 92. GBIC considers these minimum requirements to be impracticable in particular for specialised lending to professional clients, as for this type of lending because of the complex exposures with often bespoke characteristics specialised provisions apply. We would ask EBA to clarify that, as stated in the Public Hearing, these are only exemplary enumerations.

Paragraph 95
In light of the EBA Guidelines on management of non-performing and forborne exposures (EBA/GL/2018/06), the wording in paragraph 95 should be amended as follows:
"Where the borrower faces financial difficulties in meeting the contractual loan obligations, institutions should request from the borrower reliable documentation demonstrating realistic projections of its ability to maintain or return to solvency within a reasonable period. Information memorandums or reports from tax advisors, auditors, third-party-experts and/or credit related documentation of affiliated companies may also be used. Information provided from the debtor should be assessed from a prudent perspective."

Annex 2

As already mentioned at several points, it should be clarified that these are not binding minimum requirements but individual attributes that should be observed if they are relevant. Although we only present detailed comments on individual points of Annex 2 in the following, this overarching remark also applies to Annexes 1 and 3.

Point 3 (Lending to consumers)

We suggest clarifying that it is sufficient to establish whether property is involved, and if so, whether it is or will be owner-occupied. There is no need to find out about other purposes in the context of general consumer loans.

Point 4 (Lending to consumers)

We suggest clarifying that this means eligibility for support by public funding programmes.

Point 5 (Lending to consumers)

We suggest clarifying that a distinction between employment and self-employment and the question of whether it is for a limited period are sufficient, depending on the product involved. It is not evident to us what the purpose of distinguishing between full-time and part-time is, because only the corresponding income is used for the creditworthiness assessment.
Nor is the added value provided by sectors of employment evident for the creditworthiness assessment. If the lender captures this data for its internal rating, it should be provided on a voluntary basis.

Point 6 (Lending to consumers)

We suggest clarifying that an annual period is sufficient. Additionally, we assume that credit institutions cannot be forced to consider bonus payments and overtime. If credit institutions do this, it should be provided on a voluntary basis.
Obtaining documents over a period of longer than one year would not be proportionate relative to the borrower effort/lender effort for the purpose of providing more far-reaching knowledge and only slow down the lending process and make it more expensive.

Point 8 (Lending to consumers)

We suggest clarifying that in the context of proportionality, standard values can be used for unsecured loans, as well as for secured loans up to certain maximum amounts.
In addition, we wish to point out that requiring information about financial commitments such as child maintenance, education fees and alimonies is diametrically opposed to digital progress and hence to developments for the benefit of the clients. Information about child maintenance commitments in particular is not kept by credit reporting agencies, with the result that a lean credit process will be hampered or even prevented by the need to collect corresponding documents.

Point 9 (Lending to consumers)

We suggest clarifying that asking for such information is not relevant if after-tax income is used as a basis for the loan. It is not clear to us what the value added of knowledge about the tax status of a borrower would be. The disposable income is shown on the payslips; living expenses are taken into consideration in the general tax rates.

Point 10 (Lending to consumers)
We suggest clarifying that this is only relevant if the life insurance is important for extending the loan – as collateral or to repay the loan.

Point 11 (Lending to consumers)
Arrears in payment from other institutions are not generally provided by credit registers. We therefore recommend to add in the text that data should only be used if it is also provided by the corresponding credit register. *For example: "Data from credit registers or credit information bureaux, covering at least the information on financial liabilities <u>and - where available -</u> arrears in payment".*

Point 19 (Lending to consumers)
We suggest clarifying that this requirement does not apply to improvement loans that are not classified as consumer mortgage loans and are thus not secured by property liens. If not, on the one hand information (about whether property is involved) would have to be collected on every purpose of a loan – including loans not secured by property liens – and on the other, the permit and a quotation would have to be submitted for a loan for heating, window replacement or roof work, for example, that is not secured by a property lien. This cannot be demanded and would only slow down the lending process and make it more expensive.

5.2 Assessment of the borrower's creditworthiness (re Questions 8 and 9)

Question 8:
There must be a proper balance between costs and benefits regarding the detailed requirements for the data to be collected and analysed. Ideally, the aspects addressed will deliver added value for the institutions in the creditworthiness assessment of the relevant client. Any costs associated with implementation (personnel, IT, etc.) may not affect the institutions' lending capacities.

The connection between the institution's risk appetite and the borrower's profile for the creditworthiness assessment is not clear to GBIC. However, such a verification is required by paragraphs 96 and 122. Ultimately, the creditworthiness assessment depends solely on the borrower's circumstances. This requirement should therefore be deleted or expanded in greater detail. As explained in the following, the principle of proportionality must also be observed in the consumer area. This applies to paragraphs 98, 101 and 121.

The requirements of paragraph 125 are far too sweeping for lending to commercial borrowers ("professionals"). The concept of protection originating from consumer credit law should not be transferred to commercial lending here.

Question 9:
For consumer married couples or joint accounts, for example, it should suffice to fulfil the creditworthiness criteria at a consolidated level. The same should apply to professionals who have a joint account. The category of "professionals" now appears to range from small businesses to multinational corporations. The requirements should respect the principle of proportionality, and the level of granularity should be consummate with the risk profile of the counterparty or class of counterparties.

A mere distinction between consumers and "professionals" would suffice if the creditworthiness assessment were otherwise to be governed by abstract requirements, as is common for legislation. Addressing case groups in detail by specifying checklists reduces the necessary flexibility of application to new developments.

Paragraph 96
With regard to the second half of this sentence relating to the comparison of the borrower's profile with the institution's credit risk appetite, the question arises of the extent to which this should be decisive for the lending decision. Without the second half of the sentence, paragraph 96 would also be consistent with the other paragraphs (e.g. 85, 86, 97 and 98), which refer only to the borrower's ability to meet the obligations under the loan agreement consequently, the second half of the sentence should be deleted.

Paragraph 97
The current wording contradicts Article 18(6) of the MCD, which only stipulates a creditworthiness assessment for existing loans if there is a significant increase in the total amount of credit. The second half of the sentence should therefore read: "before concluding a loan agreement or significantly increasing the loan amount".

Paragraph 98
We suggest clarifying that "assessment of the borrower's [...] source of repayment capacity" does not refer to the borrower's employer, but to the borrower's financial performance or other sources of income.

We therefore also assume that, in the case of private real estate finance, rental and lease income are also meant. In the case of consumers, investment income can additionally be included here. In this case too, however, the verification requirement is unclear. This cannot mean any external evaluation of rental and lease income or other investment income. A sustained internal evaluation would mean tremendous effort that would slow down the credit process and could potentially lead to the denial of loans, because corresponding capacities would have to be developed. This is unlikely to correspond to the interests of the supervisors. We therefore recommend clarifying that the information provided by the borrower must be plausible, and that if it is, no further verification is required.
We also wish to suggest an amendment in order to avoid any interference with responsibility for methodologies relating to the design of the material credit information in the context of the initial and ongoing creditworthiness assessment. The information outlined in paragraph 98 should be understood as a suggestion and not as minimum information:
"The creditworthiness assessment should cover, ~~at a minimum~~, <u>where relevant,</u> an assessment of the borrower's income, disposable income, financial situation and source of repayment capacity to meet contractual obligations."

Paragraph 99
The parameters given in this paragraph should not be designated as binding, not least because they are not compatible with AnaCredit and hence require modifications to IT and data collection. It is also unclear what the consequences would be if certain targets for these parameters are undershot in the lending process and/or over the life of the credit relationship.

Paragraph 100
The requirement for an "accurate single customer view" should not mean that verification based on past experience or standard values is ruled out from the outset. This is necessary in order to enable an appropriate lending process in the retail business and often leads in practice to more realistic results (e.g. commonly estimated expenditures for food). It should also be clarified that the choice of these metrics is up to the discretion of the lender in question.

In addition, in line with German banking practice, multiple persons, such as married couples, should be included as well as natural persons:
"Institutions and creditors should apply metrics and parameters to have an accurate ~~single~~ customer view (<u>e.g. single customer, household, couple or life partnership</u>) that enables the assessment of the borrower's ability to service and repay all its financial commitments. <u>Commonly estimated expenditures for living, food, traffic etc. may be used, where appropriate."</u>

If each of the two individual borrowers were to be able to service the joint loan, this would have a serious impact on lending possibilities and, consequently, on the provision of financing, for example, property ownership. However, from the Public Hearing we learned that this was not intended and would be grateful for clarification.

Paragraphs 101, 114, 121, 143, 144, 145 and 146 (sensitivity analyses)
The requirements governing sensitivity analyses are too extensive overall (see also our general and the following specific comments).

Paragraphs 101, 114 and 121
For unsecured consumer loans, individual sensitivity analyses are not necessary from a risk perspective due to the low exposures at default. Paragraphs 101 and 121 should therefore be deleted. For consumer mortgage loans, the Mortgage Credit Directive stipulates that retirement, a change in the borrowing rate and foreign exchange risks must be taken into consideration in the creditworthiness assessment. The sensitivity analyses for consumer mortgage loans should not go beyond these requirements.
Besides, the scope of the lender's obligation to take into account and assess "any hedging strategies" for foreign currency loans in order to mitigate foreign currency exchange risk is unclear. Any obligation of the lender to address the client actively on this issue is very wide-ranging. We are therefore seeking clarification.

Paragraph 103
We suggest clarifying that this does not mean the verification of historical employment relationships or income history in the existing employment relationship. It is not evident how this is supposed to affect future ability to meet obligations.

Paragraph 109
We wish to refer to our comments on paragraph 100 and suggest clarifying that, depending on the credit volume, standard living expenses should also be estimated on a sound basis, with any information to be obtained from the borrower always to be measured against the estimate for plausibility. We additionally suggest clarifying that rental expenses, as part of the living expenses, can be based on substantiated regional data.

Paragraph 112
Point b. of paragraph 112 calls for very detailed information on builders, architects, engineers and other contracting parties. We consider this requirement to be overblown, in particular in

the retail business, because it would merely lead to higher personnel expenses and not to any reduction in credit risk, as previous experience in this business segment shows. Properties being built by consumers are almost exclusively small dwellings. Although construction management is also handled by a third party in some cases (e.g. when an apartment is acquired for future leasing), the extent of this is not comparable with that of large project finance schemes. A distinction must be made here. It is not the job of the institution to review the borrower's operational construction management. In addition, the consumer will be confronted with requirements that are almost impossible to implement in practice, and that will considerably complicate the acquisition of investment property. Collecting a variety of information on architects, builders and other involved companies in the context of a construction financing decision unnecessarily pushes up the costs of that decision on the one hand, and does not help assessing the creditworthiness of the individual borrower in the lending decision on the other. In addition, we see a risk that, if the planned requirements in paragraph 112 are implemented, an attempt could be made in the event of the failure of such projects to shift the resulting economic risks to the bank by construing corresponding claims for damages under civil law. Considering such risks could make the property more expensive for clients.

We are proposing to delete point b. and to make the following modification:

"For the loan agreements secured by immovable property, where the property is still being constructed and intended to provide, upon completion, an income to its owner in the form of rents or profits from its sale, the institutions and creditors should assess <u>(in proportion to the nature, complexity, volume and level of expected credit loss of the loan agreement)</u> the development phase and the phase after the completion of the development when the project converts into an income producing property. For the purposes of such loan agreements, institutions and creditors should assess:"

"112c: […] projection of all costs associated with the development <u>and, where relevant,</u> certified by a qualified and reputable quantity surveyor, valuer (or similar); and"

Paragraph 113

The institution also bases this sort of finance on other income or assets of the borrower. This therefore means potential rental income on the income side and the borrower's living expenses on the other. The sustainability of achievable rental income is one of the key criteria for the consumer's creditworthiness. It must be clear that the consumer's debt-servicing capacity is what matters. We are therefore suggesting the following amendment:

"113: For loan agreements which relate to an immovable property which explicitly state that the immovable property is not to be occupied as a place of the residence by the borrower or a family member (i.e. buy-to-let agreements), the institutions and creditors should assess <u>first of all the debt-servicing capacity of the borrower and second (where necessary)</u> the relationship between the future rental income from the immovable property and the borrower's ability to meet obligations."

Paragraphs 116ff.

The requirements of the MCD are being extended in large part to other consumer loans, although they cannot be implemented at all for overdrafts, for example (because overdrafts do not have any explicit terms and no repayment instalment is agreed). A traditional overdraft facility is granted until further notice. GBIC believes that it would not be in the interests of consumers if such uncomplicated liquidity reserves could no longer be used. The requirements appear to be too broad for loans with small amounts and mainly shorter terms. We advocate applying the principle of proportionality to Section 5.2.4 in its entirety. This will give institutions the freedom to decide the extent to which the requirements can be applied to the different types of loans, depending on the complexity and risk of the lending transactions.

Paragraph 118

We suggest clarifying that the "interest rates" for other debt obligations actually mean the specific or calculated interest and principal payments. It is not evident why the interest rates are supposed to be relevant here.
We additionally suggest clarifying that, depending on the credit volume, standard living expenses, including rental expenses, may also be estimated on a sound basis. In doing so, information to be obtained from the borrower always has to be measured against the estimate for plausibility.

Paragraph 119

We advocate deleting paragraph 119 in order to avoid any risk of ageism. Such a rule makes sense if it is limited to mortgage loans with long terms (in line with the MCD), but applying it to unsecured consumer loans is neither necessary nor reasonable. Paragraph 119 should therefore be deleted.

Paragraph 122

We refer to our comments on para. 96. Lending decisions can only be made by the areas authorised under the business and risk strategy and the risk appetite defined there (operationalised by limits and credit risk indicators), so a new assessment here appears to be neither necessary nor expedient.
"The creditworthiness assessment should aim to verify the borrower's ability and prospect to meet the obligations under the loan agreement." ~~and also to verify whether the borrower's profile is in line with the institutions' credit risk appetite, policies and limits."~~

Paragraphs 124, 125

The Guidelines require institutions to focus on the borrower's realistic and sustainable future income and cash flow from ordinary activities when assessing the creditworthiness of borrowers, and not on available collateral. According to the Guidelines, collateral by itself should under no circumstances be a criterion for approving a loan and cannot by itself justify the approval of any loan agreement, unless the original loan agreement already explicitly envisaged that the repayment of the loan would be based on the sale of the property pledged as collateral. In GBIC view, at least loans secured by cash collateral should be excluded from this requirement.
Collateral in the form of guarantees should also be excluded. Such a rule would otherwise exclude, for example, common financing structures in both corporate and project finance in which the (legal) borrower does not itself have the necessary credit quality for a loan, but that

are in line with market practice and acceptable when viewed overall (e.g. guarantees by or profit and loss transfer agreements with group parent undertakings).

Although GBIC can understand the focus on sustainable debt-servicing capacity from an economic standpoint, the wording in paragraph 125 is problematic especially for small and medium-sized clients. It is also questionable, whether the sentence "Collateral by itself should be under no circumstances a criterion for approving a loan and cannot by itself justify the approval of any loan agreement" contradicts the statement in paragraph 124. There will be no contradiction if the asset deal is part of the financed transaction, in other words it does not take place on the basis of an enforcement or other default on repayment commitments, and the ensuing cash flow is part of the normal cash flow in the cash flow planning. We wish to suggest the following amendment:
"When assessing the creditworthiness of the borrower, institutions should put emphasis on the borrower's realistic and sustainable future income and future cash flow and not rely solely on available collateral. ~~Collateral by itself should be under no circumstances a criterion for approving a loan and cannot by itself justify the approval of any loan agreement.~~ Collateral should only be considered as the institution's second way out in case of default or material deterioration of the risk profile and not as the primary source of repayment, with the exception where the loan agreement envisages that the repayment of the loan is based on the sale of the property pledged as collateral or liquid collateral provided."

Paragraph 126
The institutions should continue to be able to determine the scope and depth of the creditworthiness analysis and the verification of debt-servicing capacity on a risk-driven basis. It should be possible to determine the scope and depth of the creditworthiness analysis and the verification of debt-servicing capacity freely and flexibly, depending on the scale of the available data, the risk, the size of the amount being financed, the borrower's sector and the collateral. We therefore suggest amending the wording of paragraph 126 as follows:
"126: When carrying out the creditworthiness assessment institutions should perform ~~at least~~ the following, where appropriate and relevant considering the risk, type, size and complexity of the relevant credit facility: […]"

Point b.: The meaning of the requirement to analyse the legal capacity of non-consumers is not clear. The EBA should explain the requirement to analyse legal capacity in greater detail. It is also unclear whether, for example, legal opinions on capacity or all of the company's legal resolutions, powers of attorney and specimen signatures should be obtained for the lending decision. It should be possible to define minimum thresholds so that obtaining such documents would only be required, for example, above a certain credit volume.

In point c., the insertion "any" should be replaced by deleted. The current wording is also not used in the Governance guidelines (Sections 11 and 12). Purely theoretically, it is always possible to construe conflicts of interest, but materiality aspects must also apply when addressing them.

The wording of the requirements of point f. of paragraph 126 is ambiguous. In our opinion, this cannot be understood to mean that the (potential) debt facilities of a borrower in every client relationship with other credit institutions has to be considered. Please clarify this.

Paragraph 127
We wish to refer to our comments on paragraph 126 and also suggest amending the wording of paragraph 127 as follows:
"For the purposes of the analysis of the financial position within the creditworthiness assessment as specified above, institutions should consider the following, proportionate to the size, complexity, nature and level of risk: […]".

Paragraph 128 (among others)
If at all, basing Pillar 2 credit risk management on groups of connected clients should only be mentioned as an option. We wish to refer here to the executive summary of EBA/GL/2017/15: "*The guidelines focus exclusively on the issue of connected clients as defined in Article 4(1)(39) of Regulation (EU) No 575/20132 and apply to all areas of that Regulation where the concept of connected clients is used, i.e. the large exposures regime …*)".

There is thus no intention to extend this to Pillar 2. Our suggestion to reword this paragraph:
"Where reliance for repayment is placed on cash flow emanating from other parties connected with the borrower, institutions should carry out an assessment of these parties and, if appropriate, also at group level."

Paragraphs 30, 89 and point a. sub-point iii of paragraph 231 should be amended in line with this.
In addition, a risk relevance threshold should be introduced here. For example, some large groups have a large number of smaller subsidiaries for which the credit institutions have provided smaller loans (in part only credit card limits). If the parent undertaking issues a guarantee for these limits, it must be possible to dispense with the need to obtain comprehensive documents from the subsidiary.

Paragraph 129
The requirements to analyse the legal environment, the extent to which the exporter meets the local legal requirements and the transfer of funds should clarify that the internal analysis performed by the credit institution is sufficient in this respect.

Paragraph 130
Please see our comments on paragraphs 48ff. Paragraph 130 sets out that institutions must generally assess the exposure of an individual borrower to climate and environmental risks, as well as other ESG risks. Examples given include the borrower's risk-return profile in respect of transition risks and the appropriateness of the mitigating strategies.
This exception-free requirement should be deleted. The related effort and expense could significantly slow down processes and make loans more expensive. The proportionality of this

requirement is therefore not evident. In most cases, analyses of material ESG risks at portfolio or business sector level, e. g. within stress testing, will be sufficient.

Additionally, the wording of paragraph 130 suggests that physical, transitory climate risks, environmental risks and "other ESG risks" are all equal and must be dealt with identically. However, this raises a very large number of methodological questions. Transitory risks in particular cannot be measured consistently or comparably; they depend to a significant extent on individual conviction about the extent to which certain political decisions (carbon tax) will be implemented or not.

In addition, there is a risk that institutions will price themselves out of the market with more restrictive requirements if there is no common understanding of ESG. A comprehensive ESG assessment in the lending process demands strategic decisions from the institutions and adequate training of the staff members, which will take more time. It is also not appropriate to intend creating an understanding for ESG in the real economy via the financial economy. Lending in Europe and Germany is focused on the small and medium-sized economic structure. A general inclusion of ESG in the lending process raises the question of proportionality. A large number of SMEs are not yet aware of the impact of climate change. It is not the job of the banking industry to establish the socially important change in awareness in the course of the lending process.

Paragraph 131

Preparation by the institution of financial projections for its borrower should be limited to larger financing packages. In the case of larger, material financing projects, it is not uncommon for the borrower or a mandated consulting and/or auditing firm to submit financial projections. A requirement for the bank to prepare financial projections in order to challenge the documents submitted, however, only makes sense for material exposures and is only reasonable when measured against cost aspects. Paragraph 131 should be amended as follows:
"For significant credit risks, institutions should ensure that the analysis of the borrower's financial position is based on tangible facts and not on an expected significant increase in the borrower's income unless there is sufficient evidence. Where applicable, this evidence regarding financial projections and debt-servicing capacity can also be based on external opinions." ~~Institutions should make their own projections of the borrowers' financial position and use them to challenge the projections provided by the borrowers. "~~

Paragraphs 132 and 135

The question of which metrics are available, relevant and financially meaningful for assessing financial position depends on the applicant (size, sector) and possibly also the type of financing. Proportionality clauses should be inserted.
In addition, the metrics required in the Draft Guidelines are often simply not available at small companies, traders, self-employed persons and members of the individual professions (because they are not required to prepare financial statements). We suggest including a reference to the requirements of national commercial law. If concrete metrics are to be given

in the Guidelines (which would run counter to the notion of principle-based requirements), they should be designated as being merely illustrative.
The financial analysis of the debtor should follow the principle of proportionality. The emphasis on free cash flow is uncommon in German banking practice and also not practicable especially for debtors who do not prepare financial statements. We therefore suggest amending paragraph 132 as follows:
"For the purposes of the analysis of the financial position within the creditworthiness assessment as specified above, institutions should consider ~~at least~~ the following, where appropriate and relevant, reflecting the proportionality principle:"
'132 d: […] the use of appropriate financial, asset class and product type-specific metrics and indicators, in line with their credit risk appetite, policies and limits set out in accordance with Sections 4.2 and 4.3, and also ~~at least~~ considering which metrics in Annex 3 would be applicable in the specific credit proposal."

Paragraph 135 should also be reworded:
"Institutions, where relevant, use ~~at least~~ the following financial metrics, where appropriate depending on the nature, size, complexity and level of default risk, for the purposes of the creditworthiness assessment, and, where relevant, assess them against the metrics and limits as set out in their credit risk appetite, credit risk policies, and limits in accordance with Sections 4.2 and 4.3:"

Regarding point a. of paragraph 135, we wish to point out that the applicability of the debt service coverage ratio is limited to corporate finance transactions. We do not see traditional deleveraging in terms of total debt over the term in the same way as project finance – where the debt service coverage ratio is the most relevant metric – as relevant in corporate finance. In this case, a company selects the mix of equity and debt that matches its business model, and the debt capacity, a debt limit and a theoretical deleveraging period for the company are normally calculated.

Regarding point g. of paragraph 135, we wish to point out that a market value is only directly available for listed companies (although this value is then subject to corresponding fluctuations and is not necessary meaningful). We suggest deleting at least this metric.

Paragraph 134
The analysis requirements contained in paragraph 134 cannot be implemented as reasonably, because such analyses are not necessary in particular with regard to low-risk credit transactions. We are therefore requesting the deletion of this paragraph.

Paragraph 136
We suggest rewording this paragraph as follows:
"Institutions should assess working capital facility where necessary, taking into account the cash flow generation ability of the borrower to turn the working capital into a cash positive position on a regular basis. If this is not the case, the institutions should assess the capacity of

the borrower to convert the working capital facility into a term loan and repay the term loan on a principal and interest basis."

Paragraph 138
We suggest rewording this paragraph as follows:
"<u>Especially in cases where receivables have been assigned by way of collateral,</u> institutions should carry out, where possible, an assessment of the borrower's debtor and creditor cash cycle, and aging profile using aged debtors and creditors information, in particular to understand how efficient the borrower is in collecting debtor monies owned and potential scenarios if some amount of the outstanding debtor monies may be uncollectable."

Paragraphs 138 to 141
We consider the requirements of paragraphs 138 to 141 to be applicable only to certain SME segments and therefore suggest making the requirements optional or deleting them. In the interests of proportionality, it would in any case make more sense to develop requirements for large-volume corporate finance instead of additional requirements for SME finance. It should in any event be clarified that these can only be best practice.

Paragraphs 142 – 146
Paragraphs 142 to 146 require sensitivity analyses to be performed at the single client level in the context of the creditworthiness assessment. They should only be performed in indicated cases ("where appropriate"). In particular in the case of the macroeconomic scenarios, it is almost impossible to implement a standard at the single client level because a range of client- and sector-specific assumptions must be made in order to model the impact of the changes on the clients. Even though the principle of proportionality is mentioned in paragraph 144, reference should only be made to particularly risk-relevant credit facilities. These paragraphs contain very far-reaching requirements and should be limited to financing transactions with a very large volume. The list of idiosyncratic and market events is too prescriptive, as sensitivities should normally be driven by the idiosyncrasies of the borrower and its industry.

In addition, we are seeking clarification that the sensitivity analyses can also refer to groups of clients, in particular in such cases where no relevant additional insights are to be expected from any sensitivity analysis tailored to the individual borrower. This will also allow better compliance with the principle of proportionality already mentioned.

Paragraphs 143 and 144 should be narrowed down so that only adverse idiosyncratic events that have a medium or high probability of occurrence and that could in the aggregate jeopardise the repayment capacity should be considered in the creditworthiness assessment.

Paragraph 146 should be deleted because such analyses are performed in the course of stress testing at portfolio level and therefore do not have to be conducted for every single professional borrower.

The idiosyncratic events listed in paragraph 145 are aimed at quite probable or emerging developments and not require any general requirement to model general life risks. However, in the current wording, the analyses would almost always lead to the result that the borrower might get into financial problems. The events stated should therefore only be understood as examples.
We suggest considering breaking out leveraged finance as a separate asset class, as many banks treat it this way and require greater complexity with regard to process, analysis and lending standards.

We suggest including the following amendments:
"142: Institutions should verify that where utilised, financial projections provided by the borrower together with underlying assumptions are reliable and realistic <u>in the event of risk-relevant exposures or known/likely financial difficulties of the borrower to meet the contractual loan agreements</u>.
"143: <u>Where necessary,</u> institutions should assess the sustainability and feasibility of the borrower's financial position and repayment capacity under potential adverse market and idiosyncratic events that may occur in the duration of the loan agreement."
"144: Such sensitivity analysis should account for ~~all~~ general and asset class and product type-specific aspects that may have an impact on the creditworthiness of the borrower. Sensitivity analysis should be applied <u>where necessary</u> and should be proportionate given the purposes, size, complexity, term and potential risk associated with the loan."
"145: In the case of risk relevant lending decisions, institutions should take into account probable idiosyncratic events (proportionate to the nature, size, complexity and level of default risk embedded in the loan agreement; any risk mitigation factors should also be considered), e.g."

Paragraphs 147 – 151
GBIC recommends shifting these requirements up (before the Section "Analysis of the borrower's financial position") and adding a reference to proportionality. Knowledge of the business model is the starting point for further considerations (or indicates which analyses are necessary). In light of the economic structure of small and medium-sized enterprises (SMEs), dependence on key persons can be assessed as a risk especially at craft enterprises, members of the independent professions and owner-managed companies, but cannot be mitigated through contractual arrangements. This could even be interpreted as effective interference in the management of the business and entail potential liability risks. We therefore suggest deleting **paragraph 150**. Implementing mitigation measures with regard to any key-person dependency would effectively mean interfering in the management of the business, which the institution has no right to do and could also entail liability risks.

Paragraphs 153 and 155
We suggest amending these paragraphs as follows with regard to the assessment of guarantees:
"153: <u>Where relevant</u>, institutions should assess any guarantees, covenants, negative pledge clauses and debt service agreements <u>for risk-relevant exposures</u>. Institutions ~~should~~ <u>may also</u>

consider whether the value of the collateral is in some way correlated with the borrower's business or capacity to generate cash flows."
"155: Where a loan agreement involves any form of guarantees from third parties, institutions should assess the level of protection provided by the guarantee and, where relevant, a conduct creditworthiness assessment of the guarantor, applying the relevant provisions of these Guidelines depending whether the guarantor is a natural person or professional. The creditworthiness assessment of the guarantor should be proportionate to the size of the guarantee in relation to the loan and the type of guarantor. <u>The creditworthiness assessment of the third party by affiliated and/or parent companies that use a similar risk rating methodology, assessment processes, documentation standards, IT systems and credit decision processes can be used. The assessment must be up-to-date and reliable. In such cases, a stand-alone credit risk assessment of the third party is not mandatory."</u>

Paragraph 156
Due diligence involves a very comprehensive examination, which is performed, for example, for planned mergers and acquisitions and is not normally necessary.

In accordance with paragraph 156, guarantees and letters of credit should only be issued via the agent in the case of cross-border lending and project finance transactions. It is still not clear if this means that the common issuance of guarantees via ancillary lines under syndicated loans is to be prevented. Especially from the perspective of the borrower, this would tremendously restrict the existing financing practice. The EBA should drop this requirement or at least expand on it in greater detail.
It should also be clarified that the due diligence required by paragraph 156 only applies to agents or designated entities previously unknown to the institution. We therefore suggest the following amendment:
"156: Where in the syndicated lending or project finance transactions, the payment streams pass through the agent or another designated entity, institutions should ~~perform a due diligence~~ <u>assess the soundness</u> of the agent or the designated entity. <u>This assessment can also be performed by the mandated lead arrangers or an agent. The assessment must not necessarily be executed by each and every participant. In the event of intra-group participation, the result of another bank can be adopted. A qualified check (in the sense of a plausibility check) must be carried out.</u> For cross-border lending and project finance transactions, the agent or the designated entity should be the sole issuer of any guarantees, letters of credit or similar documents issued on behalf of the supplier in the transaction."

Paragraph 160
Among other things, point b. of paragraph 160 lit. b requires information about the payment history of the tenants. We understand the requirement to mean that the borrower has provide information about the entire cash flow from the rental income for the property to be financed as evidence of future capability to service the loan. We therefore suggest adding the phrase "when viewed overall". For reasons of proportionality, it would not make sense to have to provide information about each and every tenancy (including relatively small ones).

Additionally, we assume that the relevance of the factors referred to depends on their importance for debt-servicing capacity.

Regarding point d., we wish to point out that, if information about the necessary capital expenditures throughout the term of the loan were to be required, technical due diligence would have to be obtained in each case. Merely stating maintenance and modernisation costs would then no longer be sufficient. This would result in disproportionate additional effort and expense for the institutions.

Paragraph 162
With regard to interest-only commercial real estate financing, GBIC considers the following amendments to be necessary because the requirements of the Draft Guidelines are not appropriate if the borrower has other assets, such as other property, that are sufficient to service the loan and the bank has legally effective access to it through corresponding contractual or generally applicable legal norms in a default event.
"Where interest only loans are advanced for CRE, as part of the repayment capacity assessment, institutions should assess property cash flow to support a level of amortisation equivalent to the <u>projected economic life cycle of the property</u> to clear the principal amount and interest of the loan in the event of an increase in the LTV for the property <u>or to a regular LTV level in the relevant market (refinancing option). In the event of additional credit enhancements e.g. disposal assets (free from senior credit protection by third parties) that are legally enforceable in a reasonable time period, the aforementioned analysis shall be considered to be a recommendation."</u>

Paragraphs 166 and 177
Point a. states that a "reputable estate agent" must be used to assess the project development phase (in particular the business plan). In contrast to point c. of paragraph 166, the requirement does not contain a reference to "or similar". We consider this to be too narrowly worded and are seeking an expansion to include correspondingly qualified real estate valuer. We wish to point out in particular that in many European countries, estate agents do not have a reputation or training that is comparable with estate agents in English-speaking countries. We are therefore proposing the following addition:
"166a: The assessment of the development phase should cover: business plan, including documented rationale for the development supported by a location specific review of supply and demand in the market by a reputable estate agent <u>or valuer</u> with a relevant expertise;"

The requirements are very detailed and appear in part to be too sweeping, especially point b. Although the institution must satisfy itself of the expertise and capacities of the construction or project development management, the existence of necessary permits, etc., it does not have to have an understanding of the operational management as a whole and assess all the third parties involved. Point b. of both paragraphs should therefore be deleted.

Under point c. of paragraph 166, the projection of the costs should be certified by a "qualified and reputable quantity surveyor (or similar)" in the assessment of the project development phase. We are seeking clarification and suggest that the qualification “or similar” should also include correspondingly qualified real estate valuers. We are seeking the same clarification for point c. of paragraph 112.

Paragraph 170
Because of the subordinate status of equity investors, their assessment required in paragraph 170 has no relevant benefits; this question is relevant at best for the issue of equity margin calls and should therefore be limited to that case. Equally, the bank cannot be expected to manage the interests of the equity investors. The bank will represent its own interests, as a rule in a cooperative manner. The assessment of equity investors should be reduced to the case where they are or could potentially be subject to an equity margin call, in which case it should be limited to a verification of their financial position.
“In the case of equity margin calls, ~~In addition~~ ~~to assessing~~ ~~the creditworthiness of the borrower,~~ institutions should, in addition to the creditworthiness of the borrower, assess equity investors into the project, where relevant focusing on assessing their financial position, relevant expertise, experiences in similar projects, as well as alignment of interests between the equity investors and the institutions offering lending to the same project. The assessment should be carried out proportionately to the nature, complexity, term structure and level of embedded risk of credit loss.”

Paragraphs 171ff.
We take the view that all requirements should be construed in accordance with the proportionality principle and suggest restricting minimum requirement formulations in this light (see paragraphs 172, 173, 177 and 179). We also suggest the following amendments:
“171: When assessing creditworthiness of the borrowers in case of shipping finance, in addition to the general requirements for the creditworthiness assessment for professionals (Section 5.2.5), institutions should follow specific requirements of the current section proportionate to the complexity, term structure and level of embedded risk of credit loss. In particular institutions should assess the following:”
“173: In the case of loans to shipbuilding, institutions should assess the following, where appropriate:”
“173a: business plan, ~~including documented rationale for the shipbuilding supported by a vessel type specific review of supply and demand in the market by a reputable expert~~;”
“173b: in the case of shipbuilding companies that are not well-established on the market, background information, builders, architects, engineers, contractors and sub-contractors, who take part in the shipbuilding;”

Paragraph 173
This paragraph is unclear because it leaves open what is meant by “shipbuilding”: financing the shipyard or financing the shipowner? At least in the case of point d. of paragraph 173, there is a need to distinguish which permits and certificates are meant. If the shipowner is being financed, all of the shipyard’s permits and certificates will not normally be provided, so it will be impossible to assess them in full.

In addition, in point c. of paragraph 173 the words "internal or external" should be added before "qualified", as an external appraisal is unlikely to be necessary in all cases. The question also arises of what exactly is meant by "certified" here.

Paragraphs 174ff.
We suggest making a clearer distinction between project finance and infrastructure finance in paragraphs 174ff. In particular, infrastructure finance is not necessarily project-based, with the result that not all of the requirements for project finance are applicable to these exposures. As a minimum, a corresponding clarification should be made at a suitable point in the form of a qualification ("where appropriate").

Paragraph 176
The requirement stipulating which collateral is to be taken for project and infrastructure finance is far-reaching; by contrast, adding "to the extent possible" would allow flexibility. Please clarify how much scope for interpretation is available to the institutions for the decision. Additionally, we suggest the following amendment in order to avoid potential misunderstandings in relation to legal enforceability:
"176: ~~To the extent possible~~Where appropriate, institutions should ensure that all the assets of the project, and present and future cash flow and accounts are pledged to the institution providing the lending or to the agent/underwriter in the case of a syndicated transaction/a club deal. In case where a special purpose vehicle is established for the project, the shares of that special purpose vehicle should be pledged to the institution to enable the institution/agent to take the possession of the company, if needed. In the case of syndicated transactions/club deals, inter-creditor agreements should regulate each creditor's access to pledged funds and assets."

Paragraph 178
In our opinion, the requirement to also consider cost overruns means that the assessments required by the institution could be excessive. Please clarify that this means merely performing a plausibility check of any cost estimates by the borrower.

Paragraphs 180ff.
Without a technical solution, it will be almost impossible to implement the extended documentation and transparency requirements for the lending process required here under paragraph 180 taking into account loan documents, IT systems, multi-step application forms, etc. Implementing the requirements set out inter alia in Section 5.2 in the IT systems is not going to be possible by the proposed effective date of 30 June 2020 (see our General comments).

Section 5.3 is in general missing proportionate increments based on the riskiness of the relevant lending transaction.

Paragraphs 181, 182 and 183
Not every lending decision has to be made by a body and documented in detail (see Section 4.4, in particular paragraph 62). In the retail business, for example, decisions made by a single member of staff (with the necessary authority) or by automated lending processes (in compliance with the requirements set out in Section 4.3.3) may also be appropriate. We suggest adding these options.

Paragraph 184
We understand the requirement for a specific maximum period of validity to be an internal requirement for the institution in connection with the subsequent monitoring (Section 8.2) and credit review (Section 8.3), and are seeking corresponding clarification. By contrast, it would not be possible to require a contractual maximum period for all credit types (e.g. overdrafts/current account loans). Such facilities are granted "until further notice". This practice is also in the interests of the borrower, who can plan reliably provided that the terms of the facility are complied with, and does not have to make a new pro forma loan application at regular intervals. We suggest adding a corresponding opening clause for this case.

Paragraph 185
Paragraph 185 sets out that the loan should only be disbursed once all approval conditions as well as all preconditions set out in the lending decision or the loan agreement have been fulfilled. It is not clear whether the responsible decision-maker can approve disbursement in individual cases even if one of the disbursement conditions has not been met. The EBA should leave open the option of disbursement by a decision-maker in individual cases even if a disbursement condition has not been met.

Pricing (Section 6) (re Question 10)

Paragraphs 186ff.
The EBA's goal of ensuring risk-adjusted and cost-covering pricing throughout Europe is generally understandable. However, the proposed aspects represent a not inconsiderable restriction on the freedom of the banking industry to design its own business policies and determine its own methodologies. A particularly problematic aspect here is that no best or good practice approaches are shown, but rather that detailed supervisory requirements are imposed. In our view, pricing (methodologies and profitability calculation) should continue to be flexible for the institutions and based on individual methodologies/approaches. Minimum requirements could run counter to this goal.

Paragraph 186
We assume that the "credit quality and riskiness of the borrower" referred to in paragraph 186 relates to aspects from the scoring or rating process. If not, we would ask the EBA to clarify this.

It should also be clarified that the requirements/recommendations are only to be applied to credit exposures that are originated after the effective date of the Guidelines. Materiality aspects should also be taken into account.
"<u>Depending on the size, complexity and level of risk,</u> institutions should implement a comprehensive framework for the pricing of loans <u>for significant credit risks</u>. <u>For this area of application, the</u> pricing framework should reflect institutions' credit risk appetite and business strategies, including profitability and risk perspective and should be linked to the characteristics of the loan product. Institutions also should define their approach to pricing by borrower type and credit quality and riskiness of the borrower (in the case of individual pricing), where appropriate. Institutions should ensure that the pricing framework is well documented."

Paragraph 187
The words "and reflect" should be deleted. It is certainly possible that an institution arrives at the conclusion during the assessment that the impact of individual factors is negligible and that they therefore do not necessarily have to be taken into consideration.
In point a., it should be clarified that the cost of capital relates only to new business. If not, there could be procyclical effects (if, for example, an institution generated elevated credit risk in the past and would have to allocate the corresponding costs to new clients as well).

We also wish to point out that methodologies other than the cost of capital method constitute common pricing approaches, for example measuring RWA efficiency, return on equity, etc. The wording in point a. should be made more open in this respect.

Point b. postulates a behavioural approach to payment terms, which we interpret to mean consisting of the empirically observed repayment and drawdown behaviour of the borrower (before a default event occurs). These optionalities are often reflected as ex ante probabilities in advanced life time models of exposure at default (EAD), liquidity management and individual

risk-adjusted pricing (for material and complex exposures). For small and medium-sized banks, however, this requirement appears difficult to implement, among other reasons because of the low level of empirical data resources. In our view, it can only be applied in practice to medium- to long-term and complex financing structures. Point b. should therefore be amended as follows:
"cost of funding, which should match the key features of the loan, e.g. the expected duration of the loan. Wherever reasonable, institutions should take into account not only contractual terms but also behavioural assumptions;"

Point c.
Although managers responsible for a loan portfolio should always consider the operating and administrative costs of their portfolio in their overall decision making, it is not clear to us whether loan pricing should completely reflect those costs, as stated in the Draft Guidelines. This should be clarified as it would lead to a clearly negative impact. In product portfolios with high fixed costs, this might lead to non-competitive death-spiral pricing. The Guidelines should therefore leave more scope for modern pricing methods, such as partial cost methods or market price methods, behavioural pricing and pricing differentiation etc. The EBA should recognise that it is not feasible to break down allocated costs to every single credit product and should clarify that this is not required.

In addition, point d. should be amended as follows:
"*where useful and applicable, credit risk costs calculated for different homogenous risk groups taking into account historical experience of recognising credit risk losses and where relevant using expected loss models;"*

We generally take the view that the institutions should define their own criteria for designing and determining required returns/cost of capital, and capital allocation should take place on the basis of internally calculated requirements.
Point e. of paragraph 187 should be limited to material cost factors:
"*~~any~~ material other real costs associated with the loan~~, including~~ (e.g. tax considerations in the case of leasing transactions).*"

Paragraph 188
The factors that are relevant for pricing are already listed in sufficient detail in paragraph 187. Additionally using risk-adjusted performance measures is not absolutely necessary for management purposes, and would be associated with disproportionate effort and expense. This paragraph should be deleted overall for proportionality and materiality considerations.

Paragraph 189

Please refer to our comments on point c. of paragraph 187. The word "fair" should be replaced by "reasonable" for the distribution of costs.

Paragraph 190
When implementing the control mechanism with a monitoring requirement stipulated in paragraph 190, it is important to ensure a reasonable cost-benefit balance. In particular, this requirement should be limited to risk-relevant transactions and material elements of the calculation. Additionally, it would make sense to explicitly emphasise proportionality at this point.

As stated earlier, institutions may or may not decide to base their pricing purely on cost-plus-methods. Therefore, we disagree that every single transaction should be justified against cost. They should be reported, justified and monitored against the pricing framework documented by the bank. The EBA should recognise that it does not make sense to look at the loans on an individual basis, but rather that a portfolio view should be examined.

Valuation of immovable and movable property (Section 7) (re Question 11)

General comments on Section 7

The distinction made between "*property valuation*" and "*collateral valuation*" is insufficiently precise. Hence it is not clear what a valuation report must address and for what reference values must be given. In Germany, valuers value the property on which the collateral (e.g. real estate lien) is based. These values are used by the bank to value the collateral/the real estate lien. In other words, a property valuation report does not concern itself with the value and the legal enforceability of the real estate lien, as points a. and e. of paragraph 200 appear to expect.

Paragraph 191
It is a common and expedient practice in the German banking market to accept certain types of collateral for the purpose of improving the bank's negotiating position in respect of the borrower (for a potential scenario of financial difficulties of the borrower), but to waive the inclusion of the collateral value in the calculation of own funds requirements. There is therefore a need for a supplementary clarification that the requirements of Section 7 only have to be applied to collaterals with a positive value included in risk and capital management. Paragraph 191 should be supplemented correspondingly:
"191: Where credit facility is secured by an immovable or movable property collateral, institutions should ensure that the valuation of the collateral is carried out accurately at the point of origination. Institutions should set out internal policies and procedures for valuation that are in line with the institutions' credit risk policies and procedures. <u>The requirements of Section 7 are only mandatory for collateral that has a positive value and is used in risk quantification accordingly.</u>"

Paragraph 192
Various requirements of Section 7 refer to requirements of the CRR (in particular paragraphs 192, 207 and 211). For the recognition of the value of immovable property collateral in Pillar 2 risk management, however, it is not necessary to meet all of the CRR requirements for eligibility when calculating the own funds requirements. This should be clarified.

Requirements for valuation
Immovable property collateral

Paragraph 194
Paragraphs 194 and 201 state that all collateral must be valued. The institutions should have the flexibility to dispense with a valuation (see our comments on paragraph 191). This may be the case, for example, if the loan is granted on the basis of the borrower's credit quality and the collateral is not a material loan condition, but is merely offered by the borrower (possibly also with other banks for reasons of equality). If the institution would be forced in this case to value the collateral, it would have to reject the collateral if the expense does not appear to be

necessary. Another possible case is one where entire collateral packages are furnished, but the institution bases its decision only on individual items of collateral. In this case, only that collateral should be valued. In other words, exemptions should be possible (e.g. monetary thresholds for the credit volume or waiver of valuation documented in the lending decision or similar).

Paragraph 194 should be supplemented correspondingly:
"194: At the point of origination institutions should ensure that, <u>for risk-relevant loans,</u> the value of ~~all~~ immovable property collateral irrespective whether it is pledged against the loans to consumers or professionals is assessed by an independent qualified internal or external valuer."

The term "risk-relevant loan" should also be included in the definitions in Section 2.

Paragraph 195
The scenarios in which a desktop or purely drive-by valuation or revaluation is to be permitted are construed very narrowly, using the example of similar apartments in the same apartment block. These exemptions would therefore be almost impossible to apply in practice. Additional exemptions would be desirable here, at least for residential real estate financing (e.g. similar one-family homes houses in a residential estate, prefabricated houses of the same model, or the property is already known from a previous visit). The same applies with regard to paragraph 213.

In our opinion, the term "revaluing" is out of place here because Section 7.1 merely governs initial valuation in new business. Paragraph 213 should then contain requirements for revaluations.

In accordance with Section 4.3.3 (paragraph 47), institutions are allowed to use technology-based processes for granting credit, provided that certain conditions are met. For immovable property valuation, by contrast, this appears to be ruled out on the basis of the current wording of paragraph 194 and other paragraphs. In contrast to Section 7.2.1 (Monitoring and revaluation), the use of recognised statistical models is not mentioned in the requirements for the initial valuation of immovable property in Section 7.1.1. This does not appear to be appropriate, in particular in the retail business. When valuing standardised property, statistical or partially automated processes can deliver valid values and at the same time help to maintain or enhance process efficiency. GBIC suggests including an opening clause.

GBIC expects exemptions for the retail business of private housing finance. Depending on the size, nature, complexity and risk, institution-specific de minimis thresholds should be enabled in order to keep the time and cost required for valuing collateral in the standard business, e.g. residential real estate financing and smaller immovable property loans, under control. This is designed to prevent real estate financing only being profitable for banks above a certain amount or loans being granted unsecured (for internal cost reasons). Neither of these outcomes can be in the interests of the European banking supervisors.

"*195: Institutions should set policies and procedures specifying the approaches to be used by the valuer (e.g. desktop, drive-by or full visit with internal and external assessment of the property)~~,~~ and/or statistical models for different types of immovable property collateral ensuring that such approaches are prudent and proportionate to the type and potential values of the collateral and in relation to the credit agreements. ~~For the valuation of an immovable property by a valuer, institutions may consider using desktop or drive-by valuation approaches only in the cases of valuing or revaluing immovable property collateral (e.g. RRE and CRE) that is of similar design, specifications and characteristics to the ones already valued or re-valued by a valuer, e.g. similar apartments in the same apartment block~~. For less significant and standardised loan agreements, institutions may define de minimis limits for individual property valuation."*

Paragraph 196

In the event of financial difficulties and/or significant deterioration in the borrower's debt-servicing capacity, the liquidity, enforceability and expected time to recovery of the collateral should be reviewed. For reasons of practicability and process efficiency, GBIC considers these across-the-board requirements to be inappropriate in light of the principle of proportionality. Paragraph 196 should therefore be supplemented:

"196: In the case of significant deterioration in the repayment capacity of the borrower, institutions should carry out an assessment in terms of the liquidity and enforceability of the collateral including time to recovery. The assessment should be performed proportionately to reflect the complexity, size and type of the credit facility."

Paragraph 197

The establishment of a panel of accepted external valuers could cause friction in syndicated lending arrangements. We therefore suggest providing for an exemption from the requirement proposed here in the case of syndicated loans.

Paragraph 197 should be supplemented correspondingly:

"Where institutions use external valuers, they should establish a ~~panel~~ selection of accepted external valuers. The composition ~~of the panel of valuers~~ should ensure that valuers have relevant expertise in areas of the property sector, which is relevant to the lending activities of the institution as well as the location of these activities. In the case of syndications, the aforementioned provisions are merely recommendations."

Paragraph 198

Indemnity insurance is not market practice in every country and is not needed to ensure valuation quality. Mandatory insurance would increase costs that would be passed on to clients if they are not shouldered by large valuation firms that can afford the additional extra expense. Insurance premiums for small appraisal firms or individual experts would be necessarily higher. Hence, this would constitute a significant competitive disadvantage.

Paragraph 199

Paragraph 199 limits the purpose of the immovable property valuation solely to the loan application, which in the opinion of GBIC is neither necessary nor appropriate. The valuation should also cover following renewals or contract modifications (e.g. in the course of minor forbearance measures), and structural or legal changes to the property. In addition, paragraph 199 ignores situations such as syndicated financing or purchases of receivables of other banks, in which another credit institution orders or ordered the valuation. In the opinion of GBIC, there is no obligation on the credit institution either to carry out or to order the valuation. In this sort of scenario, a formal and material review of the submitted valuation is sufficient. GBIC considers the following amendments to be necessary:

"199: Institutions should ensure that the valuers provide an impartial, clear, transparent and objective valuation, and each valuation should have a final report providing the necessary information on the valuation process and property. The valuation report should clearly state who ordered the valuation and that the valuation has been requested for purposes of loan application ~~only~~, renewal or contractual adjustments, or in the case structural changes. Valuation should be carried out (internal valuation) or ordered (external valuation) by the institution or a collateral agent (in the case of syndicated loans), unless it is subject to a request from the borrower under certain circumstances."

Paragraph 200

GBIC recommends simplified documentation requirements for collaterals related to non-risk-relevant exposures. The disclosures and information required in a valuation report are too sweeping, especially for the standardised retail business of private residential real estate financing. Simplified documentation requirements for valuations have proven themselves in practice in Germany. The following amendments are sought:

"200: In the case of risk-relevant lending decisions, institutions should ensure at the end of the valuation process ~~institutions should ensure~~ that they have obtained for each property collateral a clear and transparent valuation report documenting all elements and parameters which determine the value of the collateral, including all information necessary and sufficient for easy understanding of such elements and parameters, in particular:

(…)"

For non-risk-relevant credit exposures, GBIC believes that simplified valuation reports should be possible. A new point g. should therefore be added to paragraph 200:

"200 g: In the case of non-risk-relevant lending decisions, the requirements of points b. and f. of paragraph 200 are not mandatory. Furthermore, a brief description of the collateral, its location and local market position is adequate. The legal attributes of the collateral can be assessed by using a simple checklist."

For small and medium sized institutions, the extensive requirements for valuation reports under points a. to f. of paragraph 200 represent significant process-related barriers that cannot be satisfied at a high quality and reasonable effort and expense. The amendments to paragraph 200 and the addition of point g. to paragraph 200 set out above also apply here.

Requirements for valuation
Movable property collateral

Paragraph 201
Article 229(3) of the CRR is not applicable to all institutions. Additionally, this article is only applicable if the collateral shall be eligible for calculating the Pillar 1 own funds requirements. Moreover, statistical models or adequate reductions based on the institution's verifiable experience with regard to the recovery of collaterals are not mentioned there and the requirements are based on the market value.

Under Article 229(3) of the CRR, we do not believe that there is a need to use a valuer to determine the market value of movable property. The requirements in paragraph 201 of the EBA Guidelines to use an independent qualified valuer therefore represent a considerable ad unnecessary tightening. We suggest deleting this requirement.

If the tightening is not deleted, paragraph 201 should at least be revised: the requirements for valuing movable property collateral should depend on loan amount, complexity and risk, as well as the type of collateral. In the case of automobile financing in the consumer credit business, among other things, it must be possible to use simplified valuation methods. For example, the purchase price taken from relevant valuation tables with flat-rate haircuts can be appropriate. Such comparatively simple valuations in the standardised retail business do not have to be performed by a valuer. An opening clause that also covers comparable assets is desirable.
"201: At the point of origination institutions should ensure that, for risk-relevant loans, the value of all movable property collateral, irrespective whether it is pledged against the loans to consumers or professionals, is assessed by an independent qualified valuer or appropriate ~~ad-vanced~~ statistical models or certain reductions based on the institution's verifiable experience ~~taking into account Article 229(3) of Regulation (EU) No 575/2013~~. Alternatively, adequate reductions based on the institution's verifiable experience can be taken into account. Based on the credit risk quality of the borrower and the market volume for a potential sale of the collateral and in case of standardised loan agreements, institutions may define de minimis limits for the individual valuation of the respective collateral and the use of simplified procedures."

We also assume that it is not necessary to provide corresponding certificates for the assessment of qualification. Many valuers have undoubtedly gained their qualification through many years of professional experience.

Paragraph 202
For groups of institutions and financial networks, it should also be possible to define the thresholds for the use of individual rather than indexed (statistical) valuation to be specified by the bank in accordance with paragraph 202 consistently using pooled data. There is thus no need for institution-specific thresholds in the case of small and medium-sized banks belonging to groups or IPS-related financial networks. It should also be clarified that the requirement for

individual valuation of movable property collateral depends on the value of the collateral in question. In the case of many items of movable property collateral, for example automobiles, which can be valued easily by standardised methods, it must be possible to value this collateral solely on the basis of statistical data. The individual valuation of a large number of motor vehicles would generate considerable costs that would not be offset by evident additional insights. The wording should be amended accordingly:
"202: <u>Given the nature, size and complexity of the</u> institutions, <u>they</u> should <u>(where appropriate)</u> set out in their policies and procedures approaches to using a valuer or statistical models for the purposes of such valuation, and specify internal thresholds and limits requiring individual valuation of the single movable property collateral at the point of origination to be performed by a valuer. <u>In the case of uniform valuation rules for a group of banks with a data pool, the thresholds can be obtained from a consolidated level for homogeneous types of institutions (e.g. size, complexity, business focus).</u> "

Paragraph 203
We presume that a "*panel*" of accepted external valuers required by paragraph 203 could also consist of two persons. Using additional valuers is associated with increased costs that would (have to) be passed on to the clients. We therefore suggest replacing the term "*panel*" by "*selection*".

Paragraph 204
Editorial note on paragraph 204: the reference given there is incorrect.

Under paragraph 204, a valuation report in accordance with paragraph 200 should also be obtained for movable property collateral. However, the requirements of paragraph 200 are tailored to immovable property and appear to be too high, at least for revolving movable property collateral such as pledges of inventory. This should be modified in the requirement.

Paragraphs 205 and 221
GBIC believes that it is necessary to clarify that, when statistical valuation models are used, the model design, the model parameters, the model limitations and assumptions (see paragraph 205), as well as the necessary data (see paragraph 221), are not mandatory required to be ensured at the level of the individual institution, but can also be appropriately modelled and reported using group-wide solutions.

Requirements for monitoring and revaluation
Immovable property collateral

Paragraph 207
Please clarify whether the requirements actually mean "*monitoring*" rather than "*reviewing*". If "*monitoring*" is actually meant, we do not consider the requirements to be expedient because monitoring real estate markets is a continuous process. Rather, the (event-driven) review of property values is mainly linked in practice to the elements listed in points a. and e. of paragraph 207. By contrast, we consider the use of gross carrying amounts and LTV ratios as

measures of the frequency of reviews and monitoring to be associated with disproportionately high effort. Point d. of paragraph 207 should therefore be deleted. In the context of implementing the NPL requirements, we consider the requirements of point b. of paragraph 208 to be met. Therefore, point b should be deleted as well.

Paragraph 208

Simplifications for the retail business and for minor cases are missing and are necessary in the opinion of GBIC.

Monitoring frequencies: The proposed parameters to be used to structure the frequencies of monitoring are not necessarily fitting. Market volatility and the risk of deterioration regarding industry, technical infrastructure and location as well as relevant market price developments are considered to be more suitable. The institutions have enough experience and market knowledge to judge what are the best parameters reflecting the risk structure of their portfolio. Hence, parameters for determining different monitoring frequencies should not be predetermined by the EBA.

Minimum valuation frequencies are not explicitly prescribed, but under paragraph 208 the institutions are supposed themselves to determine these frequencies depending on the risk of the financing transaction (e.g. completion status of the property, LTV ratio and credit quality of the borrower, etc.) and observing the applicable requirements of Article 208(3) of the CRR. Please clarify that these requirements only apply to risk-relevant credit exposures, and please delete points a. to c. of paragraph 208:

"208: <u>In the case of risk-relevant exposures</u>, institutions should set out appropriate frequencies for monitoring the value of the collateral, considering the type and value of the collateral at origination, and in relation to the credit agreement ensuring that:
(…)"

Paragraphs 209, 215 and 216

For homogeneous groups of RRE or CRE, simplified valuation is possible for revaluation purposes (paragraph 209). If the conditions of Article 208(3) of the CRR are not met, revaluation can also be supported by indexation using statistical models (paragraph 211). On the basis of solutions in groups of institutions and financial networks, GBIC wishes to recommend the following amendments to paragraph 209, as well as to paragraphs 215 and 216:

"209: Institutions should ensure that any indices and statistical models used to monitor the value of the collateral are sufficiently granular and that the methodology is adequate for the type of asset and lending product, and based on sufficient time-series of observed empirical evidence of previous transactions and appraisals of the collateral or similar collaterals. <u>These analyses may also be conducted on pool data</u>."

"215: Institutions' internal policies and procedures should indicate criteria for accepting advanced statistical model-based revaluations. These policies and procedures should account for statistical models' market experience, property-specific variables considered, use of

minimum available and accurate information, and models' statistical precision. These requirements can be fulfilled at a compound level based on a group or network of institutions with a common risk methodology and pool data. In that case, separate policies and procedures are not required for small and medium-sized institutions."

"216: If possible and suitable, institutions should ensure (on a stand-alone basis or at a compound level) that the advanced statistical models used for the purposes of revaluation of immovable property collateral are:
(…)"

Paragraph 211
Paragraph 211 refers to Article 208(3) of the CRR and requires a revaluation if the criteria for a review set out there are met. Article 208(3) of the CRR stipulates both the monitoring (point (a)) and event-driven and regular review (point (b)) of immovable property collateral. As required by point (b) of Article 208(3), a valuer must initially review whether the value of the immovable property collateral has declined materially. This is done by reviewing the parameters that are relevant for the value. A revaluation is only necessary if a material decline in the value is confirmed. With this in mind, we suggest revising paragraph 211 as follows:
"211: Where the conditions for a review in Article 208(3)(b) of Regulation (EU) No 575/2013 are met and a revaluation is necessary based on the results of the review, institutions should update the value of the immovable property collateral through a revaluation ...."

Paragraph 213
As Section 7.2. deals with monitoring and revaluation, we believe that only the requirements for revaluation should be referred to here. Use of the word "*valuing*", which refers to the initial valuation, is therefore not suitable here and should be deleted.

In our opinion, it should be possible as a simplification for revaluation visits to be at the discretion of the valuer (e.g. if material deteriorations in value are known) or using a longer cycle. We believe that this corresponds to the current requirements of Article 208 of the CRR and is compatible with the optional use of a statistical model.

Paragraph 214
For the revaluation of collateral for immovable property, paragraph 214 requires institutions to ensure the adequate rotation of valuers. In our view, a requirement to rotate the valuer for individual properties causes considerable additional costs, especially if external valuers have to be used. There are no apparent benefits from doing this. In addition, rotating valuers have to familiarise themselves with the new case. Moreover, it often happens in foreign markets that only a few qualified local valuers are available.

Especially for small and medium-sized institutions, the valuer rotation required by paragraph 214 cannot be implemented without undue cost and effort. An opening clause should be added. If not, using another (possibly external) valuer would significantly and proportionally increase the costs of mandatory valuer rotation. It cannot be the banking supervisors' intention that no

collateral should be taken in order to avoid such costs, or that immovable property loans should only be worthwhile for the banks above a certain amount. This could lead to a credit squeeze for small-scale property loans.
This requirement should be deleted or at least amended:
"214: Institutions should ensure adequate rotation of valuers, i.e. two sequential individual valuations of the same immovable property by the same valuer should result in the rotation of the valuer, leading to the appointment of either a different internal valuer or a different external valuer. For small and non-complex institutions, valuer rotation is not mandatory. Institutions may define de minimis limits and the use of simplified procedures."

Requirements for monitoring and revaluation
Movable property collateral

Paragraph 220
The minimum criteria defined in paragraph 220 (including collateral value, life span, condition of tangible assets, maintenance status, need for physical inspections and operating permits) for switching from a model-based to individual revaluation are not practicable. GBIC understands the economic imperative in the case of special assets serving as collateral, such as ships, aircraft, plant and machinery, etc., but not for less complex collateral (e.g. a car). The wording should therefore be amended as follows:
"220: […] Such criteria should be related, ~~at the minimum~~ where relevant, to the value of the single movable property collateral at the origination phase, life span, condition of tangible assets, such as depreciation and maintenance, necessity of physical inspections, and certification. The criteria should be proportionate to the exposure volume, the complexity of the collateral, the adaptability for alternative uses and the residual duration of the loan."

Requirements for valuers

Paragraph 223
As a rule, the fee for the valuation is linked to the size and the approximate estimated value of the immovable property. The existing wording should therefore be clarified. It should only rule out a conflict of interest where the valuer can increase the fee or salary by means of a more optimistic valuation.

Paragraph 224
Under paragraph 224, the institutions should continuously assess the performance of the valuers and in particular examine the concentration of valuations performed and the fees paid to specific valuers. Please clarify the objective of assessing the concentration and fees paid.

The quality of the valuation report, in particular with regard to the reliability of projections, should be subjected to back-testing using benchmarks (paragraph 224). GBIC proposes also allowing this back-testing to be performed using pool data due to the need for statistical data resources, and to be understood as merely a recommendation for small and medium-sized banks.

Paragraph 225

To avoid conflicts of interest, paragraph 225 requires the institutions to ensure that any valuers who are going to carry out the actual appraisal of a given property and their first-degree relatives meet the requirements set out in paragraph 225. Instead of the wording "*institutions should ensure*", we suggest requiring a contractual obligation on the part of the contractor. It is not clear how the institution should ensure this. Only the contractor can be responsible for assessing conflicts of interest.

In addition, extending the independence of the valuer to first-degree relatives cannot be assessed in practice by the credit institution.

Further, GBIC believes that these requirements are not practicable for small and medium-sized banks. The bank cannot undertake any active oversight. A simplification in the sense of "*compliance statements*", e.g. by checking a box in the valuation report, must suffice. Paragraph 225 should be amended accordingly.
"225: In order to mitigate any conflict of interest sufficiently, institutions should ensure <u>(by means of a compliance statement or a compliance checkbox within the valuation report)</u> that any valuers who are going to carry out the actual appraisal of a given property ~~and their first-degree relatives~~ meet the following requirements:
(…)"

Point c. of paragraph 225
Additionally, point c. of paragraph 225 should be limited to existing conflicts of interest:
"225 c. they do not have an actual or ~~potential~~, current ~~or prospective~~ conflict of interest regarding the property in question, the valuation process and the result of the valuation;"

Monitoring framework (Section 8) (re Question 12)

Section 8 General

The requirements for credit risk monitoring and reporting are very far-reaching and cannot be implemented by small and medium-sized institutions with an effort and expense that is commensurate with the risk of loss and with the earnings from credit business. Opening clauses to match the materiality of the risk of loss should therefore be added at various points. The approach outlined for early warning indicators and the watch-list does not appear appropriate for suitably taking into account the different characteristics of the institutions and the groups of clients. In many places, the requirements only appear to be practicable for corporate clients.

The requirements governing processes and data should therefore be made more differentiated in line with the principle of proportionality. It should also be ensured that the legal conditions exist for the processing and long-term storage of the extensive data. Because this information must also be collected for natural persons, we believe that it is necessary to concentrate on data that must necessarily be collected, so that the institutions can demonstrate a justified interest under the EU GDPR with legal certainty. We do not believe that this is sufficiently legally certain and transparent in the current Draft Guidelines.

Paragraph 238

The nature and scale of the requirements of paragraph 238 only fit large corporate clients and cannot be used either for consumers or for SMEs. We take a critical view of interference in the institutions' freedom to determine the methodology used in risk classification and risk monitoring processes. The aspects listed in paragraph 238 are often components of the qualitative risk factors in the creditworthiness analysis process.
We are therefore suggesting the following amendment:
"<u>For significant credit risk exposure to professionals</u>, institutions should also monitor information related to qualitative factors that could have a relevant influence on the repayment of the loan in addition to monitoring credit and financial metrics. These factors could include amongst others information […]."

Paragraph 239

It should be added here that institutions can make the scale and intensity of monitoring dependent on the nature, amount and risk of the loans.

If a technically supported portfolio approach in which the analysis of the borrowers is based on valid statistical data is chosen for subsequent assessments (e.g. renewals), the EBA should also continue to allow this portfolio approach for analysis purposes.

Paragraph 240

The words "and quantified" should be deleted. This requirement would also require small institutions with a less complex lending business to use cash flow-based methods in order to arrive at the quantifiability of changes. In addition, the requirement should be limited to risk-relevant lending transactions.

Paragraph 241
In particular in the small-scale lending business, implementation of the review requirements at the single borrower level would represent a disproportionately high effort for the institutions. As a rule, repayments are monitored automatically. In such cases, it is sufficient to prepare such reviews at a portfolio level. The requirements should be differentiated by the nature and risk of the lending transaction or an opening clause should be added.

Paragraph 243
The level of detail of this requirement is too high. Such a differentiation is not necessary for risk management especially at small and medium-sized institutions with less complex lending business. Each institution should be able to assess and define individually which type of concentration analysis is relevant. We propose streamlining this requirement as follows:
“*In addition, institutions should also consider concentration measures against the values specified in credit risk appetite, policies and procedures~~, including by product, geography, industry, collateral features (type, location), and quality of portfolios and exposures, in particular past due loans in buckets of 30, 60, and 90 days past due~~.*”.”

Paragraph 248
We are proposing the following amendment with the goal of making the requirements more proportionate:
“For significant credit exposures, borrower’s credit reviews should include an assessment of existing debt and (where feasible) borrower’s sensitivity to external factors such as foreign exchange rate volatility, where relevant, that may affect the size of debt and repayment capacity.~~, also in line with the sensitivity analysis requirements as specified in Section 5.2~~.”

Paragraph 249
We are proposing the following amendment with the goal of making the requirements more proportionate:
“For portfolio segments with a significant risk of credit loss, institutions should continuously assess risks associated with refinancing of existing debt, monitoring loans with bullet/balloon repayment terms separately from other loans. At least for the major risk exposures (in the sense of expected credit loss), institutions ~~They~~ should analyse potential effects on borrower’s inability to roll over/refinance existing credit facilities, and include where necessary ~~inter alia~~ forward-looking macroeconomic outlook, access to capital markets as well as other types of debt structures. For risk-relevant exposures, institutions should closely monitor indicators of borrowers’ ability to repay or refinance their debts throughout the loan’s life and not just for borrowers that are approaching the end of a loan’s term without a verified repayment vehicle in place.”

Paragraph 250
We are proposing the following amendment with the goal of making the requirements more proportionate:
"A regular credit risk review should take into consideration both the individual and the total risk profile of the exposure. ~~including macroeconomic factors and specific economic sectors or~~ Activities and how the repayment capacity may be affected by these factors should also be considered where needed."

Paragraph 254
We are proposing the following amendment:
"In the case of lending to professionals, institutions should also monitor non-financial covenants by means of collecting the covenant certificate, where applicable, but also by other means e.g. through close contact with the borrower by the client executive. These requirements should be understood as recommendations for less significant credit risk exposures."

Paragraph 257
We are seeking clarification that the requirement in paragraph 257 to perform sensitivity analyses does not go beyond the requirements of the EBA GL on stress testing (EBA/GL/2018/04). As stated here, external information should be used to perform sensitivity analyses regardless of the current market situation. However, this is not defined as a sensitivity analysis by the EBA GL on stress testing.

Sections 8.6 and 8.7
The approach described here for early warning indicators and the watch-list is not appropriate for suitably taking into account the different characteristics of the institutions and the groups of clients being analysed. In line with the proportionality principle, it should be possible to define more differentiated requirements for processes and data, depending on the size and complexity of the institution and the importance of the client segment for the institution.

Paragraph 261
In accordance with paragraph 261, the institutions should automatically derive measures when an early warning indicator (EWI) is identified. If an EWI is triggered, the risk situation is individually assessed on a holistic basis, so automatically deriving consequences is not expedient. We suggest replacing "predefined measures" by "individual measures/measures commensurate with the risk". Among other things, a consequence of a comprehensive early warning system is that not every EWI has to be linked to a measure.

Paragraph 263
In the course of ongoing monitoring of credit risk, among other things point f. of paragraph 263 requires the institutions to assess whether an existing transaction would be issued at different terms and conditions if it were to be originated again. In our opinion, the retroactive assessment of the original lending process is not expedient. Rather, the current situation should be assessed and individual measures should be derived.