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Leaseurope comments to the draft ECB Regulation on the materiality threshold for credit obligations past due

Leaseurope, the voice of leasing at European level, welcomes the opportunity to comment on the draft ECB Regulation on the materiality threshold for credit obligations past due.

The draft ECB Regulation establishes a relative materiality threshold equal to 1% for all significant institutions in Member States participating in the Single Supervisory Mechanism (SSM).

In the leasing industry it is common that the monthly instalment/rental on average will be higher than 1% of the contract exposure, however initially on average lower than 2.5% of the exposure.

In addition, missing 1 instalment/rental occurs more often in our industry than in a regular banking environment. In our experience this is not always a sign of deterioration of creditworthiness of the obligor. Therefore using the 1% threshold would lead to an incorrectly assigned default status for such an obligor. Applying the 2.5% threshold will mitigate this effect.

We are also concerned with the discretion included in the EBA Regulatory Technical Standards on materiality threshold for credit obligation past due, published on 28 September 2016, which allows national competent authorities (NCAs) discretion in setting the relative threshold in a range comprised between 1% and 2.5%. We assume that banks and financial institutions directly supervised by NCAs will comply with the threshold set by its NCA. Therefore, in some countries the relative limit could be higher than 1%.

For subsidiaries of large banking groups participating in the Single Supervisory Mechanism (SSM) we expect that it would apply the same relative threshold adopted by the parent institution in line with the SSM requirement. This will mean that banks and financial intermediaries operating in the same country could be using a different past due threshold depending solely on their ownership structure. This unintended consequence of the proposed ECB threshold will break the level playing field in countries where the NCA decide to apply a higher limit than the ECB.

We also would like to stress that a lower past due threshold intensifies the long term financing amortization effect on past due detection. In fact, for long term instalment payment types of financing such as leasing, the relative threshold is deemed to be increasingly conservative throughout the life of the financing contract. For fairly short residual contract duration, even a missed payment of a single instalment could lead to the breach of the relative threshold. Therefore, a unique relative threshold, that could be reasonable for a credit obligation considering its overall exposure amount, could nevertheless be excessively conservative if considered at later

stages of the credit life. Therefore, for the reasons expressed above, we call on the ECB to consider applying a 2.5% instead of a 1% relative materiality threshold.

Finally, we propose that the ECB consider an obligor defaulted only when it has at least 1 invoice with at least a 90 days past due status.

At a certain point during the lifetime of the contract, the monthly instalment/rental amount will exceed the 2.5% of exposure threshold. Analysis shows that this occurs on average already 8 months after origination of the contract. Therefore, we propose to only classify an obligor as defaulted if and when it has material arrears for 90 consecutive days, and one of the open amounts (instalment/rental) is more 90 days past the due. This approach is in line with the EBA methodology and at the same time aligns with leasing business model and portfolio characteristics, where arrears in the 0-60 day bucket are not unusual.

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About us

Leaseurope brings together 45 member associations representing the leasing, long term and/or short term automotive rental industries in the 32 European countries in which they are present. The scope of products covered by Leaseurope members' ranges from hire purchase and finance leases to operating leases of all asset categories (automotive, equipment, machinery, ICT and real estate). It also includes the short term rental of cars, vans and trucks. It is estimated that Leaseurope represents approximately 94% of the European leasing market.

Asset finance and leasing markets have developed to respond to business investment and consumption needs as well as to accompany the development of local industrial production and distribution. The types of institutions represented by the Federation include specialised banks, bank-owned subsidiaries, the financing arms of manufacturers as well as other, independently-owned institutions.

In 2016, the leasing firms represented through **Leaseurope's membership helped European businesses invest in assets worth more than 334 billion EUR**, reaching 779 billion EUR of outstandings at the end of the year¹. Leasing is used by more European SMEs than any individual category of traditional bank lending taken altogether (around 46% of all European SMEs make use of leasing which is more than any other individual form of lending)² and is also popular amongst larger corporates³. Leasing is also useful to support the public sector (e.g. leasing to schools, hospitals, etc.).

Leaseurope is entered into the European Transparency Register of Interest Representatives with ID n° 430010622057-05

¹ Leaseurope 2016 Annual Statistical Enquiry

² Oxford Economics, *The Use of Leasing Amongst European SMEs*, 2015; European Investment Fund, *The importance of leasing for SME finance, 2012*; European Central Bank, Survey on the Access to Finance of Enterprises in the euro area, June 2018

³ European Central Bank, Survey on the Access to Finance of Enterprises in the euro area, June 2018