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Leaseurope comments to the draft EBA Guidelines on Credit Risk Mitigation for institutions applying the IRB approach with own estimates of LGDs

Leaseurope, the voice of leasing at European level, welcomes the opportunity to comment on the draft EBA guidelines on credit risk mitigation (CRM).

General Observations

The EBA proposes in article 18(e) that for lease exposures treated as collateralised, the documentation should be consistent with Article 208(2) and (3) and Article 210 letters (a) and (g) of the CRR, where article 210(a) and 210(g) refer to legal certainty of the collateral and (re)valuation. For leasing, the most relevant legal certainty of the leased asset as collateral is the ownership of the asset which is stipulated in article 211. For this reason, we do not understand the purpose of the explicit reference to article 210(a). We think that under A-IRB the requirements for leasing on legal certainty and valuation are sufficiently stated in Article 181(1)(f), as being consistent with Chapter 4 of the CRR, and therefore it is not needed to refer to articles 208 and 210 of the CRR.

The reference to leasing on paragraph 21 on page 31, and on paragraph 17 on page 11 regarding the specification in the collateral agreement of the jurisdiction where the physical asset could move during the lifetime of the loan is burdensome for leasing, both at the start of the agreement and monitoring the legal effectiveness during the term of transaction. In particular, for certain movable assets such as vehicles that may move across all European jurisdictions as well as out of the EU.

As mentioned in the draft guidelines on page 11, softer alternatives, such as evaluating the jurisdiction where the collateral is usually located for the purpose of its use, should be considered.

The EBA proposes in articles 20 and 21 to assess the legal effectiveness and enforceability regarding the jurisdictions that the leased asset could be moved according to the documentation and also depending on the country of establishment of the lessee. In our view the explicit requirement to check the country of residence or where the leased asset is allowed to be moved is not strictly necessary under A-IRB for leasing as the lessor owns the physical asset, which is usually respected in all jurisdictions. It is already common business practice to ensure that it is checked as it is already mandated by Article 181(1)(f) of the CRR. Moreover, in the case of leasing, the main collateral is the ownership of the asset, which is safeguarded in principle in all jurisdictions.

It is a significant burden for lessors to verify the legal certainty of ownership in all countries where the asset may move, either when stipulated in the documentation, or for the relevant jurisdictions in general especially for small physical assets. In addition, the legal certainty of the property is always enforceable for the assets that are registered in Official National or International registers. This is the case for cars and trucks as well as for ships and aircrafts.

- For example in the general terms and conditions for a leased truck, the lessor should at least include all EU countries explicitly and it is not required to mention all the other countries that are foreseen. Excluding some countries may lead to individual adjustment of documentation that would require a full-fledged individual review of the documentation for a single truck customer. This approach is not workable for retail and SMEs leasing. In addition, if a truck is driven to an excluded country, violating the agreement, the test on legal certainty will not add any value. In addition, trucks are already subject to many taxation and goods carriage specific legislation requiring vehicle registration in a multitude of databases.
- The legal certainty of the property is always enforceable for the assets that are registered in Official National or International registers. In leasing contracts for boats and ships the lessee usually declares that it will use the asset mainly in international waters. This should not compromise the eligibility of the asset, as the registered property of an asset is legally enforceable everywhere.
- Under A-IRB limitations in legal certainty are usually covered by the internal figures on default cases, if it occurs on a structural basis.

Responses to the EBA Questions

Question 1: Do you agree with the proposed clarifications on eligibility requirements in accordance with Article 181(1)(f) of the CRR?

We have objections to the proposal for leasing in question 1 as the ownership of leasing is a very effective and strong form of physical collateral. We advocate for the deletion of the explicit requirements specified in article 210 of the CRR for leased physical collateral.

Question 2: Do you agree with the proposed clarifications on the assessment of legal certainty of movable physical collateral? How do you currently perform the assessment of legal effectiveness and enforceability for movable physical collateral?

The EBA proposes in paragraphs 20 and 21 to assess the legal effectiveness and enforceability regarding the jurisdictions that the leased asset could be moved according to the documentation and also depending on the country of establishment of lessee.

We think that in the case of leased physical assets article 181(1)(f) of the CRR provides enough guidance on legal certainty, and leaves room for each institution to make their own internal assessment on the quality of ownership and the legal documentation overall. Applying the same rules for legal certainty for a truck and an aircraft is not necessary. The explicit list of requirements

is quite burdensome for leasing, especially when dealing with SMEs and retail customers and will not contribute to a better estimation of the risks under the A-IRB, as any losses due to the risk of legal uncertainty should be reflected in the LGD estimation. To provide legal certainty is not enough in order to recover an asset in certain countries that have a less reliable judicial system. In particular, this is quite challenging for smaller assets.

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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 9% 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 2017, the leasing firms represented through **Leaseurope's membership helped European businesses invest in assets worth more than 384 billion EUR**, reaching 802 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 2017 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