

Kerstin af Jochnick
Chair
Committee of European Banking Supervisors

By email
cp18@c-eps.org

Brussels, 15 August 2008

Leaseurope response to the consultation paper on CEBS's technical advice to the European Commission on options and national discretions (CP18)

Dear Ms af Jochnick,

Please find Leaseurope's response to the CEBS consultation on options and national discretions (CP18) attached.

Leaseurope wishes to congratulate CEBS on the work it has performed on this very extensive and important topic. All in all, we have found the consultation period leading up to the publication of CP18 to be very thorough and transparent.

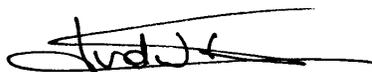
Our response focuses on the principal matters of concern for the European leasing industry as these are the areas where we believe we can bring about the most added-value to the consultation process.

Generally speaking, we are of the opinion that CEBS's proposed solutions will bring about significant improvements to the CRD as it stands today. There are however some areas where we take the view that CEBS has not entirely respected the high level considerations it sets out in the CP, in particular for the treatment of other physical collateral which is a key issue for the European leasing industry.

Going forward, we encourage CEBS, in conjunction with the European Commission, to finalise a timetable for integrating the proposed changes into the CRD as soon as possible.

For any further information you may require on our response, please do not hesitate to contact me or Jacqueline Mills at j.mills@leaseurope.org or +32 2 778 05 66.

Yours sincerely,



Tanguy van de Werve
LEASEUROPE DIRECTOR GENERAL

Copy to: Patick Peason, Head of Unit H1, DG Markt

About Leaseurope

Leaseurope is the voice of leasing and automotive rental in Europe. In 2007, the firms represented through our 46 Member Associations in 34 countries across Europe granted new leasing business worth in excess of 340 billion euros, making the European leasing market the largest in the world. Together, these companies finance just under 20% of all European investment and around 28% of all European investment in moveable goods.

Part I. General considerations

Overall approach

1. Leaseurope welcomes the opportunity to comment on CEBS's consultation paper on its advice to the Commission on national discretions and options in the CRD. Leaseurope strongly supports CEBS's work in this important field and appreciates the pragmatic approach that CEBS has developed in order to analyse each individual discretion and option systematically.
2. Moreover, we are fully supportive of the entire consultation process that has led to the publication of CP18, including the creation of the industry expert group in which Jacqueline Mills, Senior Adviser to Leaseurope, took part. Although the group was required to react under a very tight timeframe, its creation was extremely useful in order for the industry and CEBS to exchange preliminary views, thereby identifying early on in the process areas of agreement between CEBS and the industry as well as highlighting areas requiring further investigation. Moreover, we are of the opinion that the group's composition was correctly balanced, reflecting the views of larger and smaller institutions and a variety of industries. All in all, CEBS has demonstrated an exceptional degree of transparency throughout this consultation process and we would recommend that the concept of expert groups be replicated within other CEBS work streams whenever appropriate.
3. We would however wish to draw CEBS's attention to the fact that the industry expert group did not *per se* approve of the extension of CEBS's deadline for producing its final advice, although we appreciate that CEBS was asked to achieve a considerable amount of work in a very short period of time. We mention the timeframe issue as we seriously regret that the outcome of CEBS's work on national discretions and options was not timed to coincide with the Commission's work on the review of the CRD. We note that EBIC has already expressed this disappointment to the Commission in its response to the CRD Review consultation. We understand from the Commission¹ that subsequent changes to the CRD forming part of the comitology process may be addressed in a proposal before the end of this year. Nevertheless, the timing for any changes to the articles of the CRD not subject to comitology is uncertain. We wish to draw CEBS's attention to this issue as it is crucial that all issues of national discretion and options are resolved as soon as possible once CEBS's advice is final. We call on CEBS to address this issue, in conjunction with the Commission, and to provide indications of future timing within its final advice.

¹ 28 May 2008 meeting between EBIC and Commission

High level considerations

4. The development of high level considerations in §24 of the CP is very useful for understanding how CEBS has reached its conclusions relating to the individual discretions and options. We believe that the factors contained within these considerations are appropriate and that they should be respected and applied consistently throughout the analysis.
5. In particular, we welcome CEBS's recognition of industry's argument that "the discretionary part of options and national discretions could be deleted if the fulfilment of a set of criteria to be applied by the credit institutions/investment firms is satisfactorily defined in the CRD"². Indeed, we take the view that once a number of conditions are set out in the CRD and supervisory authorities are appropriately satisfied that these conditions have been respected, there is no longer a case for maintaining a level of discretion. In our response below, we have flagged some areas where we believe that CEBS has not consistently applied this principle.
6. Additionally, we support the introduction of a joint/common assessment process amongst supervisors³ as a method for dealing with certain discretions. Such a process can be particularly useful for encouraging supervisory convergence, particularly in areas where the CRD is not sufficiently explicit in the criteria that need to be respected in order to obtain a certain treatment. However, it should be made clear that joint assessment should also lead to a joint outcome; otherwise the process will not lead to any practical improvements.
7. CEBS has rightly recognised that decisions on the individual discretions and options should be subject to a high level impact assessment⁴. However, we note that the analysis contained within the consultation paper does not always reflect such an exercise which in our view should cover not only general prudential considerations but also a cost/benefit assessment for the industry. Moreover, we wish to highlight that, due to its method of functioning and the lack of time in which it had to react, the industry expert group was often not in a position to provide CEBS with detailed cost/benefit analysis.

² High level consideration d)

³ High level consideration e)

⁴ High level consideration c)

Glossary

8. CEBS's glossary is a most useful tool as it has the merit of clarifying what is meant by the various methods for dealing with discretions and options and should therefore result in improved understanding of the proposed solutions for individual provisions.
9. Regarding the category "keep as a national discretion"⁵, we welcome the breakdown into subcategories. In particular, for those discretions automatically expiring by 2011, we recognise that CEBS has chosen a pragmatic approach by allowing the discretion to run its course. However, we wish to underline that there are cases where we believe permanent discretions may be warranted (see for example our comments on NDs 68 and 70 below) and in-depth analysis of these items should not be neglected.
10. CEBS's justification for the fall back position of non-binding mutual recognition⁶ is in our opinion unsatisfactory. Indeed, the onus should be on supervisors to ensure the exchange of any relevant information so that binding mutual recognition may be applied.
11. Leaseurope fully appreciates that the CRD contains a number of supervisory decisions⁷ where supervisors are required to evaluate whether it is appropriate to apply a certain provision or not and welcomes the fact that CEBS has highlighted these as a separate category. We are however more cautious when it comes to the current distinction that is made between those cases where supervisors should exercise judgement in the evaluation of whether certain criteria have been fulfilled and where there is no longer any room for discretion⁸ and those where there is potentially still room for supervisory choice⁹. While supervisors must be able to exercise their judgement as required, we fear that category c ii) will introduce an additional layer of discretion into the CRD that will not be transparent vis-à-vis industry. Our concern is that supervisors would be able to make decisions without having to disclose or justify the underlying reasoning for doing so and could potentially make different choices for different institutions even though individual circumstances would be similar and therefore not warrant any distinction.
12. Consequently, we recommend that CEBS distinguish instead between those cases where judgement is necessary but limited to the evaluation of whether a given set of conditions is satisfied (see §5 above) and those cases where judgement is necessary and a clear set of conditions is not provided within the CRD. In the latter case, CEBS members should work together along the lines of a joint assessment process to agree on a common understanding of the criteria and to establish how they would judge these criteria to be appropriately fulfilled. Additional use of the supervisory disclosure framework should be made to render decision-making criteria and processes more transparent.

⁵ Glossary point a)

⁶ Glossary point b ii)

⁷ Glossary point c)

⁸ Referred to as judgement but no choice in point c i) of the Glossary

⁹ Referred to as judgement and choice in point c ii) of the Glossary

Part II. Individual national discretions and options

13. In line with our October 2007 response to the CEBS questionnaire on national discretions and options in the CRD, Leaseurope has chosen to comment only on those discretions or options of direct importance for the European leasing industry. This does not imply that other discretions are not relevant for European leasing institutions who are confronted with issues common to all institutions subject to the Capital Requirements Directive and we refer CEBS to the EBIC response for further information on these. Nevertheless, we feel that we can best contribute to the ongoing discussions on national discretions in areas where we have specific expertise or concerns and have therefore limited our response to these.

ND 39 - Treatment of revolving retail exposures linked to a wage account

14. We disagree with CEBS's analysis of ND 39 in terms of the relative importance of this discretion. Indeed, the discretion is extremely important for providers of consumer credit¹⁰. Moreover, CEBS's review of the discretion's application shows that 70% of Member States have already chosen to apply it. We therefore fail to see how CEBS has reached its conclusion. While local legislation may play a role in the existence and use of revolving retail exposures linked to a wage account, we take the view that if these do exist, the option should be left to the credit institution to decide whether the exposures should be recognised as qualifying revolving exposures (if all other conditions are met) or whether they should be treated as collateralised exposures.

15. We therefore propose the following wording:

Annex VII, Part 1, Point 13 (last sentence)

When collateralised credit facilities are linked to a wage account, institutions may choose to treat such exposures as qualifying revolving exposures. In this case, amounts recovered from the collateral shall not be taken into account in the LGD estimate.

ND 49 - Recognition of other physical collateral

16. Leaseurope wishes to stress that the recognition of other (i.e. non real estate) physical collateral under the CRD is one of the most important issues for the European leasing industry. This is because leasing is a form of asset-based finance where the lessor, contrary to other means of (secured) finance, maintains the ownership of the leased asset throughout the contract term. The lessor thus benefits from additional security due

¹⁰ This was signalled to CEBS in the October 2007 response of Leaseurope's sister federation, Eurofinas, the European trade association representing specialised providers of consumer credit

to the ownership of the asset and should be allowed to recognise this protection. The importance of this provision for the leasing industry could therefore be better reflected in CEBS's analysis of ND 49. Moreover, we note that this is a provision contained within the Basel II framework and is a key feature of the new approach to minimum capital requirements.

17. Leaseurope takes the view that the proposed solution for this discretion could go one step further. Indeed, Leaseurope would like to reiterate its concerns relating to maintaining the wording of the discretion as it is when the provision contains a list of conditions. Supervisors should no longer have the choice not to recognise collateral if they are satisfied that the given criteria (liquid markets, publicly available prices) are met by the institution. This point has already been made by the industry expert group and was repeated during the public hearing held by CEBS on 17 June. Failure to remove this additional level of discretion will maintain today's current situation of Member State A accepting a valid asset as collateral but Member State B not recognising the same category of assets, even though these assets fulfil all the necessary prudential requirements. This clearly creates an unlevel playing field for lessors.
18. In light of § 16 and 17 above, we take the view that it is inappropriate for CEBS to state in its analysis of a possible solution that "it would be less prudent to introduce (the discretion) across the board". Once again, we stress that supervisory oversight as to the respect of the fulfilment of the given criteria should be maintained although there should be no further degree of supervisory discretion.
19. We therefore suggest the following wording:

Annex VIII, Part 1, Point 21

*The Competent Authorities ~~may~~ **shall** recognise as eligible collateral physical items of a type other than real estate collateral, if **when** satisfied as to the following: (a) liquid markets for disposal of the collateral do exist in an expeditious and economically efficient manner; and (b) well-established, publicly available market prices for the collateral do exist. the institution must be able to demonstrate that there is no evidence that the net prices it receives when collateral is realised deviates significantly from these market prices. **Either the criteria used or the list of physical items recognised as eligible collateral other than real estate shall be disclosed by each competent authority in the supervisory disclosure framework referred to in Article 144 of this Directive***

20. We very much welcome the inclusion of a requirement to disclose more information in the supervisory disclosure framework as this is likely to highlight any discrepancies in Member States' recognition of other physical collateral and to foster convergence in supervisory practices. We would however caution that in order for information on the types of criteria used to prove useful and to increase transparency, all supervisors will have to provide complete and comparable information. We call on CEBS to ensure that this is the case.
21. Our last concern on the issue of other physical collateral recognition relates to the proposal for non-binding mutual recognition. Firstly, we wonder what exactly is meant by collateral "that is not bound to the local market". If it relates to moveable assets (which is likely to be the case for the vast majority of assets in the other physical collateral category), any concerns on the part of CEBS may not be founded, at least in the case of leasing. This is due to the fact that part of the minimum requirements for recognising these assets when they are leased (Annex VIII, Part 3, Para 11) require institutions to have robust risk management in place to address the use to which the asset is put, to ensure that there is a framework in place establishing the lessor's ownership and thus its capacity to repossess the asset if necessary. Consequently, if the lessor can prove to its supervisor that these systems are in place to guarantee the quality of the collateral and the supervisor is satisfied thereof, why should other supervisors not be required to recognise this decision even if the asset is a moveable asset? In other words, why should mutual recognition not be binding in this case?
22. Moreover, CEBS should consider whether its current drafting proposal adequately achieves its stated objectives. Indeed, CEBS mentions in the analysis of the possible solution for this discretion that "where the collateral is local and recognised (...) other supervisors will be expected to take on board the local supervisor's judgement". However, given the wording of the mutual recognition clause as it is proposed for the moment, we believe that this will not be the case as nothing obliges other supervisors to effectively do so ("the competent authorities of other Member States may allow their credit institutions to recognise that collateral as eligible"). Leaseurope therefore recommends that any mutual recognition clause introduced in this area of the CRD be binding.

ND 50 – Eligible protection providers

23. Although CEBS's proposal to add mutual recognition is an improvement on the current situation, we again fail to see how the maintenance of a discretion is justified. The current text provides for sufficiently robust criteria (the institution to be used as a protection provider must be authorised and supervised under equivalent standards to those applied to credit institutions) that, if fulfilled, no longer requires any level of supervisory discretion.

ND 55 – Reduced LGDs for leasing transactions and senior exposures secured by residential and commercial real estate

24. Leaseurope very much supports CEBS's recommendation to maintain the discretion as it is and to ensure that the required review takes place before end 2012, thereby ensuring certainty of treatment from 2013 onwards. Additionally, we believe that if the outcome of the review is in favour of maintaining lower LGD levels the discretion should be applied as a general rule in order to elevate level playing field concerns.
25. Nevertheless, we wish to point out that we are not in agreement with CEBS's statement in its analysis of the discretion that "this is a less prudent option and there are no real local market characteristics driving the choice". We wish to remind CEBS that LGDs for lease exposures tend to be lower than for other forms of secured finance as lessors benefit from the ownership of the leased asset, implying (amongst others) that they are able to repossess the leased asset without going through lengthy bankruptcy procedures or realising a pledge on the asset. Leaseurope has in the past provided evidence of the lower LGD levels of lease exposures.

ND 68 – Transitional treatment for certain property leasing transactions

26. We welcome CEBS's analysis and conclusion on ND 68 which better reflects the views of the European leasing industry than during earlier stages of the consultation process and consider binding mutual recognition to be an appropriate solution until end 2012.
27. We would like to recall that the real estate leasing industry is concentrated in 4 or 5 main markets (i.e. Italy, Germany, France, Spain, Portugal, ...) which explains why the majority of Member States do not make use of the discretion. However, within these countries, its use is of great importance to the industry. The removal of the discretion would result in a severe and unjustified penalty for the real estate leasing industry, which may see its capital requirements double. Such a treatment would not be risk-based as real estate lessors, due to the fact that they own the leased property, benefit from its immediate and direct protection.
28. Consequently, we would recommend that a review clause be inserted into the text as this was the original thinking behind the introduction of the provision into the CRD. Moreover, we wish to remind CEBS that an equivalent provision was already available under previous Directive 2000/12/EC and that it is of significant importance for institutions that do not possess historical statistical data due to the existence of small portfolios in this domain. The review should take place before end 2012 so as to guarantee certainty of treatment as from 2013. If the outcome of the review is to keep the treatment proposed in the discretion, the provision should be applied as a general rule.

ND 70 – Transitional use of a different definition of past due

29. Leaseurope takes the view that this provision should be maintained beyond the current expiry date. This is due to the existence of legal requirements for the authorisation of lease rental payments by PSEs in certain countries that imply that 90 days is too short a period to be able to identify whether such an entity is truly in default. Equally, it is also common practice for corporate lease rental payments in these countries, to be made on a quarterly basis.
30. As a result, Leaseurope recommends that expiry date for this provision be lifted. This would have the additional advantage of aligning ND 70 with the equivalent discretion under the Advanced Approaches (ND 113).

ND 102 – Waiver to definition of residential real estate

31. Similarly to other discretions of the “same nature”, Leaseurope takes that view that if supervisors are satisfied that the given conditions are fulfilled there is no longer any justification for maintaining the provision as a discretion.
32. We therefore suggest the following wording:

Annex VIII, Part 1, point 16, 1st sentence

*The competent authorities ~~may~~ **shall** waive the requirement for their credit institutions to comply with condition (b) in point 13 for exposures secured by residential real estate property situated within the territory of that Member State if the competent authority have evidence that (...).*

33. Additionally, we are fully supportive of CEBS’s insistence on the need for disclosure on the use of this provision and call on CEBS to ensure that the appropriate level of disclosure is made by the competent authorities within the supervisory disclosure framework.

ND 103 – Mutual recognition of the above waiver

34. Leaseurope welcomes CEBS’s proposal to introduce binding mutual recognition.

ND 104 – Waiver to definition of commercial real estate

35. See our comments on ND 102 above. Leaseurope believes that as a number of conditions are specified within the CRD text, further discretion is no longer justified.

36. We therefore suggest the following wording:

Annex VIII, Part 1, point 17

*The competent authorities of the Member States ~~may~~ **shall** waive the requirement for their credit institutions to comply with the condition in point 13(b) for commercial real estate property situated within the territory of that Member State, if the competent authorities have evidence that the relevant market is well-developed and long-established and that loss-rates stemming from lending secured by commercial real estate property satisfy the following conditions (...)*

ND 105 – Mutual recognition of above waiver

37. Leaseurope welcomes CEBS's proposal to introduce binding mutual recognition.

ND 113 – Number of days past due

38. See our comments for ND 70 above. Leaseurope would like to point out that due to certain specificities for real estate leasing, a higher number of days past due for real estate leasing to PSEs in particular is justified.

39. Leaseurope thus recommends that ND 113 be maintained in its current form and that ND 70 be aligned with ND 113 as it stands today (i.e. no expiry date).

ND 136 – Waiver to definition of residential real estate

40. See NDs 102 and 104 above. Where supervisors are satisfied that exposures are fully and completely secured by mortgages fulfilling the applicable criteria, the provision should apply as a general rule. Moreover, CEBS should ensure effective disclosure.

41. We therefore suggest the following wording:

Annex VI, Part 1, point 49

*Competent authorities ~~may~~ **shall** dispense with the condition contained in point 48(b) for exposures fully and completely secured by mortgages on residential property which is situated within their territory if they have evidence (...)*

ND 137 – Mutual recognition of the above waiver

42. It is our understanding that CEBS's proposal would effectively imply mutual recognition as a general rule. However, we wish to point out the inconsistency in wording in comparison to NDs 103 and 105 (i.e. the equivalent provisions for the Advanced Approaches) where CEBS proposes clear binding mutual recognition. Leaseurope takes the view that the wording used should be harmonised and recommends that binding mutual recognition be chosen for clarity's sake.

ND 138, 139, 140 – Commercial real estate treatment

43. See ND 136. When supervisors are satisfied of the application of the relevant conditions, the provision should apply as a general rule.

44. For instance for ND 140, we therefore suggest the following wording:

Annex VI, Part 1, point 53

*~~Subject to the discretion of the competent authorities, e~~Exposures related to property leasing transactions concerning offices or other commercial premises situated in their territories under which the credit institution is the lessor and the tenant has an option to purchase ~~may~~ **shall** be assigned a risk weight of 50% provided that the exposure of the credit institution is fully and completely secured to the satisfaction of the competent authorities by its ownership of the property.*

NDs 141, 142, 143 – Mutual recognition

45. Although we wish to flag a difference in wording (see ND 137), we support CEBS's proposals as we understand them to be equivalent to automatic mutual recognition.

ND 151 – Definition past due – corporate exposures

46. See our comments to ND 70 above. A higher number of days past due for leasing to corporates is useful in certain countries.