

# Public Hearing: Consultation on GLs on ADC exposure to residential property

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EBA Prudential Regulation and Supervisory Policy

Virtual meeting, 20 June 2024



# Ground rules for this virtual meeting.

## Mic and video off

Please keep yourself muted and the video off while listening.

## Questions/comments?

Please use the chat or raise your hand to ask for the floor.

## Slides on EBA website

The presentation used today will be made available on the EBA's website after this hearing.

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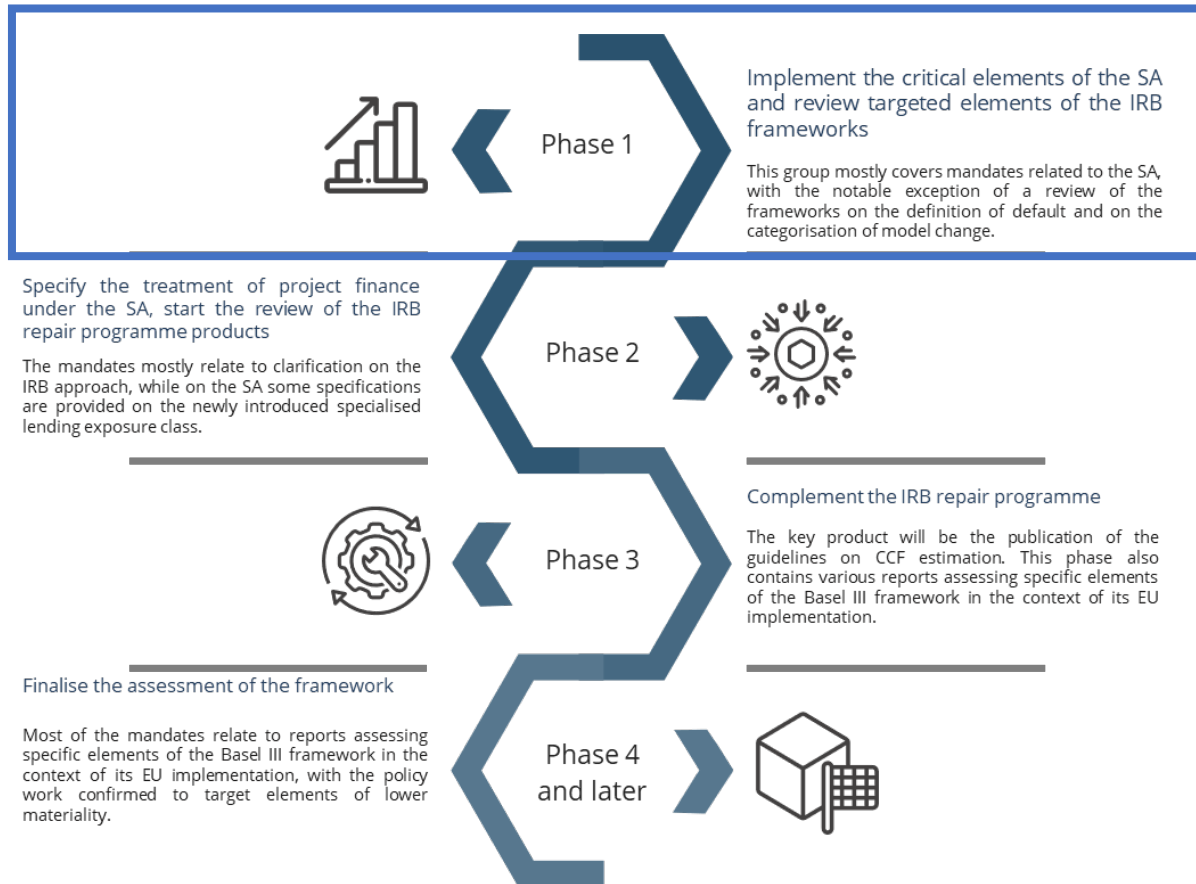
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## EBA Roadmap on CR mandates under CRR3

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# EBA Roadmap – Overview CR



# EBA Roadmap – CR Phase 1

Area	Product	Reg.	Article	Deliverable	Legal deadline
<b>Phase 1</b>					
Credit risk	Report	CRR	506	Report to the Commission on the eligibility and use of policy insurance as credit risk mitigation techniques	0 months after entry into force
Credit risk	ITS	CRR	20(8)	ITS on joint decision process for internal model applications	12 months after entry into force
Credit risk	RTS	CRR	111(8)	RTS on criteria that institutions shall use to assign off-balance-sheet items, constraining factors for UCC and notification process	12 months after entry into force
Credit risk	Guidelines	CRR	123(1)	Guidelines to specify proportionate diversification methods for retail definition	12 months after entry into force
Credit risk	RTS	CRR	124(12)(sub 1)	RTS to specify the term “equivalent legal mechanism” in place to ensure that the property under construction will be finished within a reasonable time frame	12 months after entry into force
Credit risk	Guidelines	CRR	126a(3)	Guidelines specifying the terms substantial cash deposits, appropriate amount of obligor-contributed equity and significant portion of total contracts	12 months after entry into force
Credit risk	Guidelines	CRR	178(7)(sub 1)	Guidelines on the definition of default, in particular for diminished financial obligation	12 months after entry into force





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## Legal Basis and Scope of the GLs

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# Legal Basis and Scope

## Article 126a

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*EBA shall by ... [1 year after entry into force] issue guidelines specifying the terms “substantial cash deposits”, “financing ensured in an equivalent manner”, “appropriate amount of obligor-contributed equity”, and “significant portion of total contracts”, taking into account the specificities of institutions’ lending to public housing or not-for profit entities across the Union that are regulated by law and that exist to serve social purposes and to offer tenants long-term housing.’*

## Scope of the CP GLs

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**Definition of ADC** (Article 4(1)(79)): exposures to corporates or special purpose entities financing any land acquisition for development and construction purposes, or financing development and construction of any residential or commercial immovable property;

**Preferential Risk Weight Treatment:** 100% instead of 150% for ADC exposures to residential property

- **Condition 1:** Significant portion of total contracts of which:
  - ✓ Pre-sale / pre-lease contracts with substantial cash deposit, or finance ensured in an equivalent manner (FEM).
  - ✓ Sale and lease contracts.
- **Condition 2:** Appropriate obligor-contributed equity relative to property value upon completion.





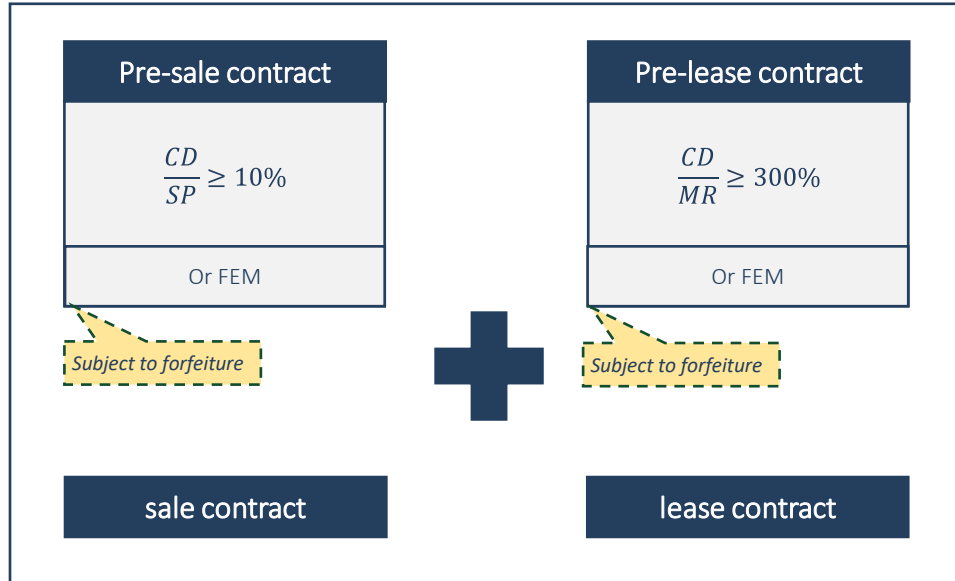
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## Condition 1

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# Condition 1: Overview



**Q1:** Pre-sale and Pre-lease characteristics

**Q2:** Relative Thresholds

**Q3:** Adequacy of 10% pre-sale contract ratio

**Q4:** Differentiation thresholds based on empirical data

**Q5:** Drawbacks of pre-lease contract ratio

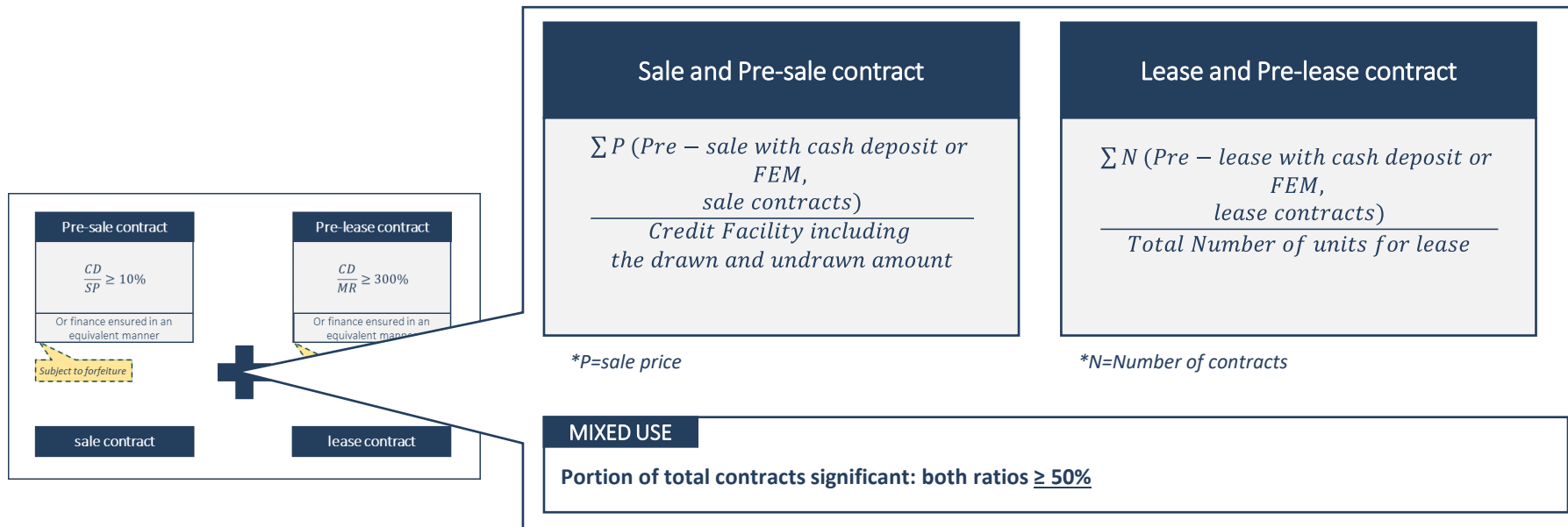
**Q6:** Other alternatives for the ratio

**Q7:** Like Q4 but for pre-lease ratio

**Q8:** Ratios equally substantial for pre-sale and pre-lease

**Q9:** Other forms of FEM

# Condition 1: How is the significant portion calculated?



**Q10:** Two different options for sale and lease

**Q11:** Drawbacks for the two above ratios

**Q12:** Materiality of mixed-use ADC projects

**Q13:** Pros & Cons of the approaches considered

**Q14:** Agreement with the Approach proposed

**Q15:** Other possible approaches

**Q16:** Other possible approaches for mixed use ADC projects

# Condition 1: Example 1

Bank B grants Realty Corp an ADC loan of **EUR 20 million**. The project consists of **70 apartments for sale** and **30 for lease**.

As of today, Real Estate Corp has achieved the following objectives:

- Pre-sold 6 apartments, of which 5 with substantial cash deposit. The 5 with cash deposits have been sold for a total of 1 million.
- Sold 35 apartments for 10 million.
- Pre - Leased 12 apartments, of which 11 with substantial cash deposit.
- Leased 5 apartments.

## Calculation of the significant portion of total contracts

$$\frac{\sum P (\text{Pre - sale with cash deposit or FEM, sale contracts})}{\text{Credit Facility including the drawn and undrawn amount}} = \frac{(1 + 10)}{20} = 55\%$$

$$\frac{\sum N (\text{Pre - lease with cash deposit or FEM, lease contracts})}{\text{Total Number of units for lease}} = \frac{(11 + 5)}{30} = 53\%$$

→ Both ratios exceed the 50% threshold: RW = 100 %.

# Condition 1: Example 2

Bank B grants Realty Corp an ADC loan of **EUR 20 million**. The project consists of **70 apartments for sale** and **30 for lease**.

As of today, Real Estate Corp has achieved the following objectives:

- Pre-sold 6 apartments, of which 2 with substantial cash deposit. The 2 with cash deposits have been sold for a total of 0.5 million.
- Sold 28 apartments for 8.5 million.
- Pre - Leased 12 apartments, of which 11 with substantial cash deposit.
- Leased 5 apartments.

## Calculation of the significant portion of total contracts

$$\frac{\sum P \text{ (Pre - sale with cash deposit or FEM, sale contracts)}}{\text{Credit Facility including the drawn and undrawn amount}} = \frac{(0.5 + 8.5)}{20} = 45\%$$

$$\frac{\sum N \text{ (Pre - lease with cash deposit or FEM, lease contracts)}}{\text{Total Number of units for lease}} = \frac{(11 + 5)}{30} = 53\%$$

→ One of the ratios does not exceed the 50% threshold: RW = 150%.



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## Condition 2

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# Condition 2: Forms of equity

5 forms<sup>(\*)</sup> of “eligible” equity, which is only a subordinated residual claim on the property, are defined:

- Cash invested in the project and segregated from other assets;
- Subsidies and grants;
- Unencumbered readily marketable assets directly linked to the project;
- Expenses for development or construction;
- Land or improvements.

*(\*) complete description in the CP.*



$$\frac{\textit{Obligor contributed equity}}{\textit{Property Value upon completion}} \geq 35\%$$

Q17: Practical impediments in the residual claim feature

Q18: Appropriateness of the threshold

Q19: Appropriateness of the approach and other options

Q20: Calibration of the level of thresholds of both condition 1 and 2



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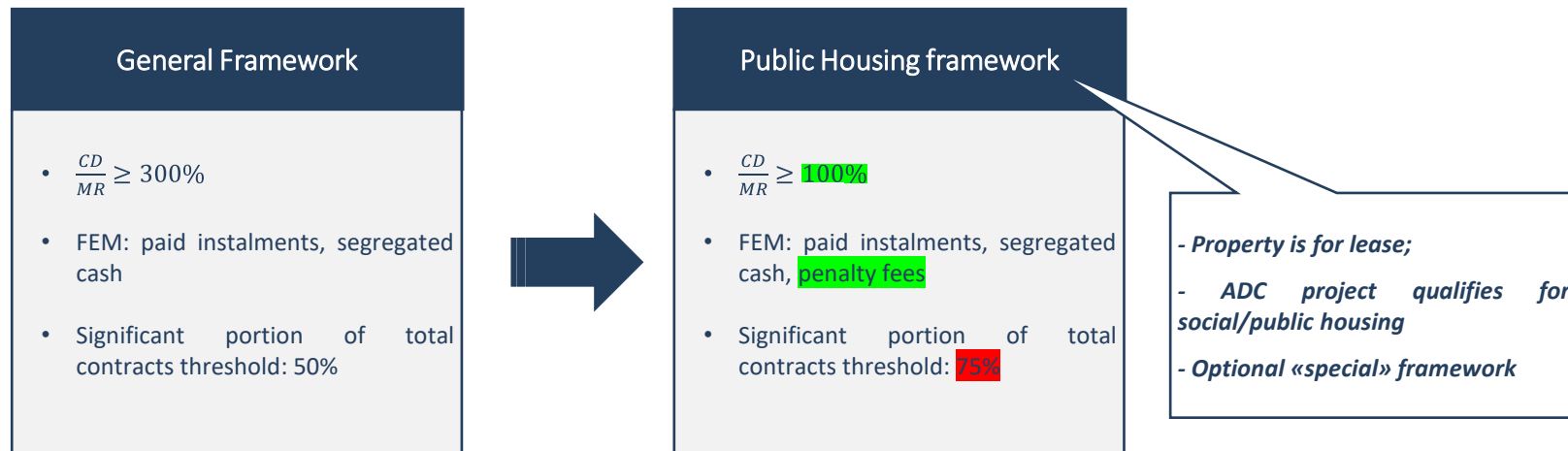
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## Public Housing Framework

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# Public Housing framework



Q21: Agreement with the adjusted criteria



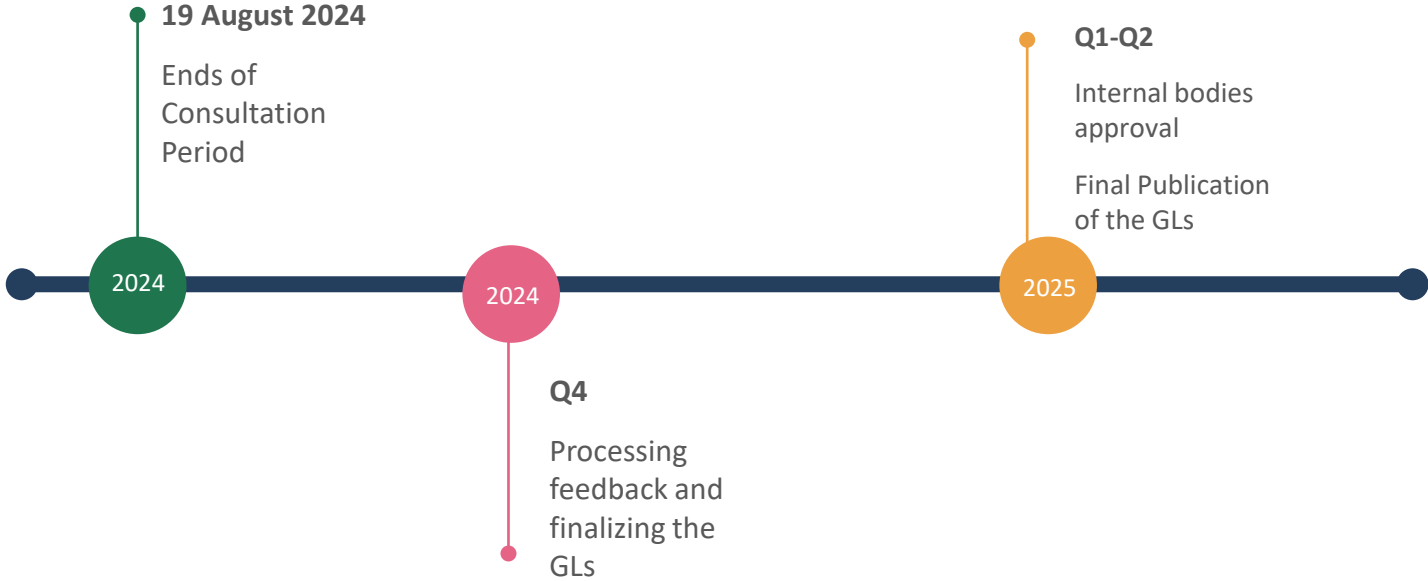
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## Next Steps

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# Next steps





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Thank you!

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Floor 24-27, Tour Europlaza  
20 Avenue André Prothin  
92400 Courbevoie, France

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Tel: +33 1 86 52 70 00  
E-mail: [info@eba.europa.eu](mailto:info@eba.europa.eu)

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<https://eba.europa.eu/>