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Ihr Zeichen, Ihre Nachricht vom Unser Zeichen, Sacharbeiter Durchwahl Datum

BSBV 115/Dr.Egger 3137 18 June 2015

**EBA – Consultation; Guidelines on limits on exposures to shadow banking entities**

The Division Bank and Insurance of the Austrian Federal Economic Chamber, as representative of the entire Austrian banking industry, appreciates the possibility to comment on the

Draft EBA Guidelines on limits on exposures to shadow banking entities which carry out banking activities outside a regulated framework under Article 395 para. 2 CRR and would like to submit the following position:

**General comments**

The proposed EBA Draft GL do not set a lower regulatory hard large exposures limit, but require banks to comply with additional requirements (stricter Pillar 2 limits) for Shadow Banking Entities. We do not agree with an approach based on stricter Pillar 2 limits and suggest instead an approach that promotes the development and/or improvement of regulatory regimes for Shadow Banking Entities (SBE). While establishing processes and IT systems for identification and control of exposures to shadow banks as suggested by the Draft GL will be a complex task for banks, the Draft GL do not elaborate on the consequences for the provision of credit to the real economy or the stability and orderly functioning of financial markets which are part of the EBA mandate according to Art. 395 para. 2 CRR.

**Q1: Do you agree with the approach the EBA has proposed for the purposes of defining shadow banking entities? In particular:**

* **Do you consider that this approach is workable in practice? If not, please explain why and present possible alternatives.**
* **Do you agree with the proposed approach to the exclusion of certain undertakings, including the approach to the treatment of funds? In particular, do you see any risks stemming from the exclusion of non-MMF UCITS given the size of the industry? If you do not agree with the proposed approach, please explain why not and present the rationale for the alternative approach(es) (e.g. on the basis of specific prudential requirements, redemption limits, maximum liquidity mismatch and leverage etc).**

We consider the definition for shadow banking entities as described in Point 6 (Definitions) of the Draft Guidelines as too imprecise which will result in inconsistency in the interpretation and not comparable results by the institutions. Furthermore the IT-implementation to identify these entities will be a complex task.

The proposed threshold for the definition of exposures to shadow banking entities with 0.25% of a bank's eligible capital is far too low, as the intended purpose of the guideline is to introduce limits for large exposures according to Art. 395 CRR. Moreover it is not defined if this threshold refers to the exposure of a client or of a group of connected clients.

As regards excluded undertakings, it is unclear how they have to be excluded - as single entity or group of connected clients (GCC)? Imagine for instance a GCC consisting of a third country and a bank owned/controlled by that third country (assuming the third country is not equivalent).

For the treatment of entities within the scope of prudential consolidation, we prefer Option 3 as described under 5. Accompanying documents point 5.1.3 (Options Considered) on page 28. With regards to entities which are not within the scope of prudential consolidation we prefer Option 2 (the intermediate approach) on page 29. As regards credit institutions of equivalent third countries, it is not clear if these countries are limited to countries listed in the COM Implementing Act dated Dec. 2014 which would be too narrow.

Under Point 6 (Definitions, page 18) point (3) (g) should be expanded. Not only sovereigns and local governments in EU Member States should be excluded from the term of shadow banking entity but every sovereign or local government without geographical restriction.

We do not support that UCITS Money market funds (MMFs) are not excluded from Shadow Banking Entities - all UCITS funds (MMF and non-MMF) should be excluded.

**Q2: Do you agree with the approach the EBA has proposed for the purposes of establishing effective processes and control mechanisms? If not, please explain why and present possible alternatives.**

We are opposed to the idea of introducing additional Pillar 2 qualitative requirements, like the ones in Title II paras 1 and 2, explicitly for shadow banking entities. The qualitative Pillar 2 requirements set by CRD IV have already been implemented in full in national law. It is not clear why these guidelines should set requirements aimed specifically at shadow banks when the same requirements already apply to all borrowers anyway and are already included in various other EBA guidelines (e.g. those on internal governance, SREP). The requirements in Title II, paras 1 and 2 would create unnecessary additional administrative work since separate frameworks, policies and reporting systems would need to be developed specifically for shadow banking entities and these would be subject to separate verification by supervisors and auditors. We do not see any corresponding benefit.

**Q3: Do you agree with the approach the EBA has proposed for the purposes of establishing appropriate oversight arrangements? If not, please explain why and present possible alternatives.**

As outlined in our comments to question two, we do oppose the idea of introducing special qualitative requirements for SBEs only that are usually part of other regulation for Pillar II. Risk management processes are reviewed by the management body on a regular basis. But this assessment covers the entire risk portfolio. In addition we would like to draw again the attention on the fact that SBEs should not be considered as a single risk category.

**Q4: Do you agree with the approaches the EBA has proposed for the purposes of establishing aggregate and individual limits? If not, please explain why and present possible alternatives.**

We do not believe it makes good sense to set special aggregate and/or individual limits on exposures to shadow banking entities under Pillar 2 since the shadow banking sector is highly heterogeneous and no risk management benefits would ensue, which should always be a prerequisite for setting a limit. In any event, individual limits are already set for every client and group of connected clients as a result of routine lending processes or banks’ strategies for managing credit risk.

**Q5: Do you think that Option 2 is preferable to Option 1 for the fallback approach? If so, why? In particular:**

* **Do you believe that Option 2 provides more incentives to gather information about exposures than Option 1?**
* **Do you believe that Option 2 can be more conservative than Option 1? If so, when?**
* **Do you see some practical issues in implementing one option rather than the other?**

We prefer a fallback approach based on option 2. SBE are a very heterogeneous group with different business models, levels of disclosure and with different risk levels within their portfolios. Based on this heterogeneity, it does not seem appropriate that, if a credit institution gathers all required information for the majority of those entities but, for a small group of SBE, cannot obtain the information required to set a meaningful limits framework, all the bank’s exposures to all SBE (regardless of the information obtained) should be perceived as an exposure to the “same client” and, as such, will be subject to a 25% aggregate limit.

Option 1 does not provide incentives to develop a robust assessment process as the non-compliance with a principal approach for just one SBE exposure will lead to an overall limit to all SBE exposures. Even if, in these situations, banks decide to run off the portfolios to the specific SBEs to which they cannot obtain the required information, this will lead to an increase of exposures to “principal approach compliant” SBE, which, on the other hand, will result in concentration risk challenges. Furthermore, option 1 could lead, on the short term, to swift systemic events resulting from the insolvency/fire sale of assets from the SBE that cannot provide the necessary information of the banking sector.

In summary, SBEs are different and will be at different stages of evolution, both features that are not controlled by banks. As such, the potential absence of information from specific SBE groups should not lead to restricted limits to other sophisticated SBE groups, as proposed under option 1.

**Q6: Taking into account, in particular, the fact that the 25% limit is consistent with the current limit in the large exposures framework, do you agree it is an adequate limit for the fallback approach? If not, why? What would the impact of such a limit be in the case of Option 1? And in the case of Option 2?**

Under fall-back Option 1, an aggregate 25% limit for all exposures to SBE would be overly conservative and spark fire sales thereby destabilising markets and affecting credit mediation. EBA should reconsider this potentially heavy cost of "incentivising" banks to use the principal approach.

We do not agree with the assumption mentioned on page 13 which states that “in the absence of sufficient information, all exposures to shadow banking entities could be connected” and so indicates that they should be understood as the same client. As such, although the information gathered could not allow the compliance with all specific rules of the principal approach under Title II, this does not mean that, based on the information collected, there is an inability to evaluate the interconnection between SBE and so, concluding that they are all connected. Moreover, this example also illustrates that the framework does not appropriately capture the risk of the exposure to the SBE thus calling for a different, simpler approach.

Please give our concerns due consideration.

Yours sincerely,

Dr. Franz Rudorfer

Managing Director

Division Bank and Insurance