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UniCredit Feedback to EBA draft guidelines on retail deposits subject to different outflows for purposes of liquidity reporting under Regulation (EU) No 575/2013 (Capital Requirements Regulation – CRR)

UniCredit is a major international financial institution with strong roots in 20 European countries, active in approximately 50 markets, with about 9.000 branches and more than 150.000 employees. UniCredit is among the top market players in Italy, Austria, Poland, CEE and Germany.

Abstract

CRR defines (Art 421 par 1) the criteria to identify stable deposits (i.e. established relationship and transactional accounts covered by insurance protection scheme) and prescribes that the residual part of retail deposits not in line with this classification shall receive a 10% run-off factor as less stable (ART. 421 par 2: "Institutions shall multiply other retail deposits not referred to in paragraph 1 by at least 10%"). Deposits already identified as stable following Basel Committee guidelines (possible run-offs are 3%, 5%, 10%) should not be subject to higher outflows rates while adopting, with reference to EU, CRR rules (level playing field principle should be assured).

In addition, it should be pointed out that assumptions underlying the approach proposed by EBA on higher outflows are not fully demonstrated by empirical evidences in our posssion. It would be helpful if EBA would publish the realized percentual outflows of impacted institutions during the past crises. In addition, their adoption may generate cumbersome costs for Banks in terms of complex IT architecture to be implemented and maintained on a monthly basis and within EoM +15 calendar days LCR reporting remittance dates.

In case EBA will confirm its intention to introduce higher outflows rates on specific deposits clusters, we deem that it should be done after a deep calibration phase to be run at least until 2018. The adoption of new requirements, should follow the release of harmonized / detailed instructions, to be defined in coherence with a "depositor-based" approach rather than the "deposit-based" one. Level playing field principle should be assured, especially if it will be required to disclose LCR to the market.

Finally, we deem relevant that banks should be allowed to adopt preferential treatments on retail deposits, in case internal econometric models on client's behaviors, validated by competent internal / external Bodies, demonstrate effective higher stability of clients.
We welcome the set-up of a working Group with EBA aimed at identifying common criteria for adoption of internal models.

Question 1 – Part 1: Do you agree with these criteria for assessing the existence of an "established relationship"?

The CP states the requirement that follows:

"A retail deposit should be considered to be part of an established relationship for purposes of liquidity reporting under a combined idiosyncratic and market-wide stress scenario when the depositor meets at least one of the following criteria:
(a) has an active contractual relationship with the institution of a minimum duration,
(b) has a borrowing relationship with the institution for mortgage loans or other long term loans, or
(c) has a minimum number of active products, other than loans, with the institution."

Harmonized definitions should be defined at EU level, in order to assure data comparability and level playing field among financial services industry players, before adherence to the minimum requirement becomes mandatory. Please refer, as an example, to the comments that follow:

- with reference to point a) the minimum duration of a relationship should be formally defined;
- with reference to point b) long term maturities should be formally defined.
- with reference to point c) we deem that in addition to a loan maturing after the LCR horizon but within the long term (not being covered by point b), the existence of an additional product is sufficient for identifying client's stability. Furthermore, we also consider that two additional products different from loans are sufficient to consider the relationship as stable. if, considering also local market peculiarities, it is objectively proven, that continuous delivery of one active product is sufficient to consider the relationship with the client as stable, Banks should be allowed to consider it within LCR calculations. With reference to the need that the products should be actively managed please refer to answer to Q3.

In addition, in light of the fact, that the regulator is explicitly mentioning the need for Banks to have available historical data on the behavior of depositors, to substantiate the classification of the depositors, we deem that the data retrieved by underlying validated econometric behavioral models (deposit based approach), may represent a better evidence of client relationship stability (intrinsically considering all possible underlying factors) rather than the effort to try to identify and manage a specific list of risk factors (depositor based approach and not deposit based approach, as proposed by EBA itself).
Reference: page 10, box "Explanatory text for consultation procedures"
Based on internal evidences deriving from validated internal models, banks should be allowed to adopt a preferential treatment.

<u>Question 1 – Part 2: In your view, what other criteria could be considered to qualify deposits as being part of an "established relationship making withdrawal highly unlikely" under a combined idiosyncratic and market-wide stress scenario?</u>

The evidence of **internal models validated by an external independent body** should represent a key element of the stability of the relationship. If the **outcomes of the model demonstrate higher stability** of Bank's clients if compared to the ones deriving from the approach proposed by CRR/EBA ITS CP, banks should be allowed to adopt a **preferential treatment** to the whole part of retail deposits identified by the internal model as stable.

In addition, it should be highlighted that, having a transactional account with the institution should qualify the client as being stable.

<u>Question 2: Do you agree with this criterion for identifying a transactional account?</u>

No, as it is not aligned with CRR 421 (1 -b) where it seems that the crediting of salaries represents a sufficient but not necessary condition (as there could be other transactions that may be considered furthermore for SME clients there may be no salaries at all), in order to consider the account as transactional, whereas the EBA CP states that a transactional account is defined as an account on which salaries and transactions are regularly credited. Some room should be left for banks to treat certain accounts as transactional if they can provide grounded evidence to prove this.

Question 3: Regarding established relationships, how would you assess that the contractual relationship with the institution and the minimum number of products are active in the sense of being actively managed?

In order to assess that the contractual relationship with the institution and the minimum number of products are active in the sense of being actively managed, a criterion based on the proportion between the interests actually paid to the deposit and the total income to the bank from the relationship with the client could be proposed, provided that a clustering rule in terms of homogeneity of the depositors and cross-selling indicators (i.e. high product penetration for each relationship) is envisaged.
Even though the approach proposed above could represent a possible proxy, **it should be pointed out that the set-up and maintenance of the underlying complex IT architecture may generate prohibitive costs for Banks** (also in light of monthly LCR calculations and T+15 remittance date). We welcome the set-up of a working Group with EBA aimed at agreeing on common definition of active management attribute. It should be still demonstrated that "active management" of a product has a direct relation in terms of stability on the relationship with customers. In fact, products are managed and used considering the effective needs of each client. Considering the complexity of the topic, we do not support the introduction of the "active management" attribute within the LCR calculation before 2018 when 100% LCR as minimum requirement is introduced (it has to be demonstrated by consistent empirical analysis).
Furthermore, it should be pointed out that each product type may be characterized by a peculiar attribute "active management", that may represent an intrinsic characteristic of the product (it may be normal that a product is not accessed with high frequency).

In addition, in part 2 at point 6 of the CP (Factors affecting the stability of retail deposit products - The value of the retail deposit, page 12), our institution does not have past evidence about the fact that clients with higher deposits have been less stable than clients with deposits covered by the DGS. For this reason we do not support the classification made in the CP about high value deposits and very high value deposits that considers these accounts riskier than others. We think that this is a clear example of "deposit-based" approach instead of a correct implementation of a "depositor-based" approach.

Question 4: What is your view concerning the threshold proposed for high and very high value deposits? Please give your reasons.

UniCredit does not have empiric evidence about different behavioral approaches among different threshold proposed: lower than EUR 100 000, between EUR 100 000 and EUR 500 000 and finally greater than EUR 500 000. In relation to "point 6 – the value of the retail deposit" (page 12), it seems that more attention is given to the value on retail deposits and not, as suggested previously, on depositors.

Question 5: Do you agree with the criterion for considering a deposit to be rate driven?

A careful assessment of possible changes in (national) frameworks of DGS should also be taken into consideration, in order to guarantee consistency with regards to criteria of exclusion related to deposits at interest rate conditions significantly exceeding the average rate for similar retail products offered by peers; this topic is currently under discussion at national level.
There are concepts reported in the CP that need further clarifications. First of all, significant dependence of deposits stability on price and persistence of higher outflow rates for products related to market indices need further deep assessments at EU level before being effectively adopted. In addition to this , it should be pointed out that comparison with peers may not be always be possible (especially for deposits with negotiated rates).
Moreover, notice that, taking into account the fact that right now current interest rates are low, a small rise in interest rates may imply the reclassification of some products as rate-driven under the new EBA regulatory approach proposed.

Question 6: Do you agree with the criteria to identify this risk factor?

No. Not necessarily there is a link between stability and the relative residence of depositors. The rationale underlying the need to open a deposit abroad may derive from an effect need and/or effective advantage in terms of remuneration.
Furthermore, we have doubts also about point 9 (High-Risk distribution channel, including Internet-only access and brokered deposits", page 14). First of all, customers that have an internet access of the banking account are not only those ones that have opened a deposit on line; in fact, also those deposit retailers that initially set up a new contract directly at branches, may additionally require to open an on line access for the same banking account. Moreover, about the possibility to react remotely and instantaneously to market movements, it's true that through internet the risk is higher in terms of time, but however also for customers that have no access to their accounts on line, they may close deposits or transfer their amount of cash in a short time horizon (hours).The decision to transfer the available cash is independent from the fact that the client has an on line access to its account. For these reasons, we may say that there might not be a great difference if a deposit has also the access on internet, taking into account that the LCR is computed on a 30 days horizon. If this risk factor will be maintained, banks will have less incentives to use and promote this type of deposit, with the potential consequence that they may stop to offer these on line accounts.

It should be pointed out that the set-up and maintenance of all risk factors proposed by the CP may generate cumbersome costs for Banks in terms of IT architecture complexity (also in light of monthly LCR calculations and T+15 remittance date).Some of them, like the need to perform peer analysis on a monthly basis on interest-rate driven contracts seem not to be manageable, also in light of the T+15 LCR remittance date. As already mentioned above adoption of externally validated behavioral model seem to be more realistic and cost-effective.

Question 7: Do you agree with the above analysis of the cost and benefit impact of the proposals?

We support EBA intention to introduce a new retail deposit category with a lower outflow based on specific characteristics of such deposits that could justify a lower outflow rate and taking into account international developments.

With reference to the options outlined in the paragraph "*Whether or not to prescribe a methodology to estimate the level of the higher outflow rates"* we do not support option B.2, as " concrete levels of rates that should be used for deposits identified as having higher outflow rates" should be better provided.
In addition, as we strongly believe that what should be estimated is the relationship of the client with the bank as a whole, without assessing each product type underlying its relationship with the bank. This would mean that higher outflows rates should not be applied to clients previously identified as stable, but just to the ones not meeting the requirements outlined at article 421 (1) and limited to the products having the risk factors proposed by the EBA approach.

In our opinion, there's no point to introduce a common liquidity indicator that whose disclosure could be officially required, unless processes underlying its calculation are not fully harmonized and certified by and independent body. Data comparability and level playing field should represent a pillar of the ITS implementing the new liquidity requirements.
As already mentioned, data retrieved from internal models (to be validated by competent authorities) should represent a key component of the effective run-off rate to be applied to deposits, thus banks should have room to provide evidence on the stability of their deposits.

Question 8: Please provide any evidence or data that would further inform the analysis of the likely cost-benefit impact of the proposals.

We strongly believe that on such topic a calibration phase should start now until 100% minimum requirement is introduced, in order to assure level playing field and unintended consequences on real economy.

It would be interesting to start the calibration activity comparing outcomes of existing internal models, in order to assess whether they could represent the most reliable source for identifying the portion of clients to be considered as stable.

Notes

- Page 10: In the box "Explanatory text for consultation purposes"
  Final criteria are not clear (points 4-5-6).In particular, regarding the part on article 421(1), the document is probably missing points number 1-2-3 in describing the definitions *"established relationship making withdrawal highly unlikely"* and *"transactional account, including accounts to which salaries are regularly credit"*.

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Please find below the list of the key people involved in this work, whose contribution made possible to coordinate and provide UniCredit answers to this Consultation. some other experts have been involved alongside the UniCredit Group, but are not listed below.

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