

**Assilea' Position Paper on EBA's Consultation Paper:
"Draft Regulatory Technical Standards on threshold of credit obligation past
due under Article 178 of Regulation (EU) 575/2013" (31 October 2014)**

Assilea, the Italian Leasing Association, represents the Italian leasing industry. Our members are leasing companies classed into generalist banks, specialist banks, non-banking financial intermediaries, brokers and dealers, long-term rental companies, outsourcers specialised in the leasing market.

The Association's key task is to carry out institutional activities with a view to providing information and assistance to its Members and contributing towards the solution of leasing-related issues at different levels, in different domestic and international venues.

*Assilea is member of **Leaseurope** (the European Leasing Federation) and of **ABI** (the Italian Banking Association) and actively participated to the drafting of the Position Papers released by the above mentioned Federation (joint Eurofinas and Leaseurope Position Paper) and Association (ABI's Position Paper).*

We thank you for the opportunity offered with this consultation. In this paper we outline the major problems and concerns of our industry on the implementation of the EBA's Regulatory Technical Standards on materiality threshold, following the track of the list of "questions for consultation" on page 32 of the EBA's Consultative Paper.

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Q1. Do you agree with the approach proposed in the draft RTS (option 1) that default should be recognized as soon as one of the components of the threshold (absolute or relative limit) is breached? Or would you rather support the alternative option, i.e. recognition of default after both thresholds are breached (option 2)?

Considering the current threshold adopted in Italy and in other European countries, we don't agree with the approach proposed in the draft RTS (option 1) that default should be recognized as soon as one of the components of the threshold (absolute or relative limit) is breached.

Option 2 would be more suitable and, if properly finalised, wouldn't lead to significant delays in default identification of large exposure. On the contrary, according to our experience, Option 1 would lead to a high number of "technical default" not only for large exposures, but also for medium and retail ones.

The choice at European level of the most prudential approach (Option 1) would not necessarily be the best solution. This, particularly, in the case of the threshold definition, if we consider its consequences in terms of number and amount of the exposures that would be classified as past-due ones.

The definition of the European threshold RTS should have the purpose to lead to a uniform level-playing field in the UE, but, at the same time, should also have – in our opinion – the purpose to limit the impacts that changes in the threshold structure would have on the banking and financing systems of the different European countries.

According to what published in tab. 1 of the EBA's document, for only three countries the breach of at least one of the threshold limits (absolute or relative) triggers default. In other words: only three, out of the eight countries adopting a combination of absolute and relative threshold, apply a "Option 1" rule. Therefore, we suppose that in many countries the introduction of these mechanism would cause an increase of "technical defaults" and would not correctly reflect the effective risk of the local portfolios.

As we will show in the reply to Question 5, the impact of the proposed new rules to the Italian leasing portfolio classification, apparently, would be very high. Considering the fact that the Italian rules¹ for the calculation of the relative threshold are more prudential than those proposed in the EBA's Paper, we will also show – in the following pages - that lower impacts on the Italian leasing retail segment can be obtained introducing specific rules in the calculation of the relative threshold.

In the following parts of this document we will explain which are the elements that would impact more the current portfolio classification and propose some alternative solutions that would remain in line with the main purposes of the EBA's RTS standards.

¹ According to the Bank of Italy's supervision rule, only a "relative" threshold (5% of the client's total exposure) can be used in the, largely more frequent, "debtor approach" for the definition of past due exposures; nevertheless – differently from what proposed in the EBA's Paper - in the Italian formula for the calculation of the threshold the numerator includes all the overdue amount even when only some of the overdue amount exceed 90 days.

Q2. Do you agree with the proposed maximum levels of the thresholds?

In the Italian supervision framework, there isn't any absolute threshold and the current relative threshold is higher (5%) than the one proposed in the EBA's Position Paper.

On the basis of the following consideration, we would like to ask you to:

1. revise the proposed maximum limit of 2% for the relative threshold;
2. introduce clear and uniform rules for the relative threshold calculation;
3. consider the possibility to introduce higher thresholds for the exposures to the public sector and real estate leasing;
4. introduce a specific threshold for the asset-finance sector, to be equal to the amount of the monthly rental/leasing payment (so that at the third whole instalment unpaid, the exposure would be classified as past due).

1. Maximum levels for the relative threshold

As a result of our first simulations on the Italian leasing portfolio, we noticed that the impact of a change in the maximum level of the absolute threshold would be lower than the impact of a change in the maximum level of the relative threshold. Therefore, we would like to ask you to consider, as a priority, to revise the proposed limit of 2% of the relative threshold.

At a national level, local Supervisory Authorities stated the most suitable threshold framework considering the main characteristics of their national market. In addition, the countries where no absolute nor relative threshold exist are probably those where other case-by-case criteria are used. Therefore, in order to fix a threshold that would minimise the average impacts on the different countries, the relative maximum threshold should be chosen in the range of national relative thresholds 2%-5%. Otherwise, the more prudential threshold proposed in the EBA's Paper (2%) would probably maximise "technical defaults" in a major number of countries. For the above mentioned reasons, in our opinion, there could be reached a general consensus on a European 4% relative maximum threshold.

2. Clear and uniform rules for the relative threshold calculation

It is also very important to introduce clear and uniform rules for the relative thresholds calculation. As we will see, the impact on an average Italian retail leasing portfolio will result to be reduced if, in the Option 2 approach, there is the possibility to allow (as mentioned in the EBA's Paper) that only the sum of all the amounts past due more than 90 days should be considered for the calculation of the threshold and not all the overdue amount when only some of the overdue amount exceed 90 days.

The impact of Option 2 approach to an average Italian retail leasing portfolio would be near to "zero" (even with a 2% relative threshold) if another rule would be introduced in the EBA's RTS, in addition to the above proposed one: the possibility to start the counter of the days past due only after the materiality threshold is exceeded.

3. Higher thresholds for the exposures to the public sector and real estate leasing

As mentioned above, the impact of a change in the absolute threshold is not proved to be as high as the impact of the relative thresholds. Nevertheless, the eventual segmentation of the absolute threshold should be coherent with the CRR segmentation of the exposure classes. This means that in addition to the proposed two absolute thresholds provided for retail (200 euro) and other exposure segment (500 euro), at least other two higher absolute thresholds should be introduced for:

- exposures (leasing and other forms of financing) to public sector entities;
- exposures secured by mortgages on immovable property (including real estate leasing).

In our opinion, the low risk profile of exposures to public sector entities and the high collateral value as a percentage of real estate leasing exposures (and more in general of exposure secured by mortgages on immovable property) would require the introduction of specific absolute thresholds for these classes of exposures.

4. A specific threshold for the Asset Finance industry

In the asset finance sector, rental payment (instalment) is a percentage of the total value of the contract. In our opinion, it could be used as a specific threshold for this sector. This solution – proposed also in the Position Paper of the European Federations (Eurofinas and Leaseurope) and in the Position Paper of the Italian Banking Association (ABI) would have the advantage to be linked to the financial contract size and to be suitable for all the different market segments of the asset finance sector in the different countries.

Q3. How much time is necessary to implement the threshold set by the competent authority according to this proposed draft RTS? Given current practices, what is the scope of work required to achieve compliance?

According to our estimates, at least three years are necessary to implement the new threshold. On the one hand, those banks and financial intermediaries who adopt FIRB/IRB approach to calculate capital requirement for credit risk, have to recreate the PD and LGD time series in order to update their FIRB and IRB models. On the other hand, those banks and financial intermediaries who adopt the standardised approach, normally are smaller entities and they need to have enough time to update their entire process of credit risk managing and monitoring, investing the necessary resources. All the above mentioned changes would strongly impact the organisation and IT structure of all banks and financial intermediaries.

Q4. Do you agree with the assessment of costs and benefits of these proposed draft RTS?

Q5. What is the expected impact of these proposed draft RTS?

As mentioned in Q1 reply, we understand the benefits of a unique European threshold, nevertheless – in our opinion - the costs and the effects of this threshold seems to be underestimated.

On the basis of the data of some major Italian leasing companies, the implementation of Option 1 with the proposed maximum threshold levels would lead – in the retail leasing portfolio - to a +46.9% increase in past due positions with a + 224.5% on their value. With the Option 2 approach the impact would result to be +24.4% increase in past due positions with a +175.3% on their value.

The impact will be reduced (+19.6% increase in past due positions with a +158.2% on their value) if, in the Option 2 approach, it is confirmed the possibility to allow (as mentioned in the EBA's Paper) that only the sum of all the amounts past due more than 90 days should be considered for the calculation of the threshold and not all the overdue amount when only some of the overdue amount exceed 90 days.

Even with a 2% relative threshold and Option 1, the impact to an average Italian retail leasing portfolio would be sensibly reduced if it was introduced the additional rule, according to which, it is possible to start the counter of the days past due only after the materiality threshold is exceeded.