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The Commission´s proposal for a directive on credit servicers, credit purchasers and the recovery of collateral and the proposal for a prudential backstop (CRR)

The Swedish Bankers´ Association appreciates the opportunity to comment on the Commission´s proposal for a new directive on credit servicers, credit purchasers and the recovery of collateral. However, we consider this proposal must be seen in conjunction with the proposal on amending regulation (EU) no 575/2013 (CRR) about minimum loss coverage for non-performing exposures and the proposal for a directive on preventive restructuring framework, second chance and measures to increase the efficiency of restructuring, insolvency and discharge procedure (restructuring directive).

Short summary

The proposed directive, in current wordings, to promote the development of secondary markets for non-performing loans (NPL) is likely to affect the Nordic market negatively. Statistics from the EU shows that the countries with low amount of NPL are the Nordic countries. Generally, banks in the Nordic region have long been working with an integrated credit assessment process where the process begins with a thorough credit assessment of the customer, in Sweden with access to credit information about costumers from business and credit reference agencies (i.e. with a high amount of transparency which is lacking in other EU countries). This credit process is built on the assumption that the creditor/bank will be fully responsible for the credit, regardless of whether payment issues arise or not. This responsibility contributes to a judicious behaviour in credit assessments which in turn results in reduced risk of building up NPL that later may entail increased risks in financial markets and in socioeconomics.

Facilitating trade with NPL may not be a long-term solution as it does not mean that these loans will disappear but only that they are moved to different creditors. The debtors will remain, regardless of the change, in current socioeconomics. To achieve long-term financial stability, it is important not to create rules, or formulas in the rules, that counteract a sound and responsible behaviour and proper long-term credit incentives.

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Existing and recently introduces regulations (CRR, CRD IV, SREP, Pillar 2 and IFRS 9 etc.) already contain sufficient tools to limit the volume of NPL, generally as for individual banks or geographical areas. The proposal to introduce an add-on layer of capital requirements will create complexity and unnecessary costs to Nordic banks, which, according to EU statistics, already have processes and methods for keeping NPL at a low level. Most importantly, an add-on layer will erase the terms and possibilities for the existing credit servicers and credit purchasers at the secondary market, where credit institutions are major players today.

In addition, the combination of the proposed package may force banks to sell NPL in an early stage in the insolvency process. The experience in Sweden is that the benefit for all involved parties is achieved if the insolvency situation is managed over time in a controlled manner, without banks being forced to sell the claim to another actor. The Nordic model, which so far has been successful in Sweden and the rest of the Nordic countries, may with the proposed package, change, with risk of negative consequences for both financial markets, creditors and socioeconomics.

General comments

Initially we want to point out that the suggested package to address high stocks of NPL fits less well for markets, such as the Swedish market, that already have well-functioning and cost-effective insolvency regime and where credit institutions also have small or moderate stocks of NPL. New requirements can, contrary to the purpose of the proposals, lead to adverse effects not only for credit institutions but also for creditors.

First a brief overview of the Swedish insolvency regime for summary proceedings and enforcement is presented to show the importance that now EU requirements are not allowed to adversely affect existing insolvency regimes in Member States. Summary Proceedings is a simplified, cost effective and accelerated procedure for order of payment, which is handled by an authority (Kronofogdemyndigheten). The purpose of Summary Proceedings is to deliver a verdict that is directly enforceable.

The procedure is for private individuals and enterprises alike and both can stand as either applicant or respondent. Normally claims are uncontested money orders but they can just as well be non-money orders. Summary truly means summary in Sweden as we do not question the validity of a claim. The applicant need not supply any evidence nor is there any examination of the case. Neither the applicant nor the respondent need representation during the process, all parties may represent themselves. Forms and written instructions are designed for this purpose, they are to be easily understood by non-professionals. The process is not obligatory and an applicant may take his claim directly to the District Court instead.

On average the process takes just short of 2 months from application to a decision. A decision is rendered in 80% of incoming applications. A decision such as this is directly enforceable by the recoveries department. It is noteworthy that all decisions from the Summary Proceedings are appealable, meaning a final decision may be contested by either party.

The Enforcement Authority is responsible for the enforcement of both public and private claims. Private matters are based on titles of execution, judgments of general and administrative courts. Other titles may emanate from the summary procedure of the Enforcement Authority, such as repossessions and evictions, normally based on summary decisions. Private enforcement matters are mainly based on court judgments, but also some other titles of execution. Examples of enforceable titles of execution are: judgments of the general courts, the District Court the Court of Appeal the Supreme Court the Administrative Court the Administrative Court of Appeal and the Administrative Supreme Court. In addition, some private documents can be enforced, such as contracts for child and spousal support.

The main legal source for the enforcement of claims is the Enforcement Code, effective from 1 January 1982. The Enforcement Code includes 18 chapters. In addition, an Enforcement statute exists, including 19 chapters, which contains detailed provisions for procedures, as a supplement to the Enforcement Code.

Restructuring directive and CRR

The proposals together constitute measures to strengthen the financial system and cross-border activities by among others to address high stocks of non-performing loans (NPLs). To achieve this purpose, it is important to analyse the overall and combining effects of the proposals so that the components do not counteract each other.

Finding ways of establishing an efficient secondary market and shortening the judicial procedures are far from being the most important factors in solving the challenge with too high NPL ratios for some of the financial players. The NPL topic and finding adequate measures for addressing such situations must be put in a broader context and be just one of several pieces in a jig-saw puzzle.

It is as important to have a prudent credit risk and payment ability assessment, including risk mitigation actions such as collateral and covenants, relevant monitoring and follow-up on disbursed credits, proactive identification of increased risk through e.g. early warning systems and adequate tools for reinstalling an acceptable risk level, such as watch list processes etc. These measures, being part of the overall credit process, serve as positive factors in the avoidance of actual losses. And the opposite, if you are acting insufficient in any of these parts the risk of increased inflow of NPLs is materially higher and by that also the risk of actual

losses. Having improved and align rules regarding NPL purchasers and recovery of collateral will not heal deficiencies in the other parts of the credit process. Therefore, it ought to be a more general reflection on how to enhance the prudent banking perspective in all parts of the credit process.

The Nordic model, that can in a simplified way be described as having collaboration with the defaulted borrowers still showing a willingness to pay trying to find voluntary solutions to overcome the distressed economic situation, has proven itself to be effective and these banks are today in general showing strong balance sheets and low ratios of NPL. By establishing the proposed rules, which inter alia strongly promote selling off NPLs, you run the risk of undermining this successful model and decrease the competition in comparison to the players choosing to sell NPLs at an early stage. This can also be violating the principle of free business competition.

The introduction of the IFRS 9 is supposed to be addressing the issue with increased risk and NPLs with the objective to avoid inadequate or delayed loss allowances. The IFRS 9 came into force on the 1st January 2018 and the effect has not yet been evaluated. The proposal to introduce a back stop in the CRR will intervene with the newly introduced IFRS 9 rules and means de facto a rejection of the outcome of IFRS 9 before it has even been evaluated. Added, the proposal is not really a back-stop rule, rather a way to introduce a gradual structure of stage 3 provisioning that will increase the complexity without proven added value.

It also seems as if the current proposal overlooks the fact that CRR regulated institutions operate as investors at the secondary market. Potential buyers who must comply with the CRR will no longer have incentives to purchase the portfolios if they must deduct the value of the NPL portfolios from their CET1 capital. Thus, there may be an inequality between supply and demand at the secondary market.

Further, when institutions sell their NPLs to the secondary market, customer protection responsibility will be moved to the secondary market where the recovery process is likely to be accelerated, which will entail social costs for the market. Today's process of debt relief, etc. have worked well. A change will mean that the current risk culture of companies will change fundamentally.

Overall, we see a need for a comprehensive analysis of the proposals that will affect the secondary market for NPLs.

A directive on credit servicers, credit purchasers and the recovery of collateral

Article 3 Definitions
(7) Credit purchaser and (8) credit servicer
The Swedish Bankers´ Association believes it would be more in line with the objective of the proposal to exclude all companies that are part of a consolidated situation in the definitions. If companies within a consolidated situation must comply with the proposal there are some challenges.

As an example, article 15.2 states that a Member States shall ensure that a credit purchaser is not subject to any additional requirements for the purchase of credit agreements other than as provided for by the national measures transposing the directive. If the requirement means that companies in a consolidated situation working with credit purchasing, shall be exempt from all banking regulations (e.g. CRR and CRD) the definitions must be re-written.

We propose the definitions to be amended as follows.

(7) 'credit purchaser' means any natural or legal person other than a credit institution, a subsidiary of a credit institution **or another company that is fully consolidated in the consolidated situation of the credit institution**, which purchases a credit agreement in the course of his trade, business or profession.

(8) 'credit servicer' means any natural or legal person, other than a credit institution, a subsidiary of a credit institution **or another company that is fully consolidated in the consolidated situation of the credit institution**, which carries out one or more of the following activities on behalf of a creditor.

Article 5 Requirements for granting an authorisation

To maintain the consumer protection and to avoid a negative acceleration of the recovery process at the secondary market, there may be reason to clarify what duties an authorisation comprises regarding consumer protection.

In the context of an authorization procedure, certain knowledge and skill requirements should also be introduced. Undoubtedly, it is a matter of credits that were surrounded by high demands on knowledge and competence of the creditor regarding the granting of the credits.

Article 9 Contractual relationship between a credit servicer and a creditor

The archiving requirements in subparagraph 3 are very far-reaching. It is difficult to see the purpose that all correspondence is to be saved for at least ten years. The ten-year filing period should be correlated to the duration of the agreement plus a certain amount of time thereafter.

Article 13 (and article 18) Right to information regarding the credit agreement

Even in this regard it is difficult to understand the purpose behind the requirement to inform the competent authority about the identity and address of the borrower and of the credit purchaser and its representative designated in accordance with article 17. Is seems sufficient that information is provided at the aggregated level. The requirement must be set in proportion to the usefulness of the competent authority in obtaining detailed information and the administrative burden imposed on the credit institutions.

Article 23 Condition for the voluntary use of accelerated extrajudicial collateral enforcement

It should be clarified how an agreement under this directive should relate to the restructuring directive, e.g. article 4 in the restructuring directive which stipulates that, where there is likelihood of insolvency, debtor in financial difficulty have access to an effective preventive restructuring framework that enables them to restructure their debts or business, restore their viability and avoid insolvency. Further, the preventive restructuring frameworks shall be available on the application by debtors or by creditors with the agreement of debtors. Since there is no definition of "likelihood of insolvency" the two directives may contradict each other unless the link between the directives is clarified.

Article 24 Enforcement

Both the creditor and the business borrower should be entitled to challenge the valuation before a court (subsection (e).

Article 30 Settlement of the outstanding amount

Full discharge of the debtor, "settlement of all liabilities under that agreement", when the amount from the use of the accelerated extrajudicial collateral enforcement is an amount lower than the sum of outstanding of the secured credit agreement, risk causing a less appropriate situation where creditors act irresponsibly for speculative purposes. Full discharge of the debtor may also cause the security to lose in efficiency for the creditor with instability as a fallout. The credit may no longer considered to be a secured credit.

Article 33 Data collection

We can understand that there are reasons to evaluate how the accelerated extrajudicial collateral enforcement work and for that reason collect data. However, it

should be noted that processes under this proposal constitute only a subset of the cases being handled within the framework of summary proceedings.

SWEDISH BANKERS' ASSOCIATION

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