EUROPEAN CENTRAL BANK
BANKING SUPERVISION

Danièle NOUY
Chair of the Supervisory Board

Mr Brian Hayes
Member of the European Parliament
European Parliament
60, rue Wiertz
B-1047 Brussels

Frankfurt am Main, 21 March 2018

Re: Your letter (QZ012)

Honourable Member of the European Parliament, dear Mr Hayes,

Thank you for your letter on non-performing loans (NPLs) in Irish banks, which was passed on to me by Mr Roberto Gualtieri, Chairman of the Committee on Economic and Monetary Affairs, accompanied by a cover letter dated 6 March 2018.

As established in the Interinstitutional Agreement between the European Parliament and the European Central Bank, any reporting obligations vis-à-vis the European Parliament are subject to the relevant professional secrecy requirements, as outlined in the Capital Requirements Directive (CRD) IV[1]. While I cannot comment on individual institutions and their actions, let me assure you that we engage in a continuous dialogue with the banks under our supervision. I will also provide you with some relevant considerations in response to your question.

There is broad consensus that high levels of NPLs ultimately have a negative impact on bank lending to the economy[2] as a result of the balance sheet, profitability, and capital constraints faced by banks with high levels of NPLs. It is therefore important that these banks address the NPL issue in a timely manner to facilitate lending activities and regain investors' trust.

To address this matter, the ECB published its Guidance to banks on non-performing loans[3] (the Guidance) in March 2017, setting out the manner in which it expects banks to manage their NPLs. The objective of the Guidance is to establish a consistent, best-practice approach to managing NPLs in individual banks across the euro area. The Guidance should help banks to significantly and continuously reduce high levels of NPLs, thereby benefitting the individual banks, the banking sector and the economy as a whole.

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1 Directive 2013/36/EU of the European Parliament and of the Council

2 See, for example, the International Monetary Fund staff discussion note "A Strategy for Resolving Europe's Problem Loans".

3 https://www.bankingsupervision.europa.eu/ecb/pub/pdf/guidance_on_npl.en.pdf

Following the completion and publication of the Guidance in March 2017, the ECB asked significant institutions with high NPL ratios to submit strategies to address their NPL issues and define their portfolio-level reduction targets over the medium term. The Guidance states that each bank with elevated levels of NPLs is expected to develop portfolio-level reduction targets with a view to reducing the level of non-performing exposures on its balance sheet in a timely manner.

Chapter 2 of the Guidance outlines best practices for the formulation of NPL reduction strategies and lists the possible tools for implementing these strategies, including forbearance, active portfolio reductions, change of exposure type and legal options.

The Guidance highlights that banks should ensure that their NPL strategies include “not just a single strategic option but rather combinations of strategies/options to best achieve their objectives over the short, medium and long term”. The optimum combination of such tools depends on the characteristics of each credit institution’s portfolio as well as the market and legal environment in which it operates.

The Joint Supervisory Teams engage with banks and monitor them on an ongoing basis, including in the area of their NPL reduction strategies. The relevant team is therefore aware of the components of a specific bank’s strategy. The ECB assesses the credibility of each of the strategic options in detail and requests that banks provide additional details or further develop their arguments in favour of certain strategic options.

It is important to note that, as stated in the Guidance, the combination of tools or strategy reduction drivers for a given bank is the responsibility of, and chosen at the discretion of, its management.

The ECB has not expressed a preference for certain NPL reduction tools over others. In addition, while the ECB expects banks to implement ambitious yet credible strategies in order to solve their NPL issues, the ECB has not imposed specific reduction targets.

The SSM Regulation[4] tasks the ECB with supervising credit institutions from a prudential perspective. This activity is without prejudice to the responsibilities and related powers of the competent authorities of the participating Member States to carry out supervisory tasks not conferred on the ECB by the SSM Regulation.[5] This means that supervisory tasks not conferred on the ECB – including consumer protection – remain with the national authorities.[6]

The ECB assesses compliance with the relevant microprudential requirements when sales of NPLs take place. The interaction between the buyers of non-performing or performing loans and the relevant borrowers, on the other hand, is a consumer protection issue that falls outside the ECB’s remit.

Yours sincerely,

Danièle Nouy

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4 Council Regulation (EU) No 1024/2013 of October 2013

5 Article 1 of the SSM Regulation.

6 Recital 28 of the SSM Regulation.