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**COMMISSION STAFF WORKING DOCUMENT**  
*Accompanying the document*

**COMMUNICATION FROM THE COMMISSION TO THE EUROPEAN  
PARLIAMENT, THE COUNCIL AND THE EUROPEAN CENTRAL BANK**

**First Progress Report on the Reduction of Non-Performing Loans in Europe**

{COM(2018) 37 final}

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## 1. SUMMARY

The financial crisis and ensuing recessions left a number of European banks with high levels of non-performing loans (NPLs). Elevated levels of NPLs may affect financial stability as they weigh on the profitability and viability of the affected institutions and have an impact, via reduced bank lending, on economic growth. They require higher provisioning by banks and increased resources to manage them. As the subgroup on NPLs of the Financial Services Committee concluded in its report this risks tying up banks' resources and holds back credit supply to businesses, particularly to small and medium-sized enterprises (SMEs) as they rely on bank lending to a much greater extent than larger companies.<sup>1</sup>

Considerable progress has been made in reducing the high levels of NPLs in parts of the banking sector, in particular in recent years. The Commission has consistently emphasised this issue in relation to the countries concerned in the context of the European Semester. However, significant stocks of NPLs are still present in many banking sectors. In its Conclusions on NPLs and building on the work initiated by the Commission, the Council therefore adopted a comprehensive "Action Plan To Tackle Non-Performing Loans in Europe" on 11 July 2017.<sup>2</sup> This Plan calls upon various actors to take appropriate measures to further address the challenges of high NPLs in the Union, recognising the balance between necessary actions by banks, Member States and the EU. It invites the Commission and other institutions to take steps on several fronts to tackle both the legacy stock of NPLs and the risk of build-up in the future. In order to achieve this, the Action Plan identifies four main areas where further action is needed to tackle NPLs: (i) supervision, (ii) reform of restructuring, insolvency and debt recovery frameworks, (iii) development of secondary markets for distressed assets, and (iv) fostering restructuring of the banking system.

The Council agreed in its Conclusions to revert to this issue regularly and initially after six months, in order to take stock of the evolution of NPLs in the Union, the restructuring of the banking sector in this context and the development of secondary markets for NPL transactions, to assess the progress made on the basis of a stock-take from the Commission. This note is the Commission services' first such factual stock-take; it comprises contributions from other European stakeholders which were also invited by the Council, along with the Commission, to take action to support and accelerate the resolution of NPLs in the Union.

Along with an overview of the progress made in implementing the Action Plan, this document also highlights recent developments of NPLs in the Union, both at Union level and within individual Member States. Overall, the positive trend, with decreasing NPL ratios and increasing coverage ratios, which has taken hold over the past years, has continued in the second half of 2017. The total volume of NPLs continues its downward trend and NPL ratios and coverage ratios continue to improve. Notwithstanding this encouraging progress, which is partly due to a stronger macroeconomic environment, there are remaining risks to financial stability and to economic growth, stemming from the still elevated level of NPLs. Member States are also continuing their efforts to reduce NPLs following the adoption of the Action Plan. In this first factual stock-take, preference is given

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<sup>1</sup> Report of the FSC Subgroup on Non-Performing Loans.

See <http://data.consilium.europa.eu/doc/document/ST-9854-2017-INIT/en/pdf>.

<sup>2</sup> Council conclusions on Action plan to tackle non-performing loans in Europe.

See <https://www.consilium.europa.eu/en/press/press-releases/2017/07/11-conclusions-non-performing-loans/>.

to a more detailed description of trends in a few countries rather than a wider, less granular, coverage. This document hence gives details on the evolution of NPLs for a non-exhaustive selection of Member States.

## **2. EVOLUTION OF NPLS IN EUROPE**

### **2.1. EU developments**

The total volume of NPLs has continued its steady decline. However, despite the ongoing downward trend, the total volume remains at an elevated level (EUR 950 billion).<sup>3</sup>

Structural impediments continue to hamper banks' efforts to reduce their NPL stocks. Among other elements, activity on secondary markets for NPLs is not yet sufficient to substantially contribute to NPL reduction efforts, notwithstanding the increasing volume of NPL-related transactions. For the purposes of this note, the term “NPL” refers to the non-performing exposures being over 90 days past due or individually impaired.

The quality of banks' loans portfolios continued to improve. The latest figures confirm the downward trend of the NPL ratio, which decreased further to 4.6% (Q2 2017), down by roughly 1 percentage point year-on-year. As a result, the ratio reached its lowest level since Q4 2014. This reduction was mainly the result of one-off events that impacted all bank-size classes, in particular smaller banks.

The provisioning ratio<sup>4</sup> has also risen, amounting to 50.8% (Q2 2017).

In nearly all Member States, NPL ratios have been falling in recent years. This has been the result of stabilising economies in concert with various pro-active measures, including sales of NPL portfolios. Nevertheless, the slow progress in some Member States, as well as the widespread dispersion among Member States remains a concern, with NPL ratios ranging from 0.7% to 46.9%.

### **2.2. Developments in selected Member States**

The stock-take by Member State is not exhaustive. In this first factual stock-take, preference is given to a more detailed description of a few Member States rather than a wider, less granular, coverage. The selection is based on the Member States' NPL ratios, the occurrence of important NPL-related evolutions and, especially, positive developments that might serve as an example to other Member States.<sup>5</sup>

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<sup>3</sup> Source: ECB data.

<sup>4</sup> Source: ECB data. Due to the unavailability of provisioning data for loans, the provisioning ratio for the EU was calculated by considering impairments and NPLs for all debt instruments, including both loans and debt securities.

<sup>5</sup> In ensuing stock-takes, the selection might be widened and other Member States covered more in-depth.

**Table: Non-performing loans and provisions by Member State <sup>6</sup>**

	<b>Gross NPLs and advances</b> (% of total gross loans and advances)		<b>Private sector NPLs</b> (% of private-sector loans)		<b>Total loss provisions (loans)</b> (% of total doubtful and non-performing loans)	
	2017Q2	2016Q2	2017Q2	2016Q2	2017Q2	2016Q2
Belgium	2.8	3.5	4.0	4.5	50.1	48.6
Bulgaria	12.1	14.0	19.2	22.4	54.8**	53.2**
Czech Republic	2.9	4.6	5.3	6.7	53.1	45.4
Denmark	2.9	3.6	3.2	4.0	38.4	39.0
Germany	2.3	2.8	4.3	5.0	43.6**	42.4**
Estonia	2.0	2.1	2.5	2.7	44.6	50.2
Ireland	11.6	14.6	15.8	18.9	37.6	42.2
Greece	46.9	47.2	50.6	50.1	49.2	49.8
Spain	5.3	5.9	7.1	7.7	59.9**	59.8**
France	3.4	3.9	4.6	4.9	59.7	60.2
Croatia	11.7	11.6	16.5	16.9	68.8	71.8
Italy	12.2	16.2	15.9	20.0	52.9	49.5
Cyprus	33.4	37.6	52.7	56.2	47.1	38.8
Latvia	5.9	5.5	9.3	8.9	43.8	53.6
Lithuania	3.7	5.0	4.9	6.5	36.3	37.5
Luxembourg	0.7	0.9	1.8	2.3	51.6	39.2
Hungary	10.4	15.0	15.3	23.0	66.4**	63.8**
Malta	3.7	4.6	6.7	7.4	41.8	44.3
Netherlands	2.3	2.6	3.0	3.1	38.3	41.8
Austria	4.1	6.0	5.7	7.5	62.6	59.1
Poland	6.6	6.7	7.2	7.3	58.0	60.5
Portugal	15.5	17.6	15.5*	17.6*	49.4	47.6
Romania	8.5	11.3	11.0	15.3	69.4	62.3
Slovenia	11.4	16.3	14.7	21.2	70.4	70.1
Slovakia	4.1	5.1	4.7	5.7	68.9	63.4
Finland	1.4	1.4	2.1	2.1	31.9	35.8
Sweden	1.2	1.2	1.4	1.5	34.8	34.5
United Kingdom	1.6	2.2	2.5	2.2*	40.6	39.4
<b>European Union</b>	<b>4.6</b>	<b>5.6</b>	<b>4.7*</b>	<b>5.6*</b>	<b>50.8**</b>	<b>47.6**</b>

Source: ECB, Consolidated Banking Data (CBD2)

### *Spain*

According to ECB data, the NPL ratio dropped from 5.9% in June 2016 to 5.3% in June 2017. Private sector NPLs also decreased from 7.7% in June 2016 to 7.1% in June 2017.

Spanish banks hence continued to reduce their NPLs over the last year. This reduction occurred in all classes of loans, except for consumer loans where NPLs slightly increased in

<sup>6</sup> Notes: Figures correspond to domestic credit institutions as well as foreign-controlled subsidiaries and branches.

\* Due to the unavailability of sector-specific data for Portugal and the EU, NPL figures correspond to loans and advances to all sectors.

\*\* Due to the unavailability of provisioning data for loans, the provisioning ratios for Bulgaria, Germany, Hungary, Spain, and the EU were calculated by considering impairments and NPLs for all debt instruments, including both loans and debt securities.

parallel with the rapidly growing consumer lending. The decline in the volume of NPLs would have been higher without the impact of the new Annex 9 accounting rules – introduced by the Bank of Spain – which toughened the classification criteria for performing loans. In the 12 months up until and including August, the total loans volume to non-financial corporations (NFCs) and households decreased by about EUR 33 billion, continuing the decline in the aggregate stock of credit in Spain since August 2009. This decline in the denominator slows down the fall in the NPL ratio.

Despite the improvements described above, NPLs remain high in certain NFC sectors. Most notably, according to local data, the NPL ratios for the construction and real estate sectors stood at 25.2% and 20.8% respectively, as of September 2017. In the first half of 2017, banks further reduced forborne and foreclosed assets. According to EBA data on sampled banks, forborne loans continued to decline and their ratio in total credit went down from 6.2% at end-2016 to 5.6% in June 2017. As in 2015, sales of existing foreclosed assets (amounting nearly to 15% of the stock of foreclosures at the end of 2015), exceeded additions of new foreclosures (around 12.3% of the stock).

The reduction of NPLs in Spain is likely to continue at a brisk pace, supported by the announcement of large portfolio disposals by the two largest banks, Santander and BBVA. Both banks agreed to sell majority stakes to private investment firms in their legacy real estate portfolios which have a combined gross book value of EUR 43 billion. Beyond these two big operations, additional smaller operations for the sale of NPLs and foreclosed assets have already been finalized or are ongoing.

Following the resolution of Banco Popular, some banks have started to accelerate the clean-up of balance sheets with potential benefits going forward. Spanish banks also continued to improve their efficiency in the first half of 2017 and according to data by the EBA their cost-to income ratio improved from 52.9% at end-2016 to 50.9% in June 2017, significantly below the EU average (61.5%).

On 6 June, the ECB (SSM) decided that Banco Popular was "failing or likely to fail" due to a significant deterioration of its liquidity position therefore triggering adoption of the resolution scheme for the bank. Popular unveiled a EUR 3.5 billion loss for 2016 as it booked a record amount of EUR 5.7 billion of provisions on its nearly EUR 45 billion legacy portfolio of property loans and foreclosed assets. After booking further provisions of EUR 400 million and a loss of EUR 200 million in Q1 2017 the liquidity situation of the bank deteriorated rapidly.

The resolution scheme prepared by the SRB and endorsed by the Commission provided for the sale of Banco Popular to Banco Santander for the price of EUR 1. The purpose of this operation was to ensure business continuity, full access by customers to deposits and to avoid adverse effects on financial stability. The resolution scheme provided for the write-down and conversion of all relevant capital instruments of Banco Popular prior to the transfer of assets to Santander in order to address the shortfall in the capital position of the institution. Hence, the implemented resolution tool ensured full protection for deposit holders and tax payers' money. This resolution of Popular was the first under the Single Resolution Mechanism Regulation (SRMR).

## *Portugal*

According to ECB data, the NPL ratio dropped from 17.9% in June 2016 to 15.5% in June 2017, corresponding to a decrease of ca EUR 8 billion of NPLs,<sup>7</sup> and the coverage ratio increased from 47.6% to 49.4%.

The reduction of the NPL stock in the last year is evidence that Portugal continues to make efforts to address the legacy NPL problem. Initial steps had already been taken by authorities to tackle some constraints to the recovery of NPLs, such as the ability for banks to recognise write-offs fiscally and incentivise the creation of a more dynamic secondary market for NPLs by facilitating the entry into the market of new servicing companies. The authorities' main focus is on the legacy NPLs stemming from loans to NFCs, which as of June 2017 made up 64% of all NPLs, amounts to some EUR 27 billion.

An assessment of the banks' non-productive assets showed the need for a comprehensive and coordinated approach among relevant stakeholders currently pursued by authorities via a three-pronged strategy: (i) legal/judicial, tax and other relevant reforms, (ii) prudential supervisory actions, and (iii) NPL management options. A quantitative analysis highlighted the heterogeneity of the NPL stock and the significant share of NFCs.<sup>8</sup>

The legal/judicial leg of the strategy is focused, inter alia, on facilitating early restructurings of firms and the use of out-of-court mechanisms, while ensuring that insolvent companies are prevented from applying for various pre-insolvency proceedings and thus benefitting from standstill protection – often used as a strategy to delay the inevitable liquidation.<sup>9</sup> Many measures related to these objectives have been recently approved by the Portuguese Parliament such as the creation of i) a new legal framework to allow majority creditors to convert their credits into share capital, enforceable before the court, ii) and a new legal framework for voluntary out-of-court restructuring and iii) a new player – the mediator for companies 'recovery to assist the debtor. Furthermore, the legal/judicial pillar of the strategy is focused on expediting insolvency proceedings. Moreover, there is a new regime for enforcement of collateral arrangements that will streamline the appropriation of the pledged assets by the creditor.

The second leg of the strategy focuses primarily on prudential supervisory actions by using, but not being limited to, the ECB's guidance on NPLs.<sup>10</sup> Banks with high levels of NPLs have elaborated 5-year NPL reduction plans and submitted them to the supervisor. These plans include measures such as cash recoveries, foreclosures, sales of NPLs and write-offs and will be closely monitored by the supervisor.

Lastly, various NPL management options are part of the third pillar of the comprehensive strategy. Banks are responsible for managing their NPL portfolios and are expected to take the initiative. Coordination among all entities involved in the overall strategy still remains essential. In addition to individual action, management options may include proposals aimed to be applicable system-wide, such as the "coordination platform" being put forward by

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<sup>7</sup> Due to the unavailability of sector-specific data for Portugal, NPL figures are limited to loans and advances to all sectors.

<sup>8</sup> Refers mostly to firms exposed to 3 or more banks.

<sup>9</sup> A pre-condition for many measures is an efficient identification of firms that are solvent/viable from those that should be liquidated.

<sup>10</sup> While being a part of the Portuguese 3-pronged strategy, submission and revision of NPL strategies per individual bank are undertaken by the SSM across the euro area banking landscape.



credit institutions – a specific approach for corporate NPLs, where loans will remain on the banks' balance sheets. It aims to promote enhanced creditor coordination to expedite credit restructuring and/or NPL sales, on the hand, and to foster the restructuring of viable firms, on the other hand. The platform is a project driven by Caixa Geral de Depósitos, Novo Banco and Millennium BCP but is also open to other lenders. It is being set up to manage loans where at least two of the three banks have a business relationship with the same corporate borrower. The enhanced coordination is aimed to help speeding up financial restructuring of the debtor companies while the debtor will negotiate only with the entity instead of running parallel talks with the three lenders. It is unclear how many NPLs will be jointly managed by the platform as it is still in early stages of development.

### *Cyprus*

According to ECB data, the NPL ratio dropped from 37.6% in June 2016 to 33.4% in June 2017. Private sector NPLs were rather stable, moving from 56.2% in June 2016 to 52.7% in June 2017.

Cyprus hence continues to make efforts to reduce the stock of NPLs in its banking system. A significant proportion of the stock of NPLs is linked to retail mortgages and SME lending backed by real estate collateral. Due to sizable deleveraging in the banking sector, the NPL ratios have remained relatively stable even though the stock of NPLs has been consistently contracting for around two years. A significant share of the NPL stock reduction has been due to the curing of restructured loans, write offs and debt to asset swaps. Exploiting the strong economic growth of the country, banks are expected to continue their efforts utilizing all available tools for further reduction of NPLs.

A number of initiatives have been put in place by the authorities in response. These were (i) new legal provisions on insolvency procedures; (ii) improvement of collateral enforcement; (iii) new sale of loans legislation; (iv) the introduction of NPL targeting procedures; and (v) supervisory actions on provisioning.

Due to relatively limited use of the insolvency procedures, which were first adopted in 2015, the authorities have set up a working group in July 2017. The aim is to review the implementation of the legislation and to address its shortcomings by late 2018.

With respect to collateral enforcement, several measures were taken in early 2017 to improve the issuance of title deeds. The use of the new foreclosure rules, which were adopted in 2015, remains very limited. Some of the shortcomings in the law are being addressed in a recent draft bill that is currently under legal vetting.

The authorities aim to adopt a legislation framework for loan securitization by mid-2018, which may result in increased sales. Meanwhile, two Cypriot banks have announced the creation of joint ventures with foreign specialised debt servicers to manage their NPL portfolios, which can facilitate sales.

Lastly, supervisory pressure, notably through the Single Supervisory Mechanism (SSM) Supervisory Review and Evaluation Processes, led to a rise in the provisioning levels in early 2017. The coverage ratios for NPLs have increased from 38.8% in June 2016 to 47.1 61.4% in June 2017. Although the aggregate figures mask divergence among individual banks, the level of provisioning in Cypriot banks is now comparable with the EU averages and should reflect more accurately the correct value of the real estate collateral.

## *Greece*

According to ECB data, the NPL ratio decreased from 47.2% in June 2016 to 46.9% in June 2017. Private sector NPLs experienced a slight uptick, going up from 50.5% in June 2016 to 50.6% in June 2017.

The reduction of NPLs clearly remains the main pillar of the financial sector policy adopted in Greece as part of the international financial assistance programme. The slight increase in the NPL ratio was due to mild loan deleveraging as well as limited net NPL inflows. This could be linked to the delayed implementation of the programme requirements as well as the protracted negotiations under the second review of the third economic adjustment programme. Write-offs remain the main tool for addressing bad loans, especially in light of the fact that the quarterly default rate remained above 2% and still exceeded the cure rate. Overall, banks have met their nominal reduction targets so far.

The authorities have implemented a series of measures that are meant to offer banks effective tools to cure distressed loans. Focusing on the most recent measures, first, the out-of-court debt negotiation framework was set up. It allows borrowers to restructure their loans with both private and public creditors, whereby accumulated fines and surcharges on tax arrears are subordinated and ultimately written down, if necessary. While the framework is fully operational since August 2017 and has attracted some interest by eligible parties (approximately 370 submitted applications and additional two thousand in the pipeline), only a small number of cases have been successfully completed so far. In this vein, a review is under way considering improvements to make it more efficient. Second, banks can now enforce their rights on collateral by using electronic auctions. The first e-auctions were conducted at end-November and early December, but notaries still appear to be reluctant to execute the physical auctions. Third, the relative liberalisation of the debt servicing companies licencing regime has allowed for genuine competition in the sector, with 10 non-bank NPL servicers already licensed and active in the market. The two major NPL transactions in the course of 2017 refer to a EUR 1.3 billion distressed SME loan portfolio (sale via a securitization vehicle) and EUR 1.5 billion unsecured consumer loans (the latter sold at single digit net prices). Moreover, banks are planning further sales of portfolios in the context of the NPE operational targets framework for improving asset quality that has been agreed among the Bank of Greece, the ECB (in its capacity as a supervisor) and the supervised banks (covering the period up to 2019).

## *Ireland*

According to ECB data, the NPL ratio decreased from 14.6% in June 2016 to 11.6% in June 2017. Private sector NPLs also went down from 18.9% in June 2016 to 15.8% in June 2017.

From the peak in 2013, NPLs have fallen cumulatively by over 60% and more than EUR 50 billion according to national data<sup>11</sup> with significant reductions in each of the past four years. A substantial part of this reduction of NPLs in the banking sector has been due to the widespread use of loan restructuring solutions.

Of the remaining NPLs of approximately EUR 34 billion at September 2017 approximately 65% are mortgages and approximately 45% of these mortgages have been restructured. Many of these mortgages will not meet the test to return to performing despite regular cash

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<sup>11</sup> Central Bank of Ireland: Residential Mortgage Arrears & Repossessions Statistics: Q3 2017. Figures are approximate as data from 2013 was not in accordance with EBA definition of NPLs.

flows. Of the mortgages on principal dwellings that are classified as restructured, 87 % were deemed to be meeting the terms of their current restructure arrangement.<sup>12</sup> The number of accounts for principal dwellings in arrears has continued to fall every quarter since 2013<sup>13</sup>.

For those remaining in serious mortgage arrears, the Abhaile Scheme was launched in late 2016 to provide free, independent expert advice and support on financial and legal issues. Abhaile is targeting those borrowers in very long term arrears that have proven to be difficult to engage with. There continues to be a high level of new applications to the Insolvency Service of Ireland, largely due to the Abhaile scheme, which includes free Personal Insolvency Practitioner Consultations for insolvent debtors. A revision to the mortgage-to-rent (MTR) scheme in early 2017, has made the process quicker, more transparent, easier to navigate for borrowers and ultimately more accessible to more households in mortgage distress. Announced in September 2017, the iCare/AIB Housing scheme is also an important development in the MTR area. Eligible customers who qualify for the MTR process will continue to live in their home as long-term tenants of iCare Housing whose purpose is to provide and manage social rented housing. Expressions of Interest from bodies interested in pursuing pilot alternative lease arrangements based on the MTR model were sought in October 2017 by the Housing Agency on behalf of the Department of Housing with a closing date of 21 December 2017.

Buoyed by a significant recovery in real estate prices, NAMA, the national Asset management Company, was able to sell a substantial portion of its portfolio, generated total cash flows of around EUR 40 billion by end-June 2017 and redeemed all of its senior debt in October 2017. NAMA now aims to generate a return of EUR 3 billion by the time it winds down in 2020.

### *Italy*

According to ECB data, the NPL ratio decreased from 16.2% in June 2016 to 12.2% in June 2017. Private sector NPLs also declined from 20% in June 2016 to 15.9% in June 2017, still well above the average NPL ratio in the EU.

The end of June 2017 data reflect some important NPL sales and securitisations that have already had their effects on banks' balance-sheets (in particular, the sale of EUR 17.7 billion of impaired assets by Unicredit was completed as at September 2017; the NPL securitisation transaction by Banca Monte dei Paschi di Siena – gross book value of EUR 26.1 billion – has not yet been completed).

In 2017, NPL securitisation has developed into an important NPL disposal strategy used by banks to clean up their balance sheets. In 2017, banks have increased their recourse to the *Garanzia Cartolarizzazione Sofferenze* (GACS), as several transactions were completed and launched. In this respect, the securitisation of the EUR 26.1 billion of gross NPLs by Monte dei Paschi di Siena constitutes the biggest NPL securitisation ever on the Italian market. Overall, based on the track record so far, the GACS appears to have been more useful for large- and medium-sized banks than for smaller credit institutions, which have more difficulties in pooling a critical mass of impaired assets and in providing detailed loan portfolio data. To facilitate the securitisation of some categories of NPLs (in particular of unlikely-to-pay), increase the scope of manoeuvre of special purpose vehicles (SPVs) and

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<sup>12</sup> Central Bank of Ireland: Residential Mortgage Arrears & Repossessions Statistics: Q3 2017

<sup>13</sup> Central Bank of Ireland: Residential Mortgage Arrears & Repossessions Statistics: Q3 2017

encourage participation in foreclosure auctions, Italy introduced several amendments to Law 130/1999 on the securitisation of loans. The main novelties are: *i*) SPVs that acquire and securitise NPLs are allowed to grant new loans to certain categories of borrowers in case this facilitates the restructuring of the financial position of borrowers and the repayment of outstanding debt; *ii*) special purpose vehicles (SPVs) are allowed to buy assets placed as collateral for secured loans.; *iii*) the simplification of loan transfers from originating banks to SPVs by exempting these transfers from the obligation to notify the borrowers.

The Italian Recovery Fund has become the main NPL investor in Italy. Through its participation in four NPL securitisation transactions involving gross NPLs of roughly EUR 31 billion and an investment of EUR 2.5 billion, it has supported the disposal of NPLs by vulnerable banks. The bulk of its investment (approximately EUR 1.5 billion) was in the securitisation of the NPL portfolio of Banca Monte dei Paschi di Siena, as it bought the mezzanine and junior tranches issued by the SPV. Overall, the Fund has participated in securitisation transactions with disposal prices between 19% and 32% of the gross book value, which reflect the different composition, data quality and impairment degree of securitised assets. The Fund has also contributed to the further development of the asset servicing market, as it entered in several agreements with CERVED on the servicing of securitised portfolios. Notwithstanding the progress so far, the number of servicing companies is still limited.

Banks have continued to upgrade their arrears management capacity, and some of them are still considering the internal NPL work-out as main priority, but have also made increased recourse to outright NPL sales. The secondary market for impaired assets has become more dynamic compared to previous years thanks to both domestic and foreign NPL buyers. Outright sales are expected to further increase as banks are optimising their NPL management and disposal strategies *inter alia* to comply with supervisory requirements. However, credit institutions are wary about the impact a rapid disposal of NPLs may have on their capital buffers and pricing of impaired assets. The bid-ask spread for NPLs is still hovering around 15% to 20%, mainly due to sub-optimal data available for some portfolios as well as the still long recovery time of collateral.

### ***Slovenia***

According to ECB data, the NPL ratio decreased from 16.3% in June 2016 to 11.4% in June 2017. Private sector NPLs also declined from 21.2% in June 2016 to 14.7% in June 2017.

Most of the recent reduction is due to restructuring efforts, repayments, write-offs, debt forgiveness and sale of NPLs to third party (private) institutions, the stock of NPLs of households remains very low, at 4.4% as of June 2017.

Since its inception in 2013 until June 2017, the Slovenian Bank Asset Management Company (BAMC) has generated cumulative cash-flows of nearly EUR 1.1 billion, representing nearly 60% of the fair value of the loans transferred. Most of these cash flows are from maturing loans on BAMC's balance sheet that have only partially been refinanced by external (i.e. bank) funding. In recent months loan and collateral sales appear to have picked up. The business strategy for the years 2016 to 2022 was adopted in December 2016. It aims to ensure the highest possible return to the state and to fully redeem bonds backed by state guarantees by 2022.

The Bank of Slovenia has introduced a number of supervisory measures in the last years. In 2015 a guidance on the organisational structure of NPL management and debt workout were

issued for banks. A horizontal analysis of the NPL exposures of all banks in Slovenia was performed in the same year. Subsequently, banks were required to develop NPL resolution strategies, accompanied by operational reduction plans. Furthermore, in March 2017 the Bank of Slovenia published a handbook for effective management and work out of the non-performing debt of micro, small and medium-sized companies.<sup>14</sup>

In order to preserve the applicability of the above mentioned measures and the handbook, the Bank of Slovenia publishes the overview of the major financial ratios by industry sector in coordination with the Chamber of Commerce annually.<sup>15</sup> The Slovenian Principles of the financial restructuring of corporate debt were adopted first by Bank Association in June 2014, the Principles of responsible commercial crediting (November 2015) and Restructuring guidelines for MSME (December 2015) followed.<sup>16</sup>

### **3. PROGRESS ON REALISING THE ECOFIN ACTION PLAN**

#### **3.1. The NPL issue: a priority for the EU**

The Council Action Plan recognises that the primary responsibility to tackle NPLs remains with the affected banks and Member States. There are indeed significant differences across Member States both in terms of structure and causes of the NPL problems, but also in terms of legal and judicial capacity. Moreover, a large part of effective policy instruments is at national level, including fiscal policy and insolvency law.

The interconnectedness of national banking and financial systems in the Union adds a European dimension to reducing current NPLs as well as preventing future build-up of NPLs. In particular, there are important potential spill-over effects from Member States with high level of NPLs to other Member States, both in terms of economic growth and financial stability. Weak growth in some Member States due to high NPLs might affect economic growth elsewhere, and investors often perceive the value and soundness of all EU banks in the light of weak balance sheets of just some banks.<sup>17</sup>

The Commission therefore announced, in its Communication on Completing the Banking Union of 11 October 2017, a comprehensive package on tackling NPLs in Europe.

This package will consist of the following parts:

- *Measures to further develop secondary markets for NPLs*, especially with the aim of removing undue impediments to loan servicing by third parties and the transfer of loans following the ongoing impact assessment.
- *Measures to enhance the protection of secured creditors* by providing them with more efficient methods of value recovery from secured loans.

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<sup>14</sup> See <https://www.bsi.si/en/publications/other-publications>.

<sup>15</sup> See <https://www.bsi.si/en/financial-stability/banking-system-supervision/supervisory-disclosure/corporate-financial-indicators>.

<sup>16</sup> See <http://www.zbs-giz.si/zdruzenje-bank.asp?StructureId=884>.

<sup>17</sup> Report of the FSC Subgroup on Non-Performing Loans.

See <http://data.consilium.europa.eu/doc/document/ST-9854-2017-INIT/en/pdf>.

- *The possible introduction of statutory (Pillar 1) prudential backstops* in order to prevent the build-up and potential under provisioning of future NPL stocks across Member States and banks via time-bound prudential deductions from own funds.
- *A Blueprint for how national Asset Management Companies (AMCs) can be set up, managed and closed down, within existing banking and State aid rules by building on best practices learned from past experiences in Member States.*
- *Measures to enhance the protection of secured creditors* by allowing them more efficient methods of value recovery from secured loans.
- Potentially, the introduction of a *common definition of non-performing exposures (NPE)* in accordance with that already used for supervisory reporting purposes<sup>18</sup>, in order to establish a sound legal basis for and ensure consistency in the prudential treatment of such exposures.

Furthermore, the Commission is also advancing a number of other work streams:

- *Undertaking of a benchmarking exercise of loan enforcement regimes* in order to establish a reliable picture of the delays and value-recovery banks experience when faced with borrowers' defaults, and inviting close cooperation from Member States and supervisors to develop a sound and significant benchmarking methodology.
- *Fostering the transparency on NPLs in Europe* by improving the data availability and comparability as regards NPLs, in full support of the EBA's efforts in this regard; and supporting the development of an *NPL transaction platform*, which could potentially contribute significantly to the growth in NPL trading.

### **3.2. Update of all work strands identified in the Action Plan**

#### ***1. Interpretation of Art 16 SSMR and Art 104 CRD IV***

The Commission issued the requested interpretation in the Single Supervisory Mechanism (SSM) Review Report published on 11 October 2017, clarifying that EU legislation, in particular Article 16(2)(d) SSMR<sup>19</sup> and Article 104(1)(d) CRDIV<sup>20</sup>, already provides supervisors with powers to influence a bank's provisioning policy with respect to NPLs within the limits of the applicable accounting framework and to apply the necessary adjustments to own funds (deductions and similar treatments) on a case-by-case basis.

#### ***2. Addressing potential under provisioning, via automatic and time-bound provisioning***

The Commission will introduce measures to prevent the risk of under-provisioning of future loans that subsequently turn non-performing. The implementation of the so-called statutory prudential backstops would be realised via a legislative proposal to amend the CRR.<sup>21</sup>

To inform its work, the Commission carried out a targeted consultation to gather stakeholders' views on the possible introduction of common minimum levels of provisions

<sup>18</sup> See Commission Implementing Regulation (EU) No. 680/2014.

<sup>19</sup> Council Regulation (EU) No 1024/2013 (Single Supervisory Mechanism Regulation – SSMR)

<sup>20</sup> Directive 2013/36/EU (Capital Requirements Directive – CRDIV)

<sup>21</sup> Regulation (EU) No 575/2013 (Capital Requirements Regulation – CRR)

and deductions from own funds that EU banks would be required to make to cover incurred and expected losses on newly originated loans that turn non-performing. Such prudential minimum treatment would act as a backstop, which would be directly applicable to all EU banks in order to put EU-wide brakes on the build-up of future loans that turn non-performing without sufficient loan loss coverage. The statutory backstops would be a prudential tool under Pillar 1 which would come on top of (i) the use of existing supervisory powers under Pillar 2 (which are bank-specific measures following a case-by-case assessment by the supervisor), and (ii) the application of accounting standards with regard to loan loss provisioning. The results of the consultation have been presented to the Commission Expert Group on NPLs on 14 December 2017.

In parallel to the consultation, the Commission sought technical advice from the EBA for the purposes of assessing the potential impact of the introduction of such statutory prudential backstops on EU banks. Based on stakeholders' feedback to the consultation and the advice from the EBA, the Commission is now finalising the impact assessment on a possible introduction of statutory prudential backstops which will inform the Commission's decision on how to proceed on this issue.

In its capacity as supervisor, the ECB has also issued a consultation on its expectations regarding banks' provisioning policies for NPLs.<sup>22</sup>

### ***3. Extend SSM NPL guidelines to small (non-directly supervised) banks***

The ECB (in its supervisory capacity) is working closely with the EBA to develop, by summer 2018, general guidelines on NPL management. Those guidelines would apply to all credit institutions in the Union and would be consistent with the existing SSM guidance concerning NPLs. During 2018, it will be assessed whether the SSM non-performing loans guidance should be extended to Less Significant Institutions (LSIs) within the Banking Union

### ***4. Adopting EU-wide NPE guidelines***

In order to enhance supervisory guidance, the EBA will issue guidelines on non-performing exposure (NPE) management and on banks' loan origination monitoring and internal governance (see item 5 below). For this purpose, the EBA established a Task Force on NPLs (NPL TF). Participants in this NPL TF are members from the NCAs and the ECB.

As per the Council's mandate, the guidelines on NPE Management will be consistent to the ECB's guidance on NPLs applicable to significant credit institutions – which was published in March 2017. The EBA guidelines will have an extended scope and will hence apply to all banks in the Union.

The major issues discussed in the NPL TF are aspects on proportionality and how the guidelines will be applied to smaller banks (Less Significant Institutions (LSIs) in the Banking Union). The EBA's NPL TF will closely coordinate with the ECB to ensure

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<sup>22</sup> Cf. ECB, Addendum to the ECB Guidance to banks on nonperforming loans, [https://www.bankingsupervision.europa.eu/legalframework/publiccons/pdf/npl2/ssm.npl\\_addendum\\_draft\\_201710.en.pdf](https://www.bankingsupervision.europa.eu/legalframework/publiccons/pdf/npl2/ssm.npl_addendum_draft_201710.en.pdf).

consistency of the relevant SSM supervisory guidance for LSIs which is being developed in parallel to the EBA guidelines on NPE Management.

The EBA draft guidelines are expected to be submitted for public consultation by end of March 2018. The final guidelines are expected to be published in summer 2018, in line with the Council's mandate.

#### **5. *New guidelines on banks' loan origination, monitoring and internal governance***

The new guidelines to be issued by EBA will leverage on the existing work from NCAs as well as on work on consumer protection issues and the relevant existing guidelines published by the EBA. The work on the new EBA guidelines on banks' loan origination, monitoring and internal governance is at a very preliminary stage. Considering the breadth of the topic, it is anticipated that the development of a comprehensive set of guidelines will be time-consuming. The work needs to be coordinated in order to consider issues related to consumer protection, macro-prudential approaches (to be aligned with the relevant work currently undertaken by the European Systemic Risk Board – ESRB), as well as micro-prudential aspects.

It is expected that the draft EBA guidelines will be submitted for public consultation during summer 2018 and that the final guidelines will be published by the end of 2018.<sup>23</sup>

#### **6. *Develop macroprudential approaches to tackle the build-up of future NPLs***

The ESRB established a dedicated work stream on macroprudential approaches to tackle NPLs. The work stream functions under the auspices of the Instruments Working Group (IWG), one of the two permanent sub-structures of the ESRB's Advisory Technical Committee.

##### *Mandate*

The aim of the work stream is to identify possible macroprudential approaches to prevent the emergence of system-wide NPL problems. The work will concentrate on new flows of NPLs. Since the focus will be on prevention, considerations for mitigating policies to address the current stock of NPLs shall be avoided, as this may also be within the remit of other institutions.

The work stream will explore approaches to be implemented when the cycle is moving upwards (i.e. ex-ante approaches), as well as approaches to deal with the downturn cycle, insofar as the latter address pro-cyclicality concerns. The proposed macroprudential approaches would further aim to ensure that their implementation would not lead to any financial disruptions and that ultimately the provision of credit to the real economy is not affected.

In pursuing its mandate, the work stream will work under the assumption that the macroprudential toolkit is in a "steady state". The work will therefore take into account the existence of a fully active countercyclical capital buffer and of a full implementation of IFRS 9, among other relevant measures.

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<sup>23</sup> As EBA is working in parallel on various NPL related work streams, a delay might occur in the delivery of the loan origination, monitoring and internal governance guidelines.



### *Membership of the work stream*

The work stream will operate within the IWG and will consist of a limited number of experts. IWG members either participate directly or nominate a representative for their national authority. Technical support is provided by the ESRB Secretariat.

### *Deliverables and Timeline*

A kick-off conference call took place on 15 December 2017 in order to discuss an initial issues note. A first physical meeting will take place in mid-January 2018. A final report is scheduled to be presented at the ESRB's General Board meeting of 27 September 2018.

#### **7. *Enhanced disclosure requirements on asset quality and non-performing loans for all banks***

The EBA published in December 2016 its guidelines on disclosure requirements under Part Eight of the CRR ('EBA GL2016 11'), which include a template on non-performing and forborne exposures requesting institutions to disclose information on the gross carrying amount and accumulated impairments of performing, non-performing and forborne exposures, and on the collaterals and guarantees received. The template must be filled in by G-SIIs and O-SIIs, and is applicable as of 31 December 2017.

Following the Council mandate to implement, by the end of 2018, enhanced disclosure requirements on asset quality and NPLs to all banks, the EBA will broaden the scope of application of the template on non-performing and forborne exposures currently included in the 'EBA GL2016 11' to all institutions; this disclosure for non-G-SIIs/non-O-SIIs will be applicable by the end of 2018.

In addition, also following the Council mandate, the EBA is planning to implement, with respect to all credit institutions in the Union, additional disclosure items on NPEs, forbearance and foreclosed assets, including disclosures aligned with those currently recommended in the ECB guidance to banks on Non-Performing Loans and other disclosures that the NPL TF might consider relevant. The implementation of these disclosure items will most likely take the form of EBA guidelines.

#### **8. *Improving loan tape information required from banks on their banking book credit exposures***

In order to strengthen the data infrastructure by uniform and standardised data for NPLs, the EBA has issued final templates on due diligence in December 2017. These loan tapes (henceforth referred to as "templates") will not be part of supervisory reporting, but banks and investors are encouraged to use these standardised EBA NPL templates for NPL-related transactions. To address the different data needs during the screening and during the financial due diligence / valuation phase of NPL-related transactions, two sets of templates were developed: the "EBA NPL transaction templates", which will serve for the financial due diligence and valuation of portfolios, and the "EBA NPL portfolio screening templates", which will be particularly useful for the initial screening of portfolios.

For the creation of the EBA NPL transaction templates, 1300 data points were examined during the course of this project, in order to create a list of about 480 data points relevant for valuation and due diligence purposes in NPL transactions. In order to minimise any

additional costs in filling out and analysing the EBA NPL transaction templates, they provide references to:

- existing reporting or similar templates (Finrep, AnaCredit, ECB / ESMA ABS templates);
- the CRR for further definitions applied as well as ISO Codes; and
- the Nomenclature of Units for Territorial Statistics (NUTS3) as laid out by Eurostat.

The templates will be allocated in specific asset classes, consistently with the asset classes applied for the ECB / ESMA ABS templates, and are based on the market experience and relevance to NPL Transactions seen so far.

The EBA NPL Transaction templates have been discussed with various public sector stakeholders, including ESMA, ECB, the Commission and the SRB, during the development phase. In November 2017, the draft templates were published for an informal interaction with the industry.

The feedback from the industry discussion on the draft templates was analysed in December 2017 and the final templates were published. A post-implementation phase at the end of the project (first half of 2018) may be necessary for accommodating additional feedback once the templates are used in actual transactions.

#### ***9. Strengthen the data infrastructure for NPLs and consider the set-up of NPL transaction platforms***

With respect to the NPL transaction platform, work by the ECB, the Commission and the EBA has progressed rapidly and should be completed within the coming weeks.

Kicking off the process, a high-level meeting took place in early October 2017, where the three institutions reached broad agreement on the collective vision for an NPL transaction platform and some key policy parameters were already clarified. On this basis, and in close cooperation with Commission and EBA staff, ECB staff prepared a draft outline for a technical paper to detail various aspects of an NPL transaction platform, and subsequently circulated a draft paper. In November, a further meeting, at technical level, was held to discuss the draft technical paper and to clarify remaining open issues. A second draft of the paper was subsequently prepared and is currently being discussed by staff at this level.

The technical paper outlines the rationale for an NPL transaction platform; contextualises a transaction platform as part of wider initiatives to resolve large stocks of NPLs; provides detail on what a transaction platform is, and how it might function; and outlines some important operational considerations. It concludes with a roadmap for future work, to bring the concept to fruition.

#### ***10. Develop an AMC Blueprint***

The Commission is developing a Blueprint for national Asset Management Companies (AMCs) in close cooperation with the ECB, EBA and SRB. The technical level drafting of the Blueprint is close to being finalised. The main features of the draft Blueprint have been discussed with Member States in the Commission's Expert Group on NPLs on 14 December 2017.

The Blueprint will provide practical recommendations for the design and set-up of AMC's at the national level, building upon best practices from past experiences. AMC's can be private or (partly) publicly supported with no need of State aid, if the State can be considered to act as any other economic agent.<sup>24</sup> The option of an AMC involving State aid should not be seen as the default solution. Nevertheless, considering AMC's with a State aid element as an exceptional solution, the Blueprint aims to clarify the permissible design for such AMC's, consistent with the EU legal framework, particularly the Bank Recovery and Resolution Directive (BRRD), Single Resolution Mechanism Regulation (SRMR) and State Aid rules.

The Blueprint will therefore put forward a number of common principles, such as the relevant asset perimeter, the participation perimeter, considerations regarding the asset-size threshold, asset valuation rules, the appropriate capital structure, and the governance and operations of the AMC.

Finally, the Commission services intend to continue analysing impaired asset relief measures which are alternatives to centralised AMC's and have been successfully implemented by Member States in the past, in full respect of the BRRD, SRMR and State Aid rules.

### *11. Develop secondary markets for NPLs*

The Commission is following up on the Action Plan in elaborating a European approach to foster the development of secondary markets for NPLs. This work is informed by an ongoing impact assessment, the results of the public consultation on NPLs and discussions within the Commission's Expert Group on NPLs.

The replies to the public consultation launched in July 2017<sup>25</sup> suggest that entry conditions and conduct rules for loan servicers play a crucial role in the development of a secondary market for NPLs. Many respondents consider that measures that lower entry barriers would increase demand and raise competitive pressure on the demand side of the NPL market. As most loan servicers are relatively small, respondents also estimate that such servicers would benefit from scale economies. Large NPL investors, on the other hand, tend to be present in most markets already. Further progress with the resolution of NPLs is generally judged to require that new and potentially smaller investors enter and bid for smaller loan portfolios, many held by small- and medium-sized banks. The entry of new, and particularly also smaller investors in the market would increase market demand for NPLs. In turn, a better functioning and more liquid secondary market could raise the effectiveness of other policy measures to tackle NPLs. In some instances the replies highlight that the potential benefits of AMC's and supervisory action depend importantly on rising market demand for NPLs.

While many consultation replies support action at Union level in this regard, they also stress the importance of consumer protection. Moreover, stakeholders emphasise that the transfer of loans to a non-bank is governed by complex legal frameworks which are enshrined in national civil law and therefore unlikely to be resolved through a legislative initiative at Union level.

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<sup>24</sup>This, inter alia, would mean that any transactions take place at Estimated Market Value (EMV).

<sup>25</sup>Public consultation on the development of secondary markets for non-performing loans and distressed assets and protection of secured creditors from borrowers' default.

See [https://ec.europa.eu/info/consultations/finance-2017-non-performing-loans\\_en](https://ec.europa.eu/info/consultations/finance-2017-non-performing-loans_en).

The impact assessment therefore explores different options to foster market entry of NPL investors and of loan servicers.

### ***12. Benchmarking exercise on the efficiency of national loan enforcement (including insolvency) regimes from a bank creditor perspective***

The benchmarking of national loan enforcement and insolvency regimes aims at establishing a reliable picture of the efficiency of various types of enforcement procedures available in national law, including both by individual creditors and collectively (insolvency), secured as well as unsecured. These outcomes are heavily influenced by judicial capacity in the respective Member States, and the benchmarking therefore aims at depicting realistic outcomes as they are experienced in practice by (bank) creditors.

Progress on the benchmarking exercise was presented to and discussed with Member States experts at the September and December 2017 meetings of the expert group on NPLs, including the issue of lack of access to meaningful data. Going forward the benchmarking will focus on the duration and (lack of) efficiency of national enforcement/insolvency systems, and on gathering aggregate, anonymised data on NPL value recovery with an involvement of bank supervisors.

### ***13. Develop the focus on insolvency issues in the European Semester***

Issues in national corporate insolvency frameworks have been a long standing topic under the European Semester. They have been analysed in several Country Reports and several dedicated Country Specific Recommendations (CSRs) were adopted. Since 2013, CSRs tackling insolvency issues were addressed in different years to twelve Member States: Bulgaria, Cyprus, Spain, Croatia, Hungary, Italy, Latvia, Malta, Portugal, Romania, Slovenia, and Slovakia.

In 2017, CSRs on insolvency were adopted for five Member States (see annex). Cyprus has received a detailed and comprehensive recommendation to increase the efficiency of its judicial system and fully implement the insolvency and foreclosure frameworks. Following up on the previous years' CSRs, Latvia has received a recommendation to strengthen conflict of interest prevention for insolvency administrators. Croatia and Slovenia received recommendations to improve efficiency of their judicial systems through the reduction of the length of civil and commercial cases. Portugal was recommended to increase the efficiency of its insolvency and tax proceedings.

Regarding the outlook for the current European Semester, insolvency issues will be analysed in the Country Reports 2018, which will be published in late February, and in mid-May 2018 the Commission will issue its recommendations to the Council for CSRs.

Apart from the European Semester, corporate insolvency problems are also the subject of technical assistance provided by the Commission's Structural Reform Support Service. Among projects accepted in the first selection round in spring 2017, four projects concerned insolvency reforms (in Lithuania, Cyprus, Croatia and Greece). In December 2017 the Commission proposed to amend the Structural Reform Support Programme Regulation,<sup>26</sup> by

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<sup>26</sup> (EU) 2017/825.

increasing the financial envelope of the Structural Reform Support Programme and adapt its general objective.<sup>27</sup>

#### ***14. Member States to consider carrying out dedicated peer-reviews on insolvency regimes***

This work strand is due by end of 2018 and, under the ECOFIN Action Plan, is meant to build on the Commission Insolvency Benchmarking Study (see item 12 above).

#### ***15. Further analyse the possibility of enhancing the protection of secured creditors***

Following the commitment taken in the Mid-term review of the CMU Action Plan, Commission services are exploring in an impact assessment the possibility of enhancing the ability of secured creditors of recovering value from collateral in case of borrowers' default on secured loans, with a view to considering a possible legislative initiative.

Accelerated Extrajudicial Collateral Enforcement (AECE) refers to an expedited and efficient out-of-court enforcement mechanism which enables secured creditors (banks) to recover value from collateral granted by companies and entrepreneurs to secure loans. This focus is important as NPLs tend to be lower in Member States where collateral foreclosure periods are shorter. The AECE would operate in relation to existing security rights in the Member States and would enable banks in all Member States to benefit from swift out-of-court procedures to enforce collateral.

The impact assessment is informed by the results of the public consultation<sup>28</sup>, discussions with an Expert Group and a mapping of Member States' systems for out-of-court enforcement of collateral. The latter has been done on the basis of a questionnaire which was sent to the Ministries of Justice of all Member States<sup>29</sup>. On 20 November 2017, Commission services (FISMA and JUST) organised a joint meeting of experts from Member States' ministries of Finance and Justice. The purpose of the meeting was to exchange views with Member States on the possible core features of an AECE and its interaction and possible interference with Member States' private and public laws, including insolvency.

Experts and stakeholders see benefits in measures which would ensure that all Member States have in place out-of-court procedures for collateral enforcement and that the effectiveness of current mechanisms is enhanced to enable banks to recover more value from collateral and in a swifter manner.

Some of the key considerations in the exploratory work are the following:

- i. ensure consistency and complementarity of an AECE with the 2016 Commission proposal on preventative restructuring and second chance frameworks;

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<sup>27</sup> See [https://ec.europa.eu/info/sites/info/files/economy-finance/com\\_825\\_0.pdf](https://ec.europa.eu/info/sites/info/files/economy-finance/com_825_0.pdf).

<sup>28</sup> Public consultation on the development of secondary markets for non-performing loans and distressed assets and protection of secured creditors from borrowers' default.

See [https://ec.europa.eu/info/consultations/finance-2017-non-performing-loans\\_en](https://ec.europa.eu/info/consultations/finance-2017-non-performing-loans_en).

<sup>29</sup> 13 Member States have replied to the questionnaire.

- ii. minimise impact on Member States' private and public laws, including property law, registration rules to transfer property rights or/and to constitute security rights, and insolvency law).
- iii. ensure the protection of corporate borrowers and manage the potential social impact that an AECE would have if it encompassed certain categories of debtors such as natural persons. Therefore, consumers should be excluded from the scope of AECE, and a set of safeguards should be established for corporate borrowers.

Depending on the outcomes of the impact assessment, the Commission may present a proposal for a principle-based framework on Accelerated Extrajudicial Collateral Enforcement as part of its broader package on NPLs.

## **ANNEX 1: INSOLVENCY ISSUES IN 2017 COUNTRY SPECIFIC RECOMMENDATIONS**

**Cyprus, CSR 2:** Increase the efficiency of the judicial system by modernising civil procedures, implementing appropriate information systems and increasing the specialisation of courts. Take additional measures to eliminate impediments to the full implementation of the insolvency and foreclosure frameworks, and to ensure reliable and swift systems for the issuance of title deeds and the transfer of immovable property rights.

**Croatia, CSR 5:** [...] Improve the quality and efficiency of the justice system, in particular by reducing the length of civil and commercial cases.

**Latvia, CSR 3:** Increase efficiency and accountability in the public sector, in particular by simplifying administrative procedures and strengthening the conflict-of-interest prevention regime, including for insolvency administrators.

**Portugal, CSR 4:** [...] Increase the efficiency of insolvency and tax proceedings.

**Slovakia, CSR 3:** [...] Improve the effectiveness of the justice system, including a reduction in the length of civil and commercial cases.

## **ANNEX 2: COUNCIL CONCLUSIONS OF 11 JULY ON AN ACTION PLAN TO TACKLE NON-PERFORMING LOANS IN EUROPE**

### **The Council:**

1. NOTES that the financial crisis and ensuing recessions, together with structural factors, sometimes accompanied by inadequate loan origination practices, have left the banks in some Member States with high ratios of non-performing loans (NPLs);
2. RECOGNISES that although in the majority of Member States high NPL ratios did not emerge in recent years, the negative effects of current high NPL ratios in a substantial number of Member States can pose risks of cross-border spill-overs in terms of the overall economy and financial system of the EU and alter market perceptions of the European banking sector as a whole, especially within the Banking Union;
3. STRESSES that while banks are primarily responsible for restructuring their business models and resolving their NPLs issues in a timely manner, further measures to address the existing stock of NPLs and to prevent the future emergence and accumulation of NPLs would be beneficial for the EU as a whole by contributing to enhanced growth and reducing financial fragmentation;
4. NOTES that, given their magnitude, the current high NPL ratios in some Member States may not decline at a satisfactory pace notwithstanding the context of economic recovery and WELCOMES the steps that have already been taken and significant progress made by certain concerned Member States and EU institutions and bodies to address this legacy issue and prevent its re-emergence; NOTES that supervisors have currently the ability to make use of specific tools, such as where appropriate, assessing incurred or likely losses through proper asset valuations; STRESSES that more efforts are needed to restore NPL ratios to sustainable lower levels and that incentives for all EU credit institutions to deal with NPLs pro-actively should be enhanced while at the same avoiding the disruptive effects of fire sales;
5. EMPHASIZES that EU post crisis regulatory reforms, including steps taken to establish the Banking Union, mark a change of system to protect taxpayers' money, ensure the preservation of financial stability in the euro area and the EU as a whole, and enhance market mechanisms in the banking sector, to which resolution tools and in particular bail-in are essential. Dealing with the issue of NPLs, which may entail lifting impediments to further restructuring in the banking sector, should be consistent with these rules, including Directive 2014/59/EU (BRRD) and State Aid rules;
6. STRESSES that a comprehensive approach combining a mix of complementing policy actions, at national level and at the European level where appropriate, is the most effective way to address the existing stocks of NPLs as well as the emergence and accumulation of new NPLs on bank balance sheets, in particular in all of the four following policy areas: (i) supervision, (ii) structural reforms of insolvency and debt recovery frameworks, (iii) development of secondary markets for distressed assets, and (iv) fostering restructuring of the banking system;



7. WELCOMES therefore the report on NPLs<sup>30</sup> produced by the Subgroup of the Financial Services Committee (NPL Report) and CALLS on Member States, EU institutions, bodies and agencies to take work forward on policy options included therein, on the basis of these Council conclusions;
8. In this context, INVITES in particular:
- the Commission to issue, in summer 2017, an interpretation of existing supervisory powers laid down in EU legislation with a view to clarifying their usability as regards banks' provisioning policies for NPLs under Article 16 of Council Regulation (EU) No 1024/2013 and under Article 104 of Directive 2013/36/EU (CRD IV); following the Commission's interpretation, the Council will, if appropriate and following a full pros and cons analysis, consider an amendment to Article 104 of the CRD IV in the context of the ongoing review of the CRR/CRD IV, in line with policy options set out in the NPL Report;
  - the Commission to consider, within the framework of the ongoing review of the CRR/CRD IV, prudential backstops addressing potential under provisioning which would apply to newly originated loans; these statutory backstops could take the shape of compulsory prudential deductions from own funds of NPL, following an assessment of the most appropriate calibrations in line with international practice;
  - the ECB Banking supervision, together with national competent authorities within the Banking Union, to implement, by the end of 2018, with regard to less significant institutions in the Banking Union a guidance similar to "Guidance to banks on Non-Performing Loans" issued by the Single Supervisory Mechanism (SSM Guidance) for significant institutions, with targeted adaptations where appropriate;
  - the European Banking Authority (EBA) to issue, by summer 2018, general guidelines on NPL management, consistent with the afore mentioned Guidance, with an extended scope applying to all banks in the entire EU;
  - the EBA to issue, by summer 2018, detailed guidelines on banks' loan origination, monitoring and internal governance which could in particular address issues such as transparency and borrower affordability assessment; these guidelines should leverage on existing national experiences where relevant;
  - the European Systemic Risk Board to develop, by the end of 2018, macro-prudential approaches to prevent the emergence of system-wide NPL problems, while taking due consideration of procyclical effects of measures addressing NPLs' stocks and potential effects on financial stability;
  - the EBA, in consultation with the ESMA, and competent authorities to implement, by the end of 2018, enhanced disclosure requirements on asset quality and non-performing loans to all banks;

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<sup>30</sup> doc. 9854/17

- the EBA to issue, by the end of 2017, guidelines for banks on loan tapes monitoring, specifying minimal detailed information required from banks on their credit exposures in the banking book;
  - the EBA, the ECB and the Commission, to propose by the end of 2017, initiatives to strengthen the data infrastructure with uniform and standardised data for NPLs and consider the setting-up of NPL transaction platforms in order to stimulate the development of this secondary market;
  - the Commission to develop, by the end of 2017, in cooperation with all relevant institutions and bodies and taking into account successful national experiences so far, a "blueprint" for the potential set-up of national asset management companies (AMCs), which would set out common principles for the relevant asset and participation perimeters, asset-size thresholds, asset valuation rules, appropriate capital structures, the governance and operational features, both private and public; it should also clarify the permissible design, consistent with the EU legislative framework, including Directive 2014/59/EU (BRRD) and Regulation (EU) No 806/2014 (SRMR) and State Aid rules, for asset relief measures and the use of AMCs;
  - the Commission to develop, by summer 2018, a European approach to foster the development of secondary markets for NPLs, in particular to remove impediments to the transfer of NPLs by banks to non-banks and to their ownership by non-banks, while safeguarding consumers' rights, as well as to simplify and potentially harmonise the licensing requirements for third-party loan servicers and to take legislative initiative in this respect, as appropriate;
  - the Commission to publish, before the end of 2017, the results of the benchmarking exercise on the efficiency of national loan enforcement (including insolvency) regimes from a bank creditor perspective, providing comparable metrics, as precise as possible, for recovery rates, recovery times and recovery costs across Member States, and to further develop the focus on insolvency issues in the European Semester, taking into account on-going reforms;
  - Member States, to consider, while building closely upon the benchmarking exercise, by the end of 2018 to carry out dedicated peer-reviews on insolvency regimes across the EU. acknowledging that legal systems and insolvency frameworks differ widely between Member States;
  - the Commission to further analyse the possibility of enhancing the protection of secured creditors;
9. AGREES to revert to this issue regularly and initially after six months, in order to take stock of the evolution of NPLs in Europe, the restructuring of banking sectors in this context and the development of secondary markets for NPL transactions, to assess the progress made on the basis of a stock-take from the Commission, and to co-ordinate the communication on NPLs in Europe.