ITFA REGULATORY UPDATE – Response To The European Commission Consultation And Collaboration With The IACPM On Non-Payment Insurance Survey 2019 By Silja Calac, ITFA Board Member And Chair Of The Insurance Committee

Response to the European Commission consultation

As many of you will know, ITFA has been engaging in its own advocacy work on behalf of its members and the wider industry, and has been co-operating with Hume Brophy – a Brussels-based consultancy specialised in European public affairs – to ensure that policymakers and regulators are well-versed in the relationship between banking and insurance, and the interests that ITFA represents.

A lot has happened since our last news flash on 16 December, which brought you up to speed on ITFA's involvement in the European Commission consultation.

Our work with Hume Brophy – led by the Insurance Committee's Regulatory Working Group – has been progressing well, and we are pleased to report that on 18 December ITFA issued its response to the European Commission public consultation on 'Implementing the final Basel III reforms in the EU'.
Although the public consultation consisted of as many as 212 questions, ITFA focused its response on six questions, all of which dealt mainly with credit risk insurance (CRI) as a credit risk mitigant (CRM).

ITFA's full response, together with an executive summary of the response, can be downloaded in the member area of the ITFA website.

In short, however, we can reveal that ITFA's stance on this matter is that should the current reforms be implemented, they are likely to have a negative impact on the cooperation between banks and insurers, and, more importantly, on the real economy:

- The Basel Committee's suggestion of a shift from A-IRBA to F-IRBA for exposures to large corporates or FIs in particular **would mean that it would no longer be economically viable for banks** to insure better rated credit risks because of the 45% prescribed Loss Given Default (LGD). (Note that ITFA is arguing for maintaining the present A-IRB approach or adopting a lower LGD floor than 45%.) See Annex 2 below for more details.
- This in turn would impact the insurers' appetite to continue offering credit insurance policies as the risks offered will be much less diversified. Some **insurers may decide to pull out of this business** line entirely. See Annex 1 below for more details.
- Should that happen, **approximately €600bn-worth of support to the real economy is at risk** as CRI is an essential facilitator for lending to the real economy, including enabling the financial sector to offer efficient financing to SMEs. Many European banks will decrease their levels of lending if the risk of non-payment is not mitigated by, and shared with, insurers.

For easy reference, please take a look at the executive summary of our response.

ITFA also included three annexes in its response to the European Commission – these too are available on the ITFA website, and listed here:

Annex 1: Impact analysis on insured corporate lending: This case study shows the impact of using credit insurance on the reduction of Risk Weight. This is a handy tool to demonstrate to the regulator what the consequences would be if banks are no longer able to make use of credit insurance.

Annex 2: Credit insurance and Basel: This was compiled with the help of Hume Brophy and neatly explains what credit insurance is, its importance and unique characteristics, and what the current and future regulatory framework looks like. It also summarise the consequences of non-action, together with ITFA's policy recommendations.

Annex 3: Multiplicity of covers: This takes a closer look at concrete examples of the effect of insurance.

Next steps:

The European Commission will soon table the legislative proposal that will implement Basel into European Law. It is hoped that, with Hume Brophy's help, ITFA will be able to obtain a draft and provide commentary on it. We plan to support the regulator by liaising with all the relevant stakeholders throughout the drafting process so as to avoid any unwanted consequences.

The next stage is that of negotiation, and is likely to begin around June 2020, once preparations have been concluded, and can take anything between 12 and 36 months. During this period the Commission text is on the table and has been sent to the Council of the EU and the European Parliament for negotiation.

The last stage – implementation, likely to occur in 2022 – happens once the CRR III and CRD VI legislative text is published in the official journal. But even then, the process is not over, as the implementation procedure needs to be monitored to ensure that it is carried out correctly.

In the meantime, the Regulatory Working Group is in discussion with key stakeholders in the drafting process to explain ITFA's concerns and suggestions. At the beginning of February, together with Hume Brophy, we met the Financial Services attachés of the Finnish, Irish, French, Danish and Luxembourgish Permanent Representations to the EU.

Collaboration with the IACPM on Non-Payment Insurance Survey 2019

In our lobbying efforts, ITFA is also cooperating closely with the International Association of Credit Portfolio Managers (IACPM), an industry association that seeks to further the practice of credit exposure management. We recently collaborated on a 'Non-payment insurance survey', which many of our members will have seen and provided feedback on.

The survey was conducted as a qualitative benchmarking study on non-payment insurance, and is a continuation of ITFA's Credit Risk Insurance survey conducted last year.

It focused in particular on current general practices and the LGD treatment for Non-Payment Insurance (NPI) policies used by lenders as a CRM tool to release capital.

ITFA is pleased to share the select high-level results of this survey with our members:

- The survey clearly shows that the use of insurance is much more widespread and therefore important for the real economy in Europe than it is in the US.
- In general, the importance of insurance as a credit risk mitigant has grown.
- The main objectives for using insurance are increasing lending capacity and releasing regulatory capital.

- Methodologies to calculate the RWA impact of use of insurance vary substantially.
- Banks use insurance over CDS mainly where no CDS cover is available (mid-size companies, mismatching maturities) – which is often the case in trade finance/transaction banking.