EUROPEAN CENTRAL BANK
BANKING SUPERVISION

Danièle NOUY
Chair of the Supervisory Board

Mr Luke Ming Flanagan
Member of the European Parliament
European Parliament
60, rue Wiertz
B-1047 Brussels

Frankfurt am Main, 23 April 2018

Re: Your letter (QZ021-24)

Honourable Member of the European Parliament, dear Mr Flanagan,

Thank you for your letter on non-performing loans (NPLs) and 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 26 March 2018.

As regards your question on sales of NPLs, the ECB published its Guidance to banks on NPLs[1] in March 2017, setting out the manner in which it expects banks to manage their NPLs. While the ECB expects banks to implement ambitious yet credible strategies in order to resolve their NPL issues, it has not imposed specific reduction targets and has not expressed a preference for certain NPL reduction tools over others. For further details, please refer to my recent letter of reply to MEP Matt Carthy.[2]

Turning to your question on tracker mortgages in Ireland, the SSM Regulation[3] has tasked the ECB with supervising credit institutions from a prudential perspective, while supervisory tasks not conferred on the ECB, including consumer protection[4], remain the responsibility of the national competent authorities. Tracker mortgage-related issues that concern failures by some Irish lenders in their treatment of some customers in respect of these kinds of contract are a matter of consumer protection. Accordingly, consumer protection-related issues on tracker mortgages do not fall under the supervisory tasks conferred on the ECB but within the national mandate of the Central Bank of Ireland.

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

2 https://www.bankingsupervision.europa.eu/ecb/pub/pdf/ssm.mepletter180321_Carthy.en.pdf.

3 Council Regulation (EU) No 1024/2013.

4 Recital 28 of the SSM Regulation.

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As I stated in my letter of 8 November 2017 to the Members of the Irish Parliament, Deputy John McGuinness and Deputy Michael McGrath[5], failures by credit institutions to comply with their obligations towards their customers may have prudential implications and may therefore raise supervisory concerns for the ECB. Such concerns include those relating to cases where there could be financial implications for credit institutions, which may be required to pay compensation for the damage suffered by their customers and which may become subject to sanctions from the Central Bank of Ireland, in its role as a consumer protection authority, for breaching their contractual obligations towards their clients. These issues therefore trigger concerns on whether banks hold sufficient capital against operational/conduct risk and whether any potential material impact is foreseen on banks' liquidity positions, as well as the adequacy of banks' governance and internal controls in preventing misconduct. Any matters that may have prudential implications are assessed under the ECB's Supervisory Review and Evaluation Process (SREP) and may lead to measures to address supervisory concerns. These measures are distinct in nature from conduct supervision, which strives to detect, correct and sanction any type of misconduct by banks in the market.

You also raised the issue of Irish credit institutions charging interest rates that are several percentage points above the euro area average, and you refer to "cartel-type behaviour". You enquired whether the ECB will start an investigation under the SREP with a view to probing these possible illegalities. The ECB, as the competent authority for the prudential supervision of credit institutions, engages with supervised institutions on all prudential aspects of risk. However, any instances of sustained market-wide rent extraction and related exceptional profits are matters for the market and competition authorities to investigate.

Furthermore, you asked whether the ECB will examine the role of all those in senior positions in all Irish banks who were involved in the tracker mortgage scandal and establish the identities of those who made the decisions that resulted in mortgage holders being overcharged. The suitability ("fit and proper") criteria set out in Capital Requirements Directive IV (CRD IV)[6] need to be fulfilled at all times by the members of the management body of a credit institution. The ECB performs the fit and proper assessment of such members according to the requirements set out in Article 91 of CRD IV – and of the transposition of those requirements into national law. Finally, you enquired about the relationship between the profitability of a bank that is not supervised by the ECB and the dividend paid by a fully consolidated subsidiary which is subject to ECB supervision. 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 CRD IV. Accordingly, I cannot comment on the situation of specific supervised entities or supervisory measures taken or to be taken with respect to them.

Without commenting on individual institutions and their actions, it must be noted that, under the consolidated method of accounting, intra-group dividend payments are treated only as internal transfers of cash and do not contribute to the financial result of the group as whole.

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[5] https://www.bankingsupervision.europa.eu/ecb/pub/pdf/ssm.mepletter171108_McGuinness_McGrath.en.pdf.

[6] Directive 2013/36/EU of the European Parliament and of the Council.

More generally, as laid down in its recommendations of 13 December 2016[7] and 28 December 2017[8], the ECB recommends that banks under its supervision should establish dividend policies using conservative and prudent assumptions in order to satisfy the applicable capital requirements and the outcomes of the SREP. At the same time, banks complying with prudential requirements are only encouraged to distribute dividends in a conservative manner to enable them to continue to fulfil all the requirements and outcomes of the SREP, even if economic and financial conditions have deteriorated.

Yours sincerely,

Danièle Nouy

[7] https://www.bankingsupervision.europa.eu/banking/letterstobanks/shared/pdf/2016/dividend_distribution_2016.en.pdf.

[8] https://www.bankingsupervision.europa.eu/banking/letterstobanks/shared/pdf/2018/Recommendation_ECB201744_on_dividend_distribution_policies.en.pdf.