

The European Market for Non-
Performing Loans:

EVOLUTION AND FUTURE PROSPECTS

September 2024

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LIST OF ABBREVIATIONS AND DEFINED TERMS

ABS	Asset-Backed Securities
CAGR	Compound Annual Growth Rate
CRR	Regulation (EU) No 575/2013 of the European Parliament and of the Council of 26 June 2013 on prudential requirements for credit institutions and amending Regulation (EU) No 648/2012
DLT	Distributed Ledger Technology
EBA	European Banking Authority
ECB	European Central Bank
EDW	European DataWarehouse
ESMA	European Securities and Markets Authority
EU	European Union
GACS	Garanzia Cartolarizzazione Sofferenze (Italian guarantee on securitisation of non-performing loans)
GDPR	Regulation (EU) 2016/679 of the European Parliament and of the Council of 27 April 2016 on the protection of natural persons with regard to the processing of personal data and on the free movement of such data, and repealing Directive 95/46/EC
GFC	Global Financial Crisis in 2008
GLS	Regulation (EU) No. 575/2013
ITS	Commission Implementing Regulation (EU) 2023/2083 of 26 September 2023 laying down implementing technical standards for the application of Article 16(1) of Directive (EU) 2021/2167 of the European Parliament and of the Council with regard to the templates to be used by credit institutions for the provision to buyers of information on their credit exposures in the banking book
NPE	Non-Performing Exposures
NPL	Non-Performing Loan
NPL Transaction Data Templates	Templates to be used by credit institutions for the provision of information referred to in Article 15(1) of Directive (EU) 2021/2167 in order to provide detailed information on their credit exposures in the banking book to credit purchasers for the analysis, financial due diligence and valuation of a creditor's rights under a non-performing credit agreement, or the non-performing credit agreement itself established by the Commission Implementing Regulation (EU) 2023/2083 of 26 September 2023

PwC	PricewaterhouseCoopers
Commission Delegated Regulation (EU) 2018/171	Commission Delegated Regulation (EU) 2018/171 of 19 October 2017 on supplementing Regulation (EU) No 575/2013 of the European Parliament and of the Council with regard to regulatory technical standards for the materiality threshold for credit obligations past due
SFTP	Secure File Transfer Protocol
Secondary Market Directive	Directive (EU) 2021/2167 of the European Parliament and of the Council of 24 November 2021 on credit servicers and credit purchasers and amending Directives 2008/48/EC and 2014/17/EU
SPV	Special Purpose Vehicle
TUB	Testo Unico Bancario (Italian Consolidated Law on Banking and Credit)
UtP	Unlikely to Pay (the debtor is assessed as unlikely to pay when its credit obligations in full without realisation of collateral, regardless of the existence of any past-due amount or of the number of days past due)

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EXECUTIVE SUMMARY

The European market for NPLs has undergone significant transformation over the past decade, driven by evolving regulatory frameworks, market dynamics, and technological advancements.

The aim of this report (the “Report”) is to provide a comprehensive analysis of the current state of, and future prospects for, the EU NPL market, with a particular focus on Italy, a key market for one of the most impacted Member States by the Secondary Market Directive. The particular focus on the Italian market derives from the historical high stock of NPLs in banks’ banking books, managed with innovative State initiatives such as GACS, adopted also by Greece with some key differences.

The EU adopted the Secondary Market Directive in 2021, and it is currently being implemented by Member States to address the reduction of the NPL stock. The Directive aims to harmonise standards across the European Union and enhance financial stability. Particularly, the NPL Transaction Data Templates, developed by EBA, are aimed at further enhancing transparency with a view to increase secondary market transactions.

Since the GFC, European banks have significantly reduced the amount of distressed credit on their balance sheets, with Italy at the forefront of this shift, observing a notable decline from a peak of approximately €400 billion in 2015 to €56 billion by mid-2023.

The de-risking process, however, has led to the transfer of NPLs from banking books to investors’ portfolios, indicating the need for ongoing management and recovery strategies via servicers. Securitisation and particularly the GACS scheme heavily supported this shift in Italy.

Looking forward, the NPL market in the EU is expected to continue evolving with further regulatory developments and technological innovations. The focus will likely remain on enhancing market liquidity, improving data quality, and ensuring a consistent secondary market for NPL sales, taking into consideration the existing differences in the insolvency laws across jurisdictions.

The Report is divided in three chapters:

- Chapter 1 presents the current EU regulatory framework and the Italian legal framework.
- Chapter 2 highlights the past and current trends in the Italian NPL market.
- Chapter 3 proposes a solution for the effective implementation of the EBA NPL Transaction Data Templates across the EU.

INTRODUCTION

The European market for NPLs has been a focal point of financial stability efforts over the past decade. The aftermath of the GFC saw a significant accumulation of distressed assets on the balance sheets of European banks, particularly in countries like Italy and Greece. To address this issue, the EU has implemented a series of regulatory measures aimed at reducing NPL volumes and improving workout solutions and market conditions.

Securitisation has been one of the main tools used for asset sales, especially making use of State guarantees, such as the GACS (in Italy) and HAPS (in Greece) regimes. This helped in shifting NPLs from banks' balance sheets to private investors and servicers, therefore improving the quality of banks' capital ratios.

To revive secondary market sales of distressed assets and portfolios from one investor to another, the quality and availability of data is essential. For this reason, the EBA implemented a set of common templates for the disclosure of information for NPL portfolio sales.

This Report provides a detailed analysis of the current state and future prospects of the NPL market within the EU. It examines the regulatory landscape, market trends, and technological advancements that have shaped the market. Taking into consideration the lessons learned from NPL securitisation, the Report focuses on how best to implement the NPL Transaction Data Templates for portfolio sales.

By delving into the evolution of the NPL market, particularly in Italy, and analysing the impact of the Secondary Market Directive and the upcoming national transposition laws, this Report seeks to provide a holistic view of the challenges and opportunities within the NPL space. It aims to guide stakeholders in navigating the complex landscape of NPL management and securitisation, ultimately contributing to a more resilient and efficient financial system.

CHAPTER 1: EU AND NATIONAL REGULATORY REQUIREMENTS APPLICABLE TO NPLS

1. THE EUROPEAN UNION REGULATORY FRAMEWORK FOR NPLS

According to EU legislation, a bank loan is considered non-performing when more than 90 days pass without the borrower paying the agreed instalments or interest. This definition stems from Articles 47a.3(a) and 178.1.b) of the CRR -respectively- according to which:

Article 47.a.3(a)

For the purposes of point (m) of Article 36(1), the following exposures shall be classified as non-performing:

*(a) **an exposure in respect of which a default is considered to have occurred in accordance with Article 178;***

Article 178.1.b)

***the obligor is more than 90 days past due on any material credit obligation to the institution, the parent undertaking or any of its subsidiaries.** Competent authorities may replace the 90 days with 180 days for exposures secured by residential property or SME commercial immovable property in the retail exposure class, as well as exposures to public sector entities. The 180 days shall not apply for the purposes of point (m) Article 36(1) or Article 127.*

The asset quality issues and the policy requirement to deal with NPLs for the purposes of financial stability and economic growth became particularly acute in the aftermath of the GFC.¹

In July 2017, the Council of the European Union adopted an action plan to reduce stocks of NPLs and prevent their future emergence (the “2017 Action Plan”). In particular, the 2017 Action Plan aimed to address the high levels of NPLs on European banks’ balance sheets after the financial crisis, providing a structured approach to reduce the NPL stock, enhance financial stability, and foster economic growth. The Action Plan emphasised the need for robust NPL management strategies, regulatory harmonisation, and the development of secondary markets for NPL transactions.²

The 2017 Action Plan built on the report of the Financial Services Committee (FSC) Subgroup on Non-Performing Loans, an expert group established in July 2016 to “assess the state of play regarding current NPL stocks and related developments in Member States and at EU level, as well as the relevant legal framework at national and EU level” and to “deliver possible options supporting a significant and sustainable reduction of NPL levels, based on the current diverse situations assessed”. The report of the FSC Subgroup on Non-Performing Loans included a range of policy objectives and recommendations that laid the foundations for the EU legislative developments in the following years.

¹ Single Resolution Board speech, Naples, 2023 Conference, available at: <https://www.srb.europa.eu/system/files/media/document/20230627%20The%20evolution%20of%20NPLs%20-%20final.pdf>

² <https://www.consilium.europa.eu/en/press/press-releases/2017/07/11/banking-action-plan-non-performing-loans/>

More specifically, the report of the FSC Subgroup on Non-Performing loans proposed:

1. Enhancing supervisory tools to address the management of NPLs by banks;
2. Promoting structural reforms of insolvency and debt recovery frameworks;
3. Developing secondary markets in Europe for NPL transactions;
4. Fostering the restructuring of banks and European banking sectors in the context of NPL resolution.

Since the issuance of the 2017 Action Plan, the Commission periodically assessed the implementation of the Action Plan. In fact, four progress reports were issued, on 18 January 2018 (first progress report); on 14 March 2018 (second progress report); on 28 November 2018 (third progress report); and on 12 June 2019 (fourth progress report). The fourth progress report showed that the 2017 Action Plan had generally been successfully implemented (see Figure 1).

No.	Initiative of the Action Plan	No.	Initiative of the Action Plan
1	Interpretation of existing supervisory powers in EU legislation as regards NPL provisioning	8	Improving loan tape information required from banks
2	Addressing potential under provisioning, via automatic and time-bound provisioning	9	Strengthening data infrastructure for NPLs, including potential transaction platforms
3	Extend Single Supervisory Mechanism NPL guidelines to small banks	10	Develop a Blueprint for asset management companies
4	Adopting EU-wide management guidelines for non-performing exposures	11	Develop secondary markets for NPLs
5	New guidelines on banks' loan origination, monitoring and internal governance	12	Benchmarking of national loan enforcement and insolvency frameworks
6	Develop macroprudential approaches to tackle the build-up of future NPLs	13	Develop the focus on insolvency issues in the European Semester
7	Enhanced disclosure requirements on asset quality and NPLs for all banks	14	Enhancing the protection of secured creditors

Accomplished

Imminent

Ongoing

Figure 1: Progress in implementing the 2017 Action Plan

Source: Communication from the Commission to the European Parliament, the European Council, the Council and the European Central Bank. Fourth Progress Report on the reduction of non-performing loans and further risk reduction in the Banking Union

In December 2020, the European Commission presented a new action plan focused on tackling NPLs in the aftermath of the COVID-19 pandemic (the “2020 Action Plan”). The plan aimed to ensure that European businesses and households continue to have access to the funding they need, throughout the pandemic crisis. The 2020 Action Plan strategy revolved around four goals:

1. Further developing secondary markets for distressed assets, which will allow banks to move NPLs off their balance sheets, while ensuring further strengthened protection for debtors;
2. Reforming the EU’s corporate insolvency and debt recovery legislation, which will help converge the various insolvency frameworks across the EU, while maintaining high standards of consumer protection;
3. Supporting the establishment and cooperation of national asset management companies (AMCs) at EU level;

4. Implementing precautionary public support measures, where needed, to ensure the continued funding of the real economy under the EU's Bank Recovery and Resolution Directive and State aid frameworks.

The 2020 Action Plan was followed by a targeted consultation on improving transparency and efficiency in secondary markets for NPLs, launched by the European Commission in June 2021, for the purpose of collecting market feedback on the remaining obstacles to the proper functioning of secondary markets for NPLs as well as possible enabling actions that the Commission could take to foster these markets by improving the quantity, quality, and comparability of NPL data.

In June 2021 the European Commission also set up the NPL Advisory Panel, which was established as an informal Commission expert group to provide expert feedback and advice to the Commission on the measures regarding the development of NPL secondary markets.³

On 8 December 2021 the Secondary Market Directive was published in the Official Journal of the European Union. The Directive aimed at culminating initiative number 11 of the 2017 Action Plan, fostering secondary markets by means of removing impediments to, and laying down safeguards for, the transfer of NPLs by credit institutions to credit purchasers, while at the same time safeguarding borrowers' rights.

The Secondary Market Directive defined the European Union regulatory framework for both purchasers and servicers of non-performing credit agreements issued by credit institutions and set the scene for the adoption of the first mandatory NPL Transaction Data Templates in September 2023.

Other key EU laws relevant for NPLs include Directive 2013/36/EU (Capital Requirements Directive IV) and Directive 2014/59/EU (Bank Recovery and Resolution Directive).

1.1 The Secondary Market Directive

The Secondary Market Directive⁴ was published in the Official Journal of the European Union on 8 December 2021, entering into force on 28 December 2021. The Directive establishes the regulatory framework for the sale and purchase and servicing of non-performing loans, laying down a common framework and requirements for:

- a. credit servicers of a creditor's rights under a non-performing credit agreement, or of the non-performing credit agreement itself, issued by a credit institution established in the Union, who act on behalf of a credit purchaser (Title II);
- b. credit purchasers of a creditor's rights under a non-performing credit agreement, or of the non-performing credit agreement itself, issued by a credit institution established in the Union (Title III).

3 The activity of the NPL Advisory Panel has resulted, amongst others, in the issuance of a paper on further developing secondary markets for non-performing loans: the role of securitisation. The paper is available at: https://finance.ec.europa.eu/document/download/4f537f03-1193-41b8-b06f-97ba84cb7f74_en?filename=2311-npl-advisory-panel-securitisation-paper_en.pdf

4 Directive (EU) 2021/2167 of the European Parliament and of the Council of 24 November 2021 on credit servicers and credit purchasers and amending Directives 2008/48/EC and 2014/17/EU, available at: <https://eur-lex.europa.eu/legal-content/en/TXT/?uri=CELEX%3A32021L2167>

In particular, the Secondary Market Directive imposes new disclosure requirements to banks selling NPLs. Article 15 of the Directive details the information obligations, both before and after the sale of NPLs.

Right to information regarding a creditor's rights under a non-performing credit agreement or the non-performing credit agreement itself (Article 15)

The Secondary Market Directive requires banks selling NPLs to credit purchasers to disclose to the prospective purchaser the necessary information regarding the creditor's rights and any collateral to enable the prospective purchaser to assess the value of those rights and the likelihood of recovery. The information must be made available according to the content and format prescribed by the NPL Transaction Data Templates issued through Commission Implementing Regulation (EU) 2023/2083.

The rationale behind the disclosure obligations to prospective buyers is that before purchasing impaired credit contracts, prospective purchasers should have access to granular information at the level of each individual credit contract concerning the impaired credit itself, the counterparties, real guarantees, legal and enforcement procedures, and the history of recoveries and repayments.

After the sale of NPLs, banks will also have to report details of their sales to their home state authority and to authorities in the relevant host Member State (biannually or, if required by the authority, quarterly). The disclosures with details of sales will include:

- a. the legal entity identifier (LEI) of the credit purchaser or, where applicable, of its representative designated in accordance with Article 19 of the Directive, or where such identifier does not exist, of:
 - the identity of the credit purchaser or of the members of the credit purchaser's management or administrative organ and the persons who hold qualifying holdings in the credit purchaser within the meaning of Article 4(1), point (36), of Regulation (EU) No 575/2013; and
 - the address of the credit purchaser or, where applicable, its representative designated in accordance with Article 19 of the Directive;
- b. the aggregate outstanding balance of the creditor's rights under the non-performing credit agreements or of the non-performing credit agreements transferred;
- c. the number and size of the creditor's rights under the non-performing credit agreements or of the non-performing credit agreements transferred; whether the transfer includes the creditor's rights under the non-performing credit agreements, or the non-performing credit agreements themselves, concluded with consumers and the types of assets securing the non-performing credit agreements, when applicable.

Obligations of credit purchasers (Article 17)

In addition, the Secondary Market Directive imposes certain obligations on credit purchasers, namely, to:

- Comply with certain obligations as to the fair treatment of borrowers of NPLs;
- Notify their Member State of any appointment of a credit servicer or an EU bank or EU supervised consumer credit or mortgage creditor to service their NPLs;
- Report sales of NPLs to their Member State authority (biannually or, if required by the authority, quarterly).

Obligations of credit servicers (Title II)

The Secondary Market Directive requires credit servicers to be authorised by an EU national supervisory authority in their EU home Member State and only EU entities will be able to obtain this authorisation. Pursuant to Article 13 of the Directive, authorised credit services are allowed to provide services across the EU without the need to obtain additional authorisations in other Member States.

Credit servicers will be subject to ongoing obligations when servicing NPLs on behalf of credit purchasers, including obligations regarding:

- the fair treatment of both consumer and commercial borrowers, including complaints handling processes (Article 10);
- information to borrowers about the purchase of the loan by their credit purchaser;
- the terms of their agreement with the credit purchaser (Article 10);
- the holding of client funds (Article 6);
- outsourcing to third parties (Article 12).

Article 2.5 of the Secondary Market Directive specifies that the Directive does not apply to the servicing of a creditor's rights under a credit agreement, or of the credit agreement itself, carried out by:

- a credit institution established in the European Union;
- an alternative investment fund manager (AIFM) authorised or registered in accordance with Directive 2011/61/EU, or a management company, or an investment company authorised in accordance with Directive 2009/65/EC provided that the investment company has not designated a management company under that Directive, on behalf of the fund it manages;
- or a non-credit institution subject to supervision by a competent authority of a Member State in accordance with Article 20 of Directive 2008/48/EC or Article 35 of Directive 2014/17/EU when performing activities in that Member State.

The Directive also does not apply to the servicing of a creditor's rights under a credit agreement, or of the credit agreement itself, that was not issued by a credit institution established in the Union, except where the creditor's rights under the credit agreement, or the credit agreement itself, is replaced by a credit agreement issued by such credit institution; to the purchase of a creditor's rights under a non-performing credit agreement, or of the non-performing credit agreement itself, by a credit institution established in the Union; and to the transfer of a creditor's rights under a credit agreement, or of the credit agreement itself, transferred before 30 December 2023.

As of June 2024, the transposition status of the Secondary Market Directive is 37% (see Figure 2 below). According to European Commission website information, 10 Member States have fully transposed the Secondary Market Directive. Some other Member States have communicated partial transposition measures to the European Commission, and the majority of Member States have not communicated any transposition measures yet.

Due to the lack or delay of the notification of national transposition measures or their incompleteness, an infringement proceeding for non-communication of the national transposition measures is pending against some EU Member States.

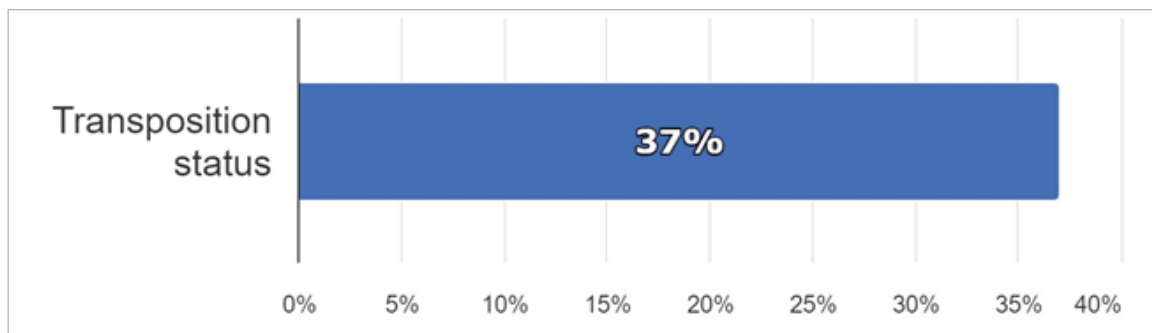


Figure 2: Secondary Market Directive transposition status as of 19 August 2024

Source: European Commission https://finance.ec.europa.eu/credit-servicers-and-credit-purchasers-directive_en

1.2 The NPL Transaction Data Templates

On 29 September 2023, the Commission Implementing Regulation (EU) 2023/2083 of 26 September 2023 was published in the Official Journal of the European Union. It lays down implementing technical standards for the application of Article 16(1) of Directive (EU) 2021/2167 of the European Parliament and of the Council with regard to the templates to be used by credit institutions for the provision to buyers of information on their credit exposures in the banking book. The ITS entered into force on 19 October 2023.

In summary, the ITS is aimed at implementing the transparency requirements imposed by the Secondary Market Directive at the pre-sale stage and applies to the sales and transfers by credit institutions established in the Union of credit agreements that are classified as non-performing exposures in accordance with Article 47a of Regulation (EU) No 575/2013 of the European Parliament and of the Council, that those credit institutions hold in their banking book.

As explained in the recitals of the ITS, before purchasing non-performing credit agreements, prospective buyers should have access to granular credit-agreement-by-credit-agreement information about the non-performing credit agreement itself, the counterparty, the collateral, the guarantees, the legal and enforcement procedures and the historical collection and repayment history. The standardisation of that information by means of common templates, data fields, definitions, and characteristics should facilitate the sale of non-performing credit agreements on secondary markets and should reduce entry barriers for small credit institutions and smaller investors wishing to conclude transactions in respect of non-performing credit agreements.

Credit institutions should use the NPL Transaction Data Templates for non-performing credit agreements when selling or transferring non-performing credit agreements that are included in a portfolio for sales or transfers, in order to provide prospective buyers with all necessary information thereby enabling them to properly assess the value of the creditor's rights under

the non-performing credit agreement, or of the non-performing credit agreement itself, and the likelihood of recovery of the value. Applying the NPL Transaction Data Templates to credit agreements would also reduce information asymmetries between prospective buyers and sellers of credit agreements and, thus, contribute to the development of a functioning secondary market in the Union. Credit institutions should use the NPL Transaction Data Templates in sales or transfers of such credit agreements involving a change to the lender of record under the credit agreement concerned.

To respect the principle of proportionality, the transaction data templates for impaired credit contracts should require different information depending on the nature and size of the impaired credit contracts and should specify the data fields that must be filled or specify cases where filling certain data fields is not mandatory. Based on the principle of proportionality too, credit institutions should not be obligated to fill all the data fields of the transaction data templates for all transactions. Such operations should involve the sale or transfer of:

1. A single impaired credit contract;
2. Several impaired credit contracts linked to a single debtor;
3. Impaired credit contracts that are part of syndicated credit lines;
4. Impaired credit contracts linked to a debtor domiciled outside the Union;
5. Impaired credit contracts that have been acquired by an entity that is not a credit institution, as in such circumstances credit institutions may not have all the information necessary to complete all data fields;
6. Impaired credit contracts concluded with natural persons, in cases where such operations concern small unsecured credit contracts that do not fall within the scope of Directive 2008/48/EC; and
7. Sale or transfer of impaired credit contracts between credit institutions belonging to the same group.

To enable potential buyers of impaired credit contracts to perform financial due diligence and assess the impaired credit contracts before concluding a purchase and sale transaction and committing to a specific price, credit institutions should provide potential buyers with all necessary information at a sufficiently early stage of the sales process.

However, the ITS requires that the right to access such information is balanced with the confidentiality and personal data protection safeguards. As such, considering the level of detail of such information and the related confidentiality implications, credit institutions should only provide such information to potential buyers who are seriously interested in purchasing the impaired credit contracts in question. For data protection reasons, credit institutions should be authorised to provide personal data only in cases where it is necessary to identify individuals whose credit contracts are impaired and in compliance with the GDPR.

The information necessary for potential buyers of impaired credit contracts to perform financial due diligence and assess such credit contracts may contain elements that credit institutions consider confidential based on legal confidentiality obligations or commercial considerations. They are therefore required to determine which data fields should be considered confidential and should ensure that all confidential information is shared through secure channels and only after the conclusion of appropriate confidentiality agreements between the credit institution and the potential buyer. The ITS suggests the use of electronic virtual data rooms as potentially secured channels to transfer the relevant information.

The NPL Transaction Data Templates issued through the ITS consist of five different data templates covering the following categories of information (Article 3 of the ITS):

a. Template 1: Counterparty information

Template 1 provides the information necessary to identify the counterparty where that counterparty may assume the role of 'borrower' or 'protection provider' in relation to different loan contracts. The counterparty may, in turn, be a private individual or a corporate. Where the counterparty is a corporate, it may or may not be part of a counterparty group. In addition, Template 1 covers some information on any insolvency or restructuring proceedings to which the counterparty is subject. Credit institutions shall provide further information on any legal proceeding in relation to a particular loan in Template 3.

b. Template 3: Credit agreement information

Template 3 provides information on the contractual loan agreement, including any lease agreement and forbearance measure granted. In addition, Template 3 covers information on any legal proceeding referred to the loan, including, among others, the legal status, the stage reached in legal proceedings and the date of initiation of legal proceedings.

c. Templates 4.1: Collateral, guarantee and enforcement information

Template 4.1 provides information on any collateral, including immovable and movable property collateral, and guarantees which secure a loan. In addition, the Template covers relevant information on any applicable enforcement procedure.

Credit institutions that are a lessee in a lease contract shall provide information on any lease asset (i.e., right-of-use assets) recognised in their financial statements in accordance with the applicable accounting standards.

Credit institutions shall also provide the latest estimated value of any collateral before or at the cut-off date. The latest estimate value may be calculated either internally by the credit institution, or by an external valuer. Credit institutions shall provide the latest evaluation (internal or external), when it is available. When both internal and external valuations are available, credit institutions may provide the prospective buyer with both values with the related valuation dates.

d. Template 4.2: Mortgage guarantee information

Template 4.2 is an add-on to Template 4.1. In case of mortgage guarantees, credit institutions shall provide the information on "mortgage amount", "lien position", and "higher ranking loan" in Template 4.2.

e. Template 5: Historical collection of repayments information

Template 5 provides information on the historical collection for each loan before the cut-off date, including when the credit institution has used an external collection agent.

Credit institutions shall aggregate the total historical repayment amounts per month and present those amounts in separate columns, covering a minimum period of 36 months before the cut-off date.

In addition to the five "substantial" templates, a sixth template (Template 2) provides the relationship between Template 1 and the other templates by using unique identifiers applied to each counterparty, loan, mortgage guarantee and protection. Credit institutions shall specify those identifiers at the cut-off date to identify the non-performing loan that is subject to a sale or transfer transaction.

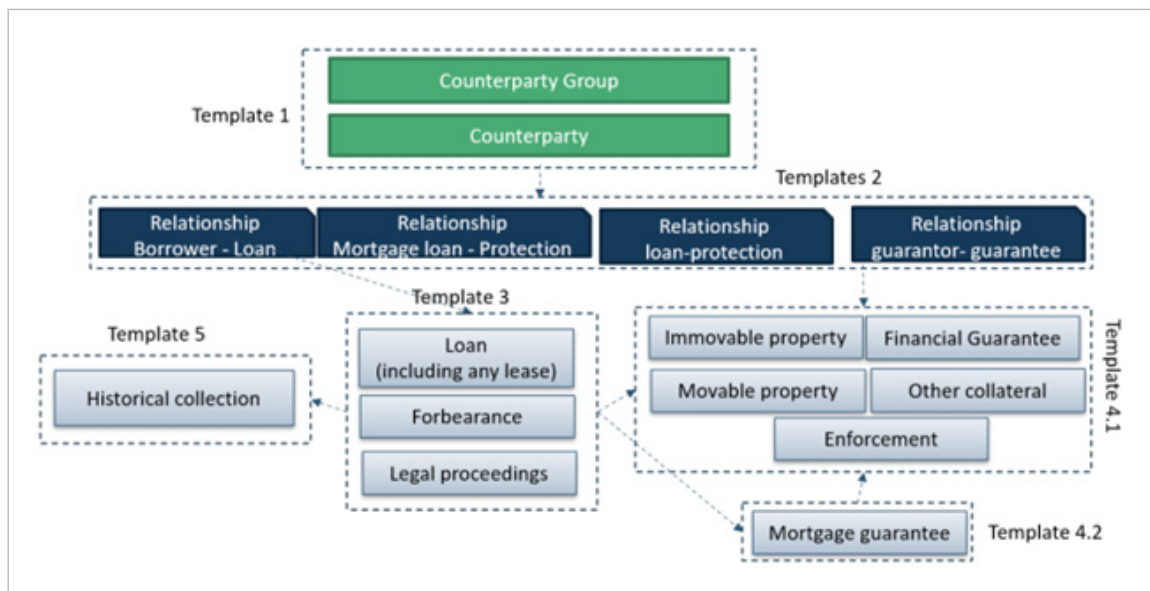


Figure 3: NPL Transaction Data Templates
Source: EBA Final Report on the draft ITS

Finally, the ITS provides guidance on the provision of the required information under each template through a data glossary (Annex 2 of the ITS) and the specific instructions for each template.

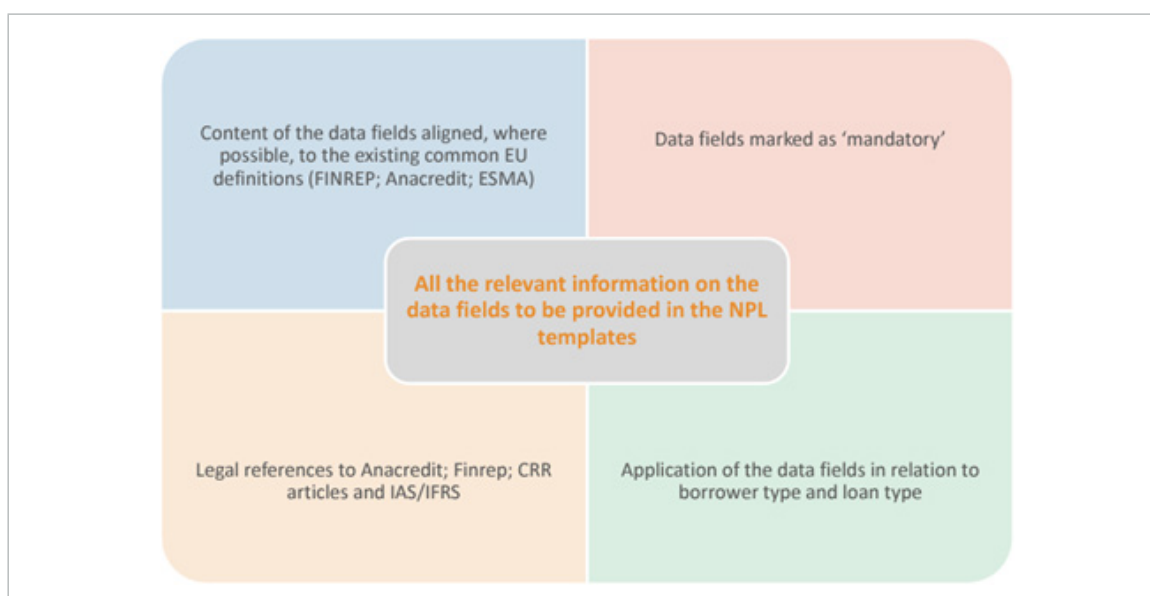


Figure 4: Summary of the data glossary of NPL Transaction Data Templates
Source: EBA slides presented at EDW Webinar "The new EBA NPL data Templates: Scope, implementation, and market benefits", of 31 January 2023

1.3 GAP analysis between the ESMA Templates and the NPL Transaction Data Templates

The preparation of the ITS was entrusted to the EBA, who published its final report ⁵ on the draft ITS on 16 December 2022, based on the experience gained with the use of the voluntary NPL transaction data templates that the EBA developed in 2017-2018 and reflecting the industry feedback with regard to the use of these templates and wider market practices. The EBA collected these experiences whilst developing the Discussion Paper that was published in May 2021 and during the public consultation on that Discussion Paper.

⁵ Implementing regulation - 2023/2083 - EN - EUR-Lex (europa.eu).

In its final report, the EBA explained that they aimed to further streamline the data fields and clarify their definitions and use in response to the comments made during the public consultation to ensure that the relevant data fields were closely aligned with market practices and meet the needs of prospective buyers for their financial due diligence and valuation before entering into a sale-purchase contract.

In the context of streamlining reporting requirements, key similarities have been found⁶ between the disclosure requirements under the technical standards on disclosure requirements under Regulation (EU) 2017/2402 (ESMA Templates) and the NPL Transaction Data Templates.

The application of the ESMA or EBA Templates depends on the type of transaction. Table 1 below highlights the reporting frameworks under the EBA and ESMA Templates by type of assets. In the case of securitisation of NPLs, financial institutions should use the ESMA Templates with the add-on of Annex 10, while for the case of straight sales the EBA Templates should be used.

Type o Asstes	Reporting Framework for Securitisation	Reporting Framework for Straight Sale
Performing Loans	ESMA Templates	—
Non-performing loans (NPL)	ESMA Templates with Add-on Annex 10	EBA Templates
Homogeneous NPL pool	One ESMA Annex with Add-on Annex 10	EBA Templates
Non-Homogeneous NPL pool	Multiple ESMA Annexes with Add-on Annex 10	EBA Templates

Table 1: Reporting frameworks under the EBA and ESMA Templates by type of assets

Source: NPL Transaction Data Templates, ESMA Templates and European DataWarehouse assessment

As shown in Table 2, the NPL Transaction Data Templates contain 129 fields, of which 69 are mandatory (excluding 5 identifiers). 71 potential correspondences between the ESMA Templates and the NPL Transaction Data Templates have been identified.

⁶ A GAP analysis was conducted by European DataWarehouse in 2022, analysing the convergences and divergences between the two reporting regimes. More information is available here: <https://eurodw.eu/edw-conducts-gap-analysis-on-the-proposed-eba-npl-templates/>

Template	Number of fields	Number of fields with potential correspondence
1 - Counterparty	33	14
2 - Relationship	4	3
3 - Loan	44	21
4 - Collateral guarantee and enforcement	43	28
4.2 - Mortgage Guarantee	5	4
5 - Historical collection of repayments	5	1
Total number of fields	134	71

Table 2: Number of data fields and potential correspondences NPL Transaction Data Templates vs ESMA Templates
Source: European DataWarehouse analysis

With a view of further simplifying the Template and facilitating NPL transactions, EBA removed the existing “No data option” approach in the ESMA Templates, considering the disclosure of the reason for the missing information to be irrelevant (Table 3). Additionally, EBA removed the differentiation of mandatory/non-mandatory fields depending on the size of the loan.

No Data Field Option	EBA Templates May 2022	ESMA Templates
ND1	Data not collected by the credit institution	Data not collected as not required by the lending or underwriting criteria
ND2	Data collected but not loaded into the credit institution's reporting system or loaded into a separate system from the credit institution's reporting system	Data collected on underlying exposure application but not loaded into the originator's reporting system
ND3	Data collected but only available from DD-MM-YYYY (DD-MM-YYYY must be completed)	Data collected on underlying exposure application but loaded onto a separate system from the originator's reporting system

No Data Field Option	EBA Templates May 2022	ESMA Templates
ND4	Data field not applicable in relation to the under-writing criteria specified in the description of the data field or in relation to the borrower type or the loan type	ND4-YYYY-MM-DD Data collected but will only be available from YYYY-MM-DD (YYYY-MM-DD shall be completed)
ND5		Required information is not applicable to the item being reported

Table 3: Options to report No Data in the proposed EBA templates (May 2022) and the ESMA Templates. The No Data option was finally discarded in the NPL Transaction Data Templates adopted through the ITS.

Sources: EBA Templates, ESMA Templates and European DataWarehouse analysis

2. THE ITALIAN LEGAL FRAMEWORK FOR NPLS

The Italian legal framework for NPLs is regulated by the Consolidated Banking Act (Testo Unico Bancario), which regulates, amongst others, the authorisation and activities of financial intermediaries and defines the entities authorised to purchase NPLs, such as banks, financial companies, and other intermediaries.

Further to the Consolidated Banking Act, special legislation such as the Decree Law no. 59/2016 (Decreto Legge 59/2016), Legislative Decree no. 180/2015 (Decreto Legislativo 180/2015) Notice (Circular) no. 285 of 2013 from the Bank of Italy sets forth specific measures for the management and recovery of NPLs, including reforms to bankruptcy and insolvency procedures; provisions regarding the management and resolution of distress loans within banks; and guidelines on transparency and disclosure requirements for banks selling NPLs.

According to the Bank of Italy, NPLs can be classified in three different types of categories:

- “Esposizioni scadute e/o sconfinanti deteriorate” (literally, expired and/or overdrawn exposures): are credits that have expired or exceeded credit limits for more than 90 days and beyond a certain threshold of relevance.
- “Inadempienze probabili” (literally, likely to default) are the next step, in which the bank deems it unlikely that the debtor will fully meet their contractual obligations unless actions such as the execution of guarantees are taken by the credit institution.
- “Sofferenze” (literally, distressed credits) are credits towards subjects in a state of insolvency or in substantially equivalent situations.

2.1 Subjects authorised to purchase NPLs in Italy

The decree No. 53 of April 2, 2015, issued by the Italian Ministry of Economy and Finance, defines what constitutes a financial activity and what is a reserved activity.

The activity of granting financing in any form includes the provision of loans, as well as the

issuance of credit substitute guarantees and signature commitments. This activity includes, among others, every type of financing provided in the form of:

- a. Financial leasing;
- b. Purchase of credits;
- c. Consumer credit, as defined by Article 121, T.U.B. (Testo Unico Bancario, i.e. Consolidated Law on Banking and Credit);
- d. Mortgage credit;
- e. Pledged loans;
- f. Issuance of guarantees, endorsement, opening of documentary credit, acceptance, endorsement, commitment to grant credit, as well as any other form of issuance of guarantees and signature commitments.

The decree states that purchasing credits is a reserved activity because it is a financial activity; therefore, it can be conducted by banks, authorised financial intermediaries according to Article 106 TUB, securitisation companies, investment funds, and Special Purpose Vehicles (SPVs).

Article 2 introduced the so-called “115 TULPS companies” clarifying that they do not perform reserved activities but can engage in credit repurchase activities when they do not intend to resell the credit, and certain conditions are met. The text of the decree reads as follows:

- The acquisition of credits does not constitute per se a financing activity, in addition to the following cases of exclusion provided by law:
 - a. the purchase of value-added tax credits related to transfers of goods and services in cases provided for by current regulations;
 - b. the purchase of credits by companies holding a license for the activity of out-of-court debt recovery pursuant to Article 115 of the Public Security Laws Consolidated Text (TULPS) when the following conditions occur:
 1. credits are purchased for recovery purposes and are transferred by:
 - i. banks or other financial intermediaries subject to the supervision of the Bank of Italy, which have classified them as distressed, or
 - ii. subjects other than those indicated in point i), provided that they are credits claimed against debtors who are in a state of insolvency, even if not judicially ascertained, or in substantially equivalent situations, as determined by the competent corporate bodies; the existence of real or personal guarantees does not matter for this purpose;
 3. the financing received from third parties by the purchasing company does not exceed the total amount of net assets;
 4. the recovery of the purchased credits occurs without the signing of new financing contracts with the transferred debtors, the renewal of the existing ones, the modification of the contractual conditions; early termination and postponement of payment terms are not relevant for these purposes.

The 115 company (third-party credit recovery company) can buy financial and non-financial credits if they are distressed credits and cannot resell them. The purchase of credits is done for recovery purposes, not for trading. The financing received from third parties (purchasing

company) must also not exceed the amount of net assets: the 115 entities that purchase credits cannot have debts, i.e. the purchase price is lower compared to the net assets.

These financing structures together with the entities operating in the financial sector will be subject to change following the proposals for regulatory amendments for the implementation of the Secondary Market Directive (SMD), including the introduction of 114 TUB companies which will also handle the “management of distressed credits”:

1. The collection and recovery of payments due from the debtor;
2. Renegotiation of terms and contractual conditions with the debtor, in accordance with instructions from the purchaser of distressed credits, provided that it does not constitute the activity of granting financing under Article 106 TUB; early termination and postponement of payment terms are not relevant for these purposes. Activities conducted by credit intermediaries as defined by Articles 120-quinquies TUB, paragraph 1, letter g), and 121, paragraph 1, letter h) do not fall under this point 2);
3. Management of complaints from debtors concerning purchasers of distressed credits, managers of distressed credits, and entities to which business functions related to the management of distressed credits have been outsourced;
4. Disclosure to the debtor concerning any change in interest rates and charges or any payments due.

The provisions apply to the purchase of distressed credits by purchasers of distressed credits and the management of distressed credits, except, unless otherwise provided, in cases where management is carried out by:

- a. Managers, as defined in Article 1, paragraph 1, letter q-bis), of Legislative Decree 24 February 1998, No. 58 (TUF), on behalf of collective investment undertakings as defined in Article 1, paragraph 1, letter k), of the same decree managed by them;
- b. Banks, also with reference to credits granted or purchased by them;
- c. Intermediaries registered in the register provided by Article 106 TUB, also with reference to credits granted or purchased by them, if the activity is carried out in Italy. Intermediaries may carry out the activity of managing distressed credits in European Union states other than Italy if authorised under Article 114.6, paragraph 5.

2.2 The transposition of the Secondary Market Directive in Italy

In early 2024 the Italian Treasury opened a consultation on the draft legislation transposing the Secondary Market Directive (Proposte di modifica per il recepimento della direttiva (UE) 2021/2167). The Council of Ministers approved the final text on 22 July 2024.⁷ Shortly after, the Legislative Decree of 30 July 2024, n. 116⁸ that implements the Secondary Market Directive was published, entering into force on 14 August 2024.

⁷ See the press release here <https://www.governo.it/it/articolo/comunicato-del-consiglio-dei-ministri-n-89/26283>

⁸ More information is available here https://www.normattiva.it/atto/caricaDettaglioAtto?atto.dataPubblicazioneGazzetta=2024-08-13&atto.codiceRedazionale=24G00129&atto.articolo.numero=0&atto.articolo.sottoArticolo=1&atto.articolo.sottoArticolo1=0&qId=&tabID=0.34284043779627726&title=lbl_dettaglioAtto

The Legislative Decree includes the following provisions:

Information rights

Article 114.4 of the draft Legislative Decree prescribed that banks must furnish potential NPL buyers with the required information to allow potential buyers' credit evaluation and the probably of recovery.

In addition, Article 114.4 obliges banks to report to Bank of Italy and, if applicable, to the authority of the host Member States, at least biannually -unless another frequency is requested by Bank of Italy-, the information relating to the sold NPLs.

Bank of Italy will issue provisions implementing the information requirements in compliance with the Secondary Market Directive and the regulatory and implementing technical standards adopted by the European Commission.

Obligations of credit servicers

In line with the Secondary Market Directive provisions, the draft Legislative Decree establishes the requirements for credit servicers to obtain the mandatory authorisation to perform their activity, as well as the conditions for holding customer funds, and the information obligations vis-à-vis the debtors assigned.

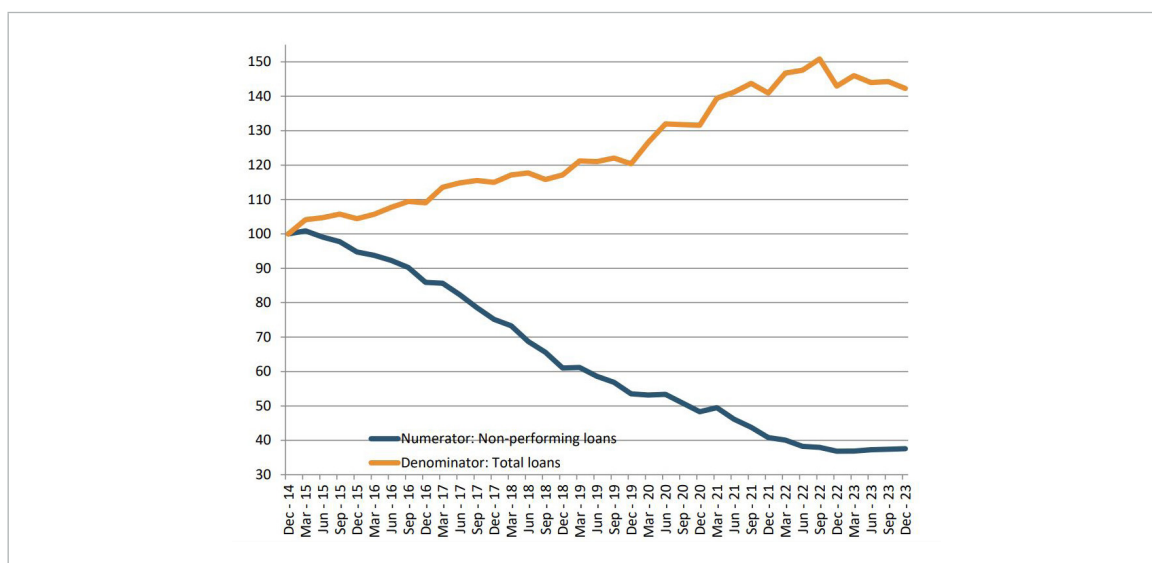
CHAPTER 2: THE EVOLUTION OF THE NPL MARKET

1. TRENDS AND EVOLUTION OF NON-PERFORMING LOANS

1.1 Europe

Starting from 2015, banks' NPL ratios consistently decreased in the EU. This improvement was driven by both a decrease in the stock of NPLs and the increase in total loans.

The increase in total loans together with the decrease in non-performing loans from 2014 improved banks NPL ratio at EU level



NPL ratio is highly heterogeneous across European countries

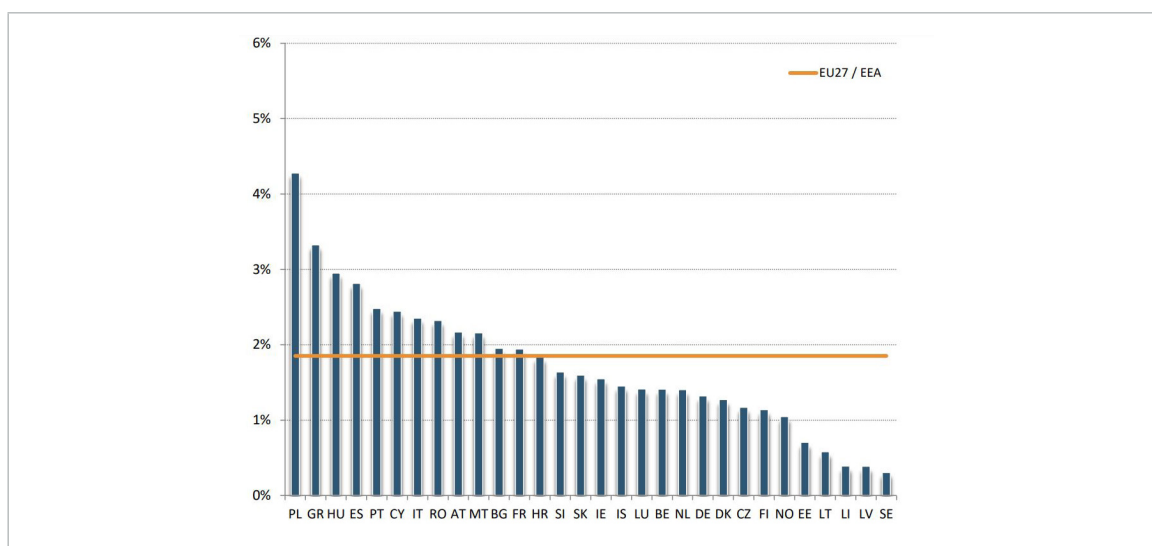


Figure 5: Total loans and non-performing loans over time and cross-country comparison.

Source: EBA Risk Dashboard, data as of Q4 2023

More recently, commercial real estate NPL ratios showed signs of increase. The causes of the increase are related to lower occupancy rates of offices and higher interest rates applied to the financing.

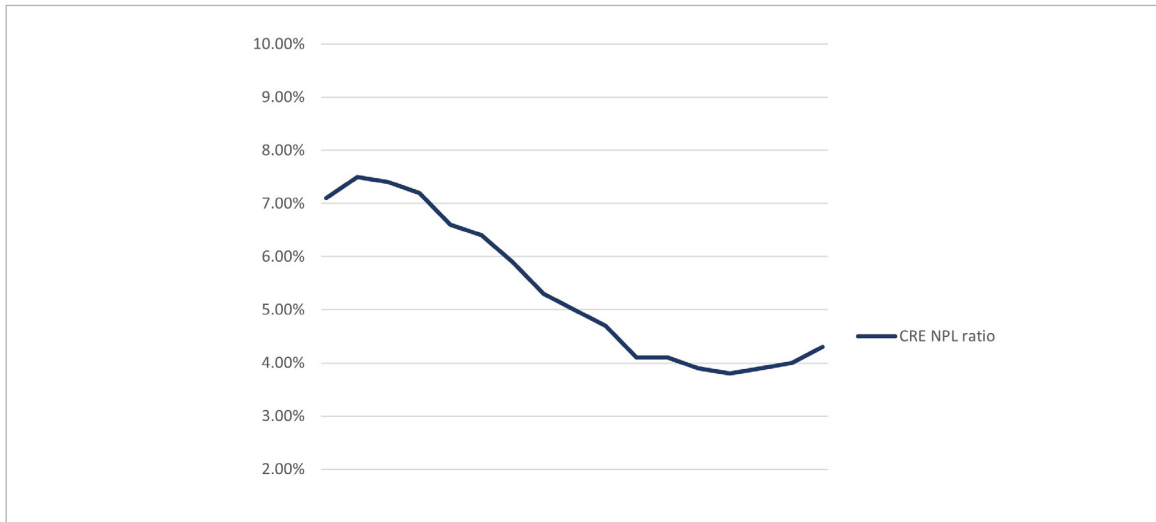


Figure 6: Commercial real estate NPL ratio evolution over time.

Source: EBA Risk dashboard, data as of Q4 2023

Comparing volumes across countries shows a significant decrease for the Italian market and, on the opposite spectrum, a significant increase for Germany and Austria (Figure 7).

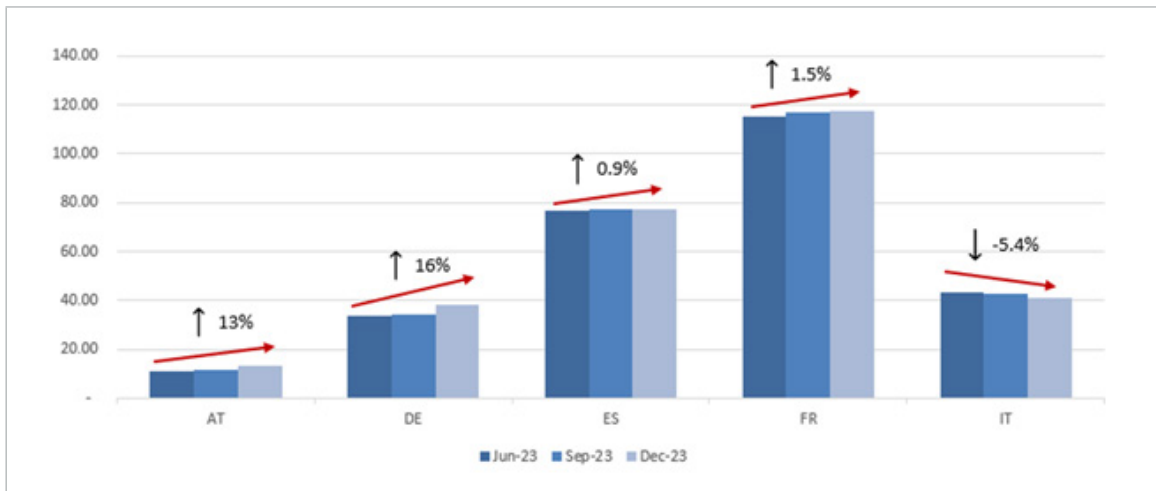


Figure 7: Non-performing loans and advances – Volumes bn. Euro

Source: EBA Risk dashboard, data as of Q4 2023

The analysis of the NPL ratio increase in Germany and Austria reveals that such increase is mostly driven by the CRE sector (Figure 8).



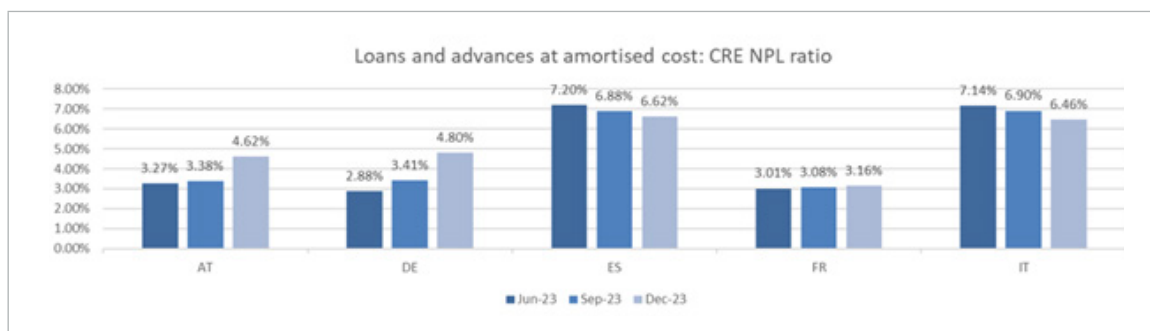


Figure 8: NPL ratio and CRE NPL ratio for selected EU countries.

Source: EBA Risk dashboard, data as of Q4 2023

While Italian NPLs show a high coverage ratio (54% as of December 2023), Germany on the other hand shows historically lower coverage ratios (33% as of December 2023). As depicted in Figures 9, coverage ratios differ across countries.

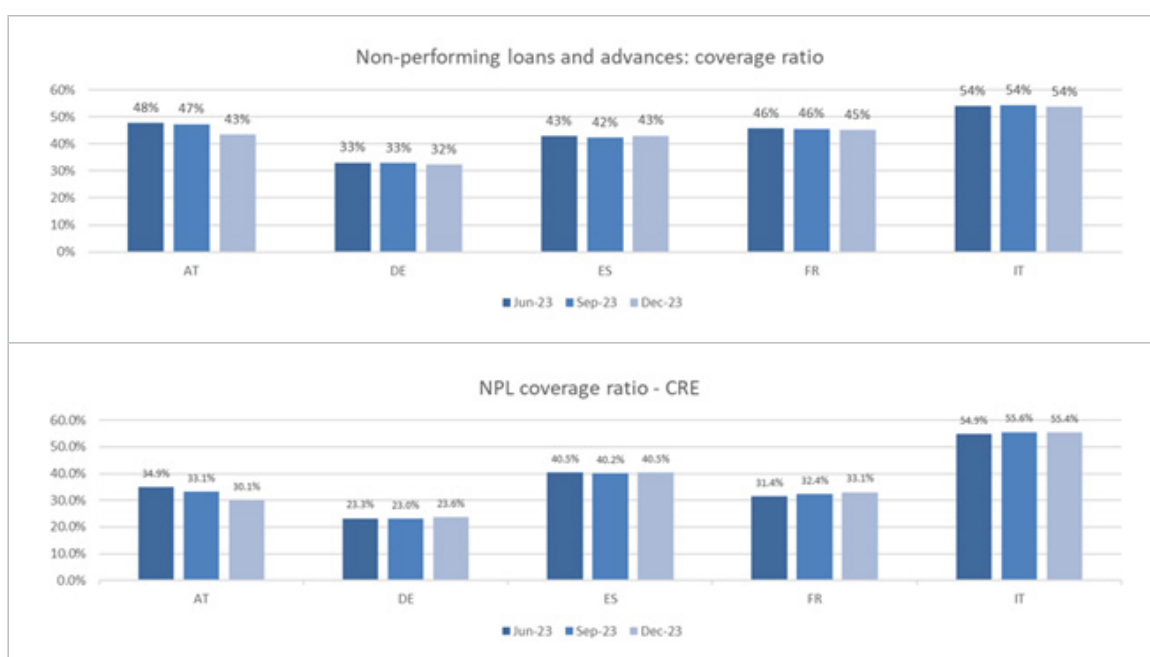


Figure 9: NPL coverage ratio for selected countries.

Source: EBA Risk dashboard, data as of Q4 2023

Looking at securitisation data from the European DataWarehouse platform, heterogeneous developments across European countries in terms of the calculated constant default rates (CDR) for RMBS deals (Figure 10) and cumulative delinquency rates (Figure 11 and Figure 12) are observed.

Figure 10 shows that the average CDR, calculated considering the total current balance of exposures in default in a period divided by the total current balance of non-defaulted underlying exposures, started to increase after the peak of EU inflation in October 2023.

Notably, delinquency rates for older mortgages originated in France in 2014 have an average default rate of 4% (Figure 11), versus an average of 15% in Italy (Figure 12). In Italy, loans originated in 2018 experienced higher cumulative defaults compared to those originated in 2016. These loans were, in fact, heavily impacted by the COVID-19 pandemic that started in early 2020.

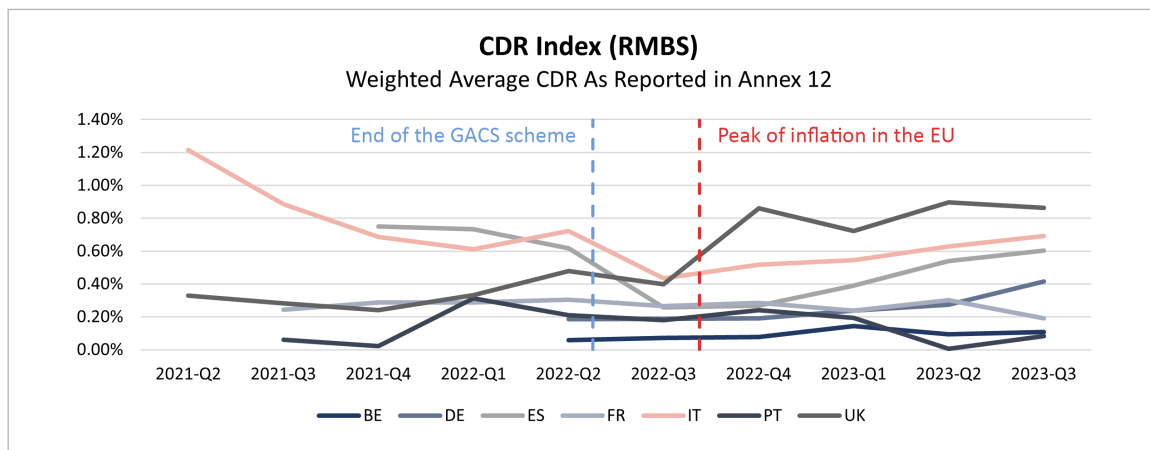


Figure 10: Constant Default Rate index as reported in Annex 12 of the ESMA templates

Source: European DataWarehouse research

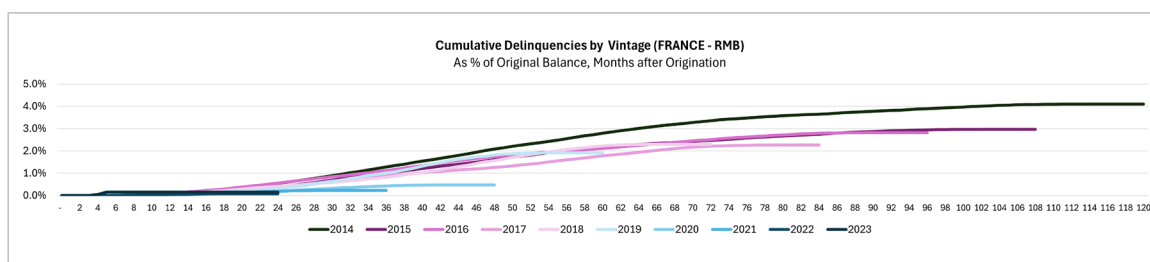


Figure 11: Cumulative delinquencies by vintage for loans included in French RMBS deals

Source: European DataWarehouse research

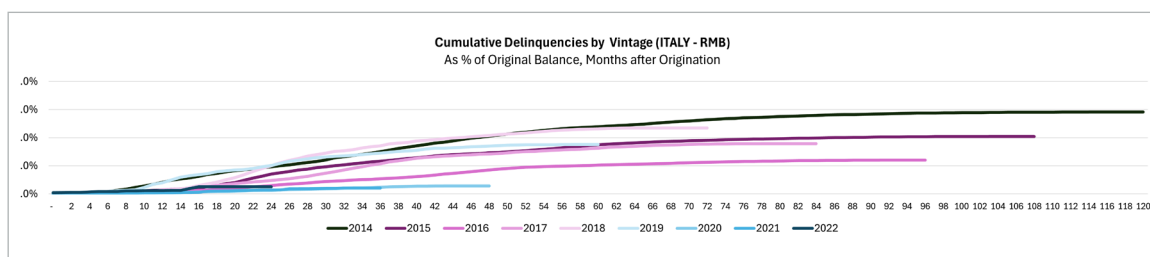


Figure 12: Cumulative delinquencies by vintage for loans included in Italian RMBS deals

Source: European DataWarehouse research

1.2 Italy

Starting from the great financial crisis and the public debt crises, Italian banks consistently reduced the amount of distressed credit on their balance sheets. According to Bank of Italy statistics ⁹, in 2022, credits amounting to approximately €22 billion were written-off from banks' balance sheets. This figure is four times the amount of new lending and is higher compared to the previous year in both absolute terms (€17 billion was the amount written off by banks in 2021) and in percentage terms, compared to the existing distressed loans at the end of the previous year (64% in 2021 versus 42% in 2022).

The increase compared to 2021 is mainly due to straight sales (which rose from €14 to €18 billion), while the number of loans written-off through ordinary procedures remained substantially stable compared to the previous year at €4 billion.

⁹ <https://www.bancaditalia.it/pubblicazioni/note-stabilita/2023-0035/index.html>

The improvement in disposal times has continued since 2015, benefiting from both the reduction in stocks and the lower amount of loans entering into a distressed stage, as well as the progress made by intermediaries in managing these credits. The share of positions written-off within one year of classification as distressed has progressively increased (from 38% for positions entered in 2015 to 65% for those in 2021).

Data from the Bank of Italy also shows that 85% of positions are closed within three years of entering into a distressed stage. Compared to previous years, the use of securitisations in relation to the total of sales was lower, also considering that since 14 June 2022, GACS is no longer available. The state guarantee has in fact been adopted for almost all major securitisation operations of distressed debt (€5.4 billion, 82% of the securitised distressed debts).

In terms of the broader non-performing exposures, the sales of distressed loans categorised as “Inadempienze Probabili” (loans likely to go into default) increased to €7 billion (compared to €5.7 billion in 2021). Recovery rates of closed distressed credits increased over time. Compared to 2021, the average recovery rate has increased both for sold positions (from 29% to 32%) and for positions closed through ordinary procedures (from 45% to 47%). The average recovery rate of distressed debts assisted by real guarantees was 40%, up from 2021 (38%) due to sales, whose recovery rate increased from 34% to 38%. For positions not assisted by guarantees, the average recovery rate was 27%, up from the previous year (25%) both on sold distressed debts (from 22% to 24%) and on those subject to ordinary recovery procedures (from 35% to 42%).

The price of loans in distress sold in 2022, based on Bank of Italy’s annual survey conducted since 2016 on a very large sample of operations, was 21% of the gross exposure on the balance sheet at the time of sale, slightly up from 20% in 2021. The increase, as already highlighted for the corresponding recovery rate, is attributable both to distressed debts assisted by real guarantee, for which the price rose to 32% (29% in 2021), and to those not assisted by real guarantees, whose price increased to 12% (11% in 2021). The sale price of impaired credits other than distressed debts was 34%, down 6 percentage points from the value observed in 2021, reflecting the lower weight of the guaranteed component.

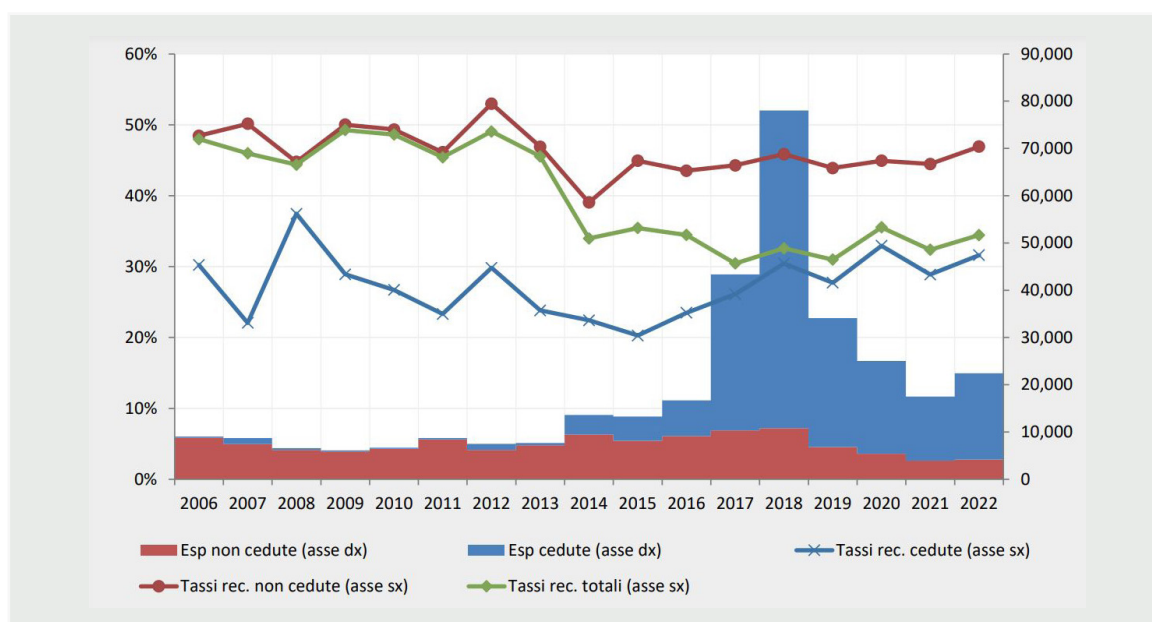


Figure 13: NPL sales and recovery rates over time

Source: Bank of Italy, *Note di stabilità finanziaria e vigilanza* N.35, December 2023

The stock of NPEs in Italy is estimated to have reached the peak in 2015 with approx. €400bn in the market. The process of de-risking that followed the peak allowed the banking system to constantly reduce NPE stock, which reached historical minimum levels in 2023 (€56bn). However, the problem has not been fully solved, as NPEs have been shifted from banking to investors' books.

According to the PwC report *The Italian NPE Market of December 2023* the total NPE stock in the Italian market decreased from €397bn in 2015 to €311bn in H1 2023 (-22% in 7.5 years, vs. -80% of the NPEs on banking books). There are still over €300bn NPEs that need to be managed and recovered, which could fuel a significant secondary market in the future. The Stage 2 loans¹⁰ on banking books amount to €211bn as of June 2023, bringing the total value of credits under scrutiny to over €500bn. The stock of NPEs have decreased continuously since 2015. The current €56.0bn balance at the end of H1 2023 confirms the decreasing trend, even if at a slower pace compared to the previous years (average CAGR of -21.4% between YE-2015 and H1-2023). The drop was driven by a decrease of €2.5bn in Gross UtP (unlikely to pay) and by a moderate decrease of €0.1bn in Gross Bad Loans, in comparison to the end of 2022. The Gross Past Due stock shows an increase of €0.3bn from the end of 2022. In addition, from 2020 to June 2023, over €340bn in loans with state guarantees (Mediocredito Centrale and SACE) have been sold, generating a loan stock of approximately €230bn as of June 2023.

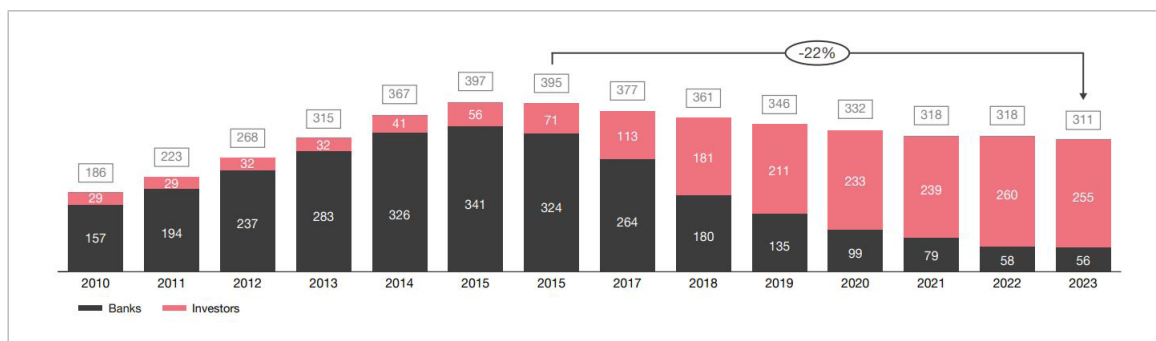


Figure 14: NPE trend in the Italian market (GBV, €bn)

Source: PwC report *The Italian NPE Market, December 2023*

In Greece, the “Hercules Asset Protection Scheme” (HAPS) scheme was introduced in 2019 and is largely based on the GACS scheme, albeit with some differences, as requirements tend to be less strict (e.g. no investment grade rating requirement for the senior tranche). As in the GACS case, HAPS requires a minimum sale of 50% plus one of the junior tranche securities to third party private investors at a positive value (it cannot be zero but can be as low as €1). Most importantly, the Italian GACS scheme does not cover exposures classified as unlikely-to-pay, whilst HAPS does foresee the inclusion of these kinds of exposures.

¹⁰ Stage 2 loans are credits that manifest a significant increase in risk, but without objective evidence of impairment. They are therefore, for all intents and purposes, “live” credits, which have a good chance of returning to a performing stage.

CHAPTER 3: A PROPOSAL FOR THE EFFECTIVE IMPLEMENTATION OF THE NPL TRANSACTION DATA TEMPLATES ACROSS THE EUROPEAN UNION

The enforcement of the Secondary Market Directive and the effective implementation of the NPL Transaction Data Templates significantly rely on the setup and use of **information systems** that facilitate the **efficient** and **secure processing** of, and the **easy access** to, the granular loan-by-loan information laid out in the Templates regarding the loan(s), the counterparty, the collateral, the guarantees, the legal and enforcement procedures, as well as the historical collection and repayment history of the loan(s).

While the NPL Transaction Data Templates help tackle the information asymmetry between the prospective buyers and sellers of NPLs thanks to common templates, data fields, definitions and characteristics, still, the **collection, organisation, structuring, storage, and availability** of such standardised information remains a challenge for sellers of NPLs due to the constraints in obtaining all the mandatory data requested in the NPL Transaction Data Templates. These constraints mainly relate to the use of legacy IT systems, poor data quality, and high operational costs involved in collecting, cleaning, and organising data. As a consequence, the intended objectives of transparency and development of secondary markets for NPLs in the EU could be jeopardised.

In this regard, the collaboration of operators in the NPL markets to streamline the **collection, organisation, structuring, storage, and availability** of the information requested in the NPL Transaction Data Templates could be a game changer in overcoming these challenges.

This Chapter elaborates on key elements for the effective implementation of the NPL Transaction Data Templates across the European Union.

1. KEY ELEMENTS FOR THE IMPLEMENTATION OF THE NPL TRANSACTION DATA TEMPLATES ACROSS THE EU

1. Efficient information systems

For the preparation of the definitions of the data fields in the data glossary of the NPL Transaction Templates, the EBA built upon the definitions already included in other EU regulatory, supervisory, and reporting frameworks to the extent possible considering the different purposes.

Following the same efficiency approach, leveraging the information already available in either the information systems of certain NPL market operators -namely, credit servicers- or other third parties -for instance credit bureaus- would minimise credit institutions' efforts in compiling the information requested by the NPL Transaction Data Templates. Moreover, automatically embedding the imported information into the required format and conventions of the NPL Transaction Data Templates would enormously facilitate the collection of the necessary information and would likely improve the completeness ratio of the mandatory NPL Transaction Data Templates.¹¹

¹¹ The leveraging of information readily available in the information systems of third parties should be subject to the appropriate legal assessment to ensure that the potential data transfers and/or data enrichment processes are lawful and compliant with all applicable laws, including but not limited to the personal data protection laws.

2. Secure information systems

The ITS sets out requirements for the treatment of confidential information, prescribing that all confidential information should be shared through secure channels and only after appropriate confidentiality arrangements have been put in place between the credit institution and the prospective buyer. Such secure channels may be, for instance, electronic virtual data rooms that should meet the applicable industry standards for confidentiality and data security.

In addition, given that the NPL Transaction Data Templates request the processing of information which qualifies as personal data within the meaning of the GDPR, such personal data should be treated and exchanged in a way that is in accordance with the requirements of the GDPR.

The alignment of market operators concerning secure channels for the exchange of the information to be disclosed according to the NPL Transaction Data Templates would highly benefit the harmonisation of the security standards applicable to the sharing of the relevant information and the creation of a level playing field for all sellers of NPLs.

3. Data quality management

Apart from data sharing security, the ITS emphasises the need to ensure that the data provided is complete and accurate. However, the verification of the completeness and accuracy of the data might be a burdensome and expensive task for credit institutions.

In this context, the involvement of third-party experts in data completeness and consistency verification procedures, such as securitisation repositories, can play a role in ensuring the quality of the data provided through the NPL Transaction Data Templates. High-quality, granular loan-by-loan data would help the transparency and development of functioning secondary markets for NPLs in the EU.

4. Easy access to the data

Sellers of NPLs should ensure that easy and user-friendly access to the loan-by-loan information regarding the loan(s), the counterparty, the collateral, the guarantees, the legal and enforcement procedures, the historical collection and the repayment history of the loan(s) is granted to prospective buyers of NPLs.

The implementation of information systems with comparison and aggregation features that enable the generation of reports based on the information provided through the NPL Transaction Data Templates would facilitate the consumption of the granular loan-by-loan data in a fully-fledged manner and thus, would foster transparency in NPL secondary markets.

Furthermore, insofar permitted by applicable laws, information systems should keep records of the NPL Transaction Data Templates used by NPLs buyers for the performance of their financial due diligence and the valuation of the respective NPLs. Such a recordkeeping system would support internal governance compliance, allowing credit institutions to consult past due diligence and valuation documentation and would serve as evidence for any audit or supervisory reviews.

2. THE SETUP OF AN INTEGRAL SOLUTION FOR NPL SERVICES

Based on the key elements listed in section 1.1, the consolidation of various NPL management and reporting functions through an integral solution is proposed.

The 31 May 2017 report of the Financial Services Committee (FSC) Subgroup on Non-Performing Loans¹² and the Commission Staff Working Document on European Platforms for Non-Performing Loans¹³ published on 28 November 2018 in the context of the Third Progress Report on the reduction of non-performing loans and further risk reduction in the Banking Union already hinted the benefits that the creation of a European-wide NPL platform would have for the development of NPL secondary markets.

Indeed, the report of the FSC Subgroup on Non-Performing Loans of 31 May 2017 included three pivotal policy options as part of the policy objective number 8, i.e., “Developing secondary markets in Europe for NPL transactions”:

- Policy Option C.1: Implement enhanced disclosure requirements on asset quality and non-performing loans to increase transparency on balance sheets with more granular information, across a broad spectrum of the banking sector.
- Policy Option C.2: Mandate the EBA to develop guidelines for banks on loan tape monitoring to standardise information in order to improve the readiness for sale of NPLs.
- Policy Option C.3: Strengthen the data infrastructure for secondary market transactions and consider the setting-up of platforms for NPL transactions to develop the secondary market and enlarge the pool of market participants.

While the Secondary Market Directive and the ITS with the NPL Transaction Data Templates have successfully addressed Policy Options C.1 and C.2., Policy Option C.3 still remains a challenge.

The FSC report made the point that, as data quality represents a key hurdle for secondary market transactions, centralised NPL management and data sharing systems could strengthen the infrastructure of secondary market transactions, improving the quality and comparability of available information on loans and counterparties for potential investors and facilitating the external assessment of the quality and the marketability of loans.

The FSC report suggested that such centralised systems could act as a central hub for NPL sales, as well as a central repository for data -standardised and of sufficient quality for due diligence purposes- on NPLs from participating banks and counterparties. In addition, the FSC report stated that they would reduce investor costs (through the standardisation of data and processes and the consolidation of sales in one data-infrastructure agency), support data cleansing efforts by banks and provide more transparency on completed transactions.

Furthermore, the report invited the Commission and other relevant institutions such as the EBA and ECB to conduct preparatory work on the potential designs of data infrastructures/hubs, taking into account previous experiences such as the ECB ABS Loan-Level Initiative and available projects such as AnaCredit.

¹² Available at: <https://data.consilium.europa.eu/doc/document/ST-9854-2017-INIT/en/pdf>

¹³ Available at: <https://eur-lex.europa.eu/legal-content/EN/TXT/?uri=CELEX:52018SC0472>

The Commission Staff Working Document published in 2018 elaborated on the benefits that a European-wide NPL platform would have for secondary markets, contributing to reducing the degree of market failure in the European secondary market for NPLs, helping to address information asymmetries, increasing creditor coordination and broadening the investor base, thus leading to improved market pricing of NPLs.

The Commission Staff Working Document defines an NPL platform as “an electronic marketplace where holders of NPLs -banks and non-bank creditors- and interested professional investors can meet to exchange information and to trade”. According to Commission staff, an EU-wide NPL platform is preferable to national solutions because it would be more effective in reaping the benefits of increased transparency and reduced transaction costs. By improving and harmonising information and data, transaction costs associated with NPL transactions could be reduced and price formation improved. This could lead to the reduction of market entry barriers, subsequently increasing competition and enabling easier price discovery. Last but not least, such an NPL platform would also become a channel through which future NPLs could be efficiently disposed of as they arise.

In fact, the Commission staff approach would be highly effective due to the combination of a set of functions in a single environment, namely:

- a. Data warehouse function;
- b. Creditor coordination function;
- c. Transaction facilitating function; and
- d. Potentially, intermediation for further ancillary services, such as valuation and collateral appraisal, legal services, advisory services, and loan servicing.

Figure 15 depicts the potential functions for a NPL platform as envisaged in the Commission Staff Working Document.

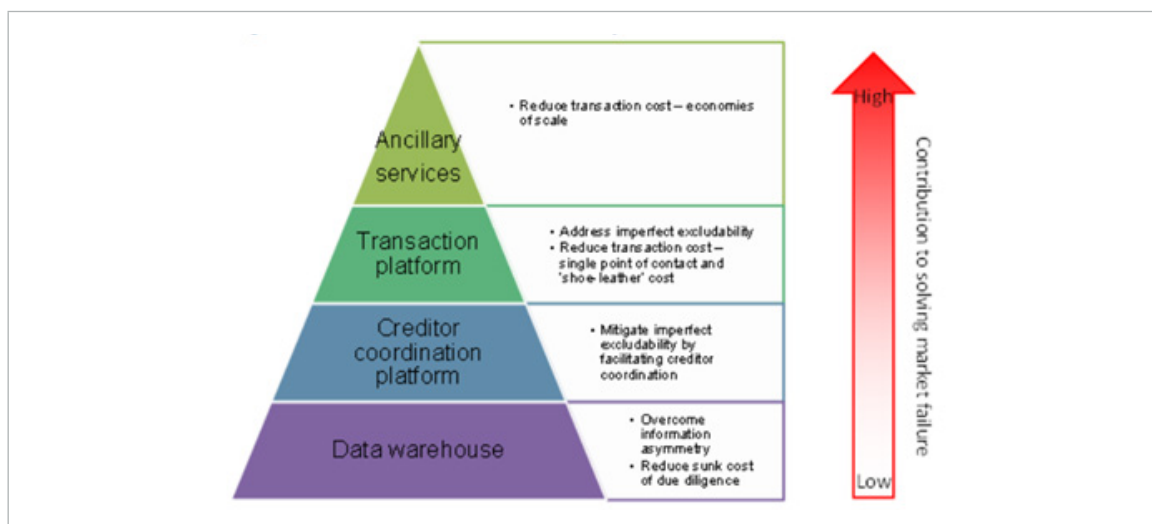


Figure 15: Potential functions for a NPL platform as per the Commission Staff Working Document

Source: COMMISSION STAFF WORKING DOCUMENT European Platforms for Non-Performing Loans Accompanying the document COMMUNICATION FROM THE COMMISSION TO THE EUROPEAN PARLIAMENT, THE EUROPEAN COUNCIL, THE COUNCIL AND THE EUROPEAN CENTRAL BANK Third Progress Report on the reduction of non-performing loans and further risk reduction in the Banking Union

One of the main reasons pledged for the establishment of a European-wide NPL platform is the need for high quality loan-level data for the successful and efficient functioning of secondary markets.

By using the standard definitions and taxonomies set through the NPL Transaction Data Templates, market participants will have access to better quality and comparable data. Moreover, the data validation checks to be conducted by the platform would ensure that the data provided is complete, accurate, and consistent. The data quality checks could be conducted – following the Commission Staff Working Document approach – at three different levels:

1. Completeness, consistency, and coherence

Implementation of validation checks to verify that all required data fields are reported (completeness) and checks to verify that the data abide by simple automatic validation rules (consistency and coherence).

2. Plausibility

Implementation of checks designed to raise flags of an unexpected result, but which do not automatically signal an error.

3. Accuracy

Implementation of data quality rules likely involving advisory services to verify the accuracy of the data.

To contribute to the enforcement of the Secondary Market Directive and the effective implementation of the NPL Transaction Data Templates, this Report suggests the coordination of expert market players in the NPL markets to provide an integral solution that combines the data warehouse function; the creditor coordination function; the transaction facilitating function, as well as further potential functions. Figure 16 below depicts the solution proposed from a procedural standpoint in the NPL management lifecycle.

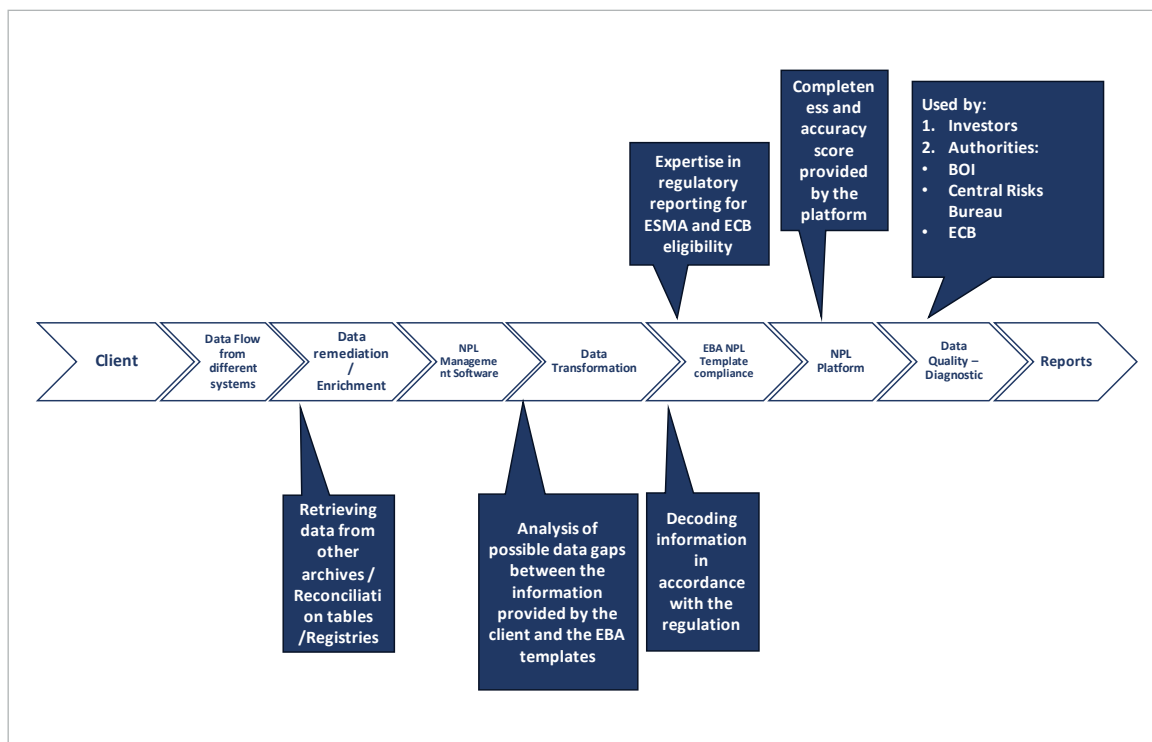


Figure 16: Integral solution in the context of the NPL management lifecycle

3. THE ROLE OF EUROPEAN DATAWAREHOUSE FOR NPL TRANSPARENCY

In the constellation proposed in this Report, European DataWarehouse could play a significant role as NPL repository. In fact, a securitisation repository's expertise regarding operational standards for data collection, aggregation, comparison, access and verification of completeness and consistency would be greatly useful for compliance with the ITS requirements applicable to the NPL Transaction Data Templates.

The use of European DataWarehouse for the NPL Transaction Data Templates disclosures would be positive for many reasons:

- a. market participants already report transactions (securitisations -both public and private-, covered bonds, pools of additional credit claims, pools of loans, either performing or non-performing) through European DataWarehouse, either following a regulatory mandate, or voluntarily. As a consequence, the submission of the NPL Transaction Data Templates through the same channel would not imply any additional expertise or technical burden.
- b. regulatory and supervisory authorities (cfr. Financial Services Committee (FSC) Subgroup on Non-Performing Loans Council Report and Commission Staff Working Document mentioned in section 3.2) have advocated for the creation of data infrastructures similar to existing infrastructures such as the European DataWarehouse set up as part of the ECB ABS Loan-Level Initiative. Leveraging the data infrastructure of European DataWarehouse for the NPL Data Transaction Templates disclosure obligations would notably simplify NPL sellers' compliance obligations, as well as facilitate potential buyers' accessibility to information. The competent authorities in charge of supervising the relevant obligations could also rely on European DataWarehouse to access the submitted information for their supervisory activity.

While European DataWarehouse does not offer creditor coordination or transaction platform services, these functions could be integrated in a single process through ad hoc collaborations with expert third parties such as Zenith Global.

CONCLUSIONS

The European NPL regulatory framework has significantly evolved since the European Commission 2017 Action Plan, with the adoption of the Secondary Market Directive and the ITS on the NPL Transaction Data Templates in 2021 and 2023, respectively. Market trends have equally changed alongside regulations.

The Secondary Market Directive and the NPL Transaction Data Templates will have a notable, positive impact on the market in terms of increased transparency and the harmonisation of the information to be disclosed by credit institutions to prospective buyers before the sale of NPLs.

However, a gap exists to further stimulate the development of the secondary market, i.e., the consolidation of the different functions linked to the NPL management process into a single, centralised solution, i.e., data warehouse, creditor coordination, and transaction management services, to enhance data quality and enlarge the pool of participants. Leveraging existing data infrastructures such as existing, designated securitisation repositories and bringing together NPL market participants to create such solutions aligned with the standards recommended in the Commission Staff Working Group of 2018 would mark a milestone in the EU's journey towards the revival of the secondary markets for NPLs.

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