Nordic Financial Unions

EBA Consultation Paper – Draft Guidelines on loan origination and monitoring

About NFU

NFU – Nordic Financial Unions is an organization that promotes the interests of the Nordic financial trade unions in Europe. Through a high level of competence and dialogue, NFU contributes to shaping a sustainable financial sector, fundamental for job creation. Currently, NFU represents seven trade unions in the bank, finance and insurance sector in Denmark, Finland, Iceland, Norway and Sweden.

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Consultation replies

1. What are the respondents' views on the scope of application of the draft guidelines?

2. Do you see any significant obstacles to the implementation of the guidelines by the application date and if so, what are they?

3. What are the respondents´ views on whether the requirements set in the draft guidelines are future proof, in particular in relation to technology-enabled innovation (Section 4.3.2) and environmental factors and green lending (Section 4.3.3)?

NFU welcomes the opportunity to participate in EBA´s public consultation on the Guidelines on Loan Origination and Monitoring. We acknowledge the general idea of addressing credit risk and ensuring that institutional practices are aligned with consumer protection rules, while nonetheless see several areas of improvement in the proposed Guidelines.

Firstly, **NFU supports ensuring relevant staff members are ´adequately skilled, resourced and experienced´** (4.1.1. Responsibilities of the management body, 21(f)). Companies need to ensure that skills and competence development is made available and taken up by employees continuously, both regarding financial products and services, as well as regulatory developments. This should become part of standing, long-term governance priorities for the company. At the same time, employees need enough resources, including time, to convey proper service. This is especially relevant in the eyes of rising administrative burden, while no changes are made to the time that an employee spends with the customer.

Furthermore, NFU wants to highlight the reference to monitoring and control processes to the institution´s credit risk culture and related deficiencies (4.1.2 Credit risk culture, 25.), as well as the reference to credit risk appetite (29). There has been a tendency in recent years for responsibility on practices and behavior to be transferred downward in the hierarchy. This is an unfortunate development, as following the explicit or implicit company culture of sales pressures may have negative outcomes for individual employees over the short and long term including a spillover effect to consumer protection. It is therefore imperative that the **accountability for company practices and policies is kept on managerial level**, as usually the tone is set at the top. This also applies to the review of credit policies and procedures (39).

Regarding technology-enabled innovation for credit granting (Section 4.3.2), we would like to add to (47) that if eventually using such innovation, institutions need to address the question of data collection, analysis, retention and integrity, among else, depending on the sophistication of the tool used. However, on a general note, NFU sees technology-enabled solutions as means of easing the work of employees and optimizing the customer experience, on the way to credit granting. Using technology and innovation in this way could make it possible that the risks from the absence of human intervention are mitigated.

Ultimately, regarding **environmental factors and green lending** (4.3.4), we find it positive that the need for corporate sustainable finance strategies is being mentioned. The financial sector as such has a central role to play in catalyzing the sustainable finance agenda, and finance sector employees play a critical role in the process. To ensure that the guidelines are indeed future-proof, we would like to encourage that the terminology used in this section is harmonized with the sustainable finance legislative package, especially when addressing environmental/green/sustainable interchangeably. Another aspect that NFU would like to raise is the mention of quantitative and qualitative targets which institutions should set up in support of the integrity of their green lending activity (50), especially if these targets are further translated down to individual sales targets for employees. If sales targets and performance measurement systems exist, they must be fair and balanced, and established in dialogue with employees. The quality of advice should not be compromised by work pressure caused by performance measurement.

We find it crucial that employees are provided with the essential skills and training to be able to correctly advise customers. Although the Nordic countries are at the forefront of making sustainable choices, there is a general lack of sufficient information and transparency around the green lending options. Connected to that, there is a need for **dilemma training as well as clear guidelines and policies preventing actual or potential conflicts of interests**. It is essential to ensure employees have the right to provide advice reflecting the sustainability-related preferences of their clients, instead of advice leading to maximized profits.

4. What are the respondents' views on the requirements for credit risk policies and procedures (Section 4.3)?

Please refer to question 3.

5. What are the respondents' views on the requirements for governance for credit granting and monitoring (Section 4)?

In addition to the abovementioned, the section on credit decision making (4.4) refers to **individual delegated authority**. We find that if such functions are assigned to individual employees and in limited cases, there needs to be a clear definition of the scope of responsibilities, adequate training, and an understanding that the accountability for following rules and procedures still resides at the top. The same considerations should apply for the ´three lines of defense´, including on how the lines are interconnected.

Furthermore, as a general principle, company objectives should be aligned with wider societal interests and sustainability goals. This also involves adopting a **sustainable approach towards employees** through ensuring that upskilling and re-skilling programmes aligned with the company´s long term credit risk policies and strategic orientations, such as green lending, are made available. NFU suggests that they are referenced as well, when addressing Resources and Skills.

According to the ´Coping with Compliance´ study that NFU carried out in 2018, regulatory requirements have increased in the Nordic financial sectors, with no adjustments made on the demands management put on employees performance in other fields, such as meetings and targets. Such situation has led to increased workload and stress levels among employees, frequently adversely affecting customers, who stand in the middle of the dilemma between following the rules and regulations and providing sound advice. While this is a general point to raise regarding EU regulation, we would emphasize its spillover effect to all levels, and down to company rules and regulations. Efforts should be made to **streamline internal processes and reduce administrative burden** for employees, allowing for the time to be used in servicing customers.

Ultimately, regarding 4.7. Remuneration, NFU strongly supports the idea of remuneration policies and practices that are consistent with and promote sound and effective risk management but believes that **remuneration policies and practices should be left to the social partners to decide upon.** This is the cornerstone of the Nordic model, and in accordance to Article 153,5 TFEU; Recital 69 of CRD, recital 10 in Directive 2014/91/EU and Recital 14 in Directive 2010/76/EU. In some jurisdictions, collective agreements also regulate small amounts of variable remuneration paid to certain employee profiles, which as such cannot be affected by a third party/institution. We urge that these considerations are included under point 82.

In addition to that, and in order **to maintain proportionality**, it is equally important to acknowledge that most employees do not receive excessive amounts of variable remuneration. In fact, in the area of banking, local agreements on variable remuneration can be extremely limited, which is the case in Denmark. Thus, in this case variable remuneration could play limited/no role in credit granting. As a principle, NFU stands for the fact that employees should be adequately paid for performing their job and that variable pay should be an additional, and not main income. Still, and as stated, we trust that remuneration policies and practices should be decided upon by the social partners.

On another note on proportionality, for financial institutions that impose low risk to the financial system and have a handful of employees, making sure that all information is reported in detail, for example on remuneration policies, may be costly and significantly raise the administrative burden.

As a final point, **not only remuneration policies and variable pay that can create risk incentives for staff,** as implied in the guidelines**.** Also, non-monetary merit rating systems and aggressive sales targets are reasons for stress and pressure among the employees that can result in mis-selling. These types of systems are not driven by monetary incentives but can instead affect the overall salary or position of the employee at the company.

6. What are the respondent's views on how the guidelines capture the role of the risk management function in credit granting process?

7. What are the respondents' views on the requirements for collection of information and documentation for the purposes of creditworthiness assessment (Section 5.1)?

8. What are the respondents' views on the requirements for assessment of borrower's creditworthiness (Section 5.2)?

9. What are the respondents' views on the scope of the asset classes and products covered in loan origination procedures (Section 5)?

10. What are the respondents' views on the requirements for loan pricing (Section 6)?

11. What are the respondents' views on the requirements for valuation of immovable and movable property collateral (Section 7)?

12. What are the respondents' views on the proposed requirements on monitoring framework (Section 8)?