

## EBA GUIDELINES ON LEGISLATIVE AND NON-LEGISLATIVE MORATORIA ON LOAN REPAYMENTS APPLIED IN THE LIGHT OF THE COVID-19 CRISIS

On 2 April 2020, the EBA published the Guidelines on legislative and non-legislative moratoria on loan repayments applied in the light of the COVID-19 crisis (EBA/GL/2020/02), in order to clarify the prudential treatment of moratoria and to prevent a sudden increase in non-performing loans that would undermine their effectiveness.

These guidelines specify the prudential treatment of the moratoria and set the relevant qualifying criteria, which were initially as follows:

- I They must either be based on national law or be private moratoria that form part of an industry- or sector-wide agreement.
- II They have to apply to a broad range of customers and allow the borrower to take advantage of the moratorium without an ex ante assessment of their ability to pay.
- III They change only the schedule of payments and offer the same conditions to all the exposures subject to the moratorium.
- IV They do not apply to new loans granted after the date when the moratorium was announced.
- V They were launched in response to COVID-19 and applied before 30 June 2020.

As regards the prudential treatment, the guidelines interpret how to apply the prudential definitions of “default” and “forbearance” to transactions subject to eligible moratoria.

Starting with the definition of “default”, the guidelines provide that, when an exposure is subject to an eligible moratorium, the instalments in question will not be considered past due, and days past due will be counted on the basis of the schedule resulting from the application of the moratorium.

The guidelines also indicate that, throughout the duration of the moratorium, banks must continue to analyse their borrowers’ creditworthiness and unlikelihood to pay in accordance with their relevant prevailing general policies.

When banks conclude that borrowers are unlikely to pay, they will be classified as defaulted. It is therefore a matter of distinguishing between those borrowers with viable businesses that are experiencing one-off liquidity difficulties owing to the measures imposed by governments and those with fundamental solvency problems. In the case of the latter, banks should not delay classification as defaulted or the recognition of losses.

Turning to the definition of “forbearance”, the guidelines provide that transactions subject to an eligible moratorium should not automatically be reclassified as forborne. This flexibility is allowed, inter alia, because eligible moratoria are granted, as part of a general scheme, to borrowers meeting certain criteria, without said borrowers being subject to an individual ex ante assessment of their creditworthiness. Moreover, as the exposures are not considered forborne, they are also exempt from the distressed restructuring test set out in the EBA Guidelines on the definition of default (EBA/GL/2016/17).

Although these guidelines were originally to expire on 30 June 2020, the EBA decided to extend them for a further three months. As a result, the new maturity extensions agreed by banks would no longer be subject to the guidelines, but instead would have to be analysed on a case-by-case basis.

In late November, the new restrictions imposed by some European governments to address the second wave of the pandemic led the EBA to reconsider its decision and agree to reactivate its guidelines – retroactively from 1 October – until 31 March 2021. Two further conditions were imposed: i) a nine-month cap was set on the period during which an exposure subject to moratoria can benefit from the prudential treatment under the guidelines (except for moratoria granted before 30 September); and ii) the mechanism of the unlikelihood to pay assessment was reinforced, and institutions were requested to submit to their competent authorities their plans for applying this criterion.