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CONSULTATION RESPONSE TO THE ACT TO AMEND THE DANISH MORTGAGE-CREDIT LOANS AND MORTGAGE-CREDIT BONDS ETC. ACT, THE DANISH FINANCIAL BUSINESS ACT AND THE DANISH ACT ON A SHIP FINANCE INSTITUTE

On 23 October 2020, the Danish Financial Supervisory Authority initiated a consultation procedure for a draft bill for an Act to amend the Danish Mortgage-Credit Loans and Mortgage-Credit Bonds etc. Act, the Danish Financial Business Act and the Danish Act on a Ship Finance Institute The purpose of the draft bill is to minimum implement the Directive on the issue of covered bonds and covered bond public supervision (CBD) and to lay down the requirement for a minimum level of excess capital adequacy for collateral resulting from the amendment to the Capital Requirements Regulation (CRR).

It is positive that the bill's general approach is to implement the outcomes required by the CBD. The introduction of uniform European standards for covered bonds, including mortgage bonds, contributes to financial stability.

Danmarks Nationalbank has two specific comments on the bill:

- The liquidity requirement should be stated on the basis of the contractual maturity of the bonds and not on the basis of the postponed maturity date for bonds with an extension option.
- It should be specified that the proposed cooperation obligation between the Danish Financial Supervisory Authority and Financial Stability is based on the competence of the Danish Financial Supervisory Authority to perform "product supervision".

INTRODUCTION OF NEW LIQUIDITY BUFFER REQUIREMENT ETC.

In accordance with the bill, covered bond models which are "match-funded" can be exempt from the new 180-day liquidity requirement because the "match funding" ensures that the liquidity is present when the payments are to be made.

For "non-match-funded" covered bond models, a 180-day liquidity requirement is introduced to ensure that there is a sufficient amount of liquid assets to pay creditors 180 days ahead. However, the bill encourages the use of national discretion to introduce the requirement in a more lenient form than the basis provided in the Directive. This means that the financial institutions may assume that the maturity date for the payments to the bondholders is based on an extension of the maturity of the bonds rather than the original maturity of the bonds.

The more lenient implementation is problematic because it does not support the ability of the financial institution to pay its commitments on time. The issuances covered by the bill will be particularly relevant to banks. The rule for banks is that covered bonds can only be extended if the bank is in resolution or liquidation. The bill consequently proposes that the liquidity requirement – which is precisely intended to reduce the liquidity risk connected with the bond and which is a key element in securing timely repayment to the creditors – is to be based on an extension of the bonds. The consequence is that the bill does not support the purpose of the liquidity requirement.

The proposed "non-match-funded" bond models should instead follow the basis of the Directive, so that the liquidity requirement is stated based on the contractual due date of the payments.

COOPERATION BETWEEN SUPERVISORY AUTHORITY AND RESOLUTION AUTHORITY

The bill proposes to insert in the Danish Financial Business Act a "principle-based cooperation obligation" between the Danish Financial Supervisory Authority and Finansiel Stabilitet in the event that a financial institution that issues covered bonds shows signs of failing. At the same time, the current Danish Act on Restructuring and Resolution of Certain Financial Undertakings already presupposes collaboration between the Danish Financial Supervisory Authority and Finansiel Stabilitet if a financial institution shows signs of failing. The independent content of the provision on a collaboration obligation in the bill is therefore unclear.

It is essential that no uncertainty arises as to which authorities have the competence to make which decisions if a financial institution which issues covered bonds shows signs of failing and enters into resolution proceedings.

The bill should therefore expressly state that the proposed obligation relates solely to the Danish Financial Supervisory Authority's control of the compliance with the rules for covered bonds (the so-called product supervision), including the ongoing and sound management of the programme for covered bonds during the resolution process. As is also the case in the Directive text, it should be stated in the explanatory notes that the purpose of the provision is not to change the way in which covered bonds are treated in the event of resolution in accordance with the Danish Act on Restructuring and Resolution of Certain Financial Undertakings.

Best regards,

Lars Rohde