



**Joint response from the Bank of England and the European Central Bank
to the Consultation Document of the European Commission:**

“An EU framework for simple, transparent and standardised securitisation”

Executive Summary

The following terms have the following meanings:

- “*qualifying securitisations*” and “*non-qualifying securitisations*”, widely used in this Green Paper.
- “*Simple, Transparent and Comparable*” *Securitisations (STC)*, used by the BCBS-IOSCO Joint Task Force on Securitisations Markets and by the Basel Committee on Banking Supervision.
- “*Simple, Standard and Transparent*” *Securitisations (SST)*, used by the European Banking Authority (EBA).

We acknowledge the common principles behind these initiatives which are reflected in the similarity, albeit with slight nuances, of the separate sets of criteria. Therefore throughout this paper we consistently refer to Simple, Transparent and Standardised (“STS”) as encompassing the collective effort to develop criteria for certain securitisation transactions going forward.

We welcome the opportunity to comment on the Commission services’ consultation on an EU framework for STS securitisation. A uniform set of criteria for STS securitisation to underpin EU legislation could play an essential role in attracting a broader investor base and in de-stigmatising European securitisations. An EU framework based on such criteria would help to facilitate robust and well-functioning securitisation markets. It would also be closely aligned with the Commission’s priority to improve financing of the EU economy through Capital Markets Union.

This section of our response summarises our views on the following key aspects of the consultation: criteria; prudential treatment; risk retention; transparency; SMEs; and implementation. The responses in the sections following this executive summary address the questions posed in the consultation document.

Criteria

Significant progress has already been made at the international and EU levels to develop criteria that could be used to identify STS securitisation, including by the Commission itself. The BoE / ECB received helpful comments from a wide range of market participants and stakeholders on the joint BoE / ECB discussion paper published last year on a better functioning securitisation market. Respondents were broadly supportive of the concept of and principles for STS securitisation. Earlier this year, the Commission adopted delegated acts on the Liquidity Coverage Ratio and Solvency II. Those delegated acts differentiated the application of certain prudential requirements for credit institutions, investment firms and insurers based on criteria for STS securitisation. That was an important step forward. In the latter part of 2014, BCBS-IOSCO and the EBA consulted on more detailed criteria. Work continues to develop and enhance those criteria further.

The BCBS-IOSCO and EBA criteria provide a good basis for an EU framework for identifying STS securitisation. In developing such a framework, it will be important to incorporate enhancements made to those criteria in light of the responses to the recent BCBS-IOSCO and EBA consultations. This will help to ensure that a new EU securitisation framework is robust, effective and internationally consistent. Furthermore, consideration should be given to the appropriate treatment of Asset Backed Commercial Paper (ABCP) within such a framework.

Prudential treatment

Appropriate prudential recognition should be afforded to STS securitisations. That recognition should reflect the lower risk profile of such transactions relative to non-STS transactions. This year, the Basel Committee is considering how to incorporate criteria for STS securitisation in its revised securitisation framework. Including such a distinction for STS transactions in the context of the revised securitisation framework for credit institutions would address the shortcomings of the current framework and introduce greater risk sensitivity. The risk sensitivity of capital charges for STS securitisations should also be increased under Solvency II. That would help to reinforce the role of insurers as long-term providers of finance to the real economy.

Risk retention

Risk retention requirements play an essential role in aligning the interests of the Securitising Party (e.g. the original lenders / sponsors / originators) and investors. To ensure the integrity of the risk retention framework, loopholes, such as the one created by the current definition of “originator” used for credit institutions should be revised. Such loopholes allow scope for structures that meet the letter of the rules but fail to align incentives properly.

For STS securitisation, the “indirect approach” to due diligence on risk retention – which places the onus on the investor of verifying compliance with risk retention rules by the Securitising Party – should be complemented with a “direct approach” that imposes compliance directly on the issuers. That would allow investors, when completing due diligence on risk retention, to place reliance upon attestation provided by the Securitising Party. It would also help to ensure risk retention rules are implemented effectively and consistently across jurisdictions.

Transparency

Further steps could be taken to increase the transparency, consistency and availability of key data for investors in securitisations. The standardisation and ease of access to data were highlighted by investors responding to the BoE / ECB Discussion Paper as aspects where further improvements would be helpful. Additionally, securitisation-related reporting requirements offering materials and terminology could be standardised and made easier to use.

SMEs

One transparency issue in particular requires urgent attention and action: the need to improve the availability of Small and Medium Enterprises (SME) credit data in the EU. A major impediment affecting the securitisation of SME loans is the lack of investor confidence in the quality of underlying SME loans. Improving the availability of key performance metrics, while complying with national confidentiality laws, would significantly increase transparency and reduce concerns about the asymmetry of information between originators and investors.

Implementation and enforcement

A process of self-attestation of Securitising Party compliance with the STS criteria would be needed. Such a process should be augmented by appropriate supervisory oversight and an appropriate sanctioning mechanism where the criteria are not met.

Monitoring and consistency

We would urge the Commission to assess on a continuing basis the adequacy of measures introduced for STS securitisation, the consistency with relevant international standards and the relative treatment of similar financial instruments, in particular covered bonds which should also be subject to appropriate improvements in prudential standards. The consistency of legislation for, and implementation of, an EU framework for STS securitisation will be imperative for ensuring the sustainable revitalisation of the European securitisation market.

Question 1:

A. Do the identification criteria need further refinements to reflect developments taking place at EU and international levels? If so, what adjustments need to be made?

Yes.

The Commission has already taken positive steps by setting out identification criteria for differentiating securitisation through the Liquidity Coverage Ratio (LCR) and Solvency II delegated acts. We agree that it would be appropriate to go further by applying foundation criteria for STS securitisations across relevant aspects of EU law. This could help to ensure the achievement of the objectives for securitisation set out in the joint Bank of England and European Central Bank discussion paper “The case for a better functioning securitisation market in the European Union”, namely: sustainability, risk transfer, funding and risk management.

It will be important for the Commission to reflect in proposals for STS securitisations the further progress made by the EBA and BCBS-IOSCO to develop criteria. Both bodies recently consulted on more developed criteria for securitisation. Both have received detailed feedback from stakeholders which will require careful consideration. The Basel Committee on Banking Supervision (BCBS) is also considering this year how to incorporate STC criteria into its revised securitisation capital framework. This may include adding supplementary criteria for the purpose of regulatory capital treatment.

Building upon the criteria developed by the EBA and BCBS-IOSCO would help to ensure that the STS framework criteria are robust, effective, practical and internationally-consistent.

B. What criteria should apply for all qualifying securitisations (‘foundation criteria’)?

It is not possible to provide a definitive answer to this question at this stage. We suggest this should be determined in light of the responses to, and results of, the EBA and BCBS-IOSCO consultations.

Question 2:

A. To what extent should criteria identifying simple, transparent, and standardised short-term securitisation instruments be developed? What criteria would be relevant?

Short-term securitisation instruments, such as Asset-Backed Commercial Paper (ABCP) programmes can provide an important source of funding for the real economy. For example, they provide financing for trade receivables originated by credit institutions, for shorter-term loans and leases, and for receivables originated by finance companies. However, short-term securitisation instruments such as ABCP have certain unique aspects that would not be consistent with the criteria applicable for longer-term securitisation. These characteristics include: the heterogeneous nature of the underlying assets, the nature of the security interest on the assets, the role of the sponsor in ABCP programmes, the use of liquidity support facilities in ABCP programme structures, and commercial sensitivities on the disclosure of data on underlying portfolios.

In the absence of distinct criteria for ABCP, it would be particularly important to develop an approach that did not classify ABCP automatically as non-STS. Otherwise there could be adverse impacts on the lending which underlies the ABCP programmes.

Internationally, the BCBS-IOSCO, in its recent discussion paper, has also asked for public input on the need to develop differentiating criteria for ABCP, in a manner similar to that for term securitisations¹.

¹ “Criteria for identifying simple, transparent and comparable securitisations”, joint BCBS-IOSCO Consultative Document, December 2014.

B. Are there any additional considerations that should be taken into account for short-term securitisations?

In considering the treatment of short-term securitisations, it is also important to draw a distinction between: (a) short-term instruments that are issued as part of long-dated securitisation transactions; and (b) other short-term securitisations, such as ABCP.

The items captured under point (a) are exposed to the same risks as longer-term notes in the same structure. Therefore, they should be subject to the same criteria as long-term notes.

ABCP is typically classified as a money market instrument. In developing any criteria for short-term securitisations such as ABCP, it would be important to differentiate between arbitrage conduits on the one hand and multi-seller ABCP conduits on the other, including considerations such as:

- commercial paper (CP) issued by arbitrage conduits proved to be illiquid at the height of the global financial crisis, due to over-reliance on asset sale proceeds to refinance issued CP; and
- CP issued by multi-seller ABCP conduits is typically reliant on liquidity provided by the bank/sponsor. The credit quality of the liquidity provider and disclosure requirements relating to the liquidity provider can therefore be critical to multi-seller ABCP conduits.

Question 3:

Are there elements of the current rules on risk retention that should be adjusted for qualifying instruments?

Yes.

Risk retention is an important means of aligning the economic interests of those originating exposures underlying a securitisation transaction - the originator, sponsor or original lender - and the investors in that transaction. The CRR requirement for the retention of a material net economic interest in a securitisation is effective and appropriate. We do not believe that alternative or additional forms of risk retention should be considered at this time. This view was also expressed by the EBA in its recent report on risk retention, due diligence and disclosure.

A particular concern, though, is a loophole in the "originator" definition of the CRR (Article 4(1)(13)). The recent EBA report on securitisation risk retention, due diligence and disclosure highlights this issue, citing the problem of securitisation structures designed to meet the definition which conflicts with the intention of the CRR's retention requirements. In particular, we are concerned that the element of the originator definition that allows an entity that purchases a third party's exposures for its own account and then securitises them - CRR Article 4(13)(b) - can result in the misalignment of the interests of the party underwriting the underlying obligations and those of the final investors. We consider this loophole should be closed in legislation, both for STS and non-STS securitisations. Further consideration should be given to which counterparty would be best placed to retain the interest for securitisations issued by non-bank originators.

B. For qualifying securitisation instruments, should responsibility for verifying risk retention requirements remain with investors (i.e. taking an "indirect approach")? Should the onus only be on originators? If so, how can it be ensured that investors continue to exercise proper due diligence?

The current setup of an indirect approach has the merit of ensuring that bank investors only purchase securitisations where there is alignment of interests, irrespective of the jurisdiction where they were issued. This approach – in place in the EU since 2011 - has been particularly useful in the aftermath of the crisis when non-European jurisdictions did not yet have risk retention regimes in place. However,

feedback from investors² is that the indirect approach sometimes causes legal uncertainty because it is difficult for investors to ascertain whether the original lender, originator or sponsor is complying with the risk retention requirement on an ongoing basis.

Both the EBA and BCBS-IOSCO have consulted on criteria that require the alignment of interests by issuers and clear disclosure confirming that this has been achieved. An indirect approach places the onus of verifying compliance with risk retention rules by the Securitising Party on the investors, while a direct approach places the onus on issuers and lowers the due diligence cost for investors.

As a result, the EBA, in its recent report, recommended that the current indirect approach should be complemented with a direct approach.

We support EBA's recommendation, which would apply to the whole securitisation market, not only to STS securitisations, and consider that it strikes the prudent balance between maintaining the responsibility and correct incentives of all parties to a securitisation, while minimising unnecessary due diligence costs for investors. When undertaking their own due diligence investors should be able to place reliance upon the attestation by the issuer that a securitisation meets with the STS criteria including risk retention requirements, for satisfaction of investors' own risk retention obligations.

A high degree of transparency and comparability of such disclosure would be helpful for investors. Disclosure about retention should be clear and accurate to assist regulated investors (for example UCITs, AIF managers) in efficiently conducting their due diligence.

Question 4:

A. How can proper implementation and enforcement of EU criteria for qualifying instruments be ensured?

A framework for proper implementation and enforcement of STS securitisation criteria would need to strike an appropriate balance between reliance on firms to ensure compliance with the criteria and supervisory oversight. Such a process needs to be designed with the following objectives in mind: a) achieve clarity and certainty as to which securitisations are STS and which are not; b) preserve the right incentives of the key parties, namely the need for investors to undertake their due diligence requirements as STS securitisations are not equivalent to risk-free investments and, for originators, the need to maintain their responsibility in the process. The implementation process needs to be designed in a way that minimises moral hazard. In this sense, certifications from supervisors and third parties should be avoided, as such certifications would obviate the need for both investors and the Securitising Party to retain responsibility for their role in the process. Further considerations include consistency with the implementation and enforcement process for covered bonds and achieving harmonisation across jurisdictions. A process might comprise the following elements:

- implementation by the Securitising Party of processes to ensure the STS criteria are met;
- self-attestation by the Securitising Party of compliance with the criteria based on an appropriate level of assurance; and
- an appropriate degree of supervisory oversight of the Securitising Party by market regulators.

Originators/ original lenders / sponsors of securitisations would be the parties most familiar with the assets underlying a securitisation, the servicing requirements and portfolios' structural characteristics. Therefore, they would be best placed to establish the processes needed to ensure compliance with the STS criteria, supported by a sufficient level of assurance. Self-attestation of compliance with the criteria would place the onus clearly on the Securitising Party to ensure they were met in practice. Those attestations would need to be disclosed clearly in offering documents for STS securitisations. To ensure the criteria were met, and to maintain market confidence in STS transactions, some degree of supervisory oversight would be needed. This could involve market regulators reviewing the Securitising Party's processes for ensuring

² See "EBA report on securitisation risk retention, due diligence and disclosure", 22 December 2014.

compliance with the criteria and sample transactions as well as developing appropriate sanctioning mechanisms.

B. How could the procedures be defined in terms of scope and process?

The scope of the self-attestation by the Securitising Party should be across all the criteria relevant to achieving STS status.

Standardised disclosure templates for attestation could be developed to assess compliance with the set of criteria. This could help to ensure concise, transparent disclosure of adherence with the criteria, by the self-attesting Securitising Party. Such templates could be employed consistently across transactions issued within a single asset type and may warrant some degree of differentiation between asset classes, accounting for specific differences. For example differentiation would be warranted between the different security rights on secured residential mortgages and on unsecured consumer assets. Any self-attestation and compliance with criteria should be clearly and fairly communicated to investors in much the same way as suggested in our response to question 3(B).

C. To what extent should risk features be part of this compliance monitoring?

The Securitising Party should confirm compliance of the asset portfolio, structure and ancillary service providers with risk-related criteria as part of their attestation. For example, originators/original lenders could attest that they originated the underlying exposures in accordance with sound and prudent credit criteria. Any self-attestation and compliance with criteria should be clearly and fairly communicated to investors in much the same way as suggested in our response to question 3 (B).

Supervisory oversight over the compliance procedures could help to ensure their effectiveness.

Question 5:

A. What impact would further standardisation in the structuring process have on the development of EU securitisation markets?

The legal form of structures or vehicles used in securitisations is significantly dependent upon specific national contractual, property and insolvency laws and practices, particularly in relation to the legal position of the underlying assets, security interest(s) and transfer of legal rights. In principle, we support efforts for further standardisation, however careful analysis of what could be standardised is needed in light of differences in contractual, property and insolvency law across the EU.

Separate to the legal form, a number of risks may be common across asset classes, jurisdictions, securitisation issuance types and underlying assets. The use of structuring techniques, such as inclusion of triggers within liability payment priorities and common conditions related to noteholders' rights, assist in mitigating such risks, whether these are pursuant to national securitisation regimes or by way of contract. These stated mitigants, along with others, share common features across jurisdictions and therefore may be worth considering for a harmonised approach in how they are used within SST securitisations.

B. Would a harmonised and/or optional EU-wide initiative provide more legal clarity and comparability for investors? What would be the benefits of such an initiative for originators?

See response to question 5(A).

C. If pursued, what aspects should be covered by this initiative (e.g. the legal form of securitisation vehicles; the modalities to transfer assets; the rights and subordination rules for noteholders)?

See response to question 5(A).

D. If created, should this structure act as a necessary condition within the eligibility criteria for qualifying securitisations?

See response to question 5(A).

Question 6:

A. For qualifying securitisations, what is the right balance between investors receiving the optimal amount and quality of information (in terms of comparability, reliability, and timeliness), and streamlining disclosure obligations for issuers/originators?

There should be sufficient disclosure to ensure investors can understand the basis on which STS criteria have been met and to be able to assess adequately the risks to which they are exposed.

Apart from the prospectus, two key building blocks for disclosure are investor reports and loan level data.

Investor reports are generally timely and reliable. However, improvements can still be made to achieve comparability and completeness. Qualitative disclosures, such as those on underwriting and servicing procedures, should be complemented with the reporting of defaults, delinquencies, arrears and other risk metrics, such as forbearance and prepayment rates, according to standardised terminology. This would help to facilitate comparability of key STS securitisation performance metrics across issuers. Comprehensive disclosure of key performance metrics is also important, e.g. it has been noted that some investor reports do not contain sufficient disclosure of prepayment information or default rates.

Loan level data are an important complement to investor reports and it is important to be able to reconcile loan level data with the investor reports. Striking the right balance between adequate disclosure and undue burden for investors is key. Developments in technology now facilitate collection and disclosure of loan level data by issuers, even for very large portfolios of assets. But feedback indicates that investors still find the management of loan level data challenging. In order to help investors exploit loan level data to the fullest, the continued development of tools to analyse large quantities of data will be beneficial. There is evidence that market data providers are filling this gap. This should improve investor analysis and due diligence, compared with investors relying just on investor reports.

With regard to the standardisation of loan level data disclosure in terms of comparability, reliability and timeliness, it should be noted that the Commission Delegated Regulation (EU) 2015/3 (the CRA Delegated Regulation)³ already establishes the required fields in the loan level templates as well as the reporting frequency (which should be at least quarterly and in line with the frequency of investor reports).

B. What areas would benefit from further standardisation and transparency, and how can the existing disclosure obligations be improved?

Loan level reporting templates are already standardised (see the CRA Delegated Regulation). There could be further standardisation of investor reports, and in particular the inclusion of standardised format for definitions of key performance metrics (see question 6(A)). Furthermore, disclosures should be required of the Securitising Party's attestation of compliance with the STS criteria. The form of these disclosures could be set out in standardised templates (see question 4).

³ Commission Delegated Regulation (EU) 2015/3 available at: <http://eur-lex.europa.eu/legal-content/EN/TXT/PDF/?uri=CELEX:32015R0003&from=EN>.

C. To what extent should disclosure requirements be adjusted – especially for loan-level data – to reflect differences and specificities across asset classes, while still preserving adequate transparency for investors to be able to make their own credit assessments?

As mentioned in question 6(A), with the rapid developments in technology and big data processing, there is a reduction in the limitations to the provision of loan level data by issuers and its processing by investors.

Question 7:

A. What alternatives to credit ratings could be used, in order to mitigate the impact of the country ceilings employed in rating methodologies and to allow investors to make their own assessments of creditworthiness?

Recent EU legislation has placed significant emphasis on reducing reliance on external ratings, and in ensuring investors have sufficient information to make their own assessments of creditworthiness. To reduce reliance on ratings, investors should ideally have the same information as that which is available to rating agencies. Further enhancement of the provision to investors of clear, concise and accessible transaction level information, as well as initial and on-going data, will thus be critical to support investors making their own assessment (see answers to question 6).

In general, the criteria underlying STS securitisations should make it easier for investors to make their own assessments, thereby reducing their reliance on ratings.

B. Would the publication by credit rating agencies of uncapped ratings (for securitisation instruments subject to sovereign ceilings) improve clarity for investors?

Yes.

The feedback we have received to our joint consultation paper shows general support for the idea that those credit rating agencies which do not already provide sovereign rating/counterparty rating sensitivities could usefully do so⁴. We have since observed positive emerging practices by credit rating agencies with the publication of further information around capped ratings. We welcome efforts by credit rating agencies and other market participants in moving towards full transparency of the rating process.

While noting the regulatory appetite for reduced reliance on credit rating agencies' ratings, where ratings are used in the determination of regulatory capital and liquidity treatment, these should continue to be based on the published rating that takes into account the full ratings methodology.

Question 8:

A. For qualifying securitisations, is there a need to further develop market infrastructure?

A central repository for all documentation and data related to STS securitisation instruments could help to ensure that investors have ready access to information. The European Data Warehouse is an example of such a central repository. More generally, we also note that the Regulation (EC) 1060/2009, as amended and supplemented (CRA), already envisages the development of a repository in the near future. We believe that access to such a central repository should be available free of charge to all investors.

⁴ "The case for a better functioning securitisation market in the European Union – Synthesis of responses" - 1 October 2014, available at <https://www.ecb.europa.eu/pub/pdf/other/141013-abs-synthesis-responses.en.pdf>.

B. What should be done to support ancillary services? Should the swaps collateralisation requirements be adjusted for securitisation vehicles issuing qualifying securitisation instruments?

Derivatives are an important ancillary service for securitisation vehicles. Derivative collateralisation requirements for securitisation special purpose entities (SSPEs) should apply in the same way as for derivatives executed by covered bond issuing entities, i.e. that all STS securitisation vehicles, meeting the definition of an SSPE under Article 4(1)(66) of the CRR should be exempted from the legislative requirements to provide collateral. This proposed exemption would likely apply to those securitisation vehicles that are categorised as either a financial counterparty or non-financial counterparty above the clearing threshold (as defined in Regulation (EU) No. 648/2012).

Such an exemption is justified on the grounds that the derivative counterparty typically benefits from greater security protection than the issuer, and that any provision of margin by the issuer to the derivative counterparty may disproportionately divert cash-flows otherwise due to fund payments due to noteholders without granting noteholders any greater protection against the risks specific to the performance of the derivative contract and/or credit risk on the derivatives counterparty. However, such a proposed exemption should not otherwise serve to limit or reduce the regulatory objectives of the risk mitigation techniques for non-CCP cleared derivatives set out in EMIR Article 11, along with other specific reporting obligations which may benefit noteholders without adversely affecting the cash-flows for note payments.

In addition to the proposed exemption we would further support an aligned treatment for derivatives executed by SSPEs and covered bond issuing entities. This is justified on the basis of similarities between these two types of issuing entities including:

- bankruptcy-remote or equivalent status;
- isolation of assets transferred to the issuer vehicles away from originators and servicers;
- the derivative instruments used are typically interest rate or currency derivatives ;
- derivatives used in both types of vehicles are generally exclusively for offsetting mismatches between flows from assets and to liabilities;
- all assets within each issuer vehicle type are assigned to different secured credit counterparties leaving no excess cash or assets for providing margin;
- being structured to provide security to credit counterparties (including derivative dealer entities) over the assets within the issuer vehicle;
- for derivatives hedging asset-side cash flows, derivative dealer entities typically rank senior to, or *pari passu* with, the senior noteholders in capital structure's priority of payments; and
- for derivatives hedging particular liabilities, derivative dealer entities typically rank *pari passu* to the liability being hedged.

In addition to the above, we support the continued trend towards greater transparency in securitisation disclosure documents in respect of derivative arrangements, including the way that specific EMIR obligations are addressed, as well as mitigating factors.

C. What else could be done to support the functioning of the secondary market?

Liquidity in the secondary market has in general been affected by the ABS markets' dwindling size and lack of primary market issuance. Nevertheless, a large amount of price information still exists for investors and the secondary market functions reasonably well given such circumstances.

A central repository for all documentation and data related to STS securitisation instruments that is free to access could help by ensuring that traders and investors have ready access to information they will require in order to price such instruments competitively (see answer to question 8(A)).

Question 9:

With regard to the capital requirements for banks and investment firms, do you think that the existing provisions in the Capital Requirements Regulation adequately reflect the risks attached to securitised instruments?

Existing rules laid down in the CRR are still largely based on the pre-crisis supervisory treatment of securitisations, as defined in the Basel II standard (International Convergence of Capital Measurement and Capital Standards, BCBS, June 2006). Therefore these provisions are subject to a number of shortcomings that have been identified during the crisis, such as:

- a mechanistic reliance on external credit rating agencies induced by the former hierarchy of approaches in the current regulatory framework;
- inappropriately distributed capital requirements across the different tranches of a transaction, with excessively low risk weights for highly-rated exposures, and excessively high risk weights for low-rated senior securitisation exposures in the light of their performance during the crisis;
- cliff-effects of capital requirements as evidenced by both the rapidity at which risk weights increased by credit quality step and the absolute differences in risk weights under the current securitisation framework.

Many of these shortcomings will be addressed once the Basel securitisation framework published in December 2014 has been implemented into European legislation. However, as evidenced by the experience of the crisis, the revised framework is insufficiently risk sensitive to the different risk profiles of securitisation products. STS securitisations, where the underlying risks can be assessed with more confidence, should have lower capital charges than complex securitisations, consistently with the EBA's findings from its October consultation paper⁵.

Question 10:

If changes to EU bank capital requirements were made, do you think that the recent BCBS recommendations on the review of the securitisation framework constitute a good baseline? What would be the potential impacts on EU securitisation markets?

We consider that the revised securitisation framework released by the Basel Committee on Banking Supervision in December 2014⁶ is an improvement compared with the existing regulatory framework as it addresses the shortcomings mentioned in question 9. We support the timely implementation of a revised framework, reflecting the improved risk sensitivity for STS securitisations, in the EU by January 2018.

BCBS-IOSCO's criteria for the identification of STC securitisations, potentially supplemented by additional, credit specific, criteria, as well as those developed by the EBA for SST securitisations, represent a good framework to identify securitisations with improved risk profiles that warrant different capital requirements from securitisations not meeting such criteria.

The incorporation of the concept of STS securitisations in the global and European regulatory framework would have benefits for the European securitisation markets:

- first, by differentiating capital charges for STS securitisations from the rest, the market could be stimulated to develop in a sustainable way;
- second, development of criteria to identify STS securitisations could considerably reduce the stigma associated with investment in securitisations post-crisis; and

⁵ <https://www.eba.europa.eu/documents/10180/846157/EBA-DP-2014-02+Discussion+Paper+on+simple+standard+and+transparent+securitisations.pdf>.

⁶ <http://www.bis.org/bcbs/publ/d303.pdf>.

- third, such securitisations could enable investors to assess investment risks with more confidence, given their simple and transparent structure.

Consequently, investors' exposure to the sector would be likely to increase, which in turn would strengthen incentives for credit institutions to use securitisation as a financial tool. That would enable credit institutions to transfer credit risk and facilitate further lending to the real economy. That would also improve the resilience of the financial system by providing an alternative funding channel for the real economy.

Question 11:

How should rules on capital requirements for securitisation exposures differentiate between qualifying securitisations and other securitisation instruments?

The implementation of any differentiated treatment between STS and non-STS securitisation should follow several principles:

- the criteria to identify STS securitisations should primarily focus on enhancing the risk sensitivity of the revised BCBS framework, upon implementation in the EU;
- any differentiation (encompassing both the criteria defining what is a STS securitisation and the differentiated regulatory capital requirements) should preferably be made in the context of the EU implementation of Basel's revised framework for securitisation;
- it should be readily implementable in a prompt and timely manner;
- it should fit within the broader framework of revised regulatory capital rules for securitisations and should not result in a completely separate regulatory treatment;
- in order to reflect the enhanced risk sensitivity that a distinction between STS and non-STS transactions would introduce, the resulting regulatory capital requirements for STS transactions should be lower relative to those for non-STS transactions; and
- any adjustment to regulatory capital requirements for STS securitisation should be appropriately prudent.

Question 12:

Given the particular circumstances of the EU markets, could there be merit in advancing work at the EU level alongside international work?

Over the past months, international regulators, supervisors and central banks have initiated several workstreams to define STS securitisations and to assess the merits of a differentiated regulatory treatment for those transactions. Although each of these initiatives is independent, they proceed from the same observation that securitisations performed differently during the financial crisis across asset and structure type as well as across jurisdictions. These various workstreams represent building blocks of a revised regulatory approach for securitisation.

As a second step, we support a uniform approach to definitions, including that of "STS securitisations". The criteria, definitions and terminology need to be interoperable across regulations yet remain flexible enough to deal with those attributes that are specific to the differing issuance types and the types of securitised assets that are originated and listed in the European capital markets. The establishment of a uniform set of criteria underpinning various pieces of European legislation would reduce regulatory uncertainty and help to de-stigmatise European securitisations.

Therefore the EU should closely monitor international developments and strive to ensure consistency within the EU regulatory framework and in relation to global initiatives. We welcome the BCBS's

announcement that it will consider during 2015 how to incorporate criteria such as those developed by BCBS-IOSCO into the revised securitisation capital framework.

Question 13:

Are there wider structural barriers preventing long-term institutional investors from participating in this market? If so, how should these be tackled?

Going beyond the need to make the changes to regulatory frameworks highlighted in the previous questions, securitisation still suffers from stigma.

The European ABS market has been shrinking steadily over the past few years, and primary market issuance is very low. Given the ABS market's dwindling importance in European capital markets, both issuers and investors are increasingly no longer seeing the ABS market as strategically important, but rather as a niche product.

It should be highlighted that ABS investments are subject to higher due diligence requirements than most other fixed income investments. Furthermore, analysis requires specialist personnel and tools. This increases the costs for institutional investors of investing in ABS relative to other instruments. Many of these costs are fixed costs which investors may find difficult to justify given the limited size of the current market for new transactions.

To reduce the costs associated with the due diligence process, standardisation, consistency, comparability and ease of access to data could be improved. Additionally, securitisation-related reporting requirements could be further standardised and made easier to use. In particular, investors would benefit from easier, more uniform access to information based on loan-level data as well as from standardised investor reports and definitions of key transaction terms and metrics.

Securitisation-related offering documentation and prospectuses could, to the extent not already required by EU legislation and regulatory requirements, further benefit from presenting relevant key information, including information set out in any "summary section" of a prospectus in a manner that allows investors an easier degree of comparability across issuances. The experience of the Netherlands, where simplification and harmonisation of prospectuses and jurisdiction-wide definitions has already occurred through market-led efforts, may be a useful case study. Moreover, full consistency for investors regarding their due diligence obligations across different regulations, e.g. applicable to credit institutions, insurance undertakings and funds, would also help minimise uncertainty, while also adding coherence (yet still reflecting inevitable differences in behaviour across investor types).

Question 14:

A. For insurers investing in qualifying securitised products, how could the regulatory treatment of securitisation be refined to improve risk sensitivity? For example, should capital requirements increase less sharply with duration?

The ECB and the Bank of England welcomed the introduction of a differentiated treatment for STS securitisations, in the form of Type 1 transactions, as defined in Article 177(1) of the Commission's Solvency II Delegated Regulation adopted in October 2014⁷. Nevertheless, the framework could benefit from increased risk sensitivity in a number of areas.

First, we agree that the current capital charges should increase less sharply with duration.

Second, risk sensitivity could be further enhanced by improving the sensitivity of STS securitisations relative to the credit quality steps. The current approach for STS (i.e. Type 1) securitisations results in equal charges for all investment-grade ratings below AAA. The risk sensitivity could be improved across the different credit ratings to ensure the charges reflect their relative risks.

⁷ <http://eur-lex.europa.eu/legal-content/EN/TXT/?uri=CELEX:32015R0035>.

Third, as discussed in question 14-B, the risk sensitivity of the framework could be significantly enhanced by considering different sets of capital charges for senior and non-senior tranches, both for STS and non-STS securitisations, recognising that both the STS status and seniority are significant risk drivers. This should also reduce the significant cliff effects between the Type 1 and Type 2 capital charges.

B. Should there be specific treatment for investments in non-senior tranches of qualifying securitisation transactions versus non-qualifying transactions?

The forthcoming framework only considers as Type 1 the senior tranches of a securitisation meeting certain simplicity, transparency, credit and liquidity criteria. Consequently, non-senior tranches in such STS securitisations are considered Type 2 and subject to the same charges as non-senior tranches in non-STS securitisations. As expressed in the joint ECB-BoE paper “The Case for a better functioning securitisation market in the European Union”, we think all tranches of a given transaction should be treated as STS securitisations, as benefits identified by the criteria would not be limited to the most senior tranche but would apply to all positions for a given issuance.

Seniority is an important risk driver for liquidity as well as credit quality and there is a case for differentiating charges. We believe there should be a distinction for seniority within both STS and non-STS securitisations. Such distinctions within (and across) STS and non-STS securitisations should be calibrated to ensure that charges for different categories appropriately reflect differences in risk. This should preclude unwarranted differences and cliff effects between STS and non-STS securitisations.

Question 15:

A. How could the institutional investor base for EU securitisation be expanded?

The EU legislative framework should seek to promote a wider institutional investor base for EU securitisation. Standardised criteria for “STS securitisation” will help to broaden the range of investors. As described in the answer to question 14, we propose a reassessment of regulatory capital requirements for insurers. We also advocate measures to increase standardisation, comparability and transparency of issuances as well as underlying data (as described in our responses). We support the view that greater standardisation and simplicity of certain ABS issuances may enhance liquidity and trading of such issuances and make them more attractive to a wider institutional base.

We also believe that such initiatives would not negate or otherwise reduce the need or appetite in the market for more complex issuances, which we would imagine could still continue to exist and be structured to meet the needs of relevant originators and investors.

B. To support qualifying securitisations, are adjustments needed to other EU regulatory frameworks (e.g. UCITS, AIFMD)? If yes, please specify.

We support the need for convergence across regulatory frameworks, including UCITS and AIFMD. This could be achieved by:

- developing common terminology for securitisation, including STS and non-STS securitisations;
- consistent disclosures of compliance with risk retention requirements; and
- harmonising due diligence requirements.

Originators also have a role to play by ensuring their offering documentation includes specific relevant information disclosures to make it easier for investors to satisfy specific contractual, fiduciary or statutory compliance requirements for certain investments. Further consideration should be given to adjustments needed to the UCITS and AIFMD frameworks for STS securitisations in the manner suggested in our responses above.

Question 16:

A. What additional steps could be taken to specifically develop SME securitisation?

We highlighted in our reply to question 13 the need for improved standardisation and ease of access to data. In our view one more specific transparency issue requires urgent attention and action: improving the availability of Small and Medium Enterprises (SME) credit data in the EU. A major impediment affecting the securitisation of SME loans, while comparably less of an issue for consumer loans, is a lack of sufficient investor confidence in the quality of the underlying SME loans. Improving the availability of key performance metrics, while complying with the national confidentiality laws, would significantly increase transparency and decrease concerns regarding the asymmetry of information between originators and investors.

Furthermore, we support the Commission's initiatives proposed in the Green Paper "Building a Capital Markets Union" and its endeavour to identify and assess obstacles to integrated capital markets arising from company law, corporate governance, insolvency laws and taxation. Overcoming such obstacles would certainly also be beneficial to develop SME lending and SME securitisation.

B. Have there been unaddressed market failures surrounding SME securitisation, and how best could these be tackled?

Refer to answer to question 18.

C. How can further standardisation of underlying assets/loans and securitisation structures be achieved, in order to reduce the costs of issuance and investment?

We would welcome investigation of the benefits of an EU framework and market infrastructure to facilitate non-financial corporate loan sales. One possibility is incorporation in a forthcoming EU legislative framework on securitisation. This might include assessing the benefits that standardisation of both loan documentation and market practice have brought in terms of origination and trading costs across certain loan markets. These benefits of standardisation in a number of loan markets have affected both the origination and issuance of corporate loans but more importantly the secondary trading of debt. Enhancing the liquidity of underlying assets/loans of securitisation structures is likely to support securitisation issuance and investment.

D. Would more standardisation of loan level information, collection and dissemination of comparable credit information on SMEs promote further investment in these instruments?

See answer to question 16 A.

Question 17:

To what extent would a single EU securitisation instrument applicable to all financial sectors (insurance, asset management, banks) contribute to the development of the EU's securitisation markets? Which issues should be covered in such an instrument?

We view having some uniform set of criteria underpinning various pieces of legislation as key to attracting a broader investor base and to de-stigmatising European issued securitisations. In this respect we see the need to harmonise legislation, building on the concept of STS securitisations.

We view the following two elements as essential to be addressed in an EU securitisation legislative framework, which would comprise a common definition of STS securitisations, building criteria developed by the main regulator-led initiatives for STC and SST securitisations:

- **Scope of application of STS criteria:** STS criteria for inclusion in an EU securitisation legislative framework should be developed as a matter of urgency. The opportunity to develop comparable criteria for ABCP will also deserve further analysis in the short to medium term.
- **Modular approach in specifying criteria:** We suggest following a modular approach in specifying the relevant criteria. In a first step harmonised foundation criteria should be developed for cross-sectorial application. The EBA criteria (excluding the credit-related criteria) as defined in the above-mentioned EBA discussion paper⁸ could serve as a starting point for term securitisation. Dedicated STS criteria should be considered for ABCP. In a second step specific modular criteria could be developed in relation to treatments for liquidity, credit, collateral, etc. within the relevant regulatory or legislative frameworks.

We also see merit in harmonising further the overall framework for securitisation. Such an initiative should cover at least the following areas:

- **Standardisation of definitions:** There are notable benefits in moving towards developing and using consistent definitions within STS securitisations. However careful consideration should be given as to whether this could be most effectively achieved through encouraging better market practice or through a legislative framework.
- **Standardisation of investor reports:** The standardisation of investor reports (short-term regulatory objective) and, to the extent necessary, a further standardisation of prospectuses to enhance the comparability of securitisations across issuances (medium-term regulatory objective) for STS securitisations could bring significant benefits to the functioning of the European securitisation market. However, as with the standardisation of definitions, careful consideration should be given to whether this could be achieved through better market practice or through a legislative framework.

Question 18:

A. For qualifying securitisation, what else could be done to encourage the further development of sustainable EU securitisation markets?

The costs securitisation vehicles incur when entering into derivatives and third party service agreements should not be increased unnecessarily.

In addition, risks relating to collection accounts, as well as transaction accounts, persist. Since the crisis a number of jurisdictions have implemented contractual and/or statutory measures to mitigate and/or reduce the risks that could arise in the event that: the account provider becomes insolvent; is placed into a recovery and/or resolution plan; and more generally to reduce commingling risk. Such events, unless mitigated, could have a possible direct adverse impact on payment of funds by the securitisation issuer to noteholders.

A number of these market-led contractual structural mitigants include any combination of standalone segregation of accounts; daily cash sweeps; collateralisation arrangements; additional security interests or creation of trusts/foundations or such analogous concepts as well as the provision of ratings-based triggers prompting the replacement of the original account provider with a suitably rated replacement provider within a set time-period. We also note and welcome steps taken by various jurisdictions that provide for asset segregation (which extends to accounts) in statutory provisions specifically catering for securitisations. Such provisions include *inter alia* the identification, isolation and segregation of funds and accounts and the immediate transfer to the issuer in accordance with contractual provisions irrespective of actions in any insolvency proceeding, and to the extent relevant/legally catered for, any action by a competent resolution authority in respect of a regulatory led resolution plan.

Feedback from bank originators is that securitisation has a role as an alternative source of funding but, in current market conditions, may remain less cost effective for many banks than other sources, including

⁸ <https://www.eba.europa.eu/documents/10180/846157/EBA-DP-2014-02+Discussion+Paper+on+simple+standard+and+transparent+securitisations.pdf>.

covered bonds and retail deposits. MREL/TLAC requirements will also encourage issuance of long-term, unsecured debt.

The added value of securitisation is therefore risk transfer, including potentially taking securitised assets off regulatory risk weighted assets and accounting balance sheets, freeing capacity for additional lending. Whereas outright sales may often make more sense for impaired assets and discontinued businesses, securitisation can work well for continuing businesses and good quality assets that remain part of a bank's core strategy.

Originators have asked for greater consistency in how the process of achieving regulatory capital relief is supervised. We welcome the recommendations of the EBA guidelines on significant risk transfer they represent a positive step towards a more consistent application across the EU. Going forward, STS required information and procedure disclosures (e.g. priorities of payments, availability of performance history, and consistency of underwriting) may contribute to facilitate regulatory reviews of SRT and improve their consistency.

With the leverage ratio, bank issuers might increasingly seek to sell the whole capital structure (all tranches) of a securitisation in order to move the assets off their accounting balance sheet. Accounting standards should continue to set robust tests for off balance sheet treatment. But it may be worth investigating further whether those tests are always applied consistently by auditors and whether processes can be improved.

B. In relation to the table in Annex 2 are there any other changes to securitisation requirements across the various aspects of EU legislation that would increase their effectiveness or consistency?

See reply to question 15 B.