



EUROPEAN CENTRAL BANK

EUROSYSTEM

RESULTS OF THE PUBLIC CONSULTATION ON THE PROVISION OF ABS LOAN-LEVEL INFORMATION IN THE EUROSYSTEM COLLATERAL FRAMEWORK

I INTRODUCTION

On 23 December 2009 the European Central Bank (ECB) launched a public consultation on loan-by-loan information requirements for asset-backed securities (ABSs) in the Eurosystem collateral framework. The public consultation included six questions on the general advisability of the initiative and on the technical implementation details. By the end of the consultation period on 26 February 2010, 53 responses had been received from a broad range of market participants, including investors, market data vendors, credit rating agencies, financial service providers, audit firms, stock exchanges, law firms, public authorities and central securities depositories. This report presents a summary of the key points made in the responses.

2 RESULTS OF THE PUBLIC CONSULTATION

The public consultation revealed very strong support for the initiative. The main reason given for supporting the initiative was the increase in transparency levels, which would contribute to more informed risk assessments, thereby helping to restoring confidence in ABS markets. In addition to expressing their strong support, respondents made a number of recommendations to the Eurosystem regarding specific implementation details that should contribute to a smoother introduction of ABS loan-by-loan data.

In the remainder of this report, the responses to the questions are summarised and the main recommendations made by market participants are listed.

QUESTION 1

What would be, in your view, the foreseeable benefits and costs of having loan-by-loan data on an ongoing basis for market participants? Do you see alternative ways of achieving a major improvement in ABS transparency?

BENEFITS

The vast majority of respondents considered that the provision of more detailed information would help the market to assess the risks associated with ABSs. Most responses also mentioned that the reporting of this type of data to the broader market on an ongoing basis would contribute to restoring investor confidence in the securitisation market.

Specific supporting arguments are listed below:

(a) Investors support the provision of more information on securities that they invest in or might invest in. Loan-level information would provide a significant amount of very valuable data. Investors think it would unquestionably benefit all types of investors, as well as the general level of liquidity in the market. It also has the potential to bring much needed new investors to the market. Some responses included cost/benefit analyses clearly indicating that the benefits would by far outweigh the costs of providing loan-level data. In an extreme scenario, one respondent estimated the annual costs for an infrastructure that would allow the availability of *daily* performance data at 0.05% of the principal amount of loans included in a securitisation, which was perceived as far outweighing potential losses stemming from the inability to accurately assess and price the risk of securitisations.

(b) The provision of loan-level data would give investors certain options: they could either use the enhanced loan-level information themselves or, alternatively, employ third parties that would transform the loan-level data into a more useable and value-added format. Among those investors that would choose to build their own transaction models, many believed that they would have the ability to process the enhanced loan-level information to construct cash-flow models of the transactions necessary for valuation purposes and that they might try to build predictive collateral performance models. Other investors may rely on third-party models developed with the enhanced loan-level data.

(c) Investors suggest that all market participants would benefit from the significantly enhanced ability of cash-flow modelling engine providers to use loan-level data rather than aggregated information in their models. Increased accuracy would help all investors that subscribe to those modelling engine providers. Enhanced modelling capabilities would undoubtedly bring much needed enhanced liquidity to the European market as both sides of the trade would be modelled on the same loan-level input assumptions (investors recognise that the much greater liquidity of the US markets has been driven by this factor).

(d) Investors are also supportive of the provision of loan-level data to all classes of investors and all market participants as the provision of information to only some investors (for example those in the more junior classes, or solely those that currently hold the securities) would cause an unhelpful information asymmetry between investors and/or potential investors and could potentially be in breach of regulations such as the EU Market Abuse Directive.

(e) It is also highly likely that the new requirements of the Capital Requirements Directive, in particular Article 122a, which increases investors' due diligence obligations not only on the underlying assets, but also on the structures and cash flows, are likely to have an impact on investor behaviour, as well

as on the need for data and the ability to assess transactions on the basis of such data.

COSTS

(a) One particular concern raised by issuers/originators regards the possible introduction of loan-level data requirements for already existing securitisations. While it is expected that standardised loan-level data reporting will be easier to implement for new transactions, where there would be an opportunity for the issuers to take the ECB requirements into consideration in the structuring and development of the transaction and asset origination, this may be more complex for already existing transactions. Similarly, such concerns were raised regarding some existing underlying assets, which may be securitised after the implementation of the loan-level reporting requirements, because for those loans the requested information may not be available or may not meet the quality standards.

(b) It was suggested to duly consider the scope, timing and costs of potentially necessary system changes. The need for such changes is particularly expected in cases where pools of assets are originated by originators operating different and not fully integrated data systems, as well as in the case of highly granular portfolios that are currently monitored and managed on the basis of more aggregated data.

(c) The envisaged reporting requirements could lead to the provision of overlapping information to more than one party, thus resulting in an additional administrative burden. This is based on the observation that issuers provide loan-level data at inception and sometimes on an ongoing basis to those credit rating agencies (CRAs) that rate each particular transaction for the purposes of ongoing monitoring. Issuers/originators propose that the ECB should coordinate with the industry and the CRAs with regard to the implementation, as well as any updates and amendments to the common reporting template, in order to maximise efficiency before and after implementation, as well as before and after issuance.

(d) Specific reservations were expressed by issuers of mortgage-backed master trusts with regard to the sometimes large number of loans involved in these trusts. Moreover, the perceived resulting degree of diversification and structural features provided by these trusts are deemed to be a sufficient reason by these issuers to have a different approach to that envisaged for more traditional RMBS transactions as regards the provision of loan-level data.

(e) Only three respondents perceived that the benefits of the availability of loan-level data would not outweigh the costs involved, mainly for highly granular portfolios that are managed differently and where information at a more aggregated level could suffice. It was proposed to assess whether, for certain asset classes, stratification tables or redemption schedules may serve better the purpose of increased transparency.

RECOMMENDATIONS BY MARKET PARTICIPANTS

- (i) A very large majority of respondents support the initiative to require loan-by-loan information on underlying assets and urge the Eurosystem to press ahead with the project.
- (ii) Issuers/originators believe that an immediate implementation of the requirement to report loan-level information at the frequency and level of detail proposed may be difficult for market participants to comply with and, therefore, may even adversely affect the quality of the information provided. This would be an issue particularly in the early stages of the reporting regime, during which participants would need to ensure that they have established the necessary framework to comply with the Eurosystem requirements. Therefore, the Eurosystem would need to consider sufficient phasing-in periods, combined with incentive and penalty schemes, to gradually introduce the loan-level requirements. At the same time, a sense of urgency permeates many

of the responses, so the Eurosystem would need to carefully balance this urgency with the need to avoid an abrupt implementation of the loan-level concept.

- (iii) Market associations propose that, in order to achieve a consistent data quality, the data should be disseminated using a single format provided to the CRAs and the data-handling infrastructure. There should be ongoing coordination and consultation between the Eurosystem, the industry and the CRAs in relation to updates and amendments to loan-level RMBS data templates, and in relation to new templates for other asset classes when appropriate.
- (iv) Some responses suggest broadening the scope of the template by adding holistic borrower information in order to increase the ability to predict arrears and default. It is proposed to aggregate data provided for one obligor using a unique matching key, but without any personal identification information, in order to adhere to data protection requirements.

QUESTION 2

Is the concept of standardised loan-level templates for all European ABS transactions and per asset class valid? For what ABS classes is it possibly less obvious?

The concept of standardised templates is widely accepted as it would help to harmonise the reporting of information and provide greater consistency in the ABS markets. Market participants think that, given the range of securitisation types and underlying legal and institutional frameworks, it is very important that the standardised reporting framework should take into account differences between asset classes and jurisdictions.

It is recognised, as presented in the public consultation and in the example provided by

the ECB's RMBS template, that while the standardised ABS templates will have some common features, each asset and securitisation type, as well as each jurisdiction, will have its own data fields due to asset, jurisdictional, legal and operational particularities. Therefore, as proposed by the Eurosystem, market participants agree that the approach to formalising reporting templates should be taken on an asset class-by-asset class basis, starting with the template for retail mortgage-backed securities (RMBSs).

In terms of asset classes other than RMBSs, it is considered that it would be quite straightforward to continue with implementation of loan-level data reporting for commercial mortgage-backed securities (CMBSs). However, CMBS pools tend not to be very granular (i.e. there is a relatively small number of underlying assets in a CMBS transaction), the assets tend to be heterogeneous and, again, relevant data may vary significantly according to the jurisdiction. Some market participants believe that the principal challenge with a CMBS reporting template would, in fact, be to capture the non-standard asset- or jurisdiction-specific aspects of the underlying mortgage loans and properties relevant for investors' decisions.

Also a number of respondents, in particular originators/issuers, expressed the view that the concept may not be suitable for well-diversified, granular and/or revolving portfolios, such as those for auto loans and credit card receivables. It is argued that granularity mitigates the portfolio risk already, while the submission and assessment of highly granular data will not add value to investors' decisions. Moreover, in particular banks specialising in auto financing expressed concerns that the envisaged disclosure could lead to the unveiling of parts of manufacturers' pricing policy and margins, as they tend to subsidise loans for new car purchases.

RECOMMENDATIONS BY MARKET PARTICIPANTS

- (v) Issuers/originators recommend that the templates be phased in over time, starting with the template for RMBS transactions,

as suggested by the Eurosystem, since: (1) RMBSs are the largest securitisation transaction type; (2) the market practices in terms of the composition of underlying assets and transaction structures are relatively homogeneous within the different jurisdictions; and (3) the RMBS loan-level reporting template has already been significantly developed. In addition, it is recommended that a clear set of criteria and definitions should be agreed upon.

- (vi) It is stressed that each asset class must be appropriately defined and delineated from other asset classes in order to avoid overlap between, and the incorrect use of, the various reporting templates.
- (vii) Templates for other asset classes, such as CMBSs and small and medium-sized enterprise securitisations, would need to be considered and developed in separate projects.

QUESTION 3

In relation to the ECB's RMBS loan-level template, what fields would not be applicable in certain national markets? Why? What additional fields would be required, if any?

In general, the concept of the RMBS template is applicable in all jurisdictions. A number of respondents proposed amendments and/or additional fields for some jurisdictions, mostly relating to differing legal standards, customs and issuance. These comments could be addressed by a modular approach incorporating some variable fields in the templates, depending on the applicable jurisdiction. Detailed comments were received from market participants for various jurisdictions (France, Germany, Italy, Spain and the Netherlands). Three rating agencies also forwarded detailed comments for these and other jurisdictions regarding borrower information, loan characteristics, property collateral and performance information.

RECOMMENDATIONS BY MARKET PARTICIPANTS

- (viii) For some fields, issuers/originators would like the Eurosystem to consider the use of assumptions with appropriate clear disclosure. This could be the case for mortgage loans where the requested information may not have been gathered during the underwriting assessment of the loans, or may not have been recorded in the originator's systems.
- (ix) Issuers/originators also recommend that clarification be given as to what the consequences would be if information were not to be available (e.g. selection of the "no data" option).
- (x) Issuers/originators recommend that a naming convention to automate the provision of certain information should be provided.¹ More specifically, issuers/originators recommend that a sample of the data should be provided in the template, together with the format and specific valid values, to make sure that the data are consistently reported. Moreover, for each field a standard missing-value entry should be defined, to be used by all providers, which is not a value that could otherwise be a valid entry for that field.
- (xi) The process of producing and transmitting the relevant information should be carefully documented as data are usually produced by a third party (calculation agent, cash manager and/or paying agent) who has to communicate the information back to the originator who then has to transmit it to the data portal(s).
- (xii) To reap the full benefits of loan-level data, the data template must contain sufficient information to project the amortisation profile and interest rate path for each mortgage loan.² In particular, data fields relating to interest rate resets and/or changes in the repayment method should be mandatory, to be able to understand

the drivers of prepayments and defaults quantitatively and to forecast pool performance based on individual loan characteristics. More specifically, it is key to have knowledge of payment patterns experienced by the borrower; interest rate modifications over the life of the mortgage loan; prepayment penalties, if any; further advance options and values; and delinquency, default and liquidation information. In this regard, investors stressed the need for detailed information with regard to the coupon structure and redemption profile of the loans since this is a key requirement for transaction cash-flow modelling.

QUESTION 4

What impediments, if any, would originators have in submitting loan-by-loan information to fulfil the loan-level data requirements?

Most of the impediments mentioned relate to the cost aspects elaborated upon in the responses to question 1, in particular regarding IT adaptations, and also the need for a different treatment of old and new securitisations due to the lack of readily available systems and processes of the former. Moreover, a number of respondents expressed concerns regarding data protection and banking secrecy. While emphasis is given to the need for appropriate procedures and technologies to ensure anonymity for RMBSs, most responses suggest that such procedures could be developed for all ABS classes. Some market participants pointed

1 For example, if a mortgage loan has more than one borrower, one guarantee or one property, an indication of how to report the information (e.g. by including additional columns, rows or templates) should be provided.

2 Cash-flow model providers understand that one of the aims of the Eurosystem is to allow analysts to build better risk and valuation models. Without access to loan-level data, it is impossible to build accurate cash-flow models to convert pricing views (i.e. spreads) and performance assumptions (e.g. on the conditional prepayment rate (CPR) and/or the constant default rate (CDR)) to a fair price. The provision of loan-level data would enable investors to build more accurate cash-flow models and allow third-party vendors to improve their products.

to potential restrictions on the transmission of loan-level data in certain jurisdictions outside Europe, e.g. US securities laws on certain communications with respect to ABSs sold in the United States, may result in the need for certain electronic filters or screening pages. Market participants are of the view that it may be helpful to resolve this issue by obtaining clearance from the relevant US regulators for the provision of loan-level data for ABSs used in the Eurosystem collateral framework.

RECOMMENDATIONS BY MARKET PARTICIPANTS

- (xiii) It is deemed necessary to clarify the form in which the template information will be disclosed at the time of issuance in case the loan-level data have to be made available contemporaneously with issuance. It should be noted that material information must also be disclosed in the prospectus.

QUESTION 5

Which of the scenarios presented, or combination thereof, would provide the best solution to the market, taking into account considerations such as data consistency and quality, competition, governance, costs, ease of transmission of data, etc.?

Unlike for the other questions where a consensus emerged from market participants, there was a significant divergence in the responses to this question. It should be recalled that two opposite scenarios were presented in the public consultation document. In scenario 1 originators/servicers would have a clear single entry point for submitting the data, while in scenario 2 they would have the option of choosing from a set of registered portal providers. The single data portal would have to be selected from existing market data platforms that would be willing to take on the role of portal provider. The portal would need to ensure that the data are made available to other data providers and that the users of the portal services would be charged an appropriate price, whereas the registered

data portal providers under scenario 2 would compete to provide the best service at the lowest cost to their users. Fourteen responses supported option 1, emphasising that the single portal is most suitable to ensure full consistency of the data due to its single entry point for all originators. However, a number of responses highlighted the weaknesses of option 1, namely the lack of competition, which may lead to inappropriate pricing and/or a lack of data quality and timeliness. Also, some respondents referred to the higher operational risk in case of a failure by the data provider or the technical platform. Reflecting the disadvantages of option 1, nineteen respondents were in favour of option 2, arguing that if a number of data portal providers were to be allowed to compete, the natural market price for the provision of the services could be discovered. However, a number of the replies portray the advantages of option 1 as potential disadvantages of option 2. In addition, some investors expressed concerns that they may need to sign up to several portals to get all the data they require which may increase the operational burden and costs. Moreover, it was highlighted that although data would be standardised, there may be different loan-level data formats between portals, which could hinder further processing and analysis of the data.

Other respondents proposed hybrid solutions combining features of the two options. One investor suggested phasing in the disclosure of loan-by-loan data, at first through multiple channels like trustee websites and later through a single data portal. This would avoid delaying progress on the initiative due to a lengthy data portal selection process. One central securities depository suggested collecting and handling the loan-level data through existing market infrastructure. For example, the information could be stored in a database maintained by a securities numbering agency and thus data handling would benefit from taking place in a pre-existing environment subject to standards for operational resilience, data consistency and governance. In the same vein, one stock exchange suggested that the loan-level data could be disseminated through

regulated stock exchanges since this would use an already existing data-handling infrastructure, while at the same time ensuring that potentially price-sensitive information would be made available to the public as required by the Market Abuse Directive.

In addition, three respondents proposed that the Eurosystem should not pursue any fixed data-handling framework, but that originators/issuers should have the freedom to choose the means they intend to use to make their data available, including publication on their website. It was acknowledged by the respondents that this would require comprehensive auditing and quality assurance of data at the level of the originator/issuer.

QUESTION 6

Is an envisaged preparation time of 12 months after the announcement date sufficient to adapt to the loan-level data requirements? If not, why?

Regarding the timing of implementation, diverging comments were received. However, the majority of the respondents concluded that the envisaged preparation period of 12 months after the announcement date would suffice.

3 WAY FORWARD

Market participants showed significant support for the initiative and confirmed that the Eurosystem would not face any major obstacles in introducing loan-level data requirements in its collateral framework. In view of this positive conclusion of the public consultation, on 22 April the Governing Council of the ECB agreed that the study phase of the loan-level initiative could be considered complete and that the Eurosystem could proceed with its preparatory work for the establishment of loan-level information requirements. This preparatory period is expected to last approximately six months. It will be dedicated to further developing the ABS loan-level

data requirements, as well as the technical implementation aspects that were mentioned in the public consultation, in particular: (i) the gradual phasing-in of loan-level data requirements; (ii) the risk control scheme applicable to ABSs for which loan-level data are temporarily not submitted; (iii) the design of the data-handling infrastructure; (iv) the final definition of the RMBS loan-level data template, taking into account the detailed technical comments received; and (v) the possible future introduction of loan-level templates for other asset classes. This further technical preparatory work will be conducted by the Eurosystem in collaboration with market participants. Technical working groups composed of relevant market participants and Eurosystem experts will be created to finalise the different loan-level templates and tackle technical issues related to the initiative.

It is envisaged that the Governing Council will assess the results of this preparatory work after summer 2010 and subsequently decide when to announce the loan-level data requirements. Subject to the approval of the Governing Council, market participants would have a 12-month adaptation period before having to submit loan-level data.

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