CONSULTATION QUESTIONS

WARNING: The IACPM response to EC targeted consultation focuses **ONLY** on the impact of SECR regulations on **synthetic on balance-sheet securitisations,** and on the impact of the 2021 framework on expected future developments in this product.
We therefore did not respond to all the questions, and refer to the **AFME response** for the questions we did not respond to, applicable to all types of securitisations (Equivalence) or more specific to true sale transactions (SSPEs, ABCPs, treatment in LCR ratio).

1. Effects of the regulation

Question 1.1. Has the Securitisation Regulation (SECR) been successful in achieving the following objectives:

	Fully agree	Somewhat agree	Neutral	Somewhat disagree	Fully disagree	No opinion
a) Improving access to credit for the real economy, in particular for SMEs					**X** for SMEs and Corporates	
b) Widening the investor base for securitisation products in the EU				**X**		
c) Widening the issuer base for securitisation products				**X**		
d) Providing a clear legal framework for the EU securitisation market				**X**		
e) Facilitating the monitoring of possible risks					**X**	
f) Providing a high level of investor protection			**X**			
g) Emergence of an integrated EU securitisation market		**X**				

Question 1.2. If you answered 'somewhat disagree' or 'fully disagree' to any of the objectives listed in the previous question, please specify the main obstacles you see to the achievement of that objective.

For synthetic on balance-sheet securitisations:

(a) Fully disagree

Loans to SMEs and corporates are "relationship banking" products which are often not transferable and/or subject to strict confidentiality clauses. ESMA template require data that would allow to easily identify the borrowers even for synthetic transactions, in contradiction also with confidentiality of banking relationship.

As a consequence, securitisation of such portfolios must be structured with a synthetic and not true sale transfer of risk. Also, many SME/corporate loan products are revolving in nature and are not well-suited to traditional securitisation.

Therefore, up to end 2020, and except for the specific transactions (mainly with the EIF) that received the STS RW benefit, the SECR did not achieve its goal of supporting the real economy by lending growth to companies – particularly SMEs - due to the absence of a fully formed STS framework for synthetic transactions, as well as a prescribed low concentration limit (2%) for those transactions that were able to obtain the Article 270 STS label.

(b) Somewhat disagree

We noted an increase in the number of private credit investment firms and of credit insurers that are now active in the synthetic securitisation market. However, this increase is not related to the SECR regulation, but to the context of persistent low yields and growth in savings, requiring further diversification in the asset allocation of real money investors.

(c) Somewhat agree

The introduction of the SEC-SA securitisation risk weight methodology has been a positive development, making it easier for smaller, often standardised, banks to release capital via securitisation. However, the methodology remains highly conservative, and improved calibration is vital to further increasing the use of securitisation by smaller banks *(see further details later in this response).*

That said, the SEC-IRBA methodology is less favourable than the previous supervisory formula approach, which has made securitisation less attractive for IRB banks. Similarly, the increased risk-weights applicable under the SEC-ERBA has had a similar disincentive. These increased risk weights are not justified by the actual observed performance of securitisation in Europe, even during the global finance crisis of 2008-09.

(d) Somewhat disagree

We support the view that harmonisation and standardisation can reduce complexity, but "one size fits all" approach is inflexible and not helpful for a diverse securitisation sector.
In addition, the implementation of the SECR regime and the development of the securitisation framework more broadly remains incomplete. In this regard we note in particular that the development of the recast risk retention technical standards and certain technical standards and guidance specific to on-balance sheet (synthetic) STS are yet to be completed. In addition, there is no consistency among designated national competent authorities (NCAs) with regard to national measures put in place (and some NCAs did not introduce any such measures) relating to how (and whether) they want to be notified about "private" and/or "public" securitisations for the purposes of supervising information made available in compliance with Article 7.

(e) Disagree

In respect of synthetic securitisation, we do not think the "one size fits all" approach to disclosure and reporting has been helpful. The reality is that investors investing in the senior tranches of a traditional securitisation have different needs from the highly sophisticated firms investing in the junior/risky tranches of a synthetic securitisation, and apply their own due diligence, monitoring and reporting requirements, which standard ESMA templates do not reflect. The overly-prescriptive approach to disclosure evidenced in the ESMA templates impose very significant additional cost and operational burdens on originators without providing any meaningful additional information for investors in synthetic securitisations, as evidenced by the fact that no investors have shown any interest in those reports since they were introduced, but continue to require bespoke reporting agreed on a deal-by-deal basis with the originator. While the principles set out in Article 7 of the SECR are sensible, at least for private securitisations, it should be for banks and investors to agree on what is required to meet those requirements rather than requiring all transactions to comply with a set of standardised reporting templates.

(f) Neutral

By introducing common rules for securitisation in the STS framework, SECR has improved the level of protection for new entrants in synthetic transactions. However, we do not believe that SECR has helped existing junior investors. ESMA templates even had an opposite effect.

(g) Somewhat agree

By harmonizing rules / standards and their implementation in the various member states (cf point (d) hereabove), SECR is facilitating the emergence of an EU securitisation market.

Question 1.3. What has been the impact of the SECR on the cost of issuing / investing in securitisation products (both STS and non-STS)? Can you identify the biggest drivers of the cost change? Please be specific.

For synthetic on balance-sheet securitisations:
As explained in 1 (e) above, the SECR increased the operational cost of issuing synthetic securitisations mainly due to the requirement for an additional set of very rigid disclosure templates, which has not replaced the existing and tailored investor reporting requirements.

Additional drivers for increase in costs include:

- Uncertainty in the outcome and delivery date of the Significant Risk Transfer / SRT assessment process, and inappropriateness of proposed new SRT tests,
- Very conservative non-neutrality of the capital treatment of securitisations under the CRR Securitisation framework, unclear prudential rules (eg SES exposure definition) and uncertainty of the future capital regime (SES, Basel IV, etc)
- Specifically for STS transactions, additional costs of compliance, both internal (e.g. data analysis and clean-up) and external (e.g. pool audit, external counsel)
- Penalties or reputation impact of (unintended) non-compliance with STS regulation, etc

For investors, SECR somewhat increased also the cost of compliance with due diligence requirements, both in terms of internal staff time and external legal advices.

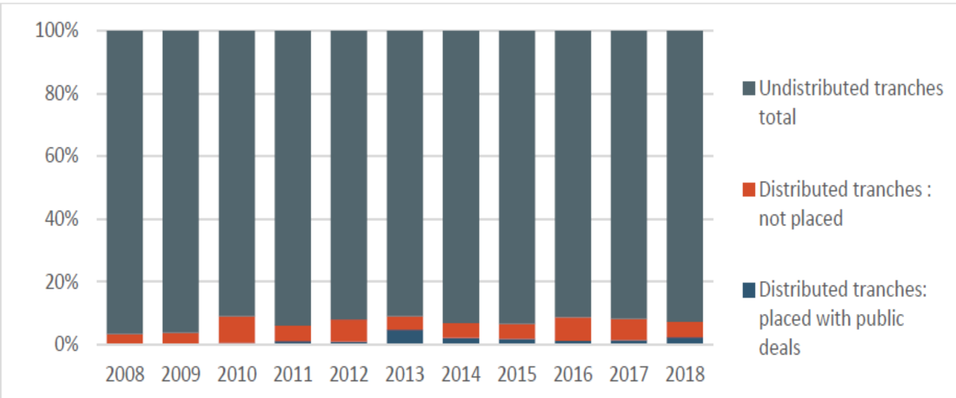
2. Private securitisations

<u>Question 2.1.</u> Are you issuing more private securitisations since the entering into application of the EU securitisation framework?

<u>For synthetic on balance-sheet securitisations:</u>
Yes, significantlyYes, slightly
No change (for synthetic securitisations)
No, it has decreased

Historically, pre-2019, many synthetic securitisations were done as private *unlisted* transactions with some deals seeking listing on EEA and non-EEA trading venues. This trend, the issue of private unlisted transactions in particular, largely continued post-2019.
In this regard, the EBA itself noted in paragraph 22 of its discussion paper of 24 September 2019 on the draft report on STS framework for synthetic securitisation (EBA/DP/2019/01) that: "*In contrast to the pre-crisis period where a substantial part of synthetic securitisation transactions were public and rated (e.g. the Promise and Provide programmes in Germany, the Bistro deals by JPMorgan), since the financial crisis the deals have mostly been executed privately/bilaterally, without involvement of credit rating agencies. Based on the data from IACPM covering transactions from 2008-2018, 18.6% of distributed tranches of all the transactions were placed publicly, which only represents 1.55% of the total size of the transactions.*"

Figure 5: Placed vs not placed part of the tranches of all transactions per year (source: IACPM)



Year/Distributed tranches (in EUR million)	Undistributed tranches Total size	Distributed tranches total size (not placed)	Distributed tranches (placed with public deals)	Distributed tranches placed with public deals (% of distributed tranches)	Distributed tranches placed with public deals (% of total size of the transactions)
Year 2008	64925	2229	0	0.0%	0.00%
Year 2009	34632	1340	0	0.0%	0.00%
Year 2010	14148	1314	78	5.6%	0.55%
Year 2011	24923	1328	276	17.2%	1.11%
Year 2012	22562	1732	221	11.3%	0.98%
Year 2013	17228	802	894	52.7%	5.19%
Year 2014	32031	1639	702	30.0%	2.19%
Year 2015	65601	3382	1226	26.6%	1.87%
Year 2016	45442	3727	5868	13.6%	1.29%
Year 2017	48738	3647	700	16.1%	1.44%
Year 2018	96975	5137	2417	32.0%	2.49%
Max value:				52.7%	5.19%
Average:				18.6%	1.55%

During the period 2016 - Q1 2021 period, the annual synthetic securitisation surveys performed by the IACPM reported that 96% of the transactions on large corporate loans were executed privately, and 100% of the transactions on SME loans.

<u>Question 2.2.</u> What are the reasons for this development (please explain your answer)?

<u>For synthetic on balance-sheet securitisations:</u>
The synthetic securitisation market has always been a private market, aiming at transferring junior credit losses and/or release capital on portfolios with a limited number of highly specialized investors.
Regardless of the legal form of the transaction (eg, listed or unlisted), most synthetic securitisations are marketed to a relatively **small group of potential investors**. It is uncommon to have more than two or three investors in the final transaction, because

- investors are taking exposure to the junior/mezzanine risk tranches of the portfolio, where losses are *expected*, and therefore will always engage in a very detailed due diligence. This is a costly process for the investors, meaning that they are usually only motivated to do so if they are taking a large position in the securitisation.
- there is a lot more bilateral negotiation of the terms of the securitisation that is usually the case for traditional securitisations where investors are investing in the senior tranches more on an "as is" basis.

For these reasons, synthetic markets have been and are likely to **remain private** when compared to traditional securitisations.

<u>Question 2.3.</u> Do the current rules enable supervisors to get the necessary information to carry out their supervisory duties for the private securitisation market?

Yes
No
No opinion

Please explain your answer.

<u>For synthetic on balance-sheet securitisations:</u>
Although synthetic securitisations might be executed for a number of reasons, it is almost always the case that *one* of the motivations is to **obtain capital relief** through the significant risk transfer (SRT) process. Where that is the case, this means that the originator will be required to provide very extensive information about the transaction to their supervisors, both as part of the initial SRT assessment and over the life of the transaction.

SECR transparency requirements are very onerous and prescriptive and provide that relevant information is made available to, among others, relevant EU regulators and NCAs. Therefore, it is absolutely the case that the EU supervisors can have access to necessary information to enable them to supervise compliance of private securitisations, like synthetic transactions. It should be noted that on private synthetic deals such information is commonly provided via a secure website to which any relevant regulator can have access or, where website-based publication of relevant information is not used, transaction parties involved can make arrangements for the relevant EU regulator to receive information required by other means.

As noted in our response to Question 1.2(d) above, there is no consistency among designated NCAs with regard to national measures put in place (and some NCAs did not introduce any such measures) relating to how (and whether) they want to be notified about "private" and/or "public" securitisations for the purposes of supervising information made available in compliance with Article 7. Therefore, misconception that it is challenging for EU regulators to supervise compliance of private securitisations is somewhat misplaced. In this regard we also note that we see a growing challenge in **coordination and communication between NCAs** of banks, insurers and financial markets. A vast amount of information is available – eg in COREP, ESMA and similar reports - but not necessarily shared between different NCAs at local level. Very detailed information per deal is also provided in the notifications/packs to the Joint Supervisory Teams. Therefore, better coordination between EU supervisors and within NCAs using existing frameworks would ensure existing information is used more efficiently.

Question 2.4. Do investors in private securitisations get sufficient information to fulfil their due diligence requirements?

Yes
No
No opinion

Please explain your answer.

For synthetic on balance-sheet securitisations:
Investors in synthetic securitisations do receive all the information they require to perform their own due diligence, monitoring and reporting (tailored to their own management framework and to the specificities of the underlying portfolio per trade). However, this information is provided separately and not fulfilled by ESMA templates, given that ESMA templates are not fit-for-purpose in the context of the synthetic transactions. In this regard we would also note that, when ESMA originally consulted on the development of the technical standards on reporting templates back in 2018, "private" securitisations were not required to use template-based reporting. However, after the initial consultation closed, ESMA subsequently changed its approach.

As a result, largely private securitisation sector like synthetic securitisations became subject to template-based reporting even though, to date, there has been no meaningful engagement of the EU regulators with the industry as to the suitability of ESMA templates in private securitisations more widely and synthetic deals more specifically.

It is important to acknowledge that different securitisations have different risks, not because they are public or private, synthetic or true-sale, but just because each deal is unique (underlying assets, concentrations, historic loss rates, jurisdiction, tranche seniority, structuring features, counterparties involved, etc).
This is no different to any other security: a vanilla unsecured bond issued by a non-investment grade corporate may well be riskier than a AT1 from a highly-rated issuer, not because of the actual format of the instrument, but because of the underlying risk.

Therefore, **a "one size fits all" approach to disclosure is not appropriate**. Private transactions tend to be more bespoke or nuanced than public deals.
Banks are fully supportive of disclosure for their private securitisations, and have been providing to investors a high level of disclosure for a number of years: investors already get significantly more information than prescribed by Article 7. The whole process of due

diligence, data requests, Q&A, etc between issuers and investors for private securitisations normally takes several months. Investors have often also an ongoing established relationship with the risk and credit functions of the banks.

We therefore believe that a better approach would be to make Art 7 disclosure for private synthetic securitisations less prescriptive, removing the need to apply ESMA templates that are no fit-for-purpose and to facilitate application of proportionate investor due diligence under Article 5, which will allow each investor to assess whether all necessary information has been received on a case-by-case basis.

Question 2.5. Do you find useful to have information provided in standard templates, as it is currently necessary according to the transparency requirements of Article 7 and the associated regulatory and implementing technical standards?

Yes

No

No opinion

Please explain your answer.

For synthetic on balance-sheet securitisations:

Standardised templates have a role to play in certain sectors of the securitisation market, but they are **not meaningful for private deals like synthetic securitisations that involve a small number of specialized junior-level investors**, some of which may not even be relevant "institutional investors" in-scope of SECR and, therefore, such investors will not even be required to verify that the synthetic securitisation complies with Article 7 transparency requirement. Instead, such investors will simply ignore reporting made available under Article 7 (even though the EU originator will nevertheless be required to go into great lengths and expense of preparing Article 7 reporting) and will instead be focusing on (and expecting) much more tailored to the deal disclosures and reporting.

Even if a synthetic securitisation involves one or more relevant "institutional investor" in-scope of SECR, additional information will still need to be provided because ESMA reporting templates are not fit-for-purpose, as noted above.

Therefore, SECR should be reviewed so that it applies in a more proportionate and balanced way reflective of commercial realities of different securitisation sectors.

Question 2.6. Does the definition of private securitisation need adjustments?

Yes

No (subject to comments below)

No opinion

If you answered 'yes' to question 2.6, please explain why and how should the definition of private securitisations be adjusted.

For synthetic on balance-sheet securitisations:

The current definition of "private" securitisation works from the perspective of synthetic securitisations. However, if "private" securitisations, as currently defined, are to be brought in-scope of more onerous reporting, including securitisation repository-based reporting, we think it is appropriate to adjust the definition of "private" securitisation to ensure that certain deals are exempt from more onerous reporting requirements or exempt from template-based reporting altogether. Given that any new definition of "private" securitisations would need to work for the relevant diverse sectors of the securitisation market, we would welcome further engagement in this regard with the European Commission and the ESAs. In this regard, we would note that we appreciate challenges in setting parameters for private securitisations that could benefit from more flexible and less onerous transparency regime. In the context of synthetic securitisation, we believe that the focus should be, for example, on the limited number of specialised credit investors involved at inception of the transaction.

3. Due diligence

Question 3.1. Do you consider the current due diligence and transparency regime proportionate?

Yes
No
No opinion

Please explain your answer.
For synthetic on balance-sheet securitisations:
Investors in the same seniority of tranche and the same underlying portfolio of true sale or synthetic transactions have the same due diligence requirements. The general principles of Art. 5 are the same for both types of transactions, even if they are met in different ways. Investors' profile and due diligence requirements are very different depending on the seniority of the tranches (cf Question 3.5).

Question 3.2. What information do investors need? How do investors carry out due diligence before taking up a securitisation position?

For synthetic on balance-sheet securitisations:
The Due Diligence performed by specialized credit investors in junior tranches covers the dynamics of the underlying credit portfolio (historical analysis, concentrations, behaviour in crisis, etc) as well as originating bank-specific features (Underwriting standards, servicing policy, retention, etc). Due diligence varies depending on asset class and specific risk profile of each securitised portfolio.

In addition to insight into the originator's credit process, investors need information on the loans that allow them to monitor, benchmark and assess portfolio future risk/return performance, i.e.
- the jump-to-default and the severity risks of the largest concentrations per name, and
- the overall portfolio risk/return dynamics based on economic scenarios tailored to the securitised loans.
Detailed loan-by-loan data is e.g. not relevant at all for granular portfolios.

Moreover, the **format** of the information has also to be carefully discussed to protect confidentiality.

Likewise the information needed on the credit process of the originating bank, the loan-level information needed to private investors in synthetic securitisations is better defined by these investors. Loan-by-loan templates used for SECR purposes are based on the templates designed and developed for loan-level reporting for the purposes of Eurosystem collateral eligibility, with senior AAA tranches of granular traditional true sale transactions in mind, rather than synthetic or certain other types of securitisations that do not qualify as Eurosystem eligible collateral. By adopting this approach to loan-level reporting under SECR, Article 7 templates are ill-suited for synthetic securitisations that can be less granular, normally transfer first loss/junior mezzanine and – in certain cases - without disclosure of borrower's names. For such blind-pools transactions, investors require the bank's assessment of the credit risk (internal ratings or PD) and expected LGD, and historical track record data on the performance of the bank's internal rating and LGD models.

Question 3.3. Is loan-by-loan information disclosure useful for all asset classes?

Yes – please specify (multiple choice accepted)

Auto-loans/leases
Trade receivables
Residential mortgages (RMBS)
SME loans
Corporate loans
Leases
Consumer loans
Credit-card receivables
Other – please specify : Asset based finance (Commercial mortgages, infrastructure/project finance, etc)

No
No opinion

Please explain your answer.
For synthetic on balance-sheet securitisations:
The level of detail required by the existing ESMA templates is not useful for most synthetic securitisations. It would be more appropriate to allow banks and investors to agree between themselves on what level of loan-by-loan information is required.

Question 3.4. Is loan-by-loan information disclosure useful for all maturities?

Yes
No
No opinion

Please explain your answer.
Loan-by-loan information does not bring value for very granular exposures with short maturities, like trade receivables, credit cards, consumer loans, etc
cf also our response to 3.2. hereabove.

<u>Question 3.5.</u> Does the level of due diligence and, consequently, the type of information needed depend on the tranche the investor is investing in?

Yes
No
No opinion

Please explain your answer.

- Tranches aiming at long term **funding** (as issued e.g. in public cash securitisations) are senior, large in nominal amount (often > 90% of the underlying portfolio nominal). Investors are exposed to structural risk (i.e. effectiveness of true sale transfer, tranching, tranches rating, etc), to market and liquidity risks, and, on the credit side, to the impact of very high correlations arising from extreme systemic scenarios. They are generally very well protected from idiosyncratic credit risk at loan and at borrower level.

- Tranches aiming at **capital relief** (junior/first loss and mezzanine) are mostly exposed to genuine credit and portfolio risks, i.e. jump-to-default of large single names, concentrations per obligor group, industry and geography concentrations, etc. Therefore, investors want to understand the credit process of the lender, have access to extensive historical data analysis, and access to the bank's internal risk assessment (rating/PD per borrower, LGD per loan) without breaking up client confidentiality for the bank.

Both types of investments require therefore very different levels of due diligence and types of information/disclosure.

<u>Question 3.6.</u> Does the level of due diligence and, consequently, the type of information needed depend on whether the securitisation is a synthetic or a true-sale one?

Yes
No
No opinion

Please explain your answer.
<u>For synthetic on balance-sheet securitisations:</u>
For the same underlying portfolio, the information needed by investors depends of the **seniority of the risk** they invest in (junior-mezzanine-senior), not of the type of risk transfer (true sale or synthetic). All else being equal, there is no difference in risk between synthetic and true-sale structures.
Investors in both true sale and synthetic transactions are exposed to the **credit risk** of the reference portfolio, i.e. to the risks of migration/default, to the options embedded in the loans, to the severity risk in work-out, and to the correlation and interconnections inside the portfolio.

Investors in **true sale** transactions are more exposed to risks related to receiving the actual cash flows, such as interest rate, currency and prepayment risks. While these risks can be partially mitigated, these hedges are not perfect.

<u>Question 3.7.</u> Are disclosures under Article 7 sufficient for investors?

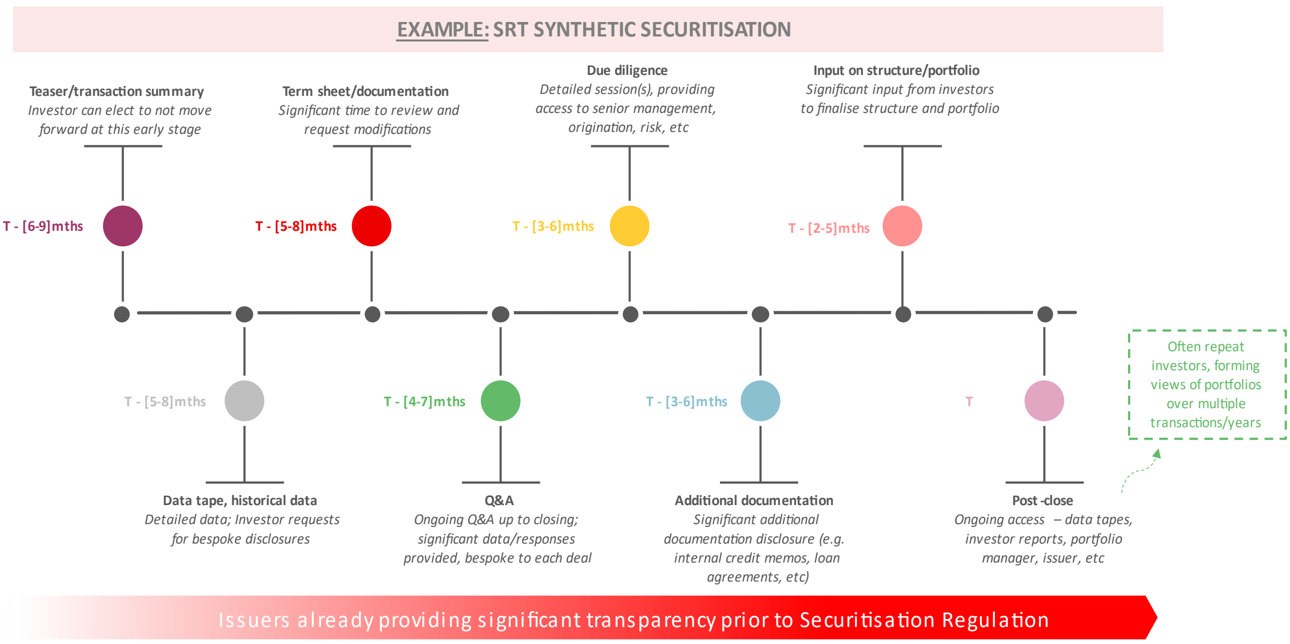
Yes
No
No opinion

Please explain your answer.

<u>For synthetic on balance-sheet securitisations:</u>
We do have an opinion on the issue at hand, but state that we have “no opinion” in the absence of any other suitable option provided in this (somewhat wrongly framed) question.

As an introduction, we want first to highlight that significant ongoing disclosure to investors is taking place **throughout the structuring process** of private synthetic securitisation, above and beyond what is required by Article 7 and the prescribed ESMA templates. As can be seen in the representative example below, the relevant information (which will be tailored to a particular transaction) is disclosed throughout the process, from initiation to closing. Therefore, investors will already be provided with a huge amount of tailored and deal-specific information during this process that often exceeds 6 months. As part of this, investors in private synthetic securitisations (which deals are commonly unrated) always receive loan-level and investor reporting in line with the requirements of article 7, but do not need to receive the overly prescribed ESMA templates.

Private Securitisations– Disclosure Timeline
Significant ongoing disclosure to investors throughout structuring process, above and beyond the requirements of Article 7



Although the industry is highly supportive of the disclosure principle outlined in Article 7, (regarding the need for disclosure of key transaction documents, reporting on underlying assets and investor reporting, including ad hoc significant event reporting), the translation of these key principles into mandatory not-fit-for-purposes reporting templates is unfortunate and not appropriate (which is different from not “sufficient”) for investors in synthetic transactions and not aligned with best practices in risk sharing transactions.

As a consequence of this, investors continue to receive bilaterally agreed information tailored to the specific transaction from issuers, as they did before the introduction of the SECR and it is the receipt of such different information (rather than the receipt of Article 7 reporting templates) that determines the investment decision. This goes to the general principle of investor due diligence. That is, should investors feel they are or will not be not receiving the information they need, they simply will not invest irrespective of whether or not the deal otherwise complies with Article 7 reporting requirements.

We strongly recommend to **permit institutional specialized investors in private synthetic securitisations to apply proportionate approach to their due diligence on transparency** so that they determine themselves which data they need, provided they apply general principles set out in Article 5(3) and Article 5(4), which provisions already require relevant "institutional investor" to assess prior to holding a securitisation position and on an ongoing basis that it receives information necessary to understand underlying assets, parties and structure involved. Doing so will not only be more efficient for both originating **banks** and **investors** in synthetic securitisations, but also for **supervisors** who will thereby have access to the most relevant data for transaction monitoring.
If you answered 'no' to question 3.7, please specify what is missing?

Question 3.8. Do you find that there are any unnecessary elements in the information that is disclosed?

Yes
No
No opinion

Please explain your answer.
cf our responses to questions 3.5, 3.7. and 3.9

Question 3.9. Can you identify data fields in the current disclosure templates that are not useful? Please explain your answer.
For synthetic on balance-sheet securitisations:
For private synthetic securitisations aimed at transferring the first loss and/or mezzanine tranches and releasing capital, the required data fields are bespoke per deal and cannot be standardized. The set of ESMA reporting standards have been designed with traditional true sale securitisations in mind and, most importantly, contain elements that make best practices in investment analysis for risk sharing transactions more difficult to implement.

We provide in attachment

- *Appendix 1*: a paper from a longstanding and meaningful investor in the synthetic transaction market, which outlines the **unintended consequences** of using the current ESMA templates, which are not providing investors with the key information to perform their due diligence, specifically for **private** capital release transactions, like
    - Client data confidentiality for the bank: to access banks risk assessment, investors accept blind pools with less granular clients' data but more information on banks' internal risk assessment
    - Competitive disadvantage for EU institutional investors, willing to enter into a risk sharing transaction with a non-EU bank: non-EU banks will become

obliged to complete templates that do not provide investors with the key information they need to perform their due diligence. Similar to EU banks it would impose a burden, and in addition for non-EU banks it would increase complexity as several fields must specifically be completed based on EU definitions.

- *Appendix 2*: an example of **"fit-for-purpose" report**, specifically on a blind pool of corporate loans, as an illustration of the difference between such a report and current ESMA templates.

For all the reasons outlined in the responses hereabove, **we advocate that EU originators and EU issuers of private synthetic securitisations are exempted from using the ESMA templates and that relevant "institutional investors" are exempted from verifying that such data has been made available.**

To be clear, the principles of Article 5 and 7 should still apply, but the requirement to use the prescriptive templates should be removed for private transactions.

Question 3.10. Can the disclosure regime be simplified without endangering the objective of protecting EU institutional investors and of facilitating supervision of the market in the public interest?

Yes
No
No opinion

Please explain your answer.

For synthetic on balance-sheet securitisations:
As noted in response to Question 3.2 above, loan-by-loan templates developed under SECR are based on the templates designed for loan-level reporting for the purposes of Eurosystem eligibility with granular traditional true sale transactions in mind, rather than synthetic or certain other types of securitisations that do not qualify as Eurosystem eligible collateral.
In addition, as noted in response to Question 2.4 above, such loan-level reporting templates were adopted into the SECR regime without any meaningful consultation with the industry as to their suitability in the context of private securitisations, like synthetic transactions, because ESMA consulted on the basis that template-based reporting will only be relevant for "public" securitisations.
Therefore, the review of SECR should use the opportunity to properly take into account the industry calls for proportionate approach to template-based reporting in relation to **private** synthetic transactions used to transfer the **junior-mezzanine risk** to **specialized credit investors.**
The disclosure regime for **private synthetic** securitisations can be simplified without endangering the objective of protecting EU institutional investors and of facilitating supervision of the market in the public interest.

The simplification consists in exempting originators and issuers of private securitisation from using the ESMA templates, and adjusting investor due diligence requirements so that relevant "institutional investors" can determine themselves in proportionate manner what they may require on any given private synthetic securitisation in terms of necessary information.
This will:
(1) reduce disclosure bloat, removing unnecessary costs for originating bank of having to

produce two sets of reports:
- standardised templates for supervisors on private synthetic securitisation where often there are **no** relevant "institutional investors"; and
- tailored reports for investors containing information that relevant investors actually need and want; and
(2) achieve greater investor protection that will ensure that investors' focus is on what is most relevant and necessary information to any given transactions specifically identified for the purposes of that transaction rather than prescribed by standardised templates that are not fit-for-purposes as noted in our responses above. This environment would actually be safer, particularly for newer investors: regulators shouldn't want investors coming into private transactions based on ESMA templates only, as they would not have the information required in order to truly understand the genuine risk. A highly prescriptive regime may give an incorrect pretence that this is the only information required by an investor.

4. Jurisdictional scope

Question 4.1. Have you experienced problems related to a lack of clarity of the Securitisation Regulation pertaining to its jurisdictional scope?

Yes
No
No opinion

Please explain your answer.

For synthetic on balance-sheet securitisations:
Although not specific to synthetic securitisations, clarity on juridical scope is critical for EU banks and for EU investors in their relationship with non-EU investors and non-EU banks.

- Article 5(1)(e) introduces uncertainty about to which extent an EU-based investor has to require non-EU-based banks to comply with the prescriptive disclosure requirements in Article 7
- The prescriptive disclosure requirements would result in specific issues for non-EU banks;
    - Some jurisdictions have strong client confidentiality regulations, preventing disclosing detailed client information
    - Complexity as a result of having to complete some field based on EU definitions (e.g. on leveraged loans and definitions of default), which are not readily available in the systems of non-EU banks.
- Requiring EU investors to receive information in these formats would put them at a disadvantage, with potentially less investment opportunities, diversification and therewith lower quality portfolios.
- This could also be addressed by exempting private securitisations as per Q3 above.

5. Equivalence *(Not responded)*

6. Sustainability disclosure

Introduction:
In the synthetic securitisation market specifically, securitisations are very relevant to support SMEs/corporates transformation during the transition phase towards a more resilient economy, and to finance all sustainability-related investment initiatives.
It is therefore important that the framework

- does not only consider strictly "sustainable", "green" or "taxonomy-aligned" loans (like labelled green bonds or social bonds), but also
- promote lending to companies which are in the transition phase either via the **underlying assets**, or via the **use-of-proceeds**, as well as by **sustainability-linked lending**, a significant part of the ESG synthetic securitisation market at the moment.

Question 6.1. Are there sufficiently clear parameters to assess the environmental performance of assets other than auto loans or mortgages?

Yes, for all asset classes
Yes, but only for some asset classes (please specify)
No
No opinion

Question 6.2. Should publishing information on the environmental performance of the assets financed by residential loans and auto loans and leases be mandatory?

Yes, the information is currently available
No
No opinion

For synthetic on balance-sheet securitisations:
The responses "yes" would only apply to synthetic securitisations intended to be marketed as sustainable/ESG securitisation, with a transitional period to ensure the availability of information, and with a grandfathering arrangement for existing deals. Otherwise, for non-STS / non-ESG synthetic securitisations, mandatory requirement to publish the environmental performance information should not apply.

We would also note in this regard that on-balance sheet (synthetic) securitisations designated as STS and involving residential loans or auto loans or leases would in any case be subject to additional transparency requirements under Article 26d of SECR relating to environmental performance, including the new technical standards prescribing the content, methodologies and presentation of such disclosure which ESAs are required to develop.

Therefore, we would also recommend caution in this area for the time being – not because we would not support the introduction of environmental performance disclosure requirements, but because there are so many overlapping developments in this area that it would be premature to do so specifically in the securitisation market now. In this regard (and apart from STS considerations noted here above), we would note that synthetic securitisations, like securitisation market more generally, can involve different asset types and different institutions acting as counterparties or investors, with a range of sustainability-related regulatory requirements, standards, taxonomies, industry-led

initiatives etc. applied to them.
Therefore, any introduction of further securitisation-specific sustainability reporting may result in duplicative disclosures and reporting, extra costs and regulatory compliance challenges on both sell- and buy-side.

Question 6.3. As an investor, do you find the information on environmental performance of assets valuable?

Yes
No
No opinion

Describe the use you have made of it?

For synthetic on balance-sheet securitisations:
The information on environmental performance is used by investors for two separate purposes:

- Assess the (positive) **sustainability impact** of the portfolio, and benchmark it to their investment strategy: without impact data, investors will not be able to incorporate securitisations in impact-related funds, generally based on SDG themes and criteria
- Assess **portfolio sensitivity to ESG risks**, run medium/long-term scenarios and benchmark it to investors' appetite for ESG risks.

Investors in synthetic securitisations acknowledge that **flexibility is required during the transition phase around the format of acceptable securitisation transaction** (combining collateral / use of proceeds or sustainability linked approach) **and the definition of underlying assets.**

This flexibility is especially relevant in the SME space, and notably on transactions supported by the EIF, where developing and increasing the proportion of sustainable lending is especially challenging.

Question 6.4. Do you think it is more useful to publish information on environmental performance or on adverse impact and why?

For synthetic on balance-sheet securitisations:
On synthetic securitisations that are intended to be marketed as sustainable/ESG securitisations, both are important as they have different purposes, as explained in 6.3. hereabove. Positive environmental impact is also as important than negative impact.
However, we would caution against developing overly prescriptive securitisation-specific disclosure requirements. Flexibility will be necessary during the transition period on the type of data that borrowers and originating banks are able to report on, and investors will have to assess if the available information is comprehensive enough to achieve their investment strategy.

With regard to the latter, we note that investors can refer

- For **risk** assessment, to the EBA report on management and supervision of ESG risk management, which tackles broader than just environmental risk, and proposes several approaches to assess ESG risks (portfolio alignment, risk framework and loan-by-loan exposure methods), and

- For **impact** assessment, to the global indicators framework designed by the UN for the monitoring of the Sustainable Development Goals,

when performing their own ESG due diligence as well as when complying with their SFDR requirements.

Question 6.5. a) Do you agree that these asset specific disclosures should become part of a general sustainability disclosures regime as EBA is developing?

Yes
No
No opinion

For synthetic on balance-sheet securitisations:
Yes, this will be relevant on securitisations intended to be marketed as sustainable/ESG provided any duplicative disclosures and reporting are avoided and flexibility is maintained during the transition period when availability of relevant data may be more limited.
There should be no difference between mandatory sustainability disclosures on loan portfolios whatever the purpose. However, depending on the asset type and the investment strategy, investors may ask for additional information that is material to them.

Avoiding additional complexity and leveraging currently existing regulatory frameworks and high-level disclosure standards are critical.

On transparency requirements, it is important to highlight that
- EU STS (traditional and synthetic) securitisations backed by auto and residential mortgage assets are already required to provide additional disclosure on sustainability and harmonisation of such disclosure will be further made under the new technical standards.
- EU on balance sheet (synthetic) STS framework requires the appointment of an external verification agent to verify that underlying assets comply with the applicable eligibility criteria. Sustainability-related criteria will be part of that verification process.
- Whether or not the deal is an EU STS, securitisations in scope of the EU Securitisation are also required to provide at least quarterly loan-by-loan and investor reporting using very prescriptive templates, which already include certain sustainability-related reporting fields (eg Residential mortgage loan templates requires loan-by-loan disclosure of the Energy Performance Certificate Value).

Therefore, any additional sustainability related transparency should be carefully incorporated into existing reporting and transparency framework avoiding duplication or creation of unnecessary burden, and must be subject to detailed consultation with the industry.

Considerations should also be made to the **extra-territorial effect** of EU regulations for sustainable finance, as many stakeholders operate beyond the boundaries of the European Union and will have to meet multiple ESG-related requirements. For example, EU investors when investing in non-EU securitisations are also required to confirm that they receive sufficient transparency and disclosures on the deal characteristics and its risk profile. However, for the last three years, since SECR became applicable, it remains unclear whether non-EU securitisations in this context are expected to prepare EU style loan/investor reporting. Therefore, the development of EU sustainable securitisation framework will need to be clear with regard to expectations for sustainability-related disclosures on non-EU deals and for EU deals that may also involve non-EU sell-side parties. In this regard, we would emphases that it is very important for the industry to be clear on the scope of application of any new SECR requirements. It should be clearly stated in any legislative proposal if the new requirements are intended to have extra-territorial effect and, if such extra-territorial effect is intended, meaningful time for consultation with the industry is provided by the European Commission and/or other relevant EU regulators.

Question 6.5. b) Should ESG disclosures be mandatory for (multiple choice accepted):

Securitisation that complies with the EU green bond standard; **YES**
RMBS; **Yes**
Auto loans/leases ABS; **Yes**

The responses "yes" above are provided on basis that the relevant synthetic securitisation is intended to be marketed as sustainable/ESG securitisation, otherwise mandatory requirement to publish ESG disclosures should not apply.

Question 6.6. Have you issued or invested in a green or sustainable securitisation? If yes, how was the green/sustainability dimension reflected in the securitisation? (multiple choice accepted)

		Please describe how the use of proceeds principle is applied **- Examples**
Green or sustainable underlying assets	Yes	• **Underlying green assets** can include physical assets and financial assets such as loans and trade receivables. • Green assets can be tangible or intangible, and they can include the share of working capital that can reasonably be attributed to their operation • Ex: Underlying loans complying with ICMA or LMA standards for sustainable loans • Ex: Mortgages to finance energy-efficient homes, electric vehicle loans/leases, solar panel leases, SME loans to fund environmental projects, etc.
Use of proceeds for green/sustainable projects.	Yes	• **Underlying brown assets**, but the use of proceeds raised or the **capital/liquidity relief** generated is applied for green purposes and/or the originator has strong credentials generally • Ex: Referencing an existing SME portfolio (brown), but commit to reinvest a majority of the **proceeds** to taxonomy-aligned investments • Ex: Commit that 25% of the **RWA reduction** will be used to spur new Positive Impact financing over the next three years
Green/sustainable collateral AND use of proceeds for green/ sustainable projects	No	
Other (please describe) Sustainability-linked securitisations	Yes	• **Underlying transitional assets** but the structure of the transaction or the terms of the bonds are more favourable if ESG KPIs related to the issuer and/or the underlying assets are met • Ex: If the Bank can redeploy twice more of the RWA reduction towards positive impact projects after 4 years, the coupon is reduced, creating an **incentive for additional Positive Impact Finance** investment.

- For the voluntary **Green/Sustainable Securitization Standard**, as for the Green Bond Standard, a common framework is necessary (min % of assets aligned with EU Taxonomy, mandatory third-party validation, grandfathering), to enable investors to include the % aligned with the EU Taxonomy in their GAR (by banks) or in the % of the investment fund aligned (by asset managers).

- For **transactions on assets that are not 100% taxonomy-aligned**, setting a minimum on share of sustainable assets would exclude transactions based on use-of-proceeds and sustainability-linked criteria, and provide limited support and incentive for sustainable economic growth. In these early years, we need more flexibility to ensure more funding/capital is available for developing sustainable economy by the use of securitisations. Therefore, as far as the transaction's characteristics are fully transparent, and disclosures are proportionate, we recommend that
    - for securitisation with a **share of sustainable assets** in the underlying pool, a sliding scale starting with e.g. 30% - 40% and gradually moving to 100%. Long-dated securitisations could in time repurchase/remove non-sustainable assets from the pool and replace them with sustainable ones to achieve higher than 40-50% during the life of the deal. Such a sliding scale would not only account for the limited availability of sustainable collateral, but also stimulate the transition
    - for securitisations based on **use of proceeds**, a similar sliding share could be applied, but starting at a higher minimum level (e.g., 50%), on the proceeds used for sustainability purposes - irrespective of whether or not any of the underlying assets are themselves sustainable. A synthetic risk transfer deal where none of the reference obligations are sustainable should nevertheless qualify if a large and growing amount of proceeds are used for sustainable purposes.

  The characteristics of the proposed sliding scales are to be subject to the review by the Joint Committee of ESAs's under Article 44 of the SECR which mandates it to report every three years, starting with 1 Jan 2021, on the functioning of the SECR regime. Article 44 should subsequently be amended to expressly mandate the Joint Committee to report on the functioning of the sustainable securitisation framework. Thus, the appropriateness of the sliding scales will be monitored and assessed from time to time.

In summary, we suggest to clearly differentiate between

a) **the qualification of "sustainable securitisation" as per the SECR regulations**, which would apply to the 3 types of transactions (based on the underlying loans, on the use-of-proceeds or on the sustainability-linked incentives embedded in the loans), applicable during the **transition phase**, with the **sliding shares**, aiming to **<u>promote the transition,</u>** and finance sustainable assets after the transition phase, and

b) **the voluntary « label »** that would only apply to close to **100% taxonomy-aligned** underlying assets, but **<u>without promoting transition</u>.** Such a label can already apply now to transactions on e.g. renewable energy projects or green mortgages, but would **not** help SME and corporates in transition.
Securities issued from transactions based on "use-of-proceeds" might qualify for a "green" or "sustainable" bond label, while the label "sustainable securitisations" is restricted to transactions collateralized by taxonomy-aligned assets.

Question 6.6. According to the [Commission proposal for a European green bond standard](), a securitisation bond may qualify as EU green bond if the proceeds of the securitisation are used by the issuing special purpose vehicle to purchase the underlying portfolio of Taxonomy-aligned assets. Is there a need to adjust this EuGB approach to better accommodate sustainable securitisations or is there a need for a separate sustainable securitisation standard?

Yes
No
No opinion

Auto-loans/leases
Trade receivables
Residential mortgages (RMBS)
SME loans - **Yes**
Corporate loans **- Yes**
Leases
Consumer loans
Credit-card receivables
Other – please specify : Asset based finance (commercial mortgages, project and infrastructure finance, etc): **Yes**

[If so, what should be the requirements for a securitisation standard?] Please explain your answer.

We don't see the need to change in EUGBS for securitisation the principle that the underlying loans should be aligned with the EU taxonomy. A limit might however be set on the assets that lose their status of "taxonomy alignment" due to strengthening of the Technical Screening Criteria over time, as long as these assets do not significant harm any sustainability objective.

It is important that this standard operates like the other bonds or loans standards from ICMA or LMA, remains voluntary, and that careful consideration is given as to how any "label" would interplay with:
- obtaining (or not) any regulatory benefit;
- existing regulatory benefit that EU STS-designated securitisations already have.
We should not end up in a maze of labels and regulatory treatments, like STS but without sustainable label, STS with sustainable label, not STS but with sustainable label, not STS without sustainable label; etc

Such a EU label would mainly be relevant for public transactions, but less for private transactions, because junior private credit investors will use their own internal framework to assess the ESG risk and the sustainability impact of the loan pools.

Harmonisation will however be very helpful, but in these early years, the markets are likely to continue to be fragmented. Therefore, without flexibility for receiving regulatory benefit that will promote sustainable securitisations, a one-size-fits-all label will likely to achieve the opposite effect and could be detrimental to the development of sustainable securitisation market.

For all these reasons, any sustainability-related securitisation framework needs to work alongside other sustainability-related frameworks avoiding duplication and ensuring that any securitisation-specific changes do not lead to unnecessary burdens and increased costs of doing a securitisation, which will inevitably further hinder the development of wider securitisation issuer- and investor-base.

7. A system of limited-licensed banks to perform the functions of SSPEs *(Not responded)*

8. Supervision *(Not responded)*

9. Assessment of non-neutrality correction factors impact

Question 9.1 a) In your view, is the capital impact of the current levels of the (p) factor proportionate, having regard to the relative riskiness of each of the tranches in the waterfall, and adequate to capture securitisations' agency and modelling risks?

Yes
No
No opinion

For synthetic on balance-sheet securitisations:
P factor and RW floors were originally introduced to create a **non-neutrality effect** in capital vs the underlying pool, and account for the agency and modelling risks specific to securitisation transactions. These risks were, between others, at the source of the collapse of US sub-prime residential mortgages securitisations during the 2007-2008 global financial crisis.

However, these risks are very different in synthetic on balance-sheet securitisations and have been materially mitigated since 2008 :

a) **Agency risk** is the operational risk arising from the multiple relationships between the agents of a securitisation structure, and related information asymetries.
   - However, in synthetic on balance-sheet securitisations aiming at risk transfer, banks are retaining the senior tranche. For this retained tranche, there is **no asymmetry of information** as the seller, the servicer and the buyer are the same institution: the originating bank
   - These transactions are also mostly private and not externally rated: they rarely bear the rating agency risk

   Therefore, **there is a specific rationale to reduce the non-neutrality effect created to account for agency risk in originators' retained tranches of synthetic on-balance-sheet transactions.**

b) **Modelling risk**, as articulated in 2012 and 2014 BCBS papers justifying non—neutrality in the securitisation framework (*) arises from the layering of models and assumptions made on the underlying pool and on transaction structural features to estimate the loss distribution which serves to define the waterfall of tranche.

   However, subsequent to those BCBS papers, and **particularly in the EU**, confidence in models has been significantly enhanced by the following initiatives:

- BA IRB repair: harmonization of modelling practices (2013)
- TRIM: deep review of banks' main internal models by supervisors
- Model risk management frameworks and capital attributed to model risk
- Forward-looking yearly stress tests, to complement historical models

P factors and RW floors have not been amended to reflect these model risk mitigants. The non-neutrality of securitisation risk weights achieved through p factor and RW floors was actually increased in recent years.
STS transactions – simpler and more standardised – and naturally embedding a lower modelling risk, only "benefitted" from a more limited increase. The reduced risk weights associated with STS do not purport to reflect the broader, fundamental, reductions in model risk achieved by EU banks and outlined above.
As indicated by BCBS, modelling risk resides mostly in the senior tranches, i.e. in the ultimate level of the waterfall structure, while junior tranches are only sensitive to genuine credit risk. **The reduction of non-neutrality due to model risk should therefore specifically target a reduction of the RW floor on senior tranches**, which are typically retained by banks.

c) Moreover,
   - the strengthening of the regulatory landscape for securitisations has reduced significantly the agency and model risks which justified the introduction of the p factor after the Global Financial Crisis
   - Many additional safeguards are now in place in regulations to offset any perceived additional risks (e.g. Systematic supervisory review of the SRT assessment process).

All in, in synthetic on balance-sheet securitisations, the absence of information asymmetry (agency risk) and the mitigation of the model risk specific to retained senior tranches justify for a recalibration of both the p factor and the RW floor.

Moreover, the finalisation of Basel III will introduce a double layer of conservatism on balance-sheet securitisations on the pools RWA and on the risk-weight of the tranches:
1. The first layer of conservatism relates to the calculation of the **RW on retained tranches**: the RW on retained tranches under SEC-IRBA is, in effect, floored based on the output of SEC-SA (or SEC-ERB) calculations, which are more conservatively calibrated than the SEC-IRBA.
2. The second layer of conservatism results from the application of the SA, which is more conservatively calibrated than the IRBA, to calculate the **RW of the underlying pool**, as an input to SEC-SA: the SA will lead to a higher capital charge without any change in the underlying risk.

The consequences of the output floor on securitisation is again particularly worrying for synthetic securitisations where - by definition - the senior tranche is retained, contrary to traditional true sale securitisations.
It is important that the RWA inflation due to the introduction of IRB input floors and the SA output floors on securitised pools is not further magnified by the non-neutrality of the securitisation risk weight functions. Hence a re-calibration of the SEC-IRBA and SEC-SA formulae should be undertaken.
By increasing the non-neutrality effect without change in the underlying risks, the finalisation of Basel III will also justify a review of the p factors and RW floors, particularly for on balance-sheet securitisation where senior tranches are retained.

(*) BCBS 2012 consultative paper: "*Model risk is arguably more acute for securitisations exposures, because setting capital requirements for securitisation exposures involves multiple layers of modelling exercises and assumptions. […] This* ***layering of models and assumptions*** *can amplify the uncertainty associated with capital estimates. In addition,* ***the uncertainty in capital estimates is higher for highly-rated****, seemingly low-risk tranches and there is an asymmetric nature to the uncertainty.*"
BCBS 2014: "*The objectives of a* ***risk-weight floor*** *are:*

- *Mitigate concerns related to incorrect model specifications and error from banks' estimates of inputs to capital formulas (ie model risk); and*
- *Reduce the variation in outcomes for similar risks.*"

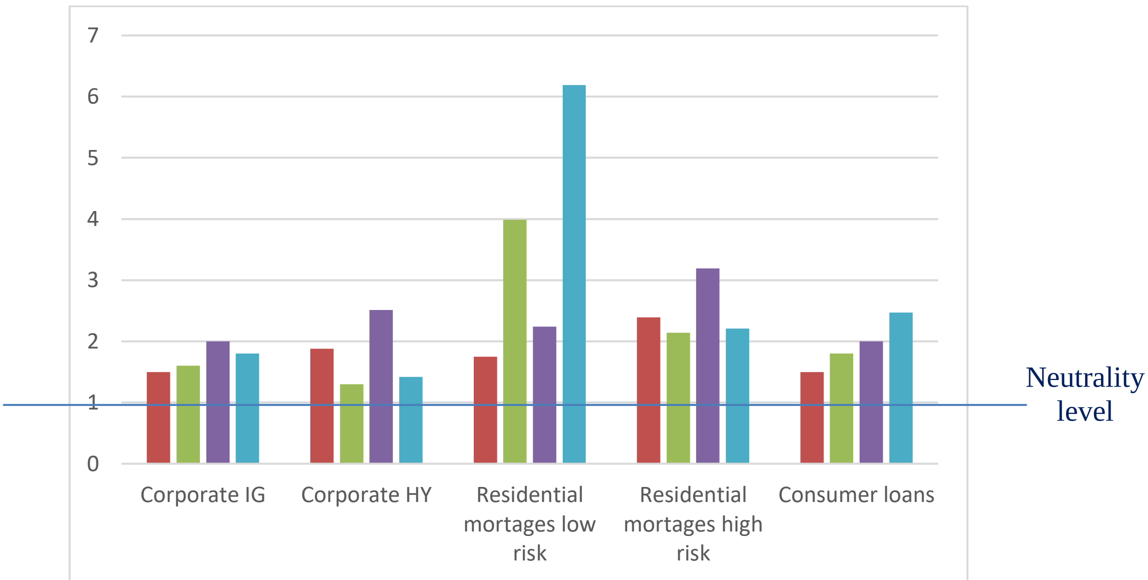
Question 9.1 b) If you would favour reassessing the current (p) factor levels, please explain why and what alternative levels for (p) you would suggest instead.

For synthetic on balance-sheet securitisations:
We estimated the level of non-neutrality that would apply to STS and non-STS securitisation of various asset classes (corporates, consumer loans, residential mortgages low/medium risk, consumer loans), and for STS/non-STS transactions, by comparing
- the average RW of the portfolio before securitisation and
- the aggregated RW of all tranches if they were fully retained by the originating bank.

Multiplication factors		Corporate IG	Corporate HY	Residential mortgages low risk	Residential mortgages high risk	Consumer loans
STS	SA	1,5	1,88	1,75	2,39	1,5
STS	IRB	1,6	1,3	3,99	2,14	1,8
Non-STS	SA	2	2,51	2,24	3,19	2
Non-STS	IRB	1,8	1,42	6,19	2,21	2,47

In synthetic on balance-sheet transactions, the multiplication factor between aggregated RW on all the tranches after securitisation and RW on a loan pool is quite substantial, forcing banks to sell thicker junior tranches and increasing the cost of such transactions before releasing enough capital to re-invest in new loans.

The multiplication factors are of course higher on non-STS than on STS transactions, as p factors are different:



Although theoretical, the examples in attachment 1 illustrate the **RWA inflation** induced by the calibration of the SEC-IRBA and the SEC-SA : if a bank was to sell 80% of all the tranches, the RWA reduction would range between 48% and 73% under SEC-IRBA and between 36% and 60% under SEC-SA.

Based on these examples, we estimated that **a fair target of non-neutrality effect could be estimated at maximum 1.5**, and simulated the level of p factor reduction which would allow to achieve this objective.

- We provide you in *Appendix 3* with an analysis performed on four real life transactions to estimate the level of p factor reduction in SEC-SA which could compensate for the RW difference resulting from the (final) Basel III 'Output Floor' pre-securitisation (IRB to SA) and post-securitisation (SEC-IRBA to SEC-SA).

  For these transactions specifically, the attached simulations come out at a **reduction of the p factor by circa 50% :**

  - In the 'SEC-SA', halving the p-factor can bring down the credit enhancement required to reach RW floor to a more reasonable level (still with 1.5 x UL coverage), which should also support smaller SA banks issuance

  - Non-Neutrality of c.150% and c.125% of pre-securitisation capital are achieved for Non-STS and STS examples respectively

  - The approach to calibration is conservative as normalising the (final) Basel III Output Floor impact does not give recognition to the senior credit risk retained vs pre-securitisation credit risk.

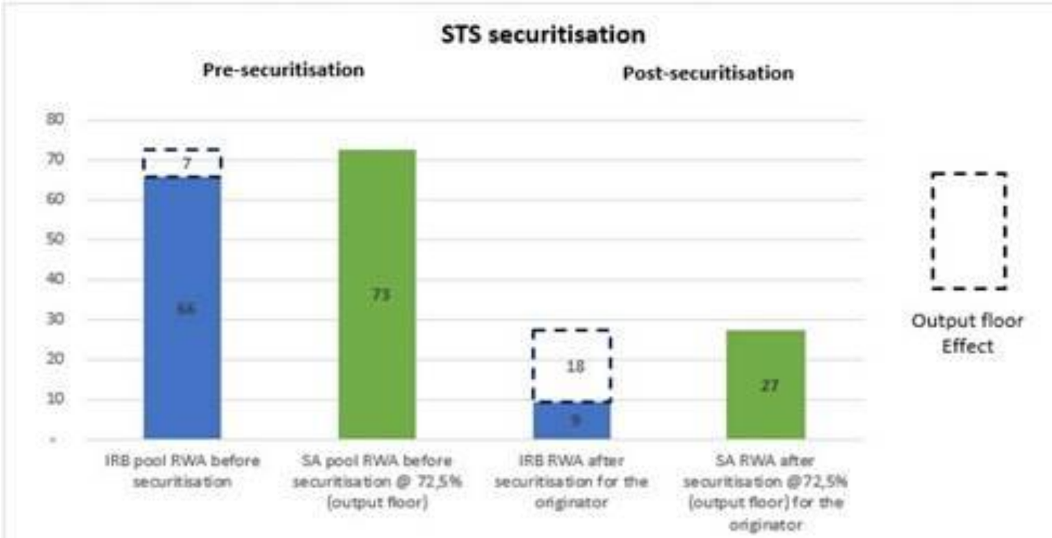
  For memory, adjusting the p-factor in SEC-SA to 0.5 for non-STS and to 0.25 for STS transactions, is aligned with the proposals made in the final report of **CMU High Level Forum** (Annex pages 61-62), and to the proposed amendments to Articles 261, 262, 263 and 264.

- However, **the necessary level of p factor reduction is very dependent of the output floor impact on the retained tranche, and varies according to the specificities of the underlying portfolios**: it is typically less important if the RW under SA is low and much more penalizing otherwise.

  As you can see in the example below, calculated for a STS transaction on a corporate pool eligible to the SME supporting factor (*), dividing the p factor by two only halves the output floor effect on the senior tranche (from +36 to +18); in other words, the transaction would still release much less capital (28 RWA vs 57 RWA under current framework).

With p factor = 0,5 :

With p factor = 0,25 :



Based on the evidences above, we recommend that **p factors are reduced by at least 50% in SEC-SA for both STS and non-STS transactions**, and offer to participate in further discussions on this subject with the regulatory community, so that the final proposal is most efficient to compensate for the impact of the output floor.

(*)Example of a corporate pool eligible to the SME supporting factor, attracting 66 RWA under IRBA and 100 RWA under SA (2.5y-maturity, 0.5% PD, 40% LGD) : the output floor impact before securitisation is +7 on the pool (i.e., the difference between the 73 RWA post SME supporting factor and 66 RWA under IRBA), but the impact on the retained senior tranche after securitisation is +36 (i.e., 45 under SEC-SA minus 9 under SEC-IRBA) in the case of an STS transaction. The STS transaction would have released ***57 RWA*** *(66 RWA on the underlying portfolio under IRBA minus 9 RWA on the retained senior tranche risk-weighted under SEC-IRBA), but will only release* ***28 RWA*** *with the output floor (73 RWA on the underlying portfolio under SA minus 45 RWA on the retained senior tranche under SEC-SA).*

<u>Question 9.2</u> Are current capital floor levels for the most senior tranches of STS and non-STS securitisations proportionate and adequate, taking into account the capital requirements of comparable capital instruments?

Yes
No
No opinion

Please explain your answer.

<u>For synthetic on balance-sheet securitisations:</u>
RW floors are now significantly higher than under the previous securitisation regulatory regime (e.g. RW of senior non-STS tranche increased from 7% to 15%).

- For the reasons explained in point 1 hereabove, we challenge the regulatory position that retaining a senior position on own originated portfolios requires the same capital than acquiring a senior position in a securitisation issued by a third party. We believe that retained senior tranches should benefit from further changes to the preferential STS risk weighted formula.
- Also, given the excellent performance of EU ABS during and after the GFC and also during the Covid-19 pandemic, it is unclear what evidence there is for these higher RW floors.

To address this issue, we recommend introducing, for originating banks, a **7% RW floor for non-STS senior tranches** treated with SEC-IRBA/SEC-SA/SEC-ERBA and (IAA) as it was in the previous framework (so called SFA formula).
This proposal is also aligned with CMU HLF recommendations, and would ensure a **level playing field between EU and US banks**, whereby the latter still benefit from the Supervisory Formula Approach (SFA) under the IRB approach, which was present in the previous version of the framework in the EU, under the IRBA approach compared to the more conservative SEC-IRBA methodology now being used in the EU.

<u>Question 9.3</u> Are there any alternative methods to the (p) factors and the capital floors to capture agency and modelling risk of securitisations that could be regarded as more proportionate?

Please provide evidence to support your responses to the above questions.

<u>For synthetic on balance-sheet securitisations:</u>
Different alternatives have already been discussed with regulators in the past.
In the interest of time, we recommend using the current framework while reducing the p factors and RW floors as proposed hereabove.

10. Maturity

<u>Question 10.1.</u> Do you think that the impact of the maturity of the tranche is adequate under the current framework?

Yes
No
No opinion

Please explain your answer.

For synthetic on balance-sheet securitisations:
The WAM calculation remains too conservative in certain aspects, with outcomes often not aligned with standard market practice for calculating the true maturity of a tranche.

Notably,

- the **exclusion of a prepayment assumption** from the WAM calculation for synthetics remains at odds with the true risk of a synthetic tranche. There is no rationale for this divergence between synthetic and traditional structures, and no valid reasons provided in the final EBA WAM Guidelines. Indeed, this lack of rationale was recognised by the EBA in the discussions preceding the preparation of the WAM Guidelines but at the time it took the view that it was constrained by the text of the CRR.
  As an example, the industry expects an increase in the issuance of synthetic securitisations linked to residential mortgages going forwards, particularly following the introduction of Basel IV. Residential mortgages are an asset class with a clear and well understood prepayment behaviour, with significant historical data to back up any assumptions, well understood by investors and rating agencies. There is absolutely no justification for excluding prepayments assumptions just because the structure is synthetic.
- The treatment of **revolving periods** is also unnecessarily complex, introducing modelling difficulties whilst making the final WAM numbers harder to interpret, resulting in a potential misunderstanding of the true risk of a tranche. This also affects transaction structuring, making replenishment transactions less attractive, which results in less effective transactions.
  We are supportive of reverting this treatment to the logic included in the original WAM consultation paper.
- Further, it appears sensible to consider **divergent WAM calculation frameworks for originators and investors**. As a risk mitigant/hedging tool, SRT transactions for banks should, all else being equal, be viewed more favourably when they offer a longer protection period. However, the current rules would penalise this greater maturity. Other equivalent hedging tools (e.g. CDS) are already treated more favourably by the CRR when being executed for longer periods.

Question 10.2. Is there an alternative way of considering the maturity of the tranche within the securitisation framework?

Yes
No
No opinion

Please explain your answer.

The alternative way would be to

- use the standard WAL logic used by the market and the industry

and,

- as proposed in 10.1 above, also consider divergent calculation methodologies for originators and investors.

11. Treatment of STS securitisations and asset-backed commercial papers(ABCPs) for the liquidity coverage ratio (LCR) *(Not responded)*

12. SRT tests

Question 12.1. Do you agree with the allocation of the LTEL and UL to the tranches for the purposes of the SRT, CRT and PBA tests, as recommended in the EBA report?

Yes
No
No opinion

Please explain your answer.

For synthetic on balance-sheet securitisations:
The proposed SRT tests don't work as expected when applied to real life transactions that are transferring a significant amount of economic risk. We refer to the examples in *Appendixes 4 and 5* simulated on real life transactions, and approved for significant risk transfer.

The proposal below assumes that p factor and RW floor will be fundamentally downsized. Otherwise, we would challenge the appropriateness of introducing complex SRT tests to assess risk transfer significance, when the level of conservatism in the calculation of the RW release – just by itself – can demonstrate that commensurate risk transfer is achieved just because capital can be released despite the multiple layers of conservatism. We refer to our response to question 9 on non-neutrality effect.

Based on this assumption, and would proposed SRT tests anyhow be maintained, **the tests have to be amended**, and we investigated solutions to make these tests work.
It is also very important that these tests serve only as guidance for supervisors, who should retain the ultimate responsibility of the final SRT decision.

The new tests as designed seem to be based on the two following key assumptions:
a) issuers will run them to the time call, not the clean-up call and
b) transactions pools are largely composed of bullet amortizing loans with similar maturities, and hence – in combination - assuming a significant outstanding balance at the time of the UL event. Since the vast majority of SRT transactions do not feature any "positive incentive" for issuers to exercise the time call, the current implication is that issuers must instead run tests to the clean-up call date, resulting in a much more extreme test than intended.

These two assumptions are simply not accurate:
- *Time call*: Running the tests up to the time calls should not have a consequence that an unintended "positive incentive" requires a capital surcharge due to maturity mismatch (cf our response to Q12.2 below)
- *Bullet loans*: SRT structures are used across a variety of asset classes with significantly different maturities and amortization dynamics over time (e.g. corporates, SMEs, autos, consumer, leases, trade finance, residential and commercial mortgages, etc).

The new tests are simply impossible to pass for many real-life deals whilst remaining economically viable. The key issue is the highly conservative application of the UL event in the final year of the transaction: a UL event based on the initial size of the portfolio occurring at the end of the transaction is significantly more adverse than any realistic stress scenario based on observed historical data, making it virtually impossible to structure transactions that pass the tests. By construction, no transaction would – in such scenario – benefit its structural protections such as pro-rata to sequential triggers, as they are usually set levels above the EL.

To make the tests work, various amendments have been considered, focusing on the allocation technique of the UL event, while maintaining EBA's proposed treatment for expected loss (EL). We excluded some options, like modelling UL on a loan-by-loan basis at the maturity of every securitized exposure, as this may be overly complex for large consumer portfolios with a limited value added.

We simulated the three retained options of UL allocation (see *Appendix 6*) and believe that the option 2 is the most appropriate, i.e. amend UL event loss distribution as per EBA's proposed 'back-loaded' EL vector. Allocating 33.3% of the UL to the first 2/3 and 66.6% to the final 1/3 of transaction life, as determined by clean-up call, meets the EBA's objective in providing a significant stressed loss scenario to SRT structures (total size unchanged from original proposal) on a consistent basis across banks, which is also relatively simple to model and monitor across banks.

This amendment would make that the tested real life transactions (formerly approved by regulators for Significant Risk Transfer), would pass the tests, while ensuring that
- Significant stress is applied to test efficacy of structures
- Implementation and monitoring are simple across banks
- Structural protections for pro-rata amortization (e.g. triggers to sequential) more likely behave as intended.
- the approach is more aligned to bank economic modelling of a back-loaded stress.

We also agree with the EBA SRT Report that the proposal to model the lifetime behavior of transactions under stress, at inception, can provide a more dynamic test which better reflects the economics.

We therefore strongly recommend that the current testing methodology proposed in EBA report is reviewed so that the UL event loss distribution is amended as per EBA's proposed 'back-loaded' EL vector.

We also want to warn regulators about the **complexity** of these tests and the underlying modelling techniques, which might not necessarily fit-for-purpose whatever the profile of the underlying portfolio or the structure of the risk sharing transaction, hence the importance to grant **flexibility** to supervisors when they analyse tests outcome to assess significance of risk transfer.

Question 12.2. What are your views on the application of Art. 252 of the CRR on maturity mismatches when a time call, or similar optional feature, is expected to happen during the life of the transaction?

For synthetic on balance-sheet securitisations:
We believe that the EBA is misinterpreting the notion of **positive incentive** provided for in **Article 238** to which Article 252 refers and would be created by the time call.
As clearly stated in Article 238, the notion of "positive incentive" exists when the credit protection arrangement provides for an incentive – like an increase in the premium - at a certain

time. On the contrary, the fact that the economics of the transaction deteriorate because of the amortization of the portfolio or the improvement of its credit quality does not constitute a positive incentive since this positive incentive does not exist, for example, if credit quality deteriorates.

We therefore propose that, unless the non-exercise of a time call has an effect on the contractual terms going forward, **the existence of a time call should not be seen as creating a positive incentive to call, regardless of whether the economics of the transaction may have deteriorated since the closing date.** This point should be clarified in CRR.

13. SRT assessment process

Question 13.1. What are your views on the EBA-recommended process for theassessment of SRT as fully set out in Section 5 of the EBA report on SRT?

For synthetic on balance-sheet securitisations:
We welcome EBA's willingness to differentiate between "simple" transactions that do not exhibit complex features and more complex ones, the first category benefitting from a preferential assessment process. However, we have strong reservations regarding the length and the unfolding of the proposed processes, which fall short of industry expectations for improved efficiency and supervisory certainty.

The proposed processes are too long, whether for "simple" or more complex transactions.

- The EBA report states that the maximum period for the SRT assessment process for all transactions would be 6 months, split into a 3-month assessment period, a 1-month (Fast-track) or 2-month (structural features review) review and a 1-month review of the final documentation. So, as currently laid out, a **Fast-track transaction does not have certainty of No Objection until 4 months** after submitting the original ex-ante review material, and with a 'Structural features review' transaction this could be up to 6 months.
- Also, the proposed timeline would include
  (i) the delay between preliminary submission and the CA acknowledgement of receipt
  (ii) the potential 15 days between deal execution and final deal documents submission
  (iii) the unlimited time period(s) during which the "clock would be stopped" at the request of the CAs, should they require additional information.
  In practice, given the detailed assessment and analysis the Originator needs to submit for the Preliminary notice, which can take 1-2 months to complete, it means **some transactions may not have certainty of SRT relief for up to 7 to 8 months**, and even longer considering the potential 'stopping the clock' and preliminary notices to the CA acknowledgement.

As a result, **the effective assessment time period of some transactions is likely to largely exceed 6 months**, which is excessive and significantly longer than the recently improved process implemented by the ECB. Where a bank deems it necessary to free up some capital relatively quickly in times of uncertainty in the markets (e.g. during Q2 of 2020 at the height of coronavirus), securitisation would no longer be an effective tool in order to aid more lending to support the economy given the potentially long time-frames.

To shorten the SRT assessment process, we believe that:

- **The 3 month ex-ante review (Art 5.2.3 181) should be much shorter** as its main purpose is to identify whether a transaction falls into the 'Fast track' or 'Structural features review' path. Based on bank's determination that a transaction passes the CRR quantitative tests and the two CRT tests, and on the explicit criteria defined by the EBA to support the SRT assessment, **one month should be sufficient for SRT assessment of transactions that do not need a structural features review** and **two months for transactions that require such review.** Other steps such as reception of documents should be considered as negligible.
- **Explicit point in time feedback from the CA (Art. 5.1. 169 b) should not be required** on whether SRT has been achieved or not. The CA should be required to review the ex-ante information provided and only be required to issue an Objection stating in reasonable detail the reason(s) for an Objection. No further feedback by the CA before the proposed closing should be interpreted as the same as a No Objection being issued. Furthermore, if no Objection is received then the CA should not be able to issue an Objection post-closing unless the transaction details have changed significantly as to affect SRT.
- **Fast-track SRT assessment process (Art 5.2.3 176)** should not be limited to those transactions which do not exhibit certain structural features, but should also include **repeat transactions** with similar structural features, the first of which that may have already gone through a structural features review.
- **Notional size or capital relief amount** (Art 5.2.3 178) should not be a factor when assessing if that transaction is a 'qualifying transaction' as it would be arbitrary (unless the size itself affects the ability of the transaction to transfer risk as intended.)

Question 13.2. Do you agree with the standardised list of documents that the EBA report on SRT recommended for submission to the competent authority for SRT assessment purposes?

We generally agree with the standardised list of documents proposed that the report on SRT recommended for submission to the Competent Authority, but an industry consultation should take place to further define these documents.

Question 13.3. Once it has been established that the regulatory quantitative and qualitative criteria are met and transactions are in line with standard market practices, should a systematic ex-ante review be necessary?

Yes
No
No opinion

Please explain your answer.
For synthetic on balance-sheet securitisations:
Adding an ex-ante review for a transaction that is in line with market practice and passes all the tests would add unnecessary additional workload to the issuer (and associated costs).

We believe there should be a **presumption that a structural review is not required.** Transactions should benefit from a simplified process if they
- do not include any of the identified structural features, or
- include identified structural features but with safeguards ("safe harbours" or otherwise)

that have already been validated in previous transactions.

Based on such clear rules, **one month** should be sufficient to assess whether a transaction needs a structural review or not. A detailed "structural review" would actually lock the issuance process, given the shared experience by banks that the approach adopted by Competent Authorities is excessively restrictive.

Question 13.4 Should the ex-ante assessment by the Competent Authority be limited to complex transactions?

Yes
No
No opinion

Please explain your answer.

For synthetic on balance-sheet securitisations:
For transactions that are in line with market practice and pass all the tests, there should be no reason to add an ex-ante assessment; only complex transactions may have to be analysed to control that they comply with the set of rules.

However, whether or not the transaction requires a structural features review, **the Competent Authority's permission or objection should occur prior to execution**. Banks cannot take the risk of executing a transaction if the SRT is rejected and the existence of SRT calls is not a sufficient safeguard because of the upfront costs of the structuration and of the negative impact that such uncertainty would have on investor appetite. In this regard, the EBA proposal is a significant step backwards compared to the current setup.
In practice, securitisation full legal documentation is frozen shortly before execution ("preliminary offering memorandum"). A check by the CA that such documentation does not diverge from critical SRT criteria compared to earlier versions should be sufficient to confirm SRT assessment before execution in all cases.

14. Amendments to CRR

Question 14.1 Do you agree with the recommendations on amendments of the CRR as fully laid out in Section 6 of the EBA report on SRT?

Yes
No
No opinion

Please explain your answer.

For synthetic on balance-sheet securitisations:
We agree that the SRT/CRT tests should be formalised in the level 1 text, rather than remaining informal but still being enforced by the JSTs. These tests, of course, need to be fair and reasonable (please see question 12).

However, **synthetic excess spread** (SES) remains an area of significant uncertainty and concern for the market. We look forward to receiving the expected consultation paper from the EBA later in the year, so that we can continue our dialogue on this extremely important point.

- The new SES Capital Charge is economically punitive and, in practice, likely to be minimally impacted by SES-based retention, or, indeed, by the other adjustments intended to mitigate its effects: on-balance sheet STS and the adjustment of the attachment and detachment points of the originator's other retained tranches under Article 256(6) CRR (A/D Adjustment).
- In practice, the majority of transactions including synthetic excess spread make use of the full deduction option in which the originator applies a CET1 deduction or 1250% risk weight to all retained tranches in the securitisation under Article 245(1)(b) CRR, rather than demonstrating the transfer of significant credit risk associated with the underlying exposures under Article 245(1)(a) CRR. That is, the originator holds sufficient capital to absorb losses of 100% on the exposures to the underlying portfolio that it retains.
  In this context, the risk weight reduction available to retained senior tranches in securitisations that meet the criteria for the on-balance sheet STS designation is irrelevant to the originator (the tranche must never the less be deducted/1 250% risk weighted). Similarly, in this context, the risk weight reduction available to retained tranches flowing from A/D Adjustment is irrelevant to the originator (the tranche must never the less be deducted/1 250% risk weighted).
- The proposed SES-based retention reduction is likely to be economically unattractive. In relation to transactions that seek to demonstrate transfer of significant credit risk associated with the underlying exposures under Article 245(1)(a) CRR, this is because the originator must demonstrate that it retains less than specified amounts of mezzanine securitisation positions or first loss securitisation positions in Article 245(2) CRR. Satisfying the retention requirement (post reduction by the exposure value of the SES) via a first loss tranche makes it harder for the originator to demonstrate compliance with the required maximum amounts in the first loss test. Similarly, under the full deduction approach, satisfying the retention requirement (post reduction by the exposure value of the SES) via a first loss tranche increases the amount of deductible retained securitisation positions. By contrast, retained assets/portions of assets would be likely to attract lower risk weights.

Regarding **full deduct** transactions, the EBA's opinion appears to not yet be fully formed, with various references made in the report but no final proposal included. A clear view/proposal from the regulator would be very helpful, preceding an industry consultation. At this stage, we understand that a regulatory notification would be required to the effect that the option was being used and that an originator would have to satisfy itself re satisfaction of the "documentary / structural" (not economic) conditions in Art 245(4) CRR. It is not clear from the draft what EBA opinion/decision remains to be reached.

15. Solvency II

Question 15.1. Is there an appetite from insurers to increase their investments in securitisation (whether a senior tranche, mezzanine tranche, or a junior tranche)?

Yes
No
No opinion

Question 15.2. Is there anything preventing an increase in investments in securitisation by insurance companies?

Yes
No
No opinion

Please explain your answer.
We are not aware of insurers expressing an increased appetite to invest in securitisations on the asset side.
However, insurers are playing an important and growing role on the **liability side** as sellers of private unfunded credit protection. The provision of unfunded credit protection in the form of an insurance policy or a financial guarantee is not permitted in the STS framework for synthetic on balance-sheet securitisation, as an important tool for banks to transfer risk on single loans or on mezzanine tranches of securitized portfolios.
Providing eligibility for regulated credit insurers as providers of credit protection tranches of synthetic securitisations (particularly on mezzanine tranches) will become critical after implementation of Basel III finalisation, which will require to protect thicker tranches to release the capital absorbed by the same underlying portfolio.

Question 15.3. Is the current calculation for standard formula capital requirements for spread risk on securitisation positions in Solvency II for the senior tranches of STS securitisations proportionate and commensurate with their risk, taking into account the capital requirements for assets with similar risk characteristics?

Yes
No
No opinion

Please be specific in your reply and, where relevant, provide a comparison, including where appropriate with internal models and their relative impact on the share of securitisation investments.
Insurers investing in securitisations use their own internal models for capital adequacy calculation, and not the standard formula.

Question 15.4. Is the current calculation for standard formula capital requirements for spread risk on securitisation positions in Solvency II for the non-senior tranches of STS securitisations proportionate and commensurate with their risk, taking into account the capital requirements for assets with similar risk characteristics?

Yes
No
No opinion

Please be specific in your reply and, where relevant, provide a comparison, including where appropriate with internal models and their relative impact on the share of securitisation investments.
Insurers investing in securitisations use their own internal models for capital adequacy calculation, and not the standard formula.

<u>Question 15.5</u>. Is the current calculation for standard formula capital requirements for spread risk on securitisation positions in Solvency II for non-STS securitisations proportionate and commensurate with their risk, taking into account the capital requirements for assets with similar risk characteristics?

Yes
No
No opinion

Please be specific in your reply and, where relevant, provide a comparison, including where appropriate with internal models and their relative impact on the share of securitisation investments.
Insurers investing in securitisations use their own internal models for capital adequacy calculation, and not the standard formula.

<u>Question 15.6</u>. Should Solvency II standard formula capital requirements for spread risk differentiate between mezzanine and junior tranches of STS securitisations?

Yes
No
No opinion

Please explain your answer.
Insurers investing in securitisations use their own internal models for capital adequacy calculation, and not the standard formula.

<u>Question 15.7.</u> Should Solvency II standard formula capital requirements for spread risk differentiate between senior and non-senior tranches of non-STS securitisations? Please explain your answer.

Yes
No
No opinion

Please explain your answer.
Insurers investing in securitisations use their own internal models for capital adequacy calculation, and not the standard formula.

Appendices

1. Position paper “ESMA templates – Not fit for risk sharing transactions“ (PGGM)
2. Illustration of “fit-to-purpose” investor report on a blind pool of corporate loans in a risk sharing transaction (PGGM)
3. Simulation of p factor reduction (Santander)
4. Simulation of proposed SRT tests on real life transactions (Santander)
5. Simulation of proposed SRT tests on real life transactions (EIF)
6. Simulation of various options to amend SRT tests (Santander)