



BANKING STAKEHOLDER GROUP

CONSULTATION ON EBA/CP/2015/08 ON “DRAFT IMPLEMENTING
TECHNICAL STANDARDS
ON THE MAPPING OF ECAI’S CREDIT ASSESSMENTS FOR
SECURITISATION POSITIONS UNDER ARTICLE 270 OF REGULATION
(EU) N° 575/2013 (CAPITAL REQUIREMENTS REGULATION - CRR)”

General Comments and Replies to Questions

BY THE EBA BANKING STAKEHOLDER GROUP

London, 7th August, 2015

Foreword

The EBA's Banking Stakeholder Group (BSG) welcomes the opportunity to respond to the present Consultation Paper (EBA/CP/2015/08) on "Draft Implementing Technical Standards on the Mapping of ECAI's Credit Assessments for Securitisation Positions Under Article 270 of Regulation (EU) No. 575/2013". This BSG response to the Consultation Paper has been prepared on the basis of comments circulated and shared among the BSG members and the BSG's Technical Working Group on Capital and Risk Analysis. BSG welcomes the opportunity to contribute to the development of these guidelines. This response outlines some general comments by the BSG, as well as detailed answers to some questions indicated in the Consultation Paper.

As in the past, the BSG supports an initiative that aims at harmonizing supervisory rules and practices across Europe, in order to ensure fair conditions of competition between institutions and more efficiency for cross-border groups. The BSG also expects these initiatives to facilitate data sharing between European supervisors and avoid reporting duplications for banks.

General Comments

Regulation (EU) 575/2013 (Capital Requirements Regulation – CRR) presently allows the use of ECAI ratings to assess the credit quality and thus the correspondent risk weights under two articles: Article 251 for the Standardised Approach and Article 259 (a) under the Ratings Based Method.

However, the G-20 conclusions and the FSB principles set out in October 2010 and reiterated as a roadmap in November 2012 advocate the reduction of reliance on external credit ratings. These principles have to be implemented over a "reasonable timeframe". Thus, the Basel Committee of Banking Supervision has published in December 2014¹ a proposed revision of the securitisation framework which explicitly excludes a mechanistic reliance on external ratings as one of the objectives. In the proposal, the use of external ratings will be reduced from the two above mentioned approaches to only one (External Ratings Based Approach). In the same workstream, the three ESAs have issued in December 2014 a discussion paper on the "Use of Credit Ratings by Financial Intermediaries Article 5(a) of the CRA Regulation". The aim is to produce common guidelines on reducing contractual reliance on ratings.

In order to ensure comparability of the different ECAIs, two mapping exercises have been required: a common mapping of the three ESAs for credit assessment under Article 136 of the CRR (all credit exposures excluding securitisations) and the present one, for securitisations only, under Article 270 of the CRR. Due to the upcoming regulatory change in the securities framework, the present mapping exercise, which shall determine the correspondence between credit quality steps and credit ratings, is likely to be used for a limited period of time only. EBA intends to review the mapping proposed in this regulation, at least, before the new Basel Securitisation Framework comes into force in January 2018. The new European

¹ BCBS 269

framework for Qualifying Securitisation² proposed by EBA, and that could be implemented before 2018 if the Commission follows the announced calendar, could even require a review of the mappings before 2018.

In view of (i) the lack of data of securitisation rating for the new ECAIs (other than the four incumbent ones); (ii) the substantial change in rating methodology of the incumbent ECAIs subsequent to the crisis; and (iii) the fact that a fully quantitative approach of assessment of the incumbent ECAIs historical performance would result in overly conservative capital requirements, the EBA has proposed the maintenance of the current mapping for the incumbent ECAIs and is of the view that the mappings proposed for the more recent ECAIs should be aligned with those allocated to the incumbent ECAIs.

The BSG agrees with this pragmatic approach taken by the EBA of maintaining the current mappings, given the ongoing revision of the European framework for Qualifying Securitisation (QS) and the forthcoming European Commission's plan of action expected in September (part of the CMU project where short term action is envisaged). If a recalibrated external rating based-approach is included for QS, the revision of the mapping should be advisable before its implementation.

The new global Basel Securitisation framework (finalised in 2014 and expected to be implemented in 2018) includes a SEC-ERBA based on external ratings in the second place of the proposed hierarchy, with risk weights different from the current ones, making advisable the revision of the current mapping before its implementation³.

² Opinion of the European Banking Authority on a European framework for qualifying securitisation. EBA, 7 July 2015

³ Additionally, the finalisation at the global level of the definition of high quality securitisation (IOSCO/BCBS proposal for Simple Transparent and Standardized securitisation) and the review of its prudential framework is expected in the second half of this year.

Answers to the Questions

Question 1

Do you agree with the proposed approach to the mapping of securitisation ratings issued by the incumbent ECAIs?

Yes, the BSG agrees with the approach of maintaining the mapping for incumbent ECAIs as a transitory measure.

After a qualitative and quantitative type of analysis of the ECAIs, the rating grades of the four incumbent ECAIs (S&P, Moody's, Fitch and DBRS) were mapped to the same credit quality steps in 2006. The option selected by the EBA is to maintain the mapping of 2006 (reviewed in 2010).

This option has been selected on the basis of a qualitative assessment because:

- a) The impact assessment shows that a systematic quantitative approach based on historic default performance (three year cumulative default rates) shows very high default rates over the years following the crisis and would therefore result in overly conservative capital requirements if mappings were modified to take into account those default rates. It has to be considered that those high default rates are mostly driven by the crisis performance of very specific securitization sub-asset classes and geographical location (US RMBS and US CDO transactions cover 70% of the CEREP sample of ratings used) whereas securitization in Europe has shown a good performance with very low default rates. The better behavior in Europe is likely due to more robust securitization practices than in the US. The new securitization framework that is being designed to promote high quality securitization, should allow to differentiate the mapping for robust securitization (the kind that has prevailed in Europe) from the mapping of non-robust securitization (associated with “originate-to-sale” model, subprimes and complex securitisations), highlighting that a one-size-fits- all approach is no longer to be recommended.
- b) Rating methodologies of the incumbent ECAIs have changed subsequently to the poor performance of the pre-crisis ratings, which makes historical data not comparable to current rating practices.
- c) Moreover, a quantitative mapping would have to be reviewed in the light of the new BCBS framework.

Question 2:

Do you agree with the proposed approach to the mapping of securitisation ratings issued by small/more recent ECAIs?

Yes, the BSG agrees with this approach.

The track record of the new ECAIs is necessarily very limited as the new ECAIs were not active in the market when the first CEBS rating was established. Therefore, no, or insufficient historical data is available.

Mapping the new ECAIs in a harmonised fashion enables them to gain recognition in the rating market and achieve a higher degree of competition, which is one of the main goals of the common market. In this way, the predominant position of a very limited number of market participants might be challenged. However, as a possible drawback, we consider that the EBA is not taking into account economic and commercial realities, such as (i) the lack of experience of the new ECAIs, and (ii) the fact that issuers of securities might only contact new ECAIs after the incumbents have either refused to issue a rating (as they have become more prudent after the experience of 2008) or for other commercial reasons (cost of rating). It is likely, therefore, that the reality and the confidence which can be given to the ratings of the new and incumbent ECAIs is not equivalent.

Question 3:

Do you see any adverse market implications/conceptual drawbacks arising from potentially inconsistent mappings being applied to any given ECAI across the standardised approach for credit risk (mapping under Article 136 of the CRR) and the securitisation framework (mapping under Article 270 of the CRR)?

No, there should not be any adverse market implication arising from the different approaches.

For those institutions which utilise the IRB approach for exposures other than securitisations, there is no conflict with a mapping of ECAIs: they would use ratings only related to securitisation positions, where the equivalence of CQS is mapped according to the present ITS.

For a bank which has not transferred significant credit risk under the securitisation (Article 245 (2) and for an originating or sponsoring bank Article 252 of CRR), the securitised positions are treated as if the positions had not been securitised in order to calculate minimum capital requirements under CRR.

In the case this bank uses the Standardised Approach, the positions would be weighted according to the mapping under Article 136.

A potential inconsistency could only arise for a non-originating bank which uses the Standardised Approach and invests into securitisations⁴. This bank would apply both systems: it would use the mapping in the present ITS for securitisation positions, and the mapping under Article 136 for all other positions (corporates and banks exposures, mainly; capital requirements under the Standardised Approach for SMEs, RMBS and retail exposures in general do not depend on external ratings).

Generally, an investment in a securitisation consists of investing in a pool of assets. In addition, risks in securitisations represent not only the underlying credit risk, but also structuring risk. An analysis of securitisation risk must include structuring risk such as granularity, and, as a corollary, concentration risk, an analysis of the originator and servicer, credit-enhancement (i.e. over-collateralisation), replenishment and other structural considerations. Therefore, rating methodologies of securitisations are different from those of credit risk. A difference in mapping, resulting in a difference in CQS, should not represent a conceptual drawback.

However, adverse market conditions for securitisation could arise if the capital requirements of a portfolio of assets owned directly on the balance sheet and the capital requirements after securitisation of that portfolio differ excessively: increasing in the latter case in a disproportionate way (in comparison to the added risks of the securitisation process). This is because it could discourage investing in securitisation and promote investing in the underlying portfolio. This problem of excessive non-neutrality of capital for securitisation for European transactions (capital charges after securitisation being a high multiple of capital charges before securitisation) was revealed by EBA⁵ for RMBS, SME, etc.

Submitted on behalf of the EBA Banking Stakeholder Group

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⁴ And for an originating bank which has transferred significant credit risk, when computing minimum capital requirements for the retained positions.

⁵ EBA Discussion Paper on simple standard and transparent securitisations. October 2014