

**EBA Consultation Paper (EBA/CP/2013/45)  
Draft Guidelines On Significant Credit Risk Transfer relating to  
Article 243 and Article 244 of Regulation 575/2013.**

**Submission from the EBA Banking Stakeholder Group**

**1) General comments and background**

The BSG welcomes this regulatory initiative that promotes a consistent treatment of credit risk transfer in securitizations. The crisis revealed that in some cases financial entities (especially in the US) issued securitizations to third parties in order to “save” capital consumption without there being a real transfer of credit risk. This created systemic risk when these securitizations were reabsorbed in the banks’ balance sheets. To avoid this risk, Basel III is more demanding as regards the criteria for credit risk transfer, but allowing for substantial regulatory discretion in applying these criteria. These guidelines aim at fostering convergence in supervisory practices, thus favoring a level playing field and greater comparability across countries and institutions in the EU. However, this initiative could entail additional costs for originators in terms of information burden, changes in governance and, new procedures. This administrative burden should not be neglected when assessing this proposal.

The CRR approach towards securitizations is conservative in the sense that it only allows capital mitigations for securitizations with Significant Risk Transfer (SRT), i.e. it requires a credit risk transfer that exceeds explicit minimum quantitative thresholds, in addition to complying with several qualitative requirements.

This general framework is not rigid; on the contrary, it provides flexibility for supervisors to decide on SRT on a case-by-case basis (on their own initiative or at the request of the entity) in order to grant the benefits of

SRT when the supervisor is convinced that risks have been effectively transferred in a sufficient amount. BSG welcomes this flexibility because a rigid framework would not be able to take account of the diversity of securitization practices.

On the other hand, BSG recognises that the drawback of this flexibility is that it could generate very different supervisory approaches by different national supervisors. To mitigate these undesired effects, the CRR includes a mandate to EBA to monitor the range of practices in this field and to issue guidelines on the assessment of SRT. EBA shall review MS implementation of these guidelines, which will be followed by its advice to the Commission by 31 December 2017 on whether binding Technical Standards are required.

## **2) Main aspects of the guidelines**

The guidelines provide guidance to competent authorities in two respects:

1. When identifying transactions where originator institutions technically satisfy the rules for SRT without actually achieving commensurate risk transfer to an independent third party due, for instance, to the high cost of the credit protection purchased.
2. When assessing an originator institution's claim of SRT applying the alternative method (i.e. where originator institutions do not technically satisfy the rules of the recognition of SRT but can demonstrate to the supervisor that the reduction in own funds obtained is justified by a commensurate transfer of credit risk).

The guidelines also contemplate new requirements for originator institutions:

1. General requirements for all transactions claiming SRT: to provide the competent authority with the requested information as well as governance and policies around SRT assessments.
2. Specific requirements when the originator institution claims SRT applying the alternative method.

### 3) Initial assessment

The BSG welcomes initiatives such as these guidelines that promote convergence in supervisory practices, that contribute to the development of a level playing field, and which facilitates comparability.

However, this will entail additional costs to be assumed by originators (information to be provided, changes in governance and procedures...) and, when implementing the requirements, attention should be given not to unnecessarily overburden them. The application of the principle of proportionality should be carefully observed in this regard.

### 4) Discussion points

Whether the scope of the guidelines exceeds the CRR mandate:

- 1) The guidelines include general requirements for originator institutions for all transactions claiming SRT, which **possibly exceed the scope of the mandate**. For instance some of the guidelines concern governance and policies to be set up by originator institutions.

“1. Originator institutions should have a governance process in place for evaluating transactions claiming SRT. This process should include details of relevant committees, any internal approval procedure, and evidence of appropriate stakeholder involvement and a suitable, auditable trail of documentation.”

It is worth considering whether these requirements should be applied only to institutions applying the alternative method for SRT, and not to those that already fulfill the requirements for SRT.

2) As a general principle, the guidelines ask originator institutions to assess the reliance placed on external credit assessments in their analysis of transactions claiming SRT and the relationship between such external credit assessments and internal credit assessments. This principle is aligned with the policy objective of avoiding a mechanistic reliance on ECAI's assessments. However, and in order not to unnecessarily overburden originators, it could be appropriate to consider some exceptions when no doubts exist concerning the quality of assessments (ECAI with proven experience and a successful record in rating securitizations) or in application of the proportionality principle (setting, for instance, quantitative thresholds of materiality), in order not to unnecessarily overburden originators.

Another aspect to consider is whether, in the context of the gradual approach adopted by the CRR (issuance of guidelines in 2014, revision of the implementation and decision in 2017 on whether technical standards are needed), more specific guidance is appropriate in the short term, thus mitigating uncertainty related inter alia to RWAs.

These guidelines leave to the discretion of the national supervisor to decide the fulfillment of some criteria to determine when competent authorities should conduct a comprehensive review of SRT (page 10). These criteria include inter alia (i) the thickness of securitization tranches, (ii) losses incurred on the securitized exposures, and (iii) high costs of the transfer of credit risk. Even if the criteria are comprehensive, more effort should be made to include quantitative indicators to help supervisors decide and ensure some sort of harmonization across European financial systems, for instance in these areas:

- Thickness of securitization's tranches which are used as being relevant to demonstrate SRT. The guidelines leave to supervisory discretion to judge whether the thickness is sufficient to assume a commensurate SRT, both for

mezzanine tranches and for first loss tranches. Some quantitative indicators may be helpful in setting the range of values to decide whether this thickness is sufficient or not, taking into account also the effect of asset correlations on optimal thickness.

- High cost of the transfer of credit risk. The guidelines leave to supervisor discretion to judge if the cost is too high and undermines SRT. Some quantitative indicators may also be used in this regard, to provide some guidance on the range of values to decide whether the transfer is sufficient or not. In addition, it should be clarified in Title III, Para. 7 Subpara. 3 and 4 (at p. 13/14) that a relevant transaction for which SRT is claimed must pass the test right at the outset of the transaction, as this is the time when the costs of the credit protection are fixed on the basis of the respective expectations of the parties. Thereafter, the overall costs of a credit protection may in fact prove too high or too low in the light of the actual performance of the underlying pool. However, any deviation of the actual from the expected performance of the underlying pool (no matter in which direction) should not lead to a reassessment and subsequent disqualification of SRT by the competent authorities.
  
- SRT to third parties. It should be clarified in Title III, Para. 8 Subpara. 1 (at p. 14) that the "no connection/no affiliation" test should not be applied to existing state guarantee schemes where local governments assumed the credit risk of certain non-performing pools and thereby assisted troubled financial institutions in the aftermath of the financial crisis. Often the respective local government also held stakes (directly or indirectly) in the relevant financial institution. To impose new requirements on existing transactions that originally qualified for SRT, would lead to a reassessment of

such transactions and potentially to a retroactive disqualification of SRT by the competent authorities, which is not justifiable and may lead to unforeseen and harsh results.

The BSG recognises the advantages to be gained through the development of an active securitisation market. However, it is also conscious that this must be achieved in a way that avoids the problems that emerged in earlier years, in particular as regards the determination of significant risk transfer, where supervisory practices have presented a wide variety in the past. For this reason, BSG welcomes the harmonization of supervisory practices outlined in this draft guidelines subject to the qualifications noted in this submission.

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