

EBA/GL/2016/08

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03/10/2016

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# Final Report

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Guidelines on implicit support for securitisation transactions

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# 1. Executive Summary

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Pursuant to Article 248 of Regulation (EU) No 575/2013 (Capital Requirements Regulation – CRR), restrictions are placed on providing implicit support to securitisations. Originator institutions and sponsor institutions that have failed to comply with the relevant requirements shall at a minimum hold own funds against all of the securitised exposures as if they had not been securitised. The CRR, recognising the potential for diverging interpretations in respect of what constitutes implicit support, sets out in Article 248(2) a specific mandate for the European Banking Authority (the EBA) to issue guidelines on what constitutes arm's length conditions and when a transaction is not structured to provide support, which mandate is fulfilled by these guidelines.

The guidelines recognise the fact that implicit support should not cover support that institutions are already contractually obliged to provide. Such explicit support is assessed under guidelines EBA/GL/2014/05 on significant risk transfer. As such, the guidelines apply to transactions that an institution is under no contractual obligation to enter into at all, or is not under a contractual obligation to enter into on the specific terms of such transactions.

Pursuant to Article 248(1) CRR, a transaction shall not be considered to provide support if it is executed at arm's length conditions and taken into account in the assessment of significant risk transfer. Considering the fact that the provisions of the CRR dealing with the recognition of significant risk transfer (Articles 243 and 244) apply to originator institutions but not to sponsor institutions, the guidelines specify that, in the case of sponsor institutions, a transaction is not structured to provide support if it is executed at arm's length conditions or on conditions which are more favourable to the sponsor institution than arm's length conditions. In the case of originator institutions, the guidelines apply the conditions set out in Article 248(1) CRR by interpreting the reference to the transaction being taken into account in the assessment of significant risk transfer as meaning that, following the relevant transaction, the conditions for significant risk transfer continue to be met or, if such conditions are no longer met, the transaction was not entered into with a view to reducing potential or actual losses to investors.

Regarding the definition of arm's length conditions, the guidelines set out an objective test. In order to ensure that the test is applied correctly, the assessment is to be made having due regard to the information available to each of the parties at the time when the transaction is entered into, and not to such information as becomes available thereafter.

Furthermore, guidance is provided in respect of the application of the factors contemplated in points (a)-(e) of Article 248(1) CRR and the notification requirements applicable to such transactions.

## Next steps

The guidelines will be translated into the official EU languages and published on the EBA website. The deadline for competent authorities to report whether they comply with the guidelines will be two months after the publication of the translations. The guidelines will apply from 01 March 2017.

## 2. Background and rationale

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1. Articles 243 and 244 CRR require any reduction of capital requirements achieved through securitisation to be justified by a commensurate transfer of risk to third parties.
2. Support for a securitisation, whether the institution is required, pursuant to the terms of the securitisation, to provide such support (contractual support, i.e. credit enhancements provided at the inception of a securitised transaction) or whether the institution is not under an obligation to provide such support (implicit support), can take numerous forms. For instance, examples of contractual support include overcollateralisation, credit derivatives, spread accounts, contractual recourse obligations, subordinated notes, credit risk mitigants provided to a specific tranche, the subordination of fee or interest income or the deferral of margin income. Examples of implicit support include the purchase of deteriorating credit risk exposures from the underlying pool, improving the quality of credit enhancements, such as through the addition of higher-quality risk exposures, the sale of discounted credit risk exposures into the pool of securitised credit risk exposures after the closing of the securitisation, the purchase of underlying exposures at above market price, ad hoc credit enhancements provided to one or more tranches or an increase in the first loss position according to the deterioration of the underlying exposures.
3. It is specifically the provision of implicit support which raises significant supervisory concerns. For both traditional and synthetic securitisation structures, the provision of implicit support undermines the achievement of significant risk transfer, therefore disallowing banks from excluding the securitised exposures from regulatory capital calculations. By providing implicit support, institutions signal to the market that all or part of the contractually transferred credit risk is still with the institution and has not in effect been transferred. The capital held by the institution can therefore understate the true risk.
4. Accordingly, Article 248 CRR sets out restrictions on providing implicit support and specifies that originator institutions and sponsor institutions that have failed to comply with the relevant requirements shall at a minimum hold own funds against all of the securitised exposures as if they had not been securitised. Furthermore, pursuant to Article 98(3) of Directive 2013/36/EU, competent authorities are required to monitor whether an institution has provided implicit support to a securitisation and, if an institution is found to have provided implicit support on more than one occasion, the competent authority shall take appropriate measures reflective of the increased expectation that it will provide future support to its securitisation, thus failing to achieve a significant transfer of risk.
5. As such, Article 248 CRR states that a transaction shall not be considered to provide support if it is executed at arm's length conditions and taken into account in the assessment of significant risk transfer. Moreover, the institution shall, when assessing whether the transaction is not structured to provide support, adequately consider at least all of the following:
  - a. the price of the repurchase;
  - b. the institution's capital and liquidity position before and after repurchase;

- c. the performance of the securitised exposures;
  - d. the performance of the securitisation positions; and
  - e. the impact of support on the losses expected to be incurred by the originator relative to investors.
6. Within this context, the EBA is required to issue guidelines on what constitutes arm's length conditions and on when a transaction is not structured to provide support.

## 3. Guidelines

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## Guidelines

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# on implicit support for securitisation transactions

# 1. Compliance and reporting obligations

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## Status of these guidelines

1. This document contains guidelines issued pursuant to Article 16 of Regulation (EU) No 1093/2010<sup>1</sup>. In accordance with Article 16(3) of Regulation (EU) No 1093/2010, competent authorities and financial institutions must make every effort to comply with the guidelines.
2. Guidelines set the EBA view of appropriate supervisory practices within the European System of Financial Supervision or of how Union law should be applied in a particular area. Competent authorities as defined in Article 4(2) of Regulation (EU) No 1093/2010 to whom guidelines apply should comply by incorporating them into their practices as appropriate (e.g. by amending their legal framework or their supervisory processes), including where guidelines are directed primarily at institutions.

## Reporting requirements

3. According to Article 16(3) of Regulation (EU) No 1093/2010, competent authorities must notify the EBA as to whether they comply or intend to comply with these guidelines, or otherwise with reasons for non-compliance, by ([dd.mm.yyyy]). In the absence of any notification by this deadline, competent authorities will be considered by the EBA to be non-compliant. Notifications should be sent by submitting the form available on the EBA website to [compliance@eba.europa.eu](mailto:compliance@eba.europa.eu) with the reference 'EBA/GL/201x/xx'. Notifications should be submitted by persons with appropriate authority to report compliance on behalf of their competent authorities. Any change in the status of compliance must also be reported to the EBA.
4. Notifications will be published on the EBA website, in line with Article 16(3).

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<sup>1</sup> Regulation (EU) No 1093/2010 of the European Parliament and of the Council of 24 November 2010 establishing a European Supervisory Authority (European Banking Authority), amending Decision No 716/2009/EC and repealing Commission Decision 2009/78/EC, (OJ L 331, 15.12.2010, p. 12).



## 2. Subject matter, scope and definitions

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### Subject matter

5. These guidelines specify what constitutes arm's length conditions and when a transaction is not structured to provide support, according to Article 248 of Regulation (EU) No 575/2013<sup>2</sup>. The guidelines also elaborate further on the notification and documentation requirements of Article 248(1) of Regulation (EU) No 575/2013.

### Scope of application

6. These guidelines apply in relation to the support provided to securitisations by sponsor institutions and originator institutions beyond their contractual obligations as further specified in paragraph 10, in accordance with Article 248 of Regulation (EU) No 575/2013 and the conditions set out therein. The guidelines are without prejudice to the on-going assessment of significant risk transfer during the life of the securitisation.

### Addressees

7. These guidelines are addressed to competent authorities as defined in point (i) of Article 4(2) of Regulation (EU) No 1093/2010 and to financial institutions as defined in Article 4(1) of Regulation (EU) No 1093/2010.

### Definitions

8. Unless otherwise specified, terms used and defined in Regulation (EU) No 575/2013 have the same meaning in these guidelines.

## 3. Implementation

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### Date of application

9. These guidelines apply from 1 March 2017.

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<sup>2</sup> Regulation (EU) No 575/2013 of the European Parliament and of the Council of 26 June 2013 on prudential requirements for credit institutions and investment firms and amending Regulation (EU) No 648/2012.

## 4. Implicit support

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### Existing contractual obligations

10. Any transaction (for the avoidance of doubt, including, but not limited to, any amendments to the securitisation documentation and changes to the coupons, yields or other features of the securitisation positions) entered into by (i) a sponsor institution or (ii) an originator institution or (iii), subject to the provisions of paragraph 25, an entity connected to the originator institution in relation to a securitisation or positions therein after the closing of such securitisation, which, pursuant to the terms of the securitisation documentation as in force prior to the entering into of such transaction, the originator institution or, as the case may be, the sponsor institution or the entity connected to the originator institution:

(a) is under no contractual obligation to enter into; or

(b) is not under a contractual obligation to enter into on the specific terms of such transaction

should be considered to have been entered into beyond the scope of existing contractual obligations, its particulars should be notified in accordance with paragraph 26 and it should be assessed, in accordance with paragraph 11, whether the transaction is structured to provide support or not. Transactions which, pursuant to the terms of the securitisation documentation as in force prior to the entering into of such transactions, the relevant institution is under a contractual obligation to enter into on the specific terms of such transactions constitute existing support and are not subject to the prohibition set out in Article 248 of Regulation (EU) No 575/2013.

### Transaction not structured to provide support

11. For the purposes of Article 248 of Regulation (EU) No 575/2013, a transaction should be considered as not being structured to provide support in any of the cases referred to in paragraphs 12 and 13, taking into account the provisions of paragraph 19.

12. Subject to paragraph 25, where the transaction is carried out by a sponsor institution, the transaction should be considered as not being structured to provide support if it meets either of the following conditions:

(a) it is executed at arm's length conditions, in accordance with paragraph 15; or

(b) it is executed on conditions which are more favourable to the sponsor institution than arm's length conditions.

13. Where the transaction is carried out by an originator institution which has transferred significant credit risk associated with the underlying exposures of the securitisation in accordance with Article 243 or Article 244 of Regulation (EU) No 575/2013, the transaction should be considered as not being structured to provide support if it meets the following conditions:

- (a) the transaction is executed:
  - i. at arm's length conditions, in accordance with paragraph 15; or
  - ii. on conditions which are more favourable to the originator institution than arm's length conditions; and
- (b) either (i) the securitisation continues to meet the conditions for significant risk transfer as set out in Article 243 of Regulation (EU) No 575/2013 or, as the case may be, Article 244 of the Regulation, in accordance with these guidelines and with guidelines EBA/GL/2014/05 on significant risk transfer, or (ii) if such conditions are no longer met, the transaction was not entered into with a view to reducing potential or actual losses to investors.

14. If the conditions for significant risk transfer are no longer met, the originator institution should hold own funds against all of the securitised exposures as if they had not been securitised.

## Arm's length conditions

15. For the purposes of Article 248 of Regulation (EU) No 575/2013, a transaction should be considered to be executed at arm's length conditions where the terms of the transaction are such as they would be in a normal commercial transaction if:

- (a) the parties had no relationship to each other (including, but not limited to, any special duty or obligation and any possibility to control or influence each other); and
- (b) each party:
  - i. acted independently;
  - ii. entered into the transaction of its own volition;
  - iii. acted in its own interests; and
  - iv. did not enter into the transaction on the basis of extraneous considerations which are not directly connected with the transaction in question (such extraneous considerations including, but not being limited to, any reputational risk which might arise in respect of the originator institution or the sponsor institution should it not proceed with the transaction).

16. In the course of the assessment referred to in paragraph 15, due regard should be given to the information available to each of the parties at the time when the transaction is entered into, and not to such information as becomes available thereafter.

## Significant risk transfer

17. When evaluating a transaction in accordance with Article 248 of Regulation (EU) No 575/2013, any assessment of whether the conditions for significant risk transfer as set out in Article 243 or, as the case may be, Article 244 of that Regulation continue to be met should be carried out in accordance with these guidelines and with guidelines EBA/GL/2014/05 on significant risk transfer.
18. A transaction should be deemed to invalidate the conditions for significant risk transfer if, as a result of the transaction, the reduction in risk-weighted exposure amounts the originator institution initially achieved is no longer justified by a commensurate transfer of credit risk to third parties. The factors to be considered should include:
  - (a) the credit risk of the originator institution after undertaking the transaction; and
  - (b) the extent to which the capital or liquidity position of the originator institution is affected by the transaction.

## Relevant factors for assessment

19. When assessing whether a transaction is not structured to provide support as set out in paragraph 11, all relevant circumstances should be considered, including the following criteria.
20. The factor contemplated in point (a) of Article 248(1) of Regulation (EU) No 575/2013 (the price of the repurchase) should also be applied to transactions other than a repurchase and, in such cases, the amounts payable or, as the case may be, receivable by the originator institution or by the sponsor institution should be considered. For all transactions, measures of market value should be considered, including quoted prices in active markets for similar transactions that the institution can access at the measurement date. If such measures are not identifiable, then inputs other than quoted prices that are directly or indirectly observable for the asset should be considered; and, if such inputs are not identifiable, then unobservable inputs for the asset should be considered. In the case of unobservable inputs, the originator institution or sponsor institution should provide evidence to its competent authority regarding how the receivable or payable amounts have been valued and which inputs were used. The originator institution or sponsor institution should also demonstrate that this assessment is in line with its credit review and approval process. A transaction should be considered as not having been executed at arm's length conditions if the amounts receivable by the originator institution or, as the case may be, the sponsor institution are materially lower than, or the amounts payable by the originator institution or sponsor institution are materially higher than, the relevant market value.

21. The factor contemplated in point (b) of Article 248(1) of Regulation (EU) No 575/2013 (the institution's capital and liquidity position before and after repurchase) should be considered as also being relevant in the case of transactions other than a repurchase. The conditions for significant risk transfer should be considered as no longer being satisfied if, as a result of the transaction, the reduction in risk-weighted exposure amounts the originator institution initially achieved is no longer justified by a commensurate transfer of credit risk to third parties, which should be the case if the originator institution's capital or liquidity position is materially and adversely affected, directly or indirectly, by the transaction. In making such assessment, among other things, the accounting entries that the participants to the transaction made with respect to the transaction and the changes in their liquidity position should be considered.
22. Regarding the factor contemplated in point (c) of Article 248(1) of Regulation (EU) No 575/2013 (the performance of the securitised exposures), if the underlying exposures being subject to the transaction have been underperforming relative to other securitised exposures or have been reported as non-performing, it should be considered that the transaction is not executed at arm's length conditions if either such underperformance or the foreseeable future performance of such exposures as a result of the circumstances having caused such underperformance is not adequately reflected in the price of the purchase or repurchase.
23. Regarding the factor contemplated in point (d) of Article 248(1) of Regulation (EU) No 575/2013 (the performance of the securitisation positions), if the securitisation positions being subject to the transaction have been underperforming relative to other securitisation positions or have been reported as non-performing, it should be considered (i) whether the cost of measures taken to improve the performance of these securitisation positions has been fully borne by the relevant securitisation investors and (ii) whether the institution which participated in the transaction is negatively affected, directly or indirectly, by the transaction.
24. Regarding the factor contemplated in point (e) of Article 248(1) of Regulation (EU) No 575/2013 (the impact of support on the losses expected to be incurred by the originator relative to investors), it should be considered whether the expected losses of a securitisation position are materially increased or reduced, having regard, among other things, to changes in the market price of the position, in the risk-weighted exposure amounts and in the ratings of securitisation positions.

## Notification and documentation

25. The requirement of notification to the competent authorities of any transaction, regardless of whether it provides support to the securitisation, referred to in Article 248(1) of Regulation (EU) No 575/2013 should apply to any transaction which is entered into by an originator institution or by a sponsor institution or which meets the following conditions:
  - (a) it is entered into by an entity, other than the originator institution, (i) which is a parent undertaking of the originator institution, a subsidiary undertaking of the originator institution or a subsidiary undertaking of a parent undertaking of the originator institution or (ii) to or with which the originator institution or another entity contemplated in item (i) provided, directly or indirectly, any financing, support

or instructions or entered into any arrangement in relation to the entering into of such transaction; and

- (b) it would be subject to these guidelines had it been entered into by the originator institution.

Where the conditions set out in subparagraphs (a) and (b) of this paragraph 25 are met, the transaction should be assessed as if it had been entered into by the originator institution.

26. When notifying a transaction as required pursuant to Article 248 of Regulation (EU) No 575/2013 (as further specified in paragraph 25), the originator institution or, as the case may be, the sponsor institution should:

- (a) if it claims that the transaction does not constitute implicit support, provide adequate evidence of meeting the relevant conditions set out in these guidelines; and
- (b) if the transaction is undertaken by one of the entities referred to under item (i) or (ii) of paragraph 25(a), the originator institution should also provide documentation on the type of relationship between the originator institution and the relevant entity or, as the case may be, the financing, support, instructions or arrangements provided or entered into by the originator institution to or with that entity for the purposes of undertaking the relevant transaction.

## 5. Accompanying documents

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### 5.1 Cost-benefit analysis / impact assessment

#### Introduction

Article 16(1) of the EBA Regulation (Regulation (EU) No 1093/2010 of the European Parliament and of the Council) provides that any guidelines developed by the EBA shall be accompanied by an analysis of ‘the potential related costs and benefits’. This analysis should provide an overview of the findings regarding the problem to be dealt with, the solutions proposed and the potential impact of these options.

#### Scope and nature of the problem

Securitisations can help institutions to efficiently manage their balance sheet and diversify their funding sources. Securitisations are also a recognised credit risk mitigation tool, which can significantly reduce credit risk by transferring it to a third party. The CRR requires that any reduction of capital requirements achieved through securitisation be justified by a commensurate transfer of risk to third parties. Considering this, the provision of implicit support to the securitisation raises significant supervisory concerns, and therefore Article 248 CRR places restrictions on the provision of support to the securitisation beyond existing contractual obligations. It is therefore important to assess when a transaction is structured to provide support.

#### *Objectives of the guidelines*

In Article 248(2) CRR, the EBA is mandated to issue guidelines on what constitutes arm’s length conditions and when a transaction is not structured to provide support. This is necessary in order to ensure that the prohibition in Article 248 CRR is applied consistently. The arm’s length test constitutes part of the assessment of whether the transaction is structured to provide support.

The proposed guidelines seek to address the mandate by defining the notions outlined above and by providing further guidance on how the factors contemplated in points (a)-(e) of Article 248(1) CRR should be assessed.

## Technical options considered

This section explains the rationale behind some of the choices that the EBA has made when designing the guidelines. The main principle followed was that a workable test should be provided, which would ensure a consistent application of the prohibition on providing implicit support without affecting legitimate transactions.

The guidelines include (i) the conditions to be satisfied in order to determine that a relevant transaction is not structured to provide support, depending on whether the relevant transaction is entered into by a sponsor institution or by an originator institution, (ii) an objective test for assessing whether a relevant transaction is entered into at arm's length terms, (iii) clarifications regarding the notification requirements for relevant transactions and (iv) further guidance on how the conditions for checking whether a transaction is structured to provide support, including the factors set out in points (a)-(e) of Article 248(1) CRR, should be assessed. The scope of the guidelines goes partly beyond the mandate in the CRR where this is considered necessary by the EBA.

### *Requirements for originator institutions and sponsor institutions*

The guidelines set out details of the assessments that originator institutions and sponsor institutions will need to undertake and the information they should provide to competent authorities when contemplating entering into a relevant transaction.

### *Requirements for competent authorities*

The guidelines establish the test to be applied by competent authorities when assessing whether a relevant transaction constitutes implicit support and provide further guidance on how the test should be applied.

## **Costs**

The EBA believes that there will be two types of costs:

**Costs for competent authorities** – The main direct cost for competent authorities will be in relation to the processes for assessing whether a relevant transaction constitutes implicit support. The guidelines could generate additional compliance costs within those Member States which currently conduct less extensive checks than those proposed by the guidelines. Such costs for the competent authorities could be driven, for instance, by the need to change some of their existing processes, to train existing staff or to hire additional staff members.

**Costs for relevant institutions** – The main cost for relevant institutions will be related to setting up processes in order to be able to disclose the necessary information and evidence to the



competent authorities and to ensure that each relevant transaction is properly assessed. The compliance costs of these guidelines are likely to vary between jurisdictions.

### **Benefits**

By specifying the test to be applied by competent authorities and relevant institutions in assessing whether a transaction is structured to provide support and providing guidance on how it should be applied, the guidelines ensure that a more consistent approach will be taken to the application of the implicit support regime.

## 5.2 Views of the Banking Stakeholder Group (BSG)

### Summary of the BSG opinion

The BSG welcomes the EBA's consultation paper and its initiative to produce a set of clear guidelines that can eliminate uncertainty in the securitisations market, especially legal uncertainty, and act as another measure for the revival of the securitisations market in Europe. The BSG also supports the general approach followed in the guidelines, which focus on clarifying the requirements set out in Article 248 CRR in order to achieve greater consistency in its application.

Regarding the definition of arm's length conditions, the BSG argues that the definition should be comprehensive but not so strict as to hamper the functions of securitisation markets. The BSG submits that replacing existing exposures with new ones of higher quality could be a reasonable part of the implied duties of originators or sponsors towards investors in the securitisation and that sponsor or originator institutions will do so only in the full knowledge that such actions have an adverse impact on the bank's capital position and overall risk profile. In the absence of a contractual obligation, such activity will happen very rarely and when another risk would be higher (such as reputational risks, especially for the sponsor). The BSG contends that the value of continuous supervision should not be discounted and, as such, it is not clear why a replacement or topping-up activity to stave off reputational risk, in the absence of a pre-commitment do so, is an unmanageable development under the bank's capital framework and should render the securitisation in question a non-true risk transfer transaction. Furthermore, the BSG suggests the removal from the definition of arm's length conditions of the reference to extraneous considerations which are not directly connected with the transaction in question.

Regarding the proposed definition of transactions not structured to provide support, the BSG argues that failing to meet the proposed condition regarding significant risk transfer should not automatically lead to the conclusion that implicit support has been provided. The loss of significant risk transfer might result from a risk management decision of the bank, which resolves to increase its exposure on a securitisation transaction, and have nothing to do with supporting investors. If the transaction is executed at arm's length (or better) conditions, the BSG argues that it should be outside the scope of the implicit support rules and it should not be considered for the purposes of the sanctions contemplated in Article 98(3) of Directive 2013/36/EU. The BSG reiterates that replacement or topping-up activities which occur on an ad hoc basis and are based on a need to stave off reputational risk should not negate the true risk transfer.

In respect of transactions undertaken by a third party, the BSG argues that the arm's length test should be sufficient.

### 5.3 Feedback on the public consultation and on the opinion of the BSG

The EBA publicly consulted on the draft proposal contained in the consultation paper.

The consultation period lasted 3 months and ended on 20 April 2016. In addition to the BSG opinion, two other responses were received. All responses were published on the EBA website.

This paper presents a summary of the key points and other comments arising from the consultation, the analysis and discussion triggered by these comments and the actions taken to address them, if deemed necessary.

In certain cases several industry bodies made similar comments or the same body repeated its comments in the response to different questions. In such cases, the comments and the EBA analysis are included in the section of this paper where the EBA considers them most appropriate.

Changes to the draft guidelines have been incorporated as a result of the responses received during the public consultation.

#### Summary of key issues and the EBA's response

A limited number of responses to the consultation were received. Nonetheless, a number of common themes emerged.

The respondents stressed the importance of ensuring that transactions agreed upon at the inception of the securitisation should not be caught by the prohibition on implicit support, specific examples including fully supported asset-backed commercial paper conduits. The respondents were also concerned by the notification requirements and suggested that the scope of transactions to be notified to the competent authorities be limited to the extent feasible within the context of the requirements in the CRR. Other issues in respect of which comments were received regarded the desirability of providing more concrete guidance by way of examples and the extension of the assessment beyond originator institutions, sponsor institutions and their group companies.

A more detailed presentation of the comments received and of the EBA response may be found in the table set out below.

## Summary of responses to the consultation and the EBA's analysis

Comments	Summary of responses received	EBA analysis	Amendments to the proposals
<b>Responses to questions in Consultation Paper EBA/CP/2016/01</b>			
<b>Question 1: Do you have any general comments on the draft guidelines on implicit support under Article 248(2) of Regulation (EU) No 575/2013?</b>			
<b>Scope of application of the guidelines</b>			
Distinction between explicit and implicit support	<p>Implicit support should not cover support that institutions are already contractually obliged to provide. As such, it should be clarified that the guidelines do not apply to fully supported conduit sponsors. The sponsor's support in the case of a fully supported asset-backed commercial paper (ABCP) conduit is contractually documented and appropriately reflected in the bank's calculations and, as such, constitutes explicit support. Similarly, if time calls, clean-up calls or swaps are contemplated by the documentation of a transaction from its inception and are considered in the initial decision with respect to significant risk transfer, they should not be deemed to constitute implicit support.</p> <p>Paragraph 2 of the Background and rationale section of the Consultation Paper sets out examples of implicit support, in particular the sale of discounted credit risk exposures. To avoid any doubt, it should be clarified that the sale of discounted credit risk exposures into the pool of securitised credit risk exposures at the inception of a transaction and as contractually agreed does not constitute implicit support.</p>	<p>The draft guidelines already clarify this point by referring to transactions the institution (i) is under no contractual obligation to enter into or (ii) is not under a contractual obligation to enter into on the specific terms of such transaction. However, the point can be reiterated for the sake of clarity.</p>	<p>Please refer to paragraphs 6 and 10 of the guidelines.</p>

Comments	Summary of responses received	EBA analysis	Amendments to the proposals
Limitation of the scope of the guidelines	<p>Implicit support risk was an issue in relation to certain securitisation vehicles prior to the 2007/2008 financial crisis. However, implicit support was not an issue for the vast majority of securitisation asset classes or other bank-sponsored activities. As such, this was a fairly narrow problem that was not spread across a significant number of asset classes or activities. Many new regulations have been implemented since the onset of the financial crisis; therefore, the objective of the guidelines should be relatively modest, namely a simple clarification of the requirements set out in Article 248(1) with some guidance about how they are to be applied. Subject to the other comments, the respondent agrees that this is broadly the thrust of the draft guidelines and is supportive of this general approach.</p>	The EBA notes the feedback provided.	No change.
<b>Significant risk transfer</b>			
Paragraphs 16 and 17 of the draft guidelines as set out in the Consultation Paper	<p>Paragraphs 16 and 17 of the draft guidelines, as set out in the Consultation Paper, seem to introduce additional criteria for maintaining previously agreed significant risk transfer over and above the requirements of the CRR and the existing guidelines on significant risk transfer (EBA/GL/2015/05). Without commenting on the content of these paragraphs, they should be considered in the context of the guidelines on significant risk transfer (SRT) and not in the context of a consultation on implicit support.</p>	<p>The guidelines should be read in conjunction with the existing guidelines on Significant Credit Risk Transfer, to which they make specific reference. Considering the existing guidelines cover more substantially the assessment of significant risk transfer at the inception of the securitisation, it was deemed appropriate for the new guidelines to provide further clarity on the assessment to be carried out on an on-going basis. The former paragraph 16 (paragraph 18 in the final version of the guidelines) was rephrased so as to clarify that the relevant test is whether, following the transaction, the reduction in risk-weighted</p>	Please refer to paragraph 18.

Comments	Summary of responses received	EBA analysis	Amendments to the proposals
		<p>exposure amounts initially achieved is still justified by a commensurate transfer of risk to third parties. All relevant factors should be considered, including changes in the market price of the securitisation positions, changes in the total risk-weighted exposure amounts of the securitisation position holders and changes in the securitisation position ratings. Any assets that the originator institution transfers back to its balance sheet as a result of the transaction should be included in the originator institution's assessment of the changes in the total risk-weighted exposure amounts.</p>	
<p>Paragraph 16(b) of the draft guidelines as set out in the Consultation Paper</p>	<p>The draft guidelines stipulate that a transaction should, among other things, be deemed to invalidate the conditions for significant risk transfer if the capital or liquidity position of the originator institution is, directly or indirectly, materially affected by the transaction. It should be clarified that only adverse changes would be caught.</p>	<p>The paragraph was rephrased so as to refer generally to the capital or the liquidity position of the originator institution as being one of the factors to be considered. Furthermore, paragraph 21 makes reference to the originator institution's capital or liquidity position being materially and adversely affected.</p>	<p>Please refer to the revised wording of paragraphs 18(b) and 21.</p>
<p>Notification obligations</p>	<p>The guidelines should, notwithstanding the provisions of Article 248(1) CRR, define certain exceptional cases that are not subject to notification to the competent authorities, for example activities conducted by the originator concerning the continuation or liquidation of a transaction or the respective SPV that are not explicitly contractually agreed but are also not intended to protect investors from any losses or improve the performance of the securitised assets or securitisation positions. Other examples include the repurchase of ABCP, which must be</p>	<p>In accordance with Article 248(1) CRR, any such transaction shall, regardless of whether it provides support, be notified to the competent authorities. The guidelines cannot purport to amend the Regulation and, as such, no flexibility can be foreseen in respect of transactions entered into by originator institutions or by sponsor institutions. However, the scope of transactions entered into by third parties which are captured by the</p>	<p>Please refer to the revised wording of paragraphs 25 and 26.</p>

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	done at market prices and is typically subject to a market conformity check, and it was suggested that the guidelines could, to the extent feasible in the context of the CRR text, limit the scope of transactions that have to be notified to the competent authorities to those that pose a real risk of providing implicit support.	guidelines has been clarified.	
Level of specificity	The guidelines are necessarily vague. They attempt to deal with a very wide range of asset classes and transaction structures which could be supported in a multitude of different ways, all in a single set of guidelines. The challenge is compounded by the overlap with the SRT guidelines. The uncertainty might be mitigated by providing a series of illustrative examples for each of the pieces of guidance in the draft guidelines.	The guidelines are meant to provide general guidance and not necessarily to deal with each scenario which may arise. Providing illustrative examples is unlikely to constitute a meaningful exercise, as the guidelines are meant to cover a wide array of transactions and asset classes. However, further guidance on specific scenarios may be obtained via the EBA Q&A tool.	No change.
<b>Question 2: Do you have any comments on the proposed definition of transactions not structured to provide support?</b>			
	<p>The definition of transactions not structured to provide support should be amended to remove the suggestion that the loss of SRT treatment in and of itself indicates the presence of implicit support.</p> <p>There is a concern that the proposed definition implies that the loss of SRT treatment will automatically result in a conclusion that implicit support has been provided. Although the presence of implicit support will always result in the loss of SRT treatment, the converse is not true. The loss of SRT treatment might simply result from the originator exercising a right to unwind the transaction contemplated in the original documents or the originator might simply have unwound the</p>	<p>The provisions in Article 248(1) CRR regarding the reduction of potential or actual losses to investors can be further reflected in the guidelines.</p> <p>The arm's length test is not, however, sufficient on its own for the purposes of implicit support analysis. This is apparent from Article 248(1) CRR, which specifically refers to the transaction being taken into account in the assessment of significant risk transfer.</p>	Please refer to the revised wording of paragraph 13.

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	<p>transaction (or part of it) via a liability management exercise. In either case, the originator's intention may have nothing to do with supporting investors and everything to do with what is expedient for itself.</p> <p>If the transaction is executed at arm's length (or better) conditions, it should be outside the scope of the implicit support rules.</p>		
<b>Question 3: Do you have any comments on the proposed definition of arm's length conditions?</b>			
<p>Level of specificity</p>	<p>Paragraph 15 on the meaning of 'arm's length conditions' for the purposes of Article 248 is appropriate in that it accurately describes the concept of 'arm's length conditions' as understood by the industry. However, the definition is very theoretical and in practice requires institutions to come up with a hypothetical and somewhat arbitrary set of terms on which arm's length parties would have transacted in order to act as a benchmark for the transaction actually proposed or undertaken. This is necessarily a somewhat artificial exercise that could be hard to complete in a way that provides reasonable assurances that it would not be second-guessed by a competent authority.</p> <p>The guidance in paragraph 16 that only information available to the parties at the time of the transaction will be used to assess whether the terms were 'arm's length' is helpful.</p>	<p>The definition of arm's length conditions needs to be abstract. It should provide a meaningful test covering a wide range of scenarios and, as such, it cannot be tailored to apply to specific situations.</p> <p>Furthermore, as outlined in the response, the definition reflects the understanding of the industry. Thus, there appears to be no compelling reason to replace the definition, nor was a concrete suggestion provided.</p>	<p>No change, save as outlined below.</p>
<p>Replacement or topping up for the sake of avoiding reputational risk</p>	<p>It was argued that replacing existing exposures with new ones of higher quality could be a reasonable part of the implied duties of originators or sponsors towards</p>	<p>Whilst on-going supervision is extremely important, its value should not be overstated; if it were sufficient, there would be no need for restrictions on</p>	<p>Please refer to the revised wording of paragraph 15.</p>



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	<p>investors in the securitisation and that sponsor or originating institutions will do so only in the full knowledge that such actions have an adverse impact on the bank's capital position and overall risk profile. The value of continuous supervision should not be discounted and, as such, a replacement or topping-up activity to stave off reputational risk should not constitute implicit support.</p>	<p>implicit support. Furthermore, entering into a transaction for the sake of avoiding reputational risk is precisely one type of scenario that the rules on implicit support are designed to restrict.</p> <p>It is acknowledged, however, that considerations relating to avoiding reputational risk can be taken into account by the relevant institution among other matters, so long as they are not the prevalent factor in resolving to enter into the transaction.</p>	
Extraneous considerations	<p>The reference to extraneous considerations which are not directly connected with the transaction in question should be removed.</p>	<p>This issue was examined above.</p>	<p>Please refer to the revised wording of paragraph 15.</p>
<p><b>Question 4: Do you have any comments on the proposed guidance regarding the factors contemplated in points (a)-(e) of Article 248(1) of Regulation (EU) No 575/2013?</b></p>			
General comments on the factors	<p>The guidance should provide more certainty; one way of achieving this result is the provision of illustrative examples.</p>	<p>As outlined above, providing illustrative examples is not considered suitable for the guidelines.</p>	<p>No change.</p>
Paragraph 20 of the final guidelines	<p>The general comment regarding the level of certainty being provided by the guidelines is reiterated by reference to the fact that the draft guidelines do not specify what is meant by amounts receivable that are materially lower or amounts payable that are materially higher. Specific examples should be provided.</p>	<p>The considerations set out above also apply in this case. Transactions should be assessed on a case-by-case basis. The guidelines would not be a proper venue for introducing thresholds and it should be noted that any given threshold is likely to be arbitrary, considering the fact that there would be significant differences across asset classes and market conditions.</p>	<p>No change.</p>
Paragraph 20 of the final	<p>Regarding buybacks, the originator and/or sponsor institution is the most likely institution to be making a</p>	<p>Please refer to Article 248(1) CRR, which provides no carve-outs in respect of the obligation to notify</p>	<p>No change.</p>

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guidelines	<p>market in the securitisation bonds. It would be very onerous (potentially to the point of discouraging market making entirely) if originator and sponsor institutions had to verify each individual market making transaction with a competent authority prior to completing it in order to have certainty that it would not be considered to provide implicit support to the transaction.</p> <p>The guidelines should clarify that the intention is rather for originator and sponsor institutions to have systems and controls in place intended to ensure that any purchases of securitisation bonds are made on arm's length terms.</p>	<p>transactions entered into by the originator institution or the sponsor institution. However, it should be noted that neither the CRR nor the guidelines require the relevant institution to clear the transaction with the competent authority before completion (although the institution may do so).</p> <p>It is definitely expected that the relevant institutions would have systems and controls in place intended to ensure that the transactions are entered into on arm's length conditions, but this is not sufficient. It is expected, though, that competent authorities would apply proportionality in their review of the transactions.</p>	
<b>Question 5: Is the arm's length condition sufficient to test in all cases if a sponsor provides support? If not, what would be an appropriate requirement? Please provide examples.</b>			
	<p>Subject to other comments which were provided, e.g. on the definition of arm's length conditions, the proposed definition seems sensible.</p>	<p>The EBA notes the feedback provided.</p>	<p>No change.</p>
<b>Question 6: Should transactions undertaken by a third party other than the sponsor institution or originator institution be subject to the same assessment with regard to the provision of implicit support as transactions undertaken by the sponsor institution or by the originator institution or should they be subject to different assessment standards (and, if so, which standards)?</b>			
Applicable test	<p>One respondent argued that it is reasonable that the same rules should apply to the originator institution and its group companies. Likewise, the sponsor institution and its group companies should be subject to the same rules.</p> <p>A different respondent submitted that, in respect of</p>	<p>Transactions entered into by entities other than the originator institution and the sponsor institutions are considered under paragraphs 25 and 26. In this case, it is fitting that the transaction be assessed in accordance with the same criteria as a transaction entered into by the originator institution, as the relevant third party will either be a group company</p>	<p>No change.</p>

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	<p>transactions undertaken by a third party, the arm's length test should be sufficient.</p>	<p>of the originator institution or will have entered into arrangements with the originator institution in respect of the relevant transaction. As such, the transaction should be assessed as if it were a transaction entered into by the originator institution.</p>	
<p>Scope of application of the rules on implicit support</p>	<p>Beyond the group companies of the sponsor institution or originator institution, it seems unnecessary for the implicit support rules to apply at all. Whilst a general anti-avoidance rule to be applied in exceptional circumstances may be justified, it must be weighed against the possible inefficiencies that will come with banks having to expand the scope of the transactions they examine to avoid implicit support. In particular, if arranging banks (who will often be neither originator nor sponsor institutions) are required to enter into implicit support analysis for post-closing transactions they undertake in respect of securitisations they arrange, that could result in significant cost and a powerful disincentive to arrange securitisations in the future.</p>	<p>The clarification is required to ensure the restrictions on providing implicit support are not cut across by arranging that the transaction is entered into by a third party. However, the provision was rephrased for the sake of clarity.</p> <p>Regarding arranging banks, if they are not group companies of the originator institution and have not entered into arrangements with the originator institution in respect of the relevant transaction, they would not fall within the ambit of the provision.</p>	<p>Please refer to the revised wording of paragraphs 25 and 26.</p>