19/12/2017

EBF response to EBA discussion paper on the Significant Risk Transfer in Securitisation

Key points:

- The EBF welcomes the EBA efforts to produce a transparent framework for significant risk transfer (SRT) transactions. More specifically, **the EBF supports the EBA proposals that aim at enhancing the process of the SRT assessment** and would like to highlight the importance of ensuring that banks receive feedback from the competent regulatory authority ahead of the closing of the transaction.
- Notwithstanding this, **the EBF is opposed to a possible retrospective application of the legal framework** that would arise from these discussions on SRT in securitisation. EBA has up to two years to produce a report for the European Commission based on which the European Commission will elaborate a delegated act. Such a period of prolonged uncertainty for securitisation originators is not welcomed since it has the potential to materially impact originators' securitisation plans for perhaps the next 24/36 months. We recommend EBA to clarify that any retrospective application of the forthcoming legal framework is discarded.
- The EBF acknowledges and agrees that synthetic excess spread which provides funded credit enhancement in a synthetic transaction must be recognized as a 1250% securitisation position in accordance with current guidelines. However, **excess spread which is not funded or "trapped" in either traditional or synthetic securitisations should in no case be considered as a securitisation position and subject to Pillar 1 own fund requirements**, since this would raise serious concerns for the economic viability of the deals given that the non-neutrality introduced into the new capital calibrations would cause a double capital penalty if additional capital for un-trapped excess spread were to be required. As a consequence, SRT recognition would be significantly hindered, thereby reducing the efficiency of SRT deals, increasing the costs to unacceptable levels and subjecting originators to contradictory regulations: i.e. raising costs in such a way that originators violate the cost of protection restrictions.

European Banking Federation aisbl

Brussels / Avenue des Arts 56, 1000 Brussels, Belgium / +32 2 508 3711 / info@ebf.eu
Frankfurt / Weißfrauenstraße 12-16, 60311 Frankfurt, Germany
EU Transparency Register / ID number: 4722660838-23

www.ebf.eu

- It is important to **provide enough flexibility to use other alternative amortisation structures** than pro-rata amortisation. With regard to the triggers proposed for the pro-rata amortisation approach, the EBF recommends adopting some flexibility to adapt and/or omit some of these triggers since depending on the specifics of the securitisation, not every proposed trigger may not be relevant.
- The proposal that requires that **time calls in synthetic securitisations can only be exercised later than weighted average life plus replenishment period puts a significant penalty on the transactions**. In this sense, the EBF recommends maintaining the current treatment applied in those EU jurisdictions that allow time calls which do not require the replenishment period to be taken into account.
- **The EBF strongly opposes the prohibition of time calls in traditional securitisations**. The economic rationale for permitting time calls in synthetic transactions are also applicable to traditional securitisations. We do not believe an outright prohibition of time calls for traditional securitisations is a proportionate response to address regulator concern about implicit support or step-in risk that such calls present. New regulations on implicit support and step-in risk have dealt with these concerns. If concerns remain, there are other solutions, such as subjecting the exercise of a time call in a traditional securitisation to supervisory regulatory approval and/or permitting time calls in circumstances where the traditional securitisation no longer provides any regulatory capital benefit.
- **The use-it-or-lose-it approach must be allowed for both traditional and synthetic securitisations.** The use-it-or-lose-it mechanism achieves higher risk transfer than the trapping approach. In this sense, the EBA preference for the latter one is not clearly understood. The EBF does not agree that accurately calculating synthetic excess spread is difficult, as the EBA has expressed. In addition, by limiting the amount of synthetic excess spread committed as credit enhancement to the EL of the portfolio, this concern is effectively mitigated.
- **The use of the originator's bankruptcy as an early termination clause should not be automatically banned.** The originator bankruptcy can be excluded as an early termination event as long as the originator continues to fulfil its premium or interest payment obligations and reporting and servicing obligations under the contract and only if investors are protected from the counterparty risk caused by depositing the protection tranche funds with the originator.
- **The design of the new proposed tests is somehow flawed** and should be corrected to avoid discarding the achievement of SRT for operations that show viable features to achieve it.
    - The same securitisation transaction which transfers a major share of EL and UL risk to investors can nevertheless fail the mezzanine test if the capital structure of the transaction includes mezzanine tranches, because the test is applicable regardless if the first loss tranche has also been sold to investors or retained.
    - The new definition of mezzanine tranche, which excludes tranches risk weighted 1250% further aggravates the anomaly of the mezzanine test described above.
    - The new requirement on the thickness of the first loss tranche can also entail unintended consequences and unjustifiably discard some viable operations in cases where the first loss tranche does not meet the first

loss test while even in cases where the combination of the mezzanine and first loss tranches sold is sufficiently robust to covers a sufficient major share of EL and UL.

  - The requirement on a minimum thickness of the first loss tranche in the Mezzanine Test does not appear to be justified for mezzanine structures where the sold mezzanine tranches attach at the detachment point of the first loss tranche. Consequently, such sold mezzanine tranches transfer the risk of the EL that is not covered by the first loss tranche, and accordingly should be taken into consideration for purposes of determining adequate SRT.

- **The EBF agrees with the EBA's recommendation to take into account the purchase price discount in calculating the attachment points of retained tranches**. We believe the same principle should apply to securitisations of non-NPL assets which the originator may have acquired at a discount.

EBF position:

Part 1: Overview of market practices with respect to SRT

1. Does the data on synthetic and traditional SRT securitisation transactions correspond with your assessment of SRT market activity in the EU? Do you have any observations on these data?

The EBF believes that the **data provided by EBA on synthetic and traditional SRT securitisation transactions is broadly accurate,** although it has missed some very large transactions, such as the €8bn transaction completed by a Nordic bank in 2016. However, it is worth noting that some important aspects of securitisation transactions were not analysed:

1. The percentage of traditional SRT securitisations which were publicly listed transactions compared to private placements.
2. The percentage of SRT synthetic transactions which were publicly or privately issued CLNs.
3. The percentage of synthetic transactions which were structured as private bilateral guarantees or CDS.
4. Client-driven activities were not included in the sample. Pre-notifications should not apply to these transactions because they do not have structured features.

Part 2: Overview of supervisory frameworks for assessment of SRT

2. Are you aware of any material supervisory practices that have not been covered in the EBA analysis?

First of all, the EBF fully shares the opinion (paragraph 70) that lengthy feedback procedures may result in a high degree of uncertainty for the market and that it is highly important to **receive feedback from the competent regulatory authority ahead of the closing of the transaction** which is currently not ensured. SRT decisions may have important consequences for the structuring of the transaction and banks should have some time to adapt the structural features of the transaction as a consequence of the competent authority's feedback. It is also noteworthy that the issuance costs may be too high to incur if ultimately the SRT deal will be rejected. The issuance costs are too high to run the risk of rejection of the SRT treatment without having a chance to remedy.

In addition, there is too much reputational risk with investors if banks have to call the deal early because it didn't receive approval. In this case, investors may also require some minimum amount of fees which globally leads to higher costs for banks, with no effect on SRT.

The feedback provided by the competent authority before the closing of the transaction should at least highlight:

a. any issues the competent authority considers problematic
b. any issues which they intend to focus attention on
c. the type of analysis and information they will require to address any issues cited in b. above.

- The EBF also fully agrees with the EBA recommendation that, even for deals that meet the mechanistic test and therefore do not require specific supervisory approval, originators should be able to expect a no objection from the competent authority, since they always have the discretion to reject a deal. It is worth noting that currently in most cases, competent authorities provide zero feedback prior to closing. Some members report that they receive detailed feedback on final terms within the recommended 90 day window.

Accordingly, it is reasonable to insist that NCAs provide preliminary feedback prior to closing, assuming the originator is able to provide sufficient detail about the expected terms and conditions of the proposed transaction.

Part 3: Assessment and proposals for discussion in relation to the process of the SRT assessment

3. What are your views on the proposals on the assessment process set out above? Are any other changes necessary to further improve the process?

It is important to **banks to receive feedback from the competent authority early enough** for them to change the structure of the securitisation if necessary to achieve the significant risk transfer. We recognise that the competent authority cannot provide final approval until the final terms of the transaction are known, which may in some cases be after the deal closes. However, if originators are uncertain about the interpretation of the SRT rules in relation to certain structural features, originators who can provide clarity on the expected terms prior to closing should be entitled to receive supervisory feedback on such interpretative points before closing the transaction.

The EBF preferred solution regarding the assessment process would be the following:

- The **originator shall notify** the competent authority no later than **45 days** before the expected closing date ;
- The **competent authority** should provide a notification on SRT compliance and non-objection/objection at least **14 days** before the expected closing date (and no later than around 30 days after the first notification by the originator) ;
- A **non-response** can be considered by the originator as a non-objection of the competent authority.

In that context, the EBF appreciates the proposals on the standardization of the SRT assessment process and the shortening in the notification period to one month. There are costs incurred by the bank in setting up a transaction which would be closed out prematurely if it doesn't receive SRT approval. In case those potential issues are communicated by the competent authority, the bank will have the time to adjust the features as requested in order to achieve SRT.

It is important to emphasize, that once the proposals on response deadlines are agreed, they would be binding to the relevant competent authorities and do not provide them further flexibility, so e.g. the ex-ante notification period should not be extended by the competent authority. This is important in particular when considering that the ECB has currently set a period of 3 months- beyond our proposed 45 days before closing. As discussed above, the EBF member recognize that where deal terms have not been finalized at the time of the first notice to the national competent authority, that they cannot expect final approval from NCAs prior to closing. In such cases, originators should be able to expect feedback on the preliminary terms of a transaction that the NCA finds problematic. Originators can then make a risk based decision on the permitted changes to the commercial terms from that point forward comforted that a substantially final set of terms has been subjected to a supervisory assessment. However, if final terms are known prior to notice to the NCA, originators should be able to expect approval prior to closing.

The EBF further welcomes the EBA's proposal, that the competent authority should provide an explicit point in time feedback to the originator, even where there is no permission required (e.g. quantitative test).

Finally, the EBA cites the fact that very few deals have sought approval under Art 243(4) or 244(4). It is important to contextualize this observation and highlight that in our experience, competent authorities do not want to commit themselves to analyzing deals which cannot meet the mechanistic tests and much less providing timely approval. Average response time for certain of our banks has been around 11 months.

We would like also to request that the EBA provide guidance for requiring harmonised feedback on transactions issued by originators which are subject to different NCAs. For example, this may arise with originators with subsidiaries in different European countries, each of which is subject to supervision by two or more NCAs. We recognise that each NCA must exercise its supervisory responsibilities, but it would be helpful for NCAs to coordinate with each other to provide consistent feedback on the same transaction.

4. Could you provide suggestions as to whether and how the template for SRT notification by the competent authority to EBA provided in Annex I of the EBA Guidelines should be amended to reflect the new EU securitisation securitisation framework and the STS securitisation product?

Apart from the changes already implied by the new CRR articles, the new requirement of homogeneity of collateral and those required to include additional inputs for new tests, **the EBF does not envisage further amendments** to the template of SRT notification by the competent authority to EBA.
Moreover, the guidance on SRT (24th March 2016) is a clear and well detailed guide to assessment of SRT.

5. Should a standardised SRT notification template be developed, for submission by originators to competent authorities, in order to facilitate the SRT assessment process? If yes, should this template be different for traditional and synthetic securitisation? (Please provide examples of templates, as appropriate).

It is important to strike the right balance between standardisation and recognition of the diversity of situations in terms of asset classes, geographies and local laws. We should retain some level of flexibility and ensure a deal by deal review by competent authorities in order to provide a sufficient safety net in terms of banking supervision.
On the other hand, the notification template should create some kind of level playing field, where currently competent authorities in different jurisdictions have widely diverging requirements w.r.t. the information to be provided as part of the notification.
In case a new SRT notification template should be developed, the ECB required questionnaire (of 24 March 2016) would be a good reference. A separate

questionnaire should be developed for traditional and synthetic securitisation to reduce confusion. For example, banks sometimes receive questions from competent authorities that indicate that the analyst had misidentified the transaction under review.
The ECB currently assesses transactions using an internal guidance manual available only to supervisors. This internal guidance requires further information not listed in the ECB Guidance of March 2016 which results in further information requests to Originators. It is important that any standardised template is not only exhaustive in the information it requires but also states clearly how supervisors should use the information to ensure Originators understand the context in which it is being supplied.

6. Could you provide suggestions as to how a template for monitoring SRT compliance should look like (e.g. by potential amendments of the current COREP framework)?

In general, the multiplication of ad hoc reporting by institutions creates operational risk. In this sense, the EBF would suggest the EBA to **incorporate the SRT monitoring reporting into the COREP framework**.

If a template will be developed, this should be different for traditional and synthetic securitisations. We consider this distinction as useful, as a traditional securitisation is usually regarded as a standard transaction in contrast to a synthetic securitisation. Consequently, any features that are common in synthetic securitisations but not in traditional securitisations or vice-versa are regarded as a discrepancy and require further explanations.

The frequent monitoring is important but should not be overly burdensome.
And monitoring should not lead to ongoing re-assessment of the SRT status of a transaction but just to confirm that:

1. No material structural changes have been made to the transaction or to describe any amendments which have been made.
2. The originator has not engaged in any actions that would constitute implicit support or "step-in".

Part 4: Assessment and proposals for discussion with respect to selected structural features of SRT transactions

7. Do you agree with the assessment of the SRT implications of all the identified structural features? Are any material aspects missing from this representation?

First of all, the EBF would like to mention that to the best of our banks' knowledge, **the list of structural features with SRT relevance is exhaustive.**

In particular, with regard to amortisation, the EBF would like to mention that it is important to **provide enough flexibility to use other alternative amortisation structures** than pro-rata amortisation, such as:

a. A hybrid structure that features sequential amortisation until the protected tranche reaches a certain percentage threshold, whereafter the amortisation switches to pro-rata amortisation.
b. Another option that must be considered by EBA would consist in a variation of the amortisation structure for each tranche. For example, in some transactions where banks agree to hold a small first loss piece, investors have requested that banks amortise the first loss piece on a sequential basis, while the mezzanine protected tranche and senior tranche amortise on a pro-rata basis. The investor in this case is exposed to the mezzanine tranche – hence it benefits from a non-amortising first loss protection, while its exposure is reducing in line with the senior tranche.

These alternative structures should be considered valid, subject to the originator's duty to demonstrate effective SRT in their self-assessment reports.

8. Do you agree with the proposed safeguards related to the use of pro-rata amortisation?

Depending on the specifics of the securitisation, every trigger may not be relevant. It is not clear if the list given (§92) is meant to be included in all deals as a minimum. Some of the triggers are not applicable to all asset types. For example, the granularity test would not be applicable in extremely granular portfolios where no loan or groups of loans would ever be expected to reach a meaningful percentage of the pool. **The EBF recommends to provide some flexibility to adapt and/or omit some of these triggers. The triggers can be discussed with the Competent Authorities during the notification process.**

The contractual triggers that switch from a pro-rata amortisation to a sequential amortisation may significantly increase the costs of the securitisation transactions which may present concerns to competent authorities in respect of the cost of protection. As such, the triggers should represent a true stress in the portfolio (a multiple of EL rather than simply having losses equal to EL or modestly in excess of EL). There is also a role here for an IRR based trigger (already common to some market transactions) whereby when the IRR under the FG or CDS falls below a pre-defined level the amortization structure will be amended. This will ensure that there is an appropriate alignment between the cost of protection and the trigger.

9. Do you agree with the proposed safeguards related to the use of time calls? Do you agree with the different approach to time calls in traditional vs. synthetic transactions?

The theoretical framework that justifies the proposed constraints regarding time calls is somehow flawed.

First of all, **there is no clear argument about the reasons why the first call date should be so far out in the life of the transaction**.
Going back to the Basel framework approach (as early as Basel 1 & 2) about time calls, it should be clear that time calls are acceptable as long as there is no structural incentive to exercise them for the originator. As such, certain features pointing to a structural incentive (e.g. step up premiums) should be disclosed by the originator in its submission, reviewed by the competent authority and probably not allowed.
But, if the credit risk diminishes substantially (for example due to a reduction in the average PD, LGD, and/or IRBA maturity of the pool, which is typically reflected in a KIRB which is lower than the one at inception) the cost of the hedging may become too expensive relative to the value of the hedging. This situation could happen before the proposed non-call period ends. It doesn't make sense to impose this non-call period if the call exercise is favourable to the originator, and shouldn't present a prudential problem to the Competent Authority regulator, since the amount of RWAs which would be re-recognised by the Originator following the call will likely be immaterial. As discussed above, the EBA may want to recommend prior regulator approval by the Competent Authority of the exercise of a time call in cases where the level of RWA re-recognition would be material. However, as calls are in the original contracts, they are considered in the original SRT notification, and deemed to either breach SRT or not at that point, we would suggest that further approval is unnecessary, as upheld in the recent EBA guidance for Implicit Support. This would avoid administrative burden on the banks, allowing the calls to occur in a timely manner, and represents the analysis considered in the implicit support guidance. Accordingly, the exercise of this type of call should not be considered to be based on an incentive to call, nor on implicit support to the investor.

Furthermore, the EBA's proposal (paragraph 102(c)) that requires that **time calls in synthetic securitisations can only be exercised after the later than weighted average life (WAL) plus replenishment period, puts a significant penalty on many transactions**. This requirement differs from the current treatment in of those EU jurisdictions that allow time calls (such as Germany, Spain, Austria and Ireland), without requiring the replenishment period to be taken into account.

Allowing a time-call after the following WAL of the initial securitised portfolio, is a key structural element of some synthetic securitisations. Banks can typically undertake to replenish the underlying portfolio for a time equal to the WAL of their other book of assets eligible for such replenishment. Generally this WAL is in line with the WAL of the securitised portfolio. Therefore, not allowing a time call until after both the WAL and replenishment period will restrict a bank's ability to recycle securitised assets for a new transaction (particularly important for smaller banks) and will also restrict a bank's ability to benefit from changing market conditions, where calling a deal and securitising the assets in a new deal will allow the originator to benefit from reduced costs of protection. We would suggest that the exercise of the time call should follow the WAL of the securitised portfolio without reference to the replenishment period. As discussed above, the EBA may suggest that an Originator seek prior regulator approval by the Competent Authority before exercising such call if the amount of RWA re-recognition will be material.

The EBF also notes that the term Weighted Average Life needs to be clearly defined. There is a market standard (Bloomberg) definition as follows: *"The average number of years for which each dollar of unpaid principal on a loan or mortgage remains* *outstanding. Once calculated, WAL tells how many years it will take to pay half of the outstanding principal."* The calculation of WAL needs to include a standard basis for the calculation of prepayment rates which are Originator specific and a critical part of the WAL calculation.

Finally, the EBF strongly opposes the prohibition of time calls in traditional securitisations. There is no clear justification for the statement that banks will be more tempted to use time calls in a traditional SRT securitisation than in a synthetic. The reasons for exercising a time call in an SRT deal are completely different from the motivations of banks during the crisis. It is also noteworthy that EBA concerns related to step-in risk and implicit support have already been addressed through separate regulations, and therefore there is no need for this prohibition.
Since this issue is very political and involves many regulators, The EBF would suggest a **counter-proposals that allows the achievement of SRT for traditional securitisations with time calls** in the following situations:

a. Prior approval of the Competent Authority regulator has been provided in respect of Traditional Securitisations. This would give comfort that the Competent Authority regulator could examine the reasons for a bank wishing to call a deal to assure that no step-in or implicit support risk is was present, and/or in cases where the re-recognition of RWAs would be material.
b. If at any point, the transaction no longer provides any RWA reduction. This is a very real scenario likelihood for traditional securitisations with sequential amortisation, or even more so due to the higher capital calibrations which in some cases will eliminate RWA reduction, and/or make the cost of RWA reduction becomes uneconomic.

By no means, SRT should be automatically discarded when time calls are associated to traditional securitisations.

Finally, the EBF recommends the EBA to allow exercising time calls and/or regulatory calls by repurchasing certain tranches without having to unwind the entire transaction. This might be applicable for traditional deals done for both liquidity and SRT, where repurchase of expensive subordinated bonds which no longer provide RWA reduction would be useful, without having to call senior securities which were placed to receive funding.

10. Do you agree with the proposed safeguards on the use of excess spread in traditional securitisation?

The EBF would like to note that the proposed safeguards on the use of excess spread in traditional securitisation raise several important issues.

First of all, it should be highlighted that unearned excess spread should not be confused with earned or trapped excess spread. In several sections, it is not clear if EBA only refers to trapped excess spread, this must and we would appreciate this to be clarified.

We would like to highlight that EBA itself recognises that Pillar 1 own funds are not required for unearned excess spread for loan portfolios on banks' books. **The EBF strongly opposes the possibility to impose Pillar 1 funds requirements on excess spread used in securitisations**.

Indeed, **the proposal has a serious analytical flaw.** To the extent excess spread provides credit enhancement to a traditional or synthetic securitisation and has to be recognised as a securitisation position with a 1250% risk weight, **the risk of any senior retained tranches should be reduced in order to recognise the benefit of this credit enhancement**. This benefit is reflected in the SEC-ERBA approach, but not in the SEC-IRBA or SA approaches. This leads to an unfair "double counting" of capital requirements for transactions using excess spread and which must be calculated according to SEC-IRBA and SEC-SA. This problem was acknowledged by the regulators when they developed the new securitisation regulations competent authorities and is the reason for the special derogation for auto loan and lease securitisations. Unfortunately, it was not recognised for consumer loans, credit cards and other high spread portfolios. If on top of the higher capital charges reflected in the SEC-IRBA and SA formulas, it will now be required to recognise excess spread as a securitisation position, virtually no SRT transaction for these asset classes will be viable.

Any requirement to recognise excess spread as a securitisation position could raise serious concerns for the economic viability of many deals since, depending on the particular transaction, the conservative prudence of this proposal will defeat the purpose of the SRT guidelines to promote the use of securitisation for risk transfer purposes:

a. If originators are forced to recognise more 1250% securitisation positions, the RWA reduction benefit of these deals will be dramatically and negatively reduced.
b. To offset the negative effect of recognising additional securitisation positions, originators could explore selling additional tranches and/or selling the excess spread in an IO strip, but the cost of an SRT transaction in most cases would escalate above the cost of capital and/or in certain circumstances it might cause originators to violate the proposed cost of protection restrictions.

In addition, the EBF asks the EBA to clarify how "excess spread should be taken into account within the risk transfer self-assessment analysis submitted to the competent authority". More specifically, the EBA should clarify the following elements:

a. In some sections the EBA seems to refer only to excess spread committed and funded in "trapped" form to a securitisation. We understand from the public forum comments that this is the only type of excess spread for which a 1250% securitisation position would be required. This must be clarified.
b. It is unclear how the EBA proposes that the use of excess spread is to be taken into account in an originator's self-assessment. If the intent is to somehow recognise untrapped excess spread in a deal as a securitisation position, or to reduce SRT recognition for such deals, how should this be done? Through the use of some kind of NPV calculation of expected excess spread that will be available to cover losses? If so, how does this reconcile with the EBA's argument that the benefit of excess spread not trapped is limited in back-

loaded loss scenarios? As explained below, we consider that the use of excess spread in a transaction should not hinder or haircut SRT, but rather that the use of excess spread should be factored into the cost of protection. For example, in a synthetic transaction without synthetic excess spread, where losses are borne directly by investors in the protected tranches, the benefit of losses avoided should be legitimately considered as a reduction in the cost of the transaction. For traditional and synthetic securitisations which do use excess spread to absorb some losses, the originator may not legitimately claim a benefit for losses avoided as a reduction in the cost of protection (except for losses incurred in excess of such excess spread). In these latter cases, the originator would then have to justify the cost of the transaction without the benefit of losses avoided.

c. We believe the above approach of accounting for the use of excess spread as a cost is preferable to requiring recognising securitisation positions or additional Pillar 1 capital for excess spread which is committed but unfunded because requiring additional capital for future excess spread would be inconsistent with the clear statements in the CRR that banks should not be required to hold capital against future expected income.

d. As discussed above, if the EBA ultimately determines that the use of excess spread should affect the level of SRT recognition, consideration should be given to the capital double counting penalty discussed above.

11. Do you agree with the proposed safeguards constraining the use of excess spread in synthetic securitisation? In particular, do you agree with:

a. The proposal of only allowing a contractually fixed (pre-determined) excess spread commitment in synthetic transactions?

The EBF does not see the point of specifying a contractually fixed or pre-determined amount of excess spread. This requirement is inconsistent with the treatment of excess spread in traditional securitisations. As discussed in b. below, we believe the use-it-or-lose-it method is equally valid and prudentially sound. Furthermore, if the concern being addressed by this proposal is related to a belief that the amount of excess spread in the reference portfolio in a synthetic deal is somehow more difficult to calculate, as the EBA stated in the public forum, we do not agree. See our answer in b. below for an explanation.

As long as an originator correctly captures the economic effect of using excess spread, whether via a fixed or variable amount or via a trapped or use-it-or-lose-it method, there is no prudential reason for restricting the use of excess spread in the way the EBA proposes.

b. **The proposal to only allow a 'trap' excess spread allocation mechanism in synthetic transactions?**

It is important to note that the use-it-or-lose-it mechanism achieves higher risk transfer than the trapping approach. In this context, the EBA preference for the latter one is not clearly understood.

If the Use- it- or- Lose it approach is acceptable for traditional securitisations, it should also be allowed for synthetics. The concerns cited by the EBA that this approach would not be available to cover back-loaded losses is mitigated by the self-assessment requirement where the originator has to demonstrate the adequacy of risk transfer in a back loaded scenario. The EBF can agree to use conservative assumptions about the availability of excess spread when modelling the economic rationale. But there is no sound justification for eliminating the use of the use- it- or- lose it approach.

We also understand that another objection of the EBA to the use-it-or-lose-it approach is a concern that calculating the true level of synthetic excess spread provided by a reference portfolio is somehow more difficult than in the case of traditional securitisations. We disagree with this conclusion. It is quite easy for originators to calculate the interest spread earned on a portfolio and to deduct premiums and other securitisation expenses and to apply a servicing fee equivalent to fees paid in traditional securitisations, in order to calculate and monitor the total level of synthetic excess spread. In addition, with the EBA proposal to limit the use quantum of synthetic excess spread to the EL of the portfolio, this concern is further mitigated and has the same prudential effect as the proposal to trap the equivalent of EL in an excess spread account.

12. **Do you agree with the proposed way to treat the excess spread commitment in synthetic securitisation transactions for the purposes of the quantitative assessment of SRT and commensurate risk transfer?**

First of all, it is noteworthy that if the originator uses a structure that traps excess spread, it is undeniable that the trapped excess spread must be weighted at 1250%.

With regard to the commensurate risk transfer question, it may seem reasonable to say that if excess spread absorbs any losses, the originator must reduce the level of capital reduction commensurately. However, we object to this approach,: this since it is inconsistent with the CRR treatment of future income on loan portfolios. The CRR explicitly confirms that there is no need to hold capital against the possible reduction of future spread on a portfolio. There is even guidance that if an originator sells a portfolio at a gain, but does not recognise the gain upfront, neither does it have to recognise any capital or other liability against the gain.

The principle is the same in a securitisation:

a. If an originator does not recognise as income any excess spread received from a securitisation SPV at the bottom of the waterfall until it actually receives the cash, and similarly does not recognise excess spread committed as credit enhancement to a synthetic transaction, there should not be any need to recognise any liability (capital or otherwise) against that expected future excess spread stream that will absorb losses.
b. It does make sense to recognise the opportunity cost of reduced future income caused by including excess spread (i.e because of the quantum of losses which are expected to be absorbed by excess spread). As discussed above, to the extent excess spread is used to absorb losses, the originator should factor this use of excess spread into the cost of the transaction, by demonstrating that the originator has obtained a lower cost of protection from investors to off-set the reduction in the benefit of losses avoided provided by the transaction.

The above points are crucial since if they are not recognised by EBA, it would create inconsistencies with the way future excess spread is treated under the CRR for un-securitised loan portfolios and entail a double capital counting penalty such as explained previously.

13. In relation to the further considerations for stakeholders' consultation on the own funds treatment of excess spread:

a. Do you agree that the unrealised/unfunded component of the excess spread commitment should become subject to Pillar I own funds requirements?

The EBF strongly opposes the possibility to apply Pillar 1 own funds requirements to the unrealised/unfunded component of the excess spread commitment as explained in previous answers.

b. What would be the impact on SRT transactions if Pillar I own funds requirements were recognised as suggested in Section 3.2?

As described above, SRT recognition would be significantly reduced, thereby reducing the efficiency of SRT deals, increasing the costs of protection to unacceptable levels (as further described below) and potentially subjecting originators to contradictory regulations by raising costs in such a way that originators violate the cost of protection restrictions. This is because any reduction in RWA/capital benefit of a transaction means that the cost of premiums increases as a percent of RWA/capital released. This proposal will therefor undermine the intent of the SRT guidance to promote the risk transfer benefits of securitisation by further depressing the market for securitisation, including corporate/SME exposures.

14. Are there any other safeguards or alternative regulatory treatments to address risks retained through excess spread in traditional and synthetic securitisation?

As described above, the amount of excess spread which is used to absorb losses before touching the tranches should be recognised as a cost of the transaction, and this cost should then be justified by the originator in its self-assessment and with regard to the cost of protection restrictions. It is absolutely not justified to require to recognise excess spread as an additional securitisation position unless it is trapped. The self-assessment should be considered as an adequate and appropriate safeguard to prevent the abuse of the SRT regulations.

15. Should there be a specific treatment in those transactions featuring excess spread in which the originator, instead of achieving SRT in accordance with one of the SRT tests specified in the CRR, chooses to deduct all retained securitisation positions from CET 1 or apply a risk weight of 1250% to all of such securitization positions ('full deduction option'), in order to be allowed to exclude the securitised exposures from the calculation of risk-weighted exposure amounts?

As the EBF disagrees with the recognition of unrealized excess spread as a securitisation position, the EBF also disagrees with recognising it in this situation, since the originator has already effectively reserved sufficient capital to cover even a 100% loss scenario.

16. What are your views on the use of originator's bankruptcy as an early termination clause? How does this clause interact with the resolution regime (i.e. the BRRD framework)? Should this clause be banned?

The EBF is of the opinion that what works best is to make sure that the credit protection remains enforceable as long as the originator does not default on the payment of the premium. In this sense, we are in favour of the possibility of excluding originator bankruptcy as an early termination event, as long as the originator continues to fulfil its premium or interest payment obligations and all its other reporting and servicing obligations under the contract subject to the caveat that this termination event can only be excluded if investors are protected from the counterparty risk caused by depositing the protection tranche funds with the originator. This can be accomplished by:

a. Allowing the investment of cash proceeds in eligible investments held at an independent custodian. According to the latest EBA guidance, this structure would be prohibited for STS SME synthetics and presumably other asset classes if STS benefits are extended to other synthetics.

b. Allowing the cash deposited with an originator to be segregated from the bankruptcy estate of the originator through deposits in a bankruptcy remote custodian account, investments in eligible investments, repos and other similar structures.
c. Downgrade triggers which require the movement of deposited funds to another bank or investment in eligible collateral. The EBA should clarify that such clauses are not problematic for SRT, and that movements of funds due to such clauses would not cause the loss of STS status of a deal.

In some rated synthetic securitisations of certain asset classes, removing termination in case of originator bankruptcy could have a material impact on rated transactions, as ratings are generally dependent on servicing continuity. This would also be a concern for investors. For example, the performance of larger concentrated assets such as commercial real estate or certain commercial loans, including SMEs, may be highly correlated to the financial health of the originator, for instance, to the extent servicing staff were made redundant. Accordingly any ban on termination clauses involving originator bankruptcy must take these concerns into account. Investors would have to be given the right to terminate in a bankruptcy situation to the extent that servicing arrangements (and indeed investor reporting obligations) were not carried out satisfactorily.

17. Do you agree with the proposed originator's self-assessment of risk transfer? Should such assessment be formulated differently?

- Banks already provide self-assessment justifications for their deals. In fact, the EBA has basically codified what banks already do.
- It would be helpful for the EBA to give guidance on what would be considered an appropriate back-loaded scenario in order to assure consistent application of this rule across jurisdictions
- It is helpful that the EBA has specified that the stress scenario requested should be based on the official regulatory stress test levels if applicable and available. Some flexibility should be provided for where, for example, as Basel stress scenario is more applicable or indeed an ICAAP scenario which is at the core of the Originators wider risk management frameworks and most appropriate to their assets.
- Other guidelines on the type of items originators must take into account in their self-assessment would be helpful in order to promote consistent reviews of transactions across jurisdictions.
- A fully detailed self-assessment is not always necessary, especially for subsequent series of transactions using the same structure as previously approved transactions.
- The proposed tests in Paragraphs 165-169 in many cases lack the required detail and worked-out examples to assess whether they can/will achieve an insightful self-assessment (e.g.: para 165 appears to be comparing % values to monetary values; para 167 uses a subjective word "complex" and is not clear about the purpose or function of a Monte Carlo model.

18. Are you aware of circumstances where institutions have entered into a structured risk transfer transaction which is not captured by Articles 243 or 244 CRR? For example, where the accounting treatment has meant a transaction is not considered for SRT assessment, or where transactions economically similar to SRT transactions do not fall into the definition of a 'traditional securitisation' or 'synthetic securitisation'.

The EBF is not aware of any such transactions.

Part 5: Assessment and options suggested by EBA with respect to the quantitative SRT tests

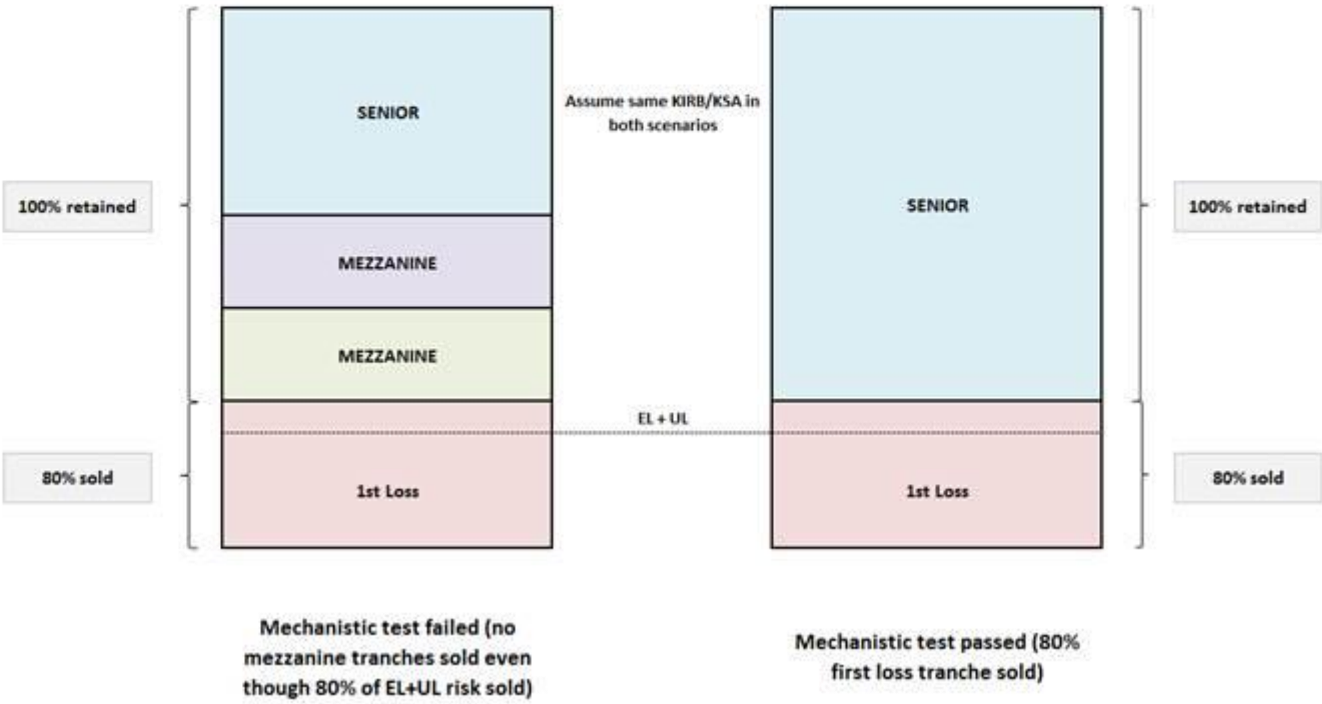
19. Do you agree with the proposed specification of the minimum first loss tranche thickness for the purpose of the first loss test?

The EBF agrees that a test for minimum thickness of protection tranches is appropriate.

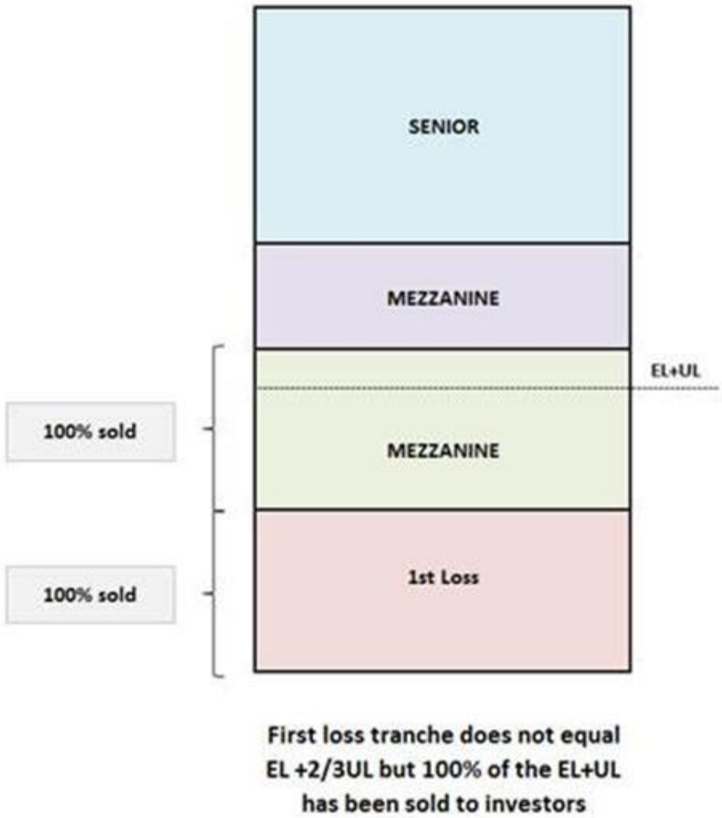
Having said that, quantitative tests on the tranches' thickness should be verified only at inception, where they can be a useful tool for the Originator for determining a tranching that can work over the life of the transaction. An ongoing check of the tranches' thickness doesn't work in our opinion as: i) the tranching cannot be adjusted on an ongoing basis to assure continued compliance with the test; ii) the thickness could be reduced over the life of the transaction due to loss absorption, but this is to be expected and would have been considered in the Originator's original self-assessment. Please consider that the thickness features are in any case captured in tranches' risk-weight calculation (and cap test).

Moreover, the current mechanistic tests show an anomaly that EBA must correct in order to avoid unjustifiably discarding the achievement of SRT for viable securitisation transactions:

1. In the first illustration below, 80% of the EL and UL risk is sold to investors, which meets the substantive requirements of the EBA guidance. However, in the first example (left hand side), the senior retained tranche has been divided into senior and mezzanine tranches (which is the most efficient structure under the SEC-ERBA and SEC-SA approach). Because the mechanistic test states that if mezzanine tranches are present, the originator must sell >50% of the risk weight of the mezzanine tranches, the mechanistic test fails. Nevertheless, in the second example (right hand side) where no mezzanine tranches are present, the first loss test is passed. The first example fails, even though substantively the same amount of risk (which exceeds EL & UL) has been transferred to investors. We believe this is an unintended consequence of the mechanistic tests which should be corrected, if the rest of the EBA guidance is ultimately agreed requiring that a significant portion of the EL and UL risk has been transferred.



2. The minimum first loss test requiring that the first loss tranche cover 100% of EL and 2/3 of UL should be modified to take into account a scenario such as the one illustrated below. In this graph, we see that the originator has transferred 100% of the EL and UL to investors. The first loss tranche does not meet the first loss test, but in substance, the combination of the mezzanine and first loss tranches sold is sufficient to transfer 100% of EL and 2/3 of UL. If not worded correctly, the first loss tranche would inadvertently disallow the illustrated transaction.



3. The revised definition of mezzanine tranches, which excludes mezzanine tranches weighted 1250% exacerbates the problem described above. Under the newly adopted capital calibrations, it is likely that many mezzanine tranches will be weighted 1250% (such as in the case of IRB consumer loans in which the SEC-IRBA approach does not recognise the benefit of excess spread). Accordingly, in the above example, if the most subordinate mezzanine tranche is weighted 1250%, the mezzanine test would fail, even though the originator has transferred risk equal to EL + 2/3 UL.

20. Do you agree with the proposed requirement of the minimum first loss thickness for the transactions assessed under the mezzanine test (i.e. transactions including mezzanine securitisation positions)? Do you consider this requirement relevant for all the approaches for calculation of securitisation own funds requirements (including e.g. SEC-ERBA)?

In principle, we agree with the substance of the test, which we understand is trying to prevent abuses of the test observed by the EBA. However the structure of the test has an unintended negative consequence, as further explained below.
Accordingly the test should be restated or clarified to take into account transactions in which a sufficiently large portion of mezzanine risk is sold to cover UL, and where the

attachment point of the sold mezzanine tranches encompasses the portion of EL not covered by a thin first loss tranche. In most cases we find that the optimal cost of protection and RWA reduction can be achieved if we retain a small first loss tranche, while transferring a sufficient amount of mezzanine tranches to cover the rest of EL and most of UL. To prevent the abuse that this test is intended to cover, the EBA could specify that the mezzanine test will not cause a transaction to fail the minimum required for SRT if the originator transfers any combination of first and mezzanine tranches with a thickness equal to EL + 2/3 UL. Another alternative would be to require banks using the mezzanine test to sell a greater percentage of mezzanine tranches than 50%, such that the percentage sold above 50% equals the amount of EL not covered by the first loss tranche.

21. Is a specification needed of the minimum thickness of tranches constituting mezzanine securitisation positions for the purpose of the mezzanine test?

The EBF believes that this kind of specifications is probably not needed. Originators who create structures to obtain capital relief, and therefore to pass the SRT test, are automatically dis-incentivised to structure too thin equity or mezzanine tranches because otherwise the senior tranches, usually fully or partially retained, would be penalized.

Moreover, the formula-based approach should suffice.
First of all, it is important to calibrate the test in such a way that the mezzanine tranches all together must be sized to cover the UL assuming that the first loss tranche already cover the EL. It should be avoided to require that one single mezzanine tranche has a minimum thickness, this would be too restrictive and unjustified.
In addition, the requirement should provide flexibility enough to allow varieties of tranche structures and percentages of tranches sold (subject to the minimum 80% first loss and 50% mezzanine tests) as long as the combination of tranches sold transfer an equivalent amount of risk as required by these tests. For example, an originator should be able to sell 100% of mezzanine risk and, say, 50% of first loss risk, as long as the total risk sold is equivalent to either 80% of the first loss risk (EL) or 50% of the mezzanine risk (UL).
All the issues raised in question 19 should be taken into consideration.

22. What impact do you expect the new CRR securitisation framework to have on tranches' minimum thickness?

EBA rules should be consistent with Basel and not impose a minimum size for the first loss tranche.

With respect to the new CRR securitisation framework, senior risk weights tend to increase dramatically whereas mezzanine risk weights tend to be rather stable and first loss tranches remain to be deducted/with 1250% risk weight. EL and provisioning of the underlying portfolio remain unchanged.

From the originator's perspective, the focus is to achieve economically efficient SRT. With senior risk weights being most impacted from the new regulation, originators might tend to structure senior tranches in a way to keep risk weights on retained senior positions as low as possible. This will likely be achieved by higher amounts of subordinated tranche notional (incl. Excess Spread). In this respect, we rather expect senior tranche sizes to shrink and mezzanine as well as first loss tranche sizes (incl. Excess Spread) being increased. However, a more likely effect in most cases is that banks will cease to do SRT deals because it is likely that the incremental cost of selling additional tranches makes the transaction uneconomic compared to the bank's cost of capital, and the sale of such additional tranches might cause the bank to fail the high cost of credit protection rules as proposed by the EBA.

From the investor's perspective, the focus is to take on an investment with an attractive risk/reward profile. Assuming the investor is not regulated under the CRR, the new regulation is not key in the assessment of risks and rewards. The focus is rather on (economic) expected and unexpected losses of the underlying portfolio in order to assess the riskiness of the investment. We expect the impact of the new CRR regulation on the investor´s minimum tranche thickness requirements to be marginal. However, those investors most interested in first and second loss tranches have yield requirements higher than the weighted average cost of protection required by originators for a deal to make economic sense. If the above-mentioned anomaly in the first loss and mezzanine tranches is not corrected, it will be difficult, if not impossible, for originators to sell a thick enough portion of tranches at an economic level.
For example, under the new CRR and commensurate risk rules, we may determine that it is necessary to sell a position with a zero attachment point and a 12% detachment point in order to demonstrate SRT and commensurate risk transfer, which is greater than the zero to 8% tranche thickness that originators would need to sell to meet the same tests under the current CRR. It is likely easier and less costly to divide such position into three tranches; a first loss and two mezzanine tranches, because originators can sell to different investors with different return requirements. The first loss investor may need for example 12%, while the senior mezzanine investor may only require for example 4%. On a weighted average basis, the total cost of selling these three tranches may be for example 8%. However, if originators cannot meet the mezzanine test in this example, they will be forced to structure one single first loss tranche with a zero attachment and 12% detachment point. It is unlikely that originators will find an investor willing to accept an 8% return for such a tranche, and originators may be forced to pay, for example, 9% or 10%.

23. Do you have any comments on the test of commensurate risk transfer proposed under Option 1?

In analyzing the impact of these tests on banks existing SRT positions, we note the following problems:

1. In many cases the new definition of mezzanine, excluding mezzanine tranches which are risk weighted 1250% causes the deal to fail the mezzanine test, even in deals which have transferred tranches equal to EL+2/3UL. The likelihood of mezzanine tranches being risk weighted 1250% is much greater under the new CRR approaches.
2. As per our responses to questions 19, 20 and 21 above, the minimum first loss tranche thickness test inadvertently causes several of our transactions to fail, even though we have transferred a total amount of tranches exceeding EL+2/3UL

The EBF would like to mention another inconsistency that particularly seems to occur to synthetic transactions which are structured to pass the mezzanine test and where the originator is obliged to apply SEC-IRBA.

In case the first loss tranche plus excess spread are retained by the originator we acknowledge the introduction of the minimum First Loss FLP thickness test as a helpful measure to ensure that the lifetime EL of a portfolio is covered by the originator whereas its UL is transferred. Given this intention, we lack transparency why the lifetime EL is considered in ratio 2 of the commensurate risk transfer test. In fact, sections 216 and 218 reveal that ratio 2 of aims at measuring "the risk transferred to the third parties" obtained "as the share of losses transferred to third parties for the life of the transaction". We understand that the commensurateness test is not solely directed towards transactions that intend to pass the mezzanine SRT test. However, it is our understanding that the test of commensurate risk transfer contradicts the minimum tranche thickness test particularly in case the mezzanine SRT test applies. This is due to the fact that the latter requires the lifetime EL not to be part of the transferred risk whereas the commensurateness test considers it to be transferred.
Furthermore, the reason why the commensurateness risk transfer test compares a 1y measure[1], ratio 1, with a lifetime measure, ratio 2 is not clear. Even though it is clear why the test is comparing capital savings to transferred risk, it remains questionable to actually base the compared figures on different time horizons.

Also it seems that Ratio 2 takes into account the lifetime excess spread: if the excess spread is committed and trapped, it should be considered as a retained position; – however as detailed in earlier questions, unearned excess spread and un-trapped excess spread should not be considered as a retained position.

24. Do you have any comments on the test of SRT and commensurate risk transfer proposed under Option 2? In particular, is the 50% threshold for SRT therein needed and appropriate?

See comments in question 23 above. In principle, if the EBF accepts this type of test, it should not matter whether the originator sells 20% of the risk or 100% of the risk, since the RWA reduction achieved will be commensurate with the risk transferred.

The significant risk transfer and the commensurate risk transfer should be tested separately as in the proposed option 1. Although the Option 1 seems less effective than Option 2, an EU-wide impact assessment should be conducted to determine the proper threshold. The Option 2 comprehensive test, in some cases involving the SEC-ERBA or SEC-SA approaches could produce misleading results, as the non-neutrality factor built into the risk weighting of senior and mezzanine tranches makes this test difficult to pass without creating uneconomic results for the originator (see discussion below)
Furthermore, the Option 1 and 2 tests may give divergent results, as there can be cases where the minimum thickness of the junior tranche determined with the first loss test (that is, Lifetime EL+ 2/3 UL, for a deal without a mezzanine tranche), doesn't allow the New Comprehensive test (Option 2) to be satisfied.

[1] We believe that ratio 1 is a 1y measure due to the fact that there is a different outcome with respect to i) a structure with a first loss piece being equal to the lifetime EL versus ii) a structure with a first loss piece being equal to the 1y EL where synthetic excess spread in the amount of the 1y EL is posted during the lifetime of the transaction on an annual basis. We understand that in contrast to our understanding, ratio 1 incorporates tranche maturities in SEC-IRBA, which are figures that can go beyond the 1y time horizon.

In addition, it is important to note that for synthetic securitisations where synthetic excess spread of the amount of the EL is trapped on an annual basis, the 1st Excess Spread payment that is trapped towards the end of the 1st year should not be considered in the calculation of Condition 1 since it serves to buffer the EL of the underlying portfolio that materializes during the 2nd year of the transaction.
In analyzing the impact of this test on banks existing SRT positions, we note that, in many cases, the increased capital on senior retained tranches required by the new capital calibrations under the revised CRR causes our SRT transactions to fail, even though the positions sold to investors exceed EL+2/3UL, which is the minimum suggested by the EBA. The effect of the new CRR calibrations is to require an originator to sell a much larger portion of first loss and/or mezzanine tranches in order to reduce the risk weighting of the senior retained tranches below the threshold required by the test. This is particularly the case for transactions involving standardized assets. For any particular transaction, some or all of the following negative impacts then may apply:

1. It increases the cost of protection above the bank's cost of capital, making the deal uneconomic to execute.
2. It causes the total cost of protection to exceed the EBA guidelines on the cost of credit protection.
3. It requires the originator to sell total tranche thicknesses far in excess of EL+2/3UL, which makes such test redundant.

In analyzing the impact of this test on banks' existing SRT positions, we note that, in many cases, the increased capital on senior retained tranches required by the new capital calibrations under the revised CRR causes our SRT transactions to fail, even though the positions sold to investors exceed EBA's suggested thresholds.

25. Should the SRT test be different depending on asset classes? Should it differ across STS and non-STS transactions?

The EBF would like to mention that it is not necessary to vary the test according to asset classes, but instead:
There should be a differentiation in the test according to the capital approach an originator is required/chooses to use, in order to take into account:

The double capital penalty inherent in the SEC-IRBA and SEC-SA approaches for non-auto transactions with high excess spread portfolios, which distort the capital weighting of the tranches, which results in a need to sell a greater number or portion of tranches than is necessary to cover EL and UL.

26. Could you provide, on the basis of SRT transactions that are part of your securitisation business, an assessment of the impact in terms of SRT achievement of the proposed requirements under both Option 1 and Option 2, taking into account the new CRR securitisation framework (Securitisation Regulation package)?

Several of our members conducted a review of several of their transactions, a number of which failed either the Option 1 or Option 2 tests for reasons discussed in questions 23 and 24.

Several of our members have submitted their examples directly to the EBA.

Part 6: The regulatory treatment of NPL securitisation

27. Do you agree with the assessment of the market practice of NPL transfer? Are there material aspects that are not covered in this representation?

In general terms, the EBF agrees with the EBA assessment of market practices of NPL transfer. In addition to this assessment, it is important to note that the main reason behind the scarcity of NPL securitisations is the wide bid-ask price, which is in part caused by the costs of NPL resolution from the investor perspective. Factors such as the collateral costs, the NPL management costs and the judicial costs are influenced by divergent national regulation, and should be harmonised in the EU. Another key issue for banks is their ability to derecognize the assets, which is often complicated by that the originating bank keeping some form of control over the assets (e.g. as servicer) even after they have been transferred to the acquirer.

28. What conditions/initiatives would, in your view, facilitate the well-functioning of the NPL securitisation market?

In order to boost the securitisation of NPLs, one of the things that can help would consist in providing public guarantees targeting more junior risk (even 50% of the junior tranche as the ECB has proposed) in order to boost demand.

The secondary market in NPLs could also be further developed if certain obstacles are removed, such as:

- Barriers to entry for NPL investors: for example, some EU jurisdictions require loan servicers to hold a license. This is a barrier to entry for entities that would otherwise be interested in becoming investors in NPLs.
- Limitations in the transferability of loans: Banks are often unable to sell loans containing restrictions on transfer/assignability of the loan. Policymakers could

(at the national level) make such clauses unenforceable by operation of law once the loan ceases to perform.

- Disclosure limitations: in some jurisdictions, banks are not permitted to make disclosures to potential acquirers of loans for which a mandate or a conciliation procedure is underway. This makes it difficult or impossible for banks to provide acquirers with the necessary disclosure in order to perform appropriate due diligence on the portfolio. Therefore, the bank cannot give the relevant representations, warranties and disclosure required by a potential reasonable acquirer.

29. Which, in your view, are the core structural features that should be assessed within the SRT assessment of NPL securitisation transactions? Are the proposals on selected structural features of securitisation transactions proposed in this document (see Section 3.2.2) equally valid for NPL securitisation transactions?

Regarding the securitisation of NPLs, the EBF understands that the proposed framework is also appropriate.
We would add however that the alignment of interests between the servicer and the investors is specific to NPLs.

30. Do you agree with the proposed way of implementing the SEC-IRBA and SEC-SA approaches for the calculation of securitisation tranche capital in the presence of a non-refundable purchase price discount? Do you envisage other ways to implement the mentioned approaches in the presence of a non-refundable purchase price discount?

The EBF agrees with the way of implementing the SEC-IRBA. We note that this method should be generalized to cases where there is a non-refundable purchase discount irrespective of the type of underlying assets, i.e. not just used for NPL securitisation.

We note as well that there is a wide discrepancy in this case between the results of the SEC-IRBA and the SEC-SA. De facto for NPL pools, due to the computation of KS_A which is based on 100% of delinquent exposures, the SEC-SA results are so conservative that the SEC-SA cannot be used by market participants as it would make transactions unprofitable. This is quite detrimental for the development of the NPL securitisation market or the securitisation market of pools with material delinquency buckets. In our view this unfairly discriminates against standard banks.

The over conservatism of the SEC-SA for NPL pools stems in our view from the way the W factor is taken into account in the SEC-SA. This issue is not specific to NPL but it is amplified in the case of NPL pools. It was already identified with a simple correction proposed in a paper called: "How to revive the European Securitisation

Market: a Proposal for a European SSFA" by Georges Duponcheele and al published in November 2014. Indeed the paper mentions: "It is to be noted that this official version of the SA in the BCBS 269 proposals contains a conceptual error in that it includes the delinquent assets (via KA) in KP. This in effect means that the capital associated with provisions for the delinquent assets is allocated to the senior tranches via the exponential function and the parameter a. To correct this conceptual error, KP should simply equal pool capital for performing loans and should not be a function of W. The delinquent assets should only affect the 100% capital charge threshold KT. It is important to distinguish between KT and KP to avoid making errors." We therefore reiterate the need to correct the way the W factor is taken into account in the SEC-SA as detailed in the extract above.

31. Do the SRT quantitative tests provided for in the CRR currently in force (Articles 243 and 244 of the CRR) work properly for NPL securitisation transactions? If not, please provide an explanation to your answer.

We think that clarification of the EBA is required on how the non-refundable purchase discount would be taken into account for SRT quantitative test purposes. This would be necessary not just for NPL but also for other cases where there is a non-refundable purchase discount.

32. How should the alternative commensurate risk transfer proposed in this report be modified to address the specificities of NPL securitisation transactions?

Same answer as question 31 (EBA 31)

33. How should the quantitative test proposed under Option 2 in this report (see Section 3.3.2) be modified to address the specificities of NPL securitisation transactions?

Same answer as question 31 (EBA 31)

Summary of key points:

- The EBF supports the EBA proposals that aim at **enhancing the process of the SRT assessment** and would like to highlight the importance of ensuring that banks receive feedback from the competent regulatory authority ahead of the closing of the transaction.
- The EBF is opposed to a **possible retrospective application** of the legal framework that would arise from these discussions on SRT in securitisation. In addition, EBA should clarify that any retrospective application of the forthcoming legal framework is discarded to minimize uncertainty.
- **Excess spread** which is not funded or "trapped" in either traditional or synthetic securitisations should **in no case be considered as a securitisation position** and subject to Pillar 1 own fund requirements,
- It is important to provide enough flexibility to use **other alternative amortisation structures** than pro-rata amortisation.
- The proposal that requires that **time calls in synthetic securitisations** can only be exercised later than weighted average life plus replenishment period **puts a significant penalty** on the transactions.
- The EBF strongly opposes the **prohibition of time calls in traditional securitisations**.
- The **use-it-or-lose-it approach must be allowed** for both traditional and synthetic securitisations.
- The use of the originator's **bankruptcy as an early termination clause** should not be automatically banned.
- **The design of the new proposed tests is somehow flawed** and should be corrected to avoid discarding the achievement of SRT for operations that show viable features to achieve it.
- The EBF agrees with the EBA's recommendation to take into account the **purchase price discount** in calculating the attachment points of retained tranches. We believe the **same principle should apply to securitisations of non-NPL assets** which the originator may have acquired at a discount.

About EBF

The European Banking Federation is the voice of the European banking sector, uniting 32 national banking associations in Europe that together represent some 4,500 banks - large and small, wholesale and retail, local and international - employing about 2.1 million people. EBF members represent banks that make available loans to the European economy in excess of €20 trillion and that securely handle more than 300 million payment transactions per day. Launched in 1960, the EBF is committed to creating a single market for financial services in the European Union and to supporting policies that foster economic growth.

www.ebf.eu @EBFeu

For more information contact:

Saïf Chaïbi
Policy Adviser
s.chaibi@ebf.eu
+32 2 508 37 23