German Banking Industry Committee

Die Deutsche Kreditwirtschaft

Comments on

STS guidelines

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STS criteria on ABCP securitisations

True sale, assignment or transfer with the same legal effect (Article 24(1), 24(2), 24(3), 24(4) and 24(5))

Q1: Do you agree with the interpretation of these criteria, and the aspects that the interpretation is focused on? Should interpretation be amended, further clarified or additional aspects be covered? Please substantiate your reasoning.

Para 13 states that the contents of the legal opinion should be accessible to third parties. The term “third parties” should be specified in more detail. Where ABCP transactions are concerned, we believe third parties should refer only to competent authorities and parties which are directly exposed to the risk associated with the pool of underlying exposures. By contrast, commercial paper investors and potential investors are protected by the “fully supported” liquidity facilities and do not, therefore, require any additional information about the true sale.

Q3: Do you believe that in addition to the guidance provided, additional guidance should be provided on the application of Article 24(2)? If yes, please provide suggestions of such severe clawback provisions to be included in the guidance.

The legal opinion should cover only the legally effective transfer of assets. It should only address risks which could impair the transfer. These are essentially clawback risks and re-characterisation risks. Commingling risks and set-off risks, on the other hand, are risks which have no direct link with the transfer of the assets, but which may exist independently of the transfer. These risks are not normally the subject of a true sale opinion, nor are they addressed by Article 20(1) or 24(1) of the STS Regulation (“…transfer of the title…”). The phrase “commingling risks and set-off risks” should therefore be dropped from para 10b.

Representations and warranties (Art 24(6)):

Q5: Do you agree with the interpretation of this criterion, and the aspects that the interpretation is focused on? Should interpretation be amended, further clarified or additional aspects be covered? Please substantiate your reasoning.

Our view is similar to that expressed in our reply to Q1. Here, too, we believe the representations and warranties should be provided only to parties directly exposed to the underlying portfolio. In para 16, the term “investors” should therefore be replaced with “parties directly holding a securitisation position at the level of the respective ABCP transaction”.

No exposures in default and to credit-impaired debtors/guarantors (Article 24(9))

Q8: Do you agree with the interpretation of this criterion, and the aspects that the interpretation is focused on? Should interpretation be amended, further clarified or additional aspects be covered? Please substantiate your reasoning.

The “best knowledge” requirement should only cover publicly available information if it was known to, and processed by, the originator. In our view, the broad wording at the end of para 29 (“including publicly available information”) runs counter to the view in para 26 that application of the guidance should not be “unduly burdensome” and the statement in para 30 that compliance “should not require the originator […] to take other steps in order to collect further information […] beyond the information referred to in Recital 26”. The phrase “including publicly available information” at the end of para 29 should therefore be deleted or reworded much more narrowly.

Q9: Do you agree with the interpretation of the criterion with respect to exposures to a credit impaired debtor or guarantor?

Please see our reply to Q8.

Q10: Do you agree with the interpretation of the criterion with respect to the exposures to credit-impaired debtors or guarantors that have undergone a debt-restructuring process?

Para 28 proposes that, if a portfolio or asset is guaranteed, “neither the debtor, nor the guarantor” should be credit-impaired. This is inappropriate and does not reflect common practice, in our view. If a debtor is credit-impaired, it is advantageous to have a guarantor in place to assume credit risk. It is then the credit status of the latter which is relevant. A portfolio or a single asset should only be deemed credit-impaired within the meaning of Article 24(9) of the STS Regulation if both the debtor and the guarantor are credit-impaired (i.e. the requirement should be cumulative). Take, for instance, widespread practice of securitising trade exposures which are fully covered by trade credit insurance. It should be of no importance whether or not the debtor has an impaired credit history since everything is covered by the trade credit insurance. There should be no need to investigate the credit history or current credit status of the originator. Para 28 should be amended accordingly.

No predominant dependence on the sale of assets (Article 24(11))

Q12: Do you agree with the interpretation of this criterion, and the aspects that the interpretation is focused on? Should interpretation be amended, further clarified or additional aspects be covered? Please substantiate your reasoning.

Para 41 proposes that the exemption in the event that there is a guarantor for the residual value should apply only if this guarantor is an eligible protection provider in accordance with Article 201(1) of the CRR and Article 24 of the revised CRR. For companies, this means there has to be an external or (for banks using the IRB approach) an internal rating.

This requirement raises the question of who needs to have an internal rating. The end of para 41 merely requires “such third party” to be “an eligible provider of unfunded credit protection in accordance with

[the IRB approach]". In our view, however, it is not clear which party has to comply with this IRB approach. Both level 1 and the beginning of para 41 refer to "holders of securitisation positions". These holders could be the sponsoring bank, one or more parties to a swap or banks investing in the ABCP. It would be logical for the sponsoring bank only to be meant, since it is the provider of full support. But if the term refers to other parties as well, differing conclusions would be arrived at. It would be equally impracticable to require guarantor companies always to have an external rating in the event of such differing conclusions. This would have severely adverse effects on the securitisation of car and equipment leasing exposures with a residual value. We would suggest either deleting para 41 altogether or clarifying that the requirements only have to be met by the sponsoring bank and adding as a further criterion (in addition to an external or internal rating) that it is possible to include the guarantor in the IAA rating of the sponsor.

To explain: under Article 265(2)(m) of the new CRR, the internal assessment approach may only be applied if all potential risks are taken into account. In consequence, a guarantor of the residual value may also be included in the risk assessment under the IAA. If this is the case, the guarantor should not need to have an external or internal rating as well.

[No resecuritisation at ABCP transaction level (Article 24(8))

Q12 on page 37 of consultation paper:
Do you agree with the interpretation of this requirement, and the aspects that the interpretation is focused on? Should other aspects be covered? Please substantiate your reasoning.

We agree with the interpretation and welcome the illustrative diagrams. It would be helpful for clarification purposes if the "additional CE" shown in Figure 1 in para 23 was granted not only by the sponsor, but also by a third party. This frequently occurs when trade exposures are securitised and the portfolio sold is insured by trade credit insurance in the form of a CE policy. This could perhaps be mentioned in the diagram as an additional example alongside the letter of credit (please see also our reply to Q31).]

Remedies and actions related to delinquency and default of debtor (Article 24(13))

Q15: Do you agree with the interpretation of this criterion, and the aspects that the interpretation is focused on? Should interpretation be amended, further clarified or additional aspects be covered? Please substantiate your reasoning.

We basically welcome the proposed reporting obligation in the event of changes in the waterfall of payment priorities. We nevertheless see room for improvement in the wording of para 49. As a rule, ABCP transactions and programmes have two "waterfalls": one at transaction and another at programme level. In consequence, there are also two different securitisation positions. While a change in the waterfall at transaction level, for example, may materially affect the parties directly involved (and thus trigger a reporting obligation), this may, by contrast, have no material effect on the repayment at programme level (owing to the full support, among other things). We would therefore recommend clarifying in para 49 parties holding a direct securitisation position, on the one hand, and investors, on the other, should be informed only if there will be a material effect on the repayment of their position. The current wording suggests both parties always need to be informed.

Data on historical default and loss performance (Article 24(14))

Q16: Do you agree with the interpretation of this criterion, and the aspects that the interpretation is focused on? Should interpretation be amended, further clarified or additional aspects be covered? Please substantiate your reasoning.

We warmly welcome the clarification in para 51 that disclosure should only be mandatory to investors which are directly exposed to the transaction portfolio and that, in other cases, confidentiality issues may be taken into account. It should nevertheless be borne in mind that, where certain asset classes are concerned (especially trade exposures), only dynamic loss and default data are available. Owing to the short-term nature of these exposures, it is neither feasible nor helpful to compile static data. Para 51 should therefore not be understood as meaning that it is always mandatory to provide both static and dynamic data but should mean that at least one of these types of data should be provided, depending on availability.

It is also unclear how frequently a comparison has to be made between exposures in revolving portfolios (e.g. trade exposures) and substantially similar exposures. Article 24(14) of the STS Regulation says “before pricing”. In ABCP programmes, the cost of funds is normally passed on to sellers once a month. It would be unreasonably burdensome if this meant that a monthly comparison had to be made between the exposures sold and substantially similar exposures. We would therefore recommend clarifying that, for ABCP programmes, “before pricing” refers only to the initial pricing of a transaction, i.e. the initial sale of the exposures.

Homogeneity, obligations of the underlying exposures, periodic payment streams, no transferable securities (Article 24(15))

Q18: Do you believe that additional guidance should be provided in these guidelines with respect to the homogeneity requirement, in addition to the requirements specified in the Delegated Regulation (EU) 2018/.... further specifying which underlying exposures are deemed homogeneous?

We see no need for additional guidance.

Following enforcement or delivery of an acceleration notice (Article 24(17))

Q20: Do you agree with the interpretation of this criterion, and the aspects that the interpretation is focused on? Should interpretation be amended, further clarified or additional aspects be covered? Please substantiate your reasoning.

Para 63 is not relevant to ABCP and can be deleted.

Underwriting standards, seller’s expertise (Article 24(18))

Comments STS **guidelines**

Q21: Do you agree with the interpretation of this criterion, and the aspects that the interpretation is focused on? Should interpretation be amended, further clarified or additional aspects be covered? Please substantiate your reasoning.

The definition of "material changes" in para 70b ("where they modify the information on the underwriting standards originally disclosed in the prospectus or made available in the initial offering document") cannot normally be applied to ABCP transactions since the underwriting standards of transactions are not contained in prospectuses or offering documents. It would be better to refer to "transaction documentation" in this context.

Q22: Do you agree with this balanced approach to the determination of the expertise of the seller? Do you believe that more rule-based set of requirements should be specified, or, instead, more principles-based criteria should be provided? Is the requirement of minimum of 5 years of professional experience appropriate and exercisable in practice?

The criteria for determining the expertise of the seller should basically mirror those for determining the expertise of the servicer (Article 26(8) of the STS Regulation). Please also see our reply to Q34.

Q23: Should alternative interpretation of the "similar exposures" be provided, such as, for example, referencing the eligibility criteria (per Article 24(7)) that are applied to select the underlying exposures? Similar exposure under Article 24(18) could thus be defined as an exposure that would qualify for the portfolio, based on the exposure level eligibility criteria (not portfolio level criteria) which has not been selected for the pool and which was originated at the time of the securitised exposure (e.g. an exposure that has repaid / prepaid by the time of securitisation). Similar interpretation could be used for the term "exposures of a similar nature" under Article 24(18), and "substantially similar exposures" under Article 24(14). The eligibility criteria considered should take into account the timing of the comparison. Please provide explanations which approach would be more appropriate in providing clear and objectively determined interpretation of the "similarity" of exposures.

We would prefer "similarity" to refer to exposures with the same eligibility criteria. This would ensure that exposures which are really similar were compared with one another. The proposed referencing of portfolio level criteria would set too broad a standard for comparison, in our view. Receivables from equipment leases to corporates, for instance, would, under Article 2(d) of the draft RTS on homogeneity, have to be subject to the same underwriting standards regardless of whether they originated abroad or domestically. If, by contrast, a securitised portfolio only permitted domestic lessees, the non-securitised (foreign) portfolio would have to be originated on the same conditions. This is often not the case. Underwriting standards can also differ according to the type of object leased. If only certain types of leased object are allowed in a securitised portfolio, the possibility cannot be ruled out that there will be divergences between the securitised and non-securitised portfolio or at portfolio level in general.

Transaction documentation (Article 24(20))

Q25: Do you agree with the interpretation of this criterion, and the aspects that the interpretation is focused on? Should interpretation be amended, further clarified or additional aspects be covered? Please substantiate your reasoning.

It is not clear how transaction documentation is supposed to be disclosed to commercial paper investors (para 77). Anonymised, aggregated and summarised documentation will not provide commercial paper investors with any benefit or additional insight. These investors can obtain sufficient information about the securitised transaction portfolios from the monthly investor reports. In addition, they largely enjoy the full support of the liquidity facility. In our view, this covers, from the perspective of commercial paper investors, the requirement for "all underlying documentation that is essential for the understanding of the transaction" in accordance with Article 7(1)(b) of the STS Regulation. In contrast, Article 24(20) of the STS Regulation specifies only the content, not the addressees of transaction documentation. Para 77 can therefore be deleted, as we see it.

Para 78 requires (for the purposes of Article 24(20)(d) of the STS Regulation) that the transaction documentation include a reference to the fact that the sponsor has demonstrated its solvency and liquidity to the satisfaction of the competent authority. While we agree with the qualification in sentence two of para 78, we believe it would make better sense to include this reference to the demonstration of solvency and liquidity in a document made available to investors. We therefore see a need to clarify that this reference may also be included in a document which is not part of the transaction documentation (such as the investors report) as long it is accessible by commercial paper investors.

Temporary non-compliance (Article 26(1))

Q26: Do you agree with the interpretation of this criterion, and the aspects that the interpretation is focused on? Should interpretation be amended, further clarified or additional aspects be covered? Please substantiate your reasoning.

We agree with the method of calculating the extent of temporary non-compliance set out in para 79. As to the definition of "temporarily" in para 80, however, we believe the three-month period should begin on the day of notification of the non-compliance, not "from the first occurrence of non-compliance". A corresponding period and mechanism is prescribed for remedial measures in the third paragraph of Article 36(6) of the STS Regulation. We assume, moreover, that the three-month period applies separately to each infringement and will start again in the event of non-compliance occurring again.

Q27: Do you agree that the external verification should only cover the criteria referenced in paragraphs (9), (10) and (11) of Article 24, or should it cover all criteria mentioned in Article 24? Do you agree with the approach on determining the frequency of the external verification?

We understand Article 26(1) of the STS Regulation to mean that external verification should only be carried out if there has been notification of temporary non-compliance with Article 24(9) to (11) of the STS Regulation ("For the purpose of the second subparagraph…"). This external verification should then cover only the relevant transactions. This means that, if all requirements have been fulfilled at transaction level, there is no need for external verification at all (and the same applies if the programme has not been notified as having STS status). We would ask that these points be clearly spelled out since they are not made clear by the guidelines in their present form. We would also ask that para 83 be deleted. We believe this is justified because investors in a fully supported ABCP programme will not experience any material impairment of their securitisation positions as a result of temporary non-compliance with Article 24(9) to (11) of the STS Regulation. If, however, all transactions had to be examined on a regular

basis, this would impose a large cost burden on sellers without delivering any appreciable added value to commercial paper investors.

In the event of notification of temporary non-compliance, therefore, only the relevant transactions should be subject to a one-off external verification, as described above (para 84).

Q28: Concerning the sample, should a minimum sample size be prescribed (in absolute or relative terms)? Should a statistical method for evaluating the outcome of the external verification of the sample be specified? Do you agree that it should be representative covering all underlying exposures of all transactions? Do you see merit in further specifying that the sample should be representative by properly representing the various asset categories of the transactions; or that representativeness may be assumed when the sample is gathered via a random selection?

Please see our reply to Q27.

No resecuritisation (Article 26(4))

Q31 Do you agree with the interpretation of this criterion, and the aspects that the interpretation is focused on? Should interpretation be amended, further clarified or additional aspects be covered? Please substantiate your reasoning.

We agree with the guidance on this criterion. We merely recommend clarifying that trade credit insurance policies at transaction level (CE policies) are also not be understood as a second layer of tranching. Please see also our reply to Q12 above.

Q32: Are there any other market practices – apart from the ones being covered by the clarification provided in the guidance – which would also fall within the conditions of Article 26(4), while from an economical point of view those should not be treated as resecuritisations? Do you agree with the clarification of which credit enhancement is to be considered as “establishing a second layer of tranching”?

Please see our reply to Q31.

Expertise of the servicer (Article 26(8))

Q34: Do you agree with the interpretation of this criterion, and the aspects that the interpretation is focused on? Should interpretation be amended, further clarified or additional aspects be covered? Please substantiate your reasoning.

As explained in our reply to Q22, the expertise of the seller and the servicer should be assessed on the basis of the same criteria. This is the case.

As to the requirement in Article 26(8) of the STS Regulation for “well-documented policies, procedures and risk-management controls”, we see no need for non-regulated entities to have this documentation

demonstrated by a third party. This would generate substantial costs for sellers without delivering any appreciable added value to commercial paper investors, which already enjoy extensive protection owing to the full support. Only the sponsor has a commercial interest in making sure that these mechanisms are duly in place. We therefore believe it would be appropriate for the sponsor to verify this in its due diligence report. It should be left to the sponsor to decide whether to carry out the review itself or commission a third party to do so. Wording should therefore be added to the final sentence of para 102b to the effect that the review can be undertaken by a third-party or by the sponsor.

STS criteria on non-ABCP securitisation

General comments

We thank the EBA for the opportunity to comment on the consultation paper. At this stage, we have concentrated primarily on some key points which have come to the attention of our member banks. We assume that, in the course of implementing and applying the guidelines, further problems of interpretation and practical difficulties will arise. We therefore hope that after the end of the consultation period, competent authorities will support the implementation process by having arrangements in place which allow problems to be swiftly addressed and resolved. In our reply to Q35, for example, we suggest establishing a Q&A tool to enable future issues to be clarified with the least possible delay.

No exposures in default and to credit-impaired debtors/guarantors (Article 20(11))

Q14. Do you agree with the interpretation of the criterion with respect to exposures to a credit impaired debtor or guarantor?

Article 20(11)(b)
In our view, the guidance does not adequately explain precisely when an adverse credit history should be deemed to exist. This point is particularly important in countries which do not have a public credit registry listing only all debtors with a negative credit history. These countries normally have instead a non-public register containing both negative and positive information about clients. It will be especially problematic if the register does not specifically flag customers with a negative credit status. It is true that para 48 of the draft guidelines gives an example of a situation which should not qualify as an adverse credit history. But there are a great many other situations where it is questionable whether an adverse credit history should be considered to exist. How, for instance, should banks regard an order to pay which was issued one year before a loan is granted if there is no indication at the time of granting the loan that any payments are past due? If, in such a case, the credit registry does not explicitly flag the borrower as having a negative credit history, no decision can be taken on the basis of the registry alone. Further information is needed to enable IT-assisted processing and the exclusion of clients of this kind. This, in turn, requires such information to be defined in more detail so that it can be evaluated by IT systems and it also requires the information to be available. We would therefore ask the EBA to spell out in greater detail what cases the term “adverse credit history” should cover.

Article 20(11)(c)
Para 50 of the draft guidelines does not help to clarify how this criterion is to be interpreted by saying: “For the purpose of Article 20(11)(c) of Regulation (EU) 2017/2402, a credit assessment or credit score of an underlying exposure should be considered to be significantly higher than for comparable exposures held by the originator which are not securitised, **when the credit score or assessment for such underlying exposures is significantly higher than the average credit score or assessment of all comparable exposures held by the originator which are not securitised**.”

In our view, the above wording does nothing to explain precisely when a credit score should be considered “significantly higher” than the average credit score of comparable exposures. Banks need hard

criteria on which programmable decisions can be based. This is the only way to ensure that their IT systems are in a position to select exposures eligible for STS securitisations. The above guidance will not be helpful in practice. Without certainty that they are interpreting the criterion correctly, and without the ability to automate the decision-making process, banks will refrain from issuing STS securitisations, especially given the harsh sanctions which the STS Regulation provides for.

The Regulation itself sets out the criterion as follows:

“(c) has a credit assessment or a credit score indicating that the risk of contractually agreed payments not being made is significantly higher than for comparable exposures held by the originator which are not securitised.”

We believe this requirement should be interpreted as meaning that the exposures to be securitised should not have a significantly lower credit assessment or credit score than comparable non-securitised exposures held by the bank. The credit quality of comparable non-securitised exposures should be determined not by an average score, but by the range of acceptable creditworthiness which normally forms part of a bank’s credit risk strategy. This means, in our view, that the bank can securitise as STS securitisations all exposures whose credit quality does not significantly differ from those it takes on in the course of its normal lending operations for a portfolio of a similar nature. Exposures in default or credit-impaired within the meaning of the other criteria in Article 20(11) naturally have to be excluded.

The objective of the criterion, as we see it, is to prevent a bank from securitising exposures of a credit quality which the bank’s own policies would no longer allow it to accept, with up-to-date knowledge of the borrower’s creditworthiness, in the course of its normal lending operations for loans of a comparable nature. We believe the intention is also to prevent the securitisation of exposures which are not yet in default or credit-impaired within the meaning of the other criteria in Article 20(11) but whose credit quality has deteriorated so significantly over time that the bank would no longer take them on in the knowledge of the current credit status. Since the credit quality of exposures held by a bank may deteriorate, it is our understanding that, in the event of a random selection, i.e. no conscious selection of low-quality exposures, it should still be possible to securitise them as long as the credit quality and probability of default do not significantly differ from the credit quality and probability of default which the bank would still find acceptable for exposures of a comparable kind in the course of its normal lending operations.

In our opinion, the term “comparable exposures” as used in Article 20(11)(c) clearly refers to the range of credit quality acceptable in normal lending operations for exposures of a comparable nature. This interpretation also has the merit of enabling practical implementation, which is a major prerequisite for the subsequent STS securitisation of exposures.

We are opposed, by contrast, to an interpretation under which the credit score or credit assessment may not differ significantly from the average credit score. This would mean that exposures taken on in the course of normal lending operations and in compliance with a bank’s risk strategy could no longer be securitised if their credit score or assessment differed significantly from the average. It is unclear, moreover, when a divergence from the average should be deemed “significant”. This interpretation is not compatible with, or covered by, the text of the regulation since the regulation makes reference not to “average”, but to “comparable” exposures. As explained above, this means a range of credit quality will be involved, not an imaginary single value arrived at by calculating an average.

No predominant dependence on the sale of assets (Article 20(13))

Q17. Do you agree with the interpretation of this criterion, and the aspects that the interpretation is focused on? Should interpretation be amended, further clarified or additional aspects be covered? Please substantiate your reasoning.

The second subparagraph of Article 20(13) of the STS Regulation makes no reference to Regulation (EU) 575/2013 with respect to the requirements to be met by guarantors or sellers obligated to repurchase the assets. The interpretation set out in the draft guidelines is therefore not covered by the STS Regulation. The more logical and systematic interpretation, in our view, is to apply the non-impairment criteria of Article 20(11) of the STS Regulation, not least in view of the objective of these criteria. When a person or company undertakes to repurchase assets, the associated market risk becomes a credit risk. With this in mind, there is no reason why the creditworthiness of the party making this undertaking should suddenly be subject to different requirements. We would therefore ask the EBA to delete the reference to Regulation (EU) 575/2013 and clarify that guarantors and sellers obligated to repurchase the assets should neither be in default nor credit-impaired within the meaning of Article 20(11) of the STS Regulation.

Non-specified Articles of the Regulation (EU) 2017/2402

Q35. Do you agree that no other requirements are necessary to be specified further? If not, please provide reference to the relevant provisions of the STS Regulation and their aspects that require such further specification.

We believe that further major problems and questions of interpretation will only become apparent when the first securitisations are carried out in practice. We therefore recommend that the EBA and ESMA make a Q&A tool available so that interpretation issues encountered by the industry can be addressed and clarified after the final guidelines are in place. Given the Commission's wish to promote the European securitisation market, queries should be processed and answered swiftly so as not to unnecessarily delay issues of new securitisations.

We would also suggest that questions should be submitted centrally to one authority, e.g. the EBA, which could then, where necessary, either respond in consultation with ESMA or forward certain questions to ESMA.