





Joint Position Paper

March 2016

Investors and issuers unite to support Simple, Transparent and Standardised securitisation

Introduction

Investors, issuers and other market participants represented by the above associations strongly support efforts by EU policymakers to develop a new framework for the regulation of securitisation, including the proposals of the European Commission (the "Commission") for simple, transparent and standardised securitisation ("STS") and consequent fairer liquidity and capital requirements appropriate to STS securitisations and the actual risks they carry.

The signatories share the following views:

- Securitisation is an important element of well-functioning financial markets. Prudently deployed and sensibly regulated, it can:
 - o act as a bridge between the banks' financing and the capital markets;
 - o enable non-banks to diversify funding sources; and
 - o provide investors with high quality fixed income securities at attractive yields.
- Securitisation should be treated on a level playing field with other forms of investment. The significant differential treatment in regulations affecting capital, liquidity, transparency and disclosure and derivatives, when compared with other investment instruments, are undermining the ability to use securitisation as a financing tool in Europe.

This paper presents high level perspectives on the Commission's proposals¹. We have identified below several key points to consider in the development of a robust and successful STS framework.

¹ References to Articles are to Articles in the Commission's text of the framework regulation, unless otherwise stated.

Key points

Due diligence

- 1. Proper due diligence is a critical component of every investment decision and we note and support that Article 3 currently requires the institutional investor to perform the due diligence itself. However, practically speaking it is often the case that an institutional investor delegates the management of its investments to an asset manager (either through a segregated mandate or a fund vehicle); the asset manager will then perform the due diligence on any securitisations purchased on behalf of the institutional investor. In this instance, we argue that the institutional investor should be able to perform a general oversight of the asset manager's due diligence and not also be required to conduct the due diligence directly itself.
- 2. The proposed requirement to verify that a non-bank, non-MiFID firm originator / original lender grants all of its credits on the basis of sound and well-defined criteria is too broad and may be difficult for investors to confirm with certainty. In particular, it should be clarified that reliance can be placed by investors on information disclosed under Article 5.
- 3. In the context of carrying out the required assessment with respect to the STS status of a particular transaction, we note that the legislative proposals expressly indicate that investors may place "appropriate reliance" on STS notifications made by originators, sponsors and SSPEs. Market participants strongly support this, but it should be made clear that investors do not need independently to verify the statements of fact made by originators or sponsors in their STS notification. Additionally, when determining whether the facts disclosed by the originators or sponsors comply with the STS requirements, investors should be allowed to rely on the independent verification performed by appropriately supervised third party certification bodies.
- 4. As currently proposed, the new requirements for STS leave investors with duplicative, costly and inefficient new mechanical compliance burdens reducing small institutional investor participation and creating disincentives across all investor groups. We believe strongly that the best way to avoid this is for the authorities to appoint and regulate one or more independent, credible bodies to issue certifications of STS compliance under appropriate supervision.

Risk retention

- 1. The industry supports the move to the "direct" approach, but is concerned that it should be clear that the obligation only arises for entities involved in the securitisation and in respect of entities established in the EU.
- 2. While we support the proposed form of the restriction on originators retaining where their "sole purpose" is to securitise exposures, we consider that significant issues will arise if this wording is further restricted. We also believe that the definition of "sponsor" (which is limited to credit institutions (as defined in the CRR) and EU-regulated investment firms having specified authorisations) should be made more flexible to include all EU-regulated investment firms and recognised third-country investment firms (as defined in the CRR) whether or not having the specified authorisations, as the existing regulatory limitations pre-date the retention requirements and are not relevant for the purpose of appropriate interest alignment.
- 3. As noted below we consider it to be essential that the new retention regime applies (directly and indirectly via the due diligence obligations) in respect of transactions established on or after the effective date of such regime only. See also "Grandfathering and legacy transactions" below.

Disclosure

- 1. We fully support appropriate and balanced disclosure for STS that delivers meaningful value for investors and urge that the required information is suitably tailored according to the asset class. Reference should be made to work undertaken in the context of discussions around Article 8(b) of the CRA Regulation, where appropriate, as well as to the existing ECB disclosure templates.
- 2. We recommend that STS notifications should be required to include a brief explanation of how each of the STS criteria has been complied with.
- 3. In order to enable potential institutional investors to receive sufficient information to conduct a proper due diligence, or oversee that this is correctly done by the asset manager working on their behalf, we recommend that information should be disclosed to "institutional investors" and not "holders". See also "Due diligence" above.
- 4. The amount of required information may be difficult to obtain in the precise format required by Article 5 for third-country securitisations. See also "Third-country provisions" below.

5. As noted below, we consider it to be essential that the new regime applies (directly and indirectly via the due diligence obligations) in respect of transactions established on or after the effective date of such regime only. See also "Grandfathering and legacy transactions" below.

Compliance with the framework

- 1. With regard to compliance with the STS framework, we fear that many of criteria, as currently described in the legislative proposal, could be subject to a degree of interpretation that is too wide, and could vary across different member states. Therefore, we strongly believe that there should be clarity, consistency, and speed in obtaining the STS designation, along with stability of the STS designation once obtained, in order for the framework to function.
- 2. We believe that for this to be achieved, the interpretation of STS criteria should be the responsibility of a single, permanent and effective regulatory body with a Europe-wide remit.

ABCP

1. We welcome the inclusion of ABCP in the proposed STS framework as it is the source of cost efficient funding for a number of key economic actors such as SMEs and the auto manufacturers; however we have concerns that the STS criteria as proposed by the Commission do not sufficiently recognise the specific structural characteristics of ABCP programmes. Consequently as currently drafted the vast majority of the ABCP transactions will not qualify as STS. This in turn will result in investors (money market funds in particular) being unable to invest in ABCP issued by a non-STS ABCP Programme. Criteria such as the maturity limits, transaction level requirements and disclosure requirements are unnecessary to establish stable and transparent ABCP programmes that fully meet the STS principles, and as proposed are extremely problematic. Further, the STS criteria for ABCP as currently drafted misunderstand the risks that an investor in ABCP is exposed to. Effectively, the rules address risks that actually fall on the bank sponsor and not the investor.

Grandfathering and legacy transactions

It is essential that the new regime on retention and disclosure applies in respect of transactions established on or after the effective date of such regime only. The "grandfathering" of existing transactions should be extended as much as possible with regard to risk retention and disclosure requirements.

- 1. Clarification is required with respect to the retention and disclosure related verifications for existing transactions to ensure that a new compliance standard is not retrospectively applied to these arrangements indirectly.
- 2. We propose that the transition period should be 12 months from the date of entry into force of the implementing legislation for the STS framework.
- 3. We would recommend that the grandfathering rules for the STS requirements should recognize the importance and quality of existing transactions by firstly carrying over the relief provided in respect of Pre-2011 Transactions when the retention rules were first introduced; and secondly providing a limited set of criteria for transactions entered into before the coming into force of the STS regulation (as was done in the Solvency II Type I securitisation criteria), so that simple and transparent securitisations can be treated as STS though they may not meet all technical requirements of the new criteria.

Sanctions regime

- 1. Although we fully accept the need for a strong and deterrent sanctions regime, we believe that a strict liability standard, particularly when coupled with very severe civil and possible criminal sanctions, is inappropriate. There should be proportionality in the application of the sanctions and market participants who act in good faith should be recognised and credited for doing so. We believe that the penalties should apply only in the case of negligence or deliberate misconduct.
- 2. The STS designation should remain during the entire life of the securitised instrument, in all cases where the designation was granted in accordance with the rules and interpretations in force at the time.
- 3. Should this no longer be the case (i.e. the STS criteria are no longer fulfilled or the designation is determined to have been erroneously granted), the change in qualification of STS should immediately be communicated by the originator to the market authorities to assess the impact and possible remedies. We consider that in the situation where a securitisation transaction loses its STS qualification, investors should only be mandated to take such corrective action as is in their best interest in such circumstances and not be required to be forced sellers. We further note that a similar regime exists currently under Article 54 of the AIFMD Delegated Regulation.²

5

² http://eur-lex.europa.eu/legal-content/EN/TXT/?uri=CELEX%3A32013R0231

4. Additionally, when a transaction loses its STS designation, appropriate mitigants need to be available in the regulations (cure periods, progressive loss of STS benefits, partial loss only for minor technical issues) to avoid investors being hit by cliff-effects and market instability.

Third-country provisions

- 1. In order to maximize the potential of STS as intended by the Commission's original proposal, we encourage EU legislators to maintain an open approach to third-country securitisation. We support the inclusion of the provisions for the designation of competent authorities for entities not covered by EU legislation. We fully accept that any regime for third-county securitisation has to operate under a safe, verifiable and enforceable regulatory structure.
- 2. However, it is important that the proposals do not unintentionally restrict the range of high quality investment choices available to European savers. We consider that a requirement for all of the originator, sponsor and SSPE to be established in the EU would limit access to high quality, simple and transparent third-country securitisations for European savers. Excluding non-EU securitisation from STS recognition (and the more appropriate capital requirements) would also result in securitisation exposures with similar levels of credit risk which could otherwise be STS-compliant being treated differently for regulatory capital purposes.

Capital for banks and insurer investors

- 1. A fair capital treatment of securitisation positions, both for STS and non-STS and both under the CRR and Solvency II, which recognises the lessons of the crisis both positive and negative and the strong performance of European securitisation is crucial for the revival of the European securitisation market. The STS proposals will not be successful if the capital weightings of STS securitisations are set at the levels which are still excessive in relation to the risks they truly carry. In addition, the capital requirements in Solvency II are currently unnecessarily high and need to better reflect the actual risks that insurers are exposed to when investing in such assets, which is often default risk and not spread risk.
- 2. As a result, we strongly support urgent work on modifications to the CRR (including leverage ratio calculation) and Solvency II calibrations to much better reflect the actual and measurable risks involved in STS securitisations and create a level playing field amongst European capital market instruments of similar risk characteristics.

LCR Treatment of securitisations

1. LCR eligibility criteria and treatment are also essential elements for revitalisation of the European securitisation market. STS requires a more level playing field with other fixed income instruments: for example, the liquidity treatment of STS in terms of haircuts, limits, etc., under the LCR should be much closer to that of covered bonds. In that context we urge the Commission to consider a review of the LCR addressing these issues as soon as possible.

Conclusions:

For the European securitisation market to revive on a safe and robust footing the new STS framework must be attractive for both issuers and investors whilst operating under a strong but fair and rational regulatory regime. The return of a robust investor base, both bank and non-bank, and including investors for every tranche, is essential. The market also needs a more level playing field with other fixed income instruments as well as sensible STS criteria and balanced regulations on capital and liquidity that recognise the strong performance of European securitisation through and since the crisis, as well as the additional strengths of simple transparent and standardised securitisation. The success of the STS framework depends as well on the stability of the label and the ability of the investors and issuers to rely on the STS designation.

We urge all policymakers to take steps to address the regulatory factors holding back the recovery of the securitisation market as soon as possible.