Setting the standard
for securitisation

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EUROPEAN COMMISSION
Directorate-General for Financial Stability
Financial Services and Capital Markets Union

4th December 2024

Dear Sirs and Madams

RESPONSE TO THE TARGETED CONSULTATION ON THE FUNCTIONING OF THE EU SECURITISATION FRAMEWORK

Prime Collateralised Securities (PCS) is an independent, not for profit initiative set up to help revitalise the securitisation market in Europe. As such, the views expressed in this paper are PCS' own and do not necessarily represent the views of the members of the PCS Association. PCS also conducts a not-for-profit third-party verification business under the European STS regime. It this capacity PCS has verified more than 630 STS transactions. PCS would like to thank the Commission for the opportunity to respond to this consultation on a crucial component of the European Financial system.

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1. Effectiveness of the securitisation framework

1.1. Do you agree that the securitisation framework (including the Securitisation Regulation and relevant applicable provisions of the CRR, Solvency II and LCR) has been successful in, or has contributed to, achieving the following objectives:

	Fully agree	Somewhat agree	Neutral	Somewhat disagree	Fully disagree	No opinion
1. Revival of a safer securitisation market					✓	
2. Improving financing of the EU economy by creating a more balanced and stable funding structure of the EU economy			✓			
3.Reducing investor stigma towards EU securitisations				✓		
4. Reducing investor stigma towards EU securitisations		✓				
5. Removing regulatory disadvantages for simple and transparent securitisation products					✓	
6. Reducing/eliminating unduly high operational costs for issuers and investors					✓	
7. Differentiating simple, transparent and standardised (STS) securitisation products from more opaque and complex ones	✓					
7.1 Increasing the price difference between STS vs non-STS products					✓	
7.2 Increasing the growth in issuance of STS vs non-STS products					✓	
8. Supporting the standardisation of processes 7 and practices in securitisation markets			✓			
8.1 Increasing the degree of standardisation of marketing and reporting material		✓				
8.2 Reducing operational costs linked to standardised securitisation products					✓	
9. Tackling regulatory inconsistencies					✓	

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2. Impact on SMEs

2.1. Have you come across any impediments to securitise SME loans or to invest in SME loan securitisations?

- **Yes**
- No
- No opinion

Please explain.

First, a trivial yet important point: the main impediments to securitizing SME loans are the impediments to securitisation generally. Fixing the multiple regulatory distortions in the current securitisation framework is the best way to increase the securitisation of SME loans.

It should also be noted that SME securitisations are usually difficult because of the way SME lending is priced: a bank will often make an SME loan at a lower interest rate than justified by the credit quality of the borrower and the size of the loan. The loan is made as part of a package of services (cash management, credit card, deposit accounts, etc…) that are globally profitable. The loan is the incentive for the SME to bank with the lender. When the loan is extracted from the overall relationship to be securitised, it is often found not to be yielding enough for a potential securitisation investor who does not get the financial benefit of the other aspects of the relationship.

The point of this comment is to draw attention to the fact that SME lending is a profitable activity for banks that banks will undertake if they have the available lending envelope. Money and capital being fungible, SME securitisation is not a pre-requisite for more SME lending. We therefore urge the Commission not to focus on specific asset classes as this is likely to be both distortive (with unpredictable consequences), complex and unnecessary.

Turning to impediments specifically to the securitisation of SME loans, we can identify two which in our opinion are in need of fixing.

First, the disclosure templates drafted by ESMA are not appropriate for SMEs, containing a number of fields that are irrelevant to the asset class.

Secondly and more problematic are the provisions of article 243(2) of the CRR. These prevent an STS transaction from benefiting from lower capital requirements when held by a bank unless, inter alia, every underlying exposure meets the conditions for being assigned, under the Standardised Approach and taking into account any eligible credit risk mitigation, a risk weight equal to or smaller than 100% (for corporate – and therefore SME – exposures). This excludes pools of SMEs containing any loan with external rating of B+ or below and risk weighted at 150%. Such rating, explicit or implied, would not be unusual for an SME.

Without the possibility of bank investors achieving lower capital requirements under the CRR, there is little incentive for originators of SME loans to strive for the STS designation. The unavailability of the lower capital requirements will also increase the

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yield required by investors further exacerbating the issue referred to in our second paragraph above.

2.2. How can securitisation support access to finance for SMEs?

As set out above, securitisation can support access to finance for SMEs by:

- Allowing European banks to manage safely but proactively their capital. This will increase the lending capacity of banks in a capital constrained world. In this respect, it should be noted that many SME securitisations are, inter alia for the reasons set out in our response to 2.1, done in synthetic format for the purpose of freeing bank capital. This creates a direct link between the SME book and securitisation as a management tool. However, also for reasons set out above, this direct link is not – in our view – essential.
- Diversifying and increasing the volume of funding which a bank can access.
- Allowing public institutions such as the EIB to finance with greater efficiency the SME sector. This can be done by the EIB (or similar institution) arranging an SME securitisation, keeping some of the securitisation on its books and selling the rest to the market. If the EIB sells 80% of the securitisation, for example, then every Euro of available funds has generated five euros of SME lending. By targeting what tranches and credit risk it wishes to retain and what it wants to sell, the EIB can also use its cheaper cost of funds and capital to reduce the overall cost to the end SME borrower. But to achieve this one needs to have a sufficiently deep investor base to purchase the 80% sold).
- In the longer term, a revived securitisation market can draw in currently underutilized European savings and be an anchor for a deep capital market. Once such a market exists, it may allow for the issuance of SME bonds which can be pooled into SME funds. This is the experience of the United States where small business bonds are financed by the capital markets via specialized funds. However, one must bear in mind the sequencing of any development of a deeper European capital market. European savers are risk averse. To convince them to move their funds from guaranteed bank deposits to capital market instruments, the offer must first be of extremely safe assets. Senior, AAA/AA rated, STS European residential mortgage-backed securities and auto-loans are an ideal first step. Their credit performance during the crisis was flawless. The underlying asset is not only extremely safe but easily understandable to investors. (We are NOT advocating that even such safe securitisations be sold directly to retail investors but via specialist funds such as UCITS, staffed by conservative and knowledgeable investors). As savers become used to investing in capital markets, these will develop over time and new products such as bonds issued by SMEs become a possibility. This would, in due course, transform the landscape for SME funding. It would also do so on a pan-European basis as funds could purchase SME bonds from any EU state allowing SMEs no longer to be limited for their funding to local banks.

- In a direct fashion, SMEs are also able directly to access the securitisation market via the asset-backed commercial paper securitisation market (ABCP). European banks that sponsor ABCP conduits can (and do) offer access to those conduits to SMEs by having the conduit purchase and securitise assets generated by those SMEs. In the vast majority of cases, these are trade receivables generated by SMEs. In cases of SMEs supplying larger (and sometimes very large) corporates, these high quality receivables can be financed at much finer rates than would be available to that SME by direct borrowing. So any amendments to the current regulatory regime that benefits the ABCP market would benefit SME funding.

We strongly encourage policymakers to see the benefits of a safe but deep European securitisation as part of a long-term transformation of European finance to make our economies competitive on a global scale – together with other necessary reforms (eg the development of European equities markets). Properly conducted and supervised, such a development will provide long term benefits to SMEs (including start-ups involved in innovation).

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3. Scope of application of the Securitisation Regulation

Jurisdictional scope

3.1. In your opinion, should the current jurisdictional scope of application of the SECR be set out more clearly in the legislation?

- Yes
- **No**
- No opinion

Please explain.

Currently, the SECR has extra-territorial effects in that a EU investor in non-EU securitisations must require such securitisations to comply with the SECR. Most non-EU securitisation issuers are not willing (because of cost in time and money) or able to comply with the SECR and so EU investors are not able to invest in their issuance.

Conceptually, lowering the standards that need to be met by non-EU issuers appears problematic. On its face, it would give an advantage to non-EU issuers as against EU issuers. This would in theory allow non-EU issuers to make their product more attractive, directing EU investors preferentially to fund economies outside the European Union. It would also worsen, rather than enhance, the global competitiveness of European banks and non-bank financial institutions as it would make their access to the securitisation market – governed by the SECR – costlier than that of non-EU banks.

However, there are two avenues that could be explored to improve the situation.

First, it should be possible to put in place an equivalence regime backed by strong MOUs between regulatory authorities. This would ensure that non-EU issuers play on a substantially level playing field with EU issuers. It would also do so whilst allowing some small divergences that may be unavoidable due to local legal requirements or practices so long as those divergences are not material.

Secondly, and more importantly, most of the difficulties encountered by non-EU issuers are the same as those encountered by EU issuers: the disproportionate and unnecessarily burdensome requirements of article 7 disclosure. It strikes us that the real answer to this problem is for changes to article 7 to reduce disclosures to what is actually needed and used by reasonably conservative EU investors. If this is achieved, then non-EU issuers would be required only to produce information that is genuinely necessary. Either they can and will do this or investors would not buy their issuance anyway as they lacked key data necessary to reach a credit decision.

On the issue of retention, we believe skin-in-the-game rules are an essential part of the reforms that allow securitisation to be a safe product and to avoid any repetition of the issues that worsened the financial crisis. Therefore, EU retention rules should be applied to non-EU securitisations sold to EU investors. Under an equivalence regime, one could contemplate small deviations when required by local law but only to the

extent EU authorities were satisfied that such deviations were entirely consistent with the retention requirements and principles applied in the EU.

3.2. If you answered yes to question 3.1, do you think it would be useful to include a specific article that states that SECR applies to any securitisation where at least one party (sell-side or buy-side) is based or authorised in the EU, and to clarify that the EU-based or EU-authorised entity(ies) shall be in charge of fulfilling the relevant provisions in the SECR?

- Yes
- No
- No opinion

Please explain.

Legal definitions

3.3. Do you think the definition of a securitisation transaction in Article 2 of SECR should be changed? You may select more than one option.

- Yes, the definition should be expanded to include transactions or vehicles that could be considered securitisations from an economic perspective;
- Yes, the definition should be narrowed to exclude certain transactions or introduce specific exceptions;
- **No, it should not be changed;**
- No opinion.

Please explain and specify, if necessary, how the definition should be expanded or narrowed in your view.

There are some good philosophical reasons why some products currently included in the definition of "securitisation" should not be. Managed CDOs for example, in that they rely for their performance on the skills of the managers and the choices they make, are closer to funds than to traditional securitisations. Synthetic securitisations where the originator retains the senior tranche are closer to credit insurance. Most of the issues identified with traditional securitisation after the financial crisis and which led to the SECR reforms do not apply to such synthetic securitisations. For example, they contain no discernible agency risk for the holder of the senior position when that entity is the originator.

However, simply narrowing the definition of securitisation to exclude such products would leave them in a form of regulatory void. It could therefore only be done if concurrently a new regulatory regime was crafted for them to replace the SECR. To make the necessary reforms of the securitisation market dependent on the creation of these parallel regulatory frameworks for the now excluded products would exponentially increase the complexity of the exercise and extend probably by years the landing time of the former. It could even doom it to failure.

On the other hand, leaving such products within the securitisation definition, whilst arguably sub-optimal and conceptually flawed, does not materially impact their availability. CDOs are the largest asset class in true sale securitisations today.

The better course of action is therefore to make amendments to the current regime to accommodate, where safe and necessary, the idiosyncrasies of these products and not to change the definition.

3.4. Should the definition of a securitisation exclude transactions or vehicles that are derisked (e.g. by providing junior equity tranche) by an EU-level or national institution (e.g. a promotional bank) with a view to crowding-in private investors towards public policy objectives?

- Yes
- **No**
- No opinion

3.5. If you answered yes to question 3.4., what criteria should be used to define such transactions?

3.6. Should the definition of a sponsor be expanded to include alternative investment firm managers established in the EU?

- Yes
- No
- **No opinion**

Please explain, including if the definition should be expanded to any other market participants.

3.7. If you answered yes to question 3.6., are any specific adaptions or safeguards necessary in the Alternative Investment Firms Directive (AIFMD13), taking into account the originate-to distribute prohibition in the AIFMD, to enable AIFMs to fulfil the functions of a sponsor in a securitisation transaction, as stipulated in the SECR? You may select more than one option.

- An AIFM should not sponsor loans originated by the AIFs it manages
- AIFs should not invest in securitisations sponsored by its AIFM
- Minimum capital requirements under the AIFMD should be adapted to enable AIFMs, in particular to fulfil the risk retention requirement under SECR
- Other safeguards
- No safeguards are needed

Please explain your answer.

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4. Due diligence requirements

4.1. Please provide an estimate of the total annual recurring costs and/or the average cost per transaction (in EUR) of complying with the due diligence requirements under Article 5.

Please differentiate between costs that are only due to Article 5 and the costs that you would incur during your regular due diligence process regardless of Article 5.

Please compare the total due diligence costs for securitisations with the total due diligence costs of other instruments with similar risk characteristics.

4.2. If possible, please estimate the total one-off costs you incurred (in EUR) to set up the necessary procedures to comply with Article 5 of SECR.

4.3. Please select your preferred option to ensure that investors are aware of what they are buying and appropriately assess the risks of their investments.

- **Option 1: The requirements should be made more principles-based, proportionate, and less complex;**
- Option 2: The requirements should be made more detailed and prescriptive for legal certainty;
- Option 3: There is no need to change the text of the due diligence requirements;
- No opinion

Due diligence requirements prior to holding a securitisation position

4.4. Should the text of Article 5(3) be simplified to mandate investors to assess at minimum the risk characteristics and the structural features of the securitisation?

- **Yes**
- No
- No opinion

Please explain.

4.5. If you answered yes to question 4.4., please specify how this could be implemented.

The current mandatory, extensive and detailed requirements impose costs in money and time that are artificially constraining the European securitisation market. This constraint results from the fact that (a) the costs of setting up and overseeing this

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mandated structure is deterring new investors and (b) the cost in time and human resources to effect all these steps – even when the prospective securitisation purchase does not warrant them – limits the number of trades any given investor can achieve in any given time frame. As such, by limiting the ***number*** of securitisations that can be due diligenced it places an artificial limit on the ***volume*** of securitisations that can be issued each year irrespective of the amount of funding theoretically available to be invested in securitisations.

In looking at article 5 requirements two facts must be borne in mind.

First, these requirements cannot be examined solely in the silo of securitisation. They must be placed in the context of all other capital market instruments – many considerably more risky than securitisation – where no such costs are imposed. Investment decisions are made by comparing the cost/reward balance of all available instruments. So, imposing an unnecessary cost on one instrument distorts the market and generates regulatory arbitrage. The issue of article 5 is not a securitisation issue but also a level playing field issue.

Second, the extremely heavy mandatory requirements of article 5 derive from a post financial crisis perception that securitisation ***per se*** was a uniquely dangerous product. Since then, the excellent performance of European traditional securitisations (today's STS) and all the reforms effected by the SECR (retention, disclosure, re-securitisation ban, creation of STS, sanctions regime…) mean that European securitisation (especially in STS format) cannot be seen as a "uniquely dangerous product". It is therefore necessary to revisit the article 5 rules to account for the fact that the underlying premise for its current form is no longer true.

In our opinion, the best way to reform the current article 5 obligations is for the SECR to require every investor to have in place a written mandatory due diligence process (MDDP). This process must be approved by senior management and required to be applied for each purchase of a securitisation position. This should ensure that individual investors in any institution do not allow due diligence standards to slip over time. For prudentially regulated investors, their supervisory authority also has the power to request and vet these MDDPs.

For investors that have delegated due diligence in accordance with article 5.5 SECR, the delegatee would be required to have an MDDP in place and the delegator should be required to review such MDDP prior to granting the mandate.

The SECR should require that the MDDP should be proportionate to the risk of the product and *must* take into account, when gauging that risk:

- The seniority of the position
- The CQS assigned to the position
- Whether the position is STS or not
- The maturity of the position
- If the position is purchased in the secondary market, the remaining maturity (including the current credit enhancement level)
- Whether the originator of the securitised positions is prudentially regulated

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- Whether the position is a "repeat transaction" for that investor – ie the investor has due diligenced and invested in previous securitisations of that originator as part of an ongoing issuance program
- Whether the investor already holds the position and so has already done due diligence of that securitisation and how long ago.
- The nature of the securitised assets – whether they are new types of assets or well known types of asset with long data sets on performance
- In the case of managed CDO's – the experience and track record of the managers

It should be left to investment firms to determine, having taking into account these factors and any other additional facts not required by the SECR mandatorily to be considered but which they believe are appropriate, what documents, data and stress tests are necessary.

4.6. Taking into account your answer to 4.4, what would you estimate to be the impact (in percent or EUR) of such a modification in Article 5(3) on your one-off and annual recurring costs for complying with the due diligence requirements under Article 5?

Please explain.

4.7. Should due diligence requirements differ based on the different characteristics of a securitisation transaction?

- **Yes**
- No
- No opinion

4.8. If you answered yes to question 4.7., please select one or more of the following options to differentiate due diligence requirements:

- **Due diligence requirements should differ based on the risk of the position (e.g. senior vs non-senior)**
- **Due diligence requirements should differ based on the risk of the underlying assets**
- **Due diligence requirements should differ based on the STS status of the securitisation (STS vs non-STS)**
- **Other**

Please explain your answer.

The due diligence requirements should impose on investors the requirement to have a mandatory due diligence process (MDDP) that takes into account these aspects. To that extent due diligence requirements should differ. See our answer to question 4.5.

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But the way in which they differ should be determined by investment entities. This is how a level-playing field can be achieved with other capital market instruments acknowledging the reforms already put in place to ensure that securitisation is not a more dangerous product than any other instrument.

4.9. Taking into account your answers to 4.7 and 4.8, what would you estimate to be the impact (in percent or EUR) of differentiating due diligence requirements on your one-off and annual recurring costs for complying with the due diligence requirements under Article 5?

Please explain your answer.

4.10. For EU investors investing in securitisations where the originator, sponsor or original lender is established in the Union and is the responsible entity for complying with those requirements, should certain due diligence verification requirements be removed as compliance with these requirements is already subject to supervision elsewhere?

This could apply to the requirements for investors to check whether the originator, sponsor or original lender complied with:

(i) risk retention requirements,

- **Yes**
- No
- No opinion

(ii) credit granting criteria requirements,

1. **Yes**
2. No
3. No opinion

(iii) disclosure requirements,

- Yes
- **No**
- No opinion

(iv) STS requirements, where the transaction is notified as STS

- **Yes**
- No
- No opinion

Please explain if you see any risks arising from the removal of these requirements, and if so, how they should be mitigated.

Our responses to question 4.10 must be heavily qualified:

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(i) Risk retention – requirement to check should ONLY be removed where the risk retainer is prudentially regulated in the European Union.

(ii) Credit granting criteria – our general approach (see response to question 4.5) is that such issues should be determined by the investment firm and included as appropriate in the MDDP.

(iii) Disclosure requirements – since all the proposed reforms are interconnected, the negative answer in this instance is partially dependent on the necessary simplifications to article 7 which would result in a much more relevant and possible slimmed down disclosure requirement. Such requirement could and should, without undue burden, be checked by investors.

(iv) STS status – the legislation has provided for authorised and supervised third party verification agents. The sole purpose of their creation in the SECR was to socialize the cost for investors of STS verification, avoid duplication and enhance standardisation of interpretations so that STS was a unified standard. It is therefore logical that if a securitisation has been verified by an authorised and supervised independent entity, investors should be able to rely on their work. (We note that the use of TPVs is not mandatory. In the absence of TPVs, we do not recommend reliance on originators who have, in this respect, an unmanageable conflict of interest. Through our work as TPV it is not uncommon that we refuse to accept interpretations of the STS criteria which we believe to be abusive and in breach of the spirit of the SECR. If investors were allowed to rely on originators, there would be, in our view, little to no barriers to a downward drift of the STS standard. So absent a TPV, investor due diligence is, in our view, unavoidable).

We have seen the argument made that STS should not be verified by investors who do not wish to rely (or cannot rely) on that status to obtain regulatory benefits. The argument is that why should investors check something they do not care about? In our opinion, this is not a convincing argument. STS was designed as a quality standard, not as a means to generate prudential benefits. The prudential benefits flow from the standard and not vice versa. The purpose of the standard is to promote safe securitisations in Europe that enhance financial stability and standardisation that deepens markets. But, for standards to work, they must have a verification mechanism that enforces compliance with the standard and so generates a sense of trust and safety amongst users. So, someone must verify. The crisis has shown the limitations of leaving such verification with originators due to the obvious conflict of interest they face. So, the verification must lie either with investors whose interests are aligned to the standard or TPVs created for that purpose and whose conflicts of interest are managed by the regulatory rules that bind them and the supervision under which they operate.

4.11. Taking into account your answers to Q.4.10, what would you estimate to be the impact (in percent or EUR) of removing those obligations on your one-off and recurring costs for complying with the due diligence requirements?

Please explain.

4.12. Do the due diligence requirements under Article 5 disincentivise investing into securitisations on the secondary market?

- **Yes**
- No
- No opinion

Please explain.

The cost of setting up and managing an internal system compliant with article 5 (and attendant sanctions risks if compliance is deemed to be faulty) disincentivises investors generally – whether they are thinking of investing via the primary or the secondary market.

The issues in the secondary can be heightened in a number of cases, such as, for example:

- Where the seller wishes to effect a quick sale. This was seen during the UK LDI crisis when funds sought immediate liquidity and EU investors were not able to purchase due to their lengthy mandatory due diligence requirements
- Where the buyer is purchasing to trade and so long-term credit considerations are not relevant compared to likely price movements
- Where the buyer is purchasing a securitisation that is a senior STS close to maturity and where sequential amortisation has created a very substantial level of credit enhancement and a very short period of risk.

4.13. If you answered yes to question 4.12., should investors be provided with a defined period of time after the investment to document compliance with the verification requirements as part of the due diligence requirements under Article 5?

- Yes
- **No**
- No opinion

The issue is that the current due diligence requirement is a "one-size-fits-all" that does not account for the differences in risk amongst securitisations and securitisation types. As such it is not proportionate. The provision of additional time post purchase for investors to perform unnecessary and disproportionate due diligence is not the answer.

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In fact, this would only introduce additional problems. What should the investor do if the post-purchase due diligence reveals an issue? Presumably, the investor would have to sell. This would generate more uncertainty. Alternatively, to be comfortable that post purchase article 5 diligence process would not be harmful because it should not have any meaningful impact is to accepts, in seems to us, the proposition that much of this due diligence is, in fact, pointless.

The answer must be that investors – whether in the primary or the secondary – do all the due diligence that is necessary properly to evaluate the risk ***before*** purchasing a position taking into account their risk appetite and the purpose for which they are buying the position.

We refer back to our answer to question 4.5 as to what this necessary due diligence should look like.

As a gloss on our response, if reforms of the existing article 5 provisions are not able to produce a proportionate set of requirements and Europe remains burdened by unnecessary mandatory due diligence, then – and only then – a fifteen-day period should be allowed to alleviate the situation of investors. However, such measures are unlikely to do much for the market or for financial stability.

4.14. If you answered yes to question 4.13., how many days should be given to investors to demonstrate compliance with their verification requirements as part of the due diligence requirements under Article 5?

- 0 – 15 days
- 15 – 29 days
- 29 – 45 days
- No opinion

4.15. If you answered yes to question 4.13., what type of transactions should this rule apply to?

4.16. Do the due diligence requirements under Article 5 disincentivise investing into repeat securitisation issuances?

- **Yes**
- No
- No opinion

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4.17. If you answered yes to question 4.16., how should repeat or similar transactions be identified in the legal text and how should the respective due diligence requirements be amended?

Although we would leave legal drafting to the statutory draughtman, the definition of a "repeat transaction" should focus on the following elements:

- Same originator
- Same asset class (as defined by the homogeneity RTS 2024/584)
- Same jurisdiction(s) of origination of the underlying exposures
- Presented to the market as a programmatic issuance (eg with the same name) or
- Underlying exposures in the same master trust (or equivalent legal structure)
- Last purchased by the relevant investor within 18 months

In this case, the rules should allow the investor to due diligence only those aspects that have changed since the last transaction purchased by that investor.

4.18. Should Article 32(1) be amended to require Member States to lay down rules establishing appropriate administrative sanctions, in the case of negligence or intentional infringement, and remedial measures in case institutional investors fail to meet the requirements provided for in Article 5?

- Yes
- No
- **No opinion**

Please explain your answer.

This question cannot be answered independently of how the article 5 requirements are drafted. If they continue to be prescriptive, onerous, unnecessary and yet vague in content but without much latitude for legitimate exercise of judgement, then sanctions – which appear to our knowledge for no other asset class – would merely make exponentially less likely the entrance of new investors. This would be one more barrier to convincing the senior management of any potential investor to return to the securitisation market.

4.19. Taking into account the answers to the questions above on due diligence requirements, do you think any safeguards should be introduced in Article 5 to prevent the build-up of financial stability risks?

Financial stability risk would presumably build up in the capital markets because mispriced instruments or instruments whose risks are substantial but misunderstood

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pooled in certain parts of the financial system where, upon the occurrence of some event or events, they caused uncontrollable losses. Another risk to financial stability would flow from liquidity drying up due to some form of panic or concern over the solvency of one or more key players.

This seems to require regulators to have a solid understanding of where risks are pooling.

Although badly structured and opaque securitisation (almost entirely from the US) played a key role in the financial crisis, we note that the SECR has profoundly reformed the market and that European securitisations performed (especially in what would now be labelled STS) spectacularly well. This financial stability risk therefore does not appear to be a securitisation issue.

Part of the reason why the securitisation market struggles is the lack of a level playing field. For historical reasons, all sorts of onerous rules apply to securitisations and only securitisations. Even when those rules are sensible, they are never extended to other asset classes even when the potential issues with those asset classes are the same.

Therefore, we do not see any safeguards applicable only to the securitisation market to prevent a buildup of financial stability risk. On the contrary, history tells us that when heavy prudential rules are imposed solely on one part of the financial markets, the risk seamlessly flows to another unregulated or less regulated part and that it is precisely there financial stability risk builds up.

Of course, we welcome any regulation designed to reduce risks to financial stability but this should be in the context of an overall review of the markets and market instruments and not limited solely to securitisation.

4.20. Taking into account your answers to the previous questions in this section, by how much would these changes impact the volume of securitisations that you invest in?

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Delegation of due diligence

4.21. If you are a supervisor, how would the changes to the due diligence requirements suggested in the previous questions affect your supervisory costs?

4.22. Should the National Competent Authorities (NCAs) continue to have the possibility to apply administrative sanctions under Article 32 and 33 of SECR in case of infringements of the requirements of Article 5 SECR to either the institutional investor or the party to which the institutional investor has delegated the due diligence obligations?

- Yes
- **No**
- No opinion

Please explain your answer.

Any growth in the securitisation market, as called for by numerous experts and policy makers, must pass by a substantial increase in the number of investors.

But securitisation is technical. Therefore, the safety and stability of the system is enhanced if the credit analysis is performed by entities with deep skills in the securitisation field. The delegation by investors to experts should be encouraged.

However, concerns that one's firm may be fined for errors made by a third party with all the requisite qualifications and contracted in good faith is a deterrent for new investors. It also does not accord well with any notion of natural justice.

4.23. If you answered no to question 4.22, which party should be subject to administrative sanctions in case of infringement of the due diligence requirements?

- the institutional investor
- **the party to which the institutional investor has delegated the due diligence obligations**

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5. Transparency requirements and definition of public securitisation

5.1. Please provide an estimate of the total annual recurring costs and/or the average cost per transaction (in EUR) of complying with the transparency regime under Article 7. Please differentiate between costs that are only due to Article 7 and costs that you would incur during your regular course of business regardless of Article 7. Please compare the total transparency costs for securitisations with the total transparency costs of other instruments with similar risk characteristics.

5.2. If possible, please estimate the total one-off costs you incurred (in EUR) to set up the necessary procedures to comply with Article 7 of SECR.

5.3. How do the disclosure costs that you provided in 5.1. compare with the disclosure costs for other instruments with similar risk characteristics?

- Significantly higher (more than 50% higher)
- Moderately higher (from 10% to 49% higher)
- Similar
- Moderately lower (from 10% to 49% lower)
- Significantly lower (more than 50% lower)

Please explain your answer.

5.4. Is the information that investors need to carry out their due diligence under Article 5 different from the information that supervisors need?

- **Significantly different**
- Moderately different
- Similar

Please explain your answer.

We are only dealing with the case of supervisory authorities. Clearly, when a public institution such as the ECB acquires a securitisation position, e.g. as repo collateral for its liquidity operations, it is in the position of an investor as it takes (albeit as security) the credit risk of position.

An investor contemplating purchasing a securitisation position will need to ascertain the accurate risk/return equation for that position. (An investor with a very large portfolio may be less concerned with the exact analysis of each position in favour of a more statistical approach but few investors are running funds so large as to believe they can forsake an in-depth analysis of each individual position.)

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When overseeing financial stability risk either systemically or at the level of an individual financial institution, the supervisory authority must, of necessity, work with aggregate type data generating outputs of a statistical nature. We write "of necessity" for, if this were not the case and supervisors were expected to analyse individual positions, this would amount to a requirement for supervisory authorities to re-underwrite each and every position held by a bank: every SME loan, every project finance loan, every currency swap position, etc... Irrespective of any issue of the SECR, this clearly does not describe how supervision does or can operate.

Therefore, our answer derives from a general consideration of how supervision works and not about any specific issue with securitisation. Putting it another way, if one were to take the view that the information needed by investors and regulators was similar, does this mean that there is an expectation that the work done by both should be similar? Are supervisors required to underwrite and monitor individual positions? And if they are, is this to be limited to securitisations or extended to a bank or insurance undertaking's entire book?

We believe that, in ascertaining the information needed by supervisors, the Commission invite (as it surely will) supervisory authorities to set out how they monitor and expect to monitor regulated entities' exposure and, aggregating individual entity data, monitor systemic risks. The Commission should specifically enquire as to the types of tools regulators believe they need to use and frequency of their monitoring so that an accurate assessment of regulatory needs can be completed.

5.5. To ensure that investors and supervisors have sufficient access to information under Article 7, please select your preferred option below.

Option 1:

- Streamline the current disclosure templates for public securitisations
- Introduce a simplified template for private securitisations and require private securitisations to report to securitisation repositories (this reporting will not be public)

•*Option 2:*

- Remove the distinction between public and private securitisations.
- Introduce principles-based disclosure for investors without a prescribed template.
- Replace the current disclosure templates with a simplified prescribed template that fits the needs of competent authorities with a reduced scope/reduced number of fields than the current templates.

• Option 3:

- No change to the existing regime under Article 7.

5.6. If you are a supervisor, what impact (in percent or EUR) would you anticipate Option 1 would have on your supervisory costs?

5.7. Assuming that transparency requirements are amended as suggested in Option 1, by how much would the volume of securitisations that you issue, or invest in, change?

5.8. What impact (in percent or EUR) would you anticipate Option 1 would have on your one-off and annual recurring costs for complying with the transparency requirements in Article 7?

Please explain your answer.

5.9. Do you see any concerns, impediments, or unintended consequences from requiring private securitisations to report to securitisation repositories?

- **Yes**
- No
- No opinion

Please explain your answer.

If the definition of “private securitisation” is modified as suggested in our response to question 5.10, private securitisations will have information in formats and containing the data that each bank or insurance company believes it requires. To send that heterogeneous data to repositories serves no discernible purpose since (a) the transaction being private no investor will be able to access the data and (b) regulators already have all the access they need to this information since, using the definition of “private” suggested in our response to 5.10, the investor will need to be prudentially regulated for the transaction to be “private”.

However, if it proves not possible or desirable to modify the definition of “public” and “private” along the lines suggested in our response to question 5.10, whether “private” transactions should report to securitisation repositories would, to a large extent, depend on what the final definition becomes. In most cases, we would be favourable to private transactions reporting through repositories but no final position can be determined without the final definition.

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5.10. Under Option 1, should the current definition of a public securitisation be expanded to a securitisation fulfilling any of the following criteria: (1) a prospectus has been drawn up in compliance with the EU Prospectus Regulation; or (2) notes were admitted a trading venue; or (3) it was marketed (to a broad range/audience of investors) and the relevant terms and conditions are non-negotiable among the parties?

- Yes
- **No**
- No opinion

Please explain your answer.

In the view of PCS, the distinction drawn between "private" and "public" securitisations focuses on the wrong issue. The issue, in our view, is that information must be available to avoid systemic risks building up outside of the gaze of regulatory authorities and policy makers. The current definition is both legalistic and formalistic. What we mean is that it draws the line between types of disclosure or disclosure modalities in an artificial place which does not reflect the reasons why such a line should be drawn.

Due to its legalistic and formalistic nature, it is relatively easy for market participants to structure their securitisation to fall on one or the other side of that line without changing much of the underlying commercial rationale for the trade. This places policy makers in a dilemma: if the rules for private transactions are lightened, how to stop market participants re-structuring their transactions to benefit from the easier rules and deprive supervisors of the visibility they need? Conversely, if the rules for private transactions are brought in line with those for public transactions, how does this not impose an undue burden on genuinely bilateral private securitisations?

For the record, we should stress that originators changing the structure of their transactions to make them private for the purpose of lightening the regulatory supervision is NOT a phenomenon that we have encountered. Private transactions have been and remain so for good commercial reasons and not for regulatory ones. However, we also note that the difference between private and public transactions from a regulatory perspective has been so far slight. As there are good reasons for wanting to deepen that difference, the rules should be crafted so as to remove the incentive to "move" public transactions to the private bucket primarily to meet lower disclosure standards.

It appears to us that the answer is to draw the line between (a) transactions where the mandated disclosure is realistically the only disclosure available to supervisory authorities and policy makers and (b) transactions where the investor/lender is a prudentially supervised entity whose underwriting and books are entirely visible to a prudential regulator.

Rather than public vs private, this is more accurately described as banking/insurance business vs capital market business.

In the former, the investor/lender is prudentially regulated, its underwriting procedures have been approved by the regulator, its books and risks are monitored on an ongoing

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basis, its internal compliance procedures have been vetted. In other words, prudential regulators have complete oversight of that entity's securitisation purchases. They are satisfied that the entity will know what disclosure they require and will obtain such disclosure to conduct proper underwriting – in securitisations as in other lending activities. For such entities, requiring a different, one-size-fits-all and parallel article 7 disclosure is costly and wasteful. It also provides no additional regulatory benefit. At a European level, regulators have the means to be perfectly cognisant of any entity's positions and can aggregate these with those of other entities to map out any potential build up of systemic risks

In the latter case (capital market business), where some or all the investors are not prudentially regulated, regulatory authorities and policy makers, if they are not provided with sufficient information via article 7, have no obvious way to obtain that information. Also, they have no way of determining whether investors are getting sufficient information to avoid the type of surprises that emerged during the financial crisis. Consequently, systemic risk build-up will be difficult to discern.

Drawing the line at bank/insurance vs capital markets would have the following specific impacts: bank bilateral facilities (sometimes called warehouse facilities) and asset-backed commercial paper conduits could operate on a principle based or very light template. Synthetic securitisations where the protection purchasing bank retains the senior piece would also fall into the category as bank supervision authorities have all the necessary oversight at a complete level of granularity.

On the other hand, deals marketed to funds, even privately and with a single purchaser, would require the normal "public" disclosure as such transactions – if done in sufficient volumes – could impact financial stability and regulatory authorities should have a sense of what is happening.

It is acknowledged that drawing the line as we suggest will raise some potentially difficult interpretation issues in a few cases. However, this seems inevitable wherever the line is drawn. Either the rules remain with an easily defined but equally easily gamed dividing line or a more subtle approach such as that referred to in question 5.10 is chosen and interpretation difficulties will arise whichever definitions are selected.

5.11. If you answered yes to question 5.10., what criteria should be used to assess point (3) in the definition above (i.e. a securitisation marketed (to a broad range/audience of investors) and the relevant terms and conditions are non-negotiable among the parties)?

5.12. If the definition of a public securitisation is expanded (for example, to encompass securitisations fulfilling the criteria set out in question 5.10), what share of your existing private transactions would now fall under this newly-expanded public definition?

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5.13. Under Option 1, what would you estimate to be the impact (in percent or EUR) of changing the definition of public securitisation on your one-off and annual recurring costs for complying with Article 7?

Please explain your answer.

5.14. Assuming that transparency requirements are amended as suggested in Option 2, by how much would the volume of securitisations that you issue, or invest in, change?

5.15. What impact (in percent or EUR) would you anticipate Option 2 would have on one-off and annual recurring costs for complying with the transparency requirements in Article 7?

Please explain your answer.

5.16. Under Option 2, what should be included in the principle-based disclosure requirements for investors to reduce compliance costs while ensuring access to information? How should investors access this information?

Please explain your answer, listing all relevant information that you think investors need to do proper due diligence that could be common across all securitisations.

We would leave the answer to this question to investors to whom we see no benefit in substituting ourselves.

In our response to an ESMA consultation, we recommended that ESMA empanel a permanent committee made up of regulators and experienced and conservative investors to advise them on an ongoing basis on the adequacy of the templates. This would allow ESMA to adapt existing templates and/or create new ones when structures change or new types of assets are securitised. This would ensure that the disclosure regime is not gamed or merely becomes inadequate having not kept up with market developments as the panel would be able to bring ESMA up-to-date with such developments in real time and suggest how templates should be adapted to ensure their continued relevance.

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5.17. Under Option 2, should intra-group transactions, and securitisations below a certain threshold, be excluded from the reporting requirements in Article 7?

- **Yes**
- No
- No opinion

Please explain your answer. If you answered yes, how should intragroup transactions be defined and how should the threshold be determined?

Our response is positive for intra-group transactions but negative for securitisations below a certain threshold.

It is almost impossible to see how intra-group transactions could cause the buildup of systemic risk or how it could lead to defaults hitting investors via agency risks.

Our negative answer on thresholds is predicated on article 7 disclosure requirements becoming more proportionate and reflective of the data actually required by reasonably conservative investors to make a proper determination of the risk of a position. In that case, it is hard to see how the rules could require a smaller transaction to provide less information than is required for a proper determination of the risk. Clearly, if no simplification (or insufficient simplification) are the disclosure requirements achieved, PCS would support a threshold so as to protect, at least, smaller players from excessive and unnecessary disclosures. In those circumstances, there is no scientific way to determine at what level inappropriate disclosures should be required. A rule of thumb could be anything below €100 million in nominal pool size. We recommend using pool size rather than issuance volume to avoid the rules being gamed by structures where risks on a large pool can be broken up into smaller issuances that interact so as to make a single commercial whole but where each component is below the chosen threshold.

5.18. Under Option 2, what would be the impact (in percent or EUR) on your one-off and annual recurring costs for complying with the transparency requirements of excluding intra-group transactions and securitisations below a certain threshold from the reporting requirements in Article 7?

Please explain your answer.

5.19. Should the text of Article 7 of the SECR explicitly provide flexibility for reporting on the underlying assets at aggregated level?

- **Yes**
- No
- No opinion

5.20. If you answered yes to question 5.19., which categories of transactions should be allowed to provide reporting only at aggregated level? You may select more than one option.

- **Granular portfolios of credit card receivables**
- **Granular portfolios of trade receivables**
- **Other**

If you chose "other", Please explain.

All highly granular pools of small ticket loans should be exempt from the requirements of loan-by-loan reporting. Discussions with investors make it clear that they never look at loan- by-loan data for this type of transaction.

Referring back to our answer to question 5.16, this is exactly the kind of question that should be addressed to a standing committee of conservative investors and supervisors.

Amongst the types of asset classes that should be exempt from loan-by-loan reporting are small ticket consumer loans (less than €5.000) including buy-now/pay later loans, handset receivable loans, store cards etc....

5.21. If you are a supervisor, what impact (in percent or EUR) would you anticipate Option 2 would have on your supervisory costs?

6. Supervision

6.1. Have you identified any divergencies or concerns with the supervision, based on the current supervisory set up?

- **Yes**
- No
- No opinion

Please explain and give specific examples.

As a third-party verification agent, PCS has been made aware of differences in approach to the interpretation of some STS criteria across jurisdiction. We have always informed the EBA and the relevant national competent authorities in such circumstances. It should be noted though that such divergences are unavoidable and do not, in themselves, indicate a problem with the supervisory set up.

6.2. Would you see merit in streamlining supervision to ensure more coordination and supervisory convergence?

- Yes
- No
- **No opinion**

6.3. If you answered yes to question 6.2., what should be the scope of coordinated supervision?

- STS securitisations only
- All securitisations
- Other (please specify)

6.4. If you answered yes to question 6.2., what should be the supervisory tasks of coordinated supervision?

- Compliance with Securitisation Regulation as a whole
- Compliance only with STS criteria
- Compliance with Securitisation Regulation and prudential requirements for securitisation
- Other (please specify)

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6.5. If you answered yes to question 6.2., which model would you prefer?

- Setting up supervisory hubs
- Having one national authority as lead coordinator in the case of one issuance involving multiple supervisors
- Another arrangement (please specify)

Please explain your answer.

6.6. If you answered yes to question 6.2, would you require participation by all NCAs or only some?

- All
- Some
- No opinion

6.7. If you answered "Some" to 6.6., based on what criteria would you select NCAs?

Please specify.

6.8. If you are a supervisor, how would the changes to supervision suggested in the previous questions affect your supervisory costs?

7. STS standard

7.1. Do you think that the STS label in its current form has the potential to significantly scale up the EU securitisation market?

- **Yes**
- No
- No opinion

Please explain.

In our response, we deal with the STS label as it applies to traditional true sale securitisations.

The STS label since its inception has accounted for less than half of publicly placed securitisations. (In 2023, last full year we have data for, it represented 40%). This is substantially below what was anticipated when the label was first introduced.

The largest part of the non-STS 60% is taken by managed CLOs – currently the largest asset class in publicly placed true sale securitisation – buy-to-let residential mortgage-backed securities and some commercial mortgage-backed securities. Generally, CLOs and CMBS cannot be STS. Buy-to-let RMBS can (and sometimes is) but most issuers, for a variety of reasons, elect not to get the label.

Near all publicly placed transactions that can get the STS label (with the exception of buy-to-let transactions) get the label. So, achieving the label is not an issue. Since the STS rules were designed to enshrine existing "best practices" in the pre-GFC European market, rather than create a new higher standard, the ease with which most originators were able to conform to the new standards is unsurprising.

The fact that a relatively small proportion of the market consists of STS is therefore not driven by the difficulties of achieving the label but by the relative unattractiveness of the type of transactions that are STS compared, on the one hand to non-STS transaction and, on the other hand, to other non-securitisation instruments.

We attribute this relative unattractiveness to the unnecessary and excessive additional costs imposed by regulation on the market and the way in which these disproportionally impact STS transactions. These costs derive from:

- additional and unnecessary capital imposed on banks and insurance companies for holding STS securitisations
- the lack of risk sensitivity of the floors under CRR that favour the securitisation of riskier assets
- the unnecessarily large haircuts imposed on STS issuance in bank liquidity coverage pools, compared to non-securitisation assets
- the additional and unnecessary due diligence costs imposed on all investors in STS and

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- the additional cost of additional and unnecessary disclosure for which STS issuers must be compensated
- for synthetic transactions, the requirement for cash collateral

STS securitisations are the safest securitisations and encompass by-and-large the most plain vanilla of assets and plain vanilla structures. As such they are the lowest yielding securitisations.

Faced with the additional costs, investors and issuers find it difficult to make the price work for both parties. So, risk-averse investors turn to products which do not incur these additional costs (eg covered bonds) and where the lower yield is more than compensated for by the absence of such costs. More risk-prone investors turn to products which do incur these additional costs (eg CLOs) but where the additional yield more than compensates them.

STS plain vanilla transactions designed to be the backbone of a safe and deep capital market fall between these two stools laid out entirely by miscalibrated regulation.

Once these miscalibrations have been corrected, the experience of other jurisdictions (Australia, Japan, US, Canada…) strongly suggest that residential mortgages and auto-loans (both STS categories) should return to being the central drivers of the European market.

7.2. Which of the below factors, if any, do you consider as holding back the expansion of the STS standard in the EU? You may select more than one option.

- Overly restrictive and costly STS criteria
- Low returns
- **High capital charges**
- **LCR treatment**
- **Other**

Please explain.

See our answer to question 7.1. The "Other" are the due diligence and disclosure costs.

Some may be inclined to respond "Low returns". In a sense this is a correct response **BUT ONLY** be reference to the costs and not in absolute terms – otherwise no investor would ever buy Swiss government debt. Returns are always compared to risk and costs.

As third-party verification agents who have verified over 630 STS transactions to date, we can attest that the STS criteria are not costly to achieve nor overly restrictive for those transactions that by consensus market participants agree should be STS. This does not mean that some criteria cannot be loosened or clarified as they are over 100. But these cause only very marginal problems. They certainly do not have a material or even noticeable effect of the operation of the STS framework as a whole.

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STS criteria

7.3. How can the attractiveness of the EU STS standard be increased, for EU and non-EU investors?

- By fixing the miscalibration in the capital requirements for bank investors especially in senior STS positions
- By paying close attention to the differential between STS and non-STS capital requirements so that a sufficient gap is maintained to reflect the robustness of the former
- By reducing the haircuts for senior STS positions in banks' liquidity coverage ratio pools
- By removing the cliff-effect in the LCR rules that require removing senior STS positions that lose their AAA
- By fixing the miscalibration in the capital requirements for insurance investors in STS positions (both senior and junior)
- By making mandatory due diligence requirements proportionate and reflective of the lower risk (all other things being equal) of STS securitisations (and especially senior positions of STS securitisations)
- By allowing investors to delegate their due diligence of the STS status of potential investors to regulated independent third-party verification agents
- For non-EU investors, by engaging with other jurisdictions for an adoption of the Basel STC standard on a basis of close alignment to the European STS standard
- For synthetic transactions, by allowing unfunded positions to be STS

7.4. In the case of an unfunded credit protection agreement where the protection provider provides no collateral to cover his potential future liabilities, should such an agreement be eligible for the STS label, to facilitate on-balance-sheet STS securitisations?

- **Yes**
- No
- No opinion

7.5. If you answered yes to question 7.4., what safeguards should be put in place to prevent the build-up of financial stability risks arising from the provision of unfunded credit protection?

• The protection provider should meet a minimum credit rating requirement.

• The provision of unfunded credit protection by the protection provider should not exceed a certain threshold out of their entire business activity.

• **Other**

Please explain.

This is another case where a rule appears only to apply to securitisation even though there is nothing specific about the risk being in a securitisation format that differentiates it from identical risks elsewhere in the prudential regulatory framework.

The capital framework acknowledges that banks run counterparty risks. They do this in a variety of guises, such as swaps, repos, liquidity lines, etc… These risks are quite properly accounted for in the CRR and require capital to be set aside to cover them.

If a bank enters into an unfunded synthetic SRT securitisation, it takes the risk that the protection seller will not honour its contractual obligations to compensate the bank for losses on the pool. This risk is fully accounted for in the CRR framework. The bank must allocate capital to this counterparty risk: for a AAA/AA rated counterparty, a 20% capital requirement is imposed.

But one should note that the capital requirements for the bank holding the senior tranche of a non-STS synthetic do not vary depending on whether the securitisation is cash collateralised. The "penalty" for lack of collateralisation is the counterparty risk capital requirement referred to above.

Therefore, it logically follows that the reduction of capital for STS senior tranches is not a function of collateralisation. If it were, capital requirements would have to be different for non-STS senior tranches based on the existence or not of collateralisation. It is not. The counterparty risk capital requirement is treated by the system as sufficient, in and of itself, to account for the additional risk of an uncollateralised position.

Therefore, there is no logical or defensible reasons why non-collateralised synthetic senior tranches could not be STS. The reason for the better capital treatment of STS synthetics, as demonstrated, is unrelated to the existence of collateralisation.

To write of the risks to financial stability, in this context, is therefore odd. The risk to financial stability from counterparty risk is real but it is accounted for in the counterparty capital framework. This is as true of synthetic securitisations as it is of swaps, credit insurance, repos, etc… So, either one believes that the current counterparty risk rules work to allocate appropriate capital to counterparty risk whatever its form and therefore there is no reason to single out synthetic STS securitisations. Or alternatively, one does not believe the current counterparty risk rules work to allocate appropriate capital to counterparty risk in which case there is urgent need to reform the general counterparty risk rules. But again, there is nothing about STS synthetics that singles out this product.

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Our suggestion is merely for an internally coherent set of capital rules that allocate the same amount of capital in the system for the same quantum of risk. Anything else will lead to regulatory arbitrage and, definitionally, the misallocation of capital in the system.

In addition, the requirement for funding synthetic securitisation in order to obtain STS, is a disincentive for AAA/AA insurance companies from taking on risk removed from banks. Since removal of risk from the banking system is a policy goal, it appears odd that the framework should encourage this activity to be done by funds (often from the US) and discourage it from being done by highly regulated and prudentially supervised European insurers. One would have thought that these are precisely the types of entities that policy makers would wish to see involved in this market.

7.6. What would be the implications for EU financial stability of allowing unfunded credit protection to be eligible for the STS label and the associated preferential capital treatment?

None, unless counterparty risk rules generally are incorrectly calibrated in which case we need to revise the counterparty risk rules, not the securitisation rules. See our response to question 7.5.

7.7. How would allowing unfunded credit protection to be eligible for the STS label and the associated preferential capital treatment impact EU insurers' business model of providing credit protection via synthetic securitisation (for example, would EU insurers account for such transactions as assets or as liabilities)?

Please explain your answer.

Currently, it is our understanding that insurance undertakings prefer to write synthetic securitisations as insurance contracts located, for regulatory purposes, on the liability side of their balance sheet rather than as guarantees, swaps or credit linked notes (the traditional forms of synthetic securitisations) located on the asset side of their balance sheet. This we are informed is because the capital requirements for the two alternatives are widely different and favourable to the former.

The rules to achieve SRT being very extensive and prescriptive, we have further been informed by lawyers that the contractual terms of both types of insurance backed synthetic securitisations are identical.

Solvency II provides for substantially different capital requirements, although it has the exact same credit risk for the tranche, the loss risk linked to realising the tranche only exists on the asset side of the insurance company. This is prima facie problematic.

Allowing for unfunded synthetics to be STS would not change this dynamic: insurance companies would still have an incentive to write synthetic protection in insurance form on the liability side of the balance sheet.

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What would change is that this synthetic written in the form of an insurance contract would now be eligible for STS treatment. This would remedy the illogical outcome of the current rules for bank issuers holding the senior piece. They could then calibrate their capital requirements at the correct STS level. (See our response to question 7.5).

Since insurers are big providers of credit protection, the lower capital requirement for the retained senior tranche would make more transactions "work" in terms of pricing.

Currently, a bank seeking synthetic SRT will calculate the viability of the securitisation in the following manner:

[A] **Before securitisation**

Pool A

Cost of pre-securitisation capital per annum for Pool A = X

[B] **After unfunded securitisation (AA insurance counterparty)**

Cost of interest/premia per annum on securitisation mezzanine/first loss tranche = Z1

Cost of counterparty risk capital requirement = Z2

Cost of capital for the retained senior tranche = Z3

If $Z1+Z2+Z3 < X$ the transaction makes sense

If unfunded STS is allowed, then Z3 becomes lower as CRR allows for lower capital requirements for STS. With Z1, Z2 and X remaining the same, more deals become possible.

Another component of the analysis is that, in a *funded* securitisation Z1 can also be broken into two components

Z1a = remuneration for the risk taken by the protection seller (equivalent to the "interest rate" on a traditional bond

Z1b= cost to the protection seller of funding the cash collateral

So Z1= Z1a + Z1b

By allowing unfunded securitisations to be STS, you add Z2 – which does not exist in a funded transaction – but you lower not only Z3 but also Z1.

By allowing unfunded synthetic STS, the European banking system's capacity to manage and recycle overall capital with positive impacts on their lending capacity is increased. This would be achieved with no increase in systemic risk (as to which see our responses to questions 7.5 and 7.6)

7.8. If you are an originator, what impact on the volume of on-balance-sheet securitisations that you issue do you expect to see if unfunded credit protection becomes eligible for the STS label and the associated preferential capital treatment?

7.9. If you answered no to question 7.4., do you see merit in expanding the list of eligible highquality collateral instruments in Article 26e(10) to facilitate on-balance-sheet STS securitisations?

- Yes
- No
- No opinion

7.10. If you answered yes to question 7.9., which high-quality collateral instruments should be added to the list?

7.11. What would be the implications for EU financial stability of extending the list of high-quality collateral arrangements under Article 26e(10)?

7.12. Do the homogeneity requirements for STS transactions represent an undue burden for the securitisation of corporate loans, including SMEs? Please explain your answer.

The key word is “undue”.

The current rules allow pools to be deemed homogeneous of all assets in the pools are all either:

- Micro, small or medium sized entities OR (b) larger entities

or

- All in the same jurisdiction

In addition, they must have been underwritten on the same approach and serviced according to similar procedures (as per the RTS).

Homogeneity is a very important part of the simplicity requirement of STS.

To loosen the rules would require either pools of assets underwritten through different approaches and/or serviced by different procedures and/or mixing large and small corporate borrowers and/or borrowers from different jurisdictions (and therefore subject to different enforcement and insolvency regimes).

None of these options appear to us to preserve homogeneity and thus the simplicity requirements of STS.

We understand that this is frustrating for originators seeking to do multi-national pools or mix companies of wildly different sizes in the pools. But standards cannot be so inclusive as to allow everything. In our view, the current rules are a burden but we do not view it as “undue”.

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7.13. Should the STS criteria (for traditional, asset-backed commercial paper (ABCP) or on-balance sheet securitisation) be further simplified or amended? Please explain your answer and provide suggestions.

- **Yes**
- No
- No opinion

Broadly, we believe the current criteria function well. There are a few criteria though that should be clarified or modified.

- **First payment**

  The first payment requirement is an anti-fraud provision. Most fraudsters obtaining money from lenders by deception pay the first instalment. But the rule – as interpreted by the EBA – requires the first payment to have been made *on the securitised exposure*. This makes no sense where the securitised exposure is a loan to a person or entity that is known to the lender and is paying on other facilities. This is a particular problem for SME lending where the SME may not have made a payment on the securitised loan but holds banks accounts and pays under other facilities with the lender. It also is a problem with the product known as "salary loans" where the repayment comes from the borrower's employer.

- **Time call for on-balance sheet securitisations**

  The WAL calculation for long dated loans should be as set out in the CRR. Also, the requirement to calculate the WAL on an assumption of no prepayments is unreasonable and in practice eliminates certain asset classes. Conservative assumptions for pre-payment rates can be substituted without creating any additional systemic risks.

- **Eligible securities rules for on-balance sheet securitisations**

  These are unnecessarily onerous, and entirely uneconomic. There are in practice impossible to meet leading originators to issue credit linked notes where the issue does not arise.

- **Cash flow model requirement for on-balance sheet securitisations**

  This is a requirement that was transposed from the traditional true sale securitisation rules. There it is an essential part of the credit analysis. In on-balance sheet securitisations, cashflows play no role whatsoever. Currently, cash flow models are generated for the sole purpose of "ticking the STS box" and ignored by all participants. It is an unnecessary cost that should be eliminated.

- **Noteholder meetings provisions for on-balance sheet securitisations**

  This is another transposition from traditional true sale rules. It requires that provisions be inserted in the documentation to regulate the calling and management of investor meetings. It should be disapplied where, as is usually the case, there is only a single protection seller/investor.

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Third-Party Verifiers (TPVs)

7.14. On a scale of 1 to 5 (1 being the least valuable), please rate the added value of TPVs in the STS securitisation market. 1 / 2 / 3 / 4 / 5

Please explain.

It is not appropriate for PCS as a TPV to rate our value to the market.

However, we would make some points. At the time of filing this response, we have verified 630 STS transactions. Five years after the introduction of the standard one would expect that verification would be routine: almost a rubber-stamping exercise since all market participants would now be so familiar with the rules and interpretations. This is not only not the case, but it is very far from being the case.

To this day we have yet to see a verification procedure where we have not sent back a checklist with objections. Often these are few, especially on repeat transactions. But recently a checklist was sent back with negative comments on close to 50% of the criteria.

The fact that STS can still remain subject to discussion and, in many cases, arguments can be attributed to a number of things:

- There are still new entrants amongst originators including from new jurisdictions (and if the securitisation market grows one would expect many more)
- There are still new asset classes being brought to market or new versions of existing asset classes which raise new STS issues (and this will continue as finance innovates eg solar panel loans)
- Market participants are continuously optimizing structures often raising new STS issues
- Market participants seek to improve the return for originators by "pushing the envelope" with sometimes extremely thin justifications as to why their new "interpretation" of the STS criteria meets the legal requirements of the SECR and we are required to push back often quite forcefully by refusing to accept their proposition or insisting that they seek a green light from a regulatory authority.

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7.15. If you answered yes to question 4.10.(iv), should the TPVs be supervised to ensure that the integrity of the STS standard is upheld?

- **Yes**
- No
- No opinion

Please explain your answer to the above, including where necessary whether TPVs should be supervised at EU level.

As a TPV this question leaves us perplexed as it suggests that we are not "supervised". Following our authorisation by the French Autorité des Marchés Financiers (AMF) we have been placed under the oversight of the AMF's supervision group. We are requested to attend regular meetings in which we are asked to respond to questions on how we meet the regulatory requirements set out in article 28 of the SECR.

So, we do believe that supervision of TPVs is essential. That essentiality would be increased further if investors were allowed to delegate their obligations to verify the STS status of securitisations to TPVs. But we point out that, for PCS, supervision exists. (It also exists in the United Kingdom, where our UK company is authorised and, as in France, under the oversight of the FCA's supervisory division. As in France, this supervision involves regular meetings where we are quizzed on our practices, procedures and control functions as well as on our financial capacity to perform the regulated task).

As to the appropriate level for supervision, this strikes us as a matter of policy rather than effectiveness and one on which we have no views.

7.16. To what extent would supervision of TPVs increase the cost of issuing an STS securitisation?

- To a large extent
- To a moderate extent
- Limited or no effect
- **No opinion**

Please explain your answer, and if available, estimate the total costs in EUR

It is impossible to answer this question without an understanding of the nature of the supervision and any fees levied by the supervisory authority.

By definition, the continuation of our current supervision would not add any costs to running PCS or, consequently, to our fees.

We do point out that PCS is a not-for-profit body with almost non-existent margins and so any additional costs would most likely have to be passed on *in toto* to originators.

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8. Securitisation platform

8.1. Would the establishment of a pan-European securitisation platform be useful to increase the use and attractiveness of securitisation in the EU?

- **Yes**
- No
- No opinion

8.2. If you answered yes to question 8.1., which of the following objectives should be main objective(s) of the platform? You may select more than one option

- **Create an EU safe asset**
- Foster standardisation (in the underlying assets and in securitisation structures, including contractual standardisation)
- Enhance transparency and due diligence processes in the securitisation market
- Promote better integration of cross-border securitisation transactions by offering standardised legal frameworks
- **Lower funding costs for the real economy**
- **Lower issuance costs**
- **Support the funding of strategic objectives (e.g. twin transition, defense, etc.)**
- Other

Please explain how the platform could be designed to achieve the objectives that you selected in your answer to question 8.2.

We wish to clarify the nature of our answers.

In answering question 8.2 we do not list the objectives that "should" be the main objectives of a platform. This list will flow from high-level policy choices. It is not for PCS to express views on the desirability and trade-offs involved in such policy goals. This is very much an area for the democratically elected representatives of the European peoples.

We did answer the question of which of these policy goals, should they be selected, are amenable to being advanced by a platform.

A platform can create an EU safe asset. But to be a unified, homogeneous EU safe asset (similar to a US treasury bill), the issuance from the platform must have a singular AAA, pan-European guarantee. This can be a new guarantee of the bonds issued, a guarantee of a new vehicle set up for the purpose (like the guarantees that stand behind Fanny Mae in the US) or an issuance by an existing AAA guaranteed entity such as the EIB.

A platform can lower the funding costs for the real economy. To do this, though, it must use some form of price subsidy. This could be some form of guarantee, a subsidy (eg

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EIB purchasing assets or bonds at below market value). Some lower funding costs could also flow from the sheer volume of issuance, if the platform is large enough. The latter is difficult to quantify but is unlikely to be very substantial in basis points.

It can lower issuance cost by providing originators with a streamlined, non-negotiable format for asset purchases.

It can support the funding of strategic objectives. But again, if it does this at market rates, it is difficult to see how a platform adds anything. For the platform to add anything it needs to operate in the same manner as set out in lowering funding costs: a guarantee, a subsidy or large volumes.

We are skeptical about standardization for a number of reasons. First, we are not sure what the benefits to Europe would be for a mortgage in Finland to have the same standard terms as a mortgage in Portugal. (It could be beneficial but only if banks across Europe were allowed to offer banking products across borders. Then it would mean that a bank in any country could offer the same product irrespective of the location of the borrower. But that is, first and foremost, a banking union issue). Also, we anticipate lively discussions around what "standard" should be chosen if different jurisdictions have, for legal or cultural reasons, different ways of lending.

Enhancing transparency and due diligence is not a proper aim of a platform. We need appropriate and effective transparency and due diligence in the European securitisation market. Either these are the same for platform or non-platform issuance or we accept that one of the two has inadequate standards.

We can see how a platform could promote better cross-border integration. But this raises the issue of homogeneity. Investors do not like non-homogeneous pools, hence the current problems with cross-border securitisations (outside the large corporate asset class). (See our response to question 12.4. Non-homogenous pools issued out of a platform will not be any more attractive. This means that to promote cross-border integration, the platform will need somehow to "homogenise" the pools. This will require some form of guarantee or support.

Another goal with which a platform could assist is in performing the role Fanny Mae performs in the US, namely providing an always available, fast and simple machine to allow banks of any size and in any location, operating in any European currency, to free capital by selling assets in a standard format. This could transform European banks' capital management flexibility.

8.3. If you answered yes to question 8.1., how would access to a pan-European securitisation platform increase the use and attractiveness of securitisation in the EU?

Our answer to question 8.1 must be qualified. A platform would likely produce a market that was different and separate from the European securitisation market. It would not therefore strictly speaking increase the use or attractiveness of the securitisation market in Europe as, more likely, create another market based on securitisation technology. The platform may be a positive development, but it is NOT a substitute for

fixing the European securitisation market by better calibrating existing regulations. The platform should also not become a distraction from the main task of getting the current market to flourish. Finally, the platform should not be designed so as to cannibalise the existing market.

8.4. Should the platform target specific asset classes?

- **Yes**
- No
- No opinion

8.5. If you answered yes to question 8.4., which asset classes should the platform target? Please provide a justification.

- **SME loans**
- Green loans (i.e. green renovation, green mobility)
- **Mortgages**
- Corporate loans
- Other

A platform is already a complex piece of financial machinery. We are extremely skeptical of the possibility to create a multi-asset class platform. From an investor point of view, it is difficult to see how such a platform could even be possible without a complete public guarantee homogenizing the credit risk. Even then, issues with different maturities and pre-payment rates and structures make this a very complex proposition. We do not believe it is an accident that all the platforms we are aware of outside Europe are single asset platforms.

Green loans are not a homogeneous asset class and so the problems referred to in the previous paragraph would apply to them. It might be possible to narrow the definition of what types of green loans to make it work but the definition needs to be very narrow.

We have not selected corporate loans because it does not strike us that large corporates find it difficult to access finance at low rates. So, we are not clear what policy goal would be met by having them as the platform's chosen asset class.

Mortgages have volumes and a fair degree of standardization even across jurisdictions. They are also extremely safe with large amounts of historical data allowing for lower risks in tranching via securitisations or in the assessment and pricing of any guarantees.

SME loans are more complex, but PCS recognizes the policy drivers that could lead to their selection.

8.6. Are guarantees necessary?

- Yes
- No
- **No opinion**

8.7. If you answered yes to question 8.6., please explain who (private or public) would provide it and how you would design such a guarantee.

8.8. What do you view as the main challenges associated with the introduction of such a platform in the EU, and how could these be managed?

It is not possible to answer that question until the purpose of the platform, its intended originator users and its intended investors have been identified. There are otherwise too many variables and too many different possible structures to ascertain the challenges.

8.9. What key considerations need to be taken in designing a pan-European securitisation platform, for such a platform to be usable and attractive for originators and/or investors?

To be very clear about (a) what is the aim of the platform, then (b) what are the incentives for the originators of assets and (c) what are the incentives for investors to utilize the platform. For this it will be crucial to identify exactly who the originators and the investors are supposed to be so as to identify precisely what the incentives for use would be.

8.10. Besides the creation of a securitisation platform, do you see other initiatives that could further increase the level of standardisation and convergence for EU securitisations, in a way that increases securitisation volumes but also benefits the deepening and integration of the market?

This question implies that the market lacks integration. We are not convinced that it does. Euro-denominated true sale public issuance is widely sold across borders. Equally, the level of standardization, taking into account the variety of asset types securitised and the different legal backgrounds of the different jurisdictions is fairly high in true sale securitisation and extremely high in synthetic securitisation.

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9. Prudential and liquidity risk treatment of securitisation for banks

9.1. What concrete prudential provisions in the CRR have the strongest influence on the banks' issuance of and demand for those types of traditional, i.e. true sale, securitisation which involve the senior tranche being sold to external investors and not retained by the originator?

As an introduction, we would counsel against a ranking of measures that will positively impact the growth of the securitisation market. We are concerned that such ranking could be used to provide a "top three" solution in the hope of achieving a proportion of the potential growth even at the cost of forsaking some of the possible upside. We emphasise that the securitisation market – like most markets – is an ecosystem. Every part of the ecosystem must play its role to the full for the system as a whole to function. Providing solutions that only allow some parts of the system to operate whilst abandoning others is most likely to result in the failure of the entire system. So fixing the capital requirements for banks without providing them a legitimate incentive to place those securitisations in their liquidity cover ratio pools will likely result in very few additional investments. Equally, fixing the capital requirements for insurers under Solvency II without fixing the capital requirements for banks will likely not lead to the growth in the market as, in the first instance, it is likely that bank purchases will provide the depth and liquidity to attract new insurance investors.

As to the response on the strongest influences, we would defer to the banks that originate and invest and will be responding to this consultation. We suspect that for the influence on bank issuance though, this is almost entirely driven by comparative pricing. From a funding side, if the bank can issue at a price that is equal to or better than competing instruments, it will do so. From a capital side, a similar calculation is made based on the cost of issuance versus the cost of the capital released. Strategic diversification will play a role but can rarely compete ultimately against meaningful pricing disadvantages.

For the banks as investors, although much is made of the capital requirements and the p factor, we believe the importance of the liquidity cover ratio pools eligibility criteria is greatly underestimated and is as important if not a more important driver of bank investment. These play, in our estimation, an important role in keeping bank investment in securitisations down. But we also refer back the our comments earlier in our answer on the market as an ecosystem.

9.2. Please explain how possible changes in the prudential treatment would change the volume of the securitisation that you issue, or invest in (for the latter, split the rationale and volumes for different tranches).

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9.3. Based on your answer to 9.1, please explain how possible changes in the prudential treatment could support the supply for and demand of SME and corporate exposure-based securitisation transactions.

We refer to our response to question 2.1 and our concerns with attempts to assist specific segments of the market. We believe these are often distortive but also, in this case, not necessary. A deep securitisation market that allows banks to manage their capital proactively and to fund at good rates will help SME lending so long as this remains a profitable business for banks. And if it is no longer a profitable business, no amount of regulatory action or SME securitisation will make it so. (In fact, that any given asset is profitable for banks originating that asset is a sine qua non of being able to securitise such asset. This is true for all asset classes).

However, we also refer back to our response to question 2.3. Removing the requirement in article 423(2) CRR for underlying exposures to meet the conditions for being assigned, under the Standardised Approach and taking into account any eligible credit risk mitigation, a risk weight equal to or smaller than 100% on an individual exposure basis would allow more SME securitisations to be STS, thus making them cheaper for investors. This would support both the demand and supply for securitisations of SME (and BB+ or lower rated corporates).

Such amendments could be done by removing the requirement for "all other exposures", or by increasing the requirement allow risk weights of up to 150%. It can also be done by removing article 243(2) entirely as its rationale is not obvious. The article appears to be another case of "just in case" gold plating, not justified by any data of which we are aware.

It always remains possible simply to add a support factor to the CRR to lower capital requirements for holdings of SME or corporate securitisations. This though is a political decision on which we express no views.

9.4. Does the prudential treatment of securitisation in the CRR appropriately reflect the different roles a bank can play in the securitisation chain, concretely the roles of originator (limb 'a' and limb 'b' of the definition of the originator in the Securitisation Regulation), servicer and investor?

- Yes
- **No**
- No opinion

9.5. If you answered no to question 9.4., please explain and provide suggestions for targeted amendments to more appropriately reflect the different roles of banks as originator, investor, and servicer.

It is difficult to answer this question without a sense of what other amendments to the CRR may be effected. The basic issue here, in our opinion, is that the current CRR

capital requirements do not take into account the fact that the bank investor in a securitisation may also be the originator of the securitised assets. This is most often the case in SRT transactions (true sale or synthetic), The problem flows from the structure of the capital calculation and the introduction of a p factor accounting for the agency risks of securitisations. Many of those agency risks usually identified by prudential regulators turn on an asymmetry of knowledge and/or a conflict of interest between the originator and the investors. For example, if the originator is the servicer, will it service securitised assets less diligently than its own assets and so lead to securitised assets suffering greater losses than non-securitised assets? When the originator and the investor are the same entity, most of these agency risks cease to exist. Yet, no adjustment exists currently to the p factor designed to account for the absence or substantial reduction of these risks.

Should appropriate adjustments be made to the p factor for STS securitisations where the application of the STS criteria has all but removed agency risks for all investors (rather than merely originator investors), the illogicality of not accounting for the removal of many of those risks due to the identity between originator and investor should resolve themselves to a very large extent. In such case, a balance should be struck between accounting for the differences between cases where the originator is the investor and where it is not, on the one hand, and on the other hand to complexity of the resulting legislation. On balance, a correctly calibrated p factor for senior STS is probably sufficient and no additional complexity should flow from the bank being both originator and investor.

(For how the p factor and floors should be approached, we refer you to our responses to the relevant questions in this section 9.)

If it proves impossible to achieve a correctly calibrated p factor for STS securitisations, then – at the very least – some adjustment should be made to account for the reduction in agency risks. One possibility would be to treat non-STS securitisations where the originating bank is the investor as if they were STS.

This would be particularly relevant for banks holding the senior tranches of synthetic securitisations. These securitisations have no agency risks relating to cash collection or the design of the distribution of cash (the “waterfall”) or the resulting cashflow models used to analyse true sale securitisations. They therefore have even fewer agency risks than true sale securitisations. As a result, the gap between the current capital required to be held and allocated to that senior tranche to reflect “non-neutrality” and the real level of “non-neutrality” is both more obvious and more extreme.

This proposal to treat non-STS transactions held by their originators as STS though is very much second best to the correct calibration of the p factor.

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9.6. Have you identified any areas of technical inconsistencies or ambiguities in the prudential treatment of securitisation in the CRR (other than the 'quick fixes' identified by the ESAs in the report JC/2022/66) that could benefit from further clarification?

- Yes
- No
- **No opinion**

9.7. If you answered yes to question 9.6., please explain and provide suggestions for possible clarifications.

9.8. Are there national legislations or supervisory practices which in your view unduly restrict banks in their potential role as investor, originator, servicer or sponsor of securitisation transactions?

- **Yes**
- No
- No opinion

9.9. If you answered yes to question 9.8., please explain and provide examples.

We are aware that a number of national central banks have indicated to banks they supervise that, notwithstanding what is allowable under the rules, they will not allow either (i) certain types or volumes of SRT transactions and/or (ii) banks to include in their liquidity coverage pools more than a certain percentage of securitisations, well below the 15% set out in the CRR.

This we hold under explicit or implicit duties of confidentiality and so do not feel we can provide further details. However, we welcome the Commission enquiring of European central banks what, if any, instructions or rules of this nature they have communicated to prudentially supervised entities.

9.10. How do banks use the capital and funding released through securitisation? Please explain your answer and if possible, quantify how much of the released capital and funding is used for further lending to the EU economy.

We leave this question to banks that are clearly better able to address it.

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Risk weight floors

9.11. Do you agree that securitisation entails a higher structural model risk compared to other financial assets (loans, leases, mortgages) due to, for example, the inherent tranching? Please explain your answer.

- Yes
- **No**
- No opinion

9.12. Do you consider that scope and the size of the reduction of the risk weight floors, as proposed by the ESAs, is proportionate and adequate to reflect the limited model and agency risks of originators and improve the risk sensitivity in the securitisation framework, taking into account the capital requirements for other financial instruments?

- Yes
- **No**
- No opinion

9.13. If you answered no to question 9.12., should the scope and size of the reduction of the risk weight floors be amended? For example, should it be extended to investors in a targeted manner (such as, for example, to investors in STS securitisations and under SEC-IRBA approaches only, to prevent discrepancies with the prudential treatment of covered bonds under the SA approach)? Or, on the contrary, should the scope be reduced to only include originators who are servicing the underlying exposures?

Please justify your reasoning.

A. To our knowledge, current floor levels (10% and 15%) are arbitrary numbers chosen for plausibility rather than derived from any data.

B. First, agency and model risks ("A&M Risks") exist. But they can and must be *enumerated* and *described*. Exactly how does a given agency risk operate and exactly what are the consequences of such risk obtaining on the credit risk of a securitisation. One cannot determine with scientific exactitude the impact in fractions of a percentage point of any A&M Risk. But without some description and enumeration, any assessment used to derive a quantum of non-neutrality (p factor) and floors becomes completely arbitrary.

   Secondly, the STS standard containing over 100 criteria was explicitly designed, over

a number of years, to remove all the A&M Risks that the EBA, the Commission and the Co-legislators could identify. Referring back to the preceding paragraph, we would invite the Commission to request from supervisory authorities an enumeration and description of A&M Risk unaccounted for in the STS standard. We do not claim there are none but only when one knows what they are can one have a stab at defining non-neutrality and floors for STS.

If one follows the EBA's approach that the great reduction in A&M Risk that occurs when the originator is the investor and also agrees that the STS standard equates to a similar reduction in risk, then there can be no reason to limitthe EBA's proposed reductions to STS securitisations to cases where the originator is the investor and extend them to all STS securitisations.

C. The current construction of the floors takes no account of the riskiness of the underlying assets.

   For example, the floor (in each case for an STS transaction) for:

   (a) a pool of BB+ corporates is 10% of its Pool RW

   (b) a pool of residential mortgages (with 80%< LTVs) is 33% of its Pool RW

   (c) a pool of consumer loans is 13.33% of its Pool RW

   Intuitively, this is illogical. It also has several unwelcome consequences. First, it disincentives the securitisation of the safest assets. The European securitisation market's possible contribution to the growth of a deep savings and investments union lies in the creation, via tranching, of very safe and understandable bonds. These are necessary to attract very risk-averse savers. So, consistent always with prudential rigour, the framework should encourage the securitisation of mortgages and consumer loans insofar as these are easily understood by retail investors

   Also, the current one-size-fits-all framework works against SME securitisations, since the floor eliminates the SME RW support factor.

   A better, more risk sensitive floor would resolve these issues.

D. The issue of non-STS securitisations is more complex.

   On the one hand, almost all European non-STS transactions currently issued are well structured. Also, the SECR introduced key provisions designed to eliminate the most problematic issues that arose with securitisations during the GFC: ban on resecuritisations, retention, transparency and mandatory due diligence.

   On the other hand, non-STS is not a "bounded" standard going from STS to another boundary. Non-STS is everything beyond STS. This leaves prudential regulation with a dilemma: to regulate non-STS transactions based on what they are or on what they could become as markets evolve and push boundaries.

   Finally, as a policy matter and a way to develop a deep savings and investment market based on safe and understandable securitisations, a proper differential

between STS and non-STS should be maintained to incentivise the former. It should be noted that this differential should take into account the actual benefit in euros of choosing STS rather than only the benefits expressed in percentages of difference. What we mean is that a floor differential of 5% is very different if the cost is €1m or €10,000. Trivially, in the first case choosing STS saves me €50,000 and in the latter case, €500. If the saving in euros is too small to compensate for the additional costs in time and money of meeting the STS standard, the regulatory framework will create an incentive to issue outside the STS standard. This runs very much counter to the policy aims of creating STS which was to have it as the bulk of the European market.

The floor for STS should be reduced to 7% in line with the EBA proposal.

The floor should be reduced to 12% for non-STS when the originator is investor.

The floors should remain at the current level of non-STS when the investor is not the originator.

The floors ***for senior tranches*** in all cases should be proportional to the Pool RW. So a 15% floor should be 15% of KA.

A very important caveat is that proportional floors only work if:

- the senior tranche has a minimum thickness. So the proportional floor should only apply where the sum of all lower rated tranches is equal to a multiple of KA. See our response to question 9.15.
- The pool has sufficient granularity (50)

9.14. Do you consider that the ESAs' proposed accompanying safeguard, with respect to the thickness of the sold non-senior tranches, is proportionate and adequate in terms of ensuring the resilience of the transactions?

- Yes
- **No**
- No opinion

9.15. If you answered no to question 9.14., please provide and explain alternative proposals to ensure a sufficient thickness of the sold non-senior tranches to justify a possible reduction of the risk-weight floor in an efficient and prudent manner.

See our response to question 9.13 as to why one should not be referring to "non-sold" tranches but to the sum of tranches below the senior tranche.

On the EBA proposal, we agree with the authors of the paper "Rethinking the Securitisation Risk Weight Floor". Although the issue of tranche thickness will always contain a considerable part of judgment rather than calibration, the EBA proposal seems very arbitrary. Intuitively, following the Bank of England's approach to tranche thickness in the context of SRT where the sum of non-senior tranches must be equal to

at least x1.5 KA appears, in the absence of hard mathematical or statistical justification, more anchored in a commonsense approach to risk.

9.16. Do you consider that the other three safeguards as proposed by the ESAs (amortisation structure, granularity and, for synthetic securitisations only, counterparty credit risk) are proportionate and adequate in terms of ensuring the resilience of the transactions?

- Yes
- **No**
- No opinion

9.17. If you answered no to question 9.16., please provide and explain alternative proposals for safeguards that would effectively ensure the resilience of the transaction and would justify the reduction of risk-weight floors.

The amortisation proposal is fine.

The granularity test is excessive – a granularity of 50 exposures (2%) is statistically sufficient. If one wished to follow the route of an excess of prudence, this could be doubled to 100 exposures (1%). However, the 200 exposures level proposed by the EBA would weight most heavily on smaller banks seeking to use their corporate/mid-cap SME loans in smaller transactions.

The counterparty risk safeguard is unnecessary and burdensome. We refer to our response to question 7.4.

9.18. If you answered no to question 9.16., as an alternative, instead of these three safeguards, taking into account the need to ensure simplicity, would it be preferable to limit the reduction of the risk weight floor to STS transactions only?

Please explain.

We note that the STS standard already contains the proposed safeguards. (Technically, the granularity safeguard is not an STS criterion but a requirement for STS transactions before they can be granted reduced capital requirements – article 243 CRR).

However, the EBA's reasoning on the reduction of A&M Risk when the originator is the investor is sound even in the context of transactions that are not STS. We refer to our response to question 9.13.

9.19. What would be the expected impact of a possible reduction of the risk weight floor on EU securitisation activity? Please explain any possible impact on different types of securitisations (traditional securitisation, synthetic securitisation), from both supply and demand sides.

A. For synthetic securitisations, we refer to our analysis in the response question 7.7. A lower floor would reduce the Z3 component of the cost, allowing for more transactions to come in below X. This is a positive impact on supply. Since currently, the demand side of the equation does not appear to be constrained, one should anticipate more transactions. Since banks are very reluctant to make public their calculations of Z and X, it is not possible for a non-bank such as PCS to assess what increase in volume such change is likely generate.

   If a proportionate floor taking into account the KA of the underlying pool were to be introduced, this would also encourage the synthetic securitisation of safer assets such as mortgages. The current low RW attributed to residential mortgages, when associated with a one-size-fits-all floor means that synthetic securitisations of that asset class are rarely competitive when compared to using corporate loan assets. The large volume of European residential mortgages – especially as a percentage of the portfolios of smaller banks in smaller economies – means that this capital management tool would become more available across Europe and across banks including smaller ones. A similar point can be made for SME lending which is a greater part of the books of smaller banks in smaller economies and where a proportional floor – preserving as it does the SME support factor – would make more such synthetic securitisations financially viable.

B. The impact on more reasonable floors on traditional securitisations will first be felt on the demand side for senior tranches. These are the tranches purchased by banks. If banks need to allocate less capital against these tranches, their threshold yield requirements will fall.

   If the amount of capital available for securitisation purchases remains the same, banks can also purchase a larger volume. This will increase investor capacity in the senior tranches. Currently, these are the tranches where investor capacity constraints are highest. In the primary market, covers for the seniors are running at x1.5/1.7 on average in 2024 (and were closer to x1/1.2 previously). The covers for junior tranches are usually x5/7 and sometimes X10.

   Greater capacity and lower yields will then feed into the supply side. Lower yields in particular will make traditional securitisation as an additional and alternative funding source for banks more viable.

   However, we must stress the notion of securitisation as an ecosystem where all the components have to work together. Just changing the floors without changes to the due diligence requirements, the p-factor, the LCR eligibility and Solvency II to attract deeper liquidity in the market by bringing in insurance investors will have a very limited effect. It will also not set up the long-term virtuous circle where more bank interest in senior tranches increases volumes and deepens liquidity, making this market more interesting to insurance companies. The build up of insurance company interest will take some time. But it will, in turn, further increase the volume and further deepen liquidity, making the European securitisation market in

senior AAA/AA STS tranches attractive to retail funds and the anchor of a European savings and investments union.

It should be further noted that maintaining a meaningful differential between STS and non-STS is important as senior AAA/AA STS tranches are the most able to anchor the savings and investments union as being most suitable for retail investors (investing through funds such as UCITS).

The (p) factor

9.20. Do you consider that the current levels of the (p) factor adequately address structural risks embedded in securitisation, such as model risk, agency risk and to some extent correlation, as well as the cliff effects?

- Yes
- **No**
- No opinion

9.21. If you answered no to question 9.20., please provide the justification, and provide quantitative and qualitative data, for whether and how the (p) factor overestimates the risks and inappropriately mitigates the cliff-effects, for specific types of securitisation exposures.

For quantitative data, we would refer the Commission to the submission of other respondents better placed to provide extensive data sets. We will deal with the qualitative aspects of our answer.

Our analysis addresses the STS segment of the market where PCS believes most needs to be done and which benefits most the aims of a deep and safe savings and investments union.

First, we refer back to paragraph [B] of our response to question 9.13 on agency and model risks ("A&M Risks").

Secondly, we note that the p factor as currently set up was the result of very little to no data calibration work and has never been the subject of any academic paper that could anchor its reliability. What little data was used was derived in large part from US GFC data, most generated by the sub-prime debacle. In this respect, it should be noted that the debacle was primarily the result of a combination of two developments: extremely bad underwriting and the multiplier effect of repackaging these badly underwritten loans in re-securitisations that concentrated risk (CDOs, CDO squareds and CDO cubed). It should also be noted that (a) no such catastrophic underwriting occurred in Europe and, arguably, could have occurred and (b) the multiplier effect of re-securitisation is now impossible as re-securitisations were banned by the SECR.

Because of the very limited use of data in calculating the p factor, the task at hand is not so much one of "re-calibrating" the p factor as "calibrating" it for the first time. In this

calibration, it will be necessary to account for all the changes that have been wrought by the SECR.

A proper calibration of the p factor for STS securitisations can proceed from two mutually supporting approaches: one conceptual, the other data based.

The conceptual approach is outlined in paragraph [B] of our response to question 9.13: STS securitisations were designed to remove A&M Risk. Therefore, one would expect the non-neutrality created by the p factor to account for A&M Risks to be very low (if existent at all) in the case of STS securitisations.

Crucial to understanding the data-based approach, the STS standard was not designed to create a new, higher standard than existed in well structured pre-GFC European securitisations. On the contrary, the STS standard codified “best practices” of the European pre-GFC true sale securitisations. As a third-party verification agent, PCS is extremely familiar with the 100 plus STS criteria. Not a single one is novel. Not a single one departs from features familiar to virtually all simple, “plain vanilla” true sale securitisations in the classic asset classes both before and after the GFC .

It follows from this that those traditional pre-GFC European securitisations are extremely good proxies to gauge the credit strength of STS securitisations. We believe the onus lies with those arguing that data analysis through the credit cycle cannot be performed for STS securitisations because the standard has only existed since 2019 to point to any STS criterion that was not routinely present in those pre-GFC transactions. (Incidentally, even if such criteria could be identified, this would make the proxy data argument even stronger rather than weaker, since any such additional criteria would presumably be improving elements indicating that STS credit performance is likely to be even better than that of pre-GFC traditional securitisations.)

We believe the p factor can be calibrated for STS on the data not just through the economic cycle but through the greatest financial shock since the 1930s. We are confident that this will generate a p factor that is very small. This is what we meant when we wrote that a conceptual and a data based approach are mutually supporting: the conceptual approach (STS is designed to eliminate A&M Risks) suggests a very low p factor; the data will confirm this by producing a negligeable difference between pool PD/LGD numbers and securitisation (all tranches) PDs and LGDs.

This still leaves issues of cliff effects and the shape of the RW distribution curve (the “half-pipe”) which will be addressed in our responses to subsequent questions.

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9.22. Do you consider that potential targeted and limited reductions to the (p) factor may increase securitisation issuance and investment in the EU, while at the same time keeping the capitalisation of the securitisation tranches at a sufficiently prudent level?

- **Yes**
- No
- No opinion

Please explain your answer.

Senior tranches, especially in STS, are extremely safe and highly rated (AAA or AA). As such they are also low yielding but extremely liquid. Being low yielding, they are not broadly speaking very attractive to funds. Being extremely liquid, they are attractive as "cash equivalent" securities for institutions that need such type of liquid assets. In Europe today, the primary institutions that have need of pools of such assets are first banks, then insurance and pension entities.

(It is worth noting that in the United States, funds do buy a very large portion of safe securitisations. This though is a consequence of the extremely deep capital market investing large amounts of risk-averse retail funds. In Europe, such risk averse retail cash remains in bank accounts. Mobilising this cash via a savings and investment union is a key reason to reform the European securitisation regime. But such mobilization requires a deep enough market whose growth can only realistically be kick-started by banks investing more in senior STS AAA/AA tranches. This is the virtuous circle referred to in the penultimate paragraph of our response to question 9.19.)

Today, in true sale/traditional securitisations, placing the senior tranche is the main limitation to increased volumes. (We refer to our comments on cover rates in our response to question 9.19).

The arguments for how a lower p factor helps grow the market are the same as for how a lower floor under CRR can do so. So we refer to our response to question 9.19 more generally.

On maintaining a prudent level of capitalization within the European financial system, we stress that we strongly believe that a lower p factor (especially for STS transactions) is fully justified by the inherent risks of the products. In other words, the advocacy for a lower p factor is not a request for a politically motivated reduction. It is not predicated on "trading" systemic safety for a politically desirable goal such as the growth of a savings and investments union or the strengthening of European banks global competitiveness. Those two things may flow from the necessary reforms of the securitisation framework. But the reforms are "necessary" to ensure that the current rules are proportionate to the actual risks embedded in European securitisations.

We also draw your attention to the two last paragraphs of our response to question 9.19 on securitisation as an ecosystem and the importance of STS/non-STS differentials. These points as equally valid in respect of any changes to the p factor.

9.23. If you answered yes to question 9.22., what criteria should be considered when considering such targeted and limited reductions? You may select more than one option.

- Exposures held by originators versus investors
- Exposures in STS versus non-STS securitisations (beyond the differentiation already provided for in Article 260 and in Article 262 CRR)
- Exposures in senior versus non-senior tranches
- Exposures calculated under different capital approaches
- Other criteria

Please explain your answer

We are not sure we entirely understand the question.

9.24. As regards your answer to 9.22., please provide quantitative and qualitative data on the likely impact of possible targeted and limited reductions to the (p) factor as investigated above, in particular how such targeted reductions would avoid cliff effects and undercapitalisation of mezzanine tranches and, how they would not create incentives for banks to invest in mezzanine tranches.

We refer to our answer to question 9.28 on cliff effects and the undercapitalization of mezzanine tranches.

Additionally, in the same way we do not believe that the lowering of the p factor should be driven by political aims at the expense of prudential considerations (see response to question 9.22) we also do not believe that achieving political aims should be a reason not to proceed with achieving a p factor that accurately reflects systemic risks.

A correctly calibrated capital regime is, in and of itself, a public good. A capital regime covering multiple instruments incorrectly calibrated will *invariably* result in regulatory arbitrage and the buildup of systemic risks. Therefore, even if a correctly calibrated p factor were to create incentives for banks to invest in mezzanine tranches, forsaking such correct calibration would result in the continuation of the current regulatory arbitrages and misallocation of capital.

However, we believe this point is moot. The reasons banks are the natural buyers of senior securitisations is because of their need for highly liquid, highly safe cash equivalent securities. This need is driven by banks' need for repo collateral and assets for their liquidity coverage ratio pools. Mezzanine tranches are not eligible for LCR pools and for central bank repo and, so far as we are aware, not used in private repo activity. Therefore, even a lower capital requirement for mezzanine tranches is very unlikely to result in much if any additional purchases, so long as the LCR and central bank rules stay as they are. We do not advocate allowing mezzanine tranches to be eligible for LCR pools.

9.25. As regards your answer to 9.22, please provide the data on how they would have a positive impact on the issuance of securitisation, the investments in securitisation, and the placement of securitisation issuances with external investors, for different types of securitisations (traditional securitisation, synthetic securitisation).

We do not have such data. We are also not certain anyone has data of this kind. Capital markets' supply and demand dynamics are extremely complex depending on too many variables (rates, monetary policy, funding needs, market sentiment, international developments, underlying economic activity, etc…). Therefore, any data on the positive impact on any specific regulatory change to the securitisation regime is bound to be entirely speculative.

We would make a number of points though:

- A properly calibrated capital regime is a public good. (See our response to question 9.24).
- Markets are ecosystem, so meaningful positive impact will likely result in multiple inter-locking reforms. We strongly urge the Commission not to follow a line of reasoning that "adds" the possible gains of reforms: if a lower floor produces a potential increase in the market of 10% and a halved p factor an increase of 10%, then if we lower the floor and take 25% off the p factor we will get (10% + ½.10%) = 15%. This is not how ecosystems work.
- Although we cannot have any certainty of growth in the European market, we can derive some inference from the much greater use of securitisation in jurisdictions with better calibrated and proportionate regulatory regimes.

9.26. Do you consider that the current approach to non-neutrality of capital requirements as one of core elements of the securitisation prudential framework, leads to undue overcapitalisation (or undercapitalisation) of the securitisation exposures, in particular when compared to the realised losses and distribution of the losses across the capital structure (different tranches of securitisation) over a full economic cycle?

- **Yes**
- No
- No opinion

Please explain your answer.

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9.27. If you answered yes to question 9.26, please justify your reasoning and provide quantitative and qualitative data to show the extent of the undue non-neutrality (overcapitalisation or undercapitalisation), in particular when compared to the realised losses and distribution of the losses across the capital structure, taking into consideration the need to cover a full economic cycle.

A. Qualitative

In a 2014 paper, the EBA analysed the causes of the extremely poor performance of some (almost entirely US) securitisations. In particular, four sources of weakness were identified:

- The originate to distribute models with no "skin-in-the-game" for originators
- Model risks deriving from using models-on-models (a feature of re-securitisations)
- Lack of transparency
- Internal refinancing risk

The first three were addressed by the SECR via, in order, mandatory retention (article 6), a ban on re-securitisations (article 8) and mandatory disclosure standards (article 7). The final one was not banned but was excluded from the STS standard (article 20.13).

In the case of STS, the SECR went much further, creating a product with almost no or no A&M Risks.

However, the p factor of one, reflecting a 100% non-neutrality, and based on pre-SECR analysis was never revisited for non-STS. If this is the correct approach, it would be a statement that key provisions of the SECR had no effect whatsoever in improving the risk characteristics of securitisations. Not only would such conclusion be deeply depressing, it is also implausible.

For STS, despite the removal of all or near all A&M Risks, the p factor was halved somewhat arbitrarily. This still leaves a 50% non-neutrality. As to the implausibility of this outcome, we refer to our responses to question 9.13 (specifically paragraph [B])

B. Quantitative

We will leave the provision of data to other respondents but the numbers are well known. We refer you to the data appearing in the Joint-Committee report of 2022 (Section 2.4); Fitch Ratings, "Global Structured Finance Losses: 2000-2020 Issuance", (March 2021); AFME's : "One-year average default comparison: US – EU issuances since 1973" and many others.

We also believe that extremely good data, not just through the economic cycle but through the GFC exists for securitisations meeting the STS standard. (See our response to question 9.21)

9.28. Based on your answer to 9.26., do you consider that alternative designs of the risk weight functions, such as an inverted S-curve, or introducing a scaling parameter to scale the KA downwards, within the current halfpipe design, as investigated in the Section 3.3.2 of the EBA report, have potential to achieve more proportionate levels of capital non-neutrality and capital distribution across tranches, address the potential cliff effects more appropriately and achieve prudential objectives?

- **Yes**
- No
- No opinion

Please explain your answer.

9.29. If you answered yes to question 9.28, please specify the impact of such alternative design compared to the existing risk weight functions and explain an appropriate calibration of such alternative designs and possible safeguards for the measures to achieve prudential objectives.

We broadly agree with the analysis set out in the Joint Committee report of 2022 on the problems flowing from the design of the p factor.

First, the p factor is a single number performing three functions:

- Distribution of capital across tranches
- Non-neutrality
- Smoothing of cliff-effects

Not only is p doing two things in setting non-neutrality and smoothing cliff-effects but, as acknowledged by the EBA, these are in a relationship that generates a see-saw effect: any reduction of p to reflect objectively the lower risk of securitisations (the non-neutrality aspect) steepens the curve and generates more pronounced risks to financial stability (the cliff-effects).

The shape of the curve and particularly the steepness of the fall after the “table” also generates, especially for some asset classes, concerns over undercapitalization for mezzanine tranches at certain attachment and detachment points. By itself, steepening the curve by reducing p will likely result in increasing this problem of mezzanine undercapitalization.

We also agree with the EBA’s analysis that the length of the “table” in the half-pipe construction (currently at KA) does not reflect reality for any granular pool securitisations. Set at 1250%, it assumes an immediate 100% PD and LGD up to Kpool upon first euro loss.

These problems make solutions that simply reduce arbitrarily the p factor somewhat unworkable.

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However, the solution lies in splitting p to reflect the two functions (smooting and non-neutrality) that it plays.

The first number (q) would determine the conditions setting out the length of the table. Currently at KA, the length of the table should be (qxKA) where q is a number below one.

The calibration of q would not be based on some arbitrarily selected number. It would be derived from the analysis of the GFC and post-GFC data.

As with the current p factor, there should be two q factors: one for STS transactions and one for non-STS transactions.

In the case of STS securitisations, data from pre-GFC and post-GFC traditional European securitisations would form the basis of this analysis. This would result in a q falling out naturally from the data and therefore reflecting the actual, documented non-neutrality of STS securitisations. (We refer to our response to question 9.13 paragraph B and 9.21)

The second number, p should continue to be a component of the SSFA and will continue to play its current role in determining the steepness of the curve. Whether p should remain at 1 or additional calibration work should be conducted is a matter which should be left to the EBA working with stakeholders. We have seen the draft version of a paper which will, we believe, provide a very solid basis for such work and the publication of which is expected very soon.

The alternative approach of using a scaling factor to reduce KA for the purposes of calculating the curve would certainly ameliorate the situation. But it suffers from the limitation that it only works for SEC SA. The splitting of p into two also works for SEC IRBA. If the scaling factor approach were to be chosen, the appropriate level of the scaling factor should also be derived from the data. It should not be fixed arbitrarily. We have, for example, seen proposals for a scaling factor of 0.65 for STS (equivalent to a 30% non-neutrality). This is better than the current level but remains an arbitrary number unlikely to reflect the correct level of capitalization (on the upside or downside) other than by sheer luck.

Significant risk transfer (SRT)

9.30. Do you agree with the conditions to be met for SRT tests as framed in the CRR (i.e. the mechanical tests - first loss and mezzanine tests, and the supervisory competence to assess the commensurateness of the risk transfer, as set out in Articles 244 and 245 of the CRR)? Are the SRT conditions effective in ensuring a robustness and consistency of the 'significant risk transfer' from an economic perspective?

- **Yes**
- No
- No opinion

Please explain your answer

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9.31. If you answered no to question 9.30, do you consider that the robustness and efficiency of the SRT framework could be enhanced by replacing the current mechanical tests with the PBA test?

The PBA test could be based on the recommendations in the EBA report, while the recommendations on the allocation of losses to the tranches could be reconsidered.

Although we responded “yes”, we felt it important to comment on a few things.

First, although the approach suggested in the EBA’s December 2020 SRT Report is broadly acceptable, it should be the subject of consultation and discussion with stakeholders so that the details can be refined. We note that this process has not taken place.

Second, although the proposals are broadly acceptable, one aspect is not. The proposed distribution of loss allocation, especially for quickly amortising pools, makes no sense. The quantum of back ending is factually unreasonable. It will result in attachment and detachment points generating a disproportionately thick protection tranche compared to the actual risk. It will also damage the capacity of banks to manage proactively their capital positions. This in turn will damage the European Union’s capacity to fund its economy.

Finally, we support the proposal of the EBA to test transactions for SRT compliance only on inception. Any other approach would be illogical since it would likely require additional capital precisely to cover the risks for which the “insurance” had been obtained from the protection sellers. It would also result in volatility that would undermine financial stability.

9.32. Do you consider the process of the SRT supervisory assessments to be efficient and adequate?

- Yes
- No
- **No opinion**

Please explain your answer

This is a question best answered by market participants who interface directly with the supervisors. We are aware that a working group exists to streamline the assessment process and suspect that it may well impact possible responses to this question.

9.33. If you answered no to question 9.32., please provide justifications and suggestions how the SRT assessment process could be improved further.

9.34. Should the process of the SRT supervisory assessments be further specified at the EU level (e.g., in guidelines, based on a clear mandate in Level 1), or should it be rather left entirely to the competent authorities to set out their own process?

- Yes
- No
- **No opinion**

Please explain your answer

We refer to our answer to question 9.32

9.35. If you answered yes to question 9.34., please provide suggestions.

9.36. If you are a supervisor, how would a change in the SRT regulatory framework (in particular on the SRT tests and the process of SRT supervisory assessments) impact your supervisory costs?

Transitional measure in Article 465(13) of the CRR

9.37. Do you consider that the transitional measure will remain necessary and should be maintained, in case of introduction of other changes to the prudential framework?

- Yes
- No
- **No opinion**

9.38. If you answered yes to question 9.37., please explain why and whether there are any alternative measures that could be more appropriate to achieve the original objective of the transitional measure.

We answered “no opinion” since whether there is a continued need to maintain the provisions of Article 465(13) will entirely depend on the course adopted with regards to reforming the current miscalibrations of bank capital requirement.

Should either of the proposals outlined in our response to question 9.29 (dual p’s or scaling factors) be adopted with an appropriate reduction of the non-neutrality of the current framework, then the transition measure should no longer be needed. In the alternative, if no reforms are effected or the reforms preserve excessive non-neutrality, then the transitional measure will continue to be necessary, since the issue that it was designed to address will remain.

9.39. If you answered yes to question 9.37, do you consider that a potential targeted and limited reduction of the p-factor might affect the effectiveness of the transitional measure under the output floor?

- **Yes**
- No
- No opinion

Please explain your answer

See our response to question 9.38

Liquidity risk treatment in the LCR Delegated Regulation

9.40. Does the liquidity risk treatment of the securitisation exposures under the LCR Delegated Regulation have a significant impact on banks' securitisation issuance and investment activities and on the liquidity of the securitisation market in the EU?

- **Yes**
- No
- No opinion

9.41. As regard to your answer to 9.40., please explain the impact on banks' issuance of securitisation, investment in securitisation, and relative importance of the liquidity treatment under the LCR in the activity of the primary and secondary securitisation markets.

For reasons set out in our response to 9.22, in the first phase of the building out of a deep and safe savings and investment union, banks play a crucial role through purchasing senior AAA/AA tranches of STS securitisations. Today, the largest constraint on the future growth of the European securitisation market is the narrow base of demand in the senior tranches. See our response to question 9.19.

One of the main reasons why banks need "cash equivalent" securities is to have repo collateral and to meet their LCR obligations. Two main reasons limit the banks' current appetite to place securitisations in their LCR pools.

First, the distortive effect of the regulatory framework on costs. The high haircuts set out in the LCR rules for securitisations mean that banks need to purchase a higher face value of securitisation than of other instruments to deliver the same LCR impact. This "extra" nominal value has a funding cost and a capital cost. Here, the additional unwarranted non-neutrality adds a second layer of distortion. This second layer means

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that for the same low risk, the bank will need to allocate more capital than for other instruments and is warranted by the risk of the extremely safe instruments allowed in the LCR pools.

We have no figures for the quantum of these additional costs since they vary from bank to bank depending on their funding cost and cost of capital. These are not usually public. But we suggest that the Commission poll banks to ascertain the quantum of these extra costs. We are aware, through private conversations of two large banking entities which told us that their additional costs were respectively 8bp and 12bp. In other words, these banks needed an extra 8bp and 12bp yield on a securitisation compared to e.g. a similarly rated covered bond to reach the same financial result. But the allowable instruments are only AAA senior tranches of RMBS/Auto/SME/Consumer STS securitisations with less than 5 years WAL. In other words, the type of instrument so safe that they suffered zero losses in any EU jurisdiction throughout the GFC. So, originators are not usually prepared to pay higher yields to issue such instruments especially when they can issue other instruments at lower yield which investing banks are prepared to purchase for their LCR pools since those instruments do not labour under the same constraints.

The second reason banks are reluctant to purchase securitisations for their LCR pools is that only AAA instuments are allowed. This creates a cliff effect for banks wishing to use such instruments. Should a AAA securitisation in their LCR pool be downgraded even slightly to AA+, they would have to immediately replace it with some other asset. They would then either be left with the downgraded bond that they could not use for LCR and was otherwise a low yielding useless drag on their balance sheet or sell it in adverse circumstances (ie immediately after a downgrade).

It should be noted that such downgrades do not even need to proceed from a deterioration of the securitisation included in the LCR pool. Even if the securitisation continued to perform with excellence, it could be downgraded as a result of a sovereign downgrade because of the operation of rating agency sovereign caps or as a result of a change in methodology, being applied retrospectively by CRAs. These types of downgrade, unconnected to the performance of a given securitisation, are even more dangerous for a bank holding a meaningful stock of such transaction in its LCR pools since they are likely to affect whole categories of securitisations that would have to be sold. No such rating requirement apply to covered bonds which can slide down the rating scale triggering only an increase in haircuts.

These factors (price distortion and cliff effect risks) are the primary reasons banks do not use securitisations for their LCR pools (together with lack of supply – see our response to question 9.49). They are both artefacts of the regulatory regime. Considering the aggregate size of LCR pools and the extremely small amount currently held in securitisation, potential growth of the senior AAA STS investor base from changing these rules is very substantial.

An additional element also shrinks the universe of securitisations eligible for the LCR pools: the 5-year limit on maximum weighted average life ("WAL"). This limit is unique to securitisation in the LCR rules. As far as we can determine, it is also not based on any empirical evidence that longer dated securitisations are less liquid than shorter

dated ones. It does, however, remove a meaningful portion of RMBS transactions from the pool of eligible securitisations.

9.42. Do you consider that the existing liquidity risk treatment of securitisation, in particular in terms of credit quality steps (CQSs) and haircuts applied to securitisations eligible for Level 2B HQLA, are adequately reflecting the liquidity and stress performance of securitisations, across the full economic cycle, including in crisis conditions, and in comparison, with the treatment of other comparable financial instruments?

- Yes
- **No**
- No opinion

9.43. If you answered no to question 9.42., please justify your reasoning, providing quantitative and qualitative data on the impact, and provide suggestions for what you would consider as appropriate and justified treatment in terms of CQSs, haircuts and other relevant requirements, without endangering financial stability.

The current rules allow only AAA securities to be eligible for inclusion in the LCR pools. This is a problem as set out in our answer to question 9.41. It is also, as acknowledged by the Joint-Committee in its 2022 report, a mistake. As set out with great clarity in the report (paragraph 4.3), originally securitisations down to AA- were eligible since the ratings cut-off was at CQS1 and CQS1 encompassed AAA down to AA-. Subsequent changes to implementing regulations changed the definition of CQS1 for one table. This led to the existence of two definitions of CQS1. Unfortunately, by dint of the legislative cross-references, the definition that applies to the LCR eligibility rules is the new AAA only definition. As acknowledged by the Joint-Committee, this was not intended.

So, at the very least, the rules should revert back to the original and intended position of allowing the ratings cut-off to go to AA-. This corresponds to CQS1 to CQS4 in the new table. This was proposed by the Joint-Committee and we agree. Amongst other benefits, it would allow high quality securitisations issued by member states labouring under low sovereign ratings to be included. Today, in a number of member states, the highest rating allowable irrespective of the strength of the securitisation is beneath AAA – the "sovereign cap" problem.

However, this change would not completely alleviate the cliff problem outlined in our response to question 9.41. Banks would still have to be worried about forced sales in the case of a downgrade. If the initial rating was AAA, admittedly the downgrade would now be three notches rather than one. But for securitisations from countries subject to a sovereign cap where securitisations cannot be rated higher than, say, AA-, it remains a one notch cliff. This cliff effect does not exist with other eligible assets such as covered bonds where downgrades result in increased haircuts. This is a reasonable approach since bonds downgraded but still investment grade do not become unsaleable. They simply see their price drop. Also, we are still talking about high quality

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instruments: STS, senior and in a limited number of asset classes. Admittedly, as the investment grade threshold is approached, the dynamic of sales become very different and so there should be a hard cut off at that stage.

Therefore, we would propose that the CQS standard on initial inclusion in LCR pools be returned to CQS1 to CQS4. We would also propose that upon any downgrade, securitisations remain eligible up to CQS8 (BBB) but with increasing haircuts with each downgrade.

On the issue of haircuts, we note that the ECB's haircut for high quality securitisations is 5% and so considerably smaller than the 25% to 35% used in the LCR rules.

We also note that almost all securitisations are floating rate. So, compared to other capital market instruments such as almost all corporate bonds, banking senior unsecured bonds, sovereign debt or covered bonds, their price is not directly and mechanically affected by interest rate movements. This was extremely visible in the handling by investors of the UK LDI crisis. Then, securitisation bonds were the primary source of liquidity in times of stress. This was because the crisis tool place in a rapidly rising rate environment. Securitisations, being floating rate, could be sold to generate liquidity without producing additional losses that would have worsened further the liquidity difficulties of the sellers.

This is another reason why the inclusion of floating rate securitisations in LCR pools is a stabilising factor. Also, it is why the much steeper haircuts imposed on them compared to fixed rate instruments is, in the absence of other evidence, odd.

As a general matter, the key modifications necessary for the LCR eligibility criteria to be reasonable, compatible with the data and proportionate are:

- Removing the ratings cliff effect
- Re-instating the intended ratings threshold
- Imposing haircuts that are proportionate and reflective of their liquidity characteristics
- Removing the 5-year WAL maturity restriction in the absence of any justification for its existence

For how these translate into specific recommendations, we refer you to our response to response to question 9.49

9.44. With a change in the CQSs, haircuts and other relevant eligibility conditions to the Level 2B liquidity buffer, by how much would the volume of securitisations that you invest in, change?

9.45. Have the senior tranches of the STS traditional securitisations reached a sufficient level of market liquidity and stress resilience based on historical data covering a full economic cycle, including crisis conditions, and are there any additional solid arguments that could justify their potential upgrade from the Level 2B to Level 2A HQLA?

- **Yes**
- No
- No opinion

Please explain your answer.

Work has been conducted and shows that liquidity of high quality securitisations compares very well with that of covered bonds, even on very conservative assumptions.

- "High Quality Securitisation: An Empirical Analysis of the PCS Definition" (Risk Control – 2014)
- "Comparing ABS and Covered Bond Liquidity" (Risk Control – 2022)
- "Comparing CB, ABS and Corporate Bond Liquidity" (Risk Control – 2022)

The Joint-Committee refers to the later paper in its 2022 report but dismisses its relevance. The reasons given for such dismissal are deeply unconvincing. If we understand the Joint-Committee's reasoning, only data from stressed periods is relevant to assess the liquidity of instruments going into LCR pools. As a general matter, this approach appears plausible. But it is not applied by the Joint-Committee with any consistency or logic. The only crisis they believe is relevant to assessing securitisations' liquidity resilience is the 2008-2012 period. However, this was a unique crisis as it was quintessentially a "securitisation crisis". By that, we mean that the trigger of the crisis was difficulties in the US securitisation market.

It is a trivial point that *any instrument* is illiquid in a crisis centered on that instrument. No greater proof of this self-evident statement is there than the disappearance of any bid for the 30-year gilt at the height of the UK LDI crisis. Until that crisis, the long-dated gilt was universally viewed as, by far, the most liquid sterling instrument in the market. We note that following the LDI crisis, the PRA is not recommending that UK gilts be downgraded to level 2B in the LCR rules.

This fact is why the core strength of an LCR framework lies in pool diversity. The LCR pools are there to meet any type of liquidity crisis. By focusing only on a securitisation triggered crisis to measure securitisation liquidity, the Joint-Committee is operating as if the LCR pools only need be effective in a securitisation triggered crisis. This could lead to the levelling of the common criticism of military leaders across the ages, namely that they are preparing to fight the last war, not the future one.

The oddity of this approach is rendered starker by the fact that we have had two liquidity crises since the GFC: the sovereign debt crisis and the UK LDI crisis. In both crises, the liquidity of high quality securitisations held extremely well. This demonstrates that securitisation can play a valuable role in LCR pools in times of stress not triggered by

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securitisations. We cannot understand why the Joint-Committee then is only prepared to measure securitisation liquidity in "securitisation triggered crisis", an approach that is not applied to other instruments. If it were, of course, for the reasons we outlined above, no instrument would ever prove liquid. Hence the value of a diversity of instruments in LCR pools. But such diversity can only be achieved if the treatment of all LCR eligible instruments is internally consistent and proportionate.

An additional consideration is that liquidity of securitisations, although healthy, would be healthier if the regulatory framework encouraged rather than restricted issuance and trading. The current restrictive LCR rules are one constraint on liquidity of securitisations, as are miscalibrated capital requirements and unnecessary and costly due diligence requirements. This consideration opens the possibility of a gradual approach – outlined in our response to question 9.49 - where improvement of the treatment of securitisations in the LCR is accompanied by some limits on amounts. As liquidity further improves, the limits can be gradually increased in a virtuous circle.

9.46. If you answered yes to question 9.45., please provide arguments and data, that could justify the potential upgrade from Level 2B to Level 2A HQLA.

See our responses to questions 9.41, 9.43 and 9.45

9.47. Considering your answer to 9.46, with an upgrade of securitisations from Level 2B to Level 2A HQLA, by how much would the volume of securitisations that you invest in, change?

9.48. Are there any impediments in the current liquidity framework that prevent or discourage banks from making a better use of their liquidity buffer capacity and from increasing their investments in securitisation exposures?

- **Yes**
- No
- No opinion

9.49. If you answered yes to question 9.48, please specify what are the impediments and provide suggestions for targeted amendments to make the liquidity treatment more proportionate, without endangering financial stability.

Provide estimates of the potential additional volumes of securitisations that could be included in banks' liquidity buffers.

For the impediments, we refer to our response to question 9.41. In this context, we strongly disagree with the Joint-Committee's conclusions in its 2022 report (page 87) that the small amount of securitisations purchased for LCR is a demonstration that "credit institutions themselves do not consider securitisations to be effectively

marketable during stress or even attractive enough to diversify into". The first part of that statement is a *non sequitur* as banks do not select assets for LCR pools solely or even primarily on the basis of their marketability in times of stress. They select from amongst allowable asset classes the most economically efficient. The latter part of the statement is somewhat self-evident: if banks do not buy securitisations for their LCR pools it is because they are not as attractive as alternative asset classes. But as we have seen, this lack of attractiveness is the result of inappropriately calibrated regulatory rules. This is not just our opinion but that of the banks investing in securitisations – as to which we refer you to the survey conducted by AFME.

Also notable from the survey was that another reason given for the small use of securitisation in LCR cover pools was the lack of supply. This reinforces the argument that European securitisation is an ecosystem where all the components have to mesh for there to be growth. (See our response to questions 9.1 and 9.25). The lack of supply is caused by a number of miscalibrations and disproportionate regulatory requirements. Ameliorating one – eg the LCR treatment – without addressing the others – eg Solvency II to increase the depth of the investor community – is unlikely to have but a minor impact.

Also, we set out in our response to 9.43 the key elements that need to change. These changes are not dependent, necessarily, on shifting securitisations from one HQLA category to another. We strongly urge that, although category changes are not an issue per se, the Commission does not approach this matter as one of "to which bucket should securitisations be allocated?" but rather, "which problems need to be resolved irrespective of buckets?"

We therefore suggest the following amendments to the current LCR eligibility rules:

- CQS 1 to CQS 4 STS senior tranches backed by autos and residential mortgages – haircut of 7% (in line with covered bonds) – this reflects the high quality and simplicity of those asset classes but also their volume and familiarity for investors
- CQS1 to CQS 4 STS senior tranches backed by other assets – haircut of 15%
- Both should be allowed to remain in the LCR pools on downgrade down to CQS8 but with the following increased haircuts

Asset Class	CQS 1 – CQS 4	CQS 5 – CQS 6	CQS 7 – CQS 8
RMBS and autos	7%	15%	25%
Other asset classes	15%	25%	35%

- As with all other types of eligible assets, no maturity restriction.

If this is felt to be important, RMBS and autos can be moved to Level 1 and other STS senior tranches to Level 2.A. But such moves are not necessary to achieve the substantial improvement that is required.

We also acknowledge both that it would not be wise for any asset type to form 40% of any bank's LCR pool and that, as outlined at the end of our response to 9.45,

some supervisors may be concerned that more improvements in securitisation liquidity need to occur before they become a main component of any LCR pools. Realistically, considering the extremely low volume of securitisations currently in LCR pools and the small size of the STS market, this issue appears to us to be somewhat academic. However, it is not an illegitimate concern in and of itself.

To address this, limits could be put on the percentage of any LCR pool that can be invested in securitisations irrespective of its formal level allocation (Level 1, 2.A or 2B). This limit could be lower than those currently available to the existing levels but designed to grow as the virtuous circle of more volume driving more liquidity driving better LCR treatment driving more volume thus building the CMU.

These sub-limits should be discussed but, by way of example, could look like this:

RMBS and autos – for the first three years, 7% then an examination of liquidity and volumes leading to an increase to 12% if justified then, three years later and if justified, an increase to 20 %

Other assets - for the first three years, 5% then an examination of liquidity and volumes leading to an increase to 10% if justified then, three years later and if justified, an increase to 15 %

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10. Prudential treatment of securitisation for insurers

10.1. Is there an interest from (re)insurance undertakings to increase their investments in securitisation (whether a senior tranche, mezzanine tranche, or a junior tranche)?

- **Yes**
- No
- No opinion

This is a question best left to insurance undertakings.

However, a number of comments might be helpful.

A. Currently, based on the Joint-Committee report of 2022, the proportion of insurance assets composed on securitisations is minuscule. It amounts to 0.33% of all insurance assets.

   This is a much smaller percentage than insurance holdings prior to the GFC. Although we note that EIOPA has not presented any data going back to that period.

   This is also a much smaller percentage than is invested in securitisation by US insurance undertakings.

   The business model of EU and US insurance undertakings is not fundamentally different. The pre-GFC business model of EU insurance undertakings is not fundamentally different from their current business model.

   The nature (yield/amortisation profiles) of pre-GFC securitisations is not fundamentally different for high quality European securitisations than the current one. This is especially true for STS securitisation. As to this, see our response to question 9.21 on how STS was designed.

   In fact, current yields for highly rated securitisations are substantially higher than they were immediately before the GFC and so should make those instruments more attractive – all other things being equal).

   The one key differential between the pre-and-post GFC landscape is the regulatory rules under which EU insurance undertakings operate.The above considerations make it very reasonable to suppose that an improvement in the regulatory framework would result in a meaningful growth in insurance investment in securitisation.

B. The point is sometimes made that the reason insurance undertakings do not invest is securitisations is only because other types of investment are more attractive. This is true but also self-evident. By definition, if insurance undertaking purchase other types of investment in preference to securitisations it is because those investments are “more attractive”. The real question is why are they more attractive? Considerations in [A] above strongly suggest that it is not to do with the inherent

structural characteristics of securitisations but most likely due to the non-level playing field, costly and complex mandatory due diligence rules and miscalibrated capital requirements.

C. The point is also made that insurance companies show little interest in amending the securitisation parts of Solvency II. We strongly believe that the main reason for this is simply the disappearance within most insurance undertakings of any human knowledgeable in or dedicated to the product. There is no-one within most insurance undertakings interested in this topic, willing to do the work necessary to analyse the impact of possible Solvency II amendments or championing progress in this field. Most insurance undertaking are unlikely to even be aware of this consultation, much less have a desire or capacity to respond.

There are two point though that need to be made here.

First, proper calibration is a public good, irrespective of whether the supervised entities wish it. Miscalibration of risk capital invariably results in regulatory arbitrage and misallocation of capital. This, in turn, is a classic way to build up systemic risk. Therefore, Solvency II should be amended correctly to reflect risk whether insurance undertaking clamour for it or not.

Secondly, even with a proper calibration of Solvency II and more reasonable due diligence requirements, the need to identify the opportunity, then build up the human resources to take advantage of that opportunity will take time. Even if Solvency II and due diligence requirements are improved, it will likely be a couple of years before we see meaningful growth in insurance undertaking investment in securitisations.

The considerations in A. though strongly point to the likelihood of such growth.

10.2. If you answered yes to question 10.1., please specify the segments of securitisations in which (re)insurers would be willing to invest more (in terms of seniority, true sale or synthetic nature, type of underlying assets, etc.) and describe the potential for increase in the share of securitisation investments in (re)insurers' balance sheet.

Again this is a response best left to insurance undertakings.

As a general matter, it is not possible to speculate reasonably as to how much greater insurance undertakings investment in securitisation would be, should Solvency II be improved. Too many variables exist. But the numbers are considerable. If European insurance undertakings were to invest 10% of their assets in securitisations (which is roughly only half of what US insurers do) this would constitute around €375bn of additional investment.

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10.3. Is there anything which in your view prevents an increase in investments in securitisation by (re)insurance undertakings?

- **Yes**
- No
- No opinion

Please explain your answer.

If you mention prudential rules as part of your answer, please provide an estimate of the impact on the level of investments in securitisation, of the reduction of capital requirements for securitisation investments by a given percentage, e.g. 5% or 10%.

We can identify three impediments to greater investment is securitisations:

- Excessive capital requirements under Solvency II especially when compared to alternative investments
- Excessive and costly mandatory due diligence requirement which are not proportionate to risk (see our response to question 4.5)
- Less impactful, the potential sanctions that can be incurred even when the insurance undertaking has entirely delegated its due diligence to a specialist fund manager, as it is allowed to do under article 5.5 of the SECR

In respect of the first issue, we draw attention to the fact that, under Solvency II, the capital required to hold a pool of whole loans is less than the capital required to hold the AAA STS senior tranche of a securitisation of the exact same pool. This is despite the fact that the latter (a) has credit enhancement of usually between 10 and 15 time the worst historical losses suffered by this type of asset in the relevant jurisdiction and (b) that it is in a bond format and so easily tradeable whereas the whole loan pool is not. By way of example, a 5-year AAA STS RMBS senior tranche will require a 5% capital charge compared to a 3% (approximatively) charge for a pool of 30-year mortgages with an 80% LTV. This is even starker for a non-senior STS tranche where the capital requirement becomes 14% even though this may be a highly rated mezzanine tranche. This illogical outcome is the result of the discrepancy between the credit risk module and the spread module. The spread module itself, under which securitisations fall, is highly questionable in its assumptions since it is based on the notion that, in difficulty, an insurance undertaking will be required to sell all its securities holding at the same time, for the worst price and irrespective of the schedule of its liabilities. Not only is this highly unlikely but would not even be allowed by the supervisory authority.

Similarly, the capital cost of an insurance undertaking entering as protection seller into a synthetic securitisation will require considerably more capital than writing the exact same protection, under the exact same contractual provisions but as an insurance policy.

These two examples evidence the internal incoherence of Solvency II's capital requirement framework that makes it unfit for purpose and a haven for regulatory arbitrage and capital misallocation. For historical reasons, securitisation is always on the losing end of such arbitrages.

On the percentage question, as stated in our response to 10.2 and consistent with our analysis of the securitisation market as an ecosystem where all the different components mesh in a complex manner, it is not possible – even theoretically – to draw a mechanistic relationship between quantum of reduction of capital requirements and even an estimated impact on the volume of investment.

10.4. Is Solvency II providing disincentives to investments in securitisation for insurers which use an internal model?

- **Yes**
- No
- No opinion

Please explain your answer, being specific in your reply.

Again, this is a question better left to insurance undertakings. We shall only comment that in our interactions with market participants, we have been informed that there are jurisdictional differences. Some supervisors apparently are happy to accept the outputs of well-constructed models whereas others, we are informed, are uncomfortable with internal models that depart too starkly from the output of the standardized approach.

10.5. Is the current calculation for standard formula capital requirements for spread risk on securitisation positions in Solvency II for the senior tranches of STS securitisations proportionate and commensurate with their risk?

- Yes
- **No**
- No opinion

Please explain your answer, being specific in your reply, and, where relevant, provide a comparison, including, where appropriate, with internal models and their relative impact on the share of securitisation investments. If you consider calibrations inappropriate, please indicate what you would consider as 'appropriate' calibrations, as well as any data/evidence of historical spread behaviours that would justify your proposal.

We do not have access to internal models and so will leave this part of the question to be responded to by insurers and their representatives.

We have read, however, the work conducted by Risk Control on this issue:

"ABS and Covered Bond Risk and Solvency II Capital Charges" (Risk Control – 2022)

Based on their conservative approach, it is clear that, although not as dramatically out of kilter as the junior tranches of STS securitisations or the non-STS securitisations, the senior tranches of STS securitisations are over-capitalised by around 30%. The

recommendation based on this work would be to align the senior STS calibration to the Bonds and Loans capital charge (eg 4.5% for a five year AAA corporate bond compared to the current 5% for a AAA securitisation of similar duration).

This modest change leaves two questions unanswered.

First, this is a single analysis and it is based on very conservative assumptions. There is a good case for a new calibration based on additional data drawing on the internal models of insurance undertakings and adjusting for changes in the securitisation market. The latter would reflect, amongst other things, the changes brought about by the SECR.

Second, the Risk Control analysis takes as its premise the current spread module approach. We have seen that this model is deeply flawed and generates regulatory inconsistencies and arbitrages. Noting the recommendations of numerous independent groups including those headed by Paschal Donoghoe, Enrico Letta and Mario Draghi for a strong growth in a safe securitisation market to allow Europe to finance its needs, is there a case for further adjustments to the formula to correct the inconsistencies and overshoots of the existing framework?

We have written elsewhere of our in-principle opposition to loosening prudential safety to achieve political aims. We have argued that the amendments we propose with respect to banks and the CRR are not a trade between the proper calibration of risk and the desire to achieve a particular outcome for the savings and investment union. We have, on the contrary, argued that we believe changes are needed to achieve the proper calibration of risk and that the benefits to securitisation and the savings and investment union will flow from correctly calibrated and proportionate rules. Our proposal below to modify the Solvency II calibrations for STS senior tranches does not depart from these principles. Although such a modification is arbitrary in the context of the current architecture of Solvency II with its module inconsistencies, it is suggested solely to achieve a more reasonable and proportionate outcome. One that does not allocate less capital to holding whole loans that to holding AAA rated STS senior tranches of the same loans.

We would therefore, in that spirit, propose aligning AAA/AA rated senior STS tranches with covered bonds. (CQS0 and CQS1 in the Solvency II ratings tables), We think that this result generates greater consistency in the allocation of capital between similar instruments (senior STS tranches and covered bonds) and between the otherwise inconsistent approaches to similar risks within the Solvency II framework. A further point in favour of this amendment is that securitisations being floating rate instruments have greater inherent price stability since their price does not shift mechanically with shifts in underlying interest rates.

If this is not acceptable, we would then suggest aligning AAA/AA senior STS tranches to the bonds/corporates, referencing the Risk Control work, notwithstanding its very conservative assumptions.

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10.6. Is the current calculation for standard formula capital requirements for spread risk on securitisation positions in Solvency II for the non-senior tranches of STS securitisations proportionate and commensurate with their risk?

- Yes
- **No**
- No opinion

Please explain your answer, being specific in your reply, and, where relevant, provide a comparison, including, where appropriate, internal models and their relative impact on the share of securitisation investments. If you consider calibrations inappropriate, please indicate what you would consider as 'appropriate' calibrations, as well as any data/evidence of historical spread behaviours that would justify your proposal.

We refer you to the previously cited paper (see our response to question 10.5). Based on the data collected by Risk Control, the miscalibration of non-Senior STS tranches is 100% leading to the conclusion that calibrations should be halved.

10.7. Is it desirable that Solvency II standard formula capital requirements for spread risk differentiate between mezzanine and junior tranches of STS securitisations?

- Yes
- No
- **No opinion**

Please explain your answer.

In general, we are favourable to simpler rather than more complex regulatory approaches. Of course, a splitting of the non-senior STS category is logical in that junior and mezzanine tranches will trade quite differently. However, such a split will unavoidably bring the necessity of defining tranche thickness and introduce a significant layer of added complexity to an already far from simple framework.

It is unclear to us whether sufficient data exists to reach sensible conclusions on the correct differentials in capital requirements between different non-senior tranches. Even if these data exist, it is impossible at this stage to say whether the differentials will be meaningful enough to justify the additional layer of complexity.

10.8. If you answered yes to question 10.7., please provide suggestions for calibrations of capital requirements for such mezzanine and junior tranches, including the data/evidence of historical spread behaviors backing such suggestions. Please indicate how you would define the mezzanine tranche as well as the assumption (e.g. of thickness of the tranche) underlying your proposed calibration. Please also indicate whether and why such introduction of a mezzanine calibration would be needed in Solvency II, even if no dedicated treatment for mezzanine tranches is introduced in EU banking regulation (CRR).

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10.9. Is the current calculation for standard formula capital requirements for spread risk on securitisation positions in Solvency II for non-STS securitisations proportionate and commensurate with their risk, taking into account?

- Yes
- No
- **No opinion**

Please explain your answer, being specific in your reply, and, where relevant, provide a comparison, including where appropriate with internal models and their relative impact on the share of securitisation investments.

The issue here is quite complex and we do not have a specific recommendation.

We do note a number of things:

- The previously cited Risk Control paper shows substantial miscalibration
- The calibration of non-STS, as we understand, draws heavily on GFC price data for the investment grade part and on no price data at all for the non-investment grade part. As such, it is subject to the same issues and problems as the eligibility rules for LCR pools. Namely, the data on an asset's liquidity should not solely be calculated on its performance through a crisis triggered by that asset. We have had two liquidity crisis since and securitisations' performance during those should be part of the calibration.
- The differential in capital requirement for a 5 year CQS 1 corporate bond and a 5 year CQS1 non-STS securitisation is 5.5% to 67%. That is over x12 greater for the securitisation notwithstanding that the latter is a floating rate instrument and the former not. This gap is beyond any plausibility.
- On the other hand, non-STS is not a "bounded" category. See our response to question 9.13 paragraph [D]. However, it should be noted that bonds and loans are not a bounded category either as they cover a wide range of credit characteristics.
- It is important for policy reasons to maintain a proper differential between STS and non-STS calibrations.

We therefore suggest a serious exercise to determine the parameters of price volatility with a view to a substantial improvement in the capital requirement rules for non-STS.

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10.10. Is there a specific sub-segment of non-STS securitisation for which evidence would justify lower capital requirements than what is currently applicable?

- Yes
- No
- **No opinion**

10.11. If you answered yes to question 10.10., please specify the sub-segment of non-STS securitisations that you have in mind as well as its related capital requirement, including any evidence/data of historical spreads supporting your proposal.

10.12. Is it desirable that Solvency II standard formula capital requirements for spread risk differentiate between senior and non-senior tranches of non-STS securitisations?

- **Yes**
- No
- No opinion

Please explain your answer, being specific in your reply.

Irrespective of the decision on non-STS calibrations (see our response to question 10.9), it is clear that senior non-STS securitisations within CQS0 or CQS1 trade considerably better than non-senior non-STS securitisations and so the two categories should be differentiated.

10.13. If you answered no to question 10.12., please provide suggestions for calibrations of capital requirements for such senior and non-senior tranches, including the data/evidence backing such suggestions. Please also indicate whether you target a specific segment of non-STS securitisation.

We assume that this should be answered if one answered “yes”. However, since we do not have an opinion on the proper calibration of non-STS securitisations generally, it is not possible for us to provide a view on how such calibrations should then be adjusted between senior and non-senior tranches. See our response to question 10.9.

PCS

11. Prudential framework for institutions for occupational retirement provision (IORPs) and other pension funds

11.1. For the purpose of this section, please indicate whether you are an IORP, a non-IORP or another type of stakeholder.

- IORP
- Nationally regulated pension fund not regulated by IORP II
- **Other**

Please elaborate in case you are not an IORP.

PCS is a third party verification agent and an independent body set up to improve European securitisation.

11.2. Is there an interest from IORPs and/or non-IORPs to increase their investments in securitisation (whether a senior tranche, mezzanine tranche, or a junior tranche)?

- Yes
- No
- **No opinion**

11.3. Please clarify whether your answer to question 11.2. concerns your own situation, or whether it is an assessment of a given national market (in which you operate for instance). If you answered yes to question 11.2., please specify the segments of securitisations in which IORPs and/or non-IORPs would be willing to invest more (in terms of seniority, type of underlying assets, etc.) and describe the potential for increase in the share of securitisation investments in their balance sheet. In addition, if your reply concerns or encompasses non-IORPs, please indicate i/ the number of non-IORP in your jurisdiction, ii/ the amount of assets under management and iii/ the type of pension business concerned, for which investment in securitisation would be interesting.

11.4. Does the IORP II Directive contain provisions which in your view restrict IORPs' ability to invest in securitisation?

- Yes
- No
- **No opinion**

Please explain your answer.

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11.5. Are there national legislations or supervisory practices which in your view unduly restrict IORPs' and non-IORPs' ability to invest in securitisation?

- Yes
- No
- **No opinion**

Please explain your answer, as well as whether it applies to IORPs, non-IORPs, or both.

Please be specific in particular where you refer to non-IORPs.

11.6. Are there wider structural barriers preventing IORPs and non-IORPs from participating in this market?

- Yes
- No
- **No opinion**

Please explain your answer, as well as whether it applies to IORPs, non-IORPs, or both.

Please be specific in particular where you refer to non-IORPs.

11.7. If you answered yes to question 11.6., please explain how these barriers should be tackled? Please explain your answer, as well as whether it applies to IORPs, non-IORPs, or both. Please be specific in particular where you refer to non-IORPs.

12. Additional questions

12.1. What segments of the securitisation market have the strongest potential to contribute to the CMU objectives, and that should be the focus of any potential regulatory review? You may select more than one option.

- **Traditional placed securitisation**
- **Synthetic securitisation**
- **SRT securitisation**
- **ABCP securitisation**
- **STS securitisation**
- Non-STS securitisation
- Securitisation of SME and corporate exposures
- **Securitisation of mortgages**
- Securitisation of other asset classes
- Other Please explain your answer.

The CMU has a number of different objectives and different parts of the securitisation market have the potential to contribute to one or more of those objectives.

A. One objective of the CMU is to channel European savings into the funding of the European economy. This requires a re-allocation of funds from bank accounts and guaranteed investment schemes to capital market instruments. Because European investors are, on the whole,extremely risk averse, funds will only be attracted away from safe low yielding instruments such as bank accounts to very safe (AAA) bonds – via funds such as UCITS. Because of tranching, traditional placed securitisation AAA STS senior tranches are the only instrument available that can scale up sufficiently fast to achieve that CMU objective. The need for safety also drives the need for a credible and very strong regulatory framework with layers of protection (such as TPVs). This is found in STS securitisations. Finally, to attract risk averse investors, the best asset class should be one that is easily understandable and seen as inherently safe by retail investors. Mortgages and auto loans meet those requirements. This is what drives our selection of "traditional securitisations", "STS securitisations" and "securitisation of mortgages" (to which should be added auto-loans)

B. Another aim of CMU is to rebalance the funding mix of the economy between banks and capital markets but not as a zero sum game. The aim of developing capital markets is to increase overall funding, not take funding away from the banking system. So a successful CMU project should have banks and capital markets work in symbiosis to increase funding overall. Securitisation achieves that since the raw material for the capital market instruments is principally generated by the banking

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sector. But the greatest benefit to the European economy is achieved if this framework both strengthens banks and generates capital market instruments purchased by savers. To strengthen the banking system vis a vis its international competitors *and* make it more resilient, European banks must be able to manage safely but pro-actively their capital. This is also essential to the banks' ability to help achieve the third objective in [C] below.

For this SRT securitisation in all its forms is essential. It is possible and some times better to achieve SRT via a traditional securitisation and so we selected "synthetic securitisations", "true sale securitisations" and "SRT securitisations"

C. Another aim of the CMU is to improve funding for SMEs.

That can be done by making the banks stronger and able to increase their lending envelopes. See our comments on [B] above.

Another way in which today SMEs are able to access the securitisation market is through ABCP conduit. And so we also selected "ABCP"

However, dealing with the categories we did not select, it is important not to turn away from effecting necessary improvements to their regulatory rules because these may have a lesser impact on CMU objectives.

First, almost all the changes being discussed in this consultation are about creating a level playing field amongst financing tools (in order, amongst other reasons, to avoid regulatory arbitrage) and to calibrate correctly the existing rules consistent with actual risk and the need for financial stability. These are, in and of themselves, public goods. The primary driver of the reforms we support is the creation of a coherent and safe regulatory framework, stripped of market distortions. This will create the best environment of market participants to finance the European economy. And it may well be that the segment of the securitisation market that does this most effectively is not one that stakeholders anticipate.

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12.2. What are the principal reasons for the slow growth of the placed traditional securitisation (where the senior tranche is not retained, but placed with the market)? Why do banks choose not to issue traditional securitisation for both funding and capital relief? You may select more than one option.

- Interest rate environment
- **Low returns**
- **Operational costs**
- **High capital charges**
- **Difficulty in placing senior tranches**
- Significant Risk Transfer process
- Preference for alternative instruments for funding
- Prefer to retain to keep the client relationships
- Prefer to retain to keep the revenue from the underlying assets
- Prefer to retain to access central bank liquidity
- Other

Please explain.

These are very simplified explanations of a complex set of mechanisms but we hope contain the essence of the arguments.

• Interest rate environment

NO - very simplistically, the choice of financing instruments amongst available types is driven by spread rather than absolute level of interest rates.

• Low returns

YES BUT - first, returns are never absolute but a component of a risk and return calculus. If low returns explained the absence of securitisation, then the Swiss government could never fund its debt. Secondly, returns must not be understood as simply the coupon on the instrument but also the coupon compared to the cost of investing. The miscalibrated capital charges together the additional unnecessary cost of due diligence distort the price equation for investors in securitisations. If I have a bond A yielding 20bp but against which I have to hold capital that costs me 3 bp and I need to pay 2bp of overheads, and my funding costs are 5bp, I am making 10bp net. I have bond B with the same risk characteristics yielding 30bp but the cost of capital is 12bp (because I have to hold more capital than for bond A), overheads of 5bp (because of regulatory requirements) and my funding costs are still 10bp. I am now making only 3bp net. So the return on B is lower than the return on A, even if A has a lower interest rate.

A similar equation operates for originators: if I have two instruments with equal risk and maturity which investors will pay the same 100bp but one requires me to pay 5bp in issuance costs and the other 30bp in issuance costs then I will choose, all other things being equal, the former.

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- **Operational costs**

  YES - mandatory and unnecessary operational costs not imposed on other no safer products factor in the calculations referred to above.

- **High capital charges**

  YES - see our comments on low returns

- **Difficulty in placing senior tranches**

  YES - the difficulty in placing senior tranches is a factor of the price distortive nature of the regulation. The natural buyers of senior tranches are banks and insurers. But excessive capital requirements, haircuts for LCR and due diligence requires securitisations to "compensate" investors through higher yields than for comparable instruments. This is, in turn, unattractive to originators who can issue other instruments. (Or in the case of SRT results inyields that remove the actual benefit of the potential capital relief.)

- **Significant Risk Transfer process**

  NO – this is an issue but not a "principal" reason.

- **Preference for alternative instruments for funding**

  NO - this is true but self-evident. The relevant question is "why do originators prefer to issue other instruments when they did not pre-GFC and they do not outside of Europe?" It is not a principal reason because it is not a "reason".

- **Prefer to retain to keep the client relationships**

  NO - since banks always fully service the securitised assets, the client relationship is always maintained. Ninety nine percent of clients with securitised assets will never know that their loans have been securitised. It is also a requirement of almost all securitisations that the originator/servicer service securitised loans in exactly the same way as a non-securitised loans (to protect investors who otherwise would be worried about misaligned interests). So not only do clients not know their loans are securitised but they are treated exactly the same way as clients whose loans have not been securitised.

- **Prefer to retain to keep the revenue from the underlying assets**

  NO- the business of banks is to raise funds at a given cost and lend them on for a return higher than the cost. When deciding whether it wishes to issue a securitisation, a bank will calculate the return on the underlying assets. It will then calculate the costs of funding those assets (cost of funds+cost of capital+admin costs) without a securitisation and with a securitisation. It will then, all other things being equal, choose the option with the greatest spread. (This is simplistic as there are other considerations such as management of maturity mismatches, diversification, ratings impacts, etc…but the point is that "revenue" and the desire to keep it is not how banks operate.)

- **Prefer to retain to access central bank liquidity**

  NO - assuming the question addresses the desire for banks to keep securitisations on their books to serve as central bank repo collateral, this is a

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non-point. Banks have more than sufficient unencumbered assets to issue considerably more traditional securitisation with a sufficient volume of remaining assets to generate as much repo collateral as they need.

12.3. Please specify which regulatory and non-regulatory measures have the strongest potential to stimulate the issuance of placed traditional securitisation.

There are six key measures:

- Better calibrated capital requirements for banks holding securitisations
- Better and more reasonable rules for eligibility of securitisations to bank LCR pools
- Better calibrated capital requirements for insurance undertakings holding securitisations
- Proportionate and more reasonable mandatory disclosure requirements (article 7 SECR)
- Proportionate and more reasonable mandatory due diligence requirements (article 5 SECR)
- Allowing unfunded synthetic securitisations to be STS

There are many other measures that will substantially improve various parts of the securitisation market. Once more, we strongly urge the Commission to consider implementing all the suggested changes bearing in mind that a market is an ecosystem in which all the components play a role. Absence of any component does not just reduce efficiency of that part of the system but of the system as a whole.

12.4. What are the main obstacles for cross-border securitisations (i.e. securitisations where the underlying exposures, or the entities involved in the securitisation, come from various EU Member States)?

Although much is made of the different legal regimes (eg insolvency regimes) that govern assets in different jurisdictions, we do not believe this is, in fact, the main reason blocking cross-border securitisations. The rules of mortgage enforcement in different states of the US are quite variable but US RMBS is plentiful (and not just via GSEs). What is not variable across the US is the type of mortgage and the contractual terms of those mortgages.

There are three issues we believe render cross-border securitisations difficult:

- Homogeneity of the underlying assets. The less homogeneous a pool the harder it is to analyse. This is why homogeneity is an STS criterion. These analytical difficulties are a factor of the time taken to do the analysis by a potential investor but also the heightened model risk they introduce. Homogeneity in cross-border deals is in part, but not the biggest part, a function of different laws. But it is also

a function of different cultural traditions on how you lend, on the different ways member state governments deal with consumers or economic downturns, what type of contractual terms exists, how local banks deal with delinquencies, etc…

- IT – Originators (even in the same group) do not usually have the same IT architecture in different jurisdictions. This makes the provision of pool wide information in a standardized fashion very costly as the different IT systems need to be modified (or an new overarching IT system created) to create homogenous pool wide data reporting.

- Investor preference – In a cross-border securitisation, issues occurring in one jurisdiction will affect the whole transaction. For example, a recent UK Supreme Court decision on auto-loans has raised questions about that asset class. If there had been a cross-border transaction with UK, French, Greek and Danish assets, even if the UK assets had only been 10% of the underlying pool, that transaction now has an issue even though the issue is limited to one jurisdiction. The counter argument that the transaction is also stronger since the problem only affects a tenth of the pool is unconvincing to an investor. That argument is a diversification argument and investors counter that they would rather achieve their own diversification by purchasing one UK, one French, one Greek and one Danish transaction. Following the UK issue, they can choose to sell only that deal and keep the unaffected three others. This leaves the decision to the investor in a way a cross-border transaction does not.

These reasons are also why the few cross-border transactions we see are with larger corporate assets (almost always in synthetic format). Although legal regimes and particularly insolvency laws are different for larger corporates in different jurisdictions, underwriting criteria and contractual terms are much more standardized across jurisdictions. If there is a single originator, the IT system for their larger corporate business is usually the same across jurisdictions. Finally, investors (and lenders) tend to look at the larger corporate lending market as an "international" market where international companies will be affected by international conditions and less by events or developments in one of the jurisdictions in which they operate.

12.5. What measures could be taken to stimulate cross-border securitisation in the EU? Please substantiate your answer for traditional and synthetic securitisation respectively.

Because of the nature of the problems (see our response to question 12.4), changes to the regulatory or legal framework are not likely to do much to assist this market. It could be argued that loosening the rules on homogeneity for STS may help. But for the reasons we set out in our response to question 7.12, this would be unwise.

One way to stimulate cross-border securitisation would be the creation of a common platform. However, if the platform only passed on the problems we identified in 12.4, the issues would not be alleviated. To have a positive impact the platform would need to “homogenise” the pools and the reporting so that investor could treat them as a unitary proposition. It is easy to see how a platform could do this but not easy how it could do it without some form of mutualised guarantee where the risks inherent in the lack of homogeneity were absorbed by the platform.

We can see a number of beneficial outcomes being sought through cross-border transactions.

First, to help create a true pan-European retail/SME lending market where the same source of finance (the securitisation investor) is accessed for lending across jurisdictions.

Second, to allow access to the benefits of the securitisation market to smaller financial institutions in smaller economies. With smaller pools, these financial institutions may not be able to enter into a stand-alone securitisation where upfront and ongoing costs and the generation of investor interest requires a minimum deal size.

Third, to push financial institutions to standardize their loans across European borders.

The first two could still be achieved, in part, simply by creating a deeper European securitisation market. At the investing level, the securitisation market is already cross-border with investors buying securitisation tranches from multiple European countries. More depth to the overall market will allow this phenomenon to grow. In fact, allowing banks to purchase senior tranches of securitisations originated in other jurisdictions is a way to mitigate the relative failure of the banking union. It creates expertise in country A on the lending and credit dynamics of an asset type in country B. Once a bank or insurer has that expertise, it will likely continue to invest in securitisations from country B creating an ongoing relationship between those investors and country B originators. This will then create an ongoing and possibly substantial web of cross-border lending via banks and insurers.

Also, with a much larger securitisation market will come more standardized documents and terms. If the regulatory costs of disclosure and due diligence are reduced, together with smaller transactions costs then smaller sized securitisations become financially viable.

Both of the above developments do require the types of changes to the securitisation regulatory framework discussed elsewhere in this paper.

Finally, smaller institution can access the securitisation market cross-border via the ABCP market. Therefore, reforms that help grow the ABCP market will also likely help this type of cross-border financing of smaller banks in smaller economies.

The standardisations of loans across borders is more complex and we are not sure how this can be achieved other than via a platform which (as with Fanny Mae in the US) makes standardisation a pre-requisite for access. We do, however, anticipate lively discussions as to which “standard” should be adopted.

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12.6. Securitisation activity is heavily concentrated in a few Member States – primarily Italy, France, Germany, Netherlands and Spain. What are the main obstacles to increasing securitisation activity in other Member States? What measures could make securitisation more attractive in those Member States?

First, we note that this is true in traditional true sale securitisations. In synthetic securitisations, the issuance is much more broadly spread.

Some of the concentrations are the result of contingent historical developments. But broadly they tend to map Member States with larger banks. This suggests that the issues are to do with larger pools not being available in smaller economies.

To make securitisation more attractive for those smaller economies, we refer you back to our answers to question 12.5. You need to lower the costs of issuing securitisations and lower the yield surcharge imposed by miscalibrated capital requirements and the relative unattractiveness of securitisations for inclusion in LCR pools.

A platform may also be used but this introduces levels of complexity and political considerations. Also, it may be unnecessary if other reforms deepen the securitisation market and reduce its costs.

12.7. Does the EU securitisation framework impact the international competitiveness of EU issuers, sponsors and investors?

- **Yes**
- No
- No opinion

Please explain your answer and where possible elaborate on the difference in regulatory costs stemming from the prudential, due diligence and transparency requirements in non-EU jurisdictions, in comparison to the EU securitisation framework.

It is important to bear in mind that securitisation frameworks in different jurisdictions operate within very different financial environments. Therefore, two identical regulatory rules in two jurisdictions can have a dramatically different impact depending on how the rest of the financial ecosystem operates. For example, severe constraints on SRT rules in the United States operate within an environment where government sponsored entities such as Fanny Mae provide a cheap and continuously available means for US banks to recycle their capital. Absent such entities in Europe, the same rules will be punitive in terms of competition with US banks. Similarly, the existence of a vast pool of retail capital market investment driven by retirement funds and associated fiscal rules in the US means that the senior securitisation tranches rely much less on the bank bids. So restrictive capital requirements imposed on US banks have considerably less impact on the securitisation market than they do in Europe. This explains, to a large extent, the lack of interest of US policy makers in introducing STC or revising existing capital rules.

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So, in focusing on the impact of European securitisation rules on competitiveness, we would recommend not looking at the micro-rules such as due diligence requirements since that is not where the most significant impact lies. The most significant impact lies in how the totality of the miscalibrated securitisation rules result in Europe's struggles on a variety of key objectives. (This is not to suggest, of course, that the macro-outcome does not result from the sum of the micro-rules).

Without a strong securitisation market, Europe will struggle to launch a safe CMU in the fixed income space. It will struggle to build an ecosystem able to finance innovation. It will not break the vicious circle of low bank profitability leading to low price to book numbers making equity capital raising too expensive. On the back of this vicious circle, bank consolidation in Europe becomes much more difficult and European banks will become ever more irrelevant on the global stage.

At the micro-level, the requirements of article 5 due diligence means that non-EU investors can purchase European securitisations much faster than EU investors. This was evident during the UK LDI crisis when we were told the fire sales of securitisation positions ended up with US investors taking up the excellent opportunity to generate profit which, had EU funds been able to do so, would have benefited EU end investors. But, looking at the macro-level challenges, we would argue that the need to change article 5 is (a) to make it more reasonable and proportionate and (b) to increase the size of the EU investor pool. The improvement of EU investors' competitive position is a fringe benefit but not, in our view, a key driver.

12.8. How could securitisation for green transition financing be further improved? What initiative could be taken in the industry or in the regulatory field?

The current position of securitisation within the EU Green Bond Standard legislation is satisfactory. In particular, the definition of green securitisation as dependant on the use of the proceeds of the issuance rather than the greenness of the underlying securitised assets is the right approach to maximise securitisation's contribution to the green transformation.

Securitisation is also well placed to help finance the green transition because it can finance start-ups whose underlying credit may not be very good since they lack a track record but who may have good quality assets in the form of receivables either from consumers or from good credit corporates. A good example would be a company that leased solar panels.

However, there are virtually no green securitisations. From extensive discussions with market participants, we are also very skeptical that we will see many (if any) securitisations seek the EU Green Bond Standard. This, however, is not a securitisation issue but an EU GBS issue. We have received similar feedback from institutions issuing green bonds in non-securitisation format. The issues appear to be:

- The complexity of the taxonomy
- The burden of data needed to prove taxonomy compliance

- The reputational and sanctions risks of finding that the complex taxonomy requirements were not met (however innocently)

Therefore, we do not have any suggestions within the field of securitisation regulation to improve the prospect of EU GBS securitisation issuance. If the general green issuance regulations are positively amended, we see no reason, based on the current regulations, why securitisation will not play a full role. This, of course, is predicated on the existence of a growing deep securitisation market thus returning the debate to how to improve securitisation regulations as a whole.

12.9. Are there any other relevant issues (outside of those addressed in the specific sections of the consultation paper above) that affect securitisation issuance and investments that you consider should be addressed?

- **Yes**
- No
- No opinion

12.10. If you answered yes to question 12.9., please explain your answer

One technical issue that could limit the growth of securitisation is the rule that stipulates that a UCITS can invest in no more than 10% of the issuance of any entity. As a general rule, this is sensible. But in a securitisation, you will usually have a single special purpose vehicle. However, the credit risk taken by the UCITS is not on the insolvency remote vehicle but on often thousands of underlying exposures. But with smaller transactions, a UCIT may well reasonably wish to purchase more than 10% of the deal.

We would suggest that for granular pools – say 100 exposures minimum – a UCIT should be able to purchase more than 10% of the issue. This would increase the size of the investor capacity without any negative prudential impacts.