Basel Committee on Banking Supervision Consultative Document Capital treatment for "simple, transparent and comparable securitisations"

This document provides the responses of the Dutch Securitisation Association on the BCBS Consultation, dated 10 November 2015.
We welcome the opportunity to respond on this Consultative Document.

DSA Background

The Dutch Securitisation Association (DSA) was established in 2012 as representative body of the Dutch securitisation industry. Our membership includes issuers of securitisations both from the insurance and the banking industry, and we are operating in close cooperation with the Dutch investor community.
Our purpose is to create a healthy and well-functioning Dutch securitisation market. We try to achieve this i.a. by providing a standard for documentation and reporting of Dutch RMBS transactions, promoting (in close cooperation with PCS) further standardisation and improvements in transparency, and active involvement in consultations about future regulation of the securitisation market.
Against this background, we would like to comment, on behalf of all Dutch RMBS issuers joined in the DSA, on the Consultative Document.

Our comments and responses are organised as follows:

1) General comments on the development of criteria for STC securitisations
2) Answers to the 4 questions raised in the Consultation document
3) Specific comments on the additional clarifications and enhancements of the expanded STC criteria

1) General comments on the development of criteria for STC securitisations

The Dutch securitisation industry, represented by the DSA, welcomes the differentiation between “high quality” and “other” securitisations for the purpose of determining the capital treatment of securitisations, as now is proposed by the Basel Committee as well as the European Commission and the European Banking Authority.
We also agree with many of the structural STS/STC criteria developed by the regulators with the help of the industry.
There remain however a number of important issues where we fundamentally disagree with the proposals:

-Capital requirements for securitisations, also those qualifying for STC status, are still multiples of the requirements for identical portfolios held as whole loan portfolios or used to support covered bonds:
For a standard RMBS tranching (90% AAA, 7% BBB, 3% B), 8% capital, p-factor 0.6, the proposed (ERBA) capital charges for non-STC (I yr: 4.8%, 5 yr: 5.7%) resp. STC (1 yr: 3.9%; 5yr: 4.7%) compare to 0.8%(AAA; SA) -1.6% (AA; SA) for covered bonds or 2.8% (SA) for a whole loan portfolio.
While some limited non-neutrality could be justified to the extent that the STC criteria may not fully capture all structural and modeling risk, the remaining high level of non-neutrality in the capital treatment will discourage a meaningful recovery of the securitisation market.

-In this respect we would also like to point to the fact that most investors will not be able to use the IRB and consequently will have to deal with the ERBA and SA and the corresponding lack of level playing field between the US and Europe.

-The introduction of credit related criteria, as in D15, results in an unjustified increase in capital charges, due to double counting: credit risk is already discounted in the normal capital treatment and should not be part of the STC criteria. STC should be limited to its own abbreviation, Standard, Transparent and Comparable, and not be expanded to a quasi credit rating.

-If the initiatives to redevelop the securitisation market aim at supporting the “real economy”, ABCP and Synthetic securitisations should also be part of the STC proposals. Securitisation of trade receivables and SME exposures can be structured in an “STC-way”, as also is reflected in several proposals from the EBA.

-Finally, the success of STC securitisation will also depend on the implementation and day-to-day operation of the STC qualification.
In order to be a reliable benchmark for investors, the STC attestation should be beyond doubt for everyone involved in the market.
In our view, this can only be achieved through STC status being granted by a (lightly) regulated third party with general recognition in the market.
Unfortunately, no such infrastructure is foreseen in your proposals.

2) Answers to the specific questions raised in the Consultative Document

Q1. Do respondents agree with the rationale for introducing STC criteria into the capital framework? Are there any other aspects that the Committee should consider before introducing STC criteria into the capital framework that are not already reflected in the rationale above?

Answer: We do agree with the rationale for introducing STC criteria into the capital framework, however subject to our response on Question 2

Q2. Do respondents agree that, for the purpose of alternative capital treatment, additional criteria are required? What are respondents' views regarding the additional criteria presented in Annex 1?

Answer: We do agree that certain structural aspects may not be captured in terms of Simple, Transparent or Comparable, so an "Other" category may be needed to cover issues like Granularity (D.16; indeed lack of granularity adds to the complexity of a transaction). The "widely recognized" third part servicer of D.17 could very well be included in "Comparable". But the credit risk related criteria of D.15 should not be part of the additional criteria, since credit risk is already covered in the normal capital framework.

Q3. What are respondents' views on the compliance mechanism and the supervision of compliance presented in this consultative document?

Answer: The Dutch securitisation industry is strongly opposed to the mechanism as presented. While we agree that originators/sponsors should indicate in some way why and how, to the best of their knowledge, they meet the STC criteria, we do not expect investors to be able to independently verify the criteria in their due diligence. But we also do not expect investors to rely only on the attestation of an originator/sponsor.
So in our view, certification by an independent (lightly) regulated third party will be indispensible to let STC securitisations take off in a meaningful way.
As regards the supervision, we do agree with some kind of legal liability for originators that have intentionally misrepresented STC status, but we are also concerned that originators/sponsors may shy away form representing STC status because of the many interpretation vaguenesses in the criteria.

Q4. What are respondents' views on the alternative capital requirements for STC securitisation presented in this consultative document?

Answer: Since the IRB will not be available to most investors, we see the IRB calibration mainly as a point of reference for the ERBA or, in a world of level playing fields, the SA. The resulting risk weights are still generating high levels of non-neutrality, so they will not really help stimulating a flourishing securitisation market (see also our general comments above).

3) Specific comments on the additional clarifications and enhancements of the expanded STC criteria

A1. Nature of assets
No comments.

A2. Asset performance history
We appreciate the clarification offered in the additional consideration and especially the fact that you indicated that “it is not the intention of the criteria to form an impediment to the entry of new participants to the market”.
In this respect we would like to repeat our comment from the consultation on the criteria, that the “established performance history” should not refer to the legal entity, but to the team involved.

A3. Payment status
We would appreciate if the definition in the additional guidance could be inserted in the criterion itself, since it eliminates definition questions around “default”, “delinquent” etc.
Please also confirm, for the sake of clarity, that in (a) “the obligor has been subject to an insolvency or debt restructuring process due to financial difficulties within three years prior to the date of origination”, “origination” refers to the start of the securitisation transaction, and not the origination of the loan (which could be a seasoned loan, well performing over many years since its origination).

A4. Consistency of underwriting
In the additional requirements, we still miss clarity on “materially non-deteriorating origination standards”.
Underwriting criteria can become more or less stringent, depending on where we are in the macro-economic cycle. We suggest replacing “non-deteriorating” by “pursuant to underwriting standards that are not less stringent than those applied at the time of origination”.

A5. Asset selection and transfer
As regards the additional requirement “an independent third-party legal opinion should support the claim that the true sale and the transfer of the assets under the applicable laws comply with points (a) through (d)”, please confirm that we can read this as “comply with points (a) to (d) to the extent not conflicting with national insolvency law”.

A6. Initial and ongoing data
We would like to repeat our comment made on the consultation of the criteria that the pool review should either be of the portfolio to be securitised or a review of the originator’s general portfolio within the last 12 months prior to the issue date.

B7. Redemption cash flows
No comments.

B8. Currency and interest rate asset and liability mismatches
No comments. We appreciate that our earlier comment on “appropriately hedged” has been reflected in the Additional requirement.

B9. Payment priorities and observability
We would like to repeat the following comments made on the consultation of the criteria:
-Information in an Investor Report about the ability of a (breach of a trigger) to be reversed adds speculative elements to an otherwise factual report. In our view this is undesirable.
-Liability cash flow models will usually not be made available by the originator/ sponsor, but *procured by* the originator/sponsor to be made available by a specialised third party (Bloomberg, Intex etc.).
-With regard to the approach with respect to asset performance remedies we agree that the transaction documentation should broadly describe an arrears and default management policy. We would oppose however to a requirement that would be too prescriptive (and to detailed) in the manner how all types of solutions should be applied. The files and circumstances of debtors in financial distress can be very different from each other and there should be a discretionary basis for the servicer to be able to tailor the best solution to a specific case in order to regain the performing status or to minimise a loss.

B10. Voting and enforcement rights
No comments.

B11. Documentation disclosure and legal review
A solution for confidentiality and data protection issues is still missing in this criterion. Referring to what is currently being discussed in Europe on this point, we suggest the following:
Information that could be in breach of national legislation or confidentiality obligations relating to customer, original lender or debtor should be anonymised or aggregated or the originator/sponsor may provide a summary of the concerned documentation.

B12. Alignment of interest
No comments (but the very different application in the US and Europe is obviously undermining the value of the criterion).

C13. Fiduciary and servicer risk
We fully agree that the remuneration of those with a fiduciary responsibility should be such that they are incentivised to meet their obligation, but please explain how anyone can ever check this criterion.

C14. Transparency to investors
No comments.

D15. Credit risk to investors
We repeat our general comment that this should not be part of the additional criteria, since credit risk is already covered in the normal capital framework.

D16. Granularity of the pool
No comments.

D17. Relationship between the originator and the servicer of the securitised assets
We appreciate the exception made for “residential mortgages in a jurisdiction where it is common practice to employ a third party servicer” (which covers most of the current Dutch market), but for other situations the presence of a back-up servicer should in our view be sufficient.