

Legal Update

EBA consults on the creation of an STS framework for synthetic securitisations

Introduction

The European Banking Authority (the **"EBA"**) has recently launched a public consultation on its proposals to create a simple, transparent and standardised (**"STS"**) framework for synthetic securitisations, as set out in its Draft Report on STS Framework for Synthetic Securitisation (the **"Discussion Paper"**).¹ In this Legal Update we consider some of the key aspects of the Discussion Paper.

Background

THE EU SECURITISATION REGULATION

The EU Securitisation Regulation² (the **"Securitisation Regulation"**) became applicable on 1 January 2019 to all securitisations (as defined

therein)³ other than securitisations existing prior to that date to the extent that they are grandfathered. The Securitisation Regulation consolidated and amended the previous rules in relation to securitisation transactions and covers two main areas.

Firstly, it sets out provisions in relation to all securitisations which are within its scope, consolidating and adding to the rules that previously applied to particular types of regulated entities. These provisions include requirements for securitisation special purpose entities (**"SSPEs"**), due diligence, risk retention and transparency obligations, credit-granting standards and a ban on resecuritisation, together with the relevant definitions.

Secondly, it sets out a framework for simple, transparent and standardised (**"STS"**) securitisations, as described further below.

¹ Discussion Paper – Draft Report on STS Framework for Synthetic Securitisation Under Art. 45 of Regulation (EU) 2017/2402, published on 24 September 2019 and available at <https://eba.europa.eu/regulation-and-policy/securitisation-and-covered-bonds/discussion-paper-on-sts-framework-for-synthetic-securitisation-under-art.-45-of-regulation-eu-2017/2402>.

² Regulation (EU) 2017/2402 of the European Parliament and of the Council of 12 December 2017 laying down a general framework for securitisation and creating a specific framework for simple, transparent and standardised securitisation, and amending Directives 2009/65/EC, 2009/138/EC and 2011/61/EC and Regulations (EC) No 1060/2009 and (EU) No 648/2012, available at <https://eur-lex.europa.eu/legal-content/EN/TXT/%20%20PDF/?uri=CELEX:32017R2402&from=EN> (hereinafter cited as **"SR"**).

³ Under Article 2(1) SR, "securitisation" means "a transaction or scheme, whereby the credit risk associated with an exposure or a pool of exposures is tranching, having all of the following characteristics:

- (a) payments in the transaction or scheme are dependent upon the performance of the exposure or of the pool of exposures;
- (b) the subordination of tranches determines the distribution of losses during the ongoing life of the transaction or scheme;
- (c) the transaction or scheme does not create exposures which possess all of the characteristics listed in Article 147(8) of Regulation (EU) No 575/2013".

In addition, the Securitisation Regulation includes provisions dealing with sanctions and penalties for non-compliance, supervision by regulatory authorities, where securitisations entered into before 1 January 2019 would fall within its scope and transitional arrangements.

Certain of the requirements of the Securitisation Regulation are in the process of being set out in more detail in various technical standards, including with respect to risk retention and transparency.

Please see our previous Legal Update, "The EU Securitisation Regulation – Where are we now?", for a more detailed discussion of the Securitisation Regulation.⁴

THE CURRENT STS REGIME

The Securitisation Regulation sets out a separate set of STS criteria for non-ABCP and for ABCP securitisations (although a lot of the criteria overlap or are similar). The EBA have published guidelines with respect to these STS criteria (the "**EBA Guidelines**"),⁵ which are non-binding but which are very helpful in clarifying the STS requirements.

Securitisations which meet the applicable STS criteria may benefit from relatively favourable regulatory treatment compared with non-STS securitisations. For example, if a securitisation is designated as STS and also meets various additional requirements under the Capital Requirements Regulation (as amended, the "**CRR**"), pursuant to the EU Regulation which was introduced at the same time as the Securitisation Regulation and which amended the CRR (the "**CRR Amending Regulation**")⁶, an EU regulated bank that invests in or otherwise takes credit exposure to that securitisation will have a lower capital charge for that exposure than would otherwise apply under

the CRR.⁷ In addition, a transaction which qualifies as STS (and with respect to Solvency II⁸ and the liquidity coverage ratio under the CRR⁹ (the "**LCR**") which meets certain additional criteria) will also benefit from lower capital requirements for insurance and reinsurance undertakings subject to regulation under Solvency II, will be eligible for inclusion in high quality liquid assets by banks for the purposes of the LCR and will be eligible for investment by money market funds subject to the Money Market Funds Regulation¹⁰. The STS regime is thus meant to encourage EU institutional investors to invest in securitisations and so to foster the growth of a healthy securitisation market.

At the time of publication, there have been over 80 STS securitisations notified to the European Securities and Markets Association ("**ESMA**"). The most popular asset class to date has been residential mortgage backed securitisations, followed by auto loans and leases, trade receivables, credit cards, consumer loans, SME loans and leases. However, not all securitisations are capable of being STS (for example, CMBS and managed CLOs) and challenges remain in interpreting certain of the criteria and in relation to legacy transactions which may not meet all the STS criteria at the relevant time.

4 Available at: https://www.mayerbrown.com/-/media/files/perspectives-events/publications/2019/06/%20eusecuritisationregulationwherearenewow_june19.pdf.

5 Final Guidelines on STS criteria for non-ABCP securitisation and Final Guidelines on STS criteria for ABCP securitisation, available at: <https://eba.europa.eu/regulation-and-policy/securitisation-and-covered-bonds/guidelines-on-the-sts-criteria-for-abcp-and-non-abcp-securitisation>

6 Regulation (EU) 2017/2401 of the European Parliament and of the Council of 12 December 2017 amending Regulation (EU) No 575/2013 on prudential requirements for credit institutions and investment firms, available at <https://eur-lex.europa.eu/legal-content/EN/TXT/PDF/?uri=CELEX:32017R2401&from=EN>.

7 Amended CRR Articles 260, 262 and 264.

8 Commission Delegated Regulation (EU) 2018/1221 of 1 June 2018 amending Delegated Regulation (EU) 2015/35 as regards the calculation of regulatory capital requirements for securitisations and simple, transparent and standardised securitisations held by insurance and reinsurance undertakings.

9 Pursuant to Commission Delegated Regulation (EU) 2018/1620 of 13 July 2018 amending Delegated Regulation (EU) 2015/61 to supplement Regulation (EU) No 575/2013 of the European Parliament and the Council with regard to liquidity coverage requirement for credit institutions, Article 1(8) (amending Article 13 of Delegated Regulation 2015/61).

10 Commission Delegated Regulation (EU) 2018/990 of 10 April 2018 amending and supplementing Regulation (EU) 2017/1131 of the European Parliament and of the Council with regard to simple, transparent and standardised (STS) securitisations and asset-backed commercial papers (ABCPs), requirements for assets received as part of reverse repurchase agreements and credit quality assessment methodologies, Article 1 (amending Article 13(1)(c) of Regulation (EU) 2017/1131 on money market funds).

STS FOR SYNTHETIC SECURITISATIONS

Synthetic securitisations¹¹ are currently precluded from STS treatment under the Securitisation Regulation because one of the criteria is that there is a true sale of the relevant assets or an assignment or transfer with the same legal effect. It was decided not to include allow synthetic securitisations to be included in the STS criteria in the Securitisation Regulation due to concerns about additional counterparty credit risk and potential complexity. However, it was recognised in the Securitisation Regulation that the EBA had already established a possible set of STS criteria for synthetic securitisation in its Report on Synthetic Securitisation published in 2015.¹² Article 45 of the Securitisation Regulation required the EBA, in close cooperation with ESMA and EIOPA, to publish a report on the feasibility of a specific framework for STS synthetic securitisation by 2 July 2019, following which the European Commission (the “**Commission**”) is required to submit a report and, if appropriate a legislative proposal, to the Parliament and the Council by 2 January 2020. Given the delay in publishing the Discussion Paper, the Commission report and legislative proposal is likely to be delayed as well. The creation of such STS framework is limited to balance sheet synthetic securitisation and arbitrage securitisations will not be within its scope.¹³

It is also useful to note that Article 270 of the CRR, as amended by the CRR Amending Regulation, already allows for preferential regulatory treatment of synthetic securitisations on a limited basis, with respect to senior tranches of SME portfolios retained by originator credit institutions, where the

11 “synthetic securitisation” is defined in Article 2(10) SR as “a securitisation where the transfer of risk is achieved by the use of credit derivatives or guarantees, and the exposures being securitised remain exposures of the originator”.

By contrast, “traditional securitisation” is defined in Article 2(9) SR as “a securitisation involving the transfer of the economic interest in the exposures being securitised through the transfer of ownership of those exposures from the originator to an SSPE or through sub-participation by an SSPE, where the securities issued do not represent payment obligations of the originator”.

12 The EBA Report on Synthetic Securitisation for SMEs, available at: <https://eba.europa.eu/-/eba-issues-advice-on-synthetic-securitisation-for-smes>.

13 The Discussion Paper differentiates between balance sheet synthetic securitisations, being “transactions where the regulated institution’s primary object is the transfer of credit risk of exposures that the regulated institution itself holds on balance sheet”, and arbitrage securitisations, being “transactions where the protection buyer purchases exposures outside their core lending/business activity, for the sole purpose of writing credit protection on them (i.e. securitising them) and arbitraging on the yields resulting from the transaction”.

securitisation meets the non-ABCP STS criteria except for those relating to true sale and no encumbrance of the exposures¹⁴ and provided that significant credit risk has been transferred to either supranational entities (central governments, central banks, multilateral development banks or international organisations) that are 0% risk weighted through unfunded guarantees or to institutional investors through guarantees which are fully collateralised by cash on deposit with the originator institution).

In addition, the EBA has also published a Discussion Paper on Significant Risk Transfer in Securitisation in September 2017.¹⁵ Under the CRR, originators can exclude a securitised exposure from the calculation of its risk-weighted exposure amounts provided that significant risk transfer, or “SRT”, is achieved. This regulatory capital relief through SRT is one of the main drivers for structuring synthetic securitisations.

The Discussion Paper

THE PROPOSED STS CRITERIA FOR SYNTHETIC SECURITISATIONS

The Discussion Paper sets out a set of proposed STS criteria for synthetic securitisations. These criteria broadly follow the existing STS criteria for non-ABCP securitisations, with some amendments and with some additional criteria covering matters which are specific to synthetic transactions.

There are 36 separate criteria, spread across four areas. “Simplicity” has 13 criteria. These include criteria in relation to representations and warranties, borrower creditworthiness and originator expertise. “Standardisation” has 10 criteria, including in relation to risk retention requirements, transaction documentation and servicer expertise. “Transparency” has 5 criteria, including in relation to data on historical default and loss performance. Finally, “Requirements specific to synthetic securitisations”, has six criteria including criteria in relation to credit events, credit protection payments and verification agents.

14 Articles 20(1)-(6) SR.

15 EBA Discussion Paper on the Significant Risk Transfer in Securitisation, published on 19 September 2017 and available at: <https://eba.europa.eu/regulation-and-policy/securitisation-and-covered-bonds/discussion-paper-on-the-significant-risk-transfer-in-securitisation>.

Please see the Annex to this Legal Update for a summary of all of the proposed criteria and a comparison to the STS criteria for non-ABCP securitisations.

The Discussion Paper allows market participants to respond to 16 questions. These are summarised in the Annex to the Discussion Paper. The questions include: "Do you agree with the assessment of the reasons that could eventually support a preferential capital treatment?"; "Do you agree with the specific criteria for synthetic securitisation?" "and What would be the impact of potential differentiated regulatory treatment from level playing perspective with regard to third countries where STS framework has not been introduced?"

The Discussion Paper considers the pros and cons of developing an STS framework for synthetic securitisations. It identifies the following points in its favour:

- increased transparency of the product;
- increasing relevance of synthetic securitisation as a credit risk and balance sheet management tool in the context of recent regulatory developments;
- increased relevance of synthetic securitisation due to some advantages compared to traditional securitisation;
- further standardisation of the product and opening of the market for smaller originators and investors;
- importance of regulatory endorsement for the revival of the market; and
- potential positive impact on the financial and capital markets, financial stability and on the real economy.

However, it also notes the following points against creating such a framework:

- the fact that an STS balance sheet synthetic framework has not been developed at a global level (unlike with traditional securitisation where alternative capital treatment is contemplated for securitisations which meet the criteria for "simple, transparent and comparable" or "STC" securitisations under the revised Basel securitisation framework);¹⁶

¹⁶ Basel III Document – Revisions to the securitisation framework - Amended to include the alternative capital treatment for "simple, transparent and comparable" securitisations, 11 December 2014 (rev. July 2016) ("BCBS 374"), available at <https://www.bis.org/bcbs/publ/d374.pdf>.

- it could be perceived as a high quality label by less sophisticated market players (leading to increased "moral hazard" risk); and
- it could lead to less issuance of traditional STS securitisations.

REGULATORY CAPITAL TREATMENT

The Discussion Paper takes the view that the assessment of an STS framework for synthetic securitisation should take a two pronged approach, firstly focusing on the STS criteria and secondly considering the potential for allowing synthetic securitisations which meet such STS criteria to benefit from preferential regulatory capital treatment compared with those that are non-STS.

The EBA identifies some pros and cons of providing differentiated regulatory capital treatment for STS synthetic securitisations. Such treatment could result in the following benefits:

- stimulation of the development of the STS product; more in line with actual performance of balance sheet synthetics; more risk sensitive regulatory framework;
- it would overcome constraints of the current limited STS risk weight treatment of SME synthetic securitisations under Article 270 of the CRR, given that such securitisations would need to meet the existing STS criteria which have not been designed for synthetic securitisations;
- it would ensure a level regulatory playing field with traditional securitisations; and
- it would fuel the potential positive impact of synthetic securitisation on the financial markets and stability (increasing banks' lending capacity, freeing up capital and diversifying risk across the financial system).

However, the EBA points out the following downsides of creating such a framework:

- it would not be compliant with the revised Basel securitisation framework (as discussed above). However, the EBA does note that deviations from the Basel regulatory capital framework are not unprecedented; and
- there could be potential risks for the banking sector.

EBA RECOMMENDATIONS

The EBA reaches the conclusion in the Discussion Paper that it would recommend the establishment of an STS framework for balance sheet synthetic securitisations and also recommends that for any synthetic securitisation to be eligible as STS it should comply with the proposed STS criteria set out in the Discussion Paper.

However, it reserves its position on the question of whether there should be differentiated capital treatment for STS synthetic securitisations, indicating that it may consider including a recommendation on this point following the public consultation.

Market response

The EBA held a public hearing on 9 October 2019 and market participants are in the process of considering the Discussion Paper. The market response to the proposed STS criteria appears to be largely positive. Market participants have expressed some concerns about certain of the criteria, for example, querying the requirement for cash collateral to be held with a third party bank and the prohibition of synthetic excess spread. In addition, for many market participants it will be a key objective that preferential regulatory capital treatment can be obtained for synthetic securitisations that meet the STS criteria, in line with traditional securitisations.

The deadline for comments is 25 November 2019. To respond, market participants must click through to the "send your comments" button from the consultation page of the EBA Website by 25th November 2019, which gives the ability to respond to the 16 listed questions in the Annex to the Discussion Paper.

Annex

PROPOSED STS CRITERIA FOR SYNTHETIC SECURITISATION AND COMPARISON WITH STS CRITERIA FOR NON-ABCP TRADITIONAL SECURITISATION

Proposed criteria for synthetic securitisations	Non-ABCP traditional securitisations
<p><i>Simplicity</i></p>	
<p>Criterion 1: Balance sheet synthetic securitisation, credit risk mitigation</p> <p><i>Replacement of the criteria on true sale/ assignment, clawback risk, perfection triggers and representation that assets are not encumbered in Articles 20(1)-(5) SR with definition of balance sheet synthetics and requirement to ensure robustness of credit protection contract (credit risk mitigation criteria).</i></p> <ul style="list-style-type: none"> • Securitisation should meet definition of “synthetic securitisation”. • Protection buyer must be an EU-regulated undertaking and an “originator” as defined in the Securitisation Regulation in respect of the underlying exposures. • Where the protection buyer is a limb (b) originator the originator should apply policies that are no less stringent than those applied to similar exposures that have not been purchased. • Underlying exposures are part of core lending or core business activity of protection buyer. • Underlying exposures are held on its balance sheet. • Undertaking not to further hedge exposure to credit risk. 	<p>Legal true sale; no severe clawback risk.¹⁷</p> <p>Specified perfection triggers including severe deterioration in seller’s credit quality, seller insolvency and seller breaches.¹⁸</p>

¹⁷ SR Article 20(1)-(4).

¹⁸ SR Article 20(5).

Proposed criteria for synthetic securitisations	Non-ABCP traditional securitisations
<p>Criterion 2: Representations and warranties</p> <p><i>Representations and warranties adapted and extended.</i></p> <p>Protection buyer must represent and warrant that:</p> <ul style="list-style-type: none"> • It has title to the underlying exposures and, where it is a credit institution or insurance company, it accounts for their credit risk in its regulatory balance sheet. • Each underlying exposure meets eligibility criteria, representations and warranties and any other conditions (other than a credit event) for a protection payment under the credit protection agreement. • Underlying agreements contain legal, valid, binding and enforceable obligation to pay of the obligor. • Standard underwriting criteria no less stringent than those applied to similar exposures of originator which are not securitised. • No material breach or default of obligors in relation to the underlying exposures. • No untrue information with respect to the underlying exposures. 	<p>Seller to represent that assets not encumbered and no adverse effect on enforceability of the sale.¹⁹</p>
<p>Criterion 3: Eligibility criteria, no active portfolio management</p> <p><i>Criterion adapted.</i></p> <p>Clear eligibility criteria required for protection under the credit protection agreement.</p> <p>No active portfolio management on discretionary basis including sale of exposures. (Substitution of exposures that are in breach of representations and warranties, and addition of exposures meeting defined conditions during a replenishment period, are permitted.)</p> <p>Later transferred assets must meet eligibility criteria that are no less strict than those applied to the initial exposures.</p> <p>An exposure may only be removed where it has been repaid or has matured, where it is subject to a refinancing, restructuring or similar non-credit driven amendment, which occurs in ordinary course (e.g. maturity extension) or where it did not meet the eligibility criteria due to an error.</p>	<p>Clear eligibility criteria.</p> <p>No active portfolio management on discretionary basis. (Substitution of exposures that are in breach of representations and warranties is permitted.)</p> <p>Later transferred assets must meet eligibility criteria that applied to the initial exposures.²⁰</p>

19 SR Article 20(6).

20 SR Article 20(7).

Proposed criteria for synthetic securitisations	Non-ABCP traditional securitisations
<p>Criterion 4: Homogeneity, enforceable obligations, full recourse to obligors, period payment streams</p> <p><i>Similar</i></p> <p>Assets must be homogeneous as to asset type, subject to clearly defined and specified conditions.</p> <p>Obligations to pay must be contractually binding and enforceable.</p> <p>Defined periodic payments required.</p> <p>Proceeds may be generated from sale of financed or leased assets.</p>	<p>Assets must be homogeneous as to asset type.</p> <p>Obligations must be contractually binding and enforceable.</p> <p>Defined periodic payments required.</p> <p>Proceeds may be generated from sale of financed or leased assets.</p>
<p>Criterion 5: No transferrable securities</p> <p><i>Same</i></p> <p>No transferable securities other than unlisted corporate bonds.</p>	<p>No transferable securities other than unlisted corporate bonds.²¹</p>
<p>Criterion 6: No resecuritisation</p> <p><i>Same</i></p> <p>Assets cannot include securitisation positions.</p>	<p>Assets cannot include securitisation positions.²²</p>
<p>Criterion 7: Underwriting standards and material changes thereto</p> <p><i>Adapted</i></p> <p>The underwriting standards pursuant to which the underlying exposures are originated and any material changes from prior underwriting standards should be fully disclosed to potential investors without undue delay.</p> <p>The underlying exposures are underwritten with full recourse to an obligor who is an individual, an SME or a corporate and who is not a special purpose entity.</p> <p>No broker intermediary or similar party was involved in the credit or underwriting decisions relating to the underlying exposures.</p>	<p>Assets must have been originated in ordinary course.</p> <p>Credit underwriting criteria to be no less stringent than for retained assets and must be disclosed.²³</p>
<p>Criterion 8: Self-certified Loans</p> <p><i>Same</i></p> <p>No "self-certified" residential mortgage loans.</p>	<p>No "self-certified" residential mortgage loans.²⁴</p>

21 SR Article 20(8).
22 SR Article 20(9).
23 SR Article 20(10).
24 SR Article 20(10).

Proposed criteria for synthetic securitisations	Non-ABCP traditional securitisations
<p>Criterion 9: Borrower's creditworthiness</p> <p><i>Similar</i></p> <p>Assessment of borrower's creditworthiness to meet regulatory requirements to the extent that such standards would apply to the individual underlying exposures.</p>	<p>Assessment of borrower's creditworthiness to meet regulatory requirements.²⁵</p>
<p>Criterion 10: Originator's expertise</p> <p><i>Same</i></p> <p>Originator should have expertise in originating exposures of a similar nature to those securitised.</p>	<p>Originator should have expertise in originating exposures of a similar nature to those securitised.²⁶</p>
<p>Criterion 11: No defaulted exposures or exposures subject to outstanding disputes</p> <p><i>Similar</i></p> <p>No assets in default or exposures to credit-impaired obligors.</p>	<p>Underlying exposures to be transferred to the SSPE after selection without undue delay. No assets in default or exposures to credit-impaired obligors.²⁷</p>
<p>Criterion 12: At least one payment made</p> <p><i>Similar</i></p> <p>At time of inclusion of the exposures in the securitisation, at least one payment has been made (except in the case of revolving securitisations with assets payable in one instalment or with a maturity of < 1 year).</p>	<p>At time of transfer of the exposures, at least one payment has been made (except in the case of revolving securitisations with assets payable in one instalment or with a maturity of < 1 year).²⁸</p>
<p>Criterion 13: No embedded maturity transformation</p> <p><i>Similar</i></p> <p>Exposures should have been underwritten on the basis that their repayment was not dependent predominantly on the refinancing of such exposures or on the re-sale value of the assets that are being financed by those exposures.</p>	<p>Repayment not dependent predominantly on sale of assets, provided that assets may be rolled over, refinanced, or subject to a repurchase obligation.²⁹</p>
Standardisation	
<p>Criterion 14: Risk retention requirements</p> <p><i>Similar</i></p> <p>Risk retention by originator or original lender per Article 6 SR.</p>	<p>Risk retention by originator, sponsor or original lender per Article 6 SR.³⁰</p>

25 SR Article 20(10).

26 SR Article 20(10).

27 SR Article 20(11).

28 SR Article 20(12).

29 SR Article 20(13).

30 SR Article 21(1).

Proposed criteria for synthetic securitisations	Non-ABCP traditional securitisations
<p>Criterion 15: Appropriate mitigation of interest rate and currency risks</p> <p><i>Adapted</i></p> <p>Currency risks and interest rate risks appropriately mitigated.</p> <p>Protection buyer should bear no currency or interest rate risk.</p> <p>SSPE's liabilities in terms of interest payments to investors should be equal to or less than the amount of its income from the protection buyer and any collateral arrangements.</p> <p>No derivatives except for the purpose of hedging interest rate or currency risk. Such derivatives to meet common standards.</p>	<p>Interest rate and currency risks appropriately mitigated.</p> <p>No derivatives except for the purpose of hedging interest rate or currency risk. Such derivatives to meet common standards.³¹</p>
<p>Criterion 16: Referenced interest payments</p> <p><i>Same</i></p> <p>Interest payments per market rates or "sectoral" cost of funds, no reference to complex formulae or derivatives.</p>	<p>Interest payments per market rates or "sectoral" cost of funds, no reference to complex formulae or derivatives.³²</p>
<p>Criterion 17: Requirements after enforcement/acceleration notice</p> <p><i>Adapted</i></p> <p>Following enforcement or acceleration event, enforcement or acceleration to be initiated immediately with sequential amortisation of all tranches.</p> <p>Where an SSPE is used within a synthetic securitisation, after enforcement or acceleration notice, no cash trapping in the SSPE beyond what is necessary to ensure the operational functioning of the SSPE or the orderly repayment of investors in accordance with the contractual terms of the securitisation.</p>	<p>After enforcement or acceleration notice, no cash trapping in the SSPE beyond what is necessary to ensure the operational functioning of the SSPE or the orderly repayment of investors in accordance with the contractual terms of the securitisation except in exceptional circumstances.</p> <p>Principal receipts to be applied via sequential amortisation. Repayment of securitisation positions not to be reversed with regard to seniority. No automatic liquidation at market value.³³</p>

31 SR Article 21(2).

32 SR Article 21(3).

33 SR Article 21(4).

Proposed criteria for synthetic securitisations	Non-ABCP traditional securitisations
<p>Criterion 18: Allocation of losses and amortisation of tranches</p> <p><i>Adapted</i></p> <p>Allocation of losses to holders of a securitisation position in a synthetic STS securitisation should always proceed in order of seniority of tranches, from the most junior tranche to the most senior tranche in the transaction.</p> <p>Pro-rata amortisation may only be applied to determine the outstanding amount of all tranches where clearly specified triggers relating to the performance of the underlying exposures ensure the switch of the amortisation scheme to sequential amortisation, including deterioration in credit quality of assets below specified threshold. Where this is not the case, sequential amortisation to apply to all tranches.</p> <p>Collateral provided to be returned to investors as tranches amortise.</p> <p>Amortisation agreements to be clearly documented.</p>	<p>Non-sequential priority of payments must include triggers for sequential payments, including deterioration in credit quality of assets below specified threshold.³⁴</p>
<p>Criterion 19: Early amortisation provisions/ triggers for termination of the revolving period</p> <p><i>Adapted</i></p> <p>For revolving securitisations, appropriate triggers to be included for termination of revolving period, and where an SSPE is used within a synthetic securitisation to issue notes placed with investors, early amortisation provisions should be included:</p> <ul style="list-style-type: none"> • deterioration in credit quality of underlying exposures below predetermined threshold; • losses rise above a predetermined threshold, or losses over a predefined period rise above a predetermined threshold; • failure to generate sufficient new underlying exposures that meet the predetermined credit quality. 	<p>For revolving securitisations, specified triggers for termination of revolving period:</p> <ul style="list-style-type: none"> • deterioration in credit quality of underlying exposures below predetermined threshold; • originator or servicer insolvency-related event; • value of underlying exposures falls below predetermined threshold (early amortisation event;) • failure to generate sufficient new underlying exposures of the required credit quality (termination of revolving period).³⁵

³⁴ SR Article 21(5).

³⁵ SR Article 21(6).

Proposed criteria for synthetic securitisations	Non-ABCP traditional securitisations
<p>Criterion 20: Transaction documentation</p> <p><i>Adapted</i></p> <p>Transaction documents to specify clearly:</p> <ul style="list-style-type: none"> contractual obligations of verification agent, servicer, trustee and other service providers; provisions for replacement of counterparties on default/insolvency other than protection buyer and investor where the services are not provided by the originator; provisions for continuity of servicing on servicer default/insolvency where servicing is not provided by the originator; servicing procedures applicable to underlying exposures at closing and how/when these procedures may be modified; servicing standards of servicer in servicing underlying exposures to maturity. 	<p>Transaction documents to specify clearly:</p> <ul style="list-style-type: none"> contractual obligations of servicer, trustee and other service providers; provisions for continuity of servicing on servicer default/insolvency; provisions for replacement of hedge counterparties, liquidity providers and account bank.³⁶
<p>Criterion 21: Servicer's expertise</p> <p><i>Similar</i></p> <p>Servicer expertise in servicing similar exposures supported by a management team with extensive industry experience.</p> <p>Servicer to have well documented policies, procedures and controls.</p> <p>Servicer to apply servicing procedures that are at least as stringent as applied to similar exposures which are not securitised.</p>	<p>Servicer expertise in servicing similar exposures.</p> <p>Servicer to have well documented policies, procedures and controls.³⁷</p>
<p>Criterion 22: Reference register</p> <p><i>Criterion on definitions and remedies in transaction documents replaced, requirement for transaction documents to specify payment conditions is covered in separate criteria</i></p> <p>The underlying exposures should be identified at all times via a reference register. The reference register should clearly identify, at all times, the reference obligors, the reference obligations from which the underlying exposures arise, the outstanding notional amount of each underlying exposure, and the protected notional amount for each underlying exposure.</p>	<p>Transaction documents to set out in clear and consistent terms definitions, remedies and actions regarding delinquency, default etc.</p> <p>Priorities of payment and triggers for changes to priorities of payment to be specified. Material changes to the priority of payments to be reported to investors.³⁸</p>

³⁶ SR Article 21(7).

³⁷ SR Article 21(8).

³⁸ SR Article 21(9).

Proposed criteria for synthetic securitisations	Non-ABCP traditional securitisations
<p>Criterion 23: Timely resolution of conflicts between investors</p> <p><i>Similar</i></p> <p>Provisions for timely resolution of conflicts between classes of investors.</p> <p>Where an SSPE is used within a synthetic securitisation to issue notes placed with investors, clearly defined voting rights allocated to noteholders and clearly identified responsibilities of trustee.</p>	<p>Provisions for timely resolution of conflicts between classes of investors; clearly defined voting rights allocated to noteholders, clearly identified responsibilities of trustee.³⁹</p>
<p>Transparency</p>	
<p>Criterion 24: Data on historical default and loss performance</p> <p><i>Similar</i></p> <p>Historical data on defaults and losses for similar exposures to be provided by originator before pricing. ≥ 5 years of data.</p>	<p>Historical data on defaults and losses for similar exposures to be provided by originator and sponsor before pricing. ≥ 5 years of data.⁴⁰</p>
<p>Criterion 25: External verification of the sample</p> <p><i>Similar</i></p> <p>Third party verification of asset sample by “appropriate and independent party” before closing, including verification that the underlying exposures meet the criteria determining eligibility for the credit protection under the credit protection agreement.</p>	<p>Third party verification of asset sample by “appropriate and independent party” before issuance.⁴¹</p>
<p>Criterion 26: Liability cash flow model</p> <p><i>Similar</i></p> <p>Provision of liability cash flow model to investors before pricing and on ongoing basis.</p>	<p>Provision of liability cash flow model to investors before pricing and on ongoing basis.⁴²</p>
<p>Criterion 27: Environmental performance of assets</p> <p><i>Similar</i></p> <p>For residential loans and auto loans or leases, disclosure of environmental performance by originator per Article 7 SR.</p>	<p>For residential loans and auto loans or leases, disclosure of environmental performance by originator and sponsor per Article 7 SR.⁴³</p>

39 SR Article 21(10).

40 SR Article 22(1).

41 SR Article 22(2).

42 SR Article 22(3).

43 SR Article 22(4).

Proposed criteria for synthetic securitisations	Non-ABCP traditional securitisations
<p>Criterion 28: Compliance with transparency requirements</p> <p><i>Similar</i></p> <p>Originator to be responsible for compliance with Article 7 SR.</p> <p>Asset level data before pricing upon request by potential investors.</p> <p>Transaction documents, prospectus or transaction summary and STS notification drafts before pricing.</p> <p>Final documents within 15 days after closing.</p>	<p>Originator and sponsor to be responsible for compliance with Article 7 SR.</p> <p>Asset level data before pricing upon request by potential investors.</p> <p>Transaction documents, prospectus or transaction summary and STS notification drafts before pricing.</p> <p>Final documents within 15 days after closing.⁴⁴</p>
<p>Criteria specific to synthetic securitisation</p>	
<p>Criterion 29: Credit events</p> <p>Credit protection agreement should cover at least the following credit events:</p> <ul style="list-style-type: none"> • Failure to pay of underlying obligor (Article 178(1)(b) of the CRR); • Bankruptcy of underlying obligor (Article 178(3)(e) and (f) of the CRR); • Restructuring of the underlying exposure (Article 178(3) (d) of the CRR). <p>Credit events to be clearly documented.</p> <p>Certain forbearance measures applied to underlying exposures shall not preclude the trigger of eligible credit events.</p>	<p>N/A</p>

⁴⁴ SR Article 22(5).

Proposed criteria for synthetic securitisations	Non-ABCP traditional securitisations
<p>Criterion 30: Credit protection payments</p> <p>Credit protection payment following a credit event to be calculated based on actual realised loss suffered by originator.</p> <p>Final credit protection payment should be payable within specified period following the end of the workout process for the relevant underlying exposure.</p> <p>Transactions to provide that an interim credit protection payment is to be made at latest within 6 months after credit event occurs where the workout of losses for underlying exposure has not been finalised by that time.</p> <p>Interim credit protection payment to be, at least, maximum of the impairment considered by the originator in its financial statements, at time interim payment is made and, if applicable, the LGD determined under Part Three Title II Chapter 3 of the CRR that has to be applied to corresponding underlying exposures in order to determine the IRB capital requirements on the originator for such underlying exposure. Where an interim credit protection payment made, a final credit protection payment should be made in order to adjust the interim settlement of losses to actual realised loss, in accordance with the first paragraph of this criterion.</p> <p>Where the protected amount is less than the outstanding notional amount of the corresponding underlying exposure, the credit protection payment should be in same proportion to protected amount as the protection buyer's realised loss bears the outstanding notional amount of the underlying exposure, subject only to the rule on interim payments.</p> <p>Method by which interim and final credit protection payments are calculated to be clearly specified in credit protection agreement.</p>	<p>N/A</p>

Proposed criteria for synthetic securitisations	Non-ABCP traditional securitisations
<p>Enforceable rights of protection buyer to receive protection payments.</p> <p>Amounts payable by investors to be clearly defined, capable of calculation and limited in amount.</p> <p>Circumstances in which investors are required to make payments under credit protection agreement should be clearly defined or subject to a determination by the verification agent, and limited in number.</p> <p>Credit protection amount to be broken down to the level of individual underlying exposures.</p>	
<p>Criterion 31: Credit protection payments following the close out/final settlement at the final legal maturity of the credit protection agreement</p> <p>Following a credit event and if the workout process has been not completed 2 years after the scheduled legal maturity or early unwinding of a transaction (the final reference date), a final credit protection payment should be made on the basis of the actual loss suffered by the originator and recorded by the originator in its financial statements at that time.</p> <p>After termination of the credit protection by investors, workout process should continue in respect of any outstanding credit events, which occurred prior to such termination in the same way as described in the first paragraph.</p>	N/A
<p>Criterion 32: Credit protection premiums</p> <p>The credit protection premiums paid under the credit protection agreement establishing the synthetic securitisation should be structured as contingent premiums: no guaranteed premiums, upfront premium payments, rebate mechanisms or other mechanisms that may avoid or reduce the actual allocation of losses to the investors or return part of the paid premiums to the originator after the maturity of the transaction.</p> <p>Documentation to contain all relevant information that has been used to price the credit protection agreement, including information on the market benchmarks and other market variables taken into account by the originator.</p>	N/A

Proposed criteria for synthetic securitisations	Non-ABCP traditional securitisations
<p>Criterion 33: Verification agent</p> <p>Third party verification agent to be appointed by originator at outset of transaction, to verify, for each of the underlying exposures in relation to which a credit event notice was given:</p> <ul style="list-style-type: none"> • that the credit event occurred in accordance with the credit protection agreement; • that the underlying exposure was included in the securitisation at the time of the relevant credit event; • that the underlying exposure met the eligibility criteria, at the time of inclusion in the reference portfolio; • that where an underlying exposure has been added as result of a replenishment, such replenishment complied with the replenishment conditions; • the accuracy of the final loss amount work out procedure, also in relation to the losses registered in the profit and loss statement by the originator; • that at the time where the final protection payment is made, the allocation of losses to investors in relation to the underlying exposures has been conducted correctly. <p>The verification agent should be independent and any SSPE and should have been appointed, and its appointment accepted, on or before the closing date.</p>	<p>N/A</p>

Proposed criteria for synthetic securitisations	Non-ABCP traditional securitisations
<p>Criterion 34: Early termination events</p> <p>Other than as a result of insolvency of the protection provider, a failure to pay (in respect of any premium or other amounts payable by the originator to investors) or breach of a material contractual obligation by the protection provider, the originator is only permitted to terminate a transaction prior to its scheduled maturity when either of the following occurs:</p> <ul style="list-style-type: none"> • relevant regulatory events which should: <ul style="list-style-type: none"> ○ include changes in all relevant law and/or regulation directly affecting the contractual relationship and/or materially affecting the allocation of benefits among the parties; ○ exclude other factors affecting the economic efficiency of the transaction that are not enshrined in law or regulation, such as credit rating agencies' methodologies or a central bank's collateral framework; • a time call is exercised, where the time period measured from the securitisation's closing date is equal to or higher than the weighted average life of the initial reference portfolio at closing. The time call should not be structured to avoid allocating losses to credit enhancement positions or other positions held by investors and should not be otherwise structured to provide credit enhancement; • a call as per Article 245(4)(f) of the amended CRR is exercised (clean-up call). <p>Such call rights should be clearly specified.</p> <p>No other originator calls should be allowed.</p>	<p>N/A</p>
<p>Criterion 35: Synthetic excess spread</p> <p>The protection buyer should not commit to any amount of excess spread available for the investors.</p>	<p>N/A</p>

Proposed criteria for synthetic securitisations	Non-ABCP traditional securitisations
<p data-bbox="165 210 772 277">Criterion 36: Eligible credit protection agreement, counterparties and collateral</p> <p data-bbox="165 300 740 367">Only the following credit protection arrangements should be allowed:</p> <p data-bbox="165 389 772 680">A. a guarantee meeting the requirements set out in Chapter 4 of Part Three Title II of the CRR, by which the credit risk is transferred to any of the entities listed under Article 214 (2) (a) to (d) of the CRR, provided that the exposures to the protection provider qualify for a 0% risk weight under Chapter Two of Part Three Title II of the CRR;</p> <p data-bbox="165 703 772 837">B. a guarantee meeting the requirements set out in Chapter 4 of Part Three Title II of the CRR which benefits from a counter-guarantee of any of the entities referred to in point (i); or</p> <p data-bbox="165 860 772 1151">C. other credit protection in the form of guarantees or credit derivatives not referred to under the previous two points that meets the requirements set out in Sub-Section 2 of Section 3, Chapter 4 of Part Three Title II of the CRR as amended by Article 249 of the CRR, provided that the obligations of the protection seller are subject to the following collateral requirements.</p> <p data-bbox="165 1173 772 1308">When the collateral is provided in accordance with point C, both the originator and the protection seller need to have recourse to high quality collateral, in either of the following forms:</p> <ul data-bbox="165 1330 772 1733" style="list-style-type: none"> <li data-bbox="165 1330 772 1621">• collateral is in the form of 0% risk weighted debt securities, held in a trust or entity set up for the sole purpose of holding securities whose notional value takes into account clearly determined and conservative haircuts to appropriately mitigate market and other risks, and which have a short remaining maturity of maximum 3 months, and under robust custody arrangements; or <li data-bbox="165 1644 772 1733">• collateral in the form of cash held with a third party credit institution with a sufficient credit quality standing. 	<p data-bbox="804 210 852 232">N/A</p>

Proposed criteria for synthetic securitisations	Non-ABCP traditional securitisations
<p>In addition, the following requirements should apply to the collateral:</p> <ul style="list-style-type: none"> • The rights of the originator to use the collateral to meet protection payment obligations of the investors should be enforceable. Security arrangements should be provided to ensure such right of the protection buyer. • The rights of the investors when the synthetic securitisation is no longer outstanding to the return of any collateral that has not been used to meet protection payments should be enforceable. • Where collateral is invested in securities, the securitisation documentation should set out the eligibility criteria and custody arrangement for such securities. <p>Where the investors remain exposed to the credit risk of the originator, this must be clearly disclosed.</p> <p>The originator should obtain an opinion from a qualified legal counsel confirming the enforceability of the credit protection in all relevant jurisdictions.</p>	

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