Intesa SanPaolo's response to the 2nd Consultative Paper

Comments on the Revisions of the Basel Securitisation Framework

20/03/2014

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1. Introduction and Overview

We welcome the opportunity to offer our comments to the BCBS with respect to its second consultative document on the "Revisions to the Basel Securitisation Framework" (a.k.a. BCBS 269).

We aknowledge that the Committee has significantly amended its original proposal of "Revisions to the Securitisation Framework", taking into account both the comments received on the first Consultative Document and the results from the Quantitative Impact Study (QIS). In particular we recognize that the changes introduced in the second Consultative Document aim at striking an appropriate balance between the risk sensitivity of the proposed approaches to risk weight calculations and their simplicity and comparability.

In this respect, we deem the most significant changes brought about by the current proposal are: a) a simplification not only of the hierarchy of calculation approaches, but also of the mathematical formulae used; and b) a revision of the calibration of all the approaches, in order to bring them more in line with the riskiness and connected capital charges of the portfolio being securitised, even if not totally accepting the arbitrage-free approach promoted by the AFA Quant Group and supported also by the EBF.

More specifically, while the previous document was characterised by two alternative hierarchies composed of numerous different approaches, the current proposal suggests a single hierarchy with three approaches, namely:

- the Internal Rating-Based Approach (IRB Approach), which replaces the much more complex Modified Supervisory Formula Approach (MSFA) and uses a mathematical formulation identical to the Standardised Approach (SA) but with different inputs (most importantly the IRB capital charge for the underlying pool of exposures) and calibration;
- the External Rating–Based Approach (ERB Approach), now applicable even when just one rating is available and characterised by a general reduction of the risk weights (RWs) with respect to the RRBA of the previous document;
- the Standardised Approach (SA), which is in fact very similar to the Simplified Supervisory Formula Approach (SSFA) of the first document.

Of significance is also the reduction of the RWs' floor, which in the new proposal is set at 15%, replacing the previously suggested value of 20%.

While we appreciate these changes, we however feel that the new proposal still falls short of the target the BCBS set itself of balancing risk sensitivity and simplicity, producing capital charges that are still too punitive, especially for higher quality exposures. We therefore believe that significant work remains to be done:

- in the area of calibration of the various approaches, both to improve their risk sensitivity - by better aligning them to the transactions features and the underlying pool risk - and to increase the consistency among themselves; and
- in the area of the definition of acceptable operating conditions for the application of the IRBA approach;

and that the specific issues of i) the Mixed Pool treatment, ii) the Risk Floor level iii) the Maturity definition and iv) the attachment/detachment points need to be revisited.

2. Main considerations

We welcome the new simplified hierarchy of approaches. In particular, the simplification of the IRB Approach with respect to the MSFA and its apparently less demanding information requirements (whereby collateral portfolios' single loan data are not strictly essential anymore) provide a strong incentive to the use of IRB methodologies, thus limiting the reliance on external ratings.

The Committee has placed the Internal Rating-Based Approach at the first place of the hierarchy, appropriately signaling its preference for methodologies based on a thorough risk assessment. However, the application of the IRB Approach - which can only be used by a bank having a verified and approved IRB model for the calculation of the credit risk capital requirement of the exposures underlying the securitisation (K_{irb}) - still entails significant problems, for investors and sponsoring banks alike.

First of all, even though the current proposal has relaxed the requirement to use collateral portfolio's single loan level information in order to be allowed to apply the IRB Approach, the issue of **data availability** - especially for third party originated exposures – is still relevant, also because it's not obvious what type of data (and derived parameter estimates) would be acceptable to regulators in the absence of detailed granular data. As no info provider – and often not even the underlying exposures' originators – is able to supply such granular detailed data, the **lack of** a formulation by the Committee of **clear operational guidelines** on how to calculate K_{irb} in these circumstances raises significant concerns as to the effective applicability of the IRB Approach. In general, we believe that in these cases the Committee should move in the direction of somehow relaxing the requirements set for the validation of the PD and LGD parameters' estimation. As an example, the depth of the time series needed for the PD estimation - 5 years - and for the LGD estimation - 7 years - could be shortened.

Secondly - even in the absence of a data availability problem, such as is often the case with exposures to internally structured ABCP programs (based on purchased third party-originated portfolios of receivables) and connected Liquidity Lines (LL) - there is, in our view, the issue of the **inappropriate extension of the scope of applicability of a bank's internal models** for the K_{irb} calculation . Banks' models are context-dependent, as they are calibrated using historical performance data relating to the bank's positions in a given product, and a bank's performance experience might be very different from that of the third party originating the exposures being securitised, thus raising doubts as to the soundness of the application of internally-estimated parameters to third party-originated portfolios.

We would therefore view the definition by the Committee of a **set of minimum requirements for the K_{irb} calculation** - addressing both the above-mentioned issues - as highly desirable, not only to facilitate and extend the IRB Approach applicability, but also to address potential concerns on the existence of a level-playing field among institutions in different jurisdictions if these were to implement the Securitisation Framework with different rules. National supervisors should then work with the local banks to develop **methods** - consistent with the Committee-defined set of minimum requirements and **more "flexible" than the current IRB-validated ones** - to be applied to the different specific asset classes and transaction types.

In particular, we would suggest, mainly for retail portfolios, to explicitly allow for so called *vintage analysis* to derive and calculate parameters of K_{irb}, as it is the standard methodological tool in the market, recognized also in the regulation in the IAA framework.

If these issues were left unaddressed, the inability to apply IRBA would imply a fall-back on less risk-sensitive and more conservative approaches (ERBA and SA), going effectively against the Committee's own wish of promoting banks' internal risk assessment and leading also to an increase of the funding cost for the real economy through this form of financing. Similarly, if, because of the data issue, the IRB Approach could not be used to its full potential and remained effectively of limited application, the proposed treatment of "Mixed Pools" of exposures - where a bank would have to assign a 1250% risk weight to underlying exposures for which it were unable to calculate K_{irb} - would prove too costly (see para. 7 for more details) and banks would adopt approaches further down the hierarchy. Moreover, given that - even in the revised proposals - these approaches (ERBA in particular, see also para.5) continue to disproportionately penalise high quality tranches, the adoption of the suggested rules could have the additional undesirable effect of skewing the securitization market in favor of lower quality paper.

In this context, the likely significant reliance on the ERBA and SA approaches, strengthen the case for a **thorough revision of their calibration** (see following paragraphs), in order to make them more risk-sensitive and improve their overall internal consistency.

As an aside, we feel it is also important to draw the attention of the Committe on the consistency of the prudential treatment of securitisation exposures in the **banking book** – the object of the proposal under consideration – and that of securitisation exposures in the **trading book** – as proposed in the Consultative Document on the " Fundamental Review of the Trading Book" (BCBS265), issued in October 2013. In particular, we would wish to make the point that there is currently a lack of coordination between the new regulatory provisions and that, in order to avoid the creation of arbitrage opportunities between the two books, it would be preferable that revisions to the prudential treatment of securitisation are addressed simultaneously for both portfolios.

Having tested the proposals of the two Consultative Documents on a few transactions, it would appear that the risk weight (comprising the sum of those for credit spread risk, default risk - aligned to that of the banking book - and general IRR) assigned to a given securitisation exposure in the trading book is almost double the one calculated for the same exposure in the banking book. This big difference - due to the particularly punitive treatment proposed for securitized exposures' credit spread risk, where no internal models are applicable and which would already penalise them with respect to any other bond position in the trading book - is likely also to foster arbitrage opportunities between the two books and discourage trading of securitisation tranches.

Additionally, it would also be desirable to have a proper understanding of the derivation of the credit spread risk capital charges in order to assuage concerns relating to some possible double-counting of risk in their quantification and in that of the default risk ones for securitisation exposures in the trading book.

Finally, we also remain of the opinion that the "Revisions to the Securitisation Framework" should include a "**grandfather clause**" - covering also the deals currently being structured - in order to avoid negative impacts on the business and the markets, keeping in mind that securitisation represents an essential funding instrument both for banks and corporates.

3. General Calibration Issues

As evidenced in the following tables - where the different approaches (and their older relative versions) are compared across a number of securitisation structures - the calibration consistency among approaches, targeted by the BCBS (pg.9. "*The proposed calibration of the SSFA …is intended to produce capital requirements that, overall, are slightly higher than those generated by the IRBA and roughly comparable to those generated under the ERBA*") is often contradicted.

The IRBA, which should normally be the least conservative of all approaches, frequently generates higher risk weights than the ERBA and the SA.

The ERBA and SA risk weights are rarely aligned.

We believe these considerations support the need of comprehensively re-addressing the issue of the calibration of the various approaches.

In particular, we support the idea of improving the calibration by:

- differentiating it (across approaches) by asset class, moving away from a situation of a single "p" parameter for all securitization exposures (in the case of the SA) or a coarsely differentiated one (in the case of the IRBA). Appropriate asset classes could either be based on regulatory asset classes or on alternative classifications supported by evidence collected through the QIS. Any such classification should be able to accommodate the concept of High Quality assets as currently being elaborated by market participants (see for example the "PCS" label);
- basing it (for both the SA-style and the IRBA-style of the SSFA) on a transparent risk model, such as the Conservative Monotone Approach (CMA)[1], the recent evolution of the originally proposed AFA model.

[1] For details refer to "Calibration of the Simplified Suprevisory Formula Approah" by G. Duponcheele, W. Perraudin, D. Totuom-Tangho, march 2014

RMBS

Deal/Tranche	Seniority	Rating	M	N	ATT	DET	SFA	New IRBA	IRB-RBA	New ERBA	SA - RBA	New SA
HERME 10 A	S	AAA	25,7	4.812	11%	100%	7%	15%	7%	15%	20%	15%
ARENA 2011-2 B	M	BBB	29,6	3.176	7,9%	11%	7%	15%	75%	310,5%	100%	148,8%
E-MAC/E-MAC DE05-I A	S	A+	33,3	1.973	19,7%	100%	7%	15%	10%	32,5%	50%	15%
E-MAC DE06-I B	M	B+	43,4	3.099	8,3%	15%	701%	1124%	1250%	893,3%	1250%	78,9%
AUBN 3 A2	S	AAA	25	834	53,8%	100%	7%	15%	7%	15%	20%	15%
ALBA 2006-2 A3A	S	A	24	1.913	46,3%	100%	7%	15%	20%	37,5%	50%	15%

CMBS

TITN 2006 – 1 b	M	CCC-	1,9	4	61,93%	100%	7%	15%	1250%	773,8%	1250%	15%

CLO SME

SMILE 2007 – 1 A	S	A	39,8	4.776	13,82	100%	217,3%	342,6%	12%	37,5%	50%	58,7%
SMILE 2007 – 1 B	M	BBB	39,8	4.776	9,87%	13,82%	1250%	1250%	75%	307,4%	100%	800,5%

AUTO LEASES

LOCAT 2006 – 4 A2	S	A2	14,8	8	63,93%	100%	7%	15%	12%	47,9%	50%	15%
LOCAT 2006 – 4 B	M	BBB-	14,8	8	18,94	63,93	7%	15%	100%	236,5%	100%	59,7%

4. Internal Rating Based Approach (IRBA)

The approach replaces the previous paper's MSFA and, in trying to increase the simplicity and comparability of approaches within the hierarchy, adopts the same formula as the SA (based on the old SSFA) for the calculation of the capital charges.

Given however that the calibration of the formula is based on the MSFA and that it needs to retain its sensitivity to various characteristics of the exposures, the **supervisory parameter "p"** within the formula is made **dependent in a rather unclear way** (no technical paper available) **on four factors**.

As “p” represents the relative capital surcharge for all securitisation exposures compared to the capital requirement for the underlying pool, it acts as a scaling factor of this requirement and bears a positive relation with the tranches’ RW.

The four factors which determine “p” through a linear function, whose coefficients vary in accordance with the typology of the underlying assets (Wholesale or Retail), the seniority of the tranche (Senior or Non – senior) and the granularity (Granular or Non – granular) of the pool, are:

- N: the effective number of exposures
- K_{irb}: the ratio of (a) the IRB capital requirement (including the expected loss portion) for the underlying exposures in the pool to (b) the exposure amount of the pool
- LGD: the exposure-weighted average Loss Given Default
- Mt: the maturity of the tranche

Translating the coefficients associated with the above-mentioned variables in terms of percentage relative contribution of the variable to the “p” parameter determination yields the following table (where A is an “intercept” not associated to any variable):

			N	K_{irb}	LGD	Mt
		A	B	C	D	E
Wholesale	**Senior,** Granular (N ≥ 25)	0,0%	59,0%	30,7%	9,1%	1,2%
	Senior, Non Granular (N < 25)	1,7%	40,9%	45,6%	10,7%	1,1%
	Non-Senior, Granular (N ≥ 25)	3,7%	66,1%	23,7%	4,8%	1,6%
	Non-Senior, Non Granular (N < 25)	3,9%	42,1%	44,1%	8,6%	1,3%
Retail	**Senior**	0,0%	0,0%	88,7%	8,4%	2,8%
	Non-Senior	0,0%	0,0%	87,0%	8,7%	4,3%

The table facilitates the coefficients’ comparison and highlights some of the oddities of their calibration:

- for example, granularity (variable B) has an almost overwhelming relevance in the determination of “p” for “Wholesale” tranches , while it carries no weight for “Retail” ones. Conversely, maturity (variable E) plays a much more relevant - although always limited – role for “Retail” tranches than for “Wholesale” ones;
- the K_{irb} weight is overall very significant, with an average value equal to 53,3% and reaching its peak for senior “Retail” tranches (88,7%). However, the K_{irb} variable has a negative impact on the “p” parameter, implying a lower surcharge for lower quality assets and thus acting to partially counterbalance the K_{irb} variable direct effect in the capital charge formula. The economic foundation of this adjustment is however unclear.

It is also worth noting that, due to the significant negative impact of both the granularity and K_{irb} variables (with an average total weight of 88%), the “p” supervisory parameter tends to be equal to its floor (0,3) for securitizations characterized by high K_{irb} value and/or high granularity, i.e. a capital surcharge of 30%.

There is however no cap on the value of “p”.

Given the odd results presented in the previous tables, it would appear that the coarse differentiation of securitization transaction on the basis of the attributes Wholesale/Retail, Senior/Non-senior, Granular/Non-granular isn't sufficient to allow a proper alignment of the determined capital charges with the effective transactions' riskiness.

5. External Rating Based Approach (ERBA)

Like all the other approaches, the ERB Approach too has been re-calibrated with respect to the first proposal's RRBA, in trying to achieve greater consistency with the underlying portfolio's capital requirements, thus resulting in a substantial reduction of capital charges, particularly for senior tranches and higher quality assets.

The following table provides a comparison of the risk-weights (RWs) proposed under the ERB Approach with those of the current framework, highlighting (with grey shading) situations where new RWS are lower than current ones.

Rating	New Regulatory Framework - Senior Tranches					New Regulatory Framework - Non Senior Tranches					Current Framework
	Maturity 1 year	Maturity 2 years	Maturity 3 years	Maturity 4 years	Maturity 5 years	Maturity 1 year	Maturity 2 years	Maturity 3 years	Maturity 4 years	Maturity 5 years	All Maturity
AAA	15%	17,5%	20,0%	22,5%	25%	15%	31,3%	47,5%	63,8%	80%	7%
AA+	15%	20,0%	25,0%	30,0%	35%	15%	36,3%	57,5%	78,8%	100%	8%
AA	25%	31,3%	37,5%	43,8%	50%	30%	55,0%	80,0%	105,0%	130%	8%
AA-	30%	36,3%	42,5%	48,8%	55%	40%	67,5%	95,0%	122,5%	150%	8%
A+	40%	46,3%	52,5%	58,8%	65%	60%	87,5%	115,0%	142,5%	170%	10%
A	50%	56,3%	62,5%	68,8%	75%	80%	107,5%	135,0%	162,5%	190%	12%
A-	60%	67,5%	75,0%	82,5%	90%	120%	145,0%	170,0%	195,0%	220%	20%
BBB+	75%	83,8%	92,5%	101,3%	110%	170%	195,0%	220,0%	245,0%	270%	35%
BBB	90%	100,0%	110,0%	120,0%	130%	220%	245,0%	270,0%	295,0%	320%	60%
BBB-	120%	132,5%	145,0%	157,5%	170%	330%	355,0%	380,0%	405,0%	430%	100%
BB+	140%	155,0%	170,0%	185,0%	200%	470%	500,0%	530,0%	560,0%	590%	250%
BB	160%	177,5%	195,0%	212,5%	230%	620%	657,5%	695,0%	732,5%	770%	425%
BB-	200%	222,5%	245,0%	267,5%	290%	750%	780,0%	810,0%	840,0%	870%	650%
B+	250%	277,5%	305,0%	332,5%	360%	900%	915,0%	930,0%	945,0%	960%	1250%
B	310%	337,5%	365,0%	392,5%	420%	1050%	1050,0%	1050,0%	1050,0%	1050%	1250%
B-	380%	395,0%	410,0%	425,0%	440%	1130%	1130,0%	1130,0%	1130,0%	1130%	1250%
CCC [+ / -]	460%	477,5%	495,0%	512,5%	530%	1250%	1250,0%	1250,0%	1250,0%	1250%	1250%
Below CCC-	1250%	1250,0%	1250,0%	1250,0%	1250%	1250%	1250,0%	1250,0%	1250,0%	1250%	1250%

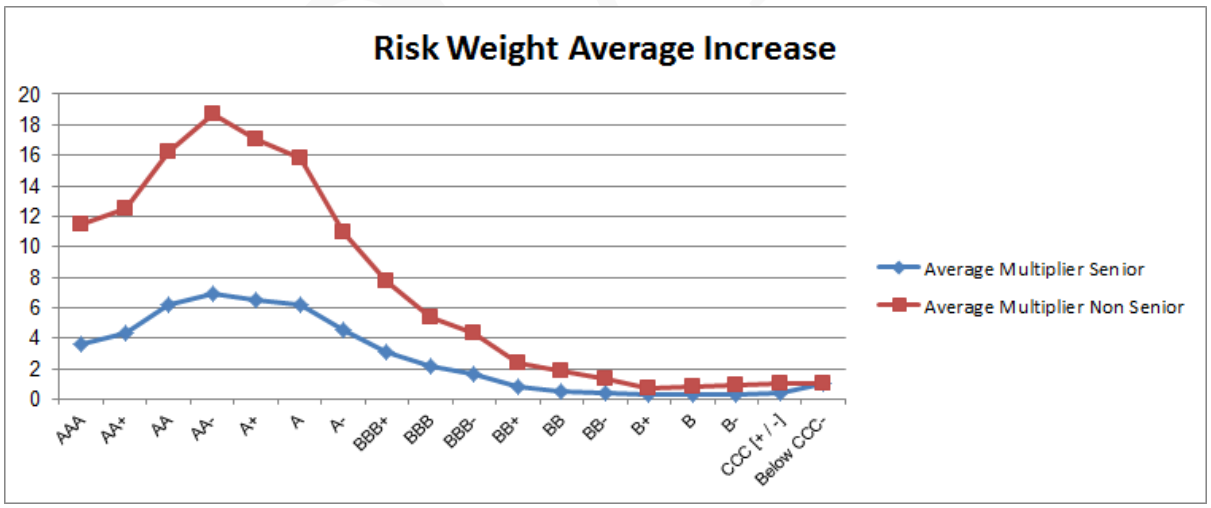
The following considerations can be drawn:

- the further reduction of RWs for low quality tranches introduced by the new Consultative Document could be justified on grounds of the lower model risk involved by these tranches with respect to high quality ones (where the capital charge is determined in correspondence with the furthest percentiles in the tail of the distribution function). However, this additional downward revision reinforces the comment, already offered in relation to the first Consultative Document, that the tilting of the RWs scale at the BB+ level - with a concomitant lowering of RWs for poorer quality tranches and increasing of RWs for better quality ones - would have the rather

unfair effect of rewarding banks currently holding low quality portfolios instead of banks that have invested more prudently;

- on the other hand, the relatively more sizeable downward revision of RWs for high quality (Investment Grade) senior and non-senior tranches, introduced in this new proposal, does not go far enough to rectify the excessive increase of these RWs introduced with the first Consultative Document and therefore doesn't alter our view that **high quality tranches would be too penalised.** The revised framework would effectively imply a significant misalignment in the credit risk treatment of securitised exposures with respect to that of the underlying non-securitised assets. For example, using, in a reverse engineering exercise, Intesa SanPaolo's Corporate IRB model for the K_{irb} calculation to derive the implied average PD consistent with a RW equal to that assigned by the ERB Approach to a 5-year AAA tranche (i.e.25%) would yield a result of 0,13%, which - according to CRA's PD matrix - corresponds to a rating equal to BBB+ for the underlying asset.

  For evidence of the pattern of RWs' increases, see also the following graph plotting separately, for Senior and Non-Senior tranches, the RWs average increase by rating class under the second consultative paper with respect to the current situation. In particular, the graph makes apparent both a relatively higher RWs' increase for Non-Senior than for Senior tranches of equivalent rating and also a spiking of the RWs' increase in the AA- area (with RWs increasing on average up to 7 times for senior exposures and up to 19 times for non-senior ones). ADD suggestion.



Additionally, it's also worth pointing out that the Committee, in finalising its proposal, should try and **coordinate with the other regulatory initiatives** impacting securitisations and, in particular, with those setting new stricter requirements on Credit Rating Agencies' (CRAs) rating assignment procedures, so as to avoid a sort of "double-counting" of the riskiness of the exposures, as a result of the increased conservatism of both CRAs and regulators.

Finally, as an aside, we also believe that, if CRAs' ratings have to maintain a role in the regulatory framework, it might be beneficial to introduce a "due date" concept for them, in order to avoid the pro-cyclical effect of a simultaneous massive updating of "stale" ratings in conjunction with the occurrence of stress situations (as was the case in the 2008 crisis).

6. Standardised Approach

The SA proposed in the new Consultative Document is very similar to the Simplified Supervisory Formula Approach (SSFA) of the first document and is also almost identical to the formula proposed by the US regulators. However, in the US proposals, the "p" parameter (defined in the same way as in the IRBA, as a scaling factor of the underlyings' capital charge) is set at 1.5 for re-securitisations, and 0.5 for all other securitisation, while the Basel Committee proposes its setting at 1 for all securitisations.

The **"p" supervisory adjustment factor** would therefore oddly be more **conservative** than the one used in the US version, even if it is commonly demonstrated that US deals are riskier than EU transactions.

Looking more specifically at the risk-drivers included in the approach and at their calibration, it can be said that the SA is even more affected than the IRBA by the problem of not appropriately capturing the effective risk of the different securitisation exposures in the different transactions, due to:

- **its oversimplification,** where a single "p" parameter fixed at a value of 1 (i.e. a capital surcharge of 100%) applies across all assets and transaction types

- **a lack of consideration of the maturity of the transaction**. Senior and mezzanine tranches have different effective maturities depending on the collateral amortization. As the SA capital charge formula only includes the attachment and detachment points as variables describing the features of the tranches, RWs cannot be properly differentiated between senior tranches with a higher prepayment and a call date with respect to senior tranches with longer maturity**.**

7. Other specific considerations

Mixed Pools. In this second Consultative Document the Committee revises its proposed treatment of "Mixed Pools" by allowing banks to use the Internal Ratings-Based Approach, provided they assign a 1250% risk weight to residual exposures in the underlying pool for which K_{irb} cannot be calculated. Alternatively, banks may use the other approaches lower in the hierarchy.

While this constitutes a welcome change - as this type of pool is certainly significant, especially for investing and/or sponsoring banks - the requirement to apply such a high weight to the residual non-K_{irb} exposures seems too punitive. It introduces a total hiatus between positions for which K_{irb} can be computed and those for which it can't and effectively

implies that the IRBA would hardly ever be used, as it would penalize even pools with a very high share of IRB assets.

According to our calculations, carried out on a sample set of securitisation tranches differing by seniority, quality and underlying asset class, the break-even point between the relative IRBA-based capital charges (and RW) and the SA-based ones - in terms of percentage of exposures of the underlying portfolio for which K_{irb} can't be calculated - is generally so low (on average about 5%) that the proposed treatment of Mixed Pools could greatly reduce the number of cases when the adoption of IRBA is economically convenient, thus counterproductively undermining support for the development of internal risk assessment capacities. In other words, shares of non-K_{irb} positions of the underlying portfolio just slightly higher than the break-even ones presented in the following tables would be sufficient to make the application of the Standardised Approach more appealing than that of the IRBA.

The tables here-below report for the various types of tranches:

- the associated risk weights, computed both with the IRBA (assuming the underlying portfolio were entirely an IRB pool) and with the Standardised Approach (assuming the underlying portfolio were entirely a SA pool); as well as

- the break-even share of the non-K_{irb} positions (to be weighed at 1250%) in the underlying portfolio, i.e. the maximum share of non-K_{irb} positions acceptable for the tranche to have an IRBA-determined risk weight not greater than the SA one.

In particular, the first two tables summarize the results respectively for Senior tranches (with assumed attachment point = 25%) and Junior tranches (with assumed detachment point =10%) of high quality (AA-AAA) RMBS, CMBS and Corporate Loans portfolios' securitisations (with K_{irb} values respectively equal to 1.6%, 2.4% and 2.8%).

	RW IRBA (if Floor)	RW IRBA	RW SA (if Floor)	RW SA	%ptf 1250%
RMBS Senior	15,0%	0% (Kirb 1,6%)	15,0%	0,0%	0,0%
CMBS Senior	15,0%	0% (Kirb 2,4%)	15,0%	0,5%	6,9%
Corporate loans Senior	15,0%	0% (Kirb 2,8%)	19,6%	19,6%	14,9%

	RW IRBA (if Floor)	RW IRBA	RW SA (if Floor)	RW SA	%ptf 1250%
RMBS Junior	313,6%	313,6%	704,9%	704,9%	2,1%
CMBS Junior	467,4%	449,5%	922,3%	922,3%	2,8%
Corporate loans Junior	542,6%	521,2%	1232,6%	1232,6%	6,2%

The last table presents results for Senior and Junior securitisation tranches of worse quality portfolios (with K_{irb} values respectively equal to 5.75%, 6.55% and 6.95% for RMBS, CMBS and Corporate Loans).

	RW IRBA (if Floor)	RW IRBA	RW SA (if Floor)	RW SA	%ptf 1250%
RMBS Senior	15,0%	0,0%	15,0%	1,4%	5,4%
CMBS Senior	15,0%	0,1%	15,0%	5,4%	8,1%
Corporate loans Senior	15,0%	0,1%	50,4%	50,4%	12,5%
RMBS Junior	1003,8%	1003,8%	1011,5%	1011,5%	0,3%
CMBS Junior	1089,2%	1089,2%	1137,3%	1137,3%	0,8%
Corporate loans Junior	1124,9%	1124,9%	1250,0%	1250,0%	3,2%

A common pattern emerges from the analysis of the various tranches, in that – as one would expect – there generally would be more room for non-K_{irb} positions in the underlying portfolio (i.e. a higher break-even share of position weighed at 1250%) the higher the SA risk weights are with respect to the IRBA-determined ones (even though results are less meaningful for RMBS and CMBS Senior tranches, where the 15% floor would effectively kick-in). In any case, the break-even percentages would be very low in most circumstances.

Given all of the above, we would recommend replacing the 1250% risk weights for the non-K_{irb} positions within the pool with the SA risk weights to determine their capital charge, which - together with the K_{irb} charge calculated for the IRB assets - would determine the weighted average capital of the underlying portfolio to be fed in the IRBA formula.

Risk Weight Floor. Even though the second Consultative Document reduces the proposed RWs' floor from 20% to 15%, we still consider it inappropriately high.

In particular, a floor set at that level:

- would increase the discrepancy in prudential treatment between securitisations' tranches and covered bonds – whose RW under the SA is 10% and under the IRBA is (estimated) between 3 to 5 % - thus further orienting the banks' funding preferences towards the covered bond market;
- would still be more than double the lowest floor of the current securitisation framework (i.e. 7% for AAA senior tranches in the IRB world) and would be hit very often by high quality tranches (see for example the RMBS tranches analysed in the table presented sub para. 3), therefore compromising the risk-sensitivity of the capital charge calculations.

While we understand the Committee's concern to protect against model risk (especially in the case of senior tranches, where capital charges are determined in the tail of the distribution function), we would suggest that it considered differentiating its floor

definition by asset class – consistently with the approach suggested for the general recalibration – and lowering it for the higher quality securitisation assets.

Maturity. In our opinion, the current treatment of Maturity distorts the quantification of securitisation exposures' capital charges, inappropriately reflecting their effective risk. The negative impact of the maturity parameter on the risk-weights is too high, especially for high quality exposures.. A tranche that has a AAA rating and a maturity greater than 5 years will move from the current 7% RW to a 25% RW (under the ERBA).

Applying the proposed Maturity definition for a securitization exposure (based either on its unconditional cash flows' redemption estimation or on its legal maturity) would effectively imply the almost ubiquitous application of the 5-year cap, as tranches' cashflows are generally conditional and as their legal maturity most often exceeds 5 years.

Ideally, in order to properly take into account the different time to PIF (i.e. "payment in full") of the issued tranches, one should consider the weighted average life (WAL) of the tranche, derived from a simulation model of the cash flows of the collateral portfolio (based on historical default, prepayment and recovery rate data for each of the asset classes included in the portfolio).

Given, the Committee's concerns relating to the numerous assumptions underlying such models, a compromise solution improving on the current proposal could be that of using the underlying pool's WAL, based on uniform no prepayments' and no defaults' assumptions.

Moreover, for what concerns replenishing transactions, we would suggest revising the current requirement, that their maturity be determined by adding the longest possible maturity of any asset eligible to be added to the pool during the replenishment period to the remaining replenishment period, in order to take into account specific contractual safeguards. The most extreme of these would be the existence of contractual triggers based on portfolio performance, that would allow originators and/or investors to terminate the replenishment period. Banks shoud be allowed to treat exposures in this type of transactions as if they weren't replenishing.

Credit Enhancements. In our opinion, the current definition of Attachment and Detachment points often doesn't appropriately reflect the Credit Enhancement and the effective risk of a securitisation structure, thus distorting the quantification of each of the securitisation's tranches capital charges, .

In particular, credit enhancements are made up of subordinated tranches, cash reserve, and overcollateralization. Under the current framework and the second Consultative Document, Institutions have to calculate attachment and detachment points of a tranche on the basis of a definition of credit enhancement that describes it as the ratio between notional amount of all securitization exposures subordinate to the tranche in question and the total amount of exposures in the pool (i.e the collateral outstanding).

By "pulling down" the attachment and detachment points, this treatment penalises vertically all the tranches in the capital structure and doesn't reflect the effective collateral benefit in the transaction. The opposite could be said in the case of undercollateralisation.

8. Questions presented in the Consultative Document

***Question 1**: The Committee seeks input as to whether the proposed treatment of derivatives other than credit derivatives achieves an appropriate balance between risk sensitivity and simplicity; and welcomes respondents' views on how to improve upon the proposed treatment.*

We consider the proposed treatment of derivatives appropriate. Intesa SanPaolo does not hold amounts and/or number of derivatives transactions of such significance as to justify a different and more refined treatment.

***Question 2**: While the formulation of the Internal Ratings-Based Approach is much simpler than the MSFA, the Committee recognizes that there may be opportunities to make further simplifications by, for example, eliminating one or more of the four variables proposed to calculate "p," while achieving a degree of risk sensitivity similar to that of the MSFA. The Committee is interested in respondents' views on ways to simplify the parameterization of "p".*

The specification of the "p" parameter, in terms of variables either already affecting the K_{irb} calculation (such as Maturitiy and LGD) or directly entering the securitisation's esposures' capital charge calculation (such as K_{irb} itself) makes the evaluation of the overall impact of those variables on the capital charge itself not immediately obvious, therefore complicating the economic interpretation and raising concerns of double-counting.

We would therefore favour linking the calibration of "p" to a proper and transparent economic model such as the CMA (currently proposed by the AFA Group). Its specification would then follow from that of the model chosen for its calibration and from the calibration method.

***Question 3**: If respondents favored a pro rata calculation of the maximum capital requirement, the Committee would welcome arguments that justify that a pro rata cap would result in appropriately conservative capital requirements.*

We support a pro-rata calculation of the maximum capital requirement (where the reference capital requirement is that of the unsecuritised assets).

As the ultimate purpose of the risk weighted assets framework is to ensure that banks set aside capital commensurate to the potential loss on the exposures owned in the securitisation transactions, we believe that if the pro rata calculation of the maximum capital requirement were based on the largest percentage tranche-level holding (calculated in terms of nominal exposures), it would reflect the effective exposure in an adequately conservative way.

Allowance should however be given to a more lenient pro-rata calculation in the case of originators' exposures in the form of a "vertical slice". In this instance, in order to ensure capital neutrality - so that a certain pool of assets doesn't require more capital after securitization than before – the pro-rata calculation should be based on the ratio of the RWA

after securitization of the positions retained by the originator over the total RWA of the pool after securitization.