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Secretariat of the Basel Committee on Banking Supervision
Bank of International Settlements
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Dear Sir/Madam

Capital treatment for simple, transparent and comparable securitisations

The Australian Securitisation Forum (ASF) appreciates the opportunity to provide comments on the above BCBS consultative document released in November 2015.

ASF is the peak industry body representing the Australian securitisation and covered bonds markets. The ASF goals are to facilitate the formation of industry positions on policy and market matters, represent the Australian industry to local and global policymakers and regulators and to advance the professional standards of the industry through a comprehensive suite of educational courses and workshops. This submission is made by the ASF through its Regulatory and Prudential subcommittee.

The ASF supports the principles of designating of certain securitisations as being simple, transparent and comparable (STC) in the context of preferential regulatory capital treatment being applied to such transactions. We are currently in the process of responding to a second Discussion Paper and draft prudential standard on securitisation issued in November 2015 by the Australian Prudential Regulation Authority (APRA). APRA noted in its Discussion Paper the BCBS's consultative document and indicated its intention to address STC once the Basel Committee has finalised its proposals.

In summary, ASF believes that

- in addition to obtaining preferential capital treatment, securitisations that satisfy the STC criteria as applied by local regulators should also be eligible as:
 - i. HQLA for the purposes of the LCR; and,
 - ii. collateral in central banks cash liquidity operations.
- Basel should continuously have regard to the G20/FSB mandates to facilitate cross-border capital flows by focussing on harmonised STC product criteria and simple STC regulations across jurisdictions, reflecting the diverse nature of global debt capital markets and the respective real economies of the world that they serve.

Furthermore, we propose that qualification for, and the benefits of, STC should not be limited to certain jurisdictions, such as European Issuers. These limitations might arise directly (for example, by stating that the underlying assets must be domiciled in Europe) and indirectly (for example, by making the criteria too restrictive thereby excluding issuers from other jurisdictions whose conventional products could never comply¹). Accordingly, we request that any STC regime implemented for Australian securitisations be recognised as equivalent by other jurisdictions' regulators with an STC regime, and therefore be granted the same capital, liquidity and repo-eligibility benefits as a STC-compliant European issued securitisation transaction in other jurisdictions. The initiative to support securitisations through an STC approach will be most successful if it is not restricted by jurisdictional anomalies.

Our submission is structured in two parts. The first provides some comments on the questions posed in the BCBS Consultative Document. The second section comments on issues raised by the STC criteria for Australian securitisations.

Yours sincerely



Chris Dalton

CHIEF EXECUTIVE OFFICER

¹ A number of examples where making the criteria too restrictive would inadvertently exclude issuers from other jurisdictions are set out in Section 2 of this document.

SECTION 1

Question 1: 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?

The ASF supports the introduction of STC criteria into the capital framework. We support the general principle that regulatory capital should be calibrated to the risk of the exposure. Securitisations can vary in nature from simple and established securitisations to newer, esoteric or more complex securitisations.

Question 2: 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?

The additional criteria proposed to address the credit risk, granularity and relationship between the originator and servicer of the pool are relevant aspects of a securitisation to consider when determining regulatory capital for the transaction. Section 2 provides the ASF's views on the additional criteria outlined in the consultative document.

Question 3: What are respondents' views on the compliance mechanism and the supervision of compliance presented in this consultative document?

The ASF believes the compliance mechanism should be determined by local regulators as part of the implementation of a STC regime. The ASF notes that whilst STC criteria contain a degree of subjectivity, self-certification should not be problematic because transparency and market discipline (chiefly in the form of the on-going desire of sponsors to maintain their reputation and therefore future issuance capacity). However, where a local regulator deems self-certification unacceptable, ASF is not in support of third-party arbitrators being engaged to opine on whether or not a transaction meets STC criteria.

See our remarks in Section 2 in relation to cross-border mutual recognition/equivalence.

Question 4: What are respondents' views on the alternative capital requirements for STC securitisation presented in this consultative document?

In general, the ASF supports the lowering of the risk-weight floor for senior exposures in STC securitisations. We also note that some Australian securitisations are structured so that the senior exposure is tranching with the mezzanine tranche still being able to achieve a rating of 'AAA'. We

suggest the risk-weighting of mezzanine tranches should also be reduced commensurately with the reduction applied to the most senior exposure.

We support the adjustment to the non-neutrality framework to achieve an outcome where less risky underlying assets can benefit from lower capital charges.

We again support the principle that the risk weights in the relevant table for the rating-based approach (SEC-ERBA) should be reduced for STC securitisations.

SECTION 2

General

It is not clear from the Consultative Document whether a securitisation can move in and out of STC designation over time. Some of the criteria may lead to transactions complying some times and not at other times leading to capital volatility. It would be helpful for the approach in such circumstances to be clarified.

Role of supervisors in the determination of STC compliance

To ensure a level playing field for all securitisation players, we strongly support a regime where bank and non-bank lenders are able to benefit from the STC regime. As such, the regulatory body should extend to the regulatory body assigning a credit licence to a sponsor of a securitisation in Australia, (i.e. any entity with an ASIC credit licence should be able to satisfy STC criteria).

A. ASSET RISK

As an overarching comment, below are a number of examples whereby the criteria is too restrictive or too aligned to the European market, therefore inadvertently excluding a number of non-European Issuers from complying with STC, despite clearly meeting the principles STC set out to achieve. In a number of the ASF's responses below, we have stipulated that the criteria should be based on the local jurisdiction's requirements to comply with STC, and that compliance should afford any issuer with the same benefits as a European Issuer.

A1 Nature of assets

Homogeneity

We note that the example of auto loans reflects a typical US auto loan transaction and not a typical Australian auto loan transaction.

In Australia the following would be considered as part of a homogeneous pool:

- Retail assets may not amortise to zero but have a balloon payment at the maturity date of the loan
- Retail assets may be mixed with commercial assets (corporate/floorplan/dealer assets)
- Finance leases including novated leases (but not operating leases) could be included with loans
- Equipment is often mixed with auto assets in commercial pools

Any consideration of homogeneity should take into account typical pools in the Australian market.

Given the scope of the market and the number of jurisdictions the proposed framework spans, this criterion appears to be prescriptive and we recommend this too be more principles-based.

Commonly encountered market interest rates

We query if this is referring to interest rates on the assets or the liabilities of the securitisations? If assets, then most Australian securitisations of residential mortgages (i.e. RMBS) are based on mortgage rates set at the discretion of the lender so we query whether this satisfies the “*commonly encountered market interest rates*” requirement.

A2 Asset Performance History

The Consultative Document notes that performance history should cover at least seven years for non-retail exposures. Consideration should be given to the nature of the assets and their underlying term. For example, corporate receivables with a maturity of 30 days will revolve many times within seven years. This will also stifle new entrants.

We highlight the practical constraints in providing the amount of data over a 7-year time series to investors will create a high barrier to entry. Also we suggest guidance is provided on a sufficient implementation period.

A3 Payment Status

“receivables ... may not, at the time of inclusion in the pool, include obligations that are in default or delinquent...”

This will cause securitisations of acquisitions of portfolios to be excluded from being classified as STC as they will typically have some level of delinquency which is no different to a STC pool after a few years once delinquencies have arisen.

This will also exclude master trusts from STC as at the time of issue of a series of notes there will almost certainly be delinquencies in the ongoing pool. In Australia, typical securitisations of non-conforming mortgages include some loans in arrears.

Exclusion of credit impaired borrowers will exclude some non-conforming portfolios from being considered STC.

The requirement for at least one payment to have been made will exclude warehouses that settle receivables from being considered STC.

A5 Asset Selection and Transfer

“Investors should be able to assess the credit risk of the asset pool prior to their investment decisions...”

This may cause an issue for master trusts (and other revolving securitisations) as investors in earlier series will be exposed to assets subsequently added without getting a chance to assess them beforehand. We note that the accompanying paragraph contemplates eligibility criteria and is mainly focused on ruling out active management in an STC securitisation which we support. Clarification should be provided that the requirement for investors to be able to assess the credit risk prior to investment wouldn't apply to subsequent mortgages added to master trust structures.

A6 Initial and ongoing data

STC requires the initial portfolio to be reviewed by an independent third party. While issuers typically have a compliance framework in place to verify data provided to investors, this may be internally based. The cost of an external review is significant and would increase the transaction costs for each issue, in addition to the data compliance requirements imposed onto the issue. Further, it is noted that auditors will not allow results to be published in external documents without their consent as outlined in footnote 20 of the BCBS STC Document.

B. STRUCTURAL RISK

B8 (currency and interest rate asset and liability mismatches)

We believe there is a potential concern that in an Australian context total return swaps provided to many ADI RMBS deals could cause Australian issuers problems in the STC framework. It would be very difficult to provide sensitivity analysis requested by the discussion paper for total return swaps given the inability to mark-to-market (MtM) these derivatives. We therefore request guidance on

what sensitivity analysis is required to be performed. For example, will BCBS provide criteria for different types of swaps?

B12 (alignment of interest)

APRA has indicated there is unlikely to be skin in the game in an Australian context which would therefore make it impossible for Australian deals to meet this requirement. BCBS should respect the local regulator's position on skin in the game when imposing this criterion in the STC framework.

B9 Payment priorities and observability

"Failure to acquire sufficient new underlying exposures of similar credit quality" is listed as a required amortisation event which would not be typical for an Australian securitisation warehouse or master trust and should be removed or qualified by whether it is typical in the jurisdiction.

B11 Document disclosure and legal review

"Terms of the documentation of the securitisation should be reviewed by an appropriately experienced third party legal practice, such as a legal counsel already instructed by one of the transaction parties e.g. by the arranger or the trustee."

We suggest this should be clarified as to what the intent is. It is not clear to us what the review should cover and from whose perspective. Each legal counsel in a transaction will review some or all of the documents from the perspective of who they are representing.

B12 Alignment of interest

"...the originator or sponsor for the credit claims or receivables should retain a material net economic exposure..."

This should be dependent on each jurisdiction's own credit risk retention requirements. We are not in favour of STC creating an additional skin in the game requirement.

D. Additional criteria for capital purposes

We support BCBS's approach to revisit the parameters in criterion D15 once the ongoing revisions to the Standardised Approach to credit risk are finalised. We support the intent of criterion D16 to limit the concentration to individual obligors in a securitisation. Further it is recognised that the level of obligor concentration may vary between different asset classes. However, we suggest an approach based on effective number of exposures be adopted instead.

With respect to D17, we suggest that there be consideration given to circumstances where a regulated entity may not be the originator of a pool of assets but rather may now be the legal owner and servicer of the assets as a result of an acquisition of the organisation that originated the assets or an acquisition of the assets. Since the financial crisis a number of financial institutions have acquired other institutions and/or portfolios in Australia and the fact that the new owner was not the originator of the assets should not automatically disqualify asset pools from being eligible for preferential capital treatment as a STC securitisation.

D15 credit risk of underlying exposures

Standardised risk weight limits will preclude certain asset classes in Australia from STC (e.g. retail auto loans, non-conforming mortgages, and commercial mortgages). The limits will need to reflect the particular risk weights in a jurisdiction.

D16 Granularity of the pool

Limit of 1% may impact some securitisations. We suggest an approach based on number of *Effective Exposures* instead.