

TSI Comments on

Basel Committee on Banking Supervision – Consultative Document – Guidelines Identification and management of step-in risks (March 2007) (“Guidelines”)

Frankfurt am Main, May 2017

TSI welcomes the opportunity to comment on the revised Guidelines.

■ **General remarks**

We believe that it always depends on the circumstances of the individual cases whether a step-in risk exists or not. In order to reflect the individual cases appropriately any blanket approach should be avoided. Thus, the entities in combination with the indicators named in the document should only entail an in-depth self-assessment of step-in risks, but not constitute the general assumption of step-in risks.

If an institution draws the conclusion that existing risks are considered appropriately and comprehensively for example by the deduction of the first loss position of the securitisation from the CET1 and no further material risks exist then it should be possible to abstain from any additional regulatory consolidation or from the application of a conversion approach even if there are relations that could indicate potential step-in risks. Such individual assessment is legitimate, because the competent authority can review the appropriateness of the self-assessment.

In addition, we propose that only material potential step-in risks should be assessed. This could be implemented by a materiality threshold to be exceeded.

■ **Special remarks - ABCP programs**

As it regards securitisation programs such as ABCP programs, we think that is inappropriate to include an ABCP program which is fully supported by its sponsoring bank, irrespective of the fact whether or not its consolidated for accounting or regulatory purposes by such bank, into the scope of the "step-in risk" regime as the Guidelines (under para. 36 and 37) imply. Instead

we propose to explicitly exclude fully supported ABCP programs for the following reasons:

1. The Guidelines define "step-in risk" as the *"risk that a bank decides to provide financial support to an unconsolidated entity that is facing stress, in the absence of, or in excess of, any contractual obligations to provide such support."* (para. 14, emphasis added)
2. A fully supported ABCP program should already, by definition, not be an entity/a relationship that is covered by the "step-in risk" regime. When a bank decides to fully support an ABCP program, such support is nowadays typically done by way of a firm liquidity commitment granted to each transaction (i.e. receivables pool) under the program. Which means that (i) it is a firm commitment of the bank contractually agreed on day one (not left to the decision or discretion of the bank on a day thereafter), (ii) it covers the entire redemption amount of any ABCP issued and outstanding plus accrued interest and costs, and (iii) it is not limited to a borrowing base or similar test. I.e. should an ABCP program so supported face financial stress, the sponsoring bank must provide liquidity to the conduit sufficient for the issuer to redeem and repay all outstanding ABCP and this is because the bank is contractually obliged to do so. Unlike in partially supported ABCP programs (which were the prevailing form of ABCP programs in the run-up of the financial crisis in 2007), there is no need to provide any support in the absence or in excess of the contractually agreed support ("full means full"). Hence there remains, emerges or re-emerges no "step-in risk" from such relationship.

3. It would also be inappropriate, in the light of aim and purpose of the "step-in risk" regime, to include fully supported ABCP programs because there is no regulatory "gap" that needs to be closed. The regulatory requirements for liquidity commitments to ABCP programs changed dramatically over the last years since the financial crisis. As a consequence, a liquidity facility which a sponsor bank grants to its fully supported ABCP program is already subject to intensive regulatory scrutiny and comprehensive measures for all relevant regulatory purposes, including enhanced capital adequacy, liquidity, large exposure, disclosure and risk management requirements. We do not think that the "comprehensive measures" (now proposed under para. 70 et seq. of the Guidelines) can add anything of value here. Rather to the contrary, we are afraid that measures in addition of the existing regulatory framework would finally prejudice fully supported ABCP programs making them again less attractive and thereby eliminating an important tool to refinance the real economy.

■ **Special remarks - Asset Backed Securities**

According to paragraph 72 a consolidation shall be applied if the indicators in paragraph 71 are observed in order to address incomplete implementation of existing accounting and regulatory frameworks. In particular, the bullet point three of paragraph 71 is problematic. According to that bullet point a consolidation ought to be applied if there are organisational or financial relations that, in substance, assign to the bank the majority of the risks and/or of the benefits arising from the activities of the entities. This substantially corresponds to the former IAS 27 in conjunction with SIC 12 that required a commercial consolidation of the SPV involved in the securitisation. Also

according to IFRS 10 in most of such cases a commercial consolidation might be required. However, according to the present supervisory regulations such SPVs included in the commercial consolidation are not to include in the consolidation for supervisory purposes upon reasonable grounds. Such SPVs are usually no financial institutions according to Article 4 (1) (26) CRR. Thus, a deconsolidation of such SPVs is required. The deconsolidation of these SPVs is a prerequisite to obtain capital relief due to a significant and effective risk transfer for the underlying assets from the originating institution to the SPV. Without a deconsolidation for supervisory purposes such effectively transferred underlying assets to the SPV would still be subject to capital requirements and thus to be backed with equity. Hence, capital relief would become impossible.

The deconsolidation of such SPVs is justified, because the question whether the underlying assets, sold to the SPV, are subject to capital requirements or not is subject to an effective risk transfer. If no effective risk transfer has occurred then the sold underlying assets are still subject to capital requirements. This has to be assessed for traditional securitisations according to article 243 CRR. An effective risk transfer has occurred in any case for the sold underlying assets if the originator only holds securitisation positions due to the provided credit enhancements e.g. in the form of overcollateralisation and cash reserve accounts and if the originator applies a risk weight of 1,250% or deduct the first loss position from the CET1 capital. In such a case the risk of the originator is limited to the first loss position that is subject to a capital requirement that reflects the theoretically maximal potential loss. If there are no further material risks that could imply a step-in risk from the structure, which is in many plain vanilla transactions the case, then there is no step-in risk beyond the already contractually obligations. Hence, it should be possible to abstain from any further consolidation if there is no step-in risk beyond the contractual

obligation to be geared to bear the first loss that is already subject to maximal capital requirements. Otherwise, capital relief by means of securitisation would virtually become impossible in the future, because it is a typical feature of traditional securitisations that are well established in the market that the originator retains the first loss position by means of overcollateralisation and cash reserves on cash reserve accounts. Such outcome would be overly conservative and not legitimated by the actual risks.

TSI – What we do

Securitisation in Germany and TSI – the two belong together. True Sale International GmbH (TSI) was set up in 2004 as an initiative of the German securitisation industry with the aim of promoting the German securitisation market.

Nowadays TSI Partners come from all areas of the German securitisation market – banks, consulting firms and service providers, law firms, rating agencies and business associations. They all have substantial expertise and experience in connection with the securitisation market and share a common interest in developing this market further. TSI Partners derive particular benefit from TSI's lobbying work and its PR activities.

Furthermore TSI's concern has always been to establish a brand for German securitization which is founded on clearly defined rules for transparency, disclosure, lending and loan processing. Detailed guidelines and samples for investor reporting ensure high transparency for investors and the Originator guarantees, by means of a declaration of undertaking, the application of clear rules for lending and loan processing as well as for sales and back office incentive systems. The offering circular, the declaration of undertaking and all investor reports are publicly available on the TSI website, thus ensuring free access to relevant information.



Another objective has always been to give banks an opportunity to securitise loans under German law on the basis of a standardised procedure agreed with all market participants.

And finally the goal is to create a platform for the German securitization industry and its concerns and to bridge the gap to politics and industry.

Events and Congress of TSI

Events of TSI provide opportunities for specialists in the fields of economics and politics to discuss current topics relating to the credit and securitisation markets. The TSI Congress in Berlin is the annual meeting place for securitisation experts and specialists from the credit and loan portfolio management, risk management, law, trade and treasury departments at banks, experts from law firms, auditing companies, rating agencies, service providers, consulting companies and investors from Germany and other countries. Many representatives of German business and politics and academics working in this field take advantage of the TSI Congress to exchange professional views and experience. As a venue, Berlin is at the pulse of German politics and encourages an exchange between the financial market and the world of politics.