

# Basel Committee on Banking Supervision

CRE

Calculation of RWA for credit  
risk

CRE40

Securitisation: general  
provisions

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First version in the format of the consolidated  
framework.



BANK FOR INTERNATIONAL SETTLEMENTS



## Scope and definitions of transactions covered under the securitisation framework

- 40.1** Banks must apply the securitisation framework for determining regulatory capital requirements on exposures arising from traditional and synthetic securitisations or similar structures that contain features common to both. Since securitisations may be structured in many different ways, the capital treatment of a securitisation exposure must be determined on the basis of its economic substance rather than its legal form. Similarly, supervisors will look to the economic substance of a transaction to determine whether it should be subject to the securitisation framework for purposes of determining regulatory capital. Banks are encouraged to consult with their national supervisors when there is uncertainty about whether a given transaction should be considered a securitisation. For example, transactions involving cash flows from real estate (eg rents) may be considered specialised lending exposures, if warranted.
- 40.2** A traditional securitisation is a structure where the cash flow from an underlying pool of exposures is used to service at least two different stratified risk positions or tranches reflecting different degrees of credit risk. Payments to the investors depend upon the performance of the specified underlying exposures, as opposed to being derived from an obligation of the entity originating those exposures. The stratified/tranched structures that characterise securitisations differ from ordinary senior/subordinated debt instruments in that junior securitisation tranches can absorb losses without interrupting contractual payments to more senior tranches, whereas subordination in a senior/subordinated debt structure is a matter of priority of rights to the proceeds of liquidation.
- 40.3** A synthetic securitisation is a structure with at least two different stratified risk positions or tranches that reflect different degrees of credit risk where credit risk of an underlying pool of exposures is transferred, in whole or in part, through the use of funded (eg credit-linked notes) or unfunded (eg credit default swaps) credit derivatives or guarantees that serve to hedge the credit risk of the portfolio. Accordingly, the investors' potential risk is dependent upon the performance of the underlying pool.
- 40.4** Banks' exposures to a securitisation are hereafter referred to as "securitisation exposures". Securitisation exposures can include but are not restricted to the following: asset-backed securities, mortgage-backed securities, credit enhancements, liquidity facilities, interest rate or currency swaps, credit derivatives and tranched cover as described in [CRE22.93](#). Reserve accounts, such as cash collateral accounts, recorded as an asset by the originating bank must also be treated as securitisation exposures.

## 40.5

A resecuritisation exposure is a securitisation exposure in which the risk associated with an underlying pool of exposures is tranced and at least one of the underlying exposures is a securitisation exposure. In addition, an exposure to one or more resecuritisation exposures is a resecuritisation exposure. An exposure resulting from retransching of a securitisation exposure is not a resecuritisation exposure if the bank is able to demonstrate that the cash flows to and from the bank could be replicated in all circumstances and conditions by an exposure to the securitisation of a pool of assets that contains no securitisation exposures.

**40.6** Underlying instruments in the pool being securitised may include but are not restricted to the following: loans, commitments, asset-backed and mortgage-backed securities, corporate bonds, equity securities, and private equity investments. The underlying pool may include one or more exposures.

## Definitions and general terminology

**40.7** For risk-based capital purposes, a bank is considered to be an originator with regard to a certain securitisation if it meets either of the following conditions:

- (1) the bank originates directly or indirectly underlying exposures included in the securitisation; or
- (2) the bank serves as a sponsor of an asset-backed commercial paper (ABCP) conduit or similar programme that acquires exposures from third-party entities. In the context of such programmes, a bank would generally be considered a sponsor and, in turn, an originator if it, in fact or in substance, manages or advises the programme, places securities into the market, or provides liquidity and/or credit enhancements.

**40.8** An ABCP programme predominantly issues commercial paper to third-party investors with an original maturity of one year or less and is backed by assets or other exposures held in a bankruptcy-remote, special purpose entity.

**40.9** A clean-up call is an option that permits the securitisation exposures (eg asset-backed securities) to be called before all of the underlying exposures or securitisation exposures have been repaid. In the case of traditional securitisations, this is generally accomplished by repurchasing the remaining securitisation exposures once the pool balance or outstanding securities have fallen below some specified level. In the case of a synthetic transaction, the clean-up call may take the form of a clause that extinguishes the credit protection.

#### **40.10**

A credit enhancement is a contractual arrangement in which the bank or other entity retains or assumes a securitisation exposure and, in substance, provides some degree of added protection to other parties to the transaction.

**40.11** A credit-enhancing interest-only strip (I/O) is an on-balance sheet asset that

- (1) represents a valuation of cash flows related to future margin income, and
- (2) is subordinated.

**40.12** An early amortisation provision is a mechanism that, once triggered, accelerates the reduction of the investor's interest in underlying exposures of a securitisation of revolving credit facilities and allows investors to be paid out prior to the originally stated maturity of the securities issued. A securitisation of revolving credit facilities is a securitisation in which one or more underlying exposures represent, directly or indirectly, current or future draws on a revolving credit facility. Examples of revolving credit facilities include but are not limited to credit card exposures, home equity lines of credit, commercial lines of credit, and other lines of credit.

**40.13** Excess spread (or future margin income) is defined as gross finance charge collections and other income received by the trust or special purpose entity (SPE, as defined below) minus certificate interest, servicing fees, charge-offs, and other senior trust or SPE expenses.

**40.14** Implicit support arises when a bank provides support to a securitisation in excess of its predetermined contractual obligation.

**40.15** For risk-based capital purposes, an internal ratings-based (IRB) pool means a securitisation pool for which a bank is able to use an IRB approach to calculate capital requirements for all underlying exposures given that it has approval to apply IRB for the type of underlying exposures and it has sufficient information to calculate IRB capital requirements for these exposures. Supervisors should expect that a bank with supervisory approval to calculate capital requirements for the type of underlying exposures be able to obtain sufficient information to estimate capital requirements for the underlying pool of exposures using an IRB approach. A bank which has a supervisory-approved IRB approach for the entire pool of exposures underlying a given securitisation exposure that cannot estimate capital requirements for all underlying exposures using an IRB approach would be expected to demonstrate to its supervisor why it is unable to do so. However, a supervisor may prohibit a bank from treating an IRB pool as such in the case of particular structures or transactions, including transactions with highly complex loss allocations, tranches whose credit enhancement could be eroded for reasons other than portfolio losses, and tranches of portfolios with high internal correlations (such as portfolios with high exposure to single sectors or with high geographical concentration).

**40.16** For risk-based capital purposes, a mixed pool means a securitisation pool for which a bank is able to calculate IRB parameters for some, but not all, underlying exposures in a securitisation.

**40.17** For risk-based capital purposes, a standardised approach (SA) pool means a securitisation pool for which a bank does not have approval to calculate IRB parameters for any underlying exposures; or for which, while the bank has approval to calculate IRB parameters for some or all of the types of underlying exposures, it is unable to calculate IRB parameters for any underlying exposures because of lack of relevant data, or is prohibited by its supervisor from treating the pool as an IRB pool pursuant to [CRE40.15](#).

**40.18** A securitisation exposure (tranche) is considered to be a senior exposure (tranche) if it is effectively backed or secured by a first claim on the entire amount of the assets in the underlying securitised pool.<sup>1</sup> While this generally includes only the most senior position within a securitisation transaction, in some instances there may be other claims that, in a technical sense, may be more senior in the waterfall (eg a swap claim) but may be disregarded for the purpose of determining which positions are treated as senior. Different maturities of several senior tranches that share pro rata loss allocation shall have no effect on the seniority of these tranches, since they benefit from the same level of credit enhancement. The material effects of differing tranche maturities are captured by maturity adjustments on the risk weights to be assigned to the securitisation exposures. For example:

- (1) In a typical synthetic securitisation, an unrated tranche would be treated as a senior tranche, provided that all of the conditions for inferring a rating from a lower tranche that meets the definition of a senior tranche are fulfilled.
- (2) In a traditional securitisation where all tranches above the first-loss piece are rated, the most highly rated position would be treated as a senior tranche. When there are several tranches that share the same rating, only the most senior tranche in the cash flow waterfall would be treated as senior (unless the only difference among them is the effective maturity). Also, when the different ratings of several senior tranches only result from a difference in maturity, all of these tranches should be treated as a senior tranche.
- (3) Usually, a liquidity facility supporting an ABCP programme would not be the most senior position within the programme; the commercial paper, which benefits from the liquidity support, typically would be the most senior position. However, a liquidity facility may be viewed as covering all losses on the underlying receivables pool that exceed the amount of overcollateralisation/reserves provided by the seller and as being most senior if it is sized to cover all of the outstanding commercial paper and other senior debt supported by the pool, so that no cash flows from the underlying pool could be transferred to the other creditors until any liquidity draws were repaid in full. In such a case, the liquidity facility can be treated as a senior exposure. Otherwise, if these conditions are not satisfied, or if for other reasons the liquidity facility constitutes a mezzanine position in economic substance rather than a senior position in the underlying pool, the liquidity facility should be treated as a non-senior exposure.

#### *Footnotes*

- 1 *If a senior tranche is retranching or partially hedged (ie not on a pro rata basis), only the new senior part would be treated as senior for capital purposes.*

**40.19** For risk-based capital purposes, the exposure amount of a securitisation exposure is the sum of the on-balance sheet amount of the exposure, or carrying value – which takes into account purchase discounts and writedowns/specific provisions the bank took on this securitisation exposure – and the off-balance sheet exposure amount, where applicable.

**40.20** A bank must measure the exposure amount of its off-balance sheet securitisation exposures as follows:

- (1) for credit risk mitigants sold or purchased by the bank, use the treatment set out in [CRE40.56](#) to [CRE40.62](#);
- (2) for facilities that are not credit risk mitigants, use a credit conversion factor (CCF) of 100%. If contractually provided for, servicers may advance cash to ensure an uninterrupted flow of payments to investors so long as the servicer is entitled to full reimbursement and this right is senior to other claims on cash flows from the underlying pool of exposures. At national discretion, the undrawn portion of servicer cash advances or facilities that are unconditionally cancellable without prior notice may receive the CCF for unconditionally cancellable commitments under [CRE20](#). For this purpose, a national supervisor that uses this discretion must develop an appropriately conservative method for measuring the amount of the undrawn portion; and
- (3) for derivatives contracts other than credit risk derivatives contracts, such as interest rate or currency swaps sold or purchased by the bank, use the measurement approach set out in [CRE51](#).

**40.21** An SPE is a corporation, trust or other entity organised for a specific purpose, the activities of which are limited to those appropriate to accomplish the purpose of the SPE, and the structure of which is intended to isolate the SPE from the credit risk of an originator or seller of exposures. SPEs, normally a trust or similar entity, are commonly used as financing vehicles in which exposures are sold to the SPE in exchange for cash or other assets funded by debt issued by the trust.

**40.22** For risk-based capital purposes, tranche maturity ( $M_T$ ) is the tranche's remaining effective maturity in years and can be measured at the bank's discretion in either of the following manners. In all cases,  $M_T$  will have a floor of one year and a cap of five years.

- (1) As the euro<sup>2</sup> weighted-average maturity of the contractual cash flows of the tranche, as expressed below, where  $CF_t$  denotes the cash flows (principal, interest payments and fees) contractually payable by the borrower in period  $t$ . The contractual payments must be unconditional and must not be dependent on the actual performance of the securitised assets. If such unconditional contractual payment dates are not available, the final legal maturity shall be used.

$$M_T = \frac{\sum_t tCF_t}{\sum_t CF_t}$$



- (2) On the basis of final legal maturity of the tranche, where  $M_L$  is the final legal maturity of the tranche.

$$M_T = 1 + 80\%(M_L - 1)$$

*Footnotes*

2 *The euro designation is used for illustrative purposes only.*

**40.23** When determining the maturity of a securitisation exposure, banks should take into account the maximum period of time they are exposed to potential losses from the securitised assets. In cases where a bank provides a commitment, the bank should calculate the maturity of the securitisation exposure resulting from this commitment as the sum of the contractual maturity of the commitment and the longest maturity of the asset(s) to which the bank would be exposed after a draw has occurred. If those assets are revolving, the longest contractually possible remaining maturity of the asset that might be added during the revolving period would apply, rather than the (longest) maturity of the assets currently in the pool. The same treatment applies to all other instruments where the risk of the commitment/protection provider is not limited to losses realised until the maturity of that instrument (eg total return swaps). For credit protection instruments that are only exposed to losses that occur up to the maturity of that instrument, a bank would be allowed to apply the contractual maturity of the instrument and would not have to look through to the protected position.

### **Operational requirements for the recognition of risk transference**

**40.24** An originating bank may exclude underlying exposures from the calculation of risk-weighted assets only if all of the following conditions have been met. Banks meeting these conditions must still hold regulatory capital against any securitisation exposures they retain.

- (1) Significant credit risk associated with the underlying exposures has been transferred to third parties.

- (2) The transferor does not maintain effective or indirect control over the transferred exposures. The exposures are legally isolated from the transferor in such a way (eg through the sale of assets or through subparticipation) that the exposures are put beyond the reach of the transferor and its creditors, even in bankruptcy or receivership. Banks should obtain legal opinion<sup>3</sup> that confirms true sale. The transferor's retention of servicing rights to the

exposures will not necessarily constitute indirect control of the exposures. The transferor is deemed to have maintained effective control over the transferred credit risk exposures if it:

- (a) is able to repurchase from the transferee the previously transferred exposures in order to realise their benefits; or
  - (b) is obligated to retain the risk of the transferred exposures.
- (3) The securities issued are not obligations of the transferor. Thus, investors who purchase the securities only have claim to the underlying exposures.
- (4) The transferee is an SPE and the holders of the beneficial interests in that entity have the right to pledge or exchange them without restriction, unless such restriction is imposed by a risk retention requirement.
- (5) Clean-up calls must satisfy the conditions set out in [CRE40.28](#).
- (6) The securitisation does not contain clauses that
- (a) require the originating bank to alter the underlying exposures such that the pool's credit quality is improved unless this is achieved by selling exposures to independent and unaffiliated third parties at market prices;
  - (b) allow for increases in a retained first-loss position or credit enhancement provided by the originating bank after the transaction's inception; or
  - (c) increase the yield payable to parties other than the originating bank, such as investors and third-party providers of credit enhancements, in response to a deterioration in the credit quality of the underlying pool.
- (7) There must be no termination options/triggers except eligible clean-up calls, termination for specific changes in tax and regulation or early amortisation provisions such as those set out in [CRE40.27](#).

*Footnotes*

<sup>3</sup> *Legal opinion is not limited to legal advice from qualified legal counsel, but allows written advice from in-house lawyers.*

**40.25** For synthetic securitisations, the use of credit risk mitigation (CRM) techniques (ie collateral, guarantees and credit derivatives) for hedging the underlying exposure may be recognised for risk-based capital purposes only if the conditions outlined below are satisfied:

- (1) Credit risk mitigants must comply with the requirements set out in [CRE22](#).
- (2) Eligible collateral is limited to that specified in [CRE22.37](#) and [CRE22.39](#). Eligible collateral pledged by SPEs may be recognised.
- (3) Eligible guarantors are defined in [CRE22.90](#). Banks may not recognise SPEs as eligible guarantors in the securitisation framework.
- (4) Banks must transfer significant credit risk associated with the underlying exposures to third parties.

- (5) The instruments used to transfer credit risk may not contain terms or conditions that limit the amount of credit risk transferred, such as those provided below:
- (a) clauses that materially limit the credit protection or credit risk transference (eg an early amortisation provision in a securitisation of revolving credit facilities that effectively subordinates the bank's interest; significant materiality thresholds below which credit protection is deemed not to be triggered even if a credit event occurs; or clauses that allow for the termination of the protection due to deterioration in the credit quality of the underlying exposures);
  - (b) clauses that require the originating bank to alter the underlying exposures to improve the pool's average credit quality;
  - (c) clauses that increase the banks' cost of credit protection in response to deterioration in the pool's quality;
  - (d) clauses that increase the yield payable to parties other than the originating bank, such as investors and third-party providers of credit enhancements, in response to a deterioration in the credit quality of the reference pool; and
  - (e) clauses that provide for increases in a retained first-loss position or credit enhancement provided by the originating bank after the transaction's inception.
- (6) A bank should obtain legal opinion that confirms the enforceability of the contract.
- (7) Clean-up calls must satisfy the conditions set out in [CRE40.28](#).

**40.26** A securitisation transaction is deemed to fail the operational requirements set out in [CRE40.24](#) or [CRE40.25](#) if the bank

- (1) originates/sponsors a securitisation transaction that includes one or more revolving credit facilities, and

- (2) the securitisation transaction incorporates an early amortisation or similar provision that, if triggered, would
  - (a) subordinate the bank's senior or pari passu interest in the underlying revolving credit facilities to the interest of other investors;
  - (b) subordinate the bank's subordinated interest to an even greater degree relative to the interests of other parties; or
  - (c) in other ways increases the bank's exposure to losses associated with the underlying revolving credit facilities.

**40.27** If a securitisation transaction contains one of the following examples of an early amortisation provision and meets the operational requirements set forth in [CRE40.24](#) or [CRE40.25](#), an originating bank may exclude the underlying exposures associated with such a transaction from the calculation of risk-weighted assets, but must still hold regulatory capital against any securitisation exposures they retain in connection with the transaction:

- (1) replenishment structures where the underlying exposures do not revolve and the early amortisation ends the ability of the bank to add new exposures;
- (2) transactions of revolving credit facilities containing early amortisation features that mimic term structures (ie where the risk on the underlying revolving credit facilities does not return to the originating bank) and where the early amortisation provision in a securitisation of revolving credit facilities does not effectively result in subordination of the originator's interest;
- (3) structures where a bank securitises one or more revolving credit facilities and where investors remain fully exposed to future drawdowns by borrowers even after an early amortisation event has occurred; or
- (4) the early amortisation provision is solely triggered by events not related to the performance of the underlying assets or the selling bank, such as material changes in tax laws or regulations.

**40.28** For securitisation transactions that include a clean-up call, no capital will be required due to the presence of a clean-up call if the following conditions are met:

- (1) the exercise of the clean-up call must not be mandatory, in form or in substance, but rather must be at the discretion of the originating bank;

- (2) the clean-up call must not be structured to avoid allocating losses to credit enhancements or positions held by investors or otherwise structured to provide credit enhancement; and
- (3) the clean-up call must only be exercisable when 10% or less of the original underlying portfolio or securities issued remains, or, for synthetic securitisations, when 10% or less of the original reference portfolio value remains.

**40.29** Securitisation transactions that include a clean-up call that does not meet all of the criteria stated in [CRE40.28](#) result in a capital requirement for the originating bank. For a traditional securitisation, the underlying exposures must be treated as if they were not securitised. Additionally, banks must not recognise in regulatory capital any gain on sale, in accordance with [CAP30.14](#). For synthetic securitisations, the bank purchasing protection must hold capital against the entire amount of the securitised exposures as if they did not benefit from any credit protection. If a synthetic securitisation incorporates a call (other than a clean-up call) that effectively terminates the transaction and the purchased credit protection on a specific date, the bank must treat the transaction in accordance with [CRE40.65](#).

**40.30** If a clean-up call, when exercised, is found to serve as a credit enhancement, the exercise of the clean-up call must be considered a form of implicit support provided by the bank and must be treated in accordance with the supervisory guidance pertaining to securitisation transactions.

## **Due diligence requirements**

**40.31** For a bank to use the risk weight approaches of the securitisation framework, it must have the information specified in [CRE40.32](#) to [CRE40.34](#). Otherwise, the bank must assign a 1250% risk weight to any securitisation exposure for which it cannot perform the required level of due diligence.

**40.32** As a general rule, a bank must, on an ongoing basis, have a comprehensive understanding of the risk characteristics of its individual securitisation exposures, whether on- or off-balance sheet, as well as the risk characteristics of the pools underlying its securitisation exposures.

**40.33** Banks must be able to access performance information on the underlying pools on an ongoing basis in a timely manner. Such information may include, as appropriate: exposure type; percentage of loans 30, 60 and 90 days past due; default rates; prepayment rates; loans in foreclosure; property type; occupancy;

average credit score or other measures of creditworthiness; average loan-to-value ratio; and industry and geographical diversification. For resecuritisations, banks should have information not only on the underlying securitisation tranches, such as the issuer name and credit quality, but also on the characteristics and performance of the pools underlying the securitisation tranches.

**40.34** A bank must have a thorough understanding of all structural features of a securitisation transaction that would materially impact the performance of the bank's exposures to the transaction, such as the contractual waterfall and waterfall-related triggers, credit enhancements, liquidity enhancements, market value triggers, and deal-specific definitions of default.

### **Calculation of capital requirements and risk-weighted assets**

**40.35** Regulatory capital is required for banks' securitisation exposures, including those arising from the provision of credit risk mitigants to a securitisation transaction, investments in asset-backed securities, retention of a subordinated tranche, and extension of a liquidity facility or credit enhancement, as set forth in the following sections. Repurchased securitisation exposures must be treated as retained securitisation exposures.

**40.36** For the purposes of the expected loss (EL) provision calculation set out in [CRE35](#), securitisation exposures do not contribute to the EL amount. Similarly, neither general nor specific provisions against securitisation exposures or underlying assets still held on the balance sheet of the originator are to be included in the measurement of eligible provisions. However, originator banks can offset 125% risk-weighted securitisation exposures by reducing the securitisation exposure amount by the amount of their specific provisions on underlying assets of that transaction and non-refundable purchase price discounts on such underlying assets. Specific provisions on securitisation exposures will be taken into account in the calculation of the exposure amount, as defined in [CRE40.19](#) and [CRE40.20](#). General provisions on underlying securitised exposures are not to be taken into account in any calculation.

- 40.37** The risk-weighted asset amount of a securitisation exposure is computed by multiplying the exposure amount by the appropriate risk weight determined in accordance with the hierarchy of approaches in [CRE40.41](#) to [CRE40.48](#). Risk weight caps for senior exposures in accordance with [CRE40.50](#) and [CRE40.51](#) or overall caps in accordance with [CRE40.52](#) to [CRE40.55](#) may apply. Overlapping exposures will be risk-weighted as defined in [CRE40.38](#) and [CRE40.40](#).
- 40.38** For the purposes of calculating capital requirements, a bank's exposure A overlaps another exposure B if in all circumstances the bank will preclude any loss for the bank on exposure B by fulfilling its obligations with respect to exposure A. For example, if a bank provides full credit support to some notes and holds a portion of these notes, its full credit support obligation precludes any loss from its exposure to the notes. If a bank can verify that fulfilling its obligations with respect to exposure A will preclude a loss from its exposure to B under any circumstance, the bank does not need to calculate risk-weighted assets for its exposure B.
- 40.39** To arrive at an overlap, a bank may, for the purposes of calculating capital requirements, split or expand<sup>4</sup> its exposures. For example, a liquidity facility may not be contractually required to cover defaulted assets or may not fund an ABCP programme in certain circumstances. For capital purposes, such a situation would not be regarded as an overlap to the notes issued by that ABCP conduit. However, the bank may calculate risk-weighted assets for the liquidity facility as if it were expanded (either in order to cover defaulted assets or in terms of trigger events) to preclude all losses on the notes. In such a case, the bank would only need to calculate capital requirements on the liquidity facility

#### *Footnotes*

<sup>4</sup> *That is, splitting exposures into portions that overlap with another exposure held by the bank and other portions that do not overlap; and expanding exposures by assuming for capital purposes that obligations with respect to one of the overlapping exposures are larger than those established contractually. The latter could be done, for instance, by expanding either the trigger events to exercise the facility and/or the extent of the obligation.*

- 40.40** Overlap could also be recognised between relevant capital charges for exposures in the trading book and capital charges for exposures in the banking book, provided that the bank is able to calculate and compare the capital charges for the relevant exposures.



**40.41** Securitisation exposures will be treated differently depending on the type of underlying exposures and/or on the type of information available to the bank.

Securitisation exposures to which none of the approaches laid out in [CRE40.42](#) to [CRE40.48](#) can be applied must be assigned a 1250% risk weight.

**40.42** A bank must use the Securitisation Internal Ratings-Based Approach (SEC-IRBA) as described in [CRE44](#) for a securitisation exposure of an IRB pool as defined in [CRE40.15](#), unless otherwise determined by the supervisor.

**40.43** If a bank cannot use the SEC-IRBA, it must use the Securitisation External Ratings-Based Approach (SEC-ERBA) as described in [CRE42.1](#) to [CRE42.7](#) for a securitisation exposure to an SA pool as defined in [CRE40.17](#) provided that

- (1) the bank is located in a jurisdiction that permits use of the SEC-ERBA and
- (2) the exposure has an external credit assessment that meets the operational requirements for an external credit assessment in [CRE42.8](#), or there is an inferred rating that meets the operational requirements for inferred ratings in [CRE42.9](#) and [CRE42.10](#).

**40.44** A bank that is located in a jurisdiction that permits use of the SEC-ERBA may use an Internal Assessment Approach (SEC-IAA) as described in [CRE43.1](#) to [CRE43.4](#) for an unrated securitisation exposure (eg liquidity facilities and credit enhancements) to an SA pool within an ABCP programme. In order to use an SEC-IAA, a bank must have supervisory approval to use the IRB approach for non-securitisation exposures. A bank should consult with its national supervisor on whether and when it can apply the SEC-IAA to its securitisation exposures, especially where the bank can apply the IRB for some, but not all, underlying exposures. To ensure appropriate capital levels, there may be instances where the supervisor requires a treatment other than this general rule.

**40.45** A bank that cannot use the SEC-ERBA or an SEC-IAA for its exposure to an SA pool may use the Standardised Approach (SEC-SA) as described in [CRE41.1](#) to [CRE41.15](#).

**40.46** Securitisation exposures of mixed pools: where a bank can calculate  $K_{IRB}$  on at least 95% of the underlying exposure amounts of a securitisation, the bank must apply the SEC-IRBA calculating the capital charge for the underlying pool as follows, where  $d$  is the percentage of the exposure amount of underlying exposures for which the bank can calculate  $K_{IRB}$  over the exposure amount of all underlying exposures; and  $K_{IRB}$  and  $K_{SA}$  are as defined in [CRE44.2](#) to [CRE44.5](#) and [CRE41.2](#) to [CRE41.4](#), respectively:

$$\text{capital charge for mixed pool} = d \times K_{IRB} + (1 - d) \times K_{SA}$$

- 40.47** Where the bank cannot calculate  $K_{IRB}$  on at least 95% of the underlying exposures, the bank must use the hierarchy for securitisation exposures of SA pools as set out in [CRE40.43](#) to [CRE40.45](#).
- 40.48** For resecuritisation exposures, banks must apply the SEC-SA, with the adjustments in [CRE41.16](#).
- 40.49** When a bank provides implicit support to a securitisation, it must, at a minimum, hold capital against all of the underlying exposures associated with the securitisation transaction as if they had not been securitised. Additionally, banks would not be permitted to recognise in regulatory capital any gain on sale, in accordance with [CAP30.14](#).

### **Caps for securitisation exposures**

- 40.50** Banks may apply a “look-through” approach to senior securitisation exposures, whereby the senior securitisation exposure could receive a maximum risk weight equal to the exposure weighted-average risk weight applicable to the underlying exposures, provided that the bank has knowledge of the composition of the underlying exposures at all times. The applicable risk weight under the IRB framework would be calculated taking into account the application of the 1.06 scaling factor pursuant to [CRE30.4](#), and would also be inclusive of the expected loss portion multiplied by 12.5. In particular:
- (1) In the case of pools where the bank uses exclusively the SA or the IRB approach, the risk weight cap for senior exposures would equal the exposure weighted-average risk weight that would apply to the underlying exposures under the SA or IRB framework, respectively.
  - (2) In the case of mixed pools, when applying the SEC-IRBA, the SA part of the underlying pool would receive the corresponding SA risk weight, while the IRB portion would receive IRB risk weights. When applying the SEC-SA or the SEC-ERBA, the risk weight cap for senior exposures would be based on the SA exposure weighted-average risk weight of the underlying assets, whether or not they are originally IRB.
- 40.51** Where the risk weight cap results in a lower risk weight than the floor risk weight of 15%, the risk weight resulting from the cap should be used.

**40.52** A bank (originator, sponsor or investors) using the SEC-IRBA for a securitisation exposure may apply a maximum capital requirement for the securitisation exposures it holds equal to the IRB capital requirement (including the expected loss portion and the scaling factor of 1.06 for the unexpected loss portion) that would have been assessed against the underlying exposures had they not been securitised and treated under the appropriate sections of [CRE30](#) to [CRE36](#). In the case of mixed pools, the overall cap should be calculated by adding up the capital before securitisation; that is, by adding up the capital required under the general credit risk framework for the IRB and for the SA part of the underlying pool.

**40.53** An originating or sponsor bank using the SEC-ERBA or SEC-SA for a securitisation exposure may apply a maximum capital requirement for the securitisation exposures it holds equal to the capital requirement that would have been assessed against the underlying exposures had they not been securitised. In the case of mixed pools, the overall cap should be calculated by adding up the capital before securitisation; that is, by adding up the capital required under the general credit risk framework for the IRB and for the SA part of the underlying pool, respectively. The IRB part of the capital requirement includes the expected loss portion and the scaling factor of 1.06 of the unexpected loss portion.

**40.54** The maximum aggregated capital requirement for a bank's securitisation exposures in the same transaction will be equal to  $K_p * P$ . In order to apply a maximum capital charge to a bank's securitisation exposure, a bank will need the following inputs:

- (1) The largest proportion of interest that the bank holds for each tranche of a given pool (P). In particular:
  - (a) For a bank that has one or more securitisation exposure(s) that reside in a single tranche of a given pool, P equals the proportion (expressed as a percentage) of securitisation exposure(s) that the bank holds in that given tranche (calculated as the total nominal amount of the bank's securitisation exposure(s) in the tranche) divided by the nominal amount of the tranche.
  - (b) For a bank that has securitisation exposures that reside in different tranches of a given securitisation, P equals the maximum proportion of interest across tranches, where the proportion of interest for each of the different tranches should be calculated as described above.

(2) Capital charge for underlying pool ( $K_p$ ):

- (a) For an IRB pool,  $K_p$  equals  $K_{IRB}$  as defined in [CRE44.2](#) to [CRE44.13](#).
- (b) For an SA pool,  $K_p$  equals  $K_{SA}$  as defined in [CRE41.2](#) to [CRE41.5](#).
- (c) For a mixed pool,  $K_p$  equals the exposure-weighted average capital charge of the underlying pool using  $K_{SA}$  for the proportion of the underlying pool for which the bank cannot calculate  $K_{IRB}$ , and  $K_{IRB}$  for the proportion of the underlying pool for which a bank can calculate  $K_{IRB}$ .

**40.55** In applying the capital charge cap, the entire amount of any gain on sale and credit-enhancing interest-only strips arising from the securitisation transaction must be deducted in accordance with [CAP30.14](#).

### **Treatment of credit risk mitigation for securitisation exposures**

**40.56** A bank may recognise credit protection purchased on a securitisation exposure when calculating capital requirements subject to the following:

- (1) collateral recognition is limited to that permitted under the credit risk mitigation framework – in particular, [CRE22.37](#) and [CRE22.39](#) when the bank applies the SEC-ERBA or SEC-SA, and [CRE32.7](#) when the bank applies the SEC-IRBA. Collateral pledged by SPEs may be recognised;
- (2) credit protection provided by the entities listed in [CRE22.90](#) may be recognised. SPEs cannot be recognised as eligible guarantors; and
- (3) where guarantees or credit derivatives fulfil the minimum operational conditions as specified in [CRE22.84](#) to [CRE22.89](#), banks can take account of such credit protection in calculating capital requirements for securitisation exposures.

**40.57** When a bank provides full (or pro rata) credit protection to a securitisation exposure, the bank must calculate its capital requirements as if it directly holds the portion of the securitisation exposure on which it has provided credit protection (in accordance with the definition of tranche maturity given in [CRE40.22](#) and [CRE40.23](#)).

**40.58** Provided that the conditions set out in [CRE40.56](#) are met, the bank buying full (or pro rata) credit protection may recognise the credit risk mitigation on the securitisation exposure in accordance with the CRM framework.

**40.59** In the case of tranching credit protection, the original securitisation tranche will be decomposed into protected and unprotected sub-tranches:<sup>5</sup>

- (1) The protection provider must calculate its capital requirement as if directly exposed to the particular sub-tranche of the securitisation exposure on which it is providing protection, and as determined by the hierarchy of approaches for securitisation exposures and according to [CRE40.60](#) to [CRE40.62](#).
- (2) Provided that the conditions set out in [CRE40.56](#) are met, the protection buyer may recognise tranching protection on the securitisation exposure. In doing so, it must calculate capital requirements for each sub-tranche separately and as follows:
  - (a) For the resulting unprotected exposure(s), capital requirements will be calculated as determined by the hierarchy of approaches for securitisation exposures and according to [CRE40.60](#) to [CRE40.62](#).
  - (b) For the guaranteed/protected portion, capital requirements will be calculated according to the applicable CRM framework (in accordance with the definition of tranche maturity given in [CRE40.22](#) and [CRE40.23](#)).

#### Footnotes

<sup>5</sup> *The envisioned decomposition is theoretical and it should not be viewed as a new securitisation transaction. The resulting subtranches should not be considered resecuritisations solely due to the presence of the credit protection.*

**40.60** If, according to the hierarchy of approaches determined by [CRE40.41](#) to [CRE40.48](#), the bank must use the SEC-IRBA or SEC-SA, the parameters A and D should be calculated separately for each of the subtranches as if the latter would have been directly issued as separate tranches at the inception of the transaction. The value for  $K_{IRB}$  (respectively  $K_{SA}$ ) will be computed on the underlying portfolio of the original transaction.

**40.61** If, according to the hierarchy of approaches determined by [CRE40.41](#) to [CRE40.48](#), the bank must use the SEC-ERBA for the original securitisation exposure, the relevant risk weights for the different subtranches will be calculated subject to the following:

- (1) For the sub-tranche of highest priority,<sup>6</sup> the bank will use the risk weight of the original securitisation exposure.
- (2) For a sub-tranche of lower priority:
  - (a) Banks must infer a rating from one of the subordinated tranches in the original transaction. The risk weight of the sub-tranche of lower priority will be then determined by applying the inferred rating to the SEC-ERBA. Thickness input T will be computed for the sub-tranche of lower priority only.
  - (b) Should it not be possible to infer a rating the risk weight for the sub-tranche of lower priority will be computed using the SEC-SA applying the adjustments to the determination of A and D described in [CRE40.60](#). The risk weight for this sub-tranche will be obtained as the greater of
    - (i) the risk weight determined through the application of the SEC-SA with the adjusted A, D points and
    - (ii) the SEC-ERBA risk weight of the original securitisation exposure prior to recognition of protection.

#### Footnotes

- <sup>6</sup> *'Sub-tranche of highest priority' only describes the relative priority of the decomposed tranche. The calculation of the risk weight of each sub-tranche is independent from the question if this sub-tranche is protected (ie risk is taken by the protection provider) or is unprotected (ie risk is taken by the protection buyer).*

- 40.62** Under all approaches, a lower-priority sub-tranche must be treated as a non-senior securitisation exposure even if the original securitisation exposure prior to protection qualifies as senior as defined in [CRE40.18](#).
- 40.63** A maturity mismatch exists when the residual maturity of a hedge is less than that of the underlying exposure.
- 40.64** When protection is bought on a securitisation exposure(s), for the purpose of setting regulatory capital against a maturity mismatch, the capital requirement will be determined in accordance with [CRE22.97](#) to [CRE22.100](#). When the exposures being hedged have different maturities, the longest maturity must be used.

**40.65** When protection is bought on the securitised assets, maturity mismatches may arise in the context of synthetic securitisations (when, for example, a bank uses credit derivatives to transfer part or all of the credit risk of a specific pool of assets to third parties). When the credit derivatives unwind, the transaction will terminate. This implies that the effective maturity of all the tranches of the synthetic securitisation may differ from that of the underlying exposures. Banks that synthetically securitise exposures held on their balance sheet by purchasing tranching credit protection must treat such maturity mismatches in the following manner: For securitisation exposures that are assigned a risk weight of 1250%, maturity mismatches are not taken into account. For all other securitisation exposures, the bank must apply the maturity mismatch treatment set forth in [CRE22.97](#) to [CRE22.100](#). When the exposures being hedged have different maturities, the longest maturity must be used.

### **Simple, transparent and comparable securitisations: scope of and conditions for alternative treatment**

**40.66** Only traditional securitisations including exposures to ABCP conduits and exposures to transactions financed by ABCP conduits fall within the scope of the simple, transparent and comparable (STC) framework. Exposures to securitisations that are STC-compliant can be subject to alternative capital treatment as determined by [CRE41.20](#) to [CRE41.22](#), [CRE42.11](#) to [CRE42.14](#) and [CRE44.27](#) to [CRE44.29](#).

**40.67** For regulatory capital purposes, the following will be considered STC-compliant:

- (1) Exposures to non-ABCP, traditional securitisations that meet the criteria in [CRE40.72](#) to [CRE40.95](#); and
- (2) Exposures to ABCP conduits and/or transactions financed by ABCP conduits, where the conduit and/or transactions financed by it meet the criteria in [CRE40.96](#) to [CRE40.165](#).

**40.68** The originator/sponsor must disclose to investors all necessary information at the transaction level to allow investors to determine whether the securitisation is STC-compliant. Based on the information provided by the originator/sponsor, the investor must make its own assessment of the securitisation's STC compliance status as defined in [CRE40.67](#) before applying the alternative capital treatment.

**40.69** For retained positions where the originator has achieved significant risk transfer in accordance with [CRE40.24](#), the determination shall be made only by the originator retaining the position.

**40.70** STC criteria need to be met at all times. Checking the compliance with some of the criteria might only be necessary at origination (or at the time of initiating the exposure, in case of guarantees or liquidity facilities) to an STC securitisation. Notwithstanding, investors and holders of the securitisation positions are expected to take into account developments that may invalidate the previous compliance assessment, for example deficiencies in the frequency and content of the investor reports, in the alignment of interest, or changes in the transaction documentation at variance with relevant STC criteria.

**40.71** In cases where the criteria refer to underlying assets – including, but not limited to [CRE40.94](#) and [CRE40.95](#) - and the pool is dynamic, the compliance with the criteria will be subject to dynamic checks every time that assets are added to the pool.

### **Simple, transparent and comparable term securitisations: criteria for regulatory capital purposes**

**40.72** All criteria must be satisfied in order for a securitisation to receive alternative regulatory capital treatment.

#### **Criterion A1: Nature of assets**

**40.73** In simple, transparent and comparable securitisations, the assets underlying the securitisation should be credit claims or receivables that are homogeneous. In assessing homogeneity, consideration should be given to asset type, jurisdiction, legal system and currency. As more exotic asset classes require more complex and deeper analysis, credit claims or receivables should have contractually identified periodic payment streams relating to rental,<sup>7</sup> principal, interest, or principal and interest payments. Any referenced interest payments or discount rates should be based on commonly encountered market interest rates,<sup>8</sup> but should not reference complex or complicated formulae or exotic derivatives.<sup>9</sup>



- (1) For capital purposes, the "homogeneity" criterion should be assessed taking into account the following principles:
  - (a) The nature of assets should be such that investors would not need to analyse and assess materially different legal and/or credit risk factors and risk profiles when carrying out risk analysis and due diligence checks.
  - (b) Homogeneity should be assessed on the basis of common risk drivers, including similar risk factors and risk profiles.
  - (c) Credit claims or receivables included in the securitisation should have standard obligations, in terms of rights to payments and/or income from assets and that result in a periodic and well-defined stream of payments to investors. Credit card facilities should be deemed to result in a periodic and well-defined stream of payments to investors for the purposes of this criterion.
  - (d) Repayment of noteholders should mainly rely on the principal and interest proceeds from the securitised assets. Partial reliance on refinancing or re-sale of the asset securing the exposure may occur provided that re-financing is sufficiently distributed within the pool and the residual values on which the transaction relies are sufficiently low and that the reliance on refinancing is thus not substantial.
- (2) Examples of "commonly encountered market interest rates" would include:
  - (a) interbank rates and rates set by monetary policy authorities, such as the London Interbank Offered Rate (LIBOR), the Euro Interbank Offered Rate (Euribor) and the fed funds rate; and
  - (b) sectoral rates reflective of a lender's cost of funds, such as internal interest rates that directly reflect the market costs of a bank's funding or that of a subset of institutions.
- (3) Interest rate caps and/or floors would not automatically be considered exotic derivatives.

## Footnotes

<sup>7</sup> *Payments on operating and financing leases are typically considered to be rental payments rather than payments of principal and interest.*

<sup>8</sup> *Commonly encountered market interest rates may include rates reflective of a lender's cost of funds, to the extent that sufficient data are provided to investors to allow them to assess their relation to other market rates.*

<sup>9</sup> *The Global Association of Risk Professionals defines an exotic instrument as a financial asset or instrument with features making it more complex than simpler, plain vanilla, products.*

## Criterion A2: Asset performance history

**40.74** In order to provide investors with sufficient information on an asset class to conduct appropriate due diligence and access to a sufficiently rich data set to enable a more accurate calculation of expected loss in different stress scenarios, verifiable loss performance data, such as delinquency and default data, should be available for credit claims and receivables with substantially similar risk characteristics to those being securitised, for a time period long enough to permit meaningful evaluation by investors. Sources of and access to data and the basis for claiming similarity to credit claims or receivables being securitised should be clearly disclosed to all market participants.

- (1) In addition to the history of the asset class within a jurisdiction, investors should consider whether the originator, sponsor, servicer and other parties with a fiduciary responsibility to the securitisation have an established performance history for substantially similar credit claims or receivables to those being securitised and for an appropriately long period of time. It is not the intention of the criteria to form an impediment to the entry of new participants to the market, but rather that investors should take into account the performance history of the asset class and the transaction parties when deciding whether to invest in a securitisation.<sup>10</sup>

- (2) The originator/sponsor of the securitisation, as well as the original lender who underwrites the assets, must have sufficient experience in originating exposures similar to those securitised. For capital purposes, investors must determine whether the performance history of the originator and the original lender for substantially similar claims or receivables to those being securitised has been established for an "appropriately long period of time".

This performance history must be no shorter than a period of seven years for non-retail exposures. For retail exposures, the minimum performance history is five years.

*Footnotes*

[10](#)

*This "additional consideration" may form part of investors' due diligence process, but does not form part of the criteria when determining whether a securitisation can be considered "simple, transparent and comparable".*

### **Criterion A3: Payment status**

**40.75** Non-performing credit claims and receivables are likely to require more complex and heightened analysis. In order to ensure that only performing credit claims and receivables are assigned to a securitisation, credit claims or receivables being transferred to the securitisation may not, at the time of inclusion in the pool, include obligations that are in default or delinquent or obligations for which the transferor<sup>[11](#)</sup> or parties to the securitisation<sup>[12](#)</sup> are aware of evidence indicating a material increase in expected losses or of enforcement actions.

- (1) To prevent credit claims or receivables arising from credit-impaired borrowers from being transferred to the securitisation, the originator or sponsor should verify that the credit claims or receivables meet the following conditions:
  - (a) the obligor has not been the subject of an insolvency or debt restructuring process due to financial difficulties within three years prior to the date of origination;<sup>13</sup> and
  - (b) the obligor is not recorded on a public credit registry of persons with an adverse credit history; and,
  - (c) the obligor does not have a credit assessment by an external credit assessment institution or a credit score indicating a significant risk of default; and
  - (d) the credit claim or receivable is not subject to a dispute between the obligor and the original lender.
- (2) The assessment of these conditions should be carried out by the originator or sponsor no earlier than 45 days prior to the closing date. Additionally, at the time of this assessment, there should to the best knowledge of the originator or sponsor be no evidence indicating likely deterioration in the performance status of the credit claim or receivable.
- (3) Additionally, at the time of their inclusion in the pool, at least one payment should have been made on the underlying exposures, except in the case of revolving asset trust structures such as those for credit card receivables, trade receivables, and other exposures payable in a single instalment, at maturity.

*Footnotes*

<sup>11</sup> *Eg the originator or sponsor.*

<sup>12</sup> *Eg the servicer or a party with a fiduciary responsibility.*

<sup>13</sup> *This condition would not apply to borrowers that previously had credit incidents but were subsequently removed from credit registries as a result of the borrower cleaning their records. This is the case in jurisdictions in which borrowers have the "right to be forgotten".*

## **Criterion A4: Consistency of underwriting**

**40.76** Investor analysis should be simpler and more straightforward where the securitisation is of credit claims or receivables that satisfy materially non-deteriorating origination standards. To ensure that the quality of the securitised credit claims and receivables is not affected by changes in underwriting standards, the originator should demonstrate to investors that any credit claims or receivables being transferred to the securitisation have been originated in the ordinary course of the originator's business to materially non-deteriorating underwriting standards. Where underwriting standards change, the originator should disclose the timing and purpose of such changes. Underwriting standards should not be less stringent than those applied to credit claims and receivables retained on the balance sheet. These should be credit claims or receivables which have satisfied materially non-deteriorating underwriting criteria and for which the obligors have been assessed as having the ability and volition to make timely payments on obligations; or on granular pools of obligors originated in the ordinary course of the originator's business where expected cash flows have been modelled to meet stated obligations of the securitisation under prudently stressed loan loss scenarios.

- (1) In all circumstances, all credit claims or receivables must be originated in accordance with sound and prudent underwriting criteria based on an assessment that the obligor has the "ability and volition to make timely payments" on its obligations.
- (2) The originator/sponsor of the securitisation is expected, where underlying credit claims or receivables have been acquired from third parties, to review the underwriting standards (ie to check their existence and assess their quality) of these third parties and to ascertain that they have assessed the obligors' "ability and volition to make timely payments on obligations".

## **Criterion A5: Asset selection and transfer**

**40.77** Whilst recognising that credit claims or receivables transferred to a securitisation will be subject to defined criteria,<sup>14</sup> the performance of the securitisation should not rely upon the ongoing selection of assets through active management<sup>15</sup> on a discretionary basis of the securitisation's underlying portfolio. Credit claims or receivables transferred to a securitisation should satisfy clearly defined eligibility criteria. Credit claims or receivables transferred to a securitisation after the closing date may not be actively selected, actively managed or otherwise cherry-picked on a discretionary basis. Investors should be able to assess the credit risk of the asset pool prior to their investment decisions.

*Footnotes*

[14](#)

*Eg the size of the obligation, the age of the borrower or the loan-to-value of the property, debt-to-income and/or debt service coverage ratios.*

[15](#)

*Provided they are not actively selected or otherwise cherry-picked on a discretionary basis, the addition of credit claims or receivables during the revolving periods or their substitution or repurchasing due to the breach of representations and warranties do not represent active portfolio management.*

**40.78** In order to meet the principle of true sale, the securitisation should effect true sale such that the underlying credit claims or receivables:

- (1) are enforceable against the obligor and their enforceability is included in the representations and warranties of the securitisation;
- (2) are beyond the reach of the seller, its creditors or liquidators and are not subject to material recharacterisation or clawback risks;
- (3) are not effected through credit default swaps, derivatives or guarantees, but by a transfer<sup>16</sup> of the credit claims or the receivables to the securitisation;
- (4) demonstrate effective recourse to the ultimate obligation for the underlying credit claims or receivables and are not a securitisation of other securitisations; and
- (5) for regulatory capital purposes, an independent third-party legal opinion must support the claim that the true sale and the transfer of assets under the applicable laws comply with the points under [CRE40.78](#)(1) to [CRE40.78](#)(4).

*Footnotes*

[16](#)

*The requirement should not affect jurisdictions whose legal frameworks provide for a true sale with the same effects as described above, but by means other than a transfer of the credit claims or receivables.*

**40.79** In applicable jurisdictions, securitisations employing transfers of credit claims or receivables by other means should demonstrate the existence of material obstacles preventing true sale at issuance<sup>17</sup> and should clearly demonstrate the method of recourse to ultimate obligors.<sup>18</sup> In such jurisdictions, any conditions where the transfer of the credit claims or receivable is delayed or contingent upon specific events and any factors affecting timely perfection of claims by the securitisation should be clearly disclosed. The originator should provide representations and warranties that the credit claims or receivables being transferred to the securitisation are not subject to any condition or encumbrance that can be foreseen to adversely affect enforceability in respect of collections due.

*Footnotes*

<sup>17</sup> *Eg the immediate realisation of transfer tax or the requirement to notify all obligors of the transfer.*

<sup>18</sup> *Eg equitable assignment, perfected contingent transfer.*

## **Criterion A6: Initial and ongoing data**

**40.80** To assist investors in conducting appropriate due diligence prior to investing in a new offering, sufficient loan-level data in accordance with applicable laws or, in the case of granular pools, summary stratification data on the relevant risk characteristics of the underlying pool should be available to potential investors before pricing of a securitisation. To assist investors in conducting appropriate and ongoing monitoring of their investments' performance and so that investors that wish to purchase a securitisation in the secondary market have sufficient information to conduct appropriate due diligence, timely loan-level data in accordance with applicable laws or granular pool stratification data on the risk characteristics of the underlying pool and standardised investor reports should be readily available to current and potential investors at least quarterly throughout the life of the securitisation. Cut-off dates of the loan-level or granular pool stratification data should be aligned with those used for investor reporting. To provide a level of assurance that the reporting of the underlying credit claims or receivables is accurate and that the underlying credit claims or receivables meet the eligibility requirements, the initial portfolio should be reviewed<sup>19</sup> for conformity with the eligibility requirements by an appropriate legally accountable and independent third party, such as an independent accounting practice or the calculation agent or management company for the securitisation.

### Footnotes

[19](#)

*The review should confirm that the credit claims or receivables transferred to the securitisation meet the portfolio eligibility requirements. The review could, for example, be undertaken on a representative sample of the initial portfolio, with the application of a minimum confidence level. The verification report need not be provided but its results, including any material exceptions, should be disclosed in the initial offering documentation.*

## **Criterion B7: Redemption cash flows**

**40.81** Liabilities subject to the refinancing risk of the underlying credit claims or receivables are likely to require more complex and heightened analysis. To help ensure that the underlying credit claims or receivables do not need to be refinanced over a short period of time, there should not be a reliance on the sale or refinancing of the underlying credit claims or receivables in order to repay the liabilities, unless the underlying pool of credit claims or receivables is sufficiently granular and has sufficiently distributed repayment profiles. Rights to receive income from the assets specified to support redemption payments should be considered as eligible credit claims or receivables in this regard.<sup>[20](#)</sup>

### Footnotes

[20](#)

*For example, associated savings plans designed to repay principal at maturity.*

## **Criterion B8: Currency and interest rate asset and liability mismatches**

**40.82** To reduce the payment risk arising from the different interest rate and currency profiles of assets and liabilities and to improve investors' ability to model cash flows, interest rate and foreign currency risks should be appropriately mitigated<sup>[21](#)</sup> at all times, and if any hedging transaction is executed the transaction should be documented according to industry-standard master agreements. Only derivatives used for genuine hedging of asset and liability mismatches of interest rate and / or currency should be allowed.



- (1) For capital purposes, the term “appropriately mitigated” should be understood as not necessarily requiring a completely perfect hedge. The appropriateness of the mitigation of interest rate and foreign currency through the life of the transaction must be demonstrated by making available to potential investors, in a timely and regular manner, quantitative information including the fraction of notional amounts that are hedged, as well as sensitivity analysis that illustrates the effectiveness of the hedge under extreme but plausible scenarios.
- (2) If hedges are not performed through derivatives, then those risk-mitigating measures are only permitted if they are specifically created and used for the purpose of hedging an individual and specific risk, and not multiple risks at the same time (such as credit and interest rate risks). Non-derivative risk mitigation measures must be fully funded and available at all times.

*Footnotes*

- 21 *The term “appropriately mitigated” should be understood as not necessarily requiring a matching hedge. The appropriateness of hedging through the life of the transaction should be demonstrated and disclosed on a continuous basis to investors.*

## **Criterion B9: Payment priorities and observability**

**40.83** To prevent investors being subjected to unexpected repayment profiles during the life of a securitisation, the priorities of payments for all liabilities in all circumstances should be clearly defined at the time of securitisation and appropriate legal comfort regarding their enforceability should be provided. To ensure that junior noteholders do not have inappropriate payment preference over senior noteholders that are due and payable, throughout the life of a securitisation, or, where there are multiple securitisations backed by the same pool of credit claims or receivables, throughout the life of the securitisation programme, junior liabilities should not have payment preference over senior liabilities which are due and payable. The securitisation should not be structured as a "reverse" cash flow waterfall such that junior liabilities are paid where due and payable senior liabilities have not been paid. To help provide investors with full transparency over any changes to the cash flow waterfall, payment profile or priority of payments that might affect a securitisation, all triggers affecting the cash flow waterfall, payment profile or priority of payments of the securitisation should be clearly and fully disclosed both in offering documents and in investor reports, with information in the investor report that clearly identifies the breach status, the ability for the breach to be reversed and the consequences of the breach. Investor reports should contain information that allows investors to monitor the evolution over time of the indicators that are subject to triggers. Any triggers breached between payment dates should be disclosed to investors on a timely basis in accordance with the terms and conditions of all underlying transaction documents.

**40.84** Securitisations featuring a replenishment period should include provisions for appropriate early amortisation events and/or triggers of termination of the replenishment period, including, notably:

- (1) deterioration in the credit quality of the underlying exposures;
- (2) a failure to acquire sufficient new underlying exposures of similar credit quality; and
- (3) the occurrence of an insolvency-related event with regard to the originator or the servicer.

**40.85** Following the occurrence of a performance-related trigger, an event of default or an acceleration event, the securitisation positions should be repaid in accordance with a sequential amortisation priority of payments, in order of tranche seniority, and there should not be provisions requiring immediate liquidation of the underlying assets at market value

**40.86**

To assist investors in their ability to appropriately model the cash flow waterfall of the securitisation, the originator or sponsor should make available to investors, both before pricing of the securitisation and on an ongoing basis, a liability cash flow model or information on the cash flow provisions allowing appropriate modelling of the securitisation cash flow waterfall.

**40.87** To ensure that debt forgiveness, forbearance, payment holidays and other asset performance remedies can be clearly identified, policies and procedures, definitions, remedies and actions relating to delinquency, default or restructuring of underlying debtors should be provided in clear and consistent terms, such that investors can clearly identify debt forgiveness, forbearance, payment holidays, restructuring and other asset performance remedies on an ongoing basis.

**Criterion B10: Voting and enforcement rights**

**40.88** To help ensure clarity for securitisation note holders of their rights and ability to control and enforce on the underlying credit claims or receivables, upon insolvency of the originator or sponsor, all voting and enforcement rights related to the credit claims or receivables should be transferred to the securitisation. Investors' rights in the securitisation should be clearly defined in all circumstances, including the rights of senior versus junior note holders.

## **Criterion B11: Documentation disclosure and legal review**

**40.89** To help investors to fully understand the terms, conditions, legal and commercial information prior to investing in a new offering<sup>22</sup> and to ensure that this information is set out in a clear and effective manner for all programmes and offerings, sufficient initial offering<sup>23</sup> and draft underlying<sup>24</sup> documentation should be made available to investors (and readily available to potential investors on a continuous basis) within a reasonably sufficient period of time prior to pricing, or when legally permissible, such that the investor is provided with full disclosure of the legal and commercial information and comprehensive risk factors needed to make informed investment decisions. Final offering documents should be available from the closing date and all final underlying transaction documents shortly thereafter. These should be composed such that readers can readily find, understand and use relevant information. To ensure that all the securitisation's underlying documentation has been subject to appropriate review prior to publication, the terms and 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, eg by the arranger or the trustee. Investors should be notified in a timely fashion of any changes in such documents that have an impact on the structural risks in the securitisation.

### *Footnotes*

<sup>22</sup> *For the avoidance of doubt, any type of securitisation should be allowed to fulfil the requirements of [CRE40.89](#) once it meets its prescribed standards of disclosure and legal review.*

<sup>23</sup> *Eg draft offering circular, draft offering memorandum, draft offering document or draft prospectus, such as a "red herring"*

<sup>24</sup> *Eg asset sale agreement, assignment, novation or transfer agreement; servicing, backup servicing, administration and cash management agreements; trust/management deed, security deed, agency agreement, account bank agreement, guaranteed investment contract, incorporated terms or master trust framework or master definitions agreement as applicable; any relevant inter-creditor agreements, swap or derivative documentation, subordinated loan agreements, start-up loan agreements and liquidity facility agreements; and any other relevant underlying documentation, including legal opinions.*

## **Criterion B12: Alignment of interest**

**40.90** In order to align the interests of those responsible for the underwriting of the credit claims or receivables with those of investors, the originator or sponsor of the credit claims or receivables should retain a material net economic exposure and demonstrate a financial incentive in the performance of these assets following their securitisation.

## **Criterion C13: Fiduciary and contractual responsibilities**

**40.91** To help ensure servicers have extensive workout expertise, thorough legal and collateral knowledge and a proven track record in loss mitigation, such parties should be able to demonstrate expertise in the servicing of the underlying credit claims or receivables, supported by a management team with extensive industry experience. The servicer should at all times act in accordance with reasonable and prudent standards. Policies, procedures and risk management controls should be well documented and adhere to good market practices and relevant regulatory regimes. There should be strong systems and reporting capabilities in place. In assessing whether "strong systems and reporting capabilities are in place" for capital purposes, well documented policies, procedures and risk management controls, as well as strong systems and reporting capabilities, may be substantiated by a third-party review for non-banking entities.

**40.92** The party or parties with fiduciary responsibility should act on a timely basis in the best interests of the securitisation note holders, and both the initial offering and all underlying documentation should contain provisions facilitating the timely resolution of conflicts between different classes of note holders by the trustees, to the extent permitted by applicable law. The party or parties with fiduciary responsibility to the securitisation and to investors should be able to demonstrate sufficient skills and resources to comply with their duties of care in the administration of the securitisation vehicle. To increase the likelihood that those identified as having a fiduciary responsibility towards investors as well as the servicer execute their duties in full on a timely basis, remuneration should be such that these parties are incentivised and able to meet their responsibilities in full and on a timely basis.

## **Criterion C14: Transparency to investors**

**40.93** To help provide full transparency to investors, assist investors in the conduct of their due diligence and to prevent investors being subject to unexpected disruptions in cash flow collections and servicing, the contractual obligations, duties and responsibilities of all key parties to the securitisation, both those with a fiduciary responsibility and of the ancillary service providers, should be defined clearly both in the initial offering and all underlying documentation. Provisions should be documented for the replacement of servicers, bank account providers, derivatives counterparties and liquidity providers in the event of failure or non-performance or insolvency or other deterioration of creditworthiness of any such counterparty to the securitisation. To enhance transparency and visibility over all receipts, payments and ledger entries at all times, the performance reports to investors should distinguish and report the securitisation's income and disbursements, such as scheduled principal, redemption principal, scheduled interest, prepaid principal, past due interest and fees and charges, delinquent, defaulted and restructured amounts under debt forgiveness and payment holidays, including accurate accounting for amounts attributable to principal and interest deficiency ledgers.

- (1) For capital purposes, the terms "initial offering" and "underlying transaction documentation" should be understood in the context defined by [CRE40.89](#).
- (2) The term "income and disbursements" should also be understood as including deferment, forbearance, and repurchases among the items described.

## **Criterion D15: Credit risk of underlying exposures**

**40.94** At the portfolio cut-off date the underlying exposures have to meet the conditions under the Standardised Approach for credit risk, and after taking into account any eligible credit risk mitigation, for being assigned a risk weight equal to or smaller than:

- (1) 40% on a value-weighted average exposure basis for the portfolio where the exposures are loans secured by residential mortgages or fully guaranteed residential loans;
- (2) 50% on an individual exposure basis where the exposure is a loan secured by a commercial mortgage;
- (3) 75% on an individual exposure basis where the exposure is a retail exposure;  
or

- (4) 100% on an individual exposure basis for any other exposure.

## **Criterion D16: Granularity of the pool**

**40.95** At the portfolio cut-off date, the aggregated value of all exposures to a single obligor shall not exceed 1%<sup>25</sup> of the aggregated outstanding exposure value of all exposures in the portfolio.

### *Footnotes*

<sup>25</sup>

*In jurisdictions with structurally concentrated corporate loan markets available for securitisation subject to ex ante supervisory approval and only for corporate exposures, the applicable maximum concentration threshold could be increased to 2% if the originator or sponsor retains subordinated tranche(s) that form loss absorbing credit enhancement, as defined in [CRE44.16](#), and which cover at least the first 10% of losses. These tranche(s) retained by the originator or sponsor shall not be eligible for the STC capital treatment.*

## **Simple, transparent and comparable short-term securitisations: criteria for regulatory capital purposes**

**40.96** The following definitions apply when the terms are used in [CRE40.97](#) to [CRE40.165](#) :

- (1) ABCP conduit/conduit – ABCP conduit, being the special purpose vehicle which can issue commercial paper;
- (2) ABCP programme – the programme of commercial paper issued by an ABCP conduit;
- (3) Assets/asset pool – the credit claims and/or receivables underlying a transaction in which the ABCP conduit holds a beneficial interest;
- (4) Investor – the holder of commercial paper issued under an ABCP programme, or any type of exposure to the conduit representing a financing liability of the conduit, such as loans;
- (5) Obligor – borrower underlying a credit claim or a receivable that is part of an asset pool;

- (6) Seller – a party that:
- (a) concluded (in its capacity as original lender) the original agreement that created the obligations or potential obligations (under a credit claim or a receivable) of an obligor or purchased the obligations or potential obligations from the original lender(s); and
  - (b) transferred those assets through a transaction or passed on the interest <sup>26</sup> to the ABCP conduit.
- (7) Sponsor – sponsor of an ABCP conduit. It may also be noted that other relevant parties with a fiduciary responsibility in the management and administration of the ABCP conduit could also undertake control of some of the responsibilities of the sponsor; and
- (8) Transaction – An individual transaction in which the ABCP conduit holds a beneficial interest. A transaction may qualify as a securitisation, but may also be a direct asset purchase, the acquisition of undivided interest in a replenishing pool of asset, a secured loan etc.

*Footnotes*

<sup>26</sup>

*For instance, transactions in which assets are sold to a special purpose entity sponsored by a bank's customer and then either a security interest in the assets is granted to the ABCP conduit to secure a loan made by the ABCP conduit to the sponsored special purpose entity, or an undivided interest is sold to the ABCP conduit.*

**40.97** For exposures at the conduit level (eg exposure arising from investing in the commercial papers issued by the ABCP programme or sponsoring arrangements at the conduit/programme level), compliance with the short-term STC capital criteria is only achieved if the criteria are satisfied at both the conduit and transaction levels.

**40.98** In the case of exposures at the transaction level, compliance with the short-term STC capital criteria is considered to be achieved if the transaction level criteria are satisfied for the transactions to which support is provided.



## Criterion A1: Nature of assets (conduit level)

**40.99** The sponsor should make representations and warranties to investors that the criterion set out in [CRE40.100](#) are met, and explain how this is the case on an overall basis. Only if specified should this be done for each transaction. Provided that each individual underlying transaction is homogeneous in terms of asset type, a conduit may be used to finance transactions of different asset types. Programme wide credit enhancement should not prevent a conduit from qualifying for STC, regardless of whether such enhancement technically creates re-securitisation.

## Criterion A1: Nature of assets (transaction level)

**40.100** The assets underlying a transaction in a conduit should be credit claims or receivables that are homogeneous, in terms of asset type.<sup>27</sup> The assets underlying each individual transaction in a conduit should not be composed of "securitisation exposures" as defined in [CRE40.4](#). Credit claims or receivables underlying a transaction in a conduit should have contractually identified periodic payment streams relating to rental,<sup>28</sup> principal, interest, or principal and interest payments. Credit claims or receivables generating a single payment stream would equally qualify as eligible. Any referenced interest payments or discount rates should be based on commonly encountered market interest rates,<sup>29</sup> but should not reference complex or complicated formulae or exotic derivatives.<sup>30</sup>

### Footnotes

<sup>27</sup> *For the avoidance of doubt, this criterion does not automatically exclude securitisations of equipment leases and securitisations of auto loans and leases from the short-term STC framework.*

<sup>28</sup> *Payments on operating and financing lease are typically considered to be rental payments rather than payments of principal and interest.*

<sup>29</sup> *Commonly encountered market interest rates may include rates reflective of a lender's cost of funds, to the extent sufficient data is provided to the sponsors to allow them to assess their relation to other market rates.*

<sup>30</sup> *The Global Association of Risk Professionals defines an exotic instrument as a financial asset or instrument with features making it more complex than simpler, plain vanilla, products.*

## **Additional guidance for Criterion A1**

**40.101**The “homogeneity” criterion should be assessed taking into account the following principles:

- (1) The nature of assets should be such that there would be no need to analyse and assess materially different legal and/or credit risk factors and risk profiles when carrying out risk analysis and due diligence checks for the transaction.
- (2) Homogeneity should be assessed on the basis of common risk drivers, including similar risk factors and risk profiles.
- (3) Credit claims or receivables included in the securitisation should have standard obligations, in terms of rights to payments and/or income from assets and that result in a periodic and well-defined stream of payments to investors. Credit card facilities should be deemed to result in a periodic and well-defined stream of payments to investors for the purposes of this criterion.
- (4) Repayment of the securitisation exposure should mainly rely on the principal and interest proceeds from the securitised assets. Partial reliance on refinancing or re-sale of the asset securing the exposure may occur provided that re-financing is sufficiently distributed within the pool and the residual values on which the transaction relies are sufficiently low and that the reliance on refinancing is thus not substantial.

**40.102**Examples of “commonly encountered market interest rates” would include:

- (1) interbank rates and rates set by monetary policy authorities, such as LIBOR, Euribor and the fed funds rate; and
- (2) sectoral rates reflective of a lender’s cost of funds, such as internal interest rates that directly reflect the market costs of a bank’s funding or that of a subset of institutions.

**40.103**Interest rate caps and/or floors would not automatically be considered exotic derivatives.

**40.104**The transaction level requirement is still met if the conduit does not purchase the underlying asset with a refundable purchase price discount but instead acquires a beneficial interest in the form of a note which itself might qualify as a securitisation exposure, as long as the securitisation exposure is not subject to any further tranching (ie has the same economic characteristic as the purchase of the underlying asset with a refundable purchase price discount).

## **Criterion A2: Asset performance history (conduit level)**

**40.105**In order to provide investors with sufficient information on the performance history of the asset types backing the transactions, the sponsor should make available to investors, sufficient loss performance data of claims and receivables with substantially similar risk characteristics, such as delinquency and default data of similar claims, and for a time period long enough to permit meaningful evaluation. The sponsor should disclose to investors the sources of such data and the basis for claiming similarity to credit claims or receivables financed by the conduit. Such loss performance data may be provided on a stratified basis.<sup>31</sup>

### *Footnotes*

<sup>31</sup>

*Stratified means by way of example, all materially relevant data on the conduit's composition (outstanding balances, industry sector, obligor concentrations, maturities, etc) and conduit's overview and all materially relevant data on the credit quality and performance of underlying transactions, allowing investors to identify collections, and as applicable, debt restructuring, forgiveness, forbearance, payment holidays, repurchases, delinquencies and defaults.*

## **Criterion A2: Asset performance history (transaction level)**

**40.106**In order to provide the sponsor with sufficient information on the performance history of each asset type backing the transactions and to conduct appropriate due diligence and to have access to a sufficiently rich data set to enable a more accurate calculation of expected loss in different stress scenarios, verifiable loss performance data, such as delinquency and default data, should be available for credit claims and receivables with substantially similar risk characteristics to those being financed by the conduit, for a time period long enough to permit meaningful evaluation by the sponsor.

## **Additional requirement for Criterion A2**

**40.107**The sponsor of the securitisation, as well as the original lender who underwrites the assets, must have sufficient experience in the risk analysis/underwriting of exposures or transactions with underlying exposures similar to those securitised. The sponsor should have well documented procedures and policies regarding the underwriting of transactions and the ongoing monitoring of the performance of the securitised exposures. The sponsor should ensure that the seller(s) and all other parties involved in the origination of the receivables have experience in originating same or similar assets, and are supported by a management with industry experience. For the purpose of meeting the short-term STC capital criteria, investors must request confirmation from the sponsor that the performance history of the originator and the original lender for substantially similar claims or receivables to those being securitised has been established for an "appropriately long period of time". This performance history must be no shorter than a period of five years for non-retail exposures. For retail exposures, the minimum performance history is three years.

## **Criterion A3: Asset performance history (conduit level)**

**40.108**The sponsor should, to the best of its knowledge and based on representations from sellers, make representations and warranties to investors that [CRE40.109](#) is met with respect to each transaction.

## **Criterion A3: Asset performance history (transaction level)**

**40.109**The sponsor should obtain representations from sellers that the credit claims or receivables underlying each individual transaction are not, at the time of acquisition of the interests to be financed by the conduit, in default or delinquent or subject to a material increase in expected losses or of enforcement actions.

## **Additional requirement for Criterion A3**

**40.110**To prevent credit claims or receivables arising from credit-impaired borrowers from being transferred to the securitisation, the original seller or sponsor should verify that the credit claims or receivables meet the following conditions for each transaction:

- (1) the obligor has not been the subject of an insolvency or debt restructuring process due to financial difficulties in the three years prior to the date of origination;<sup>32</sup>

- (2) the obligor is not recorded on a public credit registry of persons with an adverse credit history;
- (3) the obligor does not have a credit assessment by an external credit assessment institution or a credit score indicating a significant risk of default; and
- (4) the credit claim or receivable is not subject to a dispute between the obligor and the original lender.

*Footnotes*

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*This condition would not apply to borrowers that previously had credit incidents but were subsequently removed from credit registries as a result of the borrowers cleaning their records. This is the case in jurisdictions in which borrowers have the "right to be forgotten".*

**40.111**The assessment of these conditions should be carried out by the original seller or sponsor no earlier than 45 days prior to acquisition of the transaction by the conduit or, in the case of replenishing transactions, no earlier than 45 days prior to new exposures being added to the transaction. In addition, at the time of the assessment, there should to the best knowledge of the original seller or sponsor be no evidence indicating likely deterioration in the performance status of the credit claim or receivable. Further, at the time of their inclusion in the pool, at least one payment should have been made on the underlying exposures, except in the case of replenishing asset trust structures such as those for credit card receivables, trade receivables, and other exposures payable in a single instalment, at maturity.

#### **Criterion A4: Consistency of underwriting (conduit level)**

**40.112**The sponsor should make representations and warranties to investors that:

- (1) it has taken steps to verify that for the transactions in the conduit, any underlying credit claims and receivables have been subject to consistent underwriting standards, and explain how.
- (2) when there are material changes to underwriting standards, it will receive from sellers disclosure about the timing and purpose of such changes.

**40.113**The sponsor should also inform investors of the material selection criteria applied when selecting sellers (including where they are not financial institutions).

## **Criterion A4: Consistency of underwriting (transaction level)**

**40.114**The sponsor should ensure that sellers (in their capacity of original lenders) in transactions with the conduit demonstrate to it that:

- (1) any credit claims or receivables being transferred to or through a transaction held by the conduit have been originated in the ordinary course of the seller's business subject to materially non-deteriorating underwriting standards. Those underwriting standards should also not be less stringent than those applied to credit claims and receivables retained on the balance sheet of the seller and not financed by the conduit; and
- (2) the obligors have been assessed as having the ability and volition to make timely payments on obligations.

**40.115**The sponsor should also ensure that sellers disclose to it the timing and purpose of material changes to underwriting standards.

## **Additional requirement for Criterion A4**

**40.116**In all circumstances, all credit claims or receivables must be originated in accordance with sound and prudent underwriting criteria based on an assessment that the obligor has the "ability and volition to make timely payments" on its obligations. The sponsor of the securitisation is expected, where underlying credit claims or receivables have been acquired from third parties, to review the underwriting standards (ie to check their existence and assess their quality) of these third parties and to ascertain that they have assessed the obligors' "ability and volition to make timely payments" on their obligations.

## **Criterion A5: Asset selection and transfer (conduit level)**

**40.117**The sponsor should:

- (1) provide representations and warranties to investors about the checks, in nature and frequency, it has conducted regarding enforceability of underlying assets.
- (2) disclose to investors the receipt of appropriate representations and warranties from sellers that the credit claims or receivables being transferred to the transactions in the conduit are not subject to any condition or encumbrance that can be foreseen to adversely affect enforceability in respect of collections due.

## Criterion A5: Asset selection and transfer (transaction level)

**40.118** The sponsor should be able to assess thoroughly the credit risk of the asset pool prior to its decision to provide full support to any given transaction or to the conduit. The sponsor should ensure that credit claims or receivables transferred to or through a transaction financed by the conduit:

- (1) satisfy clearly defined eligibility criteria; and
- (2) are not actively selected after the closing date, actively managed<sup>33</sup> or otherwise cherry-picked on a discretionary basis.

### Footnotes

<sup>33</sup> *Provided they are not actively selected or otherwise cherry picked on a discretionary basis, the addition of credit claims or receivables during the replenishment periods or their substitution or repurchasing due to the breach of representations and warranties do not represent active portfolio management.*

**40.119** The sponsor should ensure that the transactions in the conduit effect true sale such that the underlying credit claims or receivables:

- (1) are enforceable against the obligor;
- (2) are beyond the reach of the seller, its creditors or liquidators and are not subject to material re-characterisation or clawback risks;
- (3) are not effected through credit default swaps, derivatives or guarantees, but by a transfer<sup>34</sup> of the credit claims or the receivables to the transaction; and
- (4) demonstrate effective recourse to the ultimate obligation for the underlying credit claims or receivables and are not a re-securitisation position.

### Footnotes

<sup>34</sup> *This requirement should not affect jurisdictions whose legal frameworks provide for a true sale with the same effects as described above, but by means other than a transfer of the credit claims or receivables.*

**40.120**The sponsor should ensure that in applicable jurisdictions, for conduits employing transfers of credit claims or receivables by other means, sellers can demonstrate to it the existence of material obstacles preventing true sale at issuance (eg the immediate realisation of transfer tax or the requirement to notify all obligors of the transfer) and should clearly demonstrate the method of recourse to ultimate obligors (eg equitable assignment, perfected contingent transfer). In such jurisdictions, any conditions where the transfer of the credit claims or receivables is delayed or contingent upon specific events and any factors affecting timely perfection of claims by the conduit should be clearly disclosed.

**40.121**The sponsor should ensure that it receives from the individual sellers (either in their capacity as original lender or servicer) representations and warranties that the credit claims or receivables being transferred to or through the transaction are not subject to any condition or encumbrance that can be foreseen to adversely affect enforceability in respect of collections due.

### **Additional requirement for Criterion A5**

**40.122**An in-house legal opinion or an independent third-party legal opinion must support the claim that the true sale and the transfer of assets under the applicable laws comply with [CRE40.118\(1\)](#) and [CRE40.118\(2\)](#) at the transaction level.

### **Criterion A6: Initial and ongoing data (conduit level)**

**40.123**To assist investors in conducting appropriate due diligence prior to investing in a new programme offering, the sponsor should provide to potential investors sufficient aggregated data that illustrate the relevant risk characteristics of the underlying asset pools in accordance with applicable laws. To assist investors in conducting appropriate and ongoing monitoring of their investments' performance and so that investors who wish to purchase commercial paper have sufficient information to conduct appropriate due diligence, the sponsor should provide timely and sufficient aggregated data that provide the relevant risk characteristics of the underlying pools in accordance with applicable laws. The sponsor should ensure that standardised investor reports are readily available to current and potential investors at least monthly. Cut off dates of the aggregated data should be aligned with those used for investor reporting.



## **Criterion A6: Initial and ongoing data (transaction level)**

**40.124**The sponsor should ensure that the individual sellers (in their capacity of servicers) provide it with:

- (1) sufficient asset level data in accordance with applicable laws or, in the case of granular pools, summary stratification data on the relevant risk characteristics of the underlying pool before transferring any credit claims or receivables to such underlying pool.
- (2) timely asset level data in accordance with applicable laws or granular pool stratification data on the risk characteristics of the underlying pool on an ongoing basis. Those data should allow the sponsor to fulfil its fiduciary duty at the conduit level in terms of disclosing information to investors including the alignment of cut off dates of the asset level or granular pool stratification data with those used for investor reporting.

**40.125**The seller may delegate some of these tasks and, in this case, the sponsor should ensure that there is appropriate oversight of the outsourced arrangements.

### **Additional requirement for Criterion A6**

**40.126**The standardised investor reports which are made readily available to current and potential investors at least monthly should include the following information:

- (1) materially relevant data on the credit quality and performance of underlying assets, including data allowing investors to identify dilution, delinquencies and defaults, restructured receivables, forbearance, repurchases, losses, recoveries and other asset performance remedies in the pool;
- (2) the form and amount of credit enhancement provided by the seller and sponsor at transaction and conduit levels, respectively;
- (3) relevant information on the support provided by the sponsor; and
- (4) the status and definitions of relevant triggers (such as performance, termination or counterparty replacement triggers).

## **Criterion B7: Full support (conduit level only)**

**40.127** The sponsor should provide the liquidity facility(ies) and the credit protection support<sup>35</sup> for any ABCP programme issued by a conduit. Such facility(ies) and support should ensure that investors are fully protected against credit risks, liquidity risks and any material dilution risks of the underlying asset pools financed by the conduit. As such, investors should be able to rely on the sponsor to ensure timely and full repayment of the commercial paper.

### *Footnotes*

<sup>35</sup> *A sponsor can provide full support either at ABCP programme level or at transaction level, ie by fully supporting each transaction within an ABCP programme.*

## **Additional requirement for Criterion B7**

**40.128** While liquidity and credit protection support at both the conduit level and transaction level can be provided by more than one sponsor, the majority of the support (assessed in terms of coverage) has to be made by a single sponsor (referred to as the "main sponsor").<sup>36</sup> An exception can however be made for a limited period of time, where the main sponsor has to be replaced due to a material deterioration in its credit standing.

### *Footnotes*

<sup>36</sup> *"Liquidity and credit protection support" refers to support provided by the sponsors. Any support provided by the seller is excluded.*

**40.129** The full support provided should be able to irrevocably and unconditionally pay the ABCP liabilities in full and on time. The list of risks provided in [CRE40.127](#) that have to be covered is not comprehensive but rather provides typical examples.

**40.130** Under the terms of the liquidity facility agreement:

- (1) Upon specified events affecting its creditworthiness, the sponsor shall be obliged to collateralise its commitment in cash to the benefit of the investors or otherwise replace itself with another liquidity provider.

- (2) If the sponsor does not renew its funding commitment for a specific transaction or the conduit in its entirety, the sponsor shall collateralise its commitments regarding a specific transaction or, if relevant, to the conduit in cash at the latest 30 days prior to the expiration of the liquidity facility, and no new receivables should be purchased under the affected commitment.

**40.131**The sponsor should provide investors with full information about the terms of the liquidity facility (facilities) and the credit support provided to the ABCP conduit and the underlying transactions (in relation to the transactions, redacted where necessary to protect confidentiality).

### **Criterion B8: Redemption cash flow (transaction level only)**

**40.132**Unless the underlying pool of credit claims or receivables is sufficiently granular and has sufficiently distributed repayment profiles, the sponsor should ensure that the repayment of the credit claims or receivables underlying any of the individual transactions relies primarily on the general ability and willingness of the obligor to pay rather than the possibility that the obligor refinances or sells the collateral and that such repayment does not primarily rely on the drawing of an external liquidity facility provided to this transaction.

### **Additional requirement for Criterion B8**

**40.133**Sponsors cannot use support provided by their own liquidity and credit facilities towards meeting this criterion. For the avoidance of doubt, the requirement that the repayment shall not primarily rely on the drawing of an external liquidity facility does not apply to exposures in the form of the notes issued by the ABCP conduit.

### **Criterion B9: Currency and interest rate asset and liability mismatches (conduit level)**

**40.134**The sponsor should ensure that any payment risk arising from different interest rate and currency profiles not mitigated at transaction-level or arising at conduit level is appropriately mitigated. The sponsor should also ensure that derivatives are used for genuine hedging purposes only and that hedging transactions are documented according to industry-standard master agreements. The sponsor should provide sufficient information to investors to allow them to assess how the payment risk arising from the different interest rate and currency profiles of assets and liabilities are appropriately mitigated, whether at the conduit or at transaction level.

## **Criterion B9: Currency and interest rate asset and liability mismatches (transaction level)**

**40.135**To reduce the payment risk arising from the different interest rate and currency profiles of assets and liabilities, if any, and to improve the sponsor's ability to analyse cash flows of transactions, the sponsor should ensure that interest rate and foreign currency risks are appropriately mitigated. The sponsor should also ensure that derivatives are used for genuine hedging purposes only and that hedging transactions are documented according to industry-standard master agreements.

### **Additional requirement for Criterion B9**

**40.136**The term "appropriately mitigated" should be understood as not necessarily requiring a completely perfect hedge. The appropriateness of the mitigation of interest rate and foreign currency risks through the life of the transaction must be demonstrated by making available, in a timely and regular manner, quantitative information including the fraction of notional amounts that are hedged, as well as sensitivity analysis that illustrates the effectiveness of the hedge under extreme but plausible scenarios. The use of risk-mitigating measures other than derivatives is permitted only if the measures are specifically created and used for the purpose of hedging an individual and specific risk. Non-derivative risk mitigation measures must be fully funded and available at all times.

## **Criterion B10: Payment priorities and observability (conduit level)**

**40.137**The commercial paper issued by the ABCP programme should not include extension options or other features which may extend the final maturity of the asset-backed commercial paper, where the right of trigger does not belong exclusively to investors. The sponsor should:

- (1) make representations and warranties to investors that the criterion set out in [CRE40.138](#) to [CRE40.143](#) is met and in particular, that it has the ability to appropriately analyse the cash flow waterfall for each transaction which qualifies as a securitisation; and
- (2) make available to investors a summary (illustrating the functioning) of these waterfalls and of the credit enhancement available at programme level and transaction level.

## **Criterion B10: Payment priorities and observability (transaction level)**

- 40.138** To prevent the conduit from being subjected to unexpected repayment profiles from the transactions, the sponsor should ensure that priorities of payments are clearly defined at the time of acquisition of the interests in these transactions by the conduit; and appropriate legal comfort regarding the enforceability is provided.
- 40.139** For all transactions which qualify as a securitisation, the sponsor should ensure that all triggers affecting the cash flow waterfall, payment profile or priority of payments are clearly and fully disclosed to the sponsor both in the transactions' documentation and reports, with information in the reports that clearly identifies any breach status, the ability for the breach to be reversed and the consequences of the breach. Reports should contain information that allows sponsors to easily ascertain the likelihood of a trigger being breached or reversed. Any triggers breached between payment dates should be disclosed to sponsors on a timely basis in accordance with the terms and conditions of the transaction documents.
- 40.140** For any of the transactions where the beneficial interest held by the conduit qualifies as a securitisation position, the sponsor should ensure that any subordinated positions do not have inappropriate payment preference over payments to the conduit (which should always rank senior to any other position) and which are due and payable.
- 40.141** Transactions featuring a replenishment period should include provisions for appropriate early amortisation events and/or triggers of termination of the replenishment period, including, notably, deterioration in the credit quality of the underlying exposures; a failure to replenish sufficient new underlying exposures of similar credit quality; and the occurrence of an insolvency related event with regard to the individual sellers.
- 40.142** To ensure that debt forgiveness, forbearance, payment holidays, restructuring, dilution and other asset performance remedies can be clearly identified, policies and procedures, definitions, remedies and actions relating to delinquency, default, dilution or restructuring of underlying debtors should be provided in clear and consistent terms, such that the sponsor can clearly identify debt forgiveness, forbearance, payment holidays, restructuring, dilution and other asset performance remedies on an ongoing basis.
- 40.143** For each transaction which qualifies as a securitisation, the sponsor should ensure it receives both before the conduit acquires a beneficial interest in the transaction and on an ongoing basis, the liability cash flow analysis or information on the cash flow provisions allowing appropriate analysis of the cash flow waterfall of these transactions.

### **Criterion B11: Voting and enforcement rights (conduit level)**

**40.144** To provide clarity to investors, the sponsor should make sufficient information available in order for investors to understand their enforcement rights on the underlying credit claims or receivables in the event of insolvency of the sponsor.

### **Criterion B11: Voting and enforcement rights (transaction level)**

**40.145** For each transaction, the sponsor should ensure that, in particular upon insolvency of the seller or where the obligor is in default on its obligation, all voting and enforcement rights related to the credit claims or receivables are, if applicable:

- (1) transferred to the conduit; and
- (2) clearly defined under all circumstances, including with respect to the rights of the conduit versus other parties with an interest (eg sellers), where relevant.

### **Criterion B12: Documentation, disclosure and legal review (conduit level only)**

**40.146** To help investors understand fully the terms, conditions, and legal information prior to investing in a new programme offering and to ensure that this information is set out in a clear and effective manner for all programme offerings, the sponsor should ensure that sufficient initial offering documentation for the ABCP programme is provided to investors (and readily available to potential investors on a continuous basis) within a reasonably sufficient period of time prior to issuance, such that the investor is provided with full disclosure of the legal information and comprehensive risk factors needed to make informed investment decisions. These should be composed such that readers can readily find, understand and use relevant information.

**40.147** The sponsor should ensure that the terms and documentation of a conduit and the ABCP programme it issues are reviewed and verified by an appropriately experienced and independent legal practice prior to publication and in the case of material changes. The sponsor should notify investors in a timely fashion of any changes in such documents that have an impact on the structural risks in the ABCP programme.

## **Additional requirement for Criterion B12**

**40.148**To understand fully the terms, conditions and legal information prior to including a new transaction in the ABCP conduit and ensure that this information is set out in a clear and effective manner, the sponsor should ensure that it receives sufficient initial offering documentation for each transaction and that it is provided within a reasonably sufficient period of time prior to the inclusion in the conduit, with full disclosure of the legal information and comprehensive risk factors needed to supply liquidity and/or credit support facilities. The initial offering document for each transaction should be composed such that readers can readily find, understand and use relevant information. The sponsor should also ensure that the terms and documentation of a transaction are reviewed and verified by an appropriately experienced and independent legal practice prior to the acquisition of the transaction and in the case of material changes.

## **Criterion B13: Alignment of interest (conduit level only)**

**40.149**In order to align the interests of those responsible for the underwriting of the credit claims and receivables with those of investors, a material net economic exposure should be retained by the sellers or the sponsor at transaction level, or by the sponsor at the conduit level. Ultimately, the sponsor should disclose to investors how and where a material net economic exposure is retained by the seller at transaction level or by the sponsor at transaction or conduit level, and demonstrate the existence of a financial incentive in the performance of the assets.

## **Criterion B14: Cap on maturity transformation (conduit level only)**

**40.150**Maturity transformation undertaken through ABCP conduits should be limited. The sponsor should verify and disclose to investors that the weighted average maturity of all the transactions financed under the ABCP conduit is three years or less. This number should be calculated as the higher of:

- (1) the exposure-weighted average residual maturity of the conduit's beneficial interests held or the assets purchased by the conduit in order to finance the transactions of the conduit<sup>37</sup>; and

- (2) the exposure-weighted average maturity of the underlying assets financed by the conduit calculated by:
  - (a) taking an exposure-weighted average of residual maturities of the underlying assets in each pool; and
  - (b) taking an exposure-weighted average across the conduit of the pool-level averages as calculated in Step 2a.<sup>38</sup>

#### Footnotes

<sup>37</sup> Including purchased securitisation notes, loans, asset-backed deposits and purchased credit claims and/or receivables held directly on the conduit's balance sheet.

<sup>38</sup> Where it is impractical for the sponsor to calculate the pool-level weighted average maturity in Step 2a (because the pool is very granular or dynamic), sponsors may instead use the maximum maturity of the assets in the pool as defined in the legal agreements governing the pool (eg investment guidelines).

### **Criterion C15: Financial institution (conduit level only)**

**40.151** The sponsor should be a financial institution that is licensed to take deposits from the public, and is subject to appropriate prudential standards and levels of supervision. National supervisors should decide what prudential standards and level of supervision is appropriate for their domestic banks. For internationally active banks, prudential standards and the level of supervision should be in accordance with the Basel framework. Subject to the determination of the national supervisor, in addition to risk-based regulatory capital this may include liquidity, leverage capital requirements and other requirements, such as related to the governance of banks.

### **Criterion C16: Fiduciary and contractual responsibilities (conduit level)**

**40.152** The sponsor should, based on the representations received from seller(s) and all other parties responsible for originating and servicing the asset pools, make representations and warranties to investors that:

- (1) the various criteria defined at the level of each underlying transaction are met, and explain how;



- (2) seller(s)'s policies, procedures and risk management controls are well-documented, adhere to good market practices and comply with the relevant regulatory regimes; and that strong systems and reporting capabilities are in place to ensure appropriate origination and servicing of the underlying assets.

**40.153**The sponsor should be able to demonstrate expertise in providing liquidity and credit support in the context of ABCP conduits, and is supported by a management team with extensive industry experience. The sponsor should at all times act in accordance with reasonable and prudent standards. Policies, procedures and risk management controls of the sponsor should be well documented and the sponsor should adhere to good market practices and relevant regulatory regime. There should be strong systems and reporting capabilities in place at the sponsor. The party or parties with fiduciary responsibility should act on a timely basis in the best interests of the investors.

### **Criterion C16: Fiduciary and contractual responsibilities (transaction level)**

**40.154**The sponsor should ensure that it receives representations from the sellers(s) and all other parties responsible for originating and servicing the asset pools that they:

- (1) have well-documented procedures and policies in place to ensure appropriate servicing of the underlying assets;
- (2) have expertise in the origination of same or similar assets to those in the asset pools;
- (3) have extensive servicing and workout expertise, thorough legal and collateral knowledge and a proven track record in loss mitigation for the same or similar assets;
- (4) have expertise in the servicing of the underlying credit claims or receivables; and
- (5) are supported by a management team with extensive industry experience.

### **Additional requirement for Criterion C16**

**40.155**In assessing whether "strong systems and reporting capabilities are in place", well documented policies, procedures and risk management controls, as well as strong systems and reporting capabilities, may be substantiated by a third-party review for sellers that are non-banking entities.

## **Criterion C17: Transparency to investors (conduit level)**

**40.156**The sponsor should ensure that the contractual obligations, duties and responsibilities of all key parties to the conduit, both those with a fiduciary responsibility and the ancillary service providers, are defined clearly both in the initial offering and any relevant underlying documentation of the conduit and the ABCP programme it issues. The “underlying documentation” does not refer to the documentation of the underlying transactions.

**40.157**The sponsor should also make representations and warranties to investors that the duties and responsibilities of all key parties are clearly defined at transaction level.

**40.158**The sponsor should ensure that the initial offering documentation disclosed to investors contains adequate provisions regarding the replacement of key counterparties of the conduit (eg bank account providers and derivatives counterparties) in the event of failure or non-performance or insolvency or deterioration of creditworthiness of any such counterparty.

**40.159**The sponsor should also make representations and warranties to investors that provisions regarding the replacement of key counterparties at transaction level are well-documented.

**40.160**The sponsor should provide sufficient information to investors about the liquidity facility(ies) and credit support provided to the ABCP programme for them to understand its functioning and key risks.

## **Criterion C17: Transparency to investors (transaction level)**

**40.161**The sponsor should conduct due diligence with respect to the transactions on behalf of the investors. To assist the sponsor in meeting its fiduciary and contractual obligations, the duties and responsibilities of all key parties to all transactions (both those with a fiduciary responsibility and of the ancillary service providers) should be defined clearly in all underlying documentation of these transactions and made available to the sponsor.

**40.162**The sponsor should ensure that provisions regarding the replacement of key counterparties (in particular the servicer or liquidity provider) in the event of failure or non-performance or insolvency or other deterioration of any such counterparty for the transactions are well-documented (in the documentation of these individual transactions).

**40.163** The sponsor should ensure that for all transactions the performance reports include all of the following: the transactions' income and disbursements, such as scheduled principal, redemption principal, scheduled interest, prepaid principal, past due interest and fees and charges, delinquent, defaulted, restructured and diluted amounts, as well as accurate accounting for amounts attributable to principal and interest deficiency ledgers.

### **Criterion D18: Credit risk of underlying exposures (transaction level only)**

**40.164** At the date of acquisition of the assets, the underlying exposures have to meet the conditions under the Standardised Approach for credit risk and, after account is taken of any eligible credit risk mitigation, be assigned a risk weight equal to or smaller than:

- (1) 40% on a value-weighted average exposure basis for the portfolio where the exposures are loans secured by residential mortgages or fully guaranteed residential loans;
- (2) 50% on an individual exposure basis where the exposure is a loan secured by a commercial mortgage;
- (3) 75% on an individual exposure basis where the exposure is a retail exposure;  
or
- (4) 100% on an individual exposure basis for any other exposure.

### **Criterion D19: Granularity of the pool (conduit level only)**

**40.165** At the date of acquisition of any assets securitised by one of the conduits' transactions, the aggregated value of all exposures to a single obligor at that date shall not exceed 2%<sup>39</sup> of the aggregated outstanding exposure value of all exposures in the programme.

## Footnotes

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*In jurisdictions with structurally concentrated corporate loan markets, subject to ex ante supervisory approval and only for corporate exposures, the applicable maximum concentration threshold could be increased to 3% if the sellers or sponsor retain subordinated tranche(s) that form loss-absorbing credit enhancement, as defined in [CRE44.16](#), and which cover at least the first 10% of losses. These tranche(s) retained by the sellers or sponsor shall not be eligible for the STC capital treatment.*