



Basel Committee on Banking Supervision  
Secretariat  
Bank for International Settlements

CH-4002 Basel

for information

Bundesanstalt für  
Finanzdienstleistungsaufsicht  
Graurheindorfer Straße 108

53117 Bonn

Deutsche Bundesbank  
Wilhelm-Epstein-Str. 14

60431 Frankfurt am Main

17 December 2002  
C 16 - Wk/g

**Revision of the Basel Capital Accord**

Second Working Paper on Securitisation of the Basel Committee on Banking Supervision  
- Comments of the German banks

Dear Sir, Madam,

We are grateful for the opportunity to comment on the Second Working Paper on Securitisation published on 28 October 2002. May we, however, point out that it was not possible for us to examine and assess your proposals fully in the short time allowed for a response. For this reason, we shall confine ourselves in the following to preliminary remarks, reserving the right to comment further at a later date.

We have divided our response into general and specific remarks. In the specific remarks, we refer to the relevant sections in the Working Paper. Where necessary, reference is also made to the same in the Technical Guidance (TG) to Quantitative Impact Study (QIS) 3.

### **General remarks**

May we begin by again underlining our central demand that the capital requirements set under the new rules for all banks involved in a securitisation transaction must, as a whole, not be higher than the capital requirements that would apply if the exposures were not securitised. As securitisation does not entail any increase in credit risk in the banking system there is no justification from a methodological standpoint for higher systemic capital requirements because of securitisation. Furthermore, this is the only way to create the conditions for a smoothly functioning securitisation market.

We also believe it is essential that identical external ratings lead to the same risk weights, and thus to an identical capital charge, for originators and investors. This is not the case in either the standardised approach or the IRB approach. As the external rating mirrors the risk of an ABS tranche, there is no reason from a risk angle to treat originators and investors differently. Moreover, the proposed unequal treatment harbours the danger of regulatory arbitrage. To take advantage of the preferential capital treatment accorded to investors, originators could swap their rated tranches with each other.

We also feel it is problematic in this context that the Basel Committee has no reliable information on how the proposed rules will affect the amount of regulatory capital. It is therefore essential that the proposed risk weights and the supervisory formula are regarded as provisional. Final calibration should thus only be performed once the results of the Basel Committee's QIS 3 have been duly evaluated.

### **Specific remarks**

#### ***Paragraph 5:***

According to the Basel Committee, the securitisation arrangements are to apply to every kind of transaction involving the "stratification" of credit risk. We assume in this connection that syndicated loans, where one bank has a different ranking in the event of bankruptcy, are not covered by the rules. For such loans, the arrangements under the standardised approach or IRB approach for corporates should apply accordingly.

**Paragraph 9:**

Banks which purchase pools of exposures under ABCP programmes are to be treated like originators. This is basically appropriate for the sake of equal treatment. We assume in this connection that such treatment is possible not only for ABCP programmes but for all securitisation programmes where banks purchase pools of exposures. Banks which only provide liquidity facilities or credit enhancements, on the other hand, should not necessarily have to be treated like originators.

It is to be welcomed that other banks than just those specified in paragraph 493 TG are to be allowed to treat securitisations under the IRB approach like originators, i.e. to apply the Supervisory Formula Approach (SFA), for example. However, our understanding is that supervisory approval is necessary for each specific transaction. This should be reviewed; an acceptable approach could be granting approval to calculate  $K_{IRB}$  for a particular class of risk assets, as is the case with originators.

Moreover, the criteria according to which such approval is to be granted are not specified further. Generally speaking, investors face the practical problem of not having enough information at their disposal to calculate  $K_{IRB}$ . For this reason, investing banks which are provided by the originator with the input parameters necessary for calculating  $K_{IRB}$  should be allowed to calculate capital requirements according to the originator approach.

**Paragraph 11:**

The Basel Committee's intention to extend the definition of "*eligible purchased corporate receivables*" to receivables with a remaining maturity of up to one year is to be welcomed, although it is not enough. The strict limitation of the top-down approach this involves would continue to make securitisations of certain types of receivables (e.g. leasing receivables) difficult or even impossible. Also where such receivables are concerned, banks purchasing the pool of receivables are not usually able to obtain the information necessary for calculating the capital charges for each individual credit exposure. This means that under the proposed system they would not be able to operate as originators. We therefore suggest extending the top-down treatment also to granular pools of receivables which contain receivables with an original maturity of more than one year.

**Paragraph 14:**

Originators are to deduct retained securitisation positions from capital up to  $K_{IRB}$ . According to paragraph 513 TG, the deduction has to be taken 50 % from Tier 1 capital and 50 % from Tier 2 capital. This arrangement must be rejected. Both Tier 1 and Tier 2 capital are freely available to banks to cover losses. This is why, under the current Basel Capital Accord, both capital components may be used at banks' discretion to back risk

assets. There is to be no change to this under Basel II either. The proposal is thus not only a breach of the tried and tested arrangement; it also *de facto* limits the eligibility of capital components, although the Basel Committee expressly stated that it would not be altering the capital components in the revised Capital Accord.

***Paragraph 16:***

In the standardised approach, banks which know the composition of pools can apply a “look-through” treatment to unrated most-senior tranches. This means that the risk weight of the tranche is to be based on the average risk weight of the securitised exposures in the pool. This treatment should be transferred to the IRB approach.

***Paragraph 17:***

According to the Basel Committee’s current proposals, the originator’s capital requirements are to be not more than  $K_{IRB}$ . This is a step in the right direction. As explained above, it must, however, be ensured that the capital requirements of all banks involved in a securitisation transaction do not exceed  $K_{IRB}$ .

The Basel Committee believes that capitalised assets should be deducted from Tier 1 capital also above  $K_{IRB}$ . In our opinion, neither the Working Paper nor the Technical Guidance make clear which assets are meant here.

It would also be interesting to know what the motivation for the deduction of capitalised assets from Tier 1 capital is. Depending on the definition and accounting method (agreed with auditors), such balance sheet items no longer contain any expected loss. Banks should be required to cover the unexpected loss in this case with Tier 1 and Tier 2 capital. A deduction from Tier 1 capital is, on the other hand, inappropriate in our view.

***Paragraph 28:***

The Basel Committee proposes, particularly for poorly rated ABS, higher capital requirements than for corporate bonds with an identical rating. Its justification is the supposedly higher marginal contribution of ABS to a bank’s portfolio risk. This is a disputed assumption. To allow a fruitful discussion of the scale of the differences in capital requirements for bonds and ABS, we urge the Basel Committee once again to disclose the methodology on which calibration of the risk weights and the supervisory formula is based.

***Paragraph 44:***

Paragraph 528 TG sets out criteria for defining an eligible liquidity facility. The aim is to draw a line between eligible liquidity facilities and credit enhancements. We feel that – in some cases at any rate – the criteria proposed are unsuitable:

- Subparagraph (b) stipulates that draws on the liquidity facility must not be subordinated to the interests of investors. This condition does not appear appropriate in every case, e.g. if the draw on the liquidity facility is accompanied by repayment of the investors. In this case, the ranking of the liquidity facility does not necessarily play a role, however. If the liquidity facility can only be drawn up to the amount of the performing loans, the bank that set up the facility has a claim on the cash flows from the pool of exposures in the above case. What is important in this connection is therefore not the ranking but the terms on which the facility can be drawn. This is regulated in the definition of the “borrowing base” in the contract. We therefore suggest deleting condition (b) and gearing the definition of eligible liquidity facilities to the borrowing base.
- Under subparagraph (c), the facility cannot be drawn once all the structure’s credit enhancements have been exhausted. This condition is also unnecessary if it is ensured that a liquidity facility may be drawn only for performing loans.

***Paragraphs 45 + 49:***

Generally speaking, we are in favour of using the same credit conversion factors (CCFs) in the standardised approach and in the IRB approach. The CCFs are a device for measuring the credit risk of liquidity facilities that is independent of the approach selected. Consideration could merely be given to setting lower CCFs in the IRB approach than in the standardised approach because of its greater risk sensitivity. This would at the same time increase the incentives to move to the IRB approach.

Eligible liquidity facilities that can only be drawn in the event of a general market disruption are not to attract any capital charge at all in the standardised approach. In the IRB approach, on the other hand, they are to be given a 20 % CCF. It is not clear when a general market disruption is to be deemed to exist, as the case referred to in the definition – where securities cannot be issued at any price (paragraph 530 TG) – is hardly realistic.

***Paragraphs 51 + 52:***

The definition of the structures that are to receive the special treatment for structures with early amortisation clauses is not clear-cut in our opinion. According to paragraph 540 TG, it includes structures which both (a) contain an early amortisation feature and (b) securitise exposures of a revolving nature.


It follows (logically) from this that all securitisations of non-revolving exposures are not subject to the special treatment regardless of whether or not they contain an early amortisation feature. For this reason, the exemption in paragraph 543 TG for securitisations if

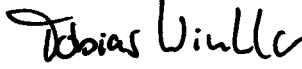
the securitised exposures do not revolve **and** the early amortisation clause merely covers a stop of replenishment is more restrictive than the arrangement proposed under the definition in paragraph 540 TG. It should therefore merely be made clear that stop of replenishment clauses do not constitute an early amortisation clause under paragraph 540 (a) TG.

Moreover, the definition of “revolving exposures” is not clear either, as in both the Working Paper (footnote 13, p. 11) (“*include assets ...*”) and the Technical Guidance (paragraph 540 (b)) (“*i.e. lines of credit ...*”) only examples are given. It is unclear whether these examples are exhaustive or whether other exposures are (must be) considered as revolving.

Please do not hesitate to contact us should you require any further clarification.

Yours sincerely,

  
Dr. Wolfgang Arnold

  
Dr. Tobias Winkler

