29th July 2015

DG FISMA
The European Commission
SPA2 – Pavilion
Rue de Spa 2
1000 Brussels
Belgium

Dear [Name],

Preliminary headline comments of AFME on the EBA Report on Qualifying Securitisation published 7 July 2015 - Criteria for ABCP Programmes and Transactions

We wish to thank the Commission for the opportunity to share our comments on the EBA Report. Further to our previous comments on the term ABS criteria, and in the spirit of our continuing constructive engagement with the Commission’s work in this area, we set out below preliminary comments on the proposed qualifying securitisation criteria for ABCP programmes and underlying securitisation transactions.

We wish to emphasise that, because these proposed criteria are complex and their adaptation to ABCP programmes and transactions are newly developed (unlike the term ABS criteria which are based fairly closely on those in earlier consultation documents), we are still reviewing and analysing the proposal and may have further significant comments. We aim to submit, within the next week, more detailed comments on individual criteria, but are sending you these preliminary comments first because we know the Commission has limited time to complete its review.

Executive summary

- We are grateful that the EBA has proposed to include ABCP programmes and transactions within the qualifying securitisation regime, and has clearly applied much effort to the difficult task of adapting criteria developed for term ABS to the programme and transaction levels of ABCP structures.

- We are concerned, however, that under the criteria as proposed, it is likely that no existing ABCP programmes would qualify, and few if any of the underlying transactions currently funded in ABCP programmes would qualify.

- This could mean that this important initiative would not achieve its goal, and that its results could instead further constrain and discourage the use of securitisation through...
ABCP conduits, and similar transactions funded by banks, to provide funding for European commercial and consumer finance.

- Qualifying securitisation status will be critical for European ABCP conduits, because up to 70% of their funding comes from European money market funds (MMFs), which, under the proposed MMF regulation, will be allowed to invest in ABCP only if it meets qualifying securitisation criteria.

- ABCP conduits that do not meet those criteria, and so cannot place their paper with EU MMF investors, will then have to rely on the USCP market, which leaves them exposed to adverse market conditions such as occurred in mid-2011.

We believe it is important that the criteria be relatively simple and clear and that they take into account the special characteristics of ABCP programmes and, at the transaction level, those of private and bilateral transactions funded by ABCP programmes or by banks directly. Please refer to AFME’s response to question 2 in the Commission’s consultation document from earlier this year on simple, standard and transparent securitisations (the “STS Comments”; copy attached). The comments and proposals made in that response should be taken into account and, we believe, would be a better starting point for designing ABCP programme and transaction criteria.

While we recognise the need to move this project forward quickly and to include ABCP programmes and transactions within qualifying securitisation, we urge the Commission to take further advice and to engage with industry representatives on these criteria before proposing legislation.

Transaction criteria

1. Criterion 1: Banks that purchase receivables or otherwise become exposed to securitisation transactions meeting the transaction level criteria for qualifying securitisations within ABCP programmes (other than any criterion that requires the transaction to be within an ABCP programme) should be allowed to treat those transactions as qualifying securitisations even though the transactions are not within an ABCP programme. See our comments under “Allowing for private transactions” on part B of question 2 in the STS Comments.

2. The one-year limit on maturity of underlying exposures (Criterion 4 point (v)) should be omitted. Otherwise few if any existing programmes will qualify, and qualifying programmes will have to cease financing standard asset classes that make up a large part of their current portfolios (such as vehicle finance and consumer credits). Where (as required by the programme-level criteria), the sponsor takes all liquidity risk and other risks of the underlying transaction, and the sponsor is already subject to prudential controls on exposure to liquidity, credit and other risks, there is no reason to require that maturities of underlying assets, like those of the ABCP, be limited to one year. In particular, the liquidity coverage ratio (LCR) already limits maturity transformation by banks. The “economic borrower” limit – which applies the large exposure rules to all of a bank’s exposures to all its commercial paper conduits together – further limits a bank’s exposures to maturity transformation through ABCP programmes. A third such constraint would be unwarranted and harmful to the market.
3. At transaction level, formal disclosure documents should not be required (Criteria 2, 14, 16 and others), so long as the relevant parties (typically the conduit sponsor(s) and/or purchasing bank(s), the originator and sometimes an independent swap counterparty or credit enhancement provider) in fact have access to the relevant information.

4. The criterion requiring no higher than 75% risk weight for retail exposures and no higher than 100% risk weight for other exposures on an individual basis (Criterion B point (ii)) will exclude many trade receivables transactions, securitisations of SME credits and other transactions with any obligors rated below investment grade. Non-bank originators will not be able to determine or report obligor risk weights, and even bank conduit sponsors in many cases (particularly in revolving pools of short-term receivables) would not determine or monitor risk weights of each obligor, but would risk-weight their exposure to the pool using the internal assessment approach, top-down approach or ratings-based approach. This criterion would also mean that a qualifying securitisation, and by extension a qualifying ABCP programme, could become non-qualifying whenever the credit rating of a single obligor in a single underlying pool was downgraded. The credit risk capital requirements framework applicable to qualifying securitisations, like that for other securitisations, is already designed to take account of variations in credit quality of underlying assets.

5. As almost all the criteria that apply to term securitisations are also proposed to apply, in slightly modified form, to qualifying transactions in ABCP programmes, AFME's preliminary comments on those term securitisation criteria (copy attached) also apply to the ABCP transaction criteria. Some of these criteria give rise to heightened issues for transactions in ABCP conduits and other bilateral or private transactions. In particular:

(a) Criterion 19 requires parties having exposure to an underlying transaction to have readily available access to data on static and dynamic historical default and loss performance data for substantially similar assets covering a period of at least 5 years for retail exposures and 7 years for other exposures. While this criterion would be difficult for many originators in term ABS transactions, we believe that companies which typically seek to access funding via conduits are even less likely to be able to generate this information.

(b) Criterion 20 requires persons holding positions in underlying transactions to have readily available access to data on the underlying exposures, including under any applicable requirements under CRA3 Article 8b, before pricing. As in the case of term ABS, this requirement overlaps with other provisions, and disclosure requirements for underlying transactions should be in line with, and not in addition to, CRR Article 409 and any applicable requirements under Article 8b. Please refer to AFME's response dated 20 May 2015 to the European Securitisation and Markets Authority's Call for Evidence on Extension of the disclosure requirements to private and bilateral transactions for Structured Finance Instruments (copy attached).

(c) Criterion 5, which defines defaulted assets and credit-impaired obligor assets that must be excluded from any qualifying securitisation, raises concerns for term ABS and equal or greater concerns for ABCP conduit transactions (and other bilateral or private securitisations). In particular, the 90 day past due test
is problematic for credit card and trade receivables, and the “significant risk of default” test is too uncertain.

Programme level criteria

6. Assets of ABCP programmes may include not only securitisation transactions, but also secured lending transactions or other transactions that, for whatever reason, do not qualify as “securitisation” under the CRR definition. In particular, ABCP conduits often buy trade receivables in transactions structured without credit risk tranching to be consistent with seller off-balance sheet accounting treatment. Such transactions – which often provide significant funding for SME clients of the bank sponsors - would not fall within the CRR definition of securitisation at all, still less conform to the qualifying securitisation criteria. Given the different nature of such arrangements, they should not be required to conform to the criteria. Indeed, it is essential that the criteria allow an ABCP programme to include such non-securitisation transactions without affecting its status as a qualifying ABCP programme.

7. Requiring every securitisation transaction in an ABCP programme to meet all the transaction criteria at all times (Criterion 1) means that a qualifying programme could cease to qualify from time to time if any one of the transaction criteria ceased to be met for any one of the transactions in the programme. This would make an ABCP programme’s qualification very unstable, especially if the underlying transaction criteria include requirements (such as maximum risk weights for each obligor) that could easily cause a previously qualifying transaction to cease to qualify. To provide for stability in qualification status, and to give sponsors some flexibility in managing their programmes, we propose an 80% minimum requirement, meaning that at any time at least 80% of the programme’s assets would have to be exposures to qualifying securitisation transactions or to non-securitisation transactions, and up to 20% of the programme’s assets could be exposures to non-qualifying securitisation transactions.

8. The criteria should make clear that investors in ABCP will not have to make their own determination (or to receive all the information that would be required to determine) that each of the underlying securitisation transactions in an ABCP programme is a qualifying securitisation (Criterion 1), and that such investors may instead rely on disclosure by the sponsor that it has determined that the transactions meet those criteria.

9. We strongly disagree with the requirement that qualifying ABCP should not include any call options, extension clauses or other clauses which have an effect on the final maturity of the ABCP (Criterion 5). While certain “extendible” CP structures were problematic during the financial crisis, those structures were very different from multi-seller ABCP programmes for the following reasons. Firstly, in those structures the conduit (not the investor) had the option to extend the maturity. Secondly, the CP was not fully supported by bank liquidity facilities and thirdly, when maturity was extended, payment depended on liquidation of underlying assets. In today’s market, those structures no longer exist and the problematic features described are simply not present in multi-seller ABCP programmes. It is however the case that many multi-seller ABCP programmes, both in Europe and in the US, have added the capacity to issue “structured” commercial paper, including CP with call options (held by the conduit) or put options (held by the investor), for purposes of prudent liquidity
management. We see no rationale for excluding ABCP with those features, and ask for this criterion to be omitted.

10. The requirement of an “identified person” with fiduciary duties to investors (Criterion 8, corresponding to Criterion 13 for term securitisations) and with powers to “take effective decisions, in all circumstances” would represent a substantial change from current market and investor requirements. Because ABCP has short maturities and full liquidity and credit support from the sponsor bank, the programme structures typically do not require a note trustee, or provisions for meetings of noteholders. Problems that arose during the financial crisis in relation to inadequate procedures or difficulty in finding decision-makers for resolving deadlocks or disputes involved structured investment vehicle (SIV) programmes that did not have full liquidity support, relied on realisation of underlying assets to pay noteholders, and usually had several classes of noteholders. Bank-sponsored multi-seller commercial programmes, like those dealt with in these criteria, do not have these attributes. On the contrary, sponsor banks most often use their multi-seller ABCP conduits to fund the best assets of their best clients, and they are highly incentivised to manage their conduits prudently in the best interests of their clients. In addition, where an ABCP programme relies on full support from the sponsor bank, it is unrealistic to require a representative of noteholders to arrange for “timely replacement of the liquidity provider” in case of default.

11. The proposed requirements (in Criterion 15) for investor reports to include “all materially relevant data on a sufficiently detailed (at least stratified) basis on the credit quality and performance of the exposures in the underlying pools, including data allowing any party holding a securitisation position at the conduit level to clearly identify debt restructuring/forgiveness, forbearance, repurchases, payment holidays, delinquencies and defaults in the underlying pools”, would make it impossible for any existing programmes and likely future programmes to qualify. Bank-sponsored multi-seller ABCP programmes typically provide monthly reporting on performance of underlying transactions, but typically do not provide, and ABCP investors do not require, details of securitised exposures underlying the transactions in the programme. There would be serious legal, commercial and operational obstacles to providing such information, and ABCP investors do not need it because they rely primarily on the sponsor bank. Our understanding was that the EBA intended programme-level disclosure criteria for qualifying ABCP to be consistent with existing market practice. Unfortunately, this criterion does not achieve this.

12. The proposed requirement for aggregate exposures to any one obligor or group of connected obligors across all transactions not to exceed 1% of all programme assets (Criterion A) would be disproportionate, impractical for ABCP investors to monitor, and unnecessary insofar as ABCP investors are not primarily exposed to the credit risk of the underlying obligors. It would be unworkable especially because of the revolving nature of most assets and transactions in ABCP programmes. This criterion should be omitted. The risk-based capital framework, and the proposed amendments to that framework for qualifying securitisations, already distinguish securitisation positions according to credit quality.

13. Consideration should be given to relaxing the requirement for the sponsor to be the sole and exclusive liquidity provider, so as to allow sharing or syndication of such facilities either within the sponsor’s consolidated group or with or to third party
banks. Syndication of lending spreads risk, and is a well-tested feature of the wholesale bank markets. We do not understand the rationale for its exclusion.

Transaction and programme level criteria

14. Where criteria allow for compliance with a specific EU regulation or, in the case of a non-EU transaction or programme, equivalent legal requirements of another jurisdiction, it should be made clear that, as an alternative, the transaction or programme may comply with the relevant EU requirements (e.g., CRR Article 409 or PD Annex VII) as if they applied to that transaction. Other jurisdictions may not have equivalent regulatory requirements that would apply to ABCP or to securitisation transactions within an ABCP conduit.

15. The criteria need to distinguish clearly between the transaction and programme levels of the ABCP structure; programme-level criteria should not refer to transaction-level matters or vice versa. Confusing or conflating criteria for the two levels may make it difficult or impossible for transactions or programmes to comply. For example, proposed programme-level Criterion 3 deals with full support being provided to ABCP investors, but starts by referring to “[s]upport provided to securitisation positions at transaction level”, including “liquidity facilities” (which are normally provided at programme level, though relating to particular transactions) and “refundable purchase price discounts” (which are a form of credit enhancement provided at transaction level). Another example is programme-level Criterion 15 which seems to require ABCP investors to have detailed information about individual exposures in underlying pools.

Thank you again for the opportunity to engage with the Commission on this subject. If it would be helpful to the Commission, we would be pleased to undertake a detailed technical discussion to help resolve and/or progress outstanding issues, or answer any questions. AFME would be pleased to arrange this with our members if and when the Commission felt it appropriate.

We hope the above comments are helpful to the Commission in its efforts to revive and rebuild Europe’s securitisation markets so that they can make their proper contribution to Capital Markets Union.

Yours faithfully,