The Association of Corporate Treasurers

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Comments in response to
An EU framework for simple, transparent and standardised securitisation
European Commission, 18 February 2015

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The Association of Corporate Treasurers (ACT)

The ACT is a professional body for those working in corporate treasury, risk and corporate finance. It is established by Royal Charter in the public interest. Further information is provided at the back of these comments and on our website www.treasurers.org.

Contact details and a link to our approach regarding policy submissions can also be found at the back of these comments.

We canvas the opinion of our members through seminars and conferences, our monthly e-newsletter to members and others, *The Treasurer magazine*, topic-specific working groups and our Policy and Technical Committee.

General

The ACT welcomes the opportunity to comment on this matter. Securitisation is an important and attractive source of funding for non-financial companies (NFCs). It provides NFCs with an alternative source of funding to bank loans and other capital market instruments such as bonds.

An example of a large user of securitisation is the European automotive industry. This industry provides financing for about seven million new cars each year through captives, which themselves rely on the securitisation of customer receivables as a source of funding.

Identification criteria for qualifying securitisation instruments

Question 1:
A. Do the identification criteria need further refinements to reflect developments taking place at EU and international levels? If so, what adjustments need to be made?
B. What criteria should apply for all qualifying securitisations ('foundation criteria')?

A. In principle we agree with the identification broad criteria, namely Simplicity, Transparency and Standardisation. However we would encourage the EU to structure the identification criteria for qualifying securitisation based on liberal broad parameters rather than specific detailed rules. Increased compliance costs will not encourage the revival of the European securitisation markets. Given that attracting international investments is one of the objectives of the CMU, the criteria should also facilitate investment from outside the EU rather than applying concepts that are only relevant in the EU.

   We acknowledge that re-securitisations do not fit within the simplicity criterion but care needs to be taken about how you define re-securitisation. The last financial crisis provided examples of re-securitisations where low credit quality notes had been re-packaged and credit enhanced, resulting in not only lack of transparency but also making it difficult to model credit quality.

   Synthetic securitisation is used in some jurisdictions where there are obstacles, such as tax, to the transfer of ownership of the asset and only the credit risk is transferred by way of a credit default swap. The costs of synthetic securitisation are often considerably lower than those of a full asset transfer. We therefore believe synthetic securitisations should be included, provided the transaction meets the STS criteria, including appropriate transparency, and that the underlying portfolio is owned by the originator of the securitisation, and appropriate collateral is provided.

   It is also of great importance to corporates that they retain the ability to negotiate non-assignment clauses in respect of loans with their banks. Corporate treasurers not only need to manage the exposure to financial institutions but also the relationship with their banks. For smaller companies this is especially important as assignment to an unsympathetic bank or to a securitisation scheme with no ability to review, could cause major problems and even business failure.

Identification criteria for short term instruments

Question 2:
A. To what extent should criteria identifying simple, transparent, and standardised short-term securitisation instruments be developed? What criteria would be relevant?
B. Are there any additional considerations that should be taken into account for short-term securitisations?

A. The ACT strongly believes short term securitisation instruments, such as ABCP should be included within the EU framework for securitisation. ABCP is an important source of funding for non-financial corporates. The most common types of ABCP are trade receivables, auto loans and leases, equipment leases, consumer loans and

credit card receivables. In order to support the development of the markets and meet the CRR definition of securitisations (which is not limited to public deals or to those involving securities, and includes bilateral transactions); other types of private transactions should also be included, e.g. transactions between banks and their customers, and investors financing ABCP programmes, provided they meet the STS criteria. Trade receivables securitisation is potentially a very important and attractive source of funding for SMEs, however we note there are other alternative structures that could potentially be more attractive and deserve consideration, such as the Nacional Financiera solution, a Mexican government platform[1].

B. An effective securitisation of trade receivables structure requires transfer of ownership without recourse. If this does not occur the structure is effectively a very short term 'loan' from the finance house and will be classed as borrowings on the originator's balance sheet and impact financial covenants. Hence transfer of ownership is key.
Disclosure requirements should also be taken into account for short term securitisations. Originators would be discouraged from using ABCP if they were required to disclose information (often commercially sensitive) at loan level rather than pool level.
Additionally the practical aspects and their potential impact on the originator should not be ignored. For example, once an asset which is 'churned' (trade receivables) is sold/securitised, it is important that the pipeline of the instrument continues. If invoices to a large customer are sold/securitised the loss or even a reduction in sales to the customer will have a significantly negative effect on liquidity of the seller/originator.

Risk retention requirements for qualifying securitisation

Question 3:
A. Are there elements of the current rules on risk retention that should be adjusted for qualifying instruments?
B. For qualifying securitisation instruments, should responsibility for verifying risk retention requirements remain with investors (i.e. taking an "indirect approach")? Should the onus only be on originators? If so, how can it be ensured that investors continue to exercise proper due diligence?

A. The consultation document notes that "by definition these (securitisation) instruments will qualify only if they fulfil the risk retention requirements." We agree with the principle of risk retention.

B. The investor should be provided with enough information in the prospectus in order to do the due diligence and understand the percentage of risk the originator has retained. We believe if transactions meet the STS criteria a "direct approach" (i.e. verification by parties other than the investor) should be permitted, subject to appropriate controls, as this will reduce compliance costs for investors and thus

[1] The Nacional Financiera (NaFin) http://www.nafin.com/portalnf/content/otros/english.html solution in Mexico is a working example of how commercial banks and large buyers can be bought together with government support. Although there are of course significant differences between Mexico and the UK, NaFin offers an interesting insight into how a central bank can work with multiple commercial banks in developing a national SCF market.
Refer also the Supply Chain Finance Working Group report https://www.treasurers.org/scf, published by the ACT.

encourage investors into the market. However we acknowledge this may require some form of independent third party certification but it is important that the cost should not be too high for the originator.

Compliance with criteria for qualifying securitisation

Question 4:
A. How can proper implementation and enforcement of EU criteria for qualifying instruments be ensured?
B. How could the procedures be defined in terms of scope and process?
C. To what extent should risk features be part of this compliance monitoring?

The ACT concurs with the European Banking Authority's comments on enforcement: "The EBA believes that all relevant competent authorities should adopt the necessary arrangements to have sufficient dedicated resources with specific knowledge of securitisation so as to ensure proper supervision of credit institutions and investment firms originating and investing in securitisations."[2]

We would suggest a mechanism to monitor and verify compliance such as a "labelling" system may work to identify securitisations that meet the qualifying criteria.

Standardisation should be based on principles rather than a set of rules, hence enforcement should allow for sensible flexibility.

Elements for a harmonised EU securitisation structure

Question 5:
A. What impact would further standardisation in the structuring process have on the development of EU securitisation markets?
B. Would a harmonised and/or optional EU-wide initiative provide more legal clarity and comparability for investors? What would be the benefits of such an initiative for originators?
C. If pursued, what aspects should be covered by this initiative (e.g. the legal form of securitisation vehicles; the modalities to transfer assets; the rights and subordination rules for noteholders)?
D. If created, should this structure act as a necessary condition within the eligibility criteria for qualifying securitisations?

In addition to private sector initiatives for a harmonised EU securitisation structure, the consultation document proposed the creation of an EU securitisation structure that might further address:
i. the legal form of the SPVs used for securitisation transactions;
ii. The modalities to transfer assets; and
iii. The rights and subordination rules among noteholders.

A. Whilst the ACT is broadly supportive of a level of standardisation in the securitisation market we do not envisage a high impact on the development of the EU securitisation markets principally due to two fundamental structural differences between countries i.e. property ownership and insolvency laws. If EU legislation

[2] EBA report on securitisation risk retention, due diligence and disclosure, 22 December 2014

cannot change the system of property ownership or insolvency laws in a member state then a unanimous resolution by all member states would be required to ensure the impact of standardisation is effective. We believe this is highly unlikely in the near future.

The ACT believes that further standardisation in the structuring process should be principles rather than rules based. Standardisation should not be unduly prescriptive or introduce a standardised format. Details rules would not assist in addressing the mis-alignment of regulatory treatment of securitisations with similar products e.g. covered bonds, loan portfolios.

B. A harmonised EU-wide initiative may allow more consistent and simple documentation for originators. A securitisation structure will often be cross border and conflicts of transfer in debtor countries can arise. An example given by an originator was a non-recourse invoice discounting transaction for invoices issued to French, Italian and German debtors. With respect to France it was necessary to ensure the debt was directly collectable, with the title of debt transferring to the finance house. In Germany, the transfer of debt required the approval of the debtor and ultimately wasn't included in the structure. Whilst in Italy it was argued that the sale was effectively a 'charge' against the total available credit of the debtor and title to the debt was only transferred after much discussion and approval by the senior creditor. This transaction required a considerable amount of work in terms of documents and legal opinions by the originator.

C. Refer point B above.

D. No, we do not believe that a harmonised EU wide structure should be mandatory as a new untested regulatory structure will do little to encourage growth in the European securitisation market (which is one of the objectives of the European Commission).

Standardisation, transparency and information disclosure

Question 6:
A. For qualifying securitisations, what is the right balance between investors receiving the optimal amount and quality of information (in terms of comparability, reliability, and timeliness), and streamlining disclosure obligations for issuers/originators?
B. What areas would benefit from further standardisation and transparency, and how can the existing disclosure obligations be improved?
C. To what extent should disclosure requirements be adjusted – especially for loan-level data[15] – to reflect differences and specificities across asset classes, while still preserving adequate transparency for investors to be able to make their own credit assessments?

A As with our comments on the EU's review of the Prospectus Directive consultation (published 18 February 2015) the ACT notes that whatever the standardisation concept agreed, it needs to be consistent across the EU member states and in each regulated market. This includes not just a centralised rule book but consistent enforcement between member states.
Disclosure requirements should be appropriate to the type of transaction. For example public disclosures are not necessary or appropriate for a private deal where the investor has opportunity for due diligence.

C Comments in our response to question 2A above are also relevant here. Disclosure at a granular level by loan will not be acceptable to many underlying obligors of the portfolio. Disclosure at a loan level may disclose commercially sensitive information which would be a strong disincentive to the use of ABCP.

Prudential treatment for banks and investment firms

Question 9:
With regard to the capital requirements for banks and investment firms, do you think that the existing provisions in the Capital Requirements Regulation adequately reflect the risks attached to securitised instruments?

The ACT is not in a position to comment in detail on prudential measures for capital, solvency and liquidity, but we believe that for a securitisation market to function efficiently the capital and liquidity weightings for securitisations that meet the STS criteria should be lower than those which apply to more complex structures. The weightings for STS securitisation should aim, in principle, to achieve capital neutrality between the securitised assets and the underlying portfolio.

Role of securitisation for SMEs

Question 16:
A. What additional steps could be taken to specifically develop SME securitisation?
B. Have there been unaddressed market failures surrounding SME securitisation, and how best could these be tackled?
C. How can further standardisation of underlying assets/loans and securitisation structures be achieved, in order to reduce the costs of issuance and investment?
D. Would more standardisation of loan level information, collection and dissemination of comparable credit information on SMEs promote further investment in these instruments?

Facilitating private deals is necessary for SMEs. Banks will bundle together packages of receivables from numerous SMEs into one structure which will then be sold onto an insurance company. It is not necessary (and will inhibit future transactions) for these private deals to become public knowledge.

The Association of Corporate Treasurers

The Association of Corporate Treasurers (ACT) is the leading professional body for international treasury, operating in the public interest under Royal Charter. We provide the widest scope of benchmark qualifications for those working in treasury, risk and corporate finance. Membership is by examination. We define standards, promote best practice and support continuing professional development. We are the professional voice of corporate treasury, representing our members.

Our 4,500 members work widely in companies of all sizes through industry, commerce and professional service firms.

For further information visit www.treasurers.org

Guidelines about our approach to policy and technical matters are available at http://www.treasurers.org/technical/manifesto.

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