afme / Finance for Europe

30 September 2021

European Banking Authority
Submitted via - www.eba.eu

RE: EBA Consultation Paper of 30 June 2021 on the revised Draft Regulatory Technical Standards Specifying the Requirements for Originators, Sponsors, Original Lenders and Servicers Relating to Risk Retention[1]

On behalf of the Association for Financial Markets in Europe (**AFME**) and its members, we welcome the opportunity to comment on the revised draft technical standards (the **Draft RTS**) relating to the risk retention requirements under Regulation (EU) 2017/2402 (the **Securitisation Regulation**). The continuing engagement of the European Banking Authority (**EBA**) with market participants on issues related to risk retention is greatly appreciated.

AFME members have identified a number of comments on the Draft RTS. These comments are set out below. In particular, we wish to draw the EBA's attention to the following points.

- **Fees payable to retainers:** A specific issue, which would make many, otherwise viable, deals un-structurable, arises from the interaction of the proposed restrictions in the Draft RTS on fees payable to retainers that are guaranteed or payable upfront, and the broad scope of fees envisaged by proposed Article 15(2). Fees that are guaranteed or payable upfront are (in effect) deductible from the recognised risk retention, while Article 15(2) potentially captures fees for pre-closing, or closing, services such as arranging/managing/underwriting, that are, generally, and appropriately, substantial and payable at or around closing, and the amount of which may have been determined in advance of the relevant service having been provided. As a minimum, to address this specific concern, fees relating to pre-closing and closing services, the amount of which may have been determined in advance of the relevant service having been provided, should be exempted from the restrictions on fees that are guaranteed or payable upfront (if those restrictions are retained). Our strong view, however, is that the proposed guidance is too prescriptive, inflexible and would introduce significant uncertainty. Therefore, (i) restrictions on fees that are guaranteed or payable upfront, and (ii) requirements elaborating the *meaning* of the term "arm's length", should be deleted altogether. Fees that are arm's length (on the ordinary meaning of the words, which is well understood in contract and legal interpretation) and therefore not designed to undermine the risk retention (contrary to the existing clear statement of principle in Article 15(1) of the regulation) should have no impact on the level of retention required.

[1] https://www.eba.europa.eu/sites/default/documents/files/document_library/Publications/Consultations/2021/Consultation%20on%20draft%20RTS%20specifying%20the%20requirements%20for%20originators%2C%20sponsors%2C%20original%20lenders%20and%20servicers%20relating%20to%20risk%20retention/1016370/Consultation%20Paper%20on%20RTS%20on%20risk%20retention%20in%20securitisation.pdf

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- **Synthetic excess spread (SES) based retention:** We appreciate the intention and the logic behind the proposal to (broadly) allow an originator retainer to count synthetic excess spread that incurs a capital charge under new Article 248(1)(e) CRR towards satisfaction of the first loss tranche retention option. However, we note that, as indicated in data shared separately by members with the EBA, the new SES capital charge is economically punitive and, in practice (for reasons articulated below), likely to be minimally impacted by SES-based retention, or, indeed, by the other adjustments that might be expected to moderate its effects (i.e. on-balance sheet STS and the adjustment of the attachment and detachment points of the originator's other retained tranches under Article 256(6) CRR). Restriction of SES-based retention to the first loss tranche retention option (as proposed) significantly limits its utility, making it virtually impossible for an originator to demonstrate compliance with the required maximum amounts in the first loss test (where SRT is demonstrated), and increasing the amount of deductible retained securitisation positions (relative to risk retention via retained assets/portions of assets) on all approaches. Although SES-based retention would still not meaningfully moderate the economically punitive consequences of the new SES capital charge, it would be preferable if the new SES capital charge could count towards (i.e. be deducted from the required material net economic interest for) **any** form of retention rather than merely the first loss tranche retention option in Article 6(3)(d) of the Securitisation Regulation. We note that the Securitisation Regulation, itself, is silent about the way(s) in which excess spread should be recognised within the risk retention framework.

- **Servicer-retainers:** Firstly, where retention is fulfilled by multiple servicer-retainers (rather than by the servicer with the predominant economic interest in successful workout), the retention should be proportional to the securitised exposures serviced rather than to the number of servicers. Secondly, the implications, for risk retention, of replacement of a servicer-retainer should also be clarified to avoid confusion. In our view, continued retention by a servicer-retainer whose appointment has terminated should be permitted (in order to ensure the initial symmetry of interests of the servicer-retainer and investors, and to avoid issues for other transaction parties in identifying replacement servicers - whose estimates and valuations of the expected NPE portfolio collections and performance may differ from those of the original servicer-retainer at closing). However, in light of the policy objective of aligning the interests of the sell-side parties with the interests of the investors in securitisations (to better protect the investors), transfer of the retained interest to a replacement servicer, or other eligible retainer, should also be permitted at the option of the securitisation's investors where the original servicer-retainer's appointment has terminated. The same logic appears relevant to other categories of retainer whose eligibility flows from their contractual appointment by the securitisation.

- **Recital 8 and retention in the context of ABCP programmes:** In discussing the retention requirements associated with resecuritisations, Recital 8 to the Draft RTS includes a reference to ABCP transactions which has confused and concerned members. The application of the risk retention requirements to ABCP programmes is highly fact-pattern specific. We would therefore ask the EBA to delete the sentence in Recital 8 that refers to ABCP.

We would, of course, be happy to meet with the EBA to discuss these points and any of the other comments raised in our response.

Finally, although outside the scope of the present consultation, we refer the EBA to our response to the "EU Targeted Consultation on the functioning of the EU Securitisation Framework" of the European Commission in so far as it relates to risk retention, and in particular our serious concerns about the possibility of jurisdictional restrictions being imposed in relation to risk retention eligibility as mooted in the Joint Committee of the ESAs' Joint Opinion of 26 March 2021.

Question 1: Do you agree with the provisions in this Article 9 with respect to the application of the retention options on the NPE securitisations, and the "net value" regime of the NPE securitisations? Are the retention options specified under Articles 4 to 8 sufficiently clear using the net value regime? Are there any other aspects of NPE securitisation and the net value regime that should be clarified in the RTS?

A. Technical drafting suggestions regarding retention options for NPE securitisations:

The drafting of Article 9 should be clarified in certain respects.

The proposed mechanic for establishing the non-refundable purchase price discount for retained randomly selected exposures (Article 6 of the Draft Retention RTS) should presumably also apply to the retention options involving a pro rata retention of a portion of each securitised asset (Articles 4(a) and 5 of the Draft RTS) since (like randomly selected exposures) the retained portion of each asset in these circumstances is not securitised.

It would be helpful to clarify that the non-refundable purchase price discount in these circumstances may be established by any of the methods referred to in Article 6(3a) of the Securitisation Regulation (i.e. it may be agreed at the level of each individual securitised exposure at the time of origination, agreed at the level of the pool of underlying exposures at the time of origination, be the difference between the nominal amount of the tranches of the NPE securitisation underwritten by the originator for subsequent sale and the price at which these tranches are first sold to unrelated third parties, or – ideally – a combination of these methods).

Points (a) to (e) inclusive of Article 6(3) of the Securitisation Regulation (in addition to Articles 4 to 8 of the Draft RTS as proposed) should be qualified by interpreting references to the nominal value of the securitised exposures/nominal value of the issued tranches as references to the net value of the non-performing exposures. This is necessary because not all of the retention options in Article 6(3) of the Securitisation Regulation are actually addressed in Articles 4 to 8 of the Draft RTS, or addressed using the terms "*the nominal value of the securitised exposures*" or "*the nominal value of the issued tranches*".[2] It may be worth clarifying that references to "*the nominal value of each of the securitised exposures*" or "*the nominal value of each of the issued tranches*" in Articles 4(c) and 5 of the Draft RTS are similarly qualified.

It would assist in terms of clarity to set out the methods identified in Article 6(3a) of the Securitisation Regulation for establishing a 'non-refundable purchase price discount' in the text of the Draft RTS, ideally flagging that any combination of these methods is permitted, and to clarify that where a non-refundable purchase price discount is agreed at the level of each individual securitised exposure at the time of origination, the net value of each non-performing exposure shall be calculated by deducting the non-refundable purchase price discount from the exposure's nominal value. The mechanic for deriving individual asset NRPPD from an NRPPD agreed at pool level[3] should also cover NRPPD resulting from the difference between the nominal amount of the tranches of the NPE securitisation underwritten by the originator for subsequent sale and the price at which these tranches are first sold to unrelated third parties.

[2] Article 6 of the Draft RTS (unlike Article 6(3)(c) of the Securitisation Regulation) only includes reference to "the nominal value of the securitised exposures" in its title and not its operative provisions. Article 7(1) of the Draft RTS does not cover the base case in Article 6(3)(d) of the Securitisation Regulation, i.e. an on-balance sheet first loss tranche covering 5% of the nominal value of the securitised exposures that is not achieved by overcollateralisation (i.e. where the originator subscribes for notes/certificates). Article 7(1) of the Draft RTS should also be amended, for this reason, to clarify that contingent retention and overcollateralisation are not the exclusive methods of satisfying Article 6(3)(d) of the Securitisation Regulation. Article 8 of the Draft RTS does not address the base case of retention option in Article 6(3)(e) of the Securitisation Regulation using the words "*the nominal value of the exposure*" and neither does Article 6e of the Securitisation Regulation itself. For this reason, Article 8(1) of the Draft RTS should be amended to refer to a "first loss exposure of 5% of the nominal value of every securitised exposure" rather than "a first loss exposure at the level of every securitised exposure".

[3] Article 9(3) in the EBA's draft and Article 9(4) in our mark-up below.

We note that Article 6(3a) of the Securitisation Regulation refers to "the exposure's nominal value or, where applicable, its outstanding value at the time of origination" but that this language is not reflected in the EBA's proposals in points 4 or 5 of Article 9. Presumably it is implicit throughout the Regulation that nominal value means outstanding nominal value? Possible amendments to Article 9 to reflect these clarifications are set out below:

Article 9

Application of the retention options ~~on~~ to traditional NPE securitisations

1. In case of NPE securitisations in accordance with Article 6(3a) of Regulation (EU) 2017/2402, points (a) to (e) inclusive of Article 6(3) of Regulation (EU) 2017/2402 and Articles 4 to 8 of this Regulation shall be applied to the share of non-performing exposures in the pool of underlying exposures of a securitisation ~~considering~~ interpreting any reference ~~in relation~~ to the nominal value of the securitised exposures (or each of the securitised exposures) or to the nominal value of the issued tranches (or each of the issued tranches) as a reference to the net value of the non-performing exposures (or each non-performing exposure, as applicable).

2. As indicated in Article 6(3a) of Regulation (EU) 2017/2402, a 'non-refundable purchase price discount' for purposes of Article 2(31) of Regulation (EU) 2017/2402 may:

(a) be agreed at the level of each individual securitised exposure at the time of origination; and/or

(b) be agreed at the level of the pool of underlying exposures at the time of origination; and/or

(c) be the difference between the nominal amount of the tranches of the NPE securitisation underwritten by the originator for subsequent sale and the price at which these tranches are first sold to unrelated third parties.

3. Where a non-refundable purchase price discount is agreed at the level of each individual securitised exposure at the time of origination, the net value of each non-performing exposure shall be calculated by deducting the non-refundable purchase price discount from the exposure's nominal value. [***Note: Article 6(3a) of Regulation (EU) 2017/2402 refers to "the exposure's nominal value or, where applicable, its outstanding value at the time of origination" but this language is not reflected in the EBA's proposals in points 4 or 5 below so is not reflected here. Presumably it is implicit throughout the Draft RTS that nominal value means outstanding nominal value.***]

~~Where Article 6 is applied, the net value of the retained non-performing exposures shall be computed using the same amount of the non-refundable purchase price discount that would be applied had the retained non-performing exposures been securitised.~~

~~3~~4. Where the non-refundable purchase price discount ~~has been~~ is agreed at the level of the pool of underlying non-performing exposures as referred to in Article 6(3a) second subparagraph of Regulation (EU) 2017/2402, or this Article 9(2)(c), the net value of individual securitised non-performing exposures shall be calculated by applying a corresponding share of the non-refundable purchase price discount to each of the non-performing securitised exposures in proportion to their nominal value.

~~4~~5. Where the non-refundable purchase price discount includes the difference between the nominal amount of one tranche or several tranches of an NPE securitisation underwritten by the originator for subsequent sale and the price at which this tranche or these tranches are first sold to unrelated third parties as referred to in Article 6(3a) second subparagraph of Regulation (EU) 2017/2402, that difference shall be taken into account in the calculation of the net value of individual securitised non-performing exposures by applying a corresponding share of the difference to each of the non-performing securitised exposures in proportion to their nominal value.

6. Where Article 4(a), Article 5 or Article 6 ~~is applied~~s, the net value of the retained non-performing exposures, or retained portion of each non-performing exposure, shall be computed using the same amount of the non-refundable purchase price discount (which may be established by any of the methods referred to in Article 9(2) of this Regulation) that would be applied had the retained non-performing exposures, or retained portion of each non-performing exposure, been securitised.

B. Retention by multiple servicers to be proportional to the securitised exposures serviced

Where a transaction involves multiple servicers and retention is fulfilled by each servicer in accordance with Article 2(6)(b) of the Draft RTS (rather than being fulfilled by the servicer with the predominant economic interest in the successful workout in accordance with Article 2(6)(a) of the Draft RTS), the retention should be proportional to the securitised exposures serviced rather than to the number of servicers.

Possible amendments to Article 2(6)(b) to this effect are set out below:

> 6. Where multiple servicers fulfil the retention requirement, it shall be fulfilled by either:
>
> (a) the servicer with the predominant economic interest in the successful workout of the exposures of the traditional NPE securitisations, as agreed by the multiple servicers on the basis of objective criteria including, inter alia, the transaction's fee structure and the servicer's available resources and expertise to manage the exposures' workout process;
>
> (b) each servicer on a pro rata basis by reference to the securitised exposures for which it is the ~~proportionately to the number~~ servicer~~of servicers~~ (using the nominal value of securitised performing exposures and net value (calculated in accordance with Article 9 of this Regulation) of the securitised non-performing exposures for purpose of this calculation).

C. Servicer as retainer and termination of servicer's appointment

Where a servicer acts as a retainer, it would be helpful to preserve flexibility so that upon termination the outgoing servicer-retainer can continue being eligible to retain (this appears important to the initial symmetry of interests of the servicer-retainer and investors), but also, in light of the policy objective of aligning the interests of the sell-side parties with the interests of the investors in securitisations (to better protect the investors), to expressly permit the retained interest to be transferred to a new replacement servicer, or other eligible retainer, at the option of the securitisation's investors.

Therefore, it would be helpful to clarify (though this is the implication of the current and proposed operative provisions of the Securitisation Regulation and the Draft RTS) that the servicer-retainer remains eligible notwithstanding termination of its appointment as servicer. Not permitting continued retention by a terminated servicer, and requiring assumption of the retention by the new servicer, could result in issues identifying replacement servicers (whose estimates and valuations of the expected NPE portfolio collections and performance could differ, including due to the passing of time since closing). The same logic appears relevant to other categories of retainer whose eligibility flows from contractual appointment by the securitisation (such as sponsors falling within Article 2(5)(a) of the Securitisation Regulation by virtue of their appointment to manage an ABCP programme or other securitisation that purchases exposures from third-party entities). The amendments, indicated below, to draft Article 2(1)(d), would clarify this position (alternative drafting suggestions are provided: (i) limited to servicer-retainers; and (ii) extending to all categories of retainer whose eligibility flows from contractual appointment by the securitisation; however, we regard the latter as logical and preferable):

Article 2

Retainers of a material net economic interest

1. The requirement that the retained material net economic interest shall not be split amongst different types of retainers under Article 6(1) of Regulation (EU) 2017/2402 shall mean that it shall be fulfilled in full by any of the following:

(a) the originator or multiple originators;

(b) the sponsor or multiple sponsors;

(c) the original lender or multiple original lenders;

(d) the servicer or servicers in a traditional NPE securitisation, provided that they meet the requirement on expertise set out in Article 19.

[Without prejudice to Article 12(4) below, where a servicer acts as a retainer in accordance with Article 6 of Regulation (EU) 2017/2402 and this Delegated Regulation, it shall remain eligible as a retainer notwithstanding termination of its appointment as servicer.] OR (and preferably): [Without prejudice to Article 12(4) below, where a retainer is eligible in accordance with Article 6 of Regulation (EU) 2017/2402 and this Delegated Regulation by virtue of its contractual appointment by the securitisation, it shall remain eligible as a retainer notwithstanding termination of that appointment.]

In addition, and as envisaged by proposed Recital 10 to the Draft RTS, which indicates that "*[w]here insolvency proceedings have been commenced in respect of the retainer or the retainer is unable to continue acting in that capacity for reasons beyond its control or the control of its shareholders, it should be possible for the remaining retained material net economic interest to be retained by another legal entity complying with Article 6 of Regulation (EU) 2017/2402 and this Regulation*", an operative provision should be included to facilitate transfer of the retention to a replacement servicer or servicers, ensuring that such provision accommodates servicer replacement triggers unrelated to insolvency. The same logic appears relevant to other categories of retainer whose eligibility flows from contractual appointment by the securitisation (such as sponsors falling within the Article 2(5)(a) of the Securitisation Regulation by virtue of their appointment to manage an ABCP programme or other securitisation that purchases exposures from third-party entities). Possible drafting for a new Article 12(4) to this effect is set out below (alternative drafting suggestions are provided: (i) limited to servicer-retainers; and (ii) extending to all categories of retainer whose eligibility flows from contractual appointment by the securitisation; however, we regard the latter as logical and preferable):

4. The condition of paragraph 1(b) shall not apply in relation to the sale, transfer or surrender by [a servicer retainer that ceases to act as servicer in relation to the securitisation] OR (and preferably): [a retainer eligible in accordance with Article 6 of Regulation (EU) 2017/2402 and this Delegated Regulation by virtue of its contractual appointment by the securitisation, which ceases to be so appointed,] of all or part of the rights, benefits or obligations arising from its remaining retained net economic interest to a new retainer or retainers of a kind eligible under Article 6 of Regulation (EU) 2017/2402 and this Regulation, [at the request/with the approval] of the securitisation's investors.

Irrespective of the EBA's conclusions/position on this point, the implications, for risk retention, of replacement of a servicer-retainer should be clarified to avoid confusion.

We also refer the EBA to the additional comments raised more generally on the replacement of the retainer provisions in Article 12(3) discussed in more detail in response to Question 8 below.

Question 2: Do you agree with the provisions with respect to the synthetic excess spread [Article 10]? Are there any aspects relating to the synthetic excess spread being considered in the measurement of the material net economic interest that should be clarified in these RTS, taking into account that separate RTS will be developed that will determine the exposure value of the synthetic excess spread?

A. New SES Capital Charge: economically punitive and likely to be minimally impacted by any of the adjustments that might be expected to moderate its effects

AFME members note that the EBA proposes (broadly) to allow an originator retainer to count synthetic excess spread that incurs a capital charge under new Article 248(1)(e) CRR introduced in the capital markets recovery package (the **New SES Capital Charge**) towards satisfaction of the first loss tranche retention option in Article 6(3)(d) of the Securitisation Regulation (**SES-based retention reduction**). We appreciate the intention and the logic behind this proposal, but note that, as indicated in data shared separately by members with the EBA, the New SES Capital Charge is economically punitive and, in practice, likely to be minimally impacted by SES-based retention, or, indeed, by the other adjustments that might be expected to moderate its effects: on-balance sheet STS and the adjustment of the attachment and detachment points of the originator's other retained tranches under Article 256(6) CRR (**A/D Adjustment**).

In practice, the majority of transactions including synthetic excess spread make use of the full deduction option in which the originator applies a CET1 deduction or 1 250% risk weight to all retained tranches in the securitisation under Article 245(1)(b) CRR, rather than demonstrating the transfer of significant credit risk associated with the underlying exposures under Article 245(1)(a) CRR. That is, the originator holds sufficient capital to absorb losses of 100% on the exposures to the underlying portfolio that it retains. This is a practical and prudent response to the complexity of, and timing implications associated with, quantitative significant risk transfer assessments, especially for newer market entrants and/or for jurisdictions where regulators are, themselves, less familiar with significant risk transfer. In this context, the risk weight reduction available to retained senior tranches in securitisations that meet the criteria for the on-balance sheet STS designation is irrelevant to the originator (the tranche must nevertheless be deducted/1 250% risk weighted). Similarly, in this context, the risk weight reduction available to retained tranches flowing from A/D Adjustment is irrelevant to the originator (the tranche must nevertheless be deducted/1 250% risk weighted).

The proposed SES-based retention reduction is likely to be economically unattractive. In relation to transactions that seek to demonstrate transfer of significant credit risk associated with the underlying exposures under Article 245(1)(a) CRR, this is because the originator must demonstrate that it retains less than specified amounts of mezzanine securitisation positions or first loss securitisation positions in Article 245(2) CRR.[4] Satisfying the retention requirement (after reduction by the exposure value of the SES) via a first loss tranche makes it virtually impossible for the originator to demonstrate compliance with the required maximum amounts in the first loss test. Similarly, under the full deduction approach, satisfying the retention requirement (after reduction by the exposure value of the SES) via a first loss tranche increases the amount of deductible retained securitisation positions. In both scenarios, even if the applicable regulatory tests could be passed, it is highly unlikely that the resulting structures would be economically viable for the issuer. By contrast, retained assets/portions of assets would be likely to attract lower risk weights.

[4] For the purposes of current Article 245(2) CRR (unlike the new PBA, CRT and first loss thickness tests proposed in the EBA SRT Report which require the exposure equivalent value of excess spread (EEVES) to be reflected as a first loss tranche in allocating EL and UL to tranches), SES is not reflected as a retained first loss tranche.

B. *New SES Capital Charge should count towards (i.e. be deducted from the required material net economic interest for) any form of retention rather than merely the first loss tranche retention option*

Although the SES-based retention reduction would still not meaningfully moderate the economically punitive consequences of the New SES Capital Charge, it would be preferable if the New SES Capital Charge could count towards (i.e. be deducted from the required material net economic interest for) **any** form of retention rather than merely the first loss tranche retention option in Article 6(3)(d) of the Securitisation Regulation. Under this approach, the existence of SES subject to the New SES Capital Charge could, for example, reduce the amount of material net economic interest that an originator is required to retain in the form of randomly selected assets under Article 6(3)(c) of the Securitisation Regulation, or in the form of a percentage share of the nominal value of each of the securitised exposures under Article 6(3)(a) or Article 6(3)(b) of the Securitisation Regulation. Possible drafting to achieve this outcome is set out below. We note that the Securitisation Regulation, itself, is silent about the way(s) in which excess spread should be recognised within the risk retention framework.

C. Clarification required that maturity requirement for SES does not preclude 'use it or lose it' SES (or ideally deletion of this requirement)

We assume that the reference in the proposals to eligible SES being "*continuously available to cover losses from the day of compliance with the retention requirement until the very end of the transaction*" is intended to be satisfied if use it or lose it or trapped excess spread is committed by the originator on an ongoing basis and hence subject to capital requirements. This, however should be clarified, as indicated below.

Importantly – though not within the immediate remit of this RTS – we assume that if SES is structured to be available to absorb losses only when and if the underlying assets have generated sufficient excess spread (as is the case in traditional securitisations), and is hence not a commitment of the originator, then this amount will not be subject to capital requirements (as is the case for traditional excess spread).

Ideally, the quantum of SES that is permitted to count towards the required material net economic interest for risk retention purposes would be fully aligned with the SES exposure value for purposes of the New SES Capital Charge and not subject to additional requirements.

Therefore, we propose that Article 10(1)(d) be amended as follows:

> (d) where the originator acts as the securitisation's retainer ~~and applies the retention option in accordance with Article 6(3)(d) of Regulation (EU) 2017/2402,~~ and ~~where~~ the exposure value of ~~the~~ 'synthetic excess spread' committed by the originator on an ongoing basis (whether use it or lose it or trapped) is subject to capital requirements in accordance with the prudential regulation applicable to the originator, ~~it~~ the originator shall ~~take~~ subtract the exposure value of the 'synthetic excess spread' ~~into account when measuring~~ from the material net economic interest that it would otherwise be required to retain in accordance with any option permitted by Article 6(3) of Regulation (EU) 2017/2402 and this Regulation ~~Article 7 up to the amount of the exposure value that is continuously available from the date of the compliance with the risk retention requirement until the end of the maturity of a synthetic securitisation for covering losses incurred on the securitised exposures~~;

It may be helpful in Article 10(1)(a), in connection with deals that are initially fully retained by the originator and sold to third parties only at a later date (and consistent with Article 6(3)(a) of the Securitisation Regulation which envisages NRPPDs established based on such later third party sales), to add "*the date of sale to unrelated third parties of tranches underwritten by the originator*" to the non-exclusive examples of dates on which securitisation may be deemed to have occurred, so that it reads as follows:

> 1. When measuring the level of retention of the net economic interest, the following criteria shall be applied:
>
> (a) the origination shall be considered as the time at which the exposures' were first securitised, such as the date of the issuance of securities, ~~or~~ the date of the signature of the credit protection agreement, the date of sale to unrelated third parties of tranches underwritten by the originator, or the date of the agreement on a refundable purchase price discount;

Question 3: Do you agree with the provisions set out in this Article 15 on fees payable to the retainer?

The wording of the last paragraph in Article 15(2) is open to interpretation and potentially goes beyond the amendments made in Article 6(1) of the Securitisation Regulation in suggesting that, where fees are guaranteed or payable upfront in any form, they should be deducted from the retained interest, irrespective of whether they have otherwise met the conditions of Article 15(2) and the policy underpinning the approach to fee arrangements in the context of risk retention. That is, the overarching principle for assessment of fee arrangements is articulated in Article 6(1), which requires that "*when measuring the material net economic interest, the retainer shall take into account any fees that may in practice be used to reduce the effective material net economic interest*".

The combination of the potentially extremely broad scope of fees envisaged by proposed Article 15(2) and the proposed restrictions on fees that are guaranteed or payable upfront would make many, otherwise viable, deals un-structurable. However, this outcome is, hopefully, unintentional. Specifically, Article 15(2) appears to encompass fees relating to pre-closing and closing, as well as post-closing, services which are, generally, and appropriately, payable at or around closing, and the amount of which may have been determined in advance of the relevant service being provided. These fees – while arm's length, and appropriate in light of the risks assumed and services provided – may also be substantial. An originator, or its affiliates, may for example act as arranger/joint lead manager/underwriter in relation to the securitisation. Such fees relating to pre-closing and closing services, the amount of which may have been determined in advance of the relevant service being provided, should clearly not be deductible from the recognised risk retention where paid upfront or guaranteed at closing. Purposively, the (effective) prohibition of fees that are guaranteed or payable upfront does not obviously make sense in relation to services (notably transaction structuring, arranging, and underwriting services, but potentially other pre- and/or post- closing services) whose value does not actually depend on the outstanding amount and/or credit quality of the securitised assets over time. The amendments to Article 15(2) set out below would effect this minimal required change, though the EBA might also, helpfully, provide examples/lists of fees that are in/out of scope in Level 3 guidance:

Fees – minimal proposal:

> 2. Arrangements on fees payable to the retainer on a priority basis to remunerate that retainer for services of any kind provided to the securitisation shall only be deemed as complying with the previous paragraph where all of the following conditions are met:
>
> (a) the amount of the fees is set on an arm's length basis having regard to comparable transactions in the market. In the absence of comparable transactions in the relevant market, the set amount may be deemed compliant by reference to fees payable in similar transactions in other markets or by using appropriate valuation metrics, taking into account the type of securitisation and the service being provided; and
>
> (b) the fees are structured as a genuine consideration for the provision of the relevant service and do not create an undue preferential claim in the securitisation cash flows that effectively declines the retained interest faster than the transferred interest.
>
> The condition in this point shall not be considered to be met, ~~where the fees are guaranteed or payable up-front in any form, in full or in part, and~~ where the effective retention amount after deducting the amount of any fees relating to services provided to the securitisation, post-closing, the value of which depends on the outstanding amount and/or credit quality of the securitised exposures over time and which are guaranteed or payable up-front (that is, in advance of the related service being provided)~~such fees~~ is lower than the minimum net economic interest required under the respective retention option in accordance with Article 6(1) of Regulation (EU) 2017/2402.

Recital 6 could also be helpfully amended, as indicated below, to provide examples of services not intended to be captured by the restriction on upfront/guaranteed fees (the language in square brackets to be included only if the restrictions on guaranteed/up-front fees are retained):

> (6) In order to ensure the ongoing retention of the material net economic interest, retainers should ensure that there is no embedded mechanism in the securitisation structure by which the retained material net economic interest measured at origination would necessarily decline faster than the interest transferred. Similarly, the retained material net economic interest should not be prioritised in terms of cash flows to preferentially benefit from being repaid or amortised such that it would fall below 5 % of the ongoing nominal value of the tranches sold or transferred to investors or the exposures securitised, or the 5 % net value in the case of non-performing exposures of traditional NPE securitisations. Moreover, the credit enhancement provided to the investor assuming exposure to a securitisation position should not decline disproportionately to the rate of repayment on the underlying exposures. This should not prevent the retainer from being remunerated on a priority basis for services rendered to the securitisation's special purpose entity (as is typical for many such services, including structuring, arranging and underwriting services, as well as asset servicing and credit enhancement-related services, because the provision of those services is essential for the transaction to take place), provided that the remuneration's amount is set on an arm's length basis and the structure of such remuneration does not undermine the retention requirement. [In satisfying this requirement, this Regulation imposes specific requirements for fees that are guaranteed, or payable, up-front (that is, in advance of the related service being provided) in respect of services rendered to the securitisation's special purpose entity, post-closing, the value of which depends on the outstanding amount and/or credit quality of the securitised exposures over time. These requirements are not relevant to services associated with the establishment of the securitisation, such as structuring, arranging and underwriting services.][***Note bracketed wording to be included only if restrictions relating to guaranteed/upfront fees are retained***]

Rather than implementing the limited amendments above, however, it is our strong view that the proposed prescriptive and inflexible: (i) restrictions on fees that are guaranteed or payable upfront, and (ii) requirements in relation to the meaning of the term "arm's length", should be deleted altogether. The current proposals are vague, unhelpful, and would introduce significant uncertainty (for example, the meaning of the phrase "*undue preferential claim*" is unclear and open to interpretation). Instead, the EBA should have faith in (i) the arm's-length concept, which is widely employed, and well understood, in contract and legal interpretation; and (ii) the clear statement of principle in Article 15(1) to the effect that: "*There shall be no arrangements or embedded mechanisms in the securitisation by virtue of which the retained interest at origination would decline faster than the interest transferred.*" Fees that are

arm's-length (on the ordinary meaning of the words) – and therefore not designed to undermine the risk retention – should have no impact on the level of retention required. On this basis, Article 15 could be redrafted as follows:

Fees – preferred proposal:

Article 15

Requirements on the allocation of cash flows and losses to the retained interest and on fees payable to the retainer

1. There shall be no arrangements or embedded mechanisms in the securitisation by virtue of which the retained interest at origination would decline faster than the interest transferred. The retained interest shall not be prioritised in the allocation of cash flows to preferentially benefit from being repaid or amortised ahead of the transferred interest. The amortisation of the retained interest via cash flow allocation or through the allocation of losses that, in effect, reduce the level of retention over time shall not be deemed as a breach of the criteria set out in this paragraph.

2. Arrangements on fees payable to the retainer on a priority basis to remunerate that retainer for services of any kind provided to the securitisation shall only be deemed as complying with the previous paragraph where ~~all of the following conditions are met:~~

~~(a)~~ the amount of the fees for the relevant service is set on an arm's length basis. ~~having regard to comparable transactions in the market. In the absence of comparable transactions in the relevant market, the set amount may be deemed compliant by reference to fees payable in similar transactions in other markets or by using appropriate valuation metrics, taking into account the type of securitisation and the service being provided; and~~

~~(b) the fees are structured as a genuine consideration for the provision of the relevant service and do not create an undue preferential claim in the securitisation cash flows that effectively declines the retained interest faster than the transferred interest.~~

~~The condition in this point shall not be considered to be met, where the fees are guaranteed or payable up-front in any form, in full or in part, and where the effective retention amount after deducting such fees is lower than the minimum net economic interest required under the respective retention option in accordance with Article 6(1) of Regulation (EU) 2017/2402.~~

We note that servicing fees are invariably paid in priority: this is required by investors and rating agencies in order to ensure that servicers are sufficiently remunerated and incentivised to provide the best service and maximise collections. Priority payment is also the norm for operating expenses which are necessary to ensure the proper operational functioning of the SSPE, such as those associated with: management companies, custodians, account banks, representatives of the noteholders, paying agents, and listing agents. Clarity of the contemplated scope of services would be welcome, as would be a recognition that it is usual for such service providers to be paid at top of the priorities of payment.

Question 4: Do you agree with the provisions with respect to securitisations of own issued debt instruments [Article 16]?

Article 16 uses the term "issuer" which is not defined in the Securitisation Regulation or the Draft RTS. The term "issuer" can be understood to mean the SSPE, but an SSPE will not be securitising its own liabilities. We propose to use instead relevant terms as defined in the Securitisation Regulation. In this case, "issuer" references should be replaced with references to "originator" and "original lender", so that the amended Article 16 would read as follows:

> **Article 16**
>
> **Fulfilment of the retention requirement in securitisations of own issued debt instruments**
>
> Where a securitisation is backed by a pool of underlying exposures comprised exclusively of own debt instruments issued by the original lender or originator~~issuer~~ or multiple original lenders or originators~~issuers~~ of the securitisation, the retention requirement in Article 6(1) of Regulation (EU) 2017/2402 shall be considered as complied with. The debt instruments referred to in this Article shall include covered bonds as defined in Article 3(1) of Directive (EU) 2019/2162.

In addition, the proposed wording in new Recital 7 should be deleted and replaced with the wording set out in Recital 1 to the pre-2019 CRR retention RTS that apply currently under the transitional provisions of the Securitisation Regulation (which Recital wording was also included in the EBA earlier draft RTS of July 2018).[5] We think that the original wording more clearly articulates the high-level principles for this exemption. Therefore, we propose to amend Recital 7 as follows:

> (7) Where an entity exclusively securitses assets consisting of own liabilities, alignment of interests is established automatically for that securitisation. Where it is clear that the credit risk remains with the originator, the retention of interest by the originiator is unnecessary and would not improve on the pre-existing position. ~~Without prejudice to the exception laid out in point (c) of Article 6(5) of Regulation (EU) 2017/2402, the retention requirement should be deemed as duly complied with in securitisations backed by exposures of such nature that the credit risk is fully retained by the relevant sell-side party. For instance, where the issuer of a securitisation securitises a pool of exposures exclusively comprising the issuer's own covered bonds or similar own debt instruments, the issuer of the securitisation has full alignment of interest as principal obligor of the covered bonds or other debt instruments and, as a result, should not be obliged to take any further action to comply with the risk retention requirement.~~

[5] https://www.eba.europa.eu/regulation-and-policy/securitisation-and-covered-bonds/rts-on-risk-retention

Question 5: Do you agree with the provisions with respect to resecuritisations [Article 17]?

No comments.

Question 6: Do you agree with the provisions in this Article 18 with respect to assets transferred to SSPE? Are there any additional aspects that should be further specified in these RTS, taking into account that no clarification is provided with respect to Recital 11 of the Securitisation Regulation (for example, do you see any specific implications for the securitisations of NPE securitisations and how these should be tackled)?

New Article 18(3) is helpful, but does not cater for scenarios in which, for example, the originator holds assets for multiple securitisations concurrently. The amendment below would address this issue.

> 3. Article 6(2) of Regulation (EU) 2017/2402 shall be deemed complied with where, after the securitisation, there are no exposures left on the originator's balance sheet that are comparable to the securitised exposures (other than exposures which the originator is committed to securitise) and where the fact that no comparable assets (other than exposures which the originator is committed to securitise) remain on the balance sheet of the originator is being clearly communicated to investors.

Question 7: Do you agree with the provisions set out in this Article 19 with respect to expertise of the servicer of a traditional NPE securitisation?

No comments.

Question 8: Do you have any comments on the remaining Articles of these draft RTS?

AFME members have identified a number of general comments on the revised draft technical standards. These comments are set out below.

A. Sole purpose test – Article 2(7)

AFME members support the principles-based approach applied to the "sole purpose test" guidance under Article 2(7) of the Draft RTS. It is essential that such guidance can be interpreted sufficiently flexibly so as to allow for appropriate application across the full range of scenarios that may arise, including in the context of existing securitisations in-scope of the Securitisation Regulation that had to comply with the sole purpose test post-1 January 2019 under the transitional provisions and in the absence of the finalised recast retention RTS having to refer, in the first instance, to Article 6(1) of the Securitisation Regulation, the EBA's final report on the earlier version of the draft RTS of July 2018[6] and related background materials on the policy behind this test, including the EBA's report of December 2014.[7]

AFME members note that the EBA's approach continues to be focused on high-level principles (by broadly being substantially similar to the wording of the earlier version of the draft RTS of July 2018). We understand that the changes made are not intended to tighten or to broaden the sole purpose test parameters provided in the earlier EBA draft of July 2018, which AFME members support. However,

[6] https://www.eba.europa.eu/regulation-and-policy/securitisation-and-covered-bonds/rts-on-risk-retention
[7] https://www.eba.europa.eu/sites/default/documents/files/documents/10180/534414/b152ba27-9a02-4d82-82a0-e05c8123a7df/Securitisation%20Risk%20Retention%20Report.pdf?retry=1

we believe that further improvements could be made to the drafting of the guidance in order to: (i) further clarify that the sole purpose test requires appropriate consideration being given to the relevant principles (i.e. it does not mean that each of the identified principles is given equal weight and fully satisfied in all circumstances); and (ii) more closely track the wording of Article 6(1) of the Securitisation Regulation itself. These improvements will assist with legal certainty, as the current wording is potentially open to interpretation (including a presumably unintentional interpretation which, if followed, would be inconsistent with the text of Article 6(1) of the Securitisation Regulation).

We believe that a minor amendment to the introductory paragraph of Article 2(7) of the Draft RTS and the deletion of the words "or predominant", as set out below, could achieve this. This will ensure clarity that the interpretation of the guidance should not result in the effective replacement of the test in Article 6(1) of the Securitisation Regulation with a more rigid test. The amended wording makes it clear that each of the principles should be taken into account when assessing whether the sole purpose test is satisfied and allows for adjustments in weighting through the reference to "*appropriate consideration*". Such adjustments may be required, for example, where the relevant entity has been established relatively recently and it is intended to operate for purposes consistent with a broader business purpose but it is not possible to point to a material operating history at the time of closing.

AFME members consider the suggested amendments (as per the mark-up of Article 2(7) set out below) to be necessary for sensible application of the guidance, and to ensure that the sole purpose test set out in Article 6(1) of the Securitisation Regulation is not effectively replaced by another test in Article 2(7) of the Draft RTS. Moreover, the revised wording should function to deliver appropriate outcomes under the retention requirements from a policy perspective.

7. For the purposes of assessing whether an entity has been established or operates for the sole purpose of securitising exposures as referred to in the first subparagraph of Article 6(1) of Regulation (EU) 2017/2402, appropriate consideration should be given to the following principles ~~shall be taken into account~~:

(a) the entity has a strategy and the capacity to meet payment obligations consistent with a broader business model that involves material support from capital, assets, fees or other sources of income, by virtue of which the entity does not rely on the exposures to be securitised, on any interests retained or proposed to be retained in accordance with this Regulation or on any corresponding income from such exposures and interests as its sole ~~or predominant~~ source of revenue;

(b) the responsible decision makers have the necessary experience to enable the entity to pursue the established business strategy, as well as adequate corporate governance arrangements.

B. Recital 8 and retention in the context of ABCP programmes

We refer to Recital 8 of the Draft RTS and, in particular, to the following sentence included in Recital 8: "*The same requirement should apply to transactions within multiple underlying securitisations, such as ABCP programme.*"

The application of the risk retention requirements to ABCP programmes is highly fact-pattern specific. Some AFME members have raised concerns that this sentence is unnecessary, as it is open to interpretation.. We would therefore ask the EBA to delete that sentence in Recital 8.

C. Prohibition on selling the retained interest – Article 12(3) should track the wording of Recital (10) more closely

Recital (10) helpfully clarifies that it is possible to change the retainer (i) where insolvency proceedings have been commenced in respect of the retainer; or (ii) the retainer is unable to continue acting in that capacity for reasons beyond its control or the control of its shareholders. However, limb (ii) of the recital wording is missing from Article 12(3). Therefore, we propose to amend Article 12(3) as follows to track the wording of Recital (10) more closely:

> 3. The condition of paragraph 1(b) shall not apply in the event of the insolvency of the retainer or in the event the retainer is unable to continue acting in that capacity for reasons beyond its control or the control of its shareholders.

If this change is made, new Article 12(4) (as requested above) is less critical, although its inclusion would still provide welcome clarity.

D. Vertical retention in accordance with Article 6(3)(a) – Article 4(a) should reinstate the guidance on revolving securitisations previously included in the pre-2019 retention RTS and in the EBA draft RTS of July 2018 in order to ensure legal certainty for existing securitisations

We note that amendments made to Article 4(a) removed guidance on revolving securitisations and retention of the originator's interest that exists under Regulation (EU) No 625/2014 (which applies during the transitional period) and that was previously included by the EBA in its earlier draft RTS of July 2018. It should be noted that this guidance is relied on by certain revolving securitisations (e.g. master trust transactions) and its removal potentially impacts on legal certainty, as the rationale for its omission is unclear. We assume that the removal of the additional wording is not an indication that previous guidance is no longer relevant, but an indication that the same conclusion could be reached by applying the general principles already provided for in Article 4(a). However, for purposes of legal certainty on existing securitisations that rely on this guidance, it would be helpful to reinstate the wording previously used, i.e. Article 4(a) should read instead as follows:

> (a) The retention of not less than 5 % of the nominal value of each of the securitised exposures, provided that the retained credit risk ranks pari passu with or is subordinated to the credit risk securitised in relation to the same exposures. In the case of a revolving securitisation, as defined in Article 2(16) of Regulation (EU) 2017/2402, this may be achieved through retention of the originator's interest provided that such originator's interest was for at least 5% of the nominal value of the securitised exposures and ranked pari passu with or subordinated to the credit risk that has been securitised with respect to those same exposures;

E. Cash collateralisation of synthetic/contingent risk retention for non-credit institutions – Article 3(2)

AFME members consider that the requirement in Article 3(2) for the cash collateralisation of synthetic and contingent forms of risk retention when held by entities other than credit institutions (whereas credit institutions can hold synthetic/contingent retentions on an unfunded basis) is disproportionate, unduly restrictive and creates an un-level playing field.

The Securitisation Regulation (unlike the CRR in which the risk retention requirement was originally housed) is a cross-sectoral regulation. In this context, and to provide a level playing field under this Capital Markets Union-based regulation, exclusion from the collateralisation requirement should cover all entities that, if they acted as investors, would qualify as "*institutional investors*" within the meaning of Article 2(12) of the Securitisation Regulation (such as investment firms, regulated (re)-insurers, and asset managers subject to the AIFMD). The exclusion should also cover entities that would be eligible providers of unfunded credit protection under limbs (a) to (e) inclusive of Article 201(1) CRR (broadly

public sector bodies). Without the latter exemption, EU sovereigns, public sector entities etc. are required to collateralise any contingent/synthetic retention that they hold.

In relation to entities that would not, if acting as investors, qualify as "*institutional investors*" within the meaning of Article 2(12) of the Securitisation Regulation, or as eligible providers of unfunded credit protection within the meaning of Article 201(1)(a)-(e) CRR, forms of collateral, other than cash, should be permitted where their fair market value is maintained in an amount equal to the retained material net economic interest. The proposed amendments to Article 3(2) are set out in the mark-up below:

> 2. Where an entity is of a type that would qualify neither as an eligible provider of unfunded credit protection within the meaning of Article 201(1)(a)-(e) inclusive (if providing credit protection) ~~other than a credit institution as defined in Article 4(1) point (1)~~ of Regulation (EU) No 575/2013 nor as an "*institutional investor*" within the meaning of Article 2(12) of the Securitisation Regulation (if investing in a securitisation), and retains an economic interest through a synthetic or contingent form of retention, the retained interest shall be fully collateralised ~~in cash~~ and held under arrangements as referred to in Article 16(9) of Directive 2014/65/EU9[4]. The estimated fair value of the collateral shall be, at all times, greater than or equal to the retained material net economic interest.

F. Consolidated application – clarification for entities other than relevant credit institutions

The Securitisation Regulation (unlike the CRR (and its predecessor CRD2) from which the risk retention requirements originate) is a cross-sectoral regulation. Ability to fulfil the risk retention on a consolidated basis under Article 6(4) of the Securitisation Regulation should also apply to sponsors, originators or original lenders other than credit institutions (as was explicitly stated in paragraph 71 of the CEBS Guidelines to CRD2 Article 122a)[8] and should apply whether or not such entities are established in the EU. This issue should be considered as part of the wider review of the Securitisation Regulation and we would welcome further engagement with the EBA on this and related topics.

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[8] See: https://www.eba.europa.eu/sites/default/documents/files/documents/10180/106202/e6774413-7668-49d9-9869-938fd9f1b3fb/Guidelines.pdf. Paragraph 71 provides that: "The ability to fulfil the requirements of Paragraph 1 on a consolidated basis should also apply to originators or original lenders other than credit institutions. In the former case, in particular, this is supported by the definition of an originator under the Directive (as provided in clause 24 above) as an entity that "either itself or through related entities, directly or indirectly" was involved in the creation of the obligations that give rise to the exposures being securitised."