

14 March 2018

SUBMITTED VIA

[www.eba.eu](http://www.eba.eu)

European Banking Authority  
One Canada Square  
Floor 46  
London E14 5AA

**RE: EBA Consultation Paper on Draft Regulatory Technical Standards on Homogeneity of Underlying Exposures in Securitisation**

**1. Do you agree with the focus of the RTS, general approach and underlying assumptions on which the RTS are based? Does the proposed approach provide sufficient clarity and certainty on the interpretation and application of the criterion of homogeneity?**

AFME members agree in general with the principles underlying the Draft RTS and, in particular, with the focus on simplifying and facilitating the assessment of underlying risks with respect to the securitised exposures by investors. We further agree with and would emphasise the importance of the principles laid out in recitals (2) and (3) of the Draft RTS relating to:

- avoiding interference with other requirements of securitisations in general and STS securitisations in particular;
- avoiding unnecessary limitations of the market; and
- ensuring the homogeneity requirement does not provide incentives that would prevent the originator from structuring a diversified portfolio or lead to excessive concentrations.

That said, it is extremely important that the final RTS makes clear that the criteria (and in particular the risk factors) can be applied and analysed flexibly and in a manner appropriate to the particular transaction. The focus on the application of the criteria and risk factors leading to "similar risk profiles and cash flow characteristics within the respective asset category, enabling the investor to assess the underlying risks on the basis of common methodologies and parameters" is appropriate and helpful in this respect.

Some AFME members have expressed significant concerns around the lack of detailed guidance for determining when risk factors are relevant in respect of a particular

**Association for Financial Markets in Europe**

**London Office:** 39<sup>th</sup> Floor, 25 Canada Square, London E14 5LQ, United Kingdom T: +44 (0)20 3828 2700

**Brussels Office:** Rue de la Loi 82, 1040 Brussels, Belgium T: +32 (0)2 788 3971

**Frankfurt Office:** Skyper Villa, Taunusanlage 1, 60329 Frankfurt am Main, Germany T: +49 (0)69 5050 60590

[www.afme.eu](http://www.afme.eu)

portfolio and – as a consequence – that certain common, well-established types of transactions considered "homogeneous" in local markets (and for the purposes of ECB collateral eligibility) may be excluded from the STS categorisation. This is, in particular, true of transactions with common credit facility types and obligor types but where there may be variations in the presence or absence of collateral or in the object of the financing. Where such transactions are homogeneous in terms of underwriting and servicing, and the risk profiles and cash flows can be assessed using common methodologies and parameters, such AFME members fully expect to be able to conclude that the pool is homogeneous within the meaning of the Securitisation Regulation, but this would be assisted by further guidance (in the RTS or, failing that, in the form of a Q&A) around the situations where it is appropriate to deem a risk factor irrelevant.

**2. Do you agree with the assessment of the homogeneity of underlying exposures based on criteria specified under (a) to (d)? Should other criteria be added or should any of the criteria be disregarded?**

AFME members agree in general with the criteria specified under (a) to (d). As mentioned above, the overriding guiding principle of ensuring "similar risk profiles and cash flow characteristics within the respective asset category, enabling the investor to assess the underlying risks on the basis of common methodologies and parameters" is appropriate. That said, it is essential that market participants be in a position to conclude with sufficient certainty that their portfolios are homogeneous (and therefore can be STS). To that end, we would ask the EBA to amend the list of criteria to make clear that it is an exhaustive list and to make certain modifications to the drafting of Article 1 of the Draft RTS more generally. Our suggested amendments appear below.

Furthermore, it is important that the requirement for "similar underwriting standards" in criterion (a) is interpreted to refer to underwriting standards designed to measure similar types of risks in the overall credit assessment, rather than the same underwriting criteria precisely. This is necessary to allow appropriate diversification of pools and to avoid preventing similar pools originated separately from being part of the same securitisation (e.g. for mortgages originated at a different time or by a different lender whose assets have been acquired). Equally, different vintages (of long-dated assets in particular) will inevitably have been originated based on slightly different underwriting standards as a result of the normal evolution of these standards and their adaptation to the then-prevailing economic climate. The requirement for "similar" underwriting standards should not be interpreted so rigidly as cause these incremental changes in underwriting standards to result in a non-homogeneous pool. In addition, the level of similarity required should be determined in part by the relationship of the investor or investors to the underlying assets; for example, an ABCP sponsor will have a different relationship to underlying assets than a third party investor in a term securitisation. See our answer to Question 5 below.

As with criterion (a), it is necessary that criterion (b) with respect to the requirement for "uniform" servicing procedures be interpreted flexibly. Small variations should be permitted provided the servicing procedures are still sufficiently similar as to "enable the investor to assess the cash flows generated by the underlying exposures on the basis of a common methodology". For example, where multiple servicers are servicing assets according to the same or similar servicing standards, there will inevitably be some variation. Consequently, we would suggest the criterion should be that servicing procedures are "similar" rather than "uniform".

Flexibility in respect of both criterion (a) and criterion (b) are both important as a practical matter for ensuring that pools can reach critical mass to be securitised, as it is sometimes necessary to group together different vintages and assets from different original lenders in order to achieve that critical mass.

On a more technical note, homogeneity is to do with the characteristics of the underlying asset pool, and not to do with the way the cash produced by that pool is allocated on the liabilities side of the securitisation structure. There are other STS criteria that impose various requirements to do with the liabilities side of administration and allocation of cash, the structuring of the waterfalls and disclosure of both that waterfall and the cash flow model.<sup>1</sup> It is therefore appropriate to specify that requirements related to the administration and allocation of cash receivables should refer to the asset side of the transaction only and not to the liabilities side.

The specific changes to the drafting we would suggest in Article 1 of the Draft RTS to deal with the above concerns (and the concerns expressed below in relation to the risk factors below in our answer to Question 8) are as follows:

"The underlying exposures in both a non-ABCP STS securitisation referred to in Article 20(8) of [the Regulation (EU) No ~~XXX/201X~~ **2017/2402**] and an ABCP STS securitisation referred to in Article 24(15) of that Regulation shall be ~~deemed~~ **considered** to be homogeneous where they have similar **overall** risk profiles and cash flow characteristics, enabling the investor to assess the underlying risks on the basis of common methodologies and parameters, ~~and more in particular~~ **Therefore**, where all of the following conditions are met **to the extent required to permit an investor to assess the underlying risks on the basis of common methodologies and parameters, then an asset pool shall be deemed to be homogeneous:**

- (a) the underlying exposures have been underwritten according to similar underwriting standards, methods and criteria;
- (b) the underlying exposures are serviced according to ~~uniform~~ **similar** servicing procedures with respect to monitoring, **and** collection;

---

<sup>1</sup> Cf. Securitisation Regulation Arts. 7(1)(b), 7(1)(c), 21(4), 21(5), 21(6) and 22(3).

~~administration and allocation~~ of cash receivables **as well as their asset-side administration and allocation**, which enable the investor to assess the cash flows generated by the underlying exposures on the basis of a common methodology;

(c) the underlying exposures all fall within the same asset category;

(d) the underlying exposures take into account the ~~relevant~~ risk factors **deemed relevant in the reasonable judgment of the originator, sponsor and issuer**, from among those that need to be considered for each asset category in accordance with Article 3, and at least one.

A risk factor shall be deemed to be relevant where, taking into account the asset category, the type of securitisation and the specific characteristics of the particular pool of underlying exposures, it results in all of the underlying exposures exhibiting similar **types (but not necessarily similar degrees) of credit and cash flow risks** ~~risk profiles and cash flow characteristics~~ within the respective asset category, enabling the investor to assess the underlying risks on the basis of common methodologies and parameters."

**3. Are there any impediments or practical implications of the criteria as defined? Are there any important and severe unintended consequences of the application of the criteria?**

See our answer to Question 1. The criteria themselves (subject to our comments above) are sufficiently broad and general as to be sensible. Flexibility in their application and appropriate recognition for the significant subjective judgments required are important (as noted in more detail elsewhere in this response) in order to achieve the laudable and correct principles set out in recitals (2) and (3).

**4. Do you agree that when considering the relevance of the risk factors, the asset category, type of securitisation (non-ABPC or ABCP), and specific characteristics of the pool of exposures, should be taken into account? Should other elements be considered as important determinants of the relevance of the individual risk factors?**

Yes. As the consultation outlines, different factors will be relevant in determining homogeneity for pools. It is helpful to have a limited range of risk factors to be considered based on asset categories and the ability to further limit the relevant risk factors on a reasoned and disclosed pool-by-pool basis.

**5. Do you agree that the same set of criteria should be applied to non-ABCP and ABCP securitisation? Or do you instead consider that additional differentiation**

**should be made between criteria applicable to non-ABCP and ABCP securitisation, and if so, which criteria?**

AFME members believe it should only be necessary to apply criteria in Article 1(a) to (c) in respect of ABCP transactions. The application of risk factors is not appropriate in the case of ABCP transactions.

In the case of an STS ABCP transaction, the only investor with direct exposure to the pool is the sponsor of the transaction who is providing liquidity support. All other investors are primarily exposed to the credit of the sponsor and will anyway be exposed to a non-homogeneous pool because the homogeneity requirement exists only at the transaction level (Article 24(15) has no equivalent in Article 26). It is irrelevant to an investor in the ABCP whether the non-homogeneity to which they are exposed derives from non-homogeneity of individual transactions as opposed to the inclusion of various internally-homogeneous transactions in an ABCP programme.

The originators of transactions in ABCP transactions will typically be clients of the sponsor institution, whose business plans, risk-profiles and receivables are well-known to the sponsor institution. The sponsor institution will necessarily be a credit institution or investment firm that has completed extensive due diligence and credit underwriting as it is required to do under its prudential regulation, meaning it is better able to model the risks associated with different assets in a pool than an external investor in a term securitisation would typically be. While the homogeneity requirements are drafted very similarly in Articles 20(8) and 24(15) of the securitisation regulation, we would submit that a purposive interpretation of this text requires the EBA to apply a more flexible approach to homogeneity for ABCP transactions given the only investor with real exposure to the assets is in far better position to assess the risk profiles and cash flow characteristics of the underlying assets than a typical investor in a non-ABCP securitisation. Consequently, it should only be necessary to segregate transactions based on asset category and, to the extent necessary to permit assessment of risks based on common methodologies and parameters, similar underwriting and servicing.

We would note, in addition, that the relevant features (a single external risk-taker who is a heavily-regulated financial institution) will mainly arise in ABCP transactions but are not exclusive to ABCP transactions. This more flexible approach to homogeneity could therefore appropriately be extended to other private securitisations with the same features.

- 6. Do you agree with providing a list of asset categories in the RTS? Do you agree with the asset categories listed? Should other asset categories be included or some categories be merged? For example, should separate asset categories of project finance, object finance, commodities finance, leasing receivables, dealer floor plan finance, corporate trade receivables, retail trade receivables, credit facilities to**

**SMEs and credit facilities to corporates, be included? Please substantiate your reasoning.**

AFME members agree a non-exhaustive list of categories should be provided as a "safe harbour" to demonstrate that all assets in a pool are of the same asset category. Although it is clear from the text of the CP and from recital (9) of the Draft RTS that this list is intended to be non-exhaustive, it would be helpful if that approach were reflected in the operative legislative text of Article 2. Accordingly, we would suggest amending the opening words of Article 2 to read as follows:

The types of pools considered to form one asset category for the purposes of Article 1(c) shall include, but are not limited to:

Furthermore, it is helpful and appropriate that the asset categories are broadly drawn, with the risk factor approach used to ensure that asset pools within those categories are homogeneous. It would be inappropriate to distinguish e.g. consumer auto loans from consumer auto leases in a blanket fashion.

In this vein, we do not think separating out e.g. corporate trade receivables from retail trade receivables at the asset category level is necessary or appropriate. Likewise, it is appropriate to combine all business loans in one asset category. These categories are not a guarantee of homogeneity on their own and they are not intended to be. The risk factors are adequate (in combination with broad asset categories) to ensure homogeneity.

Finally, we believe that dealer floorplan finance should be added to the list of asset categories. Although the underlying transactions might technically be corporate loans, the way in which such loans are originated and serviced is very different to the way normal corporate loans would be originated and services. In practice, it would not be possible (based on the risk factors) to bundle such financing arrangements with a normal corporate loan and it is therefore appropriate for them to have a separate category.

- 7. Do you agree with the definitions of the asset categories provided? For example, do you consider that the asset category of credit facilities to SMEs and corporates should be further specified and for the SMEs should refer to the definition provided in the Commission Recommendation 2003/361/EC, or should other reference be used (for example to Art. 501 of the CRR)? Please substantiate your reasoning.**

See above. AFME members agree with broad, general categories which, in combination with the risk factors, will strike the right balance between diversification of portfolios and ensuring investors are able to adequately and effectively assess the credit quality of the portfolio.

We would note, however, that while the defined asset categories in Article 2 of the Draft RTS are appropriate, some of the corresponding explanations at paragraph 23 of the CP are incorrect. Notably, the description of auto loans and leases as being "secured by automobile vehicles" is not uniformly correct and does not completely reflect the general industry understanding of what constitutes an auto loan/lease securitisation. In auto finance securitisation transactions, it is relatively rare that there should be security taken over the "metal" or the vehicles themselves. The value (net book value, the contractually agreed repurchase price or the market value, as the case may be) of the vehicles may be an important part of the borrowing base for the securitisation, but security will generally only be taken over payment streams related to the vehicles rather than the vehicles themselves.

As to the question of the appropriate definition of an SME, AFME members are of the view that a definition is not necessary, as the asset category is broad enough to include loans to all enterprises and corporates, based on the explanation of the asset category at paragraph 23 (d) of the CP. Accordingly, and in order to ensure that this meaning is preserved in the legislative text (and to ensure that the highly undesirable situation results where corporate loans in general are not included in a named asset category), it is important that the EBA slightly revise the text of Article 2(d) to read as follows:

"Credit facilities provided to **enterprises and corporates, including** micro-, small- and medium-sized enterprises and corporates, including loans and leases;"

- 8. Do you agree with the approach to determination of the homogeneity based on the risk factors, and the distinction between the concept of risk factors to be considered for each asset category, and relevant risk factors to be applied for a particular pool of underlying exposures, as proposed? Are there any impediments or practical implications of the risk factors as defined? Are there any important and severe unintended consequences of the application of the risk factors?**

In general AFME members agree with this approach. It should be open to market participants to conclude on a case-by-case basis which risk factors need to be considered and applied to each pool – guided by the overarching principle of ensuring the investor can use the same methodology for the cash flow analysis of the securitised exposures and preventing the investor having to analyse materially different servicing arrangements. It is implicit, therefore, that not all of the risk factors to be considered in respect of a given asset class (as set out in Article 3(1)) will always be relevant in respect of a pool of assets from that asset class. Indeed, the expectation of AFME members is that one or more risk factors would be deemed irrelevant on the majority of transactions; the situation where all risk factors are relevant would accordingly be relatively rare.

In addition, given the significant element of subjective judgment involved in making these assessments, AFME members would urge the EBA to make clear in the final RTS that – so long as the originator, issuer and sponsor take a reasonable approach to assessing homogeneity in their STS notification – their judgment in this respect should not be disturbed. See our proposed drafting in our response to Question 2 above in this respect.

What is more, it should be made clear (as to which see our suggested drafting in our response to Question 1 above) that proper assessment of the risk factors does not depend on the values of those risk factors being identical. Rather, the aim of applying the risk factor approach should be to ensure that the underlying exposures exhibit similar types (but not necessarily similar degrees) of credit and cash flow risks such that those risks are able to be assessed at a pool level based on common methodologies and parameters – the overarching principle underlying the concept of homogeneity.

See, however, our responses to Questions 10 below.

**9. Do you agree with the distribution of the risk factors that need to be considered for each asset category, as proposed? What other risk factors should be included for consideration for which asset category?**

In general these seem sensible. As mentioned above, however, we fully expect that market participants will determine that at least one of the "to be considered" risk factors will be irrelevant in respect of most pools. But, even relevant, applicable risk factors need to be examined flexibly with a focus on the ability for the investor to analyse the pool sensibly. Otherwise application of the applicable risk factors could unduly limit the diversification of the pool and cause the transaction to become more risky as a result.

However, we would note that there is a drafting error in Article 3(1) as no allocation of risk factors to be considered in respect of Article 2(e) is listed. Please amend this legislative drafting to reflect the table that appears on page 15 of the CP.

**10. Do you agree with the definition of the risk factor related to the governing law, which refers to the governing law for the contractual arrangements with respect to the origination and transfer to SSPE of the underlying exposures, and with respect to the realisation and enforcement of the credit claims? Do you consider the risk factor of the governing law should be further specified, or further limited (e.g. to the realisation and enforcement of the financial collateral arrangements securing the repayment of the credit claims)?**

AFME members do not believe that governing law is a relevant risk factor to be taken into account over and above jurisdiction. Governing law may vary within jurisdictions



but this has not historically been viewed by the market as a problem for homogeneity of portfolios. English, Scots and Northern Irish mortgages are routinely put into the same, homogeneous residential mortgage portfolios as are auto loans and leases from the various länder in Germany. This has not historically caused investors material difficulty with credit and cash flow analysis, but introducing such distinctions would risk creating significant problems for generating homogeneous portfolios with the critical mass necessary for securitisation.

If governing law is to be included as a risk factor, it should be limited to ensuring that the obligation to transfer all assets to the SSPE arises under the same governing law – but with allowances where necessary for local law instruments to effect that transfer. This would ensure as much as possible that investors seeking to enforce the transfer of assets to the SSPE could obtain a single judgment to that effect.

**11. Do you consider prepayment characteristics as a relevant risk factor for determining the homogeneity? If yes, based on which concrete aspect of the prepayment characteristics of the underlying exposures should the distinction be made, and for which asset categories this risk factor should be considered and should be most relevant?**

AFME members do not consider prepayment characteristics to be a relevant risk factor for determining homogeneity. Prepayment characteristics are not reflective of credit risk (prepayments create reinvestment risk rather than credit risk) and are anyway considered as part of cash flow analysis. Furthermore, the prepayment characteristics of individual assets will vary according to different factors to those that will influence the general characteristics of the pool. These include the general economic environment, interest rates and the obligor's ability and willingness to refinance their obligations on more favourable terms than those in the securitised exposure.

**12. Do you consider seniority on the liquidation of the property or collateral a relevant risk factor for determining the homogeneity? If yes, do you consider the distinction between the credit claims with higher ranking liens on the property or collateral, and credit claims with no higher ranking liens on a different property or different collateral, as appropriate for the purpose of determination of homogeneity?**

AFME members agree in general that seniority of the underlying exposure on the liquidation of the collateral is a relevant risk factor. That said, the appropriate distinction is between loans secured by first-ranking liens on the one hand and loans secured by lower-ranking liens on the other hand (except where all higher ranking liens are also included in the same portfolio).

This distinction is appropriate because – where the creditor has a first-ranking lien it need not analyse the other security to determine the extent of its subordination, which

would be a significant complicating factor that changes the analysis of credit and cash flows for investors.

It is important to note for these purposes, however, that guaranteed residential mortgages of the type referred to in Article 129(1)(e) should be assimilated to first-ranking mortgages regardless of the ranking of the security interest on the mortgage.

**13. Do you agree with the approach to determining the homogeneity for the underlying exposures that all do not fall under any of the asset categories specified in the Article 3?**

Subject to our comments in response to Question 10 above, AFME members agree that, for asset categories not listed in Article 3(1)(a)-(g) of the Draft RTS, it is sensible to have to consider all risk factors and come to a reasoned conclusion, disclosed to investors, as to the applicability of each risk factor to the particular asset category and pool.

**14. Do you believe that materiality thresholds should be introduced with respect to the risk factors i.e. that it should be possible to consider as homogeneous also those pools which, while fully compliant with requirements under Article 1 (a), (b) and (c), are composed to a significant percentage (e.g. min 95% of the nominal value of the underlying exposures at origination), by underlying exposures which share the relevant risk factors (e.g. by 95% of general residential mortgages with properties located in one jurisdiction and 5% of income producing residential mortgages located in that and other jurisdictions)? Please provide the reasoning for possible introduction of such materiality thresholds.**

AFME members are of the strong view that a materiality threshold is essential to make the day-to-day practical application of the homogeneity requirement sensibly manageable. A materiality threshold is the best way to balance the competing interests of – on the one hand – ensuring investors in (especially) a large, granular pool can sensibly assess risk with – on the other hand – the commercial realities of managing a consumer business with daily changes on the ground in underlying assets. The additional uncertainty arising out of small deviations from 100% homogeneity will not generally be sufficient to invalidate the credit analysis done by an investor on the pool overall but it does have a large beneficial effect of increasing the stability/certainty of retaining the STS label once obtained.

AFME members further consider that a 5% materiality threshold (i.e. a maximum of 5% of non-homogeneous assets) is a sensible level at which to set the threshold. It is sufficiently small that it is unlikely to materially affect the outcome of any analysis or modelling done by investors while being large enough to provide significant comfort to originators, sponsors and issuers.

- 15. Alternatively, do you see merit in introducing synergies with IRB modelling, enabling the IRB banks to rely on risk management factors validated for modelling purposes, when assessing the similarity of the underwriting standards, or assessing relevant risk factors? Please provide the reasoning and examples for possible introduction of such synergies.**

AFME members do not believe that this is an appropriate way to go about defining homogeneity for the purposes of the Securitisation Regulation. Our objections arise primarily because asset homogeneity is mainly focussed on clear communication to and simplicity for investors. The purpose of a homogeneous pool is to help ensure that investors are able to analyse credit and cash flow risks of the asset pool based on common methodologies and parameters. Integrating the definition of homogeneity with IRB banks' internal risk management factors is likely to promote opacity rather than transparency, as IRB models are agreed on a bank-by-bank basis with the bank's supervisor and are not well-known or well-understood outside the relevant bank.

- 16. Which option from the two (the existing proposal as described in this consultation paper, and the alternative option as described in this box) is considered more appropriate and provides more clarity and certainty on the determination of homogeneity? Please substantiate your reasoning.**

AFME members support the existing approach to homogeneity as described in the consultation paper and the Draft RTS and would discourage the EBA from adopting the alternative approach. The existing approach does a better job of reflecting existing market practice observed for high quality securitisation transactions, which is widely acknowledged to have been unproblematic and helpful to investors in assisting them to analyse transactions appropriately. What is more, the alternative approach has the significant drawback of requiring that the risk factors be taken into account at the stage of underwriting, which is both more opaque for investors and would cause significant compliance difficulties for legacy assets originated prior to the homogeneity framework's introduction.

- 17. Please provide an assessment of the impact of the two proposed options, on your existing securitisation practices and if possible, provide examples of impact on existing transactions.**

AFME as an association is not in a position to answer this question.

- 18. Alternatively, do you believe that a hybrid option, combining the existing proposal and the alternative proposal, would be most appropriate? The hybrid option could envisage that all the risk factors would need to be taken into account in the underwriting, and for those risk factors that are not taken into account in the underwriting, (i) either adequate justification would need to be provided that it is not required for the purpose of the homogeneity, (ii) or if the justification cannot**

**be provided, the risk factor would still need to be taken into account when determining the exposures in the pool (on the top of the requirements related to underwriting, servicing, and asset category). Or, should other hybrid option be envisaged? Please substantiate your reasoning.**

For the reasons set out in our response to Question 16, we favour the existing approach.

**19. What are the advantages, disadvantages and unintended consequences of this alternative option, in particular compared to the existing proposal?**

Please see our response to Question 16.

**20. Are there any impediments or practical implications of this alternative option as defined? Are there any important and severe unintended consequences of the application of this option?**

Please see our response to Question 16.