German Banking Industry Committee

Die Deutsche Kreditwirtschaft

Comments

on BCBS and IOSCO Consultative Document Criteria for identifying simple, transparent and comparable securitisations (BCBS 304)

Register of Interest Representatives

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The **German Banking Industry Committee** is the joint committee operated by the central associations of the German banking industry. These associations are the Bundesverband der Deutschen Volksbanken und Raiffeisenbanken (BVR), for the cooperative banks, the Bundesverband deutscher Banken (BdB), for the private commercial banks, the Bundesverband Öffentlicher Banken Deutschlands (VÖB), for the public-sector banks, the Deutscher Sparkassen- und Giroverband (DSGV), for the savings banks finance group, and the Verband deutscher Pfandbriefbanken (vdp), for the Pfandbrief banks. Collectively, they represent more than 2,000 banks.

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Comments on BCBS and IOSCO Consultative Document Criteria for identifying simple, transparent and comparable securitisations (BCBS 304)

We welcome the initiative of the Basel Committee on Banking Supervision and the International Organisation of Securities Commissions to define criteria for identifying simple, transparent and comparable securitisations. In particular, we consider it important to reconcile the perspectives of the financial services sector, of investors and of regulatory authorities when identifying and developing such criteria. Notwithstanding the EBA's parallel initiative in this respect, we expressly welcome the establishment of a uniform catalogue of criteria at the level of the Basel Committee – thus creating the fundamental basis for a harmonised implementation of such criteria across all countries recognising the securitisation framework defined by the Basel Committee. This will allow for an appropriate review of capital requirements under the securitisation framework. We are happy to participate in this process, not only by way of the comments provided in this document but also by way of constructive proposals at a later stage: please do not hesitate to contact us.

We share your view that a functioning securitisation market – supplementing bank loans – is essential to support economic development, and for providing sufficient credit to companies, particularly to small and medium-sized enterprises. This is especially true where banks require a complementary, functioning market that allows them to boost lending, in the event of higher credit demand by corporate borrowers, beyond their capacity of on-balance-sheet lending within the scope available under the Basel III regime. Having said that, limiting the criteria for simple, transparent and comparable securitisations to true-sale and term securitisations would actually impede the objective you have formulated. You emphasise the importance of short-term securitisations, ABCP programs and synthetic securitisation for large parts of the real economy – yet you exclude these forms of securitisation without analysing their suitability. We are aiming for a solution that fulfils the needs of all parties involved: all companies with their respective business models as well as all investors that may have opted for a particular form of securitisation in the past – whatever the reasons. If, from a regulatory point of view, simultaneously identifying and developing suitable criteria for all securitisation variants is too extensive a task, we believe that going through this process subsequently for all key types of securitisation – based on a schedule communicated in advance – would be an appropriate alternative.

Whether we are looking at true sales, synthetic securitisations, ABCP programs or term securitisations – what we consider decisive in this context is to apply a comparable catalogue of criteria to all types of securitisation transactions that are viable for the real economy. Such a uniform catalogue would create security – for the securitisation industry when originating transactions, for investors when conducting their due diligence, and for regulators in conducting their audits.

ABCP transactions

We have noticed that the BCBS and IOSCO consultative paper does not cover ABCP (asset-backed commercial paper) transactions. Against the background of the significant importance of ABCP programs for banks and corporate customers, and the desirable beneficial treatment of transactions meeting BCBS´s requirements, we would like to ask BCBS and IOSCO to continue their work on "simple, transparent and comparable securitisations" in order to elaborate - together with the industry - tailor-made criteria for simple, transparent and comparable ABCP transactions. Since multi-seller conduits differ

from the usual structure of a term securitisation there should be specific criteria for multi-seller conduits. In our comments to Question 3 we have illustrated how certain criteria for the definition of simple, transparent and comparable securitisations should be adjusted in order to factor in the special features of ABCP transactions.

Synthetic securitisations

We very much support extending the scope of qualification to include synthetic securitisations with real-economy links. Only synthetic securitisations permit securitisation of credit claims that are independent of individual loans. This focus on the borrower - rather than on the individual loan - would in itself contribute greatly to the flexible financing of investments as demanded by SMEs. Narrowing the scope of qualification to true sale securitisations would be counterproductive to the faster economic recovery tailored to the needs of the borrowing companies in the real economy – something which is being called for by economic policymakers. This restriction to real-economy claims could take into account reservations concerning use of synthetic securitisations to reduce capital requirements. Please refer to the Annex for additional arguments in favour of including synthetic securitisations.

Principle-oriented definition of the criteria

Against the background of the need to improve the market acceptability of securitisations, we suggest that the criteria to be defined should principally not be formulated in a too detailed fashion. This would allow for the approach to be applied to enhanced transaction models in the future (principle-orientation).

Comments on Questions

Question 1 – Do respondents agree that the criteria achieves the goals they aim to achieve? In particular, do respondents believe that the criteria could help investors to identity "simple", "transparent" and "comparable" securitisations?

In principle, yes we agree. The criteria are rather generic and more principle-oriented. Given the fact that it will be a worldwide global standard and therefore take into account major differences between the European and US securitisation markets, we believe that this is the right level of detail for a global standard. Further rules-based clarifications will be given by the competent supervisory authorities such as EBA in Europe. However, to foster further standardisation and comparability across the different ABS markets, especially between Europe and the US market, we recommend a review of the more detailed rules (after implementation, perhaps in a few years) by competent authorities, to further specify the criteria. For the time being, we advise against further detailing.

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Question 2 – Do respondents agree with the STC criteria set out in the annex of this paper? In particular, are they clear enough to allow for the development by the financial sector of simple, transparent and comparable securitisations? Or do respondents think they are too detailed as globally applicable criteria? The annex provides guidance on each on each criterion. Which additional criteria would respondents consider necessary, if any, and what additional provisions would be useful or necessary to support the use of the criteria. What are respondents´ view on the "additional considerations" set out under some criteria in the annex? Should they become part of the criteria? Are there particular criteria that could hinder the development of sustainable securitisation markets due, for example, to the costliness of their implementation?

1. Nature of assets

According to the criteria, the underlying assets of a securitisation should be credit claims or receivables that are homogeneous with respect to their asset type. It should be clarified that the securitisation of commercial and retail exposures in one transaction (as e. g. in many auto loan and –lease transactions) is not excluded by this requirement.

With regard to car loans we would like to add that in this business, loans and leases are subsidised by manufacturers or dealers to promote sales. It should be clarified that loans and leases subsidised, for instance by the manufacturer or the car dealer, are not excluded, particularly given the fact that loans or leases e. g. with interest rate subsidies normally exhibit low default rates.

2. Asset performance history

It is a requirement that loss performance data, such as delinquency and default data, should be available for credit claims and receivables. We agree that such information is available for typical bank-originated loans. Such data might not be available, however, for corporate customer receivables (e.g. trade receivables) since the customer's infrastructure does not usually provide such information. In addition, it should not be overlooked that the loss data for certain asset classes (e.g. trade receivables) indicate that losses are very low (as shown in investigations conducted by True Sale International in 2010 and 2014). Furthermore, silent assignment and transfer of the receivables is mandatory for almost all corporates (needless to say, only if allowed under the applicable law). Although the data can be anonymised, the level of confidentiality a corporate client intends to maintain would be undermined and the relative value of securitisation in comparison to loan lending would decline further.

3. Payment status

We are of the opinion that the payment status is a very critical point. The definitions of default and delinquent vary in jurisdiction. For that reason, we would suggest that the common practice should be applied, and should not depend on ECAIs.

To meet the objective of developing a sustainable securitisation market it should be possible to include credit claims or receivables of companies, such as SMEs, which have recovered after an insolvency or debt rearrangement process, if they are no longer impaired under applicable accounting rules. Such accounting rules also require an assessment after a recovery as to whether the borrower is still credit-impaired.

With the regard to the car loan business we would like to mention that it is common practice of prime Auto-ABS that all past due receivables are to be excluded. In addition, it is required that at least one instalment has been paid in respect of each of the purchased loan receivables. In some cases, even two instalments paid are common for auto loan and auto lease securitisations - in combination with the requirement that no loan or lease receivables are past due, to ensure high quality of the underlying assets. This practice has been proven to maintain a low level of losses for the underlying securitised auto loan and auto leasing contracts in the past, even under severe stress conditions. In contrast, it was typical for the originate-to-distribute model in the US subprime RMBS segment that loan receivables were sold without having obtained any payment by the debtor. Thus it is imperative to continue the former practice, to ensure high quality of the underlying securitised loan and lease contracts.

The phrase "for which the transferor or parties to the securitisation are aware of evidence indicating a material increase in expected losses" should be deleted. It could be difficult to measure and determine a material increase in expected loss. The calculation of expected losses requires the parameters PD, LGD and EAD. However, such parameters are typically calculated by IRB banks and would exclude banks that use the Standardised Approach for credit risk. Beyond such practical issues, we doubt whether an increase in the expected losses is an appropriate criterion at all. We would understand such a requirement if the aim were to avoid an originator mainly selecting receivables where he expects a significant increase in expected losses. However, this should be better addressed by the requirement that the selection of the receivables has to be carried out randomly, and that no adverse selection of receivables is permitted which could hinder the performance comparison between the non-securitised portfolio and the expected performance of the securitised loans.

4. Consistency of underwriting

It says here that in order to "ensure that the quality of the securitised credit claims and receivables is not dependent on changes in underwriting standards, the originator should demonstrate to investors that any credit claims or receivables being transferred to the securitisation have been originated in the ordinary course of the originator's business to uniform and non-deteriorating underwriting standards."

We would like to point out that underwriting standards can change because they are part of the credit and acceptance policy. Moreover, the underwriting process will change over time, for instance, due to new recognised risks as to fraud or for the sake of process optimisation. In any case, the underwriting standards for the loans and leases to be securitised and non-securitised should not differ and not deteriorate in substance. Hence, the originator should apply the same sound and well-defined criteria for credit-granting to exposures to be securitised as they apply to exposures to be held in their own book. Thus we would propose the following wording: "the originator should demonstrate to the investor that any credit claims or receivables being transferred to the securitisation have been originated in the ordinary course of the originator's business, to standards with sound and well-defined criteria for credit-granting to exposures to be securitised as they apply to exposures to be held in their own book. In addition, the originator should demonstrate that there is no deterioration of underwriting standards in substance."

5. Asset selection and transfer

The securitisation shall not be characterised by an active portfolio management on a discretionary basis. For the avoidance of doubt it should be made clear here that the revolving purchase of receivables (e.g. trade receivables) to replace maturing or ineligible assets is not to be regarded as active portfolio management in the sense of a discretionary decision by a manager.

9. Payment priorities and observability

The TFSM proposes to ensure that junior note holders do not have inappropriate payment preference over senior note holders that are due and payable throughout the life of a securitisation; or, where there are multiple securitisations backed by the same pool of credit claims or receivables, throughout the life of the securitisation program, junior liabilities should not have payment preference over senior liabilities which are due and payable.

It should be clarified that the following common priority of payments is eligible:

1. Payment of interests on the senior notes
2. Payment of interests on the junior notes
3. Redemption of the principle amount of the senior notes
4. Redemption of the principle amount of the junior notes

11. Documentation disclosure and legal review

The TFSM suggests ensuring that the securitisation's legal documentation has been subject to appropriate review prior to publication; also that the terms and documentation of the securitisation should be reviewed and verified by an appropriately experienced and independent legal practice.

It should be clarified that a law firm mandated by the originator or by the sponsor and acting as transaction counsel does not conflict with the requirement of "independence".

12. Alignment of interest

"In order to align the interests of those responsible for the underwriting of the credit claims or receivables with those of investors, the originator or sponsor of the credit claims or receivables should retain a material net economic exposure and demonstrate a financial incentive in the performance of these assets following their securitisation."

Fully supported liquidity lines within multi-seller ABCP-programs should be regarded as material net economic exposures.

For retail auto loan and auto lease securitisation transactions it is common practice that a randomly selected sub-portfolio, equivalent to no less than 5% of the nominal value of the securitised exposures, where such exposures would otherwise have been securitised in the securitisation, is retained, provided that the number of potentially securitised exposures is no less than 100 at origination. It should be possible to continue this practice. Thus, we request for clarification that this common practice does not conflict with the risk retention requirement above.

Question 3 – What are respondents´ views on the state of short-term securitization markets and the need for initiatives with involvement from public authorities? Do respondents consider useful the development of differentiating criteria for ABCP, in a manner similar to that of term securitisations? The BCBS and IOSCO would particularly welcome any data and descriptions illustrating the state of short-term securitization markets by jurisdiction and the views of respondents on concrete comparable criteria that could be applied to short-term securitisations.

As already outlined in our general remarks we would like to point out by the following comments how certain criteria for the definition of simple, transparent and comparable securitisations should be adjusted in order to factor in the special features of ABCP transactions.

Criteria for identifying simple, transparent and comparable multi-seller conduit ABCP

Multi-seller conduits are platforms that purchase predominantly trade, consumer or leasing receivables from corporations, leasing companies or Auto-Asset Backed Securities. The purchase is funded by issuing short-term commercial paper (ABCP). The sponsor bank which is running the conduit provides liquidity lines that can be drawn if the ABCP cannot be sold to the market or losses in the securitized receivables occur. Most of the ABCP issued in Germany are "fully supported". This means that any losses of the investors are borne by the provider of the liquidity facility.

ABCP conduits play an important role in the financing of businesses. They are advantageous for corporates as well as for banks. Corporates can use the sale of own receivables as a substitute for other forms of funding (especially bonds or bank loans). Furthermore, for small and medium sized companies they are often the only way to access the securitisation market as their volume of potential assets is not sufficient for a term securitisation. From a bank's perspective, providing a liquidity line to an ABCP transaction is typically less risky than a direct credit exposure to the corporate. This is predominantly due to the fact that the main driver of credit risk is not the corporate, but a diversified portfolio of independent debtors with a high granularity or the full coverage of the portfolio by a commercial credit insurance. Moreover, the eligibility criteria of the transactions often exclude higher-risk exposures and only allow receivables that are originated in the normal course of the business of the respective corporate seller. In addition, the monthly reporting obligations for the securitised portfolio give the bank more timely information than typically obtained in a traditional credit relation. Last but not least, and especially for smaller corporates, the process of structuring an ABCP transaction - including strictly defining relevant processes (e. g. credit and collection policy) - is not only beneficial for the bank, but also for the corporate and strengthen the receivables management process.

While the volume of the conduit business market shrank significantly due to the exit of arbitrage conduits and structured investment vehicles (SIVs) after the financial crisis, the share of multi-seller conduits in all conduit issuances has risen considerably. According to Moody's, multi-seller conduits in Europe securitize

trade, consumer or leasing receivables totaling 63.3 billion EUR in 2014 and thereby account for 82 per cent of the ABCP market.

Multi-seller ABCP issues show a strong performance. They have experienced stable and sound development even through the financial and economic crises 2007/2008 and subsequent years. In Germany, no ABCP investor in a multi-seller-conduit has ever suffered a loss.

We are afraid that ABCP will be negatively affected by the new Basel Framework for Securitisations that will come into effect in 2018. In this context, two roles have to be distinguished that banks can play in an ABCP multi-seller conduit transaction: investor, and sponsor bank. As ABCP cannot be issued without a sponsor bank to provide the liquidity facility, the treatment of these facilities in the capital requirements regime is of utmost importance.

According to our calculations based on the latest proposals of the Basel committee (BCBS 303), capital requirements for liquidity banks will triple or quadruple compared to the current framework - and will partially exceed those for senior unsecured corporate loans. Thus ABCP financing will become unattractive for sponsors, and very expensive for sellers.

From our point of view it is therefore of utmost importance that ABCP as well as the corresponding liquidity facilities can be recognised as “simple, transparent and comparable securitisations”, and that the respective securitisations are rewarded by a special regulatory treatment.

As multi-seller conduits differ from the usual structure of a term securitisation, specific high-quality criteria for multi-seller conduits should be developed. We would therefore like to request the TFSM to continue its work on “simple, transparent and comparable securitisation” in order to elaborate - together with the industry - tailor-made criteria for simple, transparent and comparable ABCP transactions. In the following we would like to illustrate in which respect the criteria proposed by the TFSM should be adjusted in order to better capture the special nature of multi-seller ABCP programs.

A. Asset risk

1. Nature of the assets

In simple, transparent and comparable securitisations, the assets underlying the securitisation shall be credit claims or receivables that are homogenous with respect to their asset type, jurisdiction, legal system and currency.

From our point of view this criterion shall (in the case of an ABCP program) not apply to the securitised assets, but to the risk protection scheme or the risk taker. Therefore, it should be sufficient that the credit risk of the securitised assets is fully covered by a third party (e.g. by a credit insurance in respect of the transaction specific liquidity facility or by a fully supported liquidity facility in respect of the

commercial papers issued within an ABCP program). This would enable fully supported ABCP programs to fulfil the criterion even if the various pools of such multi-seller programs stem from different originators, asset classes, currencies and legal systems. By way of full credit support the investor is exposed primarily to the risk of the sponsor bank. This adds enormous simplicity to analysis of the investment.

From the perspective of the liquidity facility (which is transaction specific and does not benefit from the full support) the homogeneity criterion should be met for each pool of trade, consumer or leasing receivables of real economy originators, if the asset type is uniform and if any material risks out of currency mismatches or different legal systems are covered by adequate measures (FX hedges, credit insurance, or legal opinions). This would enable the real economy to use ABCP structures in a most efficient manner, especially when the trade receivables derive from the cross-border delivery of goods and services.

Furthermore, according to the TFSM proposal any referenced interest payment or discount rates should be based on commonly encountered market interest rates, but should not reference complex or complicated formulae or exotic derivatives. For the avoidance of doubt it should be clarified that any lease receivables that contain interest rates at subsidized levels may be considered eligible if they are purchased with a discounted purchase price that adjusts the yield to the market rate level.

2. Asset performance history

The TFSM suggests that investors should have access to data on the loss performance, such as delinquency and default data, for substantially similar exposures to those being securitised, over a time period long enough to permit meaningful evaluation by investors. From our point of view this requirement should not apply to multi-seller ABCP programs because of the specific structure of these programs. It should be sufficient that investors have information about the materially relevant data on the credit quality and performance of the underlying assets. Because of the constant pool changes in ABCP programs (additions/removals) and the coverage through (at least 100 %) liquidity support by the sponsor bank, historical data of single pools is not relevant to investors.

3. Payment status

According to this criterion, the securitised portfolio shall not include obligations that are in default, those that are delinquent, or obligations for which the transferor or parties to the securitisation are aware of evidence indicating a material increase in expected loss, or of enforcement actions. In the case of trade, consumer and lease receivable securitisations where the original lender is not a credit institution, a borrower shall only be defined as credit-impaired if such original lender has positive knowledge of circumstances that make it highly unlikely that the borrower is able to pay its obligation in full. It should be noted that real economy originators, i.e. corporates, do not have systems and procedures in place to

perform a bank-like underwriting and credit approval process. It should also be taken into account that trade receivables often are covered by a commercial credit insurance.

5. Asset selection and transfer

The TFSM proposes that the securitisation should not be characterised by an active portfolio management on a discretionary basis. For the avoidance of doubt it should be made clear here, that the revolving purchase of receivables (e. g. trade receivables) is not to be regarded as active portfolio management, even if maturing or ineligible receivables are replaced.

Furthermore, the securitisation shall be characterized by a legal true sale. It should be clarified in that context that the true sale requirement only relates to the legal separability of the securitised assets, and not to the derecognition under IFRS or local GAAP. Likewise, any tax treatment should have no impact on the recognition of the legal true sale within this context.

In addition, the TFSM requires that the original lender should provide representations and warranties that assets being included in the securitisation are not subject to any condition or encumbrance that can be foreseen to adversely affect enforceability in respect of collections due. From our point of view the representations and warranties of the original lender regarding enforceability of collections with regard to trade receivables should allow for exclusions of such circumstances that are ordinary in the original lender’s business (e.g. dilutions, set-offs). If the ABCP program is fully supported, this requirement should be met automatically.

6. Initial and ongoing data

The TFSM is proposing that investors and prospective investors should have readily available access to data on the underlying individual assets on a loan-by-loan level, at inception, before the pricing of the securitisation, and on an ongoing basis.

From our point of view this should not apply to multi-seller ABCP programs because of the specific structure of these programs. Through the regular investor reporting, investors will have information about the materially relevant data of the underlying assets on an aggregated base (e.g. asset type, industry of sellers, currencies, geographical distribution etc.). Delivery of loan-by-loan-level data of trade receivables is not practical, already outdated, and potentially not sensible to disclose. It may even be critical, in terms of business secrets of the corporate sellers. Furthermore, investors do not benefit from such data as they rely primarily on the liquidity support of the sponsor/liquidity bank. Aggregated pool data has proven to be fully sufficient.

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B. Structural risk

9. Payment priorities and observabilities

The transaction documentation of those transactions featuring a revolving period shall include provisions for appropriate early amortisation events, or triggers of termination of the revolving period if the originator/sponsor is unable to generate sufficient new underlying exposures of at least similar credit quality (ii). For the avoidance of doubt it should be clarified that this requirement does not apply to ABCP programs, as these are designed to refinance fluctuating receivables pools.

Furthermore, the originator or sponsor shall provide investors a liability cash flow model or information on the cash flow provisions. We think that cash flow statements should not be mandatory, especially not within ABCP programs where assets and liabilities are constantly revolving. Any reporting of cash flow information should be made in a reasonable and sufficient manner to enable the investor to have a clear picture of all materially relevant aspects regarding his risk position in the respective investment. Especially in fully supported, multi-seller ABCP programs with trade or lease receivables from various real economy companies, certain data may be kept confidential if information memorandums and investor reporting provide all materially relevant information for assessing the risk position of the investor. Therefore the originator and sponsor should only provide investors with a liability cash flow where applicable.

Last but not least, the TFSM proposes to ensure that junior note holders do not have inappropriate payment preference over senior note holders that are due and payable throughout the life of a securitisation; or, where there are multiple securitisations backed by the same pool of credit claims or receivables, throughout the life of the securitisation program, junior liabilities should not have payment preference over senior liabilities which are due and payable. This paragraph should only apply if the transaction structure within the ABCP program contains junior notes (which is in many instances not the case because the receivables are bought at a reduced purchase price creating an over-collateralisation).

11. Documentation disclosure and legal review

"To help investors to fully understand the terms, conditions, legal and commercial information prior to investing in a new offering and to ensure that this information is set out in a clear and effective manner for all programs and offerings, sufficient initial offering documentation should be provided to investors (and readily available to potential investors on a continuous basis) within a reasonably sufficient period of time prior to issuance, such that the investor is provided with full disclosure of the legal and commercial information and comprehensive risk factors needed to make informed investment decisions. These should be composed such that readers can readily find, understand and use relevant information."

For ABCP-Programs access should be limited to materially relevant underlying documentation in order to assess the structure and the credit quality of the securitisation.

For the securitisation of trade and lease receivables, the relevant real economy originator may define which information is to be protected as business secrets and whether there is information that may be published.

Even where a disclosure is legally possible, the disclosure could endanger the business secrets of real economy companies where trade and lease receivables are securitised. In such cases the originator is not a bank, but a real economy company. As is the case for factoring transactions, the securitisation transactions are off-balance for many companies and in some cases they are even off-notes. In such cases even the mentioning of the name of the originator company could negatively affect the originating company. Furthermore, a disclosure of portfolio data in combination with the name of the originator could allow competitors of the company to extract sensitive data (such as payment terms accepted by the company, distribution of the customer base, general business development (e.g. high turnover/low turnover), etc.).

This applies even more if the securitisation is fully supported by a sponsor/liquidity bank or other means which cover all risks (e.g. credit insurance). Where investors rely on the support of a third party, they should only be entitled to request documentation that is materially relevant to understand their risk position to the extent that they may reasonably request such information without jeopardising the business secrets of any of the counterparties involved.

Question 4 - What are respondents' views on the level of standardisation of securitisation transactions' documentation? Would some minimum level of standardisation of prospectuses, investor reports and key transaction terms be beneficial? Do respondents think there are other areas that could benefit from more standardisation? Would a standardised template including where to find the relevant information in the prospectus be helpful? The BCBS and IOSCO would particularly welcome a description, by jurisdiction, of the extent to which different elements of initial documentation are standardised.

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Annex - Criteria for identifying simple, transparent and comparable synthetic securitisations

According to criterion 5 only those securitisations shall be eligible where the assignment of rights is not effected through credit default swaps, derivatives or guarantees, but by a legal assignment of the credit claims or the receivables. Thus synthetic securitisations would not be eligible.

We think that synthetic transactions should not be excluded from the framework for simple, transparent and comparable securitisations. This particularly holds true when the set-up of a securitisation as a synthetic securitisation is the only reason for not meeting the TFSM's criteria for simple transparent and comparable securitisations. The essential benefits of synthetic transactions for many originating banks are the transfer of credit risk (e. g. SME loans) to third parties, when true sale transactions (traditional securitisations) cannot be employed since bank customers do not want the bank to sell their loans (transfer clause limitations), and the release of risk-weighted assets for new real economy transactions. Moreover, synthetic transactions are often the only way to manage risks arising from certain off-balance sheet exposures, e.g. letters of credit or guarantees provided to bank's customers. This also applies to certain on-balance sheet exposures, such as until-further-notice overdraft facilities. In other words, synthetic transactions do support - in the most efficient way - real economy SME transactions by enabling banks to transfer the risks of various lending products as well as taking care of bank client concerns such as data secrecy or the causeless but widely spread threat of a sale of the relationship to third parties like hedge funds. Synthetic transactions also support risk-sharing in the financial system.

In comparison to true sale transactions, synthetic transactions show further advantages. Since the securitised assets will not be sold to the SPV, risks such as legal validity of the receivables, commingling risk, settlement risk and collection risk will not be present. This implies that the investor does not suffer any losses arising from such risks, since they are not credit default risk. Moreover, if the originator bank defaults, the guarantee or credit default swap will be terminated and the investor gets back the provided cash (from purchased CLN) over and above any occurred credit events in the underlying portfolio (in contrast to selling the securitised assets or awaiting any scheduled repayments in the portfolio). This is of particular interest to investors who want to buy certain credit risk, but not buy the actual underlyings (and potentially therefore wait for their cash back until all assets are sold).

As mentioned above, synthetic transactions can be structured in a simple and transparent way. Often, the transactions and associated documentation are less complex for both issuer and investor as they do not involve the sale of assets. By way of example, there are much less involved parties in a synthetic transaction. A synthetic transaction could therefore be considered simple, transparent and comparable, under almost the same conditions/criteria proposed for a true sale securitisation.

In summary, we believe that when synthetic securitisations of bank loans meet the spirit of the remaining TFSM criteria, the set-up as a synthetic securitisation should not hamper the inclusion of such transactions in the definition of "simple standard and transparent securitisation", and regulators should encourage the ability of banks to manage the risks associated with bank-originated loans.