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To:	Permanent Representatives Committee (Part 2)
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Subject:	Proposal for a REGULATION OF THE EUROPEAN PARLIAMENT AND OF THE COUNCIL amending Regulation (EU) No 575/2013 as regards adjustments to the securitisation framework to support the economic recovery in response to the COVID-19 pandemic - Mandate for negotiations with the European Parliament

Delegations will find below the Presidency compromise text on the above-mentioned Commission proposal.

2020/0156 (COD)

Proposal for a REGULATION OF THE EUROPEAN PARLIAMENT AND OF THE COUNCIL amending Regulation (EU) No 575/2013 as regards adjustments to the securitisation framework to support the economic recovery in response to the COVID-19 pandemic

(Text with EEA relevance)

THE EUROPEAN PARLIAMENT AND THE COUNCIL OF THE EUROPEAN UNION,

Having regard to the Treaty on the Functioning of the European Union, and in particular Article 114 thereof,

Having regard to the proposal from the European Commission,

After transmission of the draft legislative act to the national parliaments,

Having regard to the opinion of the European Central Bank,

Having regard to the opinion of the European Economic and Social Committee,

Acting in accordance with the ordinary legislative procedure,

Whereas:

(1) The COVID-19 pandemic is severely affecting people, companies, health systems and the economies of Member States. The Commission, in its Communication to the European Parliament, the European Council, the Council, the European Economic and Social Committee and the Committee of the Regions of 27 May 2020 entitled 'Europe's moment: Repair and Prepare for the Next Generation' stressed that liquidity and access to finance will be a continued challenge in the months to come. It is therefore crucial to support the recovery from the severe economic shock caused by the COVID-19 pandemic by introducing targeted amendments to existing pieces of financial legislation. This package of measures is adopted under the label "Capital Markets Recovery Package".

(2) Credit institutions and investment firms ('institutions') will have a key role in contributing to the recovery. At the same time, they are likely to be impacted by the deteriorating economic situation. Competent authorities have provided temporary capital, liquidity and operational relief to institutions to ensure that institutions can continue to fulfil their role in funding the real economy in a more challenging environment.

(3) Securitisations are an important component of well-functioning financial markets since they contribute to diversifying institutions' funding sources and releasing regulatory capital that can be reallocated to support further lending. Furthermore, securitisations provide institutions and other market participants with additional investment opportunities, thus allowing portfolio diversification and facilitating the flow of funding to businesses and individuals both within Member States and on a cross-border basis throughout the Union.

(4) It is important to reinforce the capacity of institutions to provide the necessary flow of funding to the real economy in the aftermath of the COVID-19 pandemic, while ensuring that adequate prudential safeguards are in place to preserve financial stability. Targeted changes to Regulation (EU) No 575/2013 as regards the securitisation framework should contribute to the achievement of those objectives and enhance the coherence and complementarity of that framework with the various measures taken at Union and national level to address the COVID-19 pandemic.

(5) The final elements of the Basel III framework published on 7 December 2017 impose, in case of securitisation exposures, a minimum credit rating requirement only upon a limited set of protection providers, namely to entities that are not sovereign entities, public sector entities, institutions or other prudentially regulated financial institutions. It is therefore necessary to amend Article 249(3) of Regulation (EU) No 575/2013 to align it with the Basel III framework in order to enhance the effectiveness of national public guarantee schemes assisting institutions' strategies to securitise non-performing exposures (NPEs) in the aftermath of the COVID-19 pandemic.

(6) The current Union prudential framework for securitisation is designed on the basis of the most common features of typical securitisation transactions, i.e. performing loans. In its "Opinion on the Regulatory Treatment of Non-Performing Exposure Securitisations"[1] of 23 October 2019, the European Banking Authority (EBA) pointed out that the current prudential framework for securitisation set out in Regulation (EU) No 575/2013, when applied to securitisations of NPEs, leads to disproportionate capital requirements because the Securitisation Internal Ratings Based Approach (SEC-IRBA) and the Securitisation Standardised Approach (SEC-SA), is not consistent with the specific risk drivers of NPEs. A specific treatment for the securitisation of NPEs should therefore be introduced.

[1] https://eba.europa.eu/risk-analysis-and-data/npls

(7) The EBA recommends in its "Report on STS framework for synthetic securitisation" of 6 May 2020 to introduce a specific framework for simple, transparent and standardised (STS) on-balance-sheet securitisation. Given the lower agency risk and modelling risk of an STS on-balance-sheet securitisation compared with a non-STS synthetic securitisation, a fitting risk-sensitive calibration for STS on-balance-sheet securitisations as discussed by the EBA in its report should be introduced and accompanied by a mandate to the EBA to monitor the functioning of the respective market. The greater recourse to the STS on-balance-sheet securitisation promoted by the more risk sensitive treatment of the senior tranche of such securitisations will free up regulatory capital and could ultimately further expand the lending capacity of institutions in a prudentially sound manner.

(8) The synthetic excess spread (SES) is a mechanism commonly used in the securitisation of certain asset classes for originators and investors to reduce the cost of protection and the exposure at risk, respectively. A dedicated prudential treatment of SES should be provided for to prevent it from being used for regulatory arbitrage purposes. This regulatory arbitrage happens when the originator institution provides credit enhancement to the securitisation positions hold by the protection providers by contractually designating certain amounts to cover losses of the securitised exposures during the life time of the transaction, and such amounts, which encumber the originator's income statement in a similar way as an unfunded guarantee, are not risk-weighted.

(9) To ensure a harmonised determination of the exposure value of SES, the EBA should be mandated to develop draft regulatory technical standards. Those technical standards should be in place before the new prudential treatment becomes applicable. Institutions should be given sufficient time to apply the new prudential treatment of SES to avoid disruptions to the synthetic securitisations market. As part of its report on the functioning of Regulation (EU) 2017/2402, the Commission should also review the new prudential treatment of SES in light of developments at international level.

(10) Since the objectives of this Regulation, namely to maximise the capacity of institutions to lend and to absorb losses related to the COVID-19 pandemic, while still ensuring their continued resilience, cannot be sufficiently achieved by the Member States but can rather, by reason of their scale and effects, be better achieved at Union level, the Union may adopt measures, in accordance with the principle of subsidiarity as set out in Article 5 of the Treaty on European Union. In accordance with the principle of proportionality, as set out in that Article, this Regulation does not go beyond what is necessary in order to achieve those objectives.

(11) Regulation (EU) No 575/2013 should therefore be amended accordingly,

HAVE ADOPTED THIS REGULATION:

Article 1

Amendments to Regulation (EU) No 575/2013

Regulation (EU) No 575/2013 is amended as follows:

(1) in Article 242, the following number (20) is inserted:

"(20) 'synthetic excess spread' means a synthetic excess spread as defined in point (28) of Article 2 of Regulation (EU) 2017/2402.";

(2) Article 248 is amended as follows:

(a) in paragraph (1), the following point (e) is inserted:

"(e) The exposure value of a synthetic excess spread shall include the following items, as applicable:

i. any income from the securitised exposures already recognised by the originator institution in its income statement under the applicable accounting framework that the originator institution has contractually designated to the transaction as synthetic excess spread that is still available to absorb losses;

ii. any synthetic excess spread contractually designated by the originator institution in any previous periods that is still available to absorb losses;

iii. any synthetic excess spread contractually designated by the originator for the current period that is still available to absorb losses;

iv. any synthetic excess spread contractually designated by the originator for future periods.

For the purposes of point (i) of the first subparagraph, any amount that is provided as collateral or credit enhancement in relation to the synthetic securitisation and that is already subject to an own funds requirement in accordance with the provisions set out in this Chapter shall not be included in the exposure value.";

(b) the following paragraph 4 is inserted:

“4. The EBA shall develop draft regulatory technical standards to specify how originator institutions shall determine the exposure value referred to in point (e) of paragraph 1.

The EBA shall submit those draft regulatory technical standards to the Commission 6 months after the date of entry into force of this amending Regulation.

Power is delegated to the Commission to adopt the regulatory technical standards referred to in the first subparagraph in accordance with Articles 10 to 14 of Regulation (EU) No 1093/2010.”;

(3) in Article 249(3), the first subparagraph is replaced by the following:

“By way of derogation from paragraph 2, the eligible providers of unfunded credit protection listed in point (g) of Article 201(1) shall have been assigned a credit assessment by a recognised ECAI which was credit quality step 2 or above at the time the credit protection was first recognised and is currently credit quality step 3 or above.”;

(4) in Article 256, the following paragraph (6) is inserted:

"For the purpose of calculating the attachment points (A) and detachment points (D) of a synthetic securitisation, the originator institution of the securitisation shall treat the exposure value of the securitisation position corresponding to synthetic excess spread referred to in point (e) of Article 248 as a tranche, and adjust the attachment points (A) and detachment points (D) of the other tranches it retains by adding that exposure value to the outstanding balance of the pool of underlying exposures in the securitisation. Institutions other than the originator institution shall not make this adjustment.";

(5) the following Article 269a is inserted:

"Article 269a

Treatment of non-performing exposures (NPE) securitisations

[1. The risk weight for a position in an NPE securitisation shall be calculated in accordance with Article 254, subject to a floor of 100%.

2. By way of derogation from paragraph 1, institutions shall assign a risk weight of 100% to the senior securitisation position in a traditional NPE securitisation, provided the exposures in the pool backing the securitisation have been transferred to the SSPE with a non-refundable purchase price discount of at least 50% on the nominal amount of the exposures as of the securitisation's origination cut-off date.

3. Institutions that pursuant to Chapter 3 of this Title are not permitted to use own estimates of LGD and conversion factors with respect to the exposures of the pool shall not be permitted to use the SEC-IRBA for the calculation of risk-weighted exposure amounts for a position in an NPE securitisation and shall also not be permitted to use paragraph 4.]

4. For the purposes of Article 268(1), expected losses associated with positions in an NPE securitisation shall be included after deduction of the non-refundable purchase price discount that meets the condition set out in paragraph 2 of this Article and, where applicable, any additional specific credit risk adjustments.

5. For the purposes of this Article, 'NPE securitisation' means NPE securitisation as defined in point (24) of Article 2 of Regulation (EU) 2017/2402.";

(6) Article 270 is replaced by the following:

"Article 270

Senior positions in STS on-balance-sheet securitisation

(1) An originator institution may calculate the risk-weighted exposure amounts of an STS on-balance-sheet securitisation as referred to in Article 26a(1) of Regulation (EU) 2017/2402 in accordance with Articles 260, 262 or 264 of this Regulation, as applicable, where both of the following conditions are met:

(a) the securitisation meets the requirements set out in Article 243(2);

(b) the position qualifies as the senior securitisation position.

(2) The EBA shall monitor the application of paragraph 1 of this Article in particular with regard to:

(a) the market volume and market share of STS on-balance sheet securitisations in respect of which the originator institution applies paragraph 1, across different asset classes;

(b) the observed allocation of losses to the senior tranche and to other tranches of STS on-balance sheet securitisations, where the originator institution applies paragraph 1 in respect of the senior position held in such securitisations;

(c) the impact of the application of paragraph 1 on the leverage of institutions;

(d) the impact of the use of STS on-balance sheet securitisations in respect of which the originator institution applies paragraph 1 on the issuance of capital instruments by the respective originator institutions.

(3) The EBA shall publish a report on its findings to the Commission [by 24 months after the date of entry into force].

(4) By [30 months after the date of entry into force] the Commission shall, on the basis of the EBA report referred to in paragraph 2, submit a report to the European Parliament and the Council on the application of this Article with particular regard to the risk of excessive leverage and to the potential substitution of the issuance of capital instruments by originator institutions due to the use of STS on-balance-sheet securitisations qualifying for the treatment in accordance with aragraph 1, together with a legislative proposal for amending this Article, if appropriate."

(7) the following Article 494c is inserted:

"Article 494c

Grandfathering of securitisation positions

By way of derogation from Article 270, an originator institution may calculate the risk-weighted exposure amounts of a senior securitisation position in accordance with Articles 260, 262 or 264 where both the following conditions are met:

(a) the securitisation was issued before [date of entry into force];

(b) the securitisation met the conditions laid down in Article 270 as applicable on [day before date of entry into force]."

Article 2

Entry into force

(1) This Regulation shall enter into force on the twentieth day following that of its publication in the *Official Journal of the European Union*.

(2) By way of derogation from paragraph 1, points (2) and (4) of Article 1 shall apply from [entry into force of this Regulation + 12 months].

Done at Brussels,

For the European Parliament	For the Council
The President	The President