

# Comments

*on the EBA Draft guidelines on the determination of the weighted average maturity (WAM) of the contractual payments due under the tranche*

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# Questions

## Question 1

Do you agree that the contractual payments due under the contract that provides credit protection by virtue of which the credit risk is transferred, and not those contractual payments of the borrowers in relation to the underlying exposures, are the ones to be considered for determining the WAM of a tranche in a synthetic securitisation from a regulatory perspective? If not, please provide evidence supporting your views. (p. 18)

We acknowledge that in a synthetic transaction there are no contractual payments of the borrowers as such which, from a legal point of view, seem suitable for distribution to tranches. However, the outstanding guaranteed tranche amounts in a synthetic securitisation are, in fact, dependent on borrowers' principal payments. In other words, from an economic point of view, borrowers' principal payments are taken into account in the definition of the outstanding guaranteed tranche amounts. For that reason, we propose taking reductions in outstanding tranche amounts into consideration when calculating the tranche WAM and defining such reductions as equivalent to a contractual payment. Of course, premia paid under the guarantee agreement would also count as a contractual payment for such purpose.

## Question 2

Do you agree that, in the case of funded credit protection, the reimbursement of the collateral pledged, and any interest or coupons collected by the protection providers from the collateral, should be considered contractual payments due under the tranche along with the premia, as referred to between brackets, and highlighted in italic, in paragraph 20 of the Rationale; paragraphs 12, 57 and 64 of the draft guidelines; and paragraphs 7, 13 and 14 of the impact assessment? If not, please provide evidence supporting your views. (p. 19)

It is proposed in this consultation paper that, in the case of funded credit protection, the reimbursement of the collateral pledged should be considered a contractual payment due under a tranche. The reimbursed amount of collateral mirrors the borrowers' principal payments. As already stated in our reply to question 1, we wish to propose including such amounts in the definition of contractual payments for the purpose of determining the tranche WAM.

## Question 3

Do you agree that zero prepayments should be assumed on the performing portfolio for calculating the WAM of a tranche? Do you think that such assumption has a significant impact on the calculation of risk-weighted exposure amounts for certain asset classes or for certain tranches, depending also on their seniority? If so, please provide evidence supporting your views. (p. 25)

The zero prepayments assumption is a simplification which is highly unlikely to hold true for any portfolio and/or asset class in reality. For that reason, we support the idea to incorporate a zero prepayments

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assumption whenever the assumption is reasonable. Moreover, we would appreciate the additional option to incorporate own estimates of prepayment rates in the calculation of the WAM.

This is, for example, pertinent in regard to automobile asset backed securities (ABSs). It should in any event be possible to take prepayments into account to ensure as realistic as possible a portfolio scenario. In the case of automobile ABSs, for example, repayment rates of partly well over 10% have been reported during the past seven years. This shortens the maturity of the respective securitisation tranche, which should also be reflected in the calculation of the WAM. Otherwise investors would incur an unreasonable, incorrect extra burden as a result of an incorrect, excessively high WAM.

**Question 4**

Do you agree that zero defaults should be assumed on the performing portfolio for calculating the WAM of a tranche? Do you think that such assumption has a significant impact on the calculation of risk-weighted exposure amounts for certain asset classes or for certain tranches, depending also on their seniority? If so, please provide evidence supporting your views. (p. 27)

The proposal to assume zero defaults on the performing portfolio would be easy to implement and would be a pragmatic way to achieve a uniform, simple calculation. If this approach is adopted, it should, however, be ensured that performing and non-performing exposures are differentiated on the basis of a data field that will have to be reported in future in accordance with the still-to-be-adopted technical standards prepared by the ESMA on disclosure requirements under the Securitisation Regulation. In this context, it should be made sure by way of an appropriate requirement/reference to the Delegated Regulation or, as the case may be, the draft Regulation that this does in fact happen.

However, the zero defaults assumption is a simplification which is highly unlikely to hold true for the majority of portfolios and/or asset classes in reality. For that reason, we support the idea to incorporate a zero defaults assumption whenever the assumption is reasonable. Moreover, we would appreciate the additional option to incorporate own estimates of default rates in the calculation of the WAM.

**Question 5**

Do you consider the assumption that, in the case of the existing non-performing exposures at the time of the calculation of WAM, the principal and interest payments in respect of such exposures throughout the life of the securitisation should be assumed zero, and the asset model should also assume that no exposure will cure in the future, reasonable? If not, would the added complexity introduced by a differentiated modelling of payments received on non-performing exposures be justified in terms of the impact on risk-weighted exposure amounts? If so, could you provide evidence supporting your views? [Please substantiate your views.] (p. 28)

As regards traditional securitisations, we refer to our reply to question 4. The proposal that the principal and interest payments for non-performing exposures should be assumed zero would likewise be easy to implement and would be a pragmatic way to achieve a uniform, simple calculation. This, however, presupposes that performing and non-performing exposures are differentiated on the basis of a data field that will have to be reported in future in accordance with the still-to-be-adopted technical standards prepared by the ESMA on disclosure requirements under the Securitisation Regulation. In this context, it

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should be made sure by way of an appropriate requirement/reference to the Delegated Regulation or, as the case may be, the draft Regulation that this does in fact happen.

The following refers to synthetic securitisations only:

Given that an originator institution has extensive knowledge of the historic performance of the securitised portfolio and is, in addition, required to demonstrate a comprehensive significant risk transfer assessment to competent authorities, it may be assumed that the originator has a good idea of the future performance of the non-performing exposures in terms of interest and principal payments/recoveries. We would therefore consider it an oversimplification to assume zero future interest and principal payments.

**Question 6**

In synthetic securitisations, do you agree that no modelling of future non-occurred losses should be allowed in order to calculate the future outstanding balance of the underlying portfolio and the tranches? Or do you think that the modelling of losses should be taken into account? If so, could you provide the rationale supporting your views and the impact on risk-weighted exposure amounts? (p. 35)

It is our understanding that the modelling of losses should be allowed in order to determine the tranche WAM. The information needed for this is at hand in any event. In fact, synthetic securitisations claiming that significant credit risk has been transferred to third parties are subject to a comprehensive assessment. The assessment focusses in particular on the transaction's performance throughout the lifetime of the transaction. We believe it is fair to assume that the originator has a good idea of the future performance of the portfolio.

**Question 7**

In synthetic securitisations, do you agree that only clean-up calls in accordance with Article 245(4)(f) of the CRR should be taken into account to determine the WAM? In your view, should time calls, which can be exercised by the protection buyer after the WAL of the underlying portfolio (as defined in paragraph 53 of the Guidelines on the STS criteria for ABCP securitisation), also be taken into account? If so, could you provide the rationale supporting your views and the impact on risk-weighted exposure amounts? (p. 35)

We believe it is reasonable to include time calls in the calculation of the tranche WAM.

**Question 8**

What are your views on the model validation and quality review of the asset and liability models and on due diligence on third party model providers? Do you perceive it as too burdensome? If so, please provide alternative proposals to account for compliance of third party model providers with these guidelines and for the assessment of the quality and accuracy of the asset and liability models (p. 37)

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Initial, plus annual internal or external, validation of the model is too burdensome and unlikely to provide any substantially better assumptions for tranche WAMs. We propose validating each model initially but not on an ongoing basis.

This would be in line with established and proven market practice.

**Question 9**

Are there any other issues that you would consider necessary to comment on? If so, please provide them with the alternatives to the wording adopted in these draft guidelines (p. 38)

No comment.