
Consultation response

ESMA Consultation Paper: Draft Guidelines on securitisation repository data completeness and consistency thresholds

Response on behalf of AFME Members

12 March 2020

General points

Scope of guidelines

AFME members are conscious of the scope of application of the draft guidelines and our comments are made in reliance on that scope. That is to say, because the guidelines are intended to be applicable to securitisation repositories and only "public" securitisations¹ need report to securitisation repositories².

AFME members strongly support the limitation on the usage of ND responses to public securitisation markets only.

This is because, as has been made clear in many representations by AFME (and others) over the years, the private securitisation markets are fundamentally different to the public markets. The private markets are characterised by an even greater level of investor sophistication than public markets and far greater investor power than public markets. Investors in private transactions do their own very technical analysis and credit assessments and will not invest unless they have sufficient data from sell-side entities on a transaction that they have determined is "sufficiently representative" (taking into account any use of ND1-4 responses) such that they can properly assess their investment and fulfil their due diligence obligations under Article 5 of the Securitisation Regulation. Where it is not sufficient, investors in private markets have the commercial power to require appropriate data to be supplied.

Separate treatment of ND1 as compared to ND2-4

AFME members believe that ND1 (like ND5) is a qualitatively different kind of "no data" response and should be treated differently. While ND2-4 responses are all appropriate in circumstances where the information is "credit relevant" and has been collected at origination of the asset, ND1 reflects circumstances where the information has not been collected "because it was not required by the lending or underwriting criteria at the time of origination". This, in turn, suggests that that information was judged by the originator not to be credit relevant. In turn, because it is not relevant to the assessment of the credit of the underlying exposure in question, its absence from loan-level data reporting to investors would cause no harm to those investors. AFME members would generally expect that any field reported initially as ND1

¹ That is, securitisations in relation to which there is an obligation to publish a prospectus under Regulation (EU) 2017/1129.

² That is, not securitisations in relation to which no obligation to publish a prospectus arises under Regulation (EU) 2017/1129.

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would continue to be reported in that way as it is not relevant to credit assessment by either the originator or the investors. It therefore would not be sensible to build IT systems to collect that information.

By way of example, in Annex II, information on the primary income of the obligor (fields RREL16-19, none of which permit an ND5 response) will be irrelevant to the underwriting of a buy-to-let mortgage where the lending decision is made solely on the basis of the rental income from the property – which will frequently be the case. There should be no expectation that this information will be collected in the future because its omission is intentional and in accordance with sound underwriting practices for the originator. Forcing originators to use 4 of their "legacy IT systems" allowance to report this as ND1 is not appropriate.

There are other, more "technical" cases for this approach to ND1 as well. For example, Annex IV, CRPL10 requires reporting of the geographic region of an underlying exposure using NUTS3 classifications. This can be done even for non-EU jurisdictions because there are adaptations (using a two digit country code followed by "ZZZ"). But CRPL11 requires entities to report the year of the NUTS3 classification used, and does not permit the use of ND5 (which AFME members would suggest is the most appropriate response where all of the assets report a non-EU jurisdiction under CRPL10). In the absence of ND5 as an option, reporting entities will most likely use ND1 as a response for CRPL11, as it is the closest to an appropriate response available. This use of ND1 will have to continue indefinitely, since it is not possible to "collect" this information in respect of a non-EU portfolio.

In order to solve these problems, AFME members would suggest that ND1 is treated in the same way as ND5. Complete information is not an appropriate policy objective in itself where information completeness refers to providing information that is irrelevant to the credit assessment made by commercial parties to transactions, and the information completeness rules and guidance should reflect this. To do otherwise would be to impose differential obligations on providers of finance based on how they fund themselves. Those who fund themselves via securitisation would find themselves at a competitive disadvantage compared to those who fund themselves via other means³. The requirement to collect irrelevant information would be costly for originators (because of the time and resources required to collect the information and build appropriate reporting systems) and would risk putting customers off by requiring them to provide information that is not relevant to the underwriting process. ND1 should therefore be excluded from the limitations on use of ND responses, which limitations should properly apply only to ND2-4 responses.

Use of ND1-4 options by non-EU originators

AFME members would also draw to ESMA's attention that non-EU domiciled originators may be required contractually by EU institutional investors to complete the ESMA templates as a result of the Article 5(1)(e) due diligence requirement and EU entities must in any case do so in relation to non-EU originated assets. In some cases, reporting of the information required by the templates will be restricted by relevant (non-EU) banking secrecy laws. The result of this, in turn, is that the relevant information is not collected or loaded into the reporting systems because there is a relevant regulatory prohibition on doing so. For example, Swiss banks would generally need to report CRPL16 through CRPL23 using ND1-4 options in order to comply with Swiss banking secrecy laws. AFME members believe that the use of ND1-4 responses for reasons of regulatory compliance should be unrestricted, and therefore excluded from the "legacy assets" and "legacy IT systems" field allowances proposed in the Consultation Paper.

This problem is not merely theoretical, nor is it a case of non-EU entities having to comply due to their own voluntary, transaction-related decisions. Because the direct obligation under Article 7 will fall on any EU-regulated originator, sponsor or SSPE, this type of issue will sometimes arise because e.g. an EU-

³ This is already the case in many respects, of course, but this would make things even worse.

established SSPE is used for assets originated by a non-EU originator. It will also arise frequently for EU-established originators with large non-EU footprints.

Responses to specific questions

Q1. Do you agree with the guiding principles used for developing the thresholds, as discussed in this section (section 3.1)?

As a general matter, AFME members agree with the principles set out in section 3.1 for how thresholds should be set. In particular, AFME members would emphasise the importance of consulting with market participants before making any adjustments to thresholds, as market participants will inevitably have a store of accumulated experience that may not be obvious from raw data but is nonetheless highly relevant when setting appropriate rules.

AFME members would also like to highlight their strong support for the principle that it will sometimes be appropriate to set thresholds that are set for specific categories of securitisations within each type of underlying exposure. One example of this that is particularly relevant is synthetic securitisations. Because synthetic securitisations have not historically been eligible for use as collateral with the ECB, the data used for the threshold calibrations and the calibration of maximum number of legacy assets fields and legacy IT systems fields will not be relevant for determining the level of ND1-4 responses reasonably required for synthetic securitisations. What is more, many of the data fields required for e.g. corporate loan exposures under Annex IV have not historically been reported for synthetic securitisations and will therefore not be available in the originators' system used for managing and reporting synthetic securitisations – precisely the kind of situation ND1-4 responses are designed to address. By way of example, extended cash-flow information, interest rate and margin information is important for true sale securitisations because the cash-flows for paying off the securitisation instruments comes from the underlying assets. None of this information is relevant for synthetic securitisations (and therefore is often not caught in synthetic securitisation reporting systems) because payments on the securitisation instruments depends on the premium payable by the originator for the protection. For this reason, AFME members believe that synthetic securitisations (regardless of the asset class of the underlying) should benefit from the same approach as is being applied to ABCP, NPE and esoteric reporting – with the allowance for each of legacy assets and legacy IT systems fields being set at a level that is equal to the number of fields for which an ND1-4 response is permitted.

Q2. Do you agree with the proposed calibration approach and proposal for the percentage threshold, as discussed in this section (section 3.4)?

AFME members believe the calibration approach is generally sensible. That said, there is an exception to this in respect of relatively non-granular portfolios, such as CMBS transactions, where there would typically be fewer than 10 loans/exposures underlying the transaction. The calibration approach, and the setting of the threshold between "legacy assets" and "legacy IT systems" at 10% means in practice that such transactions do not benefit from the "legacy assets" allowance, since a single asset having an ND1-4 response in respect of a particular field will always mean that over 10% of assets are reporting an ND1-4 response. In respect of any securitisation with fewer than a certain number assets, therefore, AFME members would suggest combining the allowance for legacy assets fields and legacy IT systems fields and applying that allowance overall to the number of fields with any ND1-4 responses. So, for example, in respect of a CMBS transaction with three underlying loans, there would be a single allowance of 100 fields where it is permitted to have ND1-4 responses in respect of any asset (although as a practical matter only 75 fields permit ND1-4 responses at all, so the cap would functionally be 75). AFME members would be pleased to engage further with ESMA to discuss the threshold number of assets for which this approach would be appropriate.

Q3. Do you agree with the proposed calibration approach and proposal for the 'number of legacy assets fields' thresholds, as discussed in this section (section 3.5)?

Whilst we appreciate the significant effort that ESMA has clearly put into analysing the available ECB data, as well as understanding that sources of real-world data may be limited, we would highlight that in certain circumstances the size of the available reference transactions is very limited:

- All data comes from a self-selecting set of transactions. Those transactions where the ECB has data (even before data quality requirements were introduced) will be transactions selected by participants who were happy for loan-level data to be reported when it was not a strict legal requirement. In general, that will skew the selection of transactions toward those with more complete and better quality data than the average in the market. Setting standards for the whole market on the basis of data from this self-selecting pool must therefore be done with great care, allowing significant margins for error.
- In respect of commercial real estate and credit cards, there is no data at all.
- For Annex IV, only SME transactions are referenced, meaning the data used to calibrate is inappropriate for securitisations of large corporate exposures, which are materially different in their features, data collection and sensitivities. In particular, banks may use a different capital model and approach in managing large corporate clients vs. SME clients, which can result in different systems and data capturing for these two different categories of clients. Large corporate exposures are also typically securitised using different techniques with different requirements and approaches to data, such as synthetic securitisation – as to which see our answer to Q1 above – or securitising parts of the loan in managed CLOs. Analysis from one AFME member of their own books suggests that they would initially need an allowance of 39 "legacy IT systems" fields in reporting their large corporate book, compared to the allowance of 20 fields set out for that annex in the Consultation Paper.
- Consumer securitisations had only 28 in-scope transactions.
- Leasing securitisations had only 41 in-scope transactions.

Any limitation in available reference transactions clearly limits the effectiveness of any analysis performed, with a risk that the final thresholds are not representative of actual transactions under the new ESMA reporting framework.

Further, the Consultation Paper is explicit that, in setting limits on the number of legacy assets and legacy IT systems fields, ESMA has “also consider[ed] the expansion of new data fields in ESMA disclosure templates in comparison to ECB templates”. Whilst acknowledgement of the fact that the ESMA templates contain a number of new fields that are not included in the ECB templates is welcome, there is no information provided regarding how these new fields have been considered when producing the proposed number of permitted legacy assets and legacy IT systems fields. When then reviewing these limits in detail, it is clear that certain fields, despite being new, are not considered additive to the level at which the limits are set – that is, there appears to be an assumption that some of these fields will not pose an issue for market participants, despite there being no historical data to confirm this.

As an example, Table 4 in the Consultation Paper shows that for the autos asset class, based on ECB data, four legacy assets fields should be permitted, but the proposed Guidelines then set the limit at 15. Whilst AFME members agree that a “buffer” is required, European DataWarehouse analysis shows the ESMA autos template as having 18 new fields where ND1-4 is allowed – that is, not all new fields where ND1-4 responses are permitted have been included in the buffer. Further examples include the following:

Asset class	“Buffer” (number of data fields)	Number of new data fields (ND1-4)
Autos	11	18
Consumer	8	18
Leasing	6	16
Residential mortgage	8	20
Corp/SME	9	24

As a comparison, where no ECB data was available at all for an asset class (i.e. ABCP, NPE, Esoteric), legacy assets fields limits were set to match the total number of ND1-4 fields (i.e. functionally, no limit on the use of ND1-4 responses has been suggested – an approach we support in relation to these templates).

AFME members also have concerns regarding potential future changes to proposed maximum permitted number of both ‘legacy asset’ and ‘legacy IT system’ fields. Whilst market participants are already employing significant resources, with associated costs, in service of enhancing systems and data in line with ESMA requirements, there should be recognition that there may be some fields that can never be populated. Such fields should be analysed and well understood, to ensure they are factored in any proposed changes to the legacy asset and legacy IT system allowances.

One example is the provision of borrower income data in the autos (Annex V) loan-by-loan template. Originators may currently not collect and retain this data at loan origination in all cases, in accordance with typical underwriting practices common in the auto loan market in a particular jurisdiction. Were thresholds to be reduced such that this data *had* to be collected going forwards, this could place an originator at a competitive disadvantage when compared to those originators that do not intend to securitise their assets. This issue is further compounded when considering that although this example only really relates to one piece of information (a borrower’s income) the template splits it across four separate data fields (AUTL16-19) – meaning ND1-4 responses for approximately 25% of the 15 fields allowed to be legacy IT systems fields.

As with changes to the threshold between legacy assets and legacy IT systems, AFME members also strongly support the suggestion that any future changes to the maximum number of legacy assets or legacy IT systems fields should be subject to prior consultation with market participants.

Q4. Do you agree with the proposed calibration approach and proposal for the ‘number of legacy IT system fields’ thresholds, as discussed in this section (section 3.6)?

ESMA has included “buffers” on top of the maximum number of legacy IT systems fields determined based on the ECB data, which members agree are required given that the ESMA templates are new requirements for many market participants, and also because the ESMA templates include a number of additional fields on top of the ECB templates on which they are based. However, no information is provided on how these buffers have been determined, and different approaches appear to have been used for different asset classes. For example, for the consumer asset class the buffer is eight (seven to 15 data fields), but for leasing it is only one (14 to 15). Could ESMA please provide further details on the rationale and analysis used to produce these buffers?

Please also see our response to Question 3 above regarding the representativeness of the ECB data, which is also applicable to the maximum number of ‘legacy IT system’ fields permitted.

Q5. Do you have any comments on the threshold revision process? Are there any other aspects on this topic that are missing in your view and should be taken into consideration?

AFME members in general support the approach proposed. In particular, we support not setting a particular timeframe for the revision of the thresholds, and that they should be revisited as frequently as necessary in future when sufficient data has been collected to permit reliable recalibration exercises to be carried out.

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