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Contact:

Mr Matti LEPPÄLÄ, Secretary General/CEO

Koningsstraat 97, rue Royale – 1000 Brussels

Tel: +32 (0)2 289 14 14 – Fax: +32 (0) 289 14 15

Matti.leppala@pensionseurope.eu

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PensionsEurope’s response to the European Commission’s public consultation on an EU framework for simple, transparent and standardized securitization

PensionsEurope welcomes the opportunity to reply to the European Commission’s consultation on securitization.

Please find below an executive summary and our response to a selection of questions.

Executive Summary

PensionsEurope supports the Commission’s initiative to develop an EU framework for simple, transparent and standardized securitization. We agree with the European Central Bank and the Bank of England which note that “some securitizations may further provide long-term investors, such as (...) pension funds, with a broader pool of assets that are genuinely low-risk from a credit perspective, alongside government bonds.”¹

First and foremost, we believe that a new EU securitization framework should be internationally consistent. Hence, we suggest to align any future EU legislative measure with the Basel Committee/IOSCO recommendations and to harmonize the regulatory definitions of securitizations typologies existing across the EU.

The standardization of definitions, of information disclosure and of performance metrics across the EU could have a positive impact on the development of EU securitization markets, help ease investors’ analysis and increase the comparability of securitization instruments across the EU. The development of high quality securitization should not prevent however the development of other, non-standardized, securitized products.

¹ Discussion Paper, “The case for a better functioning securitization market in the European Union”, prepared by Bank of England and European Central Bank staff, May 2014

Secondly, PensionsEurope is of the view that the harmonization of regulatory frameworks in the EU could enable a level-playing field for investors and issuers in European securitizations. For instance, the existence of different insolvency regimes in each Member State makes Europe-wide securitisation very difficult. A harmonization of tax treatments and bankruptcy law could be helpful, but we are well aware that it will be a long way to achieve a harmonization in the abovementioned policy areas.

Thirdly, it is important to increase the transparency of data and their availability for investors, especially considering the complexity of securitizations. For instance, for qualifying securitizations we consider that the European DataWarehouse is very helpful for investors. The reference to such data platforms should however not be made mandatory.

It is crucial to remove existing barriers, such as the high due diligence costs for investors, in order to improve the attractiveness of the securitization market for pension funds.

Finally, as a general comment, we would like to stress that this and other Commission's upcoming initiatives and policy measures should be aligned with the objective of creating a Capital Markets Union. In this context, we are very concerned that EIOPA's work – fully on its own initiative – on the Holistic Balance Sheet approach (HBS approach) will discourage the participation of pension funds in this market and prevent from investing in long-term assets. The EU should definitely not copy the Solvency II framework to IORPs, while inadequately taking into account isolated characteristics of occupational pensions. The introduction of Solvency-II-style capital requirements would hamper sensible and desirable long-term investment by IORPs, rather than supporting it; and this would also negatively impact the potential of pension funds as investors in securitisations.

PensionsEurope member organisations cover the workplace pensions of about 70 million European citizens. Through its Member Associations PensionsEurope represents more than € 3.5 trillion of assets managed for future pension payments.

Question 5:
A. What impact would further standardization in the structuring process have on the development of EU securitization markets?

PensionsEurope supports the Commission's initiative to develop an EU framework for simple, transparent and standardized securitization. PensionsEurope's members agree that improving the transparency of the securitizations market would improve the attractiveness of securitization to investors.

More precisely, PensionsEurope believes that the standardization of definitions, of information disclosure and of performance metrics across the EU could have a positive impact on the development of EU securitization markets, help ease investors' analysis and increase the comparability of securitization instruments across the EU. Moreover, standardisation could positively affect the demand for

securitisation, for instance for Asset Backed Securities which availability is currently limited. One example where we note that this has happened is in the residential mortgage-backed securities (RMBS) market, where standardisation has played an important role in increasing the attractiveness of RMBS investments in the market.

Importantly, an EU initiative should aim at making all elements transparent and well-explained. Standardization and transparency should go hand in hand.

PensionsEurope believes that the creation of a single European securitization structure should not be exclusively based on standardized securitization, but should be flexible, without preventing investors from investing in non-standardized products.

B. Would a harmonised and/or optional EU wide initiative provide more legal clarity and comparability for investors? What would be the benefits of such an initiative for originators?

No comments.

C. If pursued, what aspects should be covered by this initiative (e.g. the legal form of securitisation vehicles, the modalities to transfer assets, the rights and subordination rules for noteholders)?

In our opinion the mentioned aspects in brackets are good examples for a possible standardization.

D. If created, should this structure act as a necessary condition within the eligibility criteria for qualifying securitisations?

No, this structure should not act as a condition within the eligibility criteria for qualifying securitizations. As mentioned under 5A, the creation of standardized securitization will be a positive development however the development of high quality securitization should not prevent the development of other, non-standardized, securitized products.

Question 6:

A. For qualifying securitisations, what is the right balance between investors receiving the optimal amount and quality of information (in terms of comparability, reliability, and timeliness), and streamlining disclosure obligations for issuers/originators?

B. What areas would benefit from further standardisation and transparency, and how can the existing disclosure obligations be improved?

C. To what extent should disclosure requirements be adjusted – especially for loan-level data – to reflect differences and specificities across asset classes, while still preserving adequate transparency for investors to be able to make their own credit assessments?

It is important to increase the transparency of data and their availability for investors, especially considering the complexity of securitizations. For instance, for qualifying securitizations we consider that the European DataWarehouse (ED) is very helpful for investors. The reference to such data platforms should however not be made mandatory and therefore securitizations should still be allowed to be marketed and invested without being referred to on such platforms.

Question 7:

A. What alternatives to credit ratings could be used, in order to mitigate the impact of the country ceilings employed in rating methodologies and to allow investors to make their own assessments of creditworthiness?

PensionsEurope supports the development of alternatives to credit ratings which would allow investors to make their own assessments of creditworthiness; however PensionsEurope opposes requiring investors to conduct creditworthiness assessments by their own. Pension funds should be able to continue relying on credit ratings, as the latter represent a valuable tool to evaluate the credit worthiness of financial instruments. This is important for instance for smaller pension funds as their capacity to conduct assessments by their own is limited. Consequently, credit ratings should remain an available tool indicating the specific characteristics of securitization.

As regards the alternatives, we consider that in order to allow investors to make their own assessments, investors should be provided with the same level of transaction information than credit ratings. Therefore we call on the Commission to propose measures that would improve the availability of data and transaction information to investors. This would be also aligned with the objective of improving the transparency and the comparability between securitized products.

B. Would the publication by credit rating agencies of uncapped ratings (for securitization instruments subject to sovereign ceilings) improve clarity for investors?

Indeed. Complete disclosures of the rating process can help investors to understand, evaluate external ratings and compare products issued in different member states.

Question 13:

Are there wider structural barriers preventing long-term institutional investors from participating in this market? If so, how should these be tackled?

The creation of an EU framework could open capital markets finance for e.g. SMEs – and under the right conditions create an asset class for institutional investors such as pension funds. However, securitization shouldn't be a matter of simply taking loans off bank balance sheets and selling them on to pension funds. It should be instead a tool that facilitates co-financing of loans by banks and pension funds.

Secondly, it is important to increase the transparency of data and their availability to investors, especially considering the complexity of securitizations. For instance, we consider that the European

DataWarehouse is very helpful in the context of qualifying securitizations. The reference to such data platforms should however not be made mandatory.

Thirdly, it is crucial to minimize due diligence costs for investors in order to improve the attractiveness of securitization market for pension funds.

The removal of structural barriers might enable those pension funds that are willing to participate in the securitization markets to do so. The European Commission could take action to remove these barriers, for instance by clarifying rules and wider ratios for securitization assets (e. g. ABS), decreasing due diligence costs for ABS investments, requesting originators to make available relevant information in order to facilitate due diligence by investors, improving legal certainty and improving disclosure rules.

Overall, the structural barriers preventing pension funds from participating in this market are the following:

- Unclear national rules and wider ratios for securitization assets (e. g. ABS)
- High due diligence costs, for instance for ABS investments
- Too burdensome requirements of verifying risk retention
- Non-availability of relevant information on the securitization products
- Lack of legal certainty (including on bankruptcy rules) and for instance regarding the compliance with risk retention requirements
- Lack of a clear and stable tax treatment
- Unbeneficial prepayment and disclosure rules

PensionsEurope is of the view that the harmonization of regulatory frameworks in the EU could enable a level-playing field for investors and issuers in European securitizations. For instance, the existence of different insolvency regimes in each Member State makes Europe-wide securitisation very difficult. A harmonization of tax treatments, bankruptcy law and of securitization markets across Europe could be helpful, but we are well aware that it will be a long way to achieve a harmonization in the abovementioned policy areas.

Please note that some pension funds currently want to reduce their exposure to complex products and asset classes, and they expect securitized products to remain highly complex. Therefore, alternative options such as private placements could be considered as well.

Finally, we would like to stress that this and other Commission's upcoming initiatives and policy measures should be aligned with the objective of creating a Capital Markets Union. In this context, we are very concerned that EIOPA's work – fully on its own initiative – on the Holistic Balance Sheet approach (HBS approach) will discourage the participation of pension funds in this market and prevent from investing in long-term assets. The EU should definitely not copy the Solvency II framework to IORPs, while inadequately taking into account isolated characteristics of occupational pensions. The introduction of Solvency-II-style capital requirements would hamper sensible and desirable long-term investment by IORPs, rather than supporting it; and this would also negatively impact the potential of pension funds as investors in securitisations.