



Consultation Paper | CP10/21

# Implementation of Basel standards: Non-performing loan securitisations

June 2021





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Responses are requested by Monday 26 July 2021.

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Alternatively, please address any comments or enquiries to:

Securitisation Policy  
Prudential Regulation Authority  
20 Moorgate  
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## 1 Overview

1.1 This Consultation Paper (CP) sets out the Prudential Regulation Authority's (PRA) proposed rules in respect of the implementation of updated prudential standards agreed by the Basel Committee on Banking Supervision (BCBS) for non-performing loan (NPL) securitisations. It sets out how the PRA proposes to define non-performing exposure (NPE) securitisations, and also proposes changes to the associated capital treatment.

1.2 The proposals in this CP would result in the addition of a new Non-Performing Exposure Securitisation Part of the PRA Rulebook (Appendix 1), and amendments to Supervisory Statement (SS) 10/18 'Securitisation: General requirements and capital framework' (Appendix 2).<sup>2</sup>

1.3 The proposals in this CP are relevant to all PRA-authorised firms to which the Capital Requirements Directive (CRD) applies.<sup>3</sup>

1.4 This CP sets out the PRA's proposals on how firms are to capitalise NPE securitisations. The PRA does not expect that firms would incur material additional costs as a direct result of the proposals.

1.5 A revised securitisation capital framework was implemented via the Capital Requirements Regulation (CRR)<sup>4</sup> and Policy Statement (PS) 29/18 'Securitisation: The new EU framework and Significant Risk Transfer'<sup>5</sup> in order to tackle shortcomings in the framework as observed during the global financial crisis. However, those Basel standards did not provide any specific treatment for securitisations of NPLs.<sup>6</sup> In order to address this gap, in Q4 2020 the BCBS published a technical amendment with a bespoke treatment for NPL securitisations.<sup>7</sup> The amendment is for implementation no later than January 2023. The proposals in this CP aim to implement the amendment in the UK.

1.6 In developing the proposals, the PRA has considered the interaction between its primary and secondary objectives and the matters it is required to 'have regard' to, including (for these proposed rules) international standards, relative standing of the UK, and finance for the real economy (see Chapter 3 for further details). The PRA considers that its proposed approach to the capital treatment of NPE securitisations promotes its primary objective, as there are safety and soundness benefits to a more appropriately calibrated NPE securitisation framework, and as a consequence, improved market functioning.

1.7 In addition, when making CRR rules, the PRA must consider and consult HM Treasury about the likely effect of the rules on 'relevant' equivalence decisions, as notified to it by HM Treasury.

1.8 The proposals in this CP relate specifically to the capital treatment of NPE securitisations. The PRA considers that the NPE securitisations tool can allow firms to gain additional certainty on their balance sheets, which could potentially free up capital that can support lending to the real economy.

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<sup>2</sup> November 2018: <https://www.bankofengland.co.uk/prudential-regulation/publication/2018/securitisation-general-requirements-and-capital-framework-ss>.

<sup>3</sup> The onshored and amended UK version of Regulation (EU) No 575/2013 of the European Parliament and of the Council of 26 June 2013 on prudential requirements for credit institutions and investment firms and amending Regulation (EU) No 648/2012.

<sup>4</sup> The onshored and amended UK version of Regulation (EU) No 575/2013.

<sup>5</sup> November 2018: <https://www.bankofengland.co.uk/prudential-regulation/publication/2018/securitisation-the-new-eu-framework-and-significant-risk-transfer>.

<sup>6</sup> Basel standards CRE40.

<sup>7</sup> Technical Amendment published November 2020: Capital treatment of securitisations of non-performing loans.

While the PRA does not have the empirical data necessary to estimate the direct impact of the proposals on capital requirements for UK firms given limited NPE securitisations in the UK, a case study within the European Banking Authority (EBA) 2019 opinion on NPE Securitisations suggests that for the securitisation internal ratings based approach ((SEC-IRBA), excluding the foundation approach), and securitisation standardised approach (SEC-SA) there may be a material reduction in capital costs.<sup>8</sup>

### Summary of proposals

1.9 The proposals in this CP include:

- (i) definitions for non-performing exposure securitisations and qualifying non-performing exposure securitisations;
- (ii) revised rules for calculating capital requirements on exposures to NPE securitisations; and
- (iii) a new expectation with regard to NPE securitisations.

### Implementation

1.10 The PRA proposes that the implementation date for the changes resulting from this CP would be Saturday 1 January 2022.

1.11 The PRA's proposals in this consultation would take effect in conjunction with any consequential amendment to the CRR by HM Treasury.

1.12 The PRA has consulted with the Financial Conduct Authority (FCA) on the proposals in this consultation. Responses to this CP will be shared with the FCA where they affect FCA objectives.

### Responses and next steps

1.13 This consultation closes on Monday 26 July 2021. The PRA invites feedback on the proposals set out in this consultation. Please address any comments or enquiries to [CP10\\_21@bankofengland.co.uk](mailto:CP10_21@bankofengland.co.uk).

1.14 The proposals set out in this CP have been designed in the context of the UK having left the European Union and the transition period having come to an end. Unless otherwise stated, any references to EU or EU derived legislation refer to the version of that legislation which forms part of retained EU law.<sup>9</sup> The PRA will keep the policy under review to assess whether any changes would be required due to changes in the UK regulatory framework.

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<sup>8</sup> <https://www.eba.europa.eu/eba-publishes-opinion-regulatory-treatment-non-performing-exposure-securitisations>.

<sup>9</sup> For further information please see <https://www.bankofengland.co.uk/eu-withdrawal/transitioning-to-post-exit-rules-and-standards>.

## 2 Proposals

2.1 The PRA proposes to introduce a definition of, and treatment for, NPE securitisations. The purpose of this proposal is to provide a framework that is more appropriately calibrated for securitisations of NPEs, which have features that distinguish them from securitisations of performing exposures.

2.2 The PRA considers securitisation to be an important element of well-functioning financial markets, since it contributes to diversifying the funding sources of institutions and releasing regulatory capital that can be reallocated to support further lending. Furthermore, securitisation provides institutions and other market participants with additional investment opportunities, thereby allowing portfolio diversification and facilitating the flow of funding to businesses and individuals.

### Definition of non-performing exposure securitisation

2.3 The Basel standards define<sup>10</sup> an NPL securitisation as a securitisation where the ratio of the nominal amount of 'delinquent underlying exposures'<sup>11</sup> to the nominal amount of underlying exposures (a ratio termed 'W') is equal to or higher than 90%.

2.4 The Basel standards restrict NPL securitisations to 'loans, loan-equivalent financial instruments or tradable instruments used for the sole purpose of loan sub participation'. The Basel standards explicitly allow national supervisors the discretion to use a stricter definition of NPL securitisations than the Basel standards, both with regard to the scope of eligible exposures and 'W'.<sup>12</sup>

2.5 The PRA proposes to use the existing CRR definition of NPE to define the underlying assets eligible for a NPE securitisation.<sup>13</sup> The PRA considers that the use of a single definition across the capital framework, that is already familiar to firms, would ensure that its rules remain transparent and proportional, in line with the PRA's duty to have regard to such matters.

2.6 The PRA proposes to define an NPE securitisation as a securitisation backed by a pool of NPEs that make up, at minimum, 90% of the entire pool's nominal value at origination, and at any later stage when assets are added or removed from the underlying pool. Setting the minimum below 100% allows firms to securitise exposures that they expect to become non-performing after execution of the securitisation, or become re-performing in the process of preparing the transaction.

2.7 The Basel standards define the non-refundable purchase price discount (NRPPD) as 'the difference between the outstanding balance of the exposures in the underlying pool and the price at which these exposures are sold by the originator to the securitisation entity, when neither originator nor the original lender are reimbursed for this difference. In cases where the originator underwrites tranches of the NPL securitisation for subsequent sale, the NRPPD may include the difference between the nominal amount of the tranches and the price at which these tranches are first sold to unrelated third parties. For any given piece of a securitisation tranche, only its initial sale from the

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<sup>10</sup> Basel standards CRE45.1.

<sup>11</sup> Basel standards CRE41.7: 'Delinquent underlying exposures are underlying exposures that are 90 days or more past due, subject to bankruptcy or insolvency proceedings, in the process of foreclosure, held as real estate owned, or in default, where default is defined within the securitisation deal documents.'

<sup>12</sup> Basel standard CRE45.2.

<sup>13</sup> Article 47a(3) of CRR.

originator to investors is taken into account in the determination of NRPPD. The purchase prices of subsequent re-sales are not considered.<sup>14</sup>

2.8 The PRA proposes to define the NRPPD in line with the Basel definition.

2.9 The PRA proposes to define a qualifying NPE securitisation as a traditional NPE securitisation, where the NRPPD is at least 50% of the outstanding amount of the underlying exposure at the time they were transferred to the securitisation special purpose entity (SSPE).<sup>15</sup>

### **Fixed risk weight for qualifying senior tranches**

2.10 Where firms use the internal ratings based (IRB) or standardised approach (SA), the Basel standards apply a fixed risk weight of 100% to senior tranches of NPL securitisations when those securitisations are traditional and have an NRPPD that is at least 50% of the outstanding balance of the pool of exposures.<sup>16</sup>

2.11 The PRA proposes to implement a fixed risk weight of 100% for senior tranches of qualifying NPE securitisations where firms use the SEC-IRBA and SEC-SA. The PRA considers that a 100% fixed risk weight for senior tranches of qualifying NPE securitisations is aligned with the standardised approach risk weight for exposures in default, and is consistent with the PRA's safety and soundness objective.<sup>17</sup>

2.12 The PRA also proposes to update SS10/18 to include an expectation that a firm's Senior Management Function (SMF) 16 (Compliance Oversight) should satisfy themselves that performing loans are not being included in an NPE securitisation for the purpose of reducing the capital charge on such loans.

### **Risk weight floor**

2.13 The Basel standards apply a floor of 100% for the risk weights on all NPL securitisations calculated through the SEC-IRBA, SEC-SA, or look-through approach.<sup>18</sup>

2.14 The PRA proposes to implement a 100% risk weight floor for all tranches of NPE securitisations, unless the firm uses the securitisation external ratings based approach (SEC-ERBA) where the PRA does not propose to implement a risk weight floor.<sup>19</sup> Given the unique nature of NPE securitisations, with the underlying securitised exposures being non-performing, the PRA considers this to be in line with its safety and soundness objective.

### **Look-through approach and maximum capital requirements**

2.15 The EU has updated Capital Requirements Regulation: Regulation (EU) No. 575/2013 such that Articles 269a (5) and (6) provide for expected loss pursuant to Articles 267 (look-through approach) and 268 (maximum capital requirements) on a basis net of NRPPD. This is in the context of the senior tranche of qualifying NPE securitisations, and qualifying NPE securitisations respectively.<sup>20</sup>

2.16 The PRA does not propose to adopt the EU approach, as it considers there is insufficient evidence to determine that it would be in line with the PRA's safety and soundness objective. The PRA would welcome evidence from firms that for methods within Articles 267 and 268, an approach net of NRPPD is compatible with the PRA's general objective of safety and soundness. The PRA

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<sup>14</sup> Basel standards CRE45.6.

<sup>15</sup> (13) of Article 242 of CRR.

<sup>16</sup> Basel standards CRE45.5.

<sup>17</sup> Article 127 of CRR.

<sup>18</sup> Basel standards CRE45.4.

<sup>19</sup> Article 263 of CRR.

<sup>20</sup> Regulation (EU) 2021/558 amending Regulation (EU) No 575/2013.

would also welcome evidence that for the look-through approach (Article 267), a risk weight floor below 100% for the senior tranche of qualifying NPE securitisations is compatible with the PRA's primary objective on safety and soundness.

### **Exclusion of foundation approach**

2.17 The Basel standards preclude<sup>21</sup> firms from applying the SEC-IRBA to an exposure to an NPE securitisation when the foundation approach<sup>22</sup> is used to calculate the  $K_{IRB}$ <sup>23</sup> of the underlying pool of exposures.

2.18 The PRA proposes to preclude firms from applying the SEC-IRBA approach to NPE securitisations where a firm applies the IRB Approach to any exposures in the pool of underlying exposures, but does not use own estimates of LGD and conversion factors. This is to prevent eligible firms from applying unduly low risk weights as a result of foundation IRB parameters being used as an input in the SEC-IRBA for NPE securitisations.

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<sup>21</sup> Basel standards CRE45.3.

<sup>22</sup> Basel 30.36: 'Under the foundation approach, banks must provide their own estimates of PD [probably of default] associated with each of their borrower grades, but must use supervisory estimates for the other relevant risk components. The other risk components are LGD [loss given default], EAD [exposure at default] and M [effective maturity].'

<sup>23</sup> Determination of  $K_{IRB}$ , Article 255 of CRR.



### 3 The PRA's statutory obligations

3.1 In carrying out its policy making functions, the PRA is required to comply with several legal obligations. The PRA has a statutory duty to consult when introducing new rules (FSMA s138J), or new standards instruments (FSMA s138S). When not making rules, the PRA has a public law duty to consult widely where it would be fair to do so.

3.2 The PRA fulfils its statutory obligations and public law duties by providing the following in relation to the proposed policy:

- (i) **a cost benefit analysis;**
- (ii) **compatibility with the PRA's objectives:** an explanation of the PRA's reasons for considering that making the proposed rules is compatible with the PRA's duty to act in a way that advances its general objective<sup>24</sup> and secondary competition objective;<sup>25</sup>
- (iii) **FSMA regulatory principles:** an explanation of the ways in which having regard to the regulatory principles has affected the proposed rules;<sup>26</sup>
- (iv) **CRR rules:** in addition to the above, FSMA requires the PRA to 'have regard' to several further matters when making CRR rules.<sup>27</sup> It also requires the PRA to explain how the new 'have regards' have affected its proposed rules.<sup>28</sup> FSMA further requires the PRA to 'consider, and consult the Treasury about, the likely effect of the rules on relevant equivalence decisions';<sup>29</sup>
- (v) **impact on mutuals:** a statement as to whether the impact of the proposed rules will be significantly different to mutuals than to other persons.<sup>30</sup>
- (vi) **HM Treasury recommendation letter:** The Prudential Regulation Committee (PRC) should have regard to aspects of the Government's economic policy as recommended by HM Treasury;<sup>31</sup> and
- (vii) **equality and diversity:** the PRA is also required by the Equality Act 2010 to have due regard to the need to eliminate discrimination and to promote equality of opportunity in carrying out its policies, services and functions.

3.3 Appendix 3 lists the statutory obligations applicable to the PRA's policy development process. The analysis in this chapter explains how the proposals have had regard to the most relevant matters as listed in paragraph 3.2, including an explanation of the ways in which having regard to these matters has affected the proposals.

#### Capital Treatment of NPE securitisations

3.4 The proposals in this CP relate to the PRA's approach with regard to the capital treatment of NPE Securitisations. The PRA considers that its proposed approach to NPE securitisation would advance its primary objective of promoting the safety and soundness of PRA authorised persons, the

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<sup>24</sup> Section 2B of FSMA.

<sup>25</sup> Section 2H(1) of FSMA.

<sup>26</sup> Sections 2H(2) and 3B of FSMA.

<sup>27</sup> Section 144C(1) of FSMA.

<sup>28</sup> Section 144D of FSMA.

<sup>29</sup> Section 144C(3) of FSMA.

<sup>30</sup> Section 138K of FSMA.

<sup>31</sup> Section 30B of the Bank of England Act 1998.

relative standing of the UK as a place for business for internationally active banks and investment firms, and the ability of firms to provide finance to business and consumers for the benefit of the real economy (see further below).

### Cost benefit analysis

3.5 This CP proposes to introduce a bespoke treatment for NPE securitisations that applies to all PRA-regulated CRR firms. In summary, the proposals are expected to have positive net benefits, as firms would be able to reduce a source of balance sheet uncertainty and free up capital to support more productive lending as the costs of issuing NPE securitisation is reduced.

### *Benefits*

3.6 The PRA does not have the empirical data necessary to estimate directly the beneficial impact on the real economy. Analysis by the EBA for European NPEs suggests that the rate of NPE reduction via disposal for European banks has been slow since the global financial crisis.<sup>32</sup> Non-performing exposures can be a source of uncertainty on balance sheets, for example regarding the adequacy of provisions. These exposures could be reduced by securitisation, allowing the issuing bank to gain greater certainty over the balance sheet impact of NPEs, and providing investors with a risk priced investment product. The lack of an appropriate capital treatment for securitised NPEs may make securitisation overly expensive. The proposals can help banks re-allocate capital towards supporting more productive (ie performing) exposures, potentially supporting lending to the real economy.

### *Costs*

3.7 The PRA does not have the empirical data necessary to estimate the direct impact on capital requirements for UK firms. The current regulatory framework for securitisation is not well calibrated for securitisation of NPEs and may require significantly more capital than the underlying risk would imply (for SEC-SA and SEC-IRBA, excluding the foundation approach). The proposals are intended to improve the capacity of firms to issue NPE securitisation. A case study within the EBA 2019 opinion on NPE securitisations suggests that for SEC-SA and SEC-IRBA (excluding the foundation approach), there is a material reduction in capital costs, which would thus increase the viability of NPE securitisation by firms.<sup>33</sup>

### PRA objectives

3.8 The proposed changes are intended to reduce capital requirements for firms holding senior tranches of qualifying NPE securitisations and using SEC- SA and SEC-IRBA (apart from the foundation approach). These approaches can result in overly conservative risk weights for NPE securitisations. The proposed approach remains appropriately prudent by providing a risk weight floor for NPE securitisations (using the SEC-SA, SEC-IRBA, and look-through approach), while not allowing the use of the foundation approach for SEC-IRBA (as it may lead to insufficient capital requirements for NPE securitisations).

3.9 By supporting the use of NPE securitisations, the PRA is providing additional flexibility for firms to release and reallocate their regulatory capital, enhancing firms' safety and soundness by removing the capital uncertainty from NPEs with uncertain recoveries.

3.10 The PRA considers that the proposed changes would help to facilitate effective competition, for instance by allowing firms to deploy freed up capital to support the provision of other products to the market. The PRA considers that proposing to use the existing CRR definition of NPEs, and providing a standardised definition both of NRPPD and qualifying NPE securitisations, will help to facilitate effective competition in the market by supporting common definitions across firms. The

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<sup>32</sup> EBA Report on NPLs 2019.

<sup>33</sup> <https://www.eba.europa.eu/eba-publishes-opinion-regulatory-treatment-non-performing-exposure-securitisations>.

rules are concise and targeted in nature, and so the PRA considers them proportionate and to not pose an undue burden on firms.

Have regards

*FSMA regulatory principles*

3.11 In developing the proposals in this CP, the PRA has had regard to the regulatory principles. The following four principles are of particular relevance:

- (i) **The need to use the PRA's resources in the most efficient and economical way:** The proposals support the efficient and economic use of the PRA's resources by providing a clear and targeted update to the capital framework with respect to NPE securitisations. This will help ensure the PRA's resources are appropriately focused in this area. The PRA considers that the update to SS10/18 is a proportionate method of supervising the risk weight treatment for the senior tranche of qualifying NPE securitisations.
- (ii) **The desirability of sustainable growth in the economy of the UK:** The PRA expects its proposals to help firms managing NPEs, which may help reduce capital uncertainty. As a result, the PRA expects that this proposal would support finance in the real economy without negatively affecting growth or sustainable growth. The materiality of this impact is unclear given relatively limited NPEs in the UK currently.
- (iii) **The principle that the burden or restriction which is imposed on a person should be proportionate to benefits which are expected to result from the imposition of that burden:** The PRA considers the proposals relating to capital requirements from NPE securitisations would not impose any significant burden or restriction on firms as, depending on the capital approach taken by firms and their NPEs, the proposal may result in a reduction in capital requirements.
- (iv) **The desirability of the PRA exercising its functions in a way that recognises differences in the nature and objectives of businesses carried on by different persons (including different kinds of persons such as mutual societies and other kinds of business organisation), subject to requirements imposed by or under FSMA:** The PRA considers that the proposals in this CP for the definition and capital treatment of NPE securitisations would be beneficial for a variety of business models, as it would provide additional tools to manage NPEs for CRR firms with varying business models.
- (v) **the responsibilities of the senior management of PRA-authorized persons in relation to compliance with requirements imposed by the PRA:** The PRA considers it appropriate to propose an update to SS10/18 such that expectations for a firm's SMF 16, with regards to NPE securitisations, are clear and transparent in order to ensure that appropriate controls are in place in the creation of these unique products.

3.12 The PRA considers that the principle that the PRA should exercise its functions transparently is relevant to the proposals, but has not materially changed the proposals, as the PRA considers that it is functioning transparently through this consultation and the proposed update to SS10/18.

3.13 The PRA has considered the remaining FSMA regulatory principles (see references in Appendix 3), and considers that they are not relevant to this proposal.

### *CRR rules*

3.14 The proposed rules in this CP are 'CRR rules' (as defined in section 144A of the FSMA). As a result, in developing the proposal in this CP, the PRA considered the additional have regards applicable to CRR rules. The following three are of particular relevance:

- (i) relevant standards recommended by the Basel Committee on Banking Supervision from time to time;
- (ii) the likely effect of the rules on the relative standing of the United Kingdom as a place for internationally active credit institutions and investment firms to be based or to carry on activities; and
- (iii) the likely effect of the rules on the ability of CRR firms to continue to provide finance to businesses and consumers in the United Kingdom on a sustainable basis in the medium and long term.

3.15 The PRA has had regard to (i) in that the PRA considers the proposal is broadly consistent with the requirements for NPL securitisations under the new Basel technical amendment for NPL securitisations. Where the PRA proposes deviations from the Basel standards, for example on the definition of NPEs, the PRA considers the deviations not to be material, and that they are warranted by considerations regarding transparency and proportionality.

3.16 The PRA has had regard to (ii), as these proposals are the implementation of a technical amendment to international standards, which other Basel jurisdictions are expected to implement. By implementing these standards, the PRA expects to preserve the relative standing of the UK and the competitiveness of the UK. In addition, the PRA considers the approach to the implementation of the internationally agreed standard is broadly in line with the approach taken in the EU, which is the only peer jurisdiction to have implemented the Basel proposals to date. While there are minor differences from the EU's implementation of this technical amendment (such as regarding the look-through approach), the PRA does not expect them to be material, and considers that they are warranted to meet the PRA's safety and soundness objective.

3.17 The PRA has had regard to (iii) in that the PRA would expect its proposed rules to assist firms by supporting a tool (NPE securitisations) to manage NPEs, which may help reduce capital uncertainty. As a result, the PRA expects this proposal to support finance in the real economy without negatively affecting sustainable growth in the UK. The materiality of this impact is unclear given limited NPEs in the UK currently.

3.18 The PRA has considered the remaining matters to which it should have regard when making CRR rules (see references in Appendix 3), and considers that they are not relevant to this proposal.

### *Impact on mutuals*

3.19 The PRA considers that the impact of the proposed rule changes and expectations on mutuals would not differ from the impact on other firms.

### *HM Treasury recommendation letter*

3.20 HM Treasury has made recommendations to the PRC about aspects of the Government's economic policy to which the PRC should have regard when considering how to advance the PRA's

objectives and apply the regulatory principles.<sup>34</sup> The aspects of the Government's economic policy most relevant to the proposals in this CP are:

- (i) **Competition:**<sup>35</sup> This is considered within the PRA's objectives section;
- (ii) **Growth:**<sup>36</sup> This is considered within the FSMA regulatory principles section; and
- (iii) **Competitiveness:**<sup>37</sup> This is considered within the CRR Rules section.

3.21 The PRA has considered the remaining aspects of government economic policy as laid out in the HM Treasury recommendation letter (see references in Appendix 3), and considers that they are not relevant to these proposals.

#### *Equality and diversity*

3.22 The PRA considers that the proposals do not give rise to equality and diversity implications.

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<sup>34</sup> Information about the PRC and the recommendations from HM Treasury are available on the Bank's website at <https://www.bankofengland.co.uk/about/people/prudential-regulation-committee>.

<sup>35</sup> The government is keen to see more competition in all sectors of the industry, particularly retail banking. This includes minimising barriers to entry and ensuring a diversity of business models within the industry.

<sup>36</sup> The government wishes to ensure financial services markets make a positive contribution to sustainable economic growth in the UK economy in the medium and long term, through the facilitation of finance for productive investment and as a productive sector of the UK economy.

<sup>37</sup> The government wishes to ensure that the UK remains an attractive domicile for internationally active financial institutions, and that London retains its position as the leading international financial centre. The government considers that achieving this aim in a manner that is consistent with robust institutions and a resilient system will support its aims for sustainable economic growth.

## Appendices

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## 1 Draft non-performing exposures securitisation instrument

### **CRR FIRMS: NON-PERFORMING EXPOSURES SECURITISATION (CRR 2 MODIFICATIONS) INSTRUMENT 2021**

#### **Powers exercised**

- A. The Prudential Regulation Authority (“PRA”) makes this instrument in the exercise of the following powers and related provisions in the Financial Services and Markets Act 2000 (“the Act”):
- (1) section 137G (The PRA’s general rules);
  - (2) section 137T (General supplementary powers);
  - (3) section 144H(1) and (2) (Relationship with the CRR); and
  - (4) section 192XA (Rules applying to holding companies).
- B. The rule making powers referred to above are specified for the purpose of section 138G(2) (Rule-making instrument) of the Act.

#### **Pre-conditions to making**

- C. In accordance with sections 144C (3) of the Act the PRA consulted the Treasury about the likely effect of the rules on relevant equivalence decisions within the meaning of section 144C (4) of the Act.
- D. In accordance with section 138J (1) (a) of the Act (consultation by the PRA), the PRA consulted the Financial Conduct Authority.
- E. The PRA published a draft of the proposed rules in accordance with section 138J(1)(b) of the Act, accompanied by the information listed in section 138J(2) and the explanation referred to in section 144D of the Act insofar as that section is applicable to the rules.
- F. The PRA had regard to representations made.

### **PRA Rulebook: CRR Firms: Non-Performing Exposures Securitisation (CRR 2 Modifications) Instrument 2021**

- G. The PRA makes the rules in the Annex to this instrument.

#### **Commencement**

- H. This instrument comes into force on 1 January 2022.

#### **Citation**

- I. This instrument may be cited as the PRA Rulebook: CRR Firms: Non-Performing Exposures Securitisation (CRR2 Modifications) Instrument 2021.

#### **By order of the Prudential Regulation Committee**

## **Annex**

### **Non-Performing Exposures Securitisation (CRR)**

In this Annex the text is all new and is not underlined.

Part

# **Non-Performing Exposures Securitisation (CRR)**

Chapter content

- 1. APPLICATION AND DEFINITIONS**
- 2. CALCULATION OF RISK WEIGHT**



## 1 APPLICATION AND DEFINITIONS

1.1 This Part applies to:

- (1) a *CRR firm*; and
- (2) a *CRR consolidation entity*;

for the purpose of its obligations under Parts Two and Three of the CRR.

1.1A (1) A *firm* must comply with this Part on an individual basis.

(2) A *CRR consolidation entity* must comply with this Part on a consolidated basis, and for this purpose, references to a *firm* in this Part (other than in 1.1 and 1.1A) are to a *CRR consolidation entity*.

1.2 In this Part, the following definitions apply:

*non-refundable purchase price discount*

means the amount arrived at by subtracting the amount referred to in point (b) from the amount referred to in point (a), where:

(a) is the outstanding amount of the underlying exposures of the *NPE securitisation* at the time those exposures were transferred to the *SSPE*; and

(b) is the sum of the following:

(i) the initial sale price of the tranches or, where applicable, parts of the tranches of the *NPE securitisation* sold to third party investors; and

(ii) the outstanding amount, at the time the underlying exposures were transferred to the *SSPE*, of the tranches or, where applicable, parts of tranches of that securitisation held by the originator.

Where a discount is structured in such a way that it can be refunded in whole or in part to the originator or the original lender, such discount shall not count as a non-refundable purchase price discount.

*Non-performing exposure or NPE*

means an exposure that meets any of the conditions set out in Article 47a(3) CRR.

*NPE securitisation*

means a securitisation backed by a pool of non-performing exposures the nominal value of which makes up not less than 90% of the entire pool's nominal value at the time of origination and at any later time where assets are added to or removed from the underlying pool due to replenishment, restructuring or any other relevant reason.

*Qualifying NPE securitisation*

means an *NPE securitisation* that is a traditional securitisation as defined in point (9) of Article 2 of Regulation (EU) 2017/2402 where the *non-refundable purchase price discount* is at least 50% of the outstanding amount of the underlying exposures at the time they were transferred to the *SSPE*.

*SSPE*

has the meaning given by point (2) of Article 2 of Regulation (EU) 2017/2402.

## **2 CALCULATION OF RISK WEIGHT**

- 2.1 Subject to 2.2 and 2.4, the risk weight for a position in an *NPE securitisation* calculated by a *firm* in accordance with Article 254 or 267 CRR is subject to a floor of 100%, save where Article 263 CRR applies.
- 2.2 Where the risk weight for a *qualifying NPE securitisation* is calculated by a *firm* in accordance with Article 254 or 267 CRR, the *firm* must assign a risk weight of 100% to the senior securitisation position, save where Article 263 CRR applies.
- 2.3 A *firm* that applies the IRB Approach to any exposures in the pool of underlying exposures in accordance with Chapter 3 of Title II of Part Three CRR and that is not permitted to use, or does not use, own estimates of LGD and conversion factors for such exposures, must not use the SEC-IRBA for the calculation of risk-weighted exposure amounts for a position in an *NPE securitisation*.
- 2.4 By way of derogation from 2.1 and 2.2, save where 2.3 applies, a *firm* may calculate the maximum capital requirement for a position in an *NPE securitisation* in accordance with Article 268 CRR.

## 2 Draft amendments to SS10/18 'Securitisation: General requirements and capital framework'


### 2 General requirements under the Securitisation Regulation

...

Governance arrangements, processes and mechanisms

...

2.5A Where a firm acts as an originator, original lender, and/or sponsor in a non-performing exposure (NPE) securitisation subject to the requirements of the Securitisation Regulation, the PRA expects that a firm's SMF 16 (Compliance Oversight) should satisfy themselves that performing exposures are not being included in an NPE securitisation with the purpose of reducing the capital charge on performing exposures in the underlying relative to the 100% risk weight on the senior exposure to the qualifying NPE securitisation.



### 3 PRA statutory obligations

**The statutory obligations applicable to the PRA's policy development process are set out below. This CP explains the policy assessment of relevant considerations.**

- Purpose of the policy proposals (FSMA s138J(2)(b)).
- Cost benefit analysis (FSMA s138J(2)(a) and (7)(a)); and an estimate of those costs and benefits (if reasonable) (FSMA s138J(8)).
- Analysis of whether the impact on mutuals is significantly different to the impact on other authorised firms (FSMA s138J(2)(c) and 138K).
- Compatibility with the PRA's primary objectives (FSMA s138J(2)(d)(i), 2B, and 2C).
- Compatibility with the PRA's secondary competition objective (FSMA s138J(2)(d)(ii) and 2H(1)).
- Compatibility with the regulatory principles (FSMA s138J(2)(d)(ii), 2H(2), and 3B).
- Have regard to the HM Treasury recommendation letter (BoE Act s30B).
- Have due regard to the public sector equality duty (Equality Act s149).
- Have regard, subject to any other requirement affecting the exercise of the regulatory function, to the principles of good regulation and when determining general policy or principles to the Regulators Code (Legislative and Regulatory Reform Act 2006 s21 & 22).
- Have regard, so far as consistent with the proper exercise of those functions, to the purpose of conserving biodiversity. Conserving biodiversity includes, in relation to a living organism or type of habitat, restoring or enhancing a population or habitat (Natural Environment and Rural Communities Act 2006, s40).
- Consultation of the FCA (FSMA s138J(1)(a)).
- *Where the consultation proposals a PRA rule change or amendment to onshored BTS that affects the processing of personal data – consultation with the Information Commissioner's Office (Article 36(4) General Data Protection Regulation).*
- *For UK Technical Standards Instruments only:* FSMA s138J(1)(a) is replaced with: consultation of the FCA and/or Bank, where that Regulator has an interest in the technical standards (FSMA s138P(4) and (5)).
- *For UK Technical Standards Instruments only:* notice given to HMT of the consultation on the UKTS ('best efforts' basis).

- *For CRR rules only:* subject to certain exceptions, have regard to:
  - relevant standards recommended by the Basel Committee on Banking Supervision from time to time;
  - the likely effect of the rules on the relative standing of the United Kingdom as a place for internationally active credit institutions and investment firms to be based or to carry on activities. For these purposes, the PRA must consider the United Kingdom's standing in relation to the other countries and territories in which, in its opinion, internationally active credit institutions and investment firms are most likely to choose to be based or carry on activities;
  - the likely effect of the rules on the ability of CRR firms to continue to provide finance to businesses and consumers in the United Kingdom on a sustainable basis in the medium and long term; and
  - the target in section 1 of the Climate Change Act 2008 (carbon target for 2050).

(s144C (1)&(2) FSMA – exceptions in s144E FSMA).

- *For CRR rules only:* explanation of the ways in which having regard to the matters specified above has affected the proposed rules (s144D FSMA).
- *For CRR rules only:* publication of a summary of the proposed CRR rules.
- *For CRR rules only:* consideration and consultation with the Treasury about the likely effect of the rules on relevant equivalence decisions (s144C (3) &(4) FSMA).