

# Bank of England PRA

## SS10/18 - Securitisation: General requirements and capital framework

### Supervisory statement | SS10/18

April 2024 (updating October 2021)

Effective from 1 November 2024



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# 1. Introduction

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1.1 This Supervisory Statement (SS) sets out the Prudential Regulation Authority's (PRA's) expectations of firms in respect of securitisation in the following chapters:

- 'General requirements under the Securitisation Part of the PRA Rulebook' (Chapter 2) – general expectations of firms and processes under the Securitisation Part of the PRA Rulebook.
- 'STS ABCP Sponsors' (Chapter 3) - general expectations of firms seeking to become sponsors of Simple, Transparent and Standardised (STS) Asset Backed Commercial Paper (ABCP) programmes.
- 'CRR securitisation capital framework' (Chapter 4) - PRA expectations and approach as regards the securitisation capital framework for CRR firms.

1.2 This statement is relevant to PRA-authorized firms, including CRR firms, non-CRR firms, Solvency II firms and non-Solvency II firms to which the Securitisation Part of the PRA Rulebook applies, unless stated otherwise. Throughout this statement, as regards securitisations to which Chapter 3 of the Securitisation Part of the PRA Rulebook applies, references to the Securitisation Part of the PRA Rulebook or provisions therein shall be read as references to corresponding provisions applied by and read in accordance with Chapter 3 of the Securitisation Part of the PRA Rulebook.

## 2. General requirements under the Securitisation Part of the PRA Rulebook

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2.1 Deleted.

### Originator, original lender, and sponsor requirements

2.2 The PRA expects firms which act as originators, original lenders, and/or sponsors in a securitisation that are subject to the requirements of the Securitisation Part of the PRA Rulebook to be able to demonstrate to the PRA, on request, that they have in place adequate arrangements, processes and mechanisms in order to comply with Articles 6, 7, 8 and 9 of Chapter 2 and Chapters 4-6 of the Securitisation Part of the PRA Rulebook.

2.3 A firm should inform its supervisor if it anticipates material change in its securitisation activity as an originator or sponsor. That includes, engaging in securitisation issuance for the first time, securitising an asset class for the first time, or significantly increasing the amount of issuance.

### **Governance arrangements, processes and mechanisms**

2.4 Where a firm acts as an originator, original lender, and/or sponsor in a transaction subject to the requirements of the Securitisation Part of the PRA Rulebook, the PRA expects the firm's internal audit function to provide assurance that the firm's involvement in the securitisation is compliant with the requirements in Articles 6, 7, 8 and 9 of Chapter 2 and Chapters 4-6 of the Securitisation Part of the PRA Rulebook.

2.5 The PRA expects firms subject to the Senior Managers and Certification Regime to identify a relevant individual performing a Senior Management Function (SMF) to exercise effective oversight of securitisation issuance, including with regard to the requirements in Article 6(2) of Chapter 2 and Article 18 of Chapter 4 of the Securitisation Part of the PRA Rulebook on adverse selection. Where appropriate, the PRA expects SMFs to escalate issues related to oversight of securitisation issuance to the board or a relevant sub-committee.

2.5A Where a CRR firm acts as an originator, original lender, and/or sponsor in a non-performing exposure (NPE) securitisation subject to the requirements of the Securitisation Part of the PRA Rulebook, the PRA expects that the 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 such performing exposures in the underlying relative to the 100% risk weight on the senior exposure of qualifying NPE securitisation.

### **Insurance firms, reinsurance firms or ISPVs as originators**

2.6 The PRA considers that insurance firms, reinsurance firms or ISPVs (whether PRA-authorized Solvency II firms or PRA-authorized non-Solvency II firms) can be originators as defined in the Securitisation Part of the PRA Rulebook. The Securitisation Part of the PRA Rulebook makes clear that insurance or reinsurance undertakings that are PRA-authorized Solvency II firms can also be 'institutional investors' in securitisation. The PRA expects insurance and reinsurance firms, and ISPVs, to consider whether any transactions, such as those that aim to refinance loans, exposures or receivables by transforming them into tranching securities and including any internal restructurings, may be considered securitisations as defined in the Securitisation Part of the PRA Rulebook. The Securitisation Part of the PRA Rulebook imposes a set of requirements on originators, original lenders, sponsors and securitisation special purpose entities (SSPEs) as well as institutional investors in securitisations.

2.7 Insurance or reinsurance firms (whether PRA-authorised Solvency II firms or PRA-authorised non-Solvency II firms) can be both originators and investors in the same securitisation transaction, such as an internal restructuring of exposures or receivables for capital efficiency or matching adjustment (MA) eligibility purpose. In such cases the insurance or reinsurance firm must comply with Articles 6, 7, 8 and 9 of Chapter 2 and Chapters 4-6 of the Securitisation Part of the PRA Rulebook as applicable. Where an insurance firm, reinsurance firm, or ISPV identifies itself as the originator of a securitisation, it should inform its supervisor without undue delay.

2.8 Where the originator is also the sole investor in the transaction, the PRA expects that the firm may consider the information specified in Article 7(1)(a) and (e) of Chapter 2 of the Securitisation Part of the PRA Rulebook as 'made available' to investors through internal reporting to appropriate committees or the management board, provided the reporting contains the required information.

### Investor requirements

2.9 The PRA expects institutional investors that invest in securitisation to be able to demonstrate on request that they have in place adequate due diligence arrangements, processes, and mechanisms to ensure compliance with Article 5 of Chapter 2 of the Securitisation Part of the PRA Rulebook. The level and nature of due diligence prior to holding a securitisation position may be proportionate to the risks of the securitisation position, provided they comply with the requirements of Article 5 of Chapter 2 of the Securitisation Part of the PRA Rulebook.

2.10 A firm that has delegated the authority to manage its investments to another institutional investor may instead evidence that it has instructed the managing party to fulfil the due diligence requirements on its behalf.

## 3. STS ABCP sponsors

3.1 This chapter is relevant to PRA-authorised CRR credit institutions.

3.2 A credit institution supervised under CRR may act as a sponsor for an STS ABCP programme using one of the following routes:

- (i) the credit institution demonstrates to the PRA that the support it provides to the programme would not endanger its solvency and liquidity, even in an extreme market stress (SECN 2.3.25R(1) of the FCA Handbook); or
- (ii) the PRA has determined on the basis of the review and evaluation referred to in Regulation 34A(2) of the Capital Requirements Regulations 2013 that the arrangements,

strategies, processes, and mechanisms implemented by that credit institution and the own funds and liquidity it holds ensure the sound management and coverage of its risks (SECN 2.3.25R(2) of the FCA Handbook).

3.3 Deleted.

### **SECN 2.3.25R(1) of the FCA Handbook**

3.4 To demonstrate to the PRA that its role as an STS ABCP Sponsor under SECN 2.3.25R of the FCA Handbook will not endanger its solvency or liquidity, a firm should notify its usual supervisory contact, providing relevant information that should include:

- (i) an assessment of the impact of full support on the firm's Total Capital Requirement on an individual and consolidated basis, both with and without STS status;
- (ii) an assessment of the impact of full support on the firm's regulatory liquidity guidance and buffer resources, both with and without STS status; and
- (iii) a summary of the programme features relevant to an understanding of the assessment in (i) and (ii) above, including an assessment against STS requirements in SECN 2.3.23R to SECN 2.3.37R of the FCA Handbook.

3.5 Where a firm seeks to set up a new conduit, or is proposing to sponsor an ABCP programme or transaction for the first time, it must provide its supervisors with the request sufficiently in advance of the execution of the transaction.

### **SECN 2.3.25R(2) of the FCA Handbook**

3.6 For the purposes of being an STS ABCP sponsor, the PRA is unlikely to determine on the basis of the review and evaluation referred to in Regulation 34A(2) of the Capital Requirements Regulations 2013 that the arrangements, strategies, processes, and mechanisms implemented by that credit institution and the own funds and liquidity it holds ensure the sound management and coverage of its risks, unless the firm is currently a sponsor for at least one ABCP programme. This may include any existing non-STS ABCP programme for which the firm wishes to seek STS status.

3.7 Where a firm seeks to make use of the route specified in SECN 2.3.25R(2) of the FCA Handbook, it should make a written request to its usual supervisory contact prior to, or alongside, the submission of either its internal capital adequacy assessment process (ICAAP) or internal liquidity adequacy assessment process (ILAAP) document. Where the information specified in paragraph 3.5 is not already available in the ICAAP or ILAAP document, the firm should also provide necessary information referenced in paragraph 3.5.

## 4. The CRR securitisation capital framework

4.1 This chapter is relevant to PRA-authorised CRR firms. It sets out the PRA's expectations of firms in respect of the CRR securitisation capital framework in the following sections:

- (i) 'Hierarchy of methods' – with respect to the exercise of discretions which determine the methods applied for calculating securitisation Risk Weighted Exposure Amounts (RWEAs).
- (ii) 'Interim mapping of External Credit Assessment Institutions (ECAIs) structured finance credit assessments to Credit Quality Steps (CQS)' — with respect to the interim mapping of rating agency grades to CQS for the purposes of securitisation positions risk weighted under the External Ratings Based Approach (SEC-ERBA).

### Hierarchy of methods

#### PRA discretions under the hierarchy of methods

4.2 CRR Article 254 introduces the hierarchy of methods for calculating securitisation RWEAs, summarised below:

- (i) where the conditions set out in Article 258 are met, the Securitisation Internal Ratings Based Approach (the 'SEC-IRBA') in accordance with Articles 259-260;
- (ii) where the SEC-IRBA may not be used, the Securitisation Standardised Approach (the SEC-SA) in accordance with Article 261-262; and
- (iii) where the SEC-SA may not be used, the Securitisation External Ratings Based Approach (the 'SEC-ERBA') in accordance with Articles 263-264 for rated positions or positions in respect of which an inferred rating may be used.

4.3 Under CRR Articles 254(4) and 258(2), the PRA may use the following discretions, on a case-by-case basis to:

- (i) prohibit firms from applying SEC-SA, when the risk-weighted exposure amount resulting from the application of the SEC-SA is not commensurate with the risks posed to the institution or to financial stability; and
- (ii) prohibit the use of SEC-IRBA where securitisations have highly complex or risky features.

4.4 The PRA intends to use these discretions in order to support its primary objective of maintaining the safety and soundness of firms. Although the PRA does not favour any single method, in some cases Pillar 1 capital requirements arrived at under the SEC-ERBA may be



a more appropriate reflection of risk to the firm than those arrived at under the SEC-SA or SEC-IRBA. When considering an exercise of its discretions, the PRA will take into account, among other things, the aggregate impact on a firm's overall capital requirements. The PRA does not expect firms to solicit ECAI ratings for all of their securitisation positions.

4.5 When determining whether to exercise its discretion under Articles 254(4) and 258(2), the PRA will consider whether securitisations a firm is exposed to exhibit features which are not explicitly captured in the SEC-SA or SEC-IRBA methods. The PRA may also consider the appropriateness of underlying credit risk weights for the portfolio as reflected in the  $K_{SA}$  or  $K_{IRB}$  determined under Article 255.

4.6 The SEC-IRBA is sensitive to a wider range of inputs than the SEC-SA. Therefore where the presence of a highly complex or risky feature leads the PRA to exercise its discretion to preclude the use of the SEC-IRBA, the PRA is also likely to prohibit the use of the SEC-SA on the grounds that the risk weights under the SEC-SA are not commensurate with the risks posed to the institution.

4.7 The SEC-SA and SEC-IRBA methods can only recognise a defined number of items in their calculation of capital requirements, primarily focused on credit risk. These methods may fail to recognise the presence of non-credit risks. To an extent some additional non-credit risks which can arise from securitisation are reflected in the 'non-neutrality' of the securitisation capital framework.<sup>1</sup> However the level of non-neutrality is driven by pre-defined inputs (eg STS status).

4.8 When the SEC-SA or SEC-IRBA method is applied to a securitisation position, there is also a risk that the  $K_{SA}$  or  $K_{IRB}$  derived using the credit risk capital framework is inappropriate. This may be because the underlying exposures are affected by risk drivers which are not adequately captured by the credit risk framework.

4.9 In the presence of risk characteristics and structural features which are not explicitly captured in the formulas of the SEC-SA or SEC-IRBA, including features not adequately captured in the underlying credit risk framework, it is possible that an appropriate assessment by an ECAI takes into account those features. In such cases the SEC-ERBA may more appropriately reflect the risk posed to the institution.

4.10 Examples of features or characteristics which expose firms to risks not captured in the SEC-SA or SEC-IRBA include, but are not limited to, those listed in Article 258(2)(a) to (d), and:

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<sup>1</sup> 'Non-neutrality' of the framework here means that typically the total RWEAs calculated for the tranches of a securitisation will be higher than the RWEAs calculated for the underlying portfolio had it not been securitised. In the SEC-SA and SEC-IRBA, this non-neutrality is introduced primarily through the application of a risk weight floor (10% for STS positions and 15% for non-STs positions) and the supervisory 'p' factor.

- (a) interest rate risks or foreign exchange risks which arise due to mismatches between the underlying pool and the issued notes, and which are not adequately hedged;
- (b) features or characteristics which expose holders of securitisation notes to the risk that market conditions at the date of the sale or refinance of underlying exposures result in losses, such as exposure to residual value risk;
- (c) portfolios which exhibit a high degree of single name, sectoral or geographical credit concentration risk;
- (d) portfolios where the underlying exposures may be highly correlated in the event of a stress;
- (e) complex mechanisms which impact the priority of payments, for example the existence of turbo features; and
- (f) for transactions to which the SEC-SA applies, where the characteristics of the underlying portfolio exhibit material dilution risk.

4.11 The PRA, in conjunction with the Financial Policy Committee (FPC) or on its own initiative, may identify financial stability risks arising from firms' securitisation activity. Where the RWEA calculated under the SEC-SA method is not commensurate with the risk posed to financial stability, the PRA may mitigate the risk by use of Article 254(4).

#### **Information on methods used by firms**

4.12 The PRA expects firms to have regard, during their ICAAP, to the provisions in SS31/15 paragraphs 2.39 and 2.40.<sup>2</sup> The PRA will monitor possible risks to safety and soundness with reference to Common Reporting (COREP) and a firm's ICAAP document. The information provided in a firm's ICAAP document, supplemented by information received by other means such as regulatory reporting, will be used to assist the PRA in its assessment of whether firms' securitisation exposures using the SEC-SA or SEC-IRBA are appropriately capitalised.

4.13 The PRA may request additional information in order to evaluate whether Pillar 1 capital requirements appropriately reflect the risk posed to an institution. The PRA expects firms to provide this information within 30 business days, unless agreed otherwise.

4.14 This additional information may vary on a case-by-case basis, but should include:

- (i) A list of the securitisation positions to which the SEC-SA or the SEC-IRBA is applied.

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<sup>2</sup> [The Internal Capital Adequacy Assessment Process \(ICAAP\) and the Supervisory Review and Evaluation Process \(SREP\) \(bankofengland.co.uk\)](https://www.bankofengland.co.uk/prudential-regulation/publication/2024/april/securitisation-policy-statement).

- (ii) For each securitisation position listed in (i):
- the asset class of the underlying securitised exposures;
  - the risk characteristics and structural features exhibited by the securitisation that may materially impact the performance of the firm's securitisation position, and which are not explicitly taken into account by the method applied;
  - unless already provided in the most recent Common Reporting (COREP) submission:<sup>3</sup>
    - for positions risk-weighted under the SEC-IRBA, the risk-weighted exposure amount for that securitisation position under the SEC-IRBA, SEC-ERBA (for rated positions only) and SEC-SA insofar as each method can be used; or
    - for rated positions risk-weighted under the SEC-SA, the risk-weighted exposure amounts for that securitisation position under the SEC-ERBA.
  - a hyperlink to the prospectus of the transaction, or where no prospectus is available a copy of the offering circular or equivalent; and
  - for rated securitisation positions, the latest rating(s) attributed to the position and the ECAI(s) which provided that rating.

### Communication of decisions on the hierarchy of methods

4.15 Where the PRA considers that the exercise of its discretion under Articles 254(4) or 258(2) is justified, it will inform the firm in writing.

4.16 The PRA may choose to exercise one or both of the discretions under Articles 254(4) and 258(2) in respect of a securitisation position or a defined group of securitisation positions.

4.17 The PRA may choose to exercise the discretion under Article 254(4) to an unrated securitisation position for which a rating may not be inferred, in which case it may require the firm to apply a 1,250% risk weight to the securitisation position.

### Firms' use of the CRR hierarchy

4.18 Relevant senior management should ensure that firms are using appropriate methods to capitalise their securitisation exposures.

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<sup>3</sup> <https://www.legislation.gov.uk/eur/2014/680/contents>.

4.19 For these purposes, relevant senior management means the individual(s) performing the relevant SMF(s), and employees subject to the Certification Regime involved in investment decisions in securitisation exposures (eg relevant Material Risk Takers (MRTs) under the Remuneration rules).

4.20 Under Article 254(3), firms may decide to apply the SEC-ERBA instead of the SEC-SA to all of their rated securitisations or positions in respect of which an inferred rating may be used.

4.21 Firms should notify the PRA of a decision made under CRR Article 254(3). That notification should be sent simultaneously by email to [securitisation.hierarchy@bankofengland.co.uk](mailto:securitisation.hierarchy@bankofengland.co.uk) and to the firm's usual supervisory contact. This notification should include information on the impact of such a decision on the firm's securitisation RWEAs.

### Interim mapping of External Credit Assessment Institutions (ECAIs) structured finance credit assessments to Credit Quality Steps (CQS)

4.22 CRR Article 270e stipulates that the PRA may produce implementing Technical Standards (ITS) mapping the credit assessments of ECAIs to the CQS specified in the CRR for the purposes of calculating risk-weighted exposure amounts under the SEC-ERBA.<sup>4</sup>

4.23 Prior to adoption of this ITS, the PRA expects firms to use the illustrative Basel securitisation ERBA mapping for long-term ratings,<sup>5</sup> as set out in Table 1 below for long-term ratings. For short-term ratings, PRA expects firms to use the existing short-term mapping in Commission Implementing Regulation (EU) 2016/1801<sup>6</sup> on laying down technical standards with regard to the mapping of credit assessments for securitisation. These tables will be superseded once the relevant ITS has been adopted.

**Table 1: Long-term ECAI assessment mapping**

| Credit Quality Step | Illustrative Rating |
|---------------------|---------------------|
| 1                   | AAA / Aaa           |
| 2                   | AA+ /Aa1            |

<sup>4</sup> For ECAI credit assessments used in respect of retained tranches in a significant risk transfer (SRT) securitisation, see paragraph 4.3 of SS9/13 'Securitisation: Significant Risk Transfer', November 2018: <https://www.bankofengland.co.uk/prudential-regulation/publication/2013/securitisation-ss>.

<sup>5</sup> Basel, July 2016, 'Revisions to the Securitisation Framework'. The rating designations referenced are for illustrative purposes only and do not indicate any preference for, or endorsement of, any particular external assessment system.

<sup>6</sup> <https://www.legislation.gov.uk/eur/2016/1801/contents/adopted>.

|    |                                 |
|----|---------------------------------|
| 3  | AA / Aa2                        |
| 4  | AA- /Aa3                        |
| 5  | A+ / A1                         |
| 6  | A / A2                          |
| 7  | A- / A3                         |
| 8  | BBB+ / Baa1                     |
| 9  | BBB / Baa2                      |
| 10 | BBB- /Baa3                      |
| 11 | BB+ /Ba1                        |
| 12 | BB / Ba2                        |
| 13 | BB- / Ba3                       |
| 14 | B+ / B1                         |
| 15 | B / B2                          |
| 16 | B- /B3                          |
| 17 | CCC+/CCC/CCC-<br>Caa1/Caa2/Caa3 |
| 18 | Below CCC-<br>/Caa3             |

Effective from 1 November 2024

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## Annex – SS10/18 updates

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This annex details the changes that have been made to this SS following its initial publication in January 2019:

### 2024

#### April 2024

Following publication of policy statement (PS) 7/24 – Securitisation: General requirements<sup>7</sup>, Chapters 1-3 of this SS were updated to extend its scope to all PRA-authorized firms to which the Securitisation Part of the PRA Rulebook applies unless stated otherwise and/or to reflect the replacement of relevant provisions in the Securitisation Regulation with PRA and FCA rules. The PRA has also made minor changes throughout this SS to improve clarity of drafting.

This policy is effective from Friday 1 November 2024.

### 2021

#### October 2021

Following publication of PS24/21 'Implementation of Basel standards: Non-performing loan securitisations',<sup>8</sup> paragraph 2.5A was added to this SS to reflect expectations of a firm's SMF 16 with regard to NPE securitisation. This policy is effective from Saturday 1 January 2022.

The PRA has also made minor changes to reflect the UK's withdrawal from the EU, and improve clarity of drafting.

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<sup>7</sup> Available at: <https://www.bankofengland.co.uk/prudential-regulation/publication/2024/april/securitisation-policy-statement>.