

**Bank of England PRA**

# Appendix 6: Draft amendments to supervisory statement 10/18 – Securitisation: General requirements and capital framework

**Draft supervisory statement**

October 2024

Draft for consultation



# Draft amendments to supervisory statement 10/18 – Securitisation: General requirements and capital framework

In this appendix, new text is underlined and deleted text is struck through.

...

## 4: The CRR securitisation capital framework

4.1 This chapter is relevant to all PRA-authorised CRR firms to which the Securitisation (CRR) Part of the PRA Rulebook applies. It sets out the PRA's expectations of firms in relation to the hierarchy of methods ~~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 risk weighted assets (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 Article 254 of the Securitisation (CRR) Part sets out the hierarchy of methods for calculating securitisation RWA, summarised below:

- (i) where the conditions set out in Article 258 of the Securitisation (CRR) Part are met, the Securitisation Internal Ratings Based Approach (SEC-IRBA) must be used in accordance with Articles 259-260 of the Securitisation (CRR) Part;
- (ii) where the SEC-IRBA may not be used, the Securitisation Standardised Approach (SEC-SA) must be used in accordance with Article 261-262 of the Securitisation (CRR) Part;  
and
- (iii) where the SEC-SA may not be used, the Securitisation External Ratings Based Approach (SEC-ERBA) must be used in accordance with Articles 263-264 of the Securitisation

(CRR) Part for rated positions or positions in respect of which an inferred rating may be used.

~~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 Articles 254(4) and 258(2) of the Securitisation (CRR) Part refer to the PRA’s powers to impose a requirement under s55M of the Financial Services and Markets Act 2000 (FSMA) or give a direction under s192C of FSMA which may be used to:

- (i) prohibit firms from applying the SEC-SA; or
- (ii) preclude the use of the SEC-IRBA.

~~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 Please refer to the PRA’s statement of policy (SoP) on ‘The PRA’s approach to the exercise of powers referred to in Articles 244(3)(b), 245(3)(b), 254(4) and 258(2) of the Securitisation (CRR) Part of the PRA Rulebook’, especially Appendix 2. 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 – 4.11 Deleted. 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 KSA or KIRB 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 KSA or KIRB 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:~~

~~(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;~~

<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.

- (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 (please also refer to the PRA's SoP on 'The PRA's approach to the exercise of powers referred to in Articles 244(3)(b), 245(3)(b), 254(4) and 258(2) of the Securitisation (CRR) Part of the PRA Rulebook', especially Appendix 2).

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.

---

<sup>2</sup> [The Internal Capital Adequacy Assessment Process \(ICAAP\) and the Supervisory Review and Evaluation Process \(SREP\) \(bankofengland.co.uk\).](#)

(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 External Credit Assessment Institutions (ECAI(s)) which provided that rating.

### Communication of decisions on the hierarchy of methods

This section is deleted.

~~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.

<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) of the Securitisation (CRR) Part of the PRA Rulebook, 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 ~~must~~ should notify the PRA of a decision made under ~~CRR~~ Article 254(3) of the Securitisation (CRR) Part of the PRA Rulebook no less than 1 month prior to it coming into effect. 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.

4.21A Firms ~~must~~ should notify the PRA of any subsequent decision to further change the approach applied to all of their rated securitisation positions no less than 1 month prior to that decision coming into effect. 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. Firms ~~must~~ should not use different approaches within a 12-month period.

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

This section is deleted.

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~~

<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->

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
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- Caa1/Caa2/Caa3
18	Below CCC- /Caa3