FSB FINANCIAL STABILITY BOARD

22 January 2025

Evaluation of the effects of securitisation reforms

Overview of the responses to the consultation

1. Introduction

The consultation report on the evaluation of the effects of the G20 financial regulatory reforms on securitisation was published on 2 July 2024 and the comment period closed on 2 September.[1] The objective of the consultation was to gather stakeholder feedback on the interim findings of the evaluation. A total of 16 responses were received, with the majority coming from international trade associations.[2]

During the consultation period, the FSB hosted a virtual public workshop on 22 August.[3] The workshop gave the opportunity for industry representatives, academics, and other stakeholders to exchange views on the preliminary findings and the questions posed in the consultation report. The FSB also organised a roundtable with academics to receive additional external views on the conceptual and empirical arguments for risk retention in collateralised loan obligations (CLOs).

This note summarises the feedback received on the consultation report – both from the public responses and from the workshop – and sets out the main changes made to the final report in order to address them (section 2). The note also provides a short overview of additional analysis carried out by the FSB since the consultation report to enhance the robustness of the results.

2. Summary of feedback received

Overall, the report was well received by the respondents, including the timing of the review of the reforms given ongoing discussions about securitisation markets in some jurisdictions.

In terms of the scope of the evaluation, respondents welcomed the exclusion of government-guaranteed securitisations; however, some noted the need to exclude the retained segment in the European residential mortgage-backed securities (RMBS) market and to consider asset-backed securitisation (ABS) and synthetic risk transfer (SRT) in the analysis. Some respondents also commented that the analysis should consider the impact of reporting, disclosure and due

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1 The evaluation focuses, in terms of reforms, on the International Organization of Securities Commissions (IOSCO) minimum retention recommendations and the Basel Committee on Banking Supervision (BCBS) revisions to prudential requirements for banks' securitisation-related exposures; and in terms of scope, on the collateralised debt/loan obligation (CDO/CLO) and the non-government-guaranteed part of the residential mortgage-backed securities (RMBS) market segments. See FSB (2024), *Evaluation of the Effects of the G20 Financial Regulatory Reforms on Securitisation: Consultation report*, July.

2 Non-confidential responses are available on the FSB website.

3 See the agenda and presentations for this event in the FSB securitisation evaluation workshop webpage.

diligence rules. They also mentioned the importance of rules impacting other market participants (e.g. insurers and credit rating agencies), and structuring requirements other than risk retention.

Many respondents commented specifically on the EU securitisation market, highlighting the low levels of default since the 2008 global financial crisis (GFC) as evidence for the resilience of the market but asserting that the way that the reforms were implemented in the EU has impeded market development. This included comparisons to the growth in the US securitisation market since the GFC and the lack of comparable reforms. Several respondents argued for the calibration of prudential rules to be revisited as part of wider discussions on the functioning of the EU securitisation market, though no empirical evidence was provided for these assertions.

There were mixed views on risk retention requirements for CLOs. Some respondents argued for their removal given the existence of other factors that contribute to alignment of incentives and expressed support for third-party risk retention financing vehicles (see section 2.3). Others saw risk retention as a key reform and suggested a more uniform application for a level playing field.

2.1. Overview of securitisation markets

While most respondents indicated the report appropriately covered key securitisation market trends, several suggested including more detailed data including segmentation by region, tranche, and asset classes, as well as more information on annual issuance volume and default rates. Some argued that retained securitisations, particularly for the EU, should be excluded from market size measures as they are not distributed in the market.

Changes in response to comments

The consultation report already included a brief description of market developments at the global level in sections 2.2 and 4.2, including some issuance indicators. The final report also includes a new Annex with market and regulatory developments (including graphics on the evolution of market size based on annual issuance and outstanding volumes) in other FSB jurisdictions with material securitisation markets. The report also separates out retained versus placed RMBS transactions in jurisdictions where this is relevant and where such data are available.

2.2. Securitisation reforms

Several respondents agreed with the report's description of the post-GFC securitisation reforms but highlighted that the implementation of these reforms vary widely across jurisdictions.

In relation to jurisdictional implementation of the BCBS and IOSCO reforms, several respondents pointed out divergences in implementation that make it difficult to assess their impact on the securitisation market on a global basis. They also indicated the need to investigate further these divergences across G20 jurisdictions.

Several comments were made around the need to examine due diligence requirements and the negative consequences they had in the EU. These respondents noted that the FSB should encourage convergence and proportionality across jurisdictions to reduce market fragmentation. Some respondents also mentioned the Basel III's Liquidity Coverage Ratio (LCR) as playing a role in banks' preference for covered bonds in the EU and senior tranches in CLOs. Comments were also made on other G20 and jurisdiction-specific financial reforms, such as Solvency II, environmental, social, and governance disclosures, and fair value (IFRS 9) accounting reforms.

Many respondents pointed out that the objectives, transmission channels and expected outcomes of the securitisation reforms are appropriately described but noted that they relate only to financial stability and to the (limited) scope of the reforms. Regarding expected outcomes, some indicated the report expands on the shortcoming of securitisations pre-GFC with a suggestion that it could be useful to distinguish between expected and actual reform outcomes.

Other comments regarding the securitisation reforms refer to the different definition of securitisation in the EU and certain other jurisdictions (e.g. US), where risk retention and disclosure reforms apply only to more narrowly defined set of asset-backed securities.

Changes in response to comments

The final report highlights more clearly major divergences in implementation of the agreed reforms. Even though no evidence has been presented by the respondents on the materiality of these divergences, additional analysis by the FSB has considered commonalities across jurisdictions on the impact of the BCBS reforms and any potential impact on cross-border investments (see sections 4 and 5.1).

With respect to different securitisation definitions, no evidence was presented by the respondents to support the argument that these had a material impact on the effects of reforms.

The LCR was covered in the annex of the consultation report but has also been added in the main body when discussing the reforms (see section 3).

2.3. Effectiveness of the securitisation reforms

Several respondents argued that the report understated the resilience of CLOs, especially those issued after 2010, and noted that EU securitisation more generally did not contribute to the GFC. In this context, they noted that CLOs exhibited strong credit performance with few defaults, have proven resilient during recent economic stresses, and contribute positively to financial stability by providing financing to the real economy. These respondents also suggested that the report distinguishes between credit downgrades and defaults from higher interest rates (impacting debt servicing costs for the underlying corporates) versus poor revenue performance, with any recent downgrades being largely a result of the former. The public workshop discussion was more mixed, with some participants of the view that CLOs were yet to be tested during a prolonged economic downturn. Another point raised was around the sensitivity of CLOs to downgrades by credit rating agencies, which may put CLO managers at risk of breaching their own covenants.

The majority of respondents expressed agreement with the analysis of RMBS credit performance in the report. Some, including during the public workshop, highlighted that any improvement post-GFC in performance of European RMBS was unlikely to be solely the result of reforms, as these reforms did not raise existing standards but mostly codified existing ones.

There were mixed views on the effectiveness of risk retention for CLOs, unlike in the case of the RMBS analysis. Some respondents, including during the public workshop, argued for the removal of risk retention in jurisdictions where this is a requirement, given that CLO managers already have ‘skin in the game’ by virtue of other structural features, making the risk retention concept redundant for these structures. A specific argument was made that CLO managers were at arms’ length from the origination of the underlying loan assets and that their role in selecting, acquiring and managing loans from the open market was analogous to the role played by a fund or asset manager who don’t have risk retention requirements.

In addition, some respondents asserted that investors do not use risk retention as an indication of portfolio quality, instead undertaking due diligence on the portfolio where appropriate. On the other hand, several other respondents disagreed with an approach that would exclude specific types of issuers from the risk retention requirements. In particular, it was highlighted that risk retention rules have been a key post-GFC reform, should be consistently applied for a level playing field, and are by now a well-accepted market practice. It was also noted that removing them would not unlock significant market growth.

Some respondents also argued for the validity of third-party risk retention financing structures for CLOs, an emerging theme mentioned in the consultation report. They argued that the look-through method would only be appropriate where the special purpose risk retention vehicles were shell companies with no substance. In their view, this was not the case for these special purpose vehicles as they had boards and investment committees and made the key decisions around initial purchase of loans and establishment of the CLOs.

With respect to the impact of BCBS reforms, many respondents argued that the implementation in the EU limited the role banks could play in the securitisation market, particularly compared to US peers, but without providing empirical evidence. Their arguments largely stem from the “p-factor” in the capital calculation combined with (non-BCBS) disclosure reforms for banks acting as investors. Respondents also pointed out that the report did not evaluate the combined impact of the increase in risk-weighted assets and the output floor introduced by the final Basel III framework on retained senior tranches of SRT transactions. Some respondents noted it was difficult to disentangle the effects of the prudential reforms from macroeconomic developments and other reforms (such as ban on re-securitisations), although at the workshop it was noted that the G20 reforms have contributed to enhancing the resilience of the banking sector.

Changes in response to comments

The final report includes more details on the resilience of CLOs by noting their strong credit performance to date but also the potential second round channels through which senior tranche holders may be affected (notwithstanding the stronger structures). A key message – that the CLO market has not yet been tested in a prolonged economic downturn – remains unchanged.

With respect to risk retention in CLOs, the final report includes a box describing the overturning by a US court in 2018 of the risk retention requirements for open-market CLOs alongside analysis on its impact on CLO spreads and risk characteristics, supplementing the analysis in the consultation report (see section 4 and Annex 4). In addition, the narrative has been expanded on how other structural features (e.g. fees and covenants) may contribute to alignment of incentives for CLO managers. The final report includes insights from the commercial mortgage-backed securities (CMBS) market, where risk retention also applies and commercial property loans are facing some stress (see Annex 4).

On third-party financing structures for CLO risk retention, the report includes additional material based on industry responses, discussions with academics and work by some authorities.

On the BCBS reforms, neither the specific capital calibration of banks' securitisation exposures nor the final Basel III framework (which has not yet been widely implemented) are within the scope of the evaluation, so they are not covered in the final report. The report includes additional analysis on global banks' involvement in securitisation since the GFC (see Annex 4).

2.4. Broader effects of reforms

Some respondents highlighted that CLOs were crucial for providing capital to below-investment grade corporates and challenged the report's claim that post-GFC reforms have not impaired overall credit supply. They also argued that disclosure and due diligence requirements and capital reforms have led to a decline in traditional securitisation in the EU and UK and that, although accommodative financial conditions and the rise of private credit have mitigated some impacts, the overall effect of the post-GFC reforms on these markets appears negative. Other respondents, including some workshop participants, acknowledged the difficulty in determining an appropriate counterfactual and in disentangling factors such as macroeconomic conditions.

In general, respondents agreed that the securitisation reforms have shifted risks from banks to the NBFI sector. Some respondents felt the report could discuss further the redistribution of risk and its implications. They advocated for a clearer distinction in risk transfer trends, separating loan origination and securitisation activities. They argued that securitisation was a vital bridge between bank lending and capital markets and that it enhances financial stability by enabling risk-sharing. This theme was also discussed during the public workshop, in particular on who is best placed to originate loans and bear the ultimate credit risk (banks vs NBFIs), also given the emergence of private credit as a less regulated substitute of bank lending.

Some respondents noted that there was not enough analysis in the report on the nature of securitisation investors and their holdings before and after the GFC. Some also commented that the increase in the role of non-bank financial institutions (NBFIs) in securitisation issuance in the EU was primarily due to the lack of European Central Bank (ECB) access for liquidity and covered bond funding alternatives for those entities, rather than due to a rise in their overall activity. These respondents argued that penalizing banks for investing beyond senior CLO tranches was counterproductive.

Changes in response to comments

Respondents did not provide any evidence to support their assertion that the reforms had material negative side-effects on overall financing to the economy – an issue examined in the report – and many of their comments focused on effects in a single jurisdiction (EU). As a result, no changes have been made to the preliminary conclusions from the consultation report.

The final report includes additional analysis on the implications of risk transfer from banks to NBFIs, e.g. by distinguishing between non-bank loan origination and securitisation investments, pointing out significant information gaps that preclude a comprehensive analysis of this issue, and noting that the FSB's NBFI work programme seeks to address related vulnerabilities.

2.5. Other issues

Feedback from the consultation responses and the public workshop suggests that the simple, transparent and comparable (STC) framework applied in the EU (known as simple, transparent and standardised (STS) securitisations) does not fulfil its intended purpose effectively. Some respondents noted that the STS framework was currently a relabelling exercise and expressed concerns that it has become overly complex and onerous. These respondents also argued that, as a result, this framework fails to support market growth and attract a broader investor base. Proposed updates included revisiting the eligibility criteria (in the EU) and capital treatment to allow investors such as insurers to generate new activity and expanding the reform to CLOs. However, no evidence was presented on how the framework performed vis-à-vis its objectives or about its performance in other jurisdictions.

Several respondents also highlighted potential negative consequences of the due diligence and disclosure requirements in the EU; the capital and operational challenges faced by smaller institutions; the fact that market and regulatory conditions are leading to growth in SRT transactions; and the need to elaborate on stakeholder feedback in Box 8 of the report.

Changes in response to comments

The FSB analysis has not found evidence that the concerns raised about the STC framework apply broadly across jurisdictions. With respect to the narrative, the issue of STC is an example of jurisdictional implementation of international sound practices and standards subject to national discretion. Moreover, the objective of the STC framework is to help investors evaluate risks in securitisations, rather than to stimulate activity in the securitisation market.

The final report also includes additional analysis on the effects of risk retention reforms on large versus small CLO managers. No new analysis has been undertaken on the effects of the banking reforms on small banks since they have historically been active in the securitisation market only to a limited extent.

3. Summary of additional analysis

Following the publication of the consultation report, the FSB conducted additional analyses to validate the tentative findings of the consultation report and explore other relevant issues. The analyses, whose findings are summarised in the final report, focused on: (1) the impact of the BCBS reforms; (2) non-agency RMBS market reforms; (3) risk retention requirements and the CLO market; and (4) other issues.

On (1), the analyses have used supervisory and publicly available data to examine whether the BCBS reforms have contributed to banks shifting towards higher-rated securitisation tranches, thereby decreasing their overall risk-weighted density. On (2), the analysis examined whether issuance spread dispersion between high and lowly-rated European RMBS tranches has increased significantly since the GFC, suggesting improved investor awareness and risk pricing. On (3), the final report includes event-studies of the US court decision in 2018 to overturn the applicability of the risk retention rule to open-market CLOs. On (4), the report includes an Annex with an overview of FSB jurisdictions with material securitisation markets other than the EU, UK and US.