

Credit institutions: taking up and pursuit of the business. Recast

2004/0155(COD) - 28/05/2010 - Follow-up document

The Commission presents a report on the expected impact of Article 122A of Directive 2006/48/EC.

The document recalls that since the summer of 2007, securitisation markets have been in broad distress after large unexpected losses on securitisations of mortgage loans surfaced and are only slowly and partially recovering. Because this distress has deeply affected the financial system and the wider economy, it is crucial that regulation addresses the root causes of the large unexpected losses in certain securitisations. A root cause can be identified as a lack sound loan underwriting practices on the part of the issuers that was made possible because professional investors in the securitisation tranches did not exercise due diligence in their investments and did therefore not impose effective discipline on the issuers.

Article 122a imposes requirements on credit institutions in the European Union in order to make sure that they invest only in securitisations where they have applied appropriate due diligence and where the originators have an incentive to act diligently in the underwriting of the loans to be securitised. The article also obliges credit institutions – where they act as originators themselves – to cater for the relevant disclosures needed for investors' due diligence.

The Article underwent substantial change during the legislative process and there was, also given the difficult condition that securitisation markets were in, no impact assessment carried out about its requirements in their final shape. In particular, during the legislative process, concerns were expressed about the effectiveness of one of its elements, the requirement for issuers of securitisations to retain exposure to the securitisation ("the retention requirement") so that they have an incentive to diligently originate loans.

In accordance with Directive 2008/46/EC, this report provides a high level assessment of the overall impact of Article 122a, and then considers the questions about effectiveness of the retention requirement and the appropriateness of raising its minimum level. There is also an Annex of this report that discusses technical suggestions made by CEBS for improving specific aspects of the retention rule.

In terms of **overall impact**, the Commission expects that Article 122a will help aligning the incentives of issuers and investors more closely. Thereby, it will make securitisation sounder and instil new confidence in this source of financing. The ultimate consequence will be that securitisations return in larger volumes as a source of refinancing of the financial sector's lending to the real economy, while however preventing the excesses that became apparent in the course of the crisis. Regarding the specific question of the effectiveness of the minimum retention level chosen, the Commission concludes that the existing moderate **minimum retention level of 5% should be kept**, acknowledging that investors should require higher retention levels depending on the securitisation in question.

Therefore, the overall design of Article 122a can be expected to meet its purpose. In concluding on this report, the Commission would point to a number of technical points raised by CEBS that are briefly discussed in the annex to this report. The Commission considers that there is **no immediate need to propose legislative changes to Article 122a in this context**. However, the Commission will closely monitor international developments in this field, acknowledging that also in jurisdictions outside the EU there is interest in introducing requirements similar to Article 122a, including retention requirements. As these developments materialise further, the Commission will make sure that Article 122a will also be assessed in light of potentially different solutions found in other jurisdictions.

