

St. Michael's House
1 George Yard
London EC3V 9DH
Great Britain/Großbritannien
Tel +44.20.77 43 93 00
Fax +44.20.77 43 93 01
www.europeansecuritisation.com



20. November 2003

Europäische Kommission/Commission Européenne
Mr. Frits Bolkestein
Member of the European Commission
Cortenbergsstraat 107
B-1049 Brüssel/Bruxelles
BELGIE

Re: Response to Consultation on Capital Adequacy Directive

Dear Mr. Bolkestein:

The European Securitisation Forum ("ESF") does not consider that in the light of the current progress on the securitisation proposals set out in proposed new Basel Capital Accord ("**Basel II**") and the stated aim of the Commission Services to follow in most circumstances the positions agreed under Basel II, it is appropriate at this stage to provide a detailed response to the Third Consultation Paper for the proposed Capital Adequacy Directive ("**CAD 3**"). The ESF submitted a detailed comment letter to the Securitisation Group of the Basel Committee on Banking Supervision on 31. July 2003 (copy enclosed) which sets out its comments and positions on the key aspects of the securitisation proposals and regards these considerations as applying equally to the CAD 3 process. In addition the ESF has produced an Executive Briefing Paper on the Securitisation Proposals of Basel II, a copy of which is also enclosed and which it commends to the Commission Services.

In terms of process, the ESF considers that it would be detrimental to the goal of international regulatory standards applying equally to banks wherever they operate in the world for the CAD 3 process to move towards finalisation when it is clear that there will be changes to the securitisation proposals under Basel II. This is now particularly acute following the announcement after the meeting of the Basel Committee in Madrid on 10. and 11. October 2003 to eliminate the supervisory formula approach (SFA) for securitisation, and to work towards its replacement by a less complex approach and to delay the adoption of Basel II until the middle of 2004 at the earliest. Consequently, in our view moving forward with CAD 3 in such circumstances would cause complications and huge regulatory confusion and could even be viewed as foolhardy.

As mentioned above the ESF commends its Executive Briefing Paper to the Commission Services and notes the main areas of concern for securitisation in Europe that need to be addressed appropriately under Basel II and CAD 3 are as follows:

- the use of lower rated tranches (both investment and non-investment grade) in the European Securitisation market is more widespread than in other Markets (such as the United States). This means the impact of



the proposed risk weighting for lower rated tranches has a significantly greater adverse effect for European credit institutions and investment firms and will discourage the legitimate use of Securitisation and credit derivatives as tools to transfer economic risk;

- the nature of the asset classes securitised in European structures often gives rise to significant levels of excess spread available to support the Securitisation. This is currently not taken into account under the RBA. Ultimately European consumers are directly affected by the cumulative punitive effect of overly conservative assumptions - and hence levels of capital - at regulated firms;
- synthetic securitisation techniques are widely used in Europe as a risk transfer mechanism. This is often the case where traditional securitisations may be difficult if not impossible to utilise. Basel II discriminates against synthetic transactions by, for example, limiting the amount of capital released compared to a cash transaction in certain circumstances. This creates inconsistency of capital treatment notwithstanding the close alignment of economic substance in the two forms of transaction and impacts European credit institutions more acutely;
- european corporates are significant users of funding raised by asset-backed commercial paper (ABCP) conduits. The rules relating to the calculation of capital charges to ABCP positions held by banks are penal and unwieldy as currently proposed. ABCP Conduits fulfil a vital role in providing liquidity to the Capital Markets and allowing SMEs and other corporates to access the Capital markets and this role could well be restrained under the current form of Basel II.
- there are a number of provisions in the securitisation proposals of Basel II which are predicated on structures and legal frameworks which either do not exist in Europe or contradict the existing frameworks and structures used. Unless modified or relaxed, such provisions could effectively preclude the use of securitisation as a viable option for European credit institutions and investment firms, while allowing non-European equivalent firms to continue employing securitisations as part of their overall funding or risk management strategy.

In conclusion, we consider that the latest announcement from the Basel Committee to delay the adoption of the Accord until mid-2004 at the earliest to also provide the Commission Services with an opportunity to delay the CAD 3 process and make sure any revised Securitisation proposals emanating from the Basel Committee are adapted properly for Europe through CAD 3. Such an approach should enable work to continue to be undertaken by the Commission Services to ensure an appropriate alignment of risk and minimum required capital for European credit institutions and investment firms.

The ESF will submit a detailed comment letter in respect of CAD once the considerations of the Basel Committee following the Madrid announcement are published and we have responded to those. In the light of this uncertainty as to what the Basel Committee will produce and the certainty that it will involve material changes to the current proposals we would expect there to be another additional consultation in respect of CAD.



Respectfully submitted,

Anthony Smith-Meyer
Chairman, European Securitisation Forum
(Fortis Bank)

Jean-François Despoux
Vice-Chair, European Securitisation Forum
(Société Générale)

Fabrice Susini
Co-Chair, ESF Legal, Regulatory
& Capital Subcommittee
(BNP Paribas)

/s/

Rick Watson
Co-Chair, ESF Legal, Regulatory
& Capital Subcommittee
(HSBC)

Scott-Christopher Rankin
Executive Director, European Securitisation Forum

Cc: Mr. Alexander Schaub, *Generaldirektor, Binnenmarkt – Europäische Kommission*

Encl.